Jus Corpus Law Journal
Open Access Law Journal – Copyright © 2022 – ISSN 2582-7820
Editor-in-Chief – Prof. (Dr.) Rhishikesh Dave; Publisher – Ayush Pandey

Avitel Post Studioz Limited v HSBC PI Holdings (Mauritius) Limited: Finality on the Arbitrability Issue when fraud Allegations are made

Ammar Shahid[a] Rudra Sinsinwar[b]

[a]National University of Study and Research in Law, Ranchi, India [b]National University of Study and Research in Law, Ranchi, India

Received 18 November 2022; *Accepted* 01 December 2022; *Published* 12 December 2022

Since arbitration provides a swift resolution of disputes, procedural flexibility, confidentiality, neutrality, and, most importantly, the execution of arbitral awards in nations that have ratified the New York Convention, it is the most practical and preferred method for resolving commercial disputes globally. It must be ironed out by the Courts since it is not impervious to unresolved problems. Whether frauds are arbitrable is one of these complex problems. Or, to put it another way, should a dispute involving significant accusations of fraud be resolved by arbitration instead of going before a court with appropriate jurisdiction? The arbitrability of fraud has always been a hotly contested topic. Having stated that, this case commentary examines the judgements dating back to post-independence India with an emphasis on the arbitrability of fraud and, in particular, the inconsistent judicial statements in India relating to the arbitrability of fraud. The current scenario tells us how difficult it has been to resolve the issue of arbitrability of fraud and, more crucially, how it has been overburdened with several tests, increasing the likelihood of judicial intervention. A step towards the goal of a pro-arbitration regime has undoubtedly been made by the Supreme Court's recent judgements, which clarified its position on the issue of the arbitrability of disputes involving serious allegations of fraud and their relation to Indian public policy. However, in our opinion, the Supreme Court has left the matter unfinished by holding that "those frauds which vitiate or render the arbitration clause invalid would still be non-arbitrable," as this still leaves the issue open.

Therefore, we look at "Avitel Post Studioz Ltd v HSBC" to resolve this issue and finally settle the problem of Arbitration in Fraud Cases.

Keywords: *fraud, arbitration, commercial disputes, flexibility.*

INTRODUCTION

Arbitral tribunals have historically had authority over claims of fraud. The extent of such adjudication, however, has been a disputed matter. Is arbitration a viable option for resolving all claims of fraud? Thistopic has been addressed in several legal precedents, and the Supreme Court of India recently decided on it in Avital Post Studioz Limited & Ors. Limited by HSBC PI Holdings[1] in Mauritius (Avitel Post). To begin with, the Act does not specifically state that it does not apply to any disputes. Some legal disputes have been declared to be unresolvable through arbitration. As a result, to establish the statute, Avitel Post had to take into account numerous Supreme Court rulings.

FACTS OF THE CASE

In the year 2011, To purchase Avitel's 7.8% shares for USD 60 million, HSBC and Avitel agreed to a Share Subscription Agreement (SSA) and Shareholder's Agreement (SHA), both of which had similar SIAC arbitration clauses. This investment was made based on Avitel's representation and guarantee that it was close to finalising a contract with the British Broadcasting Corporation (the "BBC") that had the potential to generate revenue of up to USD 1 billion in the future.

In 2012, HSBC hired Ernst & Young and KPMG Dubai (the "Investigating Agencies") 2012 after growing concerned about Avitel's operations and future ambitions. The investigation by the Investigating Agencies revealed that the alleged BBC contract was a fraud and a ruse to persuade HSBC to invest. Additionally, it was discovered that a large percentage of the investment funds had been diverted to businesses linked to Avitel's promoter group. Then, In the emergency arbitration procedures, HSBC submitted notifications of arbitration to the Singapore

[1] *Avitel Post Studioz Limited & Ors v Limited by HSBC PI Holdings* (2020) SCC Online 656

International Arbitration Centre ('SIAC'). After being appointed as an emergencyarbitrator, he issued two interim judgments (the "Interim Awards") in favour of HSBC and ordered Avitel to desist from selling or otherwise reducing its assets worth less than US$50 million.

