DOCTRINAL CONFLICT IN FOREIGN INVESTMENT REGULATION IN INDIA: *NTT DOCOMO VS. TATA SONS* AND THE CASE FOR "DOWNSIDE PROTECTION"

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ABSTRACT

The strategic importance of India as an investment destination for foreign investors is highlighted by ongoing tensions in the Indo-Pacific region and the recognition that a strong economic relationship with India is in the interests of countries seeking a more stable balance of power in the region. From a policy perspective, India has struggled to balance its own economic interests with the commercial requirements of investors. Rules attempting to strike this balance have created uncertainties that have resulted in investors seeking greater protections for their investments, which in turn have triggered additional regulatory responses that enforce

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India's policy preferences. The prevalent use of put options by foreign investors, whereby Indian parties are required to buy out their counterparties at predetermined prices, has been a prominent subject of these regulations. India's judiciary has been drawn into this cycle through actions brought by foreign investors seeking to enforce arbitration awards validating their exit rights. In the process, they have created their own interpretation of the applicability of foreign investment rules that support principles of freedom of contract. This doctrinal conflict with regulatory policy is illustrated by a high-profile dispute involving one of Japan's largest and most well-known companies, NTT Docomo, and one of India's largest and most trusted companies, Tata Sons. Japan views India as a key strategic partner and, in particular, views strong economic ties as a central linchpin of the partnership. Using, principally, the Tata-Docomo case as an example, and a review of other similar disputes, this Article analyzes the regulatory and judicial doctrines that have shaped foreign investment regulation in India and explores the public policy implications of the conflict for India. In doing so, it proposes regulatory reforms to provide more clarity and certainty for investors, suggesting that express recognition of "downside protection" for investments provides a rational balance between private commercial interests and public regulatory objectives.

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I. INTRODUCTION

A key objective of the Government of India's foreign direct investment (FDI) policy is to make it transparent, predictable, and easily comprehensible.[1] These features are crucial to increase and maintain investor confidence in the Indian market. As of 2019, India attracted net FDI inflows of about fifty billion dollars.[2] Three countries— Mauritius, Singapore, and the United States of America—account for over fifty percent of India's FDI inflows.[3] Despite the pandemic, India's FDI inflows from the United States have increased in the period between April 2020 and September 2020 when compared to the period between April 2019 and March 2020.[4] Japan's percentage of total investment inflows to India over the same period is on par with that of the United States at seven percent, making it the fifth largest investor by FDI equity inflows.[5] Though the FDI policy clearly articulates the need to maintain a stable investment environment, there are portions of India's regulatory framework that create uncertainty for foreign investors. This Article examines one such area of India's regulatory landscape, namely, the treatment of foreign investors' exit rights under foreign exchange regulation.

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1 *See* Department for Promotion of Industry and Internal Trade (FDI Division), Ministry of Commerce and Industry of India, Consolidated FDI Policy Circular of 2020, at 5 (Effective from October 15, 2020) [hereinafter Consolidated FDI Policy], https://dpiit.gov.in/sites/default/files/FDI-PolicyCircular-2020-29October2020_0.pdf. The Consolidated FDI Policy is issued by the Government of India through its Department for the Promotion of Industry and Internal Trade. The Consolidated FDI Policy is a comprehensive document containing the conditions for eligible investors, sector-wise caps on foreign investment (where applicable) and the procedure for seeking government approvals where required.

2 *See* THE WORLD BANK, *Foreign direct investment, net inflows (BoP, current US$)*, https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD [https://perma.cc/569N-Y5NF].

3 *See* MINISTRY OF COM. & INDUS., INDIA, QUARTERLY FACT SHEET ON FOREIGN DIRECT INVESTMENT 2 (2020), https://dipp.gov.in/sites/default/files/FDI_Fact_sheet_September_20.pdf.

4 *See id.*

5 *See id.* According to data from the Ministry of Finance, Japan, investment outflows from Japan into India in 2019 amounted to about 452 billion Yen. *See also* MINISTRY OF FINANCE, JAPAN, DIRECT INVESTMENT FLOWS 2019 C.Y. (2019), https://www.mof.go.jp/english/international_policy/reference/balance_of_payments/ebpfdii.htm [https://perma.cc/W7SX-SQ2M].