HSBC filed a petition under *section 9 of the Arbitration Act 1996 (the "1996 Act")*[2] before the Bombay High Court's Single Judge bench, requesting interim relief and directives to require Avitel to deposit USD 60 million as security for the amount of the dispute in arbitration. To freeze Avitel's bank accounts, the court issued an interim order (known as "Order 1") in HSBC's favour. Avitel contested the three-member SIAC Arbitral Tribunal's jurisdiction at the same time, and the Arbitral Tribunal was pleased to dismiss Avitel's claim with a unanimous final partial awardon jurisdiction. Then in 2013, In the meantime, HSBC reported Avitel to Mumbai's Economic Offences Wing ('EOW') for a criminal offence. In this regard, a closure report was submitted to the Mumbai magistrate. Unhappy, HSBC filed a protest petition against the closure report, but the Magistraterejected it. The Bombay High Court is still considering HSBC's appeal of the aforementioned dismissal.

Then in 2014, With the assessment that HSBC has a fair probability of winning in the ultimate arbitration procedures, the Bombay High Court's Single Judge Bench issued an order (dubbed "Order 2") to implement Order 1 and ordered Avitel to deposit any remaining funds from the USD 60 Million. Additionally, Avitel filed an appeal against Order 2 before the Bombay High Court Division Bench under *section 37 of the 1996 Act*[3]. The Division Bench issued a decision (known as "Order 3") declaring that as Singapore law administers the arbitration agreement, Singapore law should be used to determine whether the dispute is arbitrable, and consequently. declined to challenge the Single Judge's conclusions. However, the court reduced the deposit that Avitel was required to make from USD 60 million to USD 30 million and re-evaluated the real damages to which HSBC might be entitled. Finally, the SIAC Arbitral Tribunal issued the final judgement (the "Final Award") in favour of HSBC and determined that Avitel was guilty of fraudulent misrepresentation and owed HSBC legal indemnification in the sum of USD 60

[2] Arbitration and Conciliation Act 1996, s 9
[3] Arbitration and Conciliation Act 1996, s 37

million plus interest for the crime committed.

Then in 2015, Avitel complained about the Final Award to the Bombay High Court under section 34 of the 1996 Act[4]. The petition was, however, rejected by the court as unmaintainable. The 1996 Act's section 37 appeal by Avitel against this decision was likewise denied. According to section 48 of the 1996 Act[5], HSBC petitioned the Bombay High Court to have the Final Award enforced. These enforcement actions are still underway. Then in 2017, The parties' appeals and cross-appeals against Order 3 issued by the Divisionbench of the Bombay High Court were finally heard by the Hon. Supreme Court.

ARGUMENTS ADVANCED

Avitel's Arguments

According to Avitel's argument, a dispute would not be subject to arbitration under Indian law if a transaction between the parties involved a major criminal offence, such as forgery and impersonation. Additionally, it was argued that in section 9 proceedings, the arbitrability of fraudshould be decided by Indian law rather than Singaporean law. Further, it was argued that the Division Bench of the Bombay High Court had relied on a Supreme Court decision by a single judge, ***Swiss Timing Ltd. v Commonwealth Games 2010 Organising Committee***[6], which had incorrectly ruled that the two-judge bench decision in ***N. Radhakrishnan v Maestro Engineers,***[7] as per incuriam. It was also argued that the requirements of *section 48 of the 1996 Act* must be satisfied in enforcement proceedings in India. The judgments of this Court regarding severe claims of fraudfiled in arbitration procedures are referred to as "the public policy of India," and if HSBC is unable to cross this threshold, it will be impossible to enforce a foreign award in India. A primafacie case had to be established under *section 9 of the 1996 Act* using this lens.

Avitel further claimed that the Chairman of the SIAC Tribunal was biased becauseHSBC was a

[4] Arbitration and Conciliation Act 1996, s 34
[5] Arbitration and Conciliation Act 1996, s 48
[6] *Swiss Timing Ltd. v Commonwealth Games 2010 Organising Committee* (2014) 6 SCC 677
[7] *N. Radhakrishnan v Maestro Engineers* (2010) 1 SCC 72

client of the company owned by the Chairman of the Arbitral Tribunal. It further asserted that the award's stamping was insufficient. Last but not least, Avitel stated that notwithstanding the Parliament's decision to ignore the 246th Law Commission Report's proposal that a section 16(7) be added to the 1996 Act[8] to repeal the N. Radhakrishnan judgment's reasoning, the N. Radhakrishnan judgement continues to be valid.

HSBC's Arguments

The three-judge bench decision in Rashid Raza v Sadaf Akhtar[9], which explained the judgement in A. Ayyasamy v A. Paramasivam[10], which elucidates two situations when serious allegations of fraud are non-arbitrable in nature, was used by HSBC to counter the arguments. The Final Award, which shows that Avitel not only impersonated and falsely represented itselfbut also stole the investment amount, was later cited by HSBC. As a result, these concerns mustmostly be resolved between the parties, and the alleged fraud lacks any public favour. HSBC argued that the enforcement actions under section 48 already ongoing before the Bombay High Court should be used to address the issue of bias because this is not the proper time or venue to do so. The Final Award was also made unanimously by the three members of the Arbitral Tribunal; therefore, the Chairman could not be considered prejudiced.

Regarding the claim that the award was improperly stamped, HSBC claimed that this was the first time the claim had been made and that Avitel had not made any arguments. Therefore, the assertion should be ignored in the interest of justice and in the absence of giving HSBC the chance to refute it. Last but not least, HSBC backed Order 1 in its entirety and contended that the Division Bencherred by reducing the security deposit from USD 60 million to USD 30 million without providing any justification.

[8] Arbitration and Conciliation Act 1996, s 16(7)
[9] *Rashid Raza v Sadaf Akhtar* (2019) 8 SCC 710
[10] *A. Ayyasamy v A. Paramasivam* (2016) 10 SCC 386

ISSUES OF THE CASE

- According to the Honorable Supreme Court, the only significant issue that has to be resolved in the section 9 proceedings is the degree to which it can be argued that HSBC has a strong prima facie case in the enforcement procedures under section 48 that are currently being heard by the Bombay High Court.
- If so, determine whether HSBC would suffer irreparable harm if no protective orderswere granted in its favour and, more broadly, determine whether and how much the balance of convenience favours HSBC.

JUDGEMENT BY THE SUPREME COURT

When claims of fraud are brought up by one of the parties to the arbitration agreement, the Hon'ble Supreme Court, recognising Avitel's argument, found that the prima facie case in the current situation would unavoidably depend upon what is the substantive law in India concerning arbitrability. The Court then went on to examine all pertinent legal precedents regarding the arbitrability of fraud. After conducting this thorough analysis, the Court moved on to consider the Final Award, whichconcluded that the majority of the claims made by Avitel were made to persuade HSBC to invest and that, in addition, they then stole a sizable portion of that investment for their use. Thus, as a result of this, HSBC was granted interest and damages totaling USD 60 million for their claim for false misrepresentation.

The Court concluded by opining that the questions raised have a civil profile inter se the parties and that the outcome of any criminal proceedings is irrelevant and held: -

Firstly, the arbitration agreement agreed into by the parties must be viewed as an independent clause, so the deception in the current case does not invalidate it. Furthermore, any determination that the arbitration clause is illegal, despite its broad scope, does not follow from any determination that the contract itself is void or voidable due to fraud or misrepresentation.

Second, since Avitel's impersonation, fraudulent statements, and money diversion have no "public character," the matter can be resolved by arbitration.

The Court further determined that HSBC is entitled to compensation for both the share purchase price and any additional indirect damages. Because it was based on an inaccurate assessment of damages, Order 3 of the Division Bench of the Bombay High Court to decrease the deposit from USD 60 million to USD 30 million was not acceptable. Finally, the Court determined that HSBC has the advantage in the balance of convenience and that it was successful in establishing a prima facie case against Avitel.

CRITICAL ANALYSIS

The Supreme Court ruled in Abdul Kadir Shamsuddin Bubere v Madhav Prabhakar Oak[11], a case governed under the 1940 Act on Arbitration[12] (the '1940 Act'),which was later abolished by the 1996 Act[13]:

"The Court will, in general, refuse to send a dispute to arbitration if the party charged with fraud desires a public inquiry, but where the objection to arbitration is by the party charging the fraud, the Court will not necessarily accede to it, and will never do so unless a prima facie case of fraud is proved". "Where serious allegations of fraud are made against a party and the party who is charged with fraud desires that the matter should be tried in open court, that would be a sufficientcause for the court not to order an arbitration agreement to be filed and not to make the reference. But it is not every allegation imputing some kind of dishonesty, particularly in mattersof accounts, which would be enough to dispose of a court to take the matter out of the forum which the parties themselves have chosen".