A corporation investing abroad is subject to increased downside risk (the risk of incurring losses) compared to one that only invests domestically.[6] The geographical distance of the investment and differences in language and culture between the country of the foreign investor and the country of investment reduces an investor's ability to effectively monitor their investment operations.[7] This type of information asymmetry is a risk that is unique to foreign investment.[8] The management of a company also exercises lesser control over its foreign investments than its domestic ones.[9] This can either be a result of the same informational asymmetry that affects shareholders or due to a government's FDI policy. In India, the FDI policy requires investors to partner with domestic firms if they want to make investments in certain sectors within India.[10] This is done by capping the level of foreign investment that an enterprise in India is allowed to accept.[11] Even if the investment is not capped, some sectors such as air transport services and telecom services require government approval for foreign investment exceeding specified thresholds, for example, forty-nine percent.[12]

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6 *See* Li-Hsun Wang, Chu-Hsiung Lin, Hung-Gay Fung & Tzu-Chuan Kao, *Foreign Direct Investment and Downside Risk: Evidence from Taiwan*, 57 PAC.-BASIN FIN. J. 1, 2, 13 (2019) (concluding that FDI may increase agency problems and information asymmetry, which lead to downside risks).

7 *See id.* at 2, 4.

8 *See* Wang et al., *supra* note 6 (demonstrating that FDI implies a higher degree of information asymmetry); Itay Goldstein & Assaf Razin, *An Information-Based Trade Off Between Foreign Direct Investment and Foreign Portfolio Investment*, 70 J. INT'L ECON. 271, 272, 268-88 (2006) (concluding that FDI allows for more information regarding the control and management of the corporation when compared to foreign portfolio investment; however, when it comes to the sale of the business, the information asymmetry leads to a less lucrative sale in cases of FDI than when the investment is through foreign portfolio investment).

9 *See* Wang et al., *supra* note 6, at 4 (arguing that factors such as geographical constraints and cultural, legal, and linguistic differences create agency problems, which would not exist in the case of domestic investments).

10 *See* Consolidated FDI Policy, *supra* note 1, at 20, 34.

11 *See* Consolidated FDI Policy, *supra* note 1, at 20, 30-66. The cap is the maximum percentage of FDI investment in an undertaking in a sector as prescribed by the FDI Policy. In addition to the cap on the percentage of investment in equity that a foreign investor may make, the policy provides for two FDI routes—the automatic route and the government approval route. The existence of a cap on foreign investment does not have a bearing on the investment route. Some sectors such as publication of journals and magazines allow for 100 percent FDI, but this FDI requires government approval. Other sectors such as petroleum refining by public sector undertakings cap foreign investment in equity (forty-nine percent in this case) but do not require government approval for the investment.

12 *See* Consolidated FDI Policy, *supra* note 1, at 39, 46.

The lower level of direct control exercised by a foreign investor leads to measures to curb the extent of risk the foreign investor is exposed o; these measures are referred to as "downside risk protection."[13]

An important downside risk protection measure is the put option, which has become virtually ubiquitous in foreign investment agreements in India.[14] At a basic level, put options provide a foreign investor with an exit mechanism by granting the foreign investor the right to sell its investment position (often held in the form of shares in the venture) to its partner in India. An exit mechanism, by way of a put option, may even be a necessity in those companies whose stocks are not publicly traded or where the foreign investor's holding is illiquid and the demand for it is limited. However, put options are also used by foreign investors for protection against losses by imposing an obligation on the Indian partner to purchase shares at a predetermined price or a minimum guaranteed price. The purpose of such pricing is to control the investor's exposure to potential losses from the investment, either by ensuring principal protection (with or without an interest component), assured returns, or limitation of downside risk. The Indian foreign exchange regime (administered by the Indian central bank—the Reserve Bank of India—and the federal government in consultation with each other), however, makes it difficult to enforce such put options as it requires securities held by foreign residents to be sold to Indian residents at a price not exceeding the fair market value prevailing at the time of exercise.[15] Although the foreign exchange laws have ostensibly permitted put options, the pricing requirements for the sale of securities, which until the year 2019 used to be regulated by the Reserve Bank of India (RBI) and are now

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13 *See generally* Kashish Makkar & Sarthak Jain, *Enforcement of Exit Options in Foreign Investment Agreements: A Call for Reform in Indian Law*, 30 INT'L CO. & COM. L. REV. 399 (2019). For a discussion of a recent Delhi High Court decision that may increase foreign investment in India by providing foreign investors with downward protection of their equity investment, see Anurag Pareek, *Tata – Docomo Verdict: A Critical Analysis*, INDIACORPLAW (May 30, 2017), https://indiacorplaw.in/2017/05/tata-docomo-verdict-critical-analysis.html [https://perma.cc/K3TK-988L].

14 *See* Makkar & Jain, *supra* note 13, at 399 ("Call and put options are ubiquitous in present-day investment agreements, especially those involving joint ventures, private equity or venture capital investments."); *see also* Umakanth Varottil, *Investment Agreements in India: Is There an "Option"?*, 4 NUJS L. REV. 467, 468 (2011).

15 *See infra* text accompanying footnotes 146, 150.

regulated by India's federal government,[16] operate as an impediment to the exercise of most put options.[17] The result is that even when Indian buyers are willing to pay the agreed predetermined price for the securities, foreign exchange regulations pose significant difficulties.[18]

The extensive use of put options by foreign investors in India, and their acceptance by Indian partners, is indicative of their relative bargaining power and perception of the risks of investing in the Indian market. For instance, in the United States, a commercially advanced market characterized by a relatively developed and business-friendly regulatory regime, resort to such mechanisms is generally limited to situations dictated by the perceived risks of the specific investment, the creditworthiness of the counterparty, and the negotiating leverage of the investor. In the Indian context, uncertainties created by the regulatory environment may be another factor that drives investor desire for the protection of put options apart from the sector-specific business risks and the overall economic conditions at the time of the transaction.[19] Although the main objective of such options is to protect against losses, India's regulatory landscape has made them difficult to enforce.[20] Given that foreign exchange rules do not permit the transfer of securities from a non-resident to a resident at a price exceeding market value,[21] put options can only be legitimately exercised when the predetermined sale price is lower than or equal to the prevailing

[16] Pursuant to an amendment to foreign exchange laws notified in 2019, the power to regulate capital account transactions such as transfer of securities, other than debt instruments, vests in the federal government, i.e., the Central Government of India. This change was primarily brought about to align the legislative source of FDI regime. Earlier, there was a regulatory overlap. While the federal government (the Central Government) was in charge of framing the FDI policy, the implementing rules and regulations came from the RBI. This caused confusion at times. This gap was sought to be addressed by amendments to the foreign exchange laws proposed in 2015, which were finally notified in October 2019. *See infra* text accompanying footnote 137.

[17] *See infra* text accompanying notes 146, 150.

[18] *See infra* text accompanying notes 146, 150.

[19] For example, in the case of Tata-Docomo investment transaction, which took place in the second half of 2008, the then prevailing global financial crisis may have been one of many factors influencing parties' agreement on the put option.

[20] *See* Ministry of Finance, Foreign Exchange Management (Non-debt Instruments) Rules, S.O. 3732(E) (Notified on October 17, 2019) (India).

[21] *See id.* rule 9(5) and rule 21(2)(c)(iii).

market price at the time of exercise[22]—which, of course, defeats the purpose of the option.

In order to address this issue, parties to foreign investment agreements attempt to structure their transactions around these regulations. Foreign investors who are accustomed to relying on contractual protections (and legal opinions on their enforceability) have few legal constraints on the exercise of their rights. However, domestic Indian parties who are directly subject to regulatory sanctions for violations of foreign investment rules are often reluctant to perform their contractual obligations in the absence of express approval from the regulators, which is generally not granted as a matter of practice. A number of these transactions therefore have ended up in arbitration proceedings to resolve disputes over the domestic party's legal ability to perform.[23] On account of such cases brought before Indian courts by foreign investors to enforce arbitral awards compelling the performance of put options, the Indian judiciary has been forced to address the conflict between the contractual rights of foreign investors and the regulatory regime.

The Indian judiciary has consistently upheld a foreign investor's right to sustain monetary claims under put options notwithstanding the regulatory restrictions. However, they have done so not by ruling directly on the permissibility or enforceability of put options within the foreign exchange regulatory framework per se, but within the circumscribed role assigned to them under Indian arbitration law, which follows a narrow approach to overturning arbitral awards under the New York Convention. The Arbitration and Conciliation Act, 1996[24] adopts a pro-enforcement approach and requires that the judiciary decide on the enforceability of a foreign arbitral award without reviewing its merits. Significantly, Indian courts have gone further by holding that violations of foreign exchange rules cannot be grounds to refuse the enforcement of foreign arbitral awards.[25] Moreover, courts have held that Indian regulators also are bound by arbitral findings.[26] In doing so, the stance of the judiciary, though consistent with international

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[22] *See id.*

[23] *See e.g.*, NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078 (India); Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810 (India); Banyan Tree Growth Cap. v. Axiom Cordages Ltd., (2020) SCC Online Bom 781 (India).

[24] The Arbitration and Conciliation Act, 1996 [hereinafter Arbitration Act].

[25] *See infra* Part V(A).