In a 1942 A.C. decision from ***England v Charles Osenton & Co.***, where allegations of fraud against a party regarding accounting entries were made, the Court decided as follows: "*It seems to us that every allegation tending to suggest or imply moral dishonesty or moral misconduct in the matter of keeping accounts would not amount to such a serious allegation of fraud as would impel a court to refuse to order the arbitration agreement to be filed and refuse torefer*."

[11] *Abdul Kadir Shamsuddin Bubere v Madhav Prabhakar Oak* [1962] 3 SCR 702
[12] Arbitration Act 1940
[13] Arbitration and Conciliation Act 1996

In the ***N. Radhakrishnan decision***, the respondents were accused of engaging in several irregularities in the company's accounting records. It is to be noticed that the Supreme Court rejected the application under section 8 of the 1996 Act to refer the parties to arbitration, ostensibly basing its decision on the legal reasoning outlined in the Abdul Kadir decision, holding that the allegations of fraud precluded arbitration as a method of resolving the dispute. The decision in N. Radhakrishnan, however, did not take into account the earlier pertinent decision in ***Hindustan Petroleum Corporation Ltd. v Pinkcity Midway Petroleums,***[14] which dealt with *sections 8 of the 1996 Act*[15] and principles under *sections 5 and 16 of the 1996 Act*[16].

The Supreme Court had the opportunity to discuss categories of cases that are typically thought to be not suited for the ADR process taking into account their nature in Afcons Infrastructure Ltd. Anr v Cherian Varkey Construction Co. (P) Ltd. Accordingly, it was noted that these situations include "cases involving significant and detailed claims of fraud, fabrication of documents, forgery, impersonation, coercion, etc." and "cases requiring prosecution for criminal offences."

The Supreme Court ruled in ***Booz Allen & Hamilton Inc. v SBI Home Finance Ltd***.[17], that only disputes involving rights in personam might be arbitrated. Proceedings in rem, such as those in mortgage litigation, are not arbitrable. The court outlined six other types of conflicts that are not subject to arbitration, including disagreements over the rights and obligations that result from criminal offences. In paragraph 15 of the ruling, the Honorable Supreme Court noted that the rulings in Afcons and Booz Allen made broadstatements of the law and needed to be justified in light of later rulings on the issue. This is crucial to the case.

Vimal Kishor Shah v Jayesh Dinesh Shah[18], which dealt with issues involving trust deeds covered by the Trusts Act of 1882[19] (the "1882 Act"), created a new seventh class. The Swiss Timing decision was extensively examined by the Supreme Court, which noted that while it was

[14] *Hindustan Petroleum Corporation Ltd. v Pinkcity Midway Petroleums* (2003) 6 SCC 503
[15] Arbitration and Conciliation Act 1996, s 8
[16] Arbitration and Conciliation Act 1996, s 5, 16
[17] *Booz Allen & Hamilton Inc. v SBI Home Finance Ltd*. (2011) 5 SCC 532
[18] *Vimal Kishor Shah v Jayesh Dinesh Shah* (2016) 8 SCC 788
[19] Trust Act 1882

not a precedent that had to be followed, its logic had "high persuasive value that the court is inclined to adopt." After examining Sections 20, 35 of the 1940 Act[20], and Sections 5, 8, and 16 of the 1996 Act[21], it can be determined that:

As against this, sections 5, 8, and 16 of the 1996 Act reflect a completely new approach to arbitration, which is that when a judicial authority is shown an arbitration clause in an agreement, the authority must refer parties to arbitration bearing in mind the fact that the arbitration clause is an agreement independent of the other terms of the contract and that, therefore, a decision by the arbitral tribunal that the contract is null and void does not entail ipso jure the invalidity of the arbitration clause.

The leading ***Ayyasamy judgement*** can also be discussed and the opinion of Sikri J. can be referred to in detail where it can be discussed the need for a meticulous inquiry when allegations of fraud are raised. Serious claims of fraud are to be treated as non-arbitrable cases, and the civil court should be the sole one to decide these instances. However, we believe that it may not be essential to void the effect of the parties' arbitration agreement when there are claims of fraud simpliciter that are only allegations because the arbitral tribunal can resolve such matters. The arbitration clause need not be ignored and the parties may be required to proceed with arbitration when there are straightforward charges of fraud involving the internal affairs of the party in question and having no implications for the public at large.