[26] *See infra* Part V(B).

commercial arbitration jurisprudence, appears at odds with the domestic regulatory framework governing put options. This doctrinal conflict in foreign investment regulation raises significant public policy implications for India and the resulting uncertainties call for more clarity and predictability. This is compounded by the fact that (i) attempts to structure around restrictions will continue to be subject to the need for testing through costly arbitration and litigation, (ii) the confidential and non-*stare decisis* nature of arbitral proceedings impedes their use as precedent, and (iii) notwithstanding arbitral and judicial findings that recognize the validity of a foreign investor's rights, actual transmission of payments by Indian parties to non-residents continue to remain subject to potential regulatory hurdles.

This Article examines case law to explain how the current regime has come to be and suggests regulatory reforms to provide much needed clarity for foreign investors. *NTT Docomo, Inc. v. Tata Sons Ltd.*[27] (the *Docomo* case) is an example of the regulatory uncertainties surrounding put option agreements and how the resolution ultimately came through a contested judicial process which could have been avoided if there was better regulatory clarity. Part II uses the *Docomo* case to explain how the regulatory regime has interfered with the use of a certain form of risk protection—downside protection—by foreign investors and gives an overview of the international commercial arbitration regime in India. Parts III and IV examine the evolution of the public policy exception in detail and explain why any optimism about the prevailing pro-enforcement trend in the judiciary should be held with caution. Part V takes a closer look at the *Docomo* case and compares it to other High Court decisions that have dealt with the enforcement of put options through arbitral awards. Thereafter, Part VI explains the problem with relying on the judiciary and arbitration proceedings to enforce investors' exit option rights. This Article emphasizes the imperative to distinguish put options structured to extend downside protection to foreign investors from put options structured to assure financial returns to such investors. It finds that while courts will enforce foreign arbitral awards to allow investors to exercise a put option, the conflict between judicial and regulatory doctrine and the process of obtaining and enforcing awards come with their own quantitative and qualitative costs. Importantly, this is an unnecessary encumbrance on the enforcement of contractual rights and

27 NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078 (India).

significantly increases the cost of foreign investment—for both the foreign investor as well as the Indian party.

II. THE *TATA-DOCOMO* CASE AND THE ROCKY ROAD TO ENFORCING PUT OPTIONS IN INDIA

The case of *NTT Docomo, Inc. v. Tata Sons Ltd.*[28] is an important example of how foreign exchange laws affect a party's ability to ensure the benefits of freely negotiated contractual investment protections. Docomo had invested approximately USD 2.5 billion to acquire twenty-six percent of the shares in Tata Teleservices Limited (TTSL). As a safety net for Docomo's investment, a clause in the Shareholders Agreement allowed Docomo to exit with at least half of the value (a predetermined price) it had invested in TTSL. When Docomo exercised its right to exit, Tata claimed it was not possible for it to purchase Docomo's shares at the predetermined price (which exceeded the fair value of the shares prevailing at the time) without regulatory approval from the RBI. Tata asserted that it had made efforts to obtain the approval, which was denied. The regulators were unwilling to grant approval to Tata for the purchase of Docomo's shares based on the predetermined terms of exit. This led to a dispute between Tata and Docomo which resulted in arbitration before the London Court of International Arbitration (LCIA). The LCIA gave its award in favour of Docomo and required Tata to pay Docomo damages equivalent to Docomo's stipulated downside protection. This award was enforced in India through a decision of the Delhi High Court.

The *Docomo* case represents a peculiar situation in which an award of damages for non-performance (as opposed to specific performance) provided the only remedy for a foreign investor seeking to have its contract enforced. For the Indian party too, the situation was peculiar, as it had to face a finding of contractual

[28] *Id.* Tata Sons Ltd. ("Tata"), the respondent, is a company incorporated in India and about sixty-six percent of its equity shareholding is held by Tata Philanthropic Trusts. Tata is the principal investment holding company of the business conglomerate commonly known as the 'Tata group', which operates in more than 100 countries across six continents. NTT Docomo ("Docomo"), the petitioner, is a company incorporated in Japan and is the biggest mobile telecommunications service provider in the country. It also provides services in other countries in Asia, Europe, and the United States. At the time of the case, Docomo was listed on the Tokyo and New York stock exchanges.

breach even while it maintained that it remained ready and willing to pay the predetermined contractual price, provided the regulator granted its approval. Because the regulatory permission was denied, Tata asserted that the only legal way to perform the contract was pursuant to the pricing rules mandated by the foreign exchange regulations, which would result in a payment significantly below the agreed amount. Docomo asserted, however, that the contract could be performed in full in accordance with its terms without violation of the rules. As a result, arbitration became the only way to resolve the dispute with regard to performance of the contract. In this case, the foreign arbitral award effectively provided the means by which the parties were able to exercise contractual rights which they were prevented from exercising because of regulatory hurdles. *Docomo* was not the first case to face this situation. India's restrictive put option enforcement regime has virtually made arbitration a pre-requisite to their enforcement.[29]

The circumstances described above exemplify why the Indian government and the RBI need to rationalise their policy on put options exercisable by foreign investors.[30] Put options give parties the right (but not the obligation) to sell their shares in a company at a pre-agreed sale price, and impose an obligation on the counterparty to purchase the shares at such price.[31] As discussed above, because foreign investors use put options to secure their exit from a venture, the stable and predictable enforcement of put options is an important means to attract and retain investments.[32] The Indian government and particularly the RBI, being India's monetary policy regulator, are legitimately concerned by put options because they are capable of requiring Indian residents to pay large sums of money as consideration to purchase the securities of foreign investors using foreign currency.[33] From a monetary policy perspective, this is capable of straining India's foreign exchange reserves.[34] Another objective of the regulation of put options is to address a policy issue at a conceptual level—balancing the

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29 *See infra* Part II.

30 Makkar & Jain, *supra* note 13, at 400.

31 Makkar & Jain, *supra* note 13, at 401.

32 Makkar & Jain, *supra* note 13, at 401-02.

33 Makkar & Jain, *supra* note 13, at 410, 414.

34 Makkar & Jain, *supra* note 13, at 414. Technically, payment is made in Rupees and are converted to dollars under hedging arrangements that are entered into by the relevant party. India's foreign exchange reserves are affected when the Rupees that the counterparty sells into the market flow back to India for dollars.

objectives of FDI policy with the purpose of put options. The FDI regime is aimed at attracting, facilitating, and incentivizing long-term equity investments in which the foreign investor has a stake in the country's economy and gets to share both the reward and risk. An option to exit at a pre-agreed price takes away from these long-term objectives of the FDI policy. It would also, if allowed in an unfettered manner, incentivise parties to structure transactions (which appear to be equity investments in nature) in a manner that attain the characteristics of debt (which are separately regulated under external borrowing rules).[35] However, put options also play a role in attracting investments by allowing foreign investors (even long-term strategic investors) to cap their losses. This is the regulatory conundrum that needs to be addressed and requires a balancing act on the part of the Indian government and the RBI.

a. Assured Return vs. Downside Protection

Put options can either allow investors to exit at a price which provides them assured returns or simply provide downside protection.[36] When an investor secures assured returns through a put option, it will allow the investor a route to exit while recovering all of its invested capital in addition to returns on the investment.[37] This effectively removes the risk associated with the investment and converts equity risk into an instrument with debt-like characteristics.[38] The association of put options with debt instruments occurs because when exercised, put options require shareholders or the company to purchase the investor's shares at the predetermined sale price, which includes a return component. An investor's ability to exit at a predetermined price that is higher than or equal to the original investment takes away the essential risk-

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35 *See* Reserve Bank of India, Foreign Exchange Management (Borrowing and Lending) Regulations, Notification No. FEMA.3(R)/2018-RB (Notified on December 17, 2018) [hereinafter External Borrowing Rules].

36 Makkar & Jain, *supra* note 13, at 410-11.

37 Makkar & Jain, *supra* note 13, at 410-11. Investors can also negotiate for a return of original principal invested, or for a sale at current appraised market value. As a commercial matter, most investors (particularly financial investors) would seek to be compensated for the use of their money through an interest component. A current fair market value approach is the one preferred by the regulators, which for the reasons stated above defeats the protective purpose of exit options. For these reasons, this Article focuses on the assured return and downside risk options.

38 Makkar & Jain, *supra* note 13, at 409-10.

bearing equity characteristic of a shareholder.[39] This raises concerns because the incurrence of external debt is separately regulated by external commercial borrowing (ECB) rules which are intended to control capital outflows under the same policy considerations governing maintenance of foreign exchange reserves.[40]

In contrast, put options designed for downside risk protection do not guarantee investors an assured return on their investment.[41] Rather, they limit the losses that an investor incurs. Typically, such options are structured (as in the *Docomo* case) to calculate the sale price as the higher of the prevailing fair market price and a set percentage of the original investment amount. The sale price in put options providing downside protection will not necessarily enable the investor to recover the entire amount it has invested when the put option is exercised by it. In fact, such put options merely establish a floor price for their exercise; fair market value will always be used as a baseline because the selling party will want to preserve that possibility up to the point it merges with the floor amount. From a regulatory perspective, concerns about foreign exchange outflows are mitigated to the extent of the portion of the original investment amount that remains in the country.