We should also cite the ruling in ***Ameet Lalchand Shah v Rishabh Enterprises***[22], where the court rejected the claim that claims of deception and inducement to pay a higherprice could not be arbitrated by drawing on the ruling in Ayyasamy. Relevantly, citing the Rashid Raza decision, we should note that two working standards wereestablished in paragraph 25 of the Ayyasamy decision to determine whether a dispute can be arbitrated when one party makes substantial charges of fraud, namely whether –

- the allegation pervades the entire contract, including the arbitration clause, rendering it

[20] Arbitration Act 1940, s 20, 35
[21] Arbitration and Conciliation Act 1996, s 5, 8, 16
[22] *Ameet Lalchand Shah v Rishabh Enterprises* (2018) 15 SCC 678

null and void;

- or the charges of fraud are directed at the private matters of the parties and have no bearing on the public interest.

Following these rulings, it is evident that "serious charges of fraud" only occur when one of the two established requirements is met, and never in any other circumstance. In a clear example where the court determines that the party against whom a breach is alleged cannot be said to have entered into the arbitration agreement at all, the first criterion is only satisfied when it can be declared that the arbitration provision or agreement itself cannot be saidto exist. The second criterion can be said to have been satisfied in cases where accusations of capricious, dishonest, or malicious behaviour against the State or its agents are made, necessitating the case's hearing by a writ court and raising concerns that are more generally related to public law than to the contract itself or its breach.

It was explicitly stated that the *Afcons judgment's paragraph 27(vi)* and the *Booz Allen judgment's paragraph 36(i)*[23] must now be read with the caveat that the same set of facts could result in both civil and criminal procedures. The mere fact that criminal proceedings can or have been instituted about the same subject matter would not lead to the conclusion that an otherwise arbitrable dispute, ceases to be so if it is clear that a civil dispute involves questions of fraud, misrepresentation, etc. that can be the subject of such a proceeding under *section 17 of the Contract Act*, and/or the tort of deceit.

In ***Fazal D. Allana v Mangaldas M. Pakvasa***, (hereinafter "Fazal")[24], thereare two categories of fraud: those where –

- the deception was used to get the contract (formation issue), and
- a legitimate contract's performance was tainted by deceit or fraud.

It should be noted that the latter would be outside the purview of the Contract Act and that the remedy for damages would be accessible under the tort or deceit law, but not the remedy to treat

[23] *Ibid*
[24] *Fazal D. Allana v Mangaldas M. Pakvasa* (1922) Bom 303

the contract itself as void. However, each of these circumstances would be arbitrable, and the arbitral tribunal's jurisdiction would remain intact. When a party to a contract is persuaded to enter into it, some precedents must be examined relevant to the number of damages for false misrepresentation. The Court summarized the "dateof transaction rule," which explains - the House of Lords decision in Doyle v Olby (Ironmongers) Ltd.[25], (hereinafter referred to as "Doyle"), the facts of which were identical to the disagreement between Avitel and HSBC.

There are only one and not two alternative measures of damages in circumstances of fraudulent misrepresentation, namely the loss sustained by the party affected who must be placed back in the same position as if he had never engaged in the transaction. In addition to providing much-needed clarity regarding the arbitrability of disputes involving serious allegations of fraud in both domestic arbitrations and international arbitrations with Indiaas the seat, this judgement has deftly filled the interpretational gaps that surrounded the pertinentissue. Relevantly, the Supreme Court concluded in World Sport Group (Mauritius) Ltd v MSM Satellite[26] that such claims are arbitrable in foreign-seated arbitrations.

It is admirable that the Supreme Court made an effort to smooth out the wrinkles left over from the Rashid Raza decision and to lay out the criteria for determining whether substantial or complicated fraud can be arbitrated. By providing proper deference to the fundamental principles of competence-competence and separability, this ruling significantly strengthens India's pro-arbitration regime and brings it into compliance with worldwide best practices. Practically speaking, this decision will guarantee that vexatious and baseless claims of fraud by a party seeking to avoid the arbitration agreement be rejected. It will also prevent and end moonshine accusations of major fraud that are brought up incidentally to scuttle or halt arbitration processes.

[25] *Doyle v Olby (Ironmongers) Ltd* [1969] 2 All ER 119
[26] *World Sport Group (Mauritius) Ltd. v MSM Satellite (Singapore) Pte. Ltd.* (2014) 11 SCC 639