Unfortunately, the current blanket regulation of all put options does not appear to contemplate allowing put options even for downside protection. Both types of these put options were effectively made impermissible by a circular issued by the RBI in January 2014,[42] and that position continues to date in the extant rules.[43] As a result, exercise of either type of option by foreign investors leads to Indian parties seeking assurance from regulators that their performance of obligations under investment contracts will not violate local rules, and further lead to assertions by the Indian party that performance in the absence of such assurances is

[39] Makkar & Jain, *supra* note 13, at 412; Davide Contini & Guido Motti, *Option agreements in private equity transactions in Italy*, FINANCIER WORLDWIDE (Oct. 2016), https://www.financierworldwide.com/option-agreements-in-private-equity-transactions-in-italy#.YrItCXbMJPY [https://perma.cc/U553-XD4S].

[40] External Borrowing Rules, *supra* note 35.

[41] NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, ¶ 45 (India); Makkar & Jain, *supra* note 13, at 411-12.

[42] Makkar & Jain, *supra* note 13, at 413; Reserve Bank of India, Pricing Guidelines for FDI Instruments with optionality clauses, RBI/2013-2014/436 (Issued on January 9, 2014).

[43] See *infra* notes 135, 155, and accompanying text.

prohibited.[44] Deadlocks among parties and regulators created by such exercises of exit rights inevitably lead to disputes requiring resort to India's international commercial arbitration regime, which is contained in the Arbitration and Conciliation Act, 1996.[45]

The Arbitration Act of India follows the scheme of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958.[46] The grounds on which the enforcement of a foreign arbitral award can be refused under the Arbitration Act are the same as those under Article V of the New York Convention.[47] These grounds cover the capacity of the tribunal, arbitrability of the dispute brought to the tribunal, and procedural aspects such as the right to notice and the right to present one's case.[48] In addition to the aforementioned grounds, the courts in the country where the enforcement of a foreign award is sought can reject its enforcement if such enforcement would be contrary to the public policy of that country.[49] Indian courts have long grappled with the scope of the public policy exception to enforcing foreign arbitral awards. While the current arbitration law adopts a "pro-enforcement" approach,[50]

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[44] Shahezad Kazi & Aditi Agarwal, *India: Enforcement Of Foreign Awards Granting A Put Option Despite Objections Under The FEMA*, MONDAQ (July 22, 2020), https://www.mondaq.com/india/securities/968018/enforcement-of-foreign-awards-granting-a-put-option-despite-objections-under-the-fema [https://perma.cc/WNP6-B2MW]; Nandan Nelivigi, Dipen Sabharwal QC & Aditya Singh, *In a landmark ruling, Indian court rejects objections to enforcement of a $300 million LCIA award*, WHITE & CASE (June 7, 2017), https://www.whitecase.com/publications/alert/landmark-ruling-indian-court-rejects-objections-enforcement-300-million-lcia [https://perma.cc/WY6Z-EJFU].

[45] Arbitration Act, *supra* note 24.

[46] Convention on the Recognition and Enforcement of Foreign Arbitral Awards, Oct. 6, 1958, 330 U.N.T.S 3 [hereinafter New York Convention].

[47] *See* Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶ 54 (India) (in referring to Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810 (India), " . . . Section 48 of the Act is a statutory expression of Article V of the New York Convention and is similarly worded."); LAW COMM'N OF INDIA, AMENDMENTS TO THE ARBITRATION AND CONCILIATION ACT, 1996, REPORT NO. 246, at 4 (2014) [hereinafter LAW COMMISSION REPORT].

[48] Arbitration Act, *supra* note 24, § 48(1), at 24.

[49] Arbitration Act, *supra* note 24, § 48(2), at 24.

[50] Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶ 47 (India); Debarshi Dutta & Rajat Pradhan, *India: Delhi High Court Reaffirms "Pro-Enforcement" Approach – Enforcement Of Foreign Awards Is Slowly Becoming The Rule*, MONDAQ (July 10, 2020), https://www.mondaq.com/india/arbitration-dispute-resolution/963570/delhi-high-court-reaffirms-pro-enforcement-approach-enforcement-of-foreign-awards-is-slowly-becoming-the-rule [https://perma.cc/LJE3-MGYR].

a 2020 Supreme Court decision has brought back uncertainty regarding the public policy exception's scope.[51]

Foreign arbitral awards based on put option clauses have been consistently challenged on the grounds that their enforcement would violate India's foreign exchange law, and consequently, India's public policy. So far, High Courts and the Supreme Court of India have rejected this reasoning.[52] The courts' stance has been that the public policy exception ought to be applied narrowly and that this approach would have to be followed even when it comes to foreign awards which effectively enforce put options. It has also been held that a contravention of India's foreign exchange laws alone will not warrant the application of the public policy exception.[53] The courts' consistent approach to enforcing foreign awards is an important reassurance for foreign investors. However, this pro-enforcement approach has its limitations; a general commitment to creating a foreign investor-friendly policy and regulatory reform from the Indian government and the RBI are also required to create a stable and predictable investment environment in India. This would also significantly reduce the costs of enforcing contractual exit rights held by foreign investors by reducing disputes and the need to resort to arbitration.

III. THE PUBLIC POLICY EXCEPTION UNDER INDIAN COMMERCIAL ARBITRATION LAW

International arbitration law in India has been consolidated by the Arbitration and Conciliation Act, 1996.[54] The Arbitration Act divides arbitration proceedings into foreign seated arbitration and India seated arbitration.[55] Any reference to a foreign arbitral award is thus a reference to an award of a foreign seated arbitration. This

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51 National Agricultural Cooperative Market Federation in India v. Alimenta, (2020) SCC Online SC 381 (India).

52 *See* Banyan Tree Growth Cap. v. Axiom Cordages Ltd., (2020) SCC Online Bom 781 (India); Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177 (India); NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078 (India); Shakti Nath v. Alpha Tiger Cyprus Inv., (2017) SCC Online Del 6894 (India); Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810 (India).

53 *See* Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶ 97 (India).

54 *See* Arbitration Act, *supra* note 24, Preamble.

55 Pierre Tercier & Dilber Devitre, *The Public Policy Exception – A Comparison of the Indian and Swiss Perspectives*, 5 INDIAN J. ARB. L. 7, 9 (2016).

is significant as the international nature of the dispute (number of international parties) does not have a bearing on how the Arbitration Act treats the award rendered as a result of the dispute.[56] The nature of the award is determined on the basis of the seat of arbitration and not based on the international or domestic status of its parties.[57] This framework has allowed even domestic parties to choose seats of arbitration outside India and have these awards enforced as foreign arbitral awards.[58] High Court decisions have largely supported this practice with a few exceptions[59] and the Supreme Court has not made any conclusive pronouncements on the issue.[60] While the decision of one High Court in India is not binding on others, the prevailing jurisprudence allows domestic parties to choose foreign seats of arbitration.[61] When an foreign party is involved, it is unquestionably clear that parties can choose a foreign seat of arbitration.

In India, the enforcement of foreign arbitral awards is governed by Part II of the Arbitration Act. Section 48 of this Part applies Article V of the New York Convention to India and contains the public policy exception.[62] A key difference between Article V and section 48 in the context of the public policy exception is that the latter explains what comprises public policy. As of 2020, the constituents of an award in violation of public policy have been exhaustively defined as awards that are either the result of any fraud

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56 *Id.*

57 *Id.*

58 *See* GE Power Conversion India v. Pasl Wind Sols. Priv. Ltd., (2020) Petition under Arbitration Act No. 131/2019 (India); GMR Energy Ltd. V. Doosan Power Sys. India, (2017) SCC Online Del 11625 (India); Sasan Power Ltd. v. North Am. Coal Corp. India Priv. Ltd., First Appeal No. 310/2015 (India).

59 *See* Shree Jagdamba Agrico Exps. Ltd. v. Addhar Mercantile Priv. Ltd., (2015) SCC Online Bom 7752 (India); Seven Islands Shipping v. SAH Petroleums Ltd., (2012) SCC Online Bom 910 (India).

60 *See* Tejas Karia, Ila Kapoor & Ananya Aggarwal, *Post Amendments: What Plagues Arbitration in India?*, 5 INDIAN J. ARB. L. 230, 240-41 (2016); Vivek Bajaj & Vinay Butani, *Can two Indian Parties agree to foreign seated arbitration?*, AZB PARTNERS: ADVOCS. & SOLICS. (May 5, 2020), https://www.azbpartners.com/bank/can-two-indian-parties-agree-to-foreign-seated-arbitration/ [https://perma.cc/X8VG-NAPX].

61 Bajaj & Butani, *supra* note 60; Sudipto Dey, *Arbitration proceedings: Order on foreign jurisdiction has a caveat*, BUS. STANDARD (Nov. 7, 2020, 06:10 IST), https://www.business-standard.com/article/companies/arbitration-proceedings-order-on-foreign-jurisdiction-has-a-caveat-120110700070_1.html [https://perma.cc/TE4A-WSU5].

62 Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶¶ 34, 39 (India).

of corruption, or in contravention of the fundamental policy of Indian law, or opposed to the basic notions of justice and morality.[63] Section 48 also clarifies that it cannot be used as a basis to review the merits of a foreign arbitral award. A court's scope of review is limited to the findings of the arbitral tribunal and does not extend to scrutinising the basis of those findings or reviewing the rationale of the arbitral tribunal in arriving at them. This refinement of the public policy exception under the Arbitration Act was effected through an amendment to it in 2015.[64] The circumstances necessitating the 2015 amendment were created by judicial decisions that broadly applied the public policy exception. These decisions also shed light on the underlying uncertainty of the Indian Courts' approach to enforcing foreign awards. The evolution of the application of the public policy exception in India has been discussed below through case laws. These case laws have influenced India's arbitration law not only by establishing precedent but also guiding legislative action.

a. Setting the Course of History – the Renusagar Decision

The case of *Renusagar v. General Electric*[65] (*Renusagar*) was decided by the Supreme Court in 1993, three years before the 1996 Arbitration Act came into effect. The law in force that governed the enforcement of foreign arbitral awards at that time was the Foreign Awards (Enforcement and Recognition) Act, 1961.[66] Like the Arbitration Act, the Foreign Awards Act was also enacted to give effect to the New York Convention.[67] The provisions of the Foreign Awards Act for the objections to the enforcement of foreign arbitral awards are essentially the same as that of the Arbitration Act. The public policy exception in the Foreign Awards Act was contained in section 7(1)(b)(ii). The provisions of section 7 of the Foreign Awards Act and section 48 of the Arbitration Act are substantially the same

63 Arbitration Act, *supra* note 24, ¶ 48(2)(b).

64 Amendments to the Arbitration and Conciliation Act of 1996, No. 3, Acts of Parliament, 2016 [hereinafter Arbitration Amendment].

65 Renusagar Power Co. v. General Electric Co., (1993) 3 SCR 22 (India).

66 Foreign Awards (Recognition and Enforcement) Act, No. 45, Act of Parliament, 1961 [hereinafter Awards Act].

67 *Id.* at Preamble.

and are considered in *pari materia*.[68] A recent Supreme Court judgement (discussed in detail in Part IV) has held that precedents set in the context of section 7 of the Foreign Awards Act will apply to section 48 of the Arbitration Act.[69] This is why the *Renusagar* case continues to be extensively relied on by High Courts and the Supreme Court even though it was not decided under the current commercial arbitration law.[70]

The facts of *Renusagar* concerned provisions of the Indian foreign exchange law which were prevalent at that time and will be discussed in Part IV. Here, the discussion will focus on the interpretation of the public policy exception given under the *Renusagar* case. In *Renusagar*, the Supreme Court acknowledged that it was impossible to come up with an accurate definition of public policy.[71] The court cited its own precedent which explained the meaning of the concept in broad terms. Public policy referred to matters concerning the public good and public interest, but the court acknowledged that the notions of public interest were itself temporal and bound to vary with time.[72] Although the Supreme Court could not define the concept, the court addressed three important questions surrounding it:

1. whether the public policy exception referred to the public policy of India or public policy under private international law;

2. whether the exception ought to be construed narrowly or broadly; and

3. whether a violation of law would amount to a contravention of public policy.

As discussed above, the Foreign Awards Act used the same grounds for refusing the enforcement of a foreign arbitral award as Article V of the New York Convention. However, there was a small difference in how the public policy exception was phrased in both

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68 Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶¶ 34, 39 (India); David Tarh-Akong Eyongndi, *An Appraisal of Perennial Hurdles in the Enforcement of Arbitral Awards in Nigeria and India*, 10 RMLNLU J. 84, 104-05 (2018).

69 Shri Lal Mahal Ltd. v. Progetto Grano SPA, (2014) 2 SCC 433, ¶ 28 (India); Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶¶ 35, 39 (India).

70 Shri Lal Mahal Ltd. v. Progetto Grano SPA, (2014) 2 SCC 433, ¶ 28 (India); Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶¶ 34, 39 (India).

71 *See* Renusagar Power Co. v. General Electric Co., (1993) 3 SCR 22, ¶ 46 (India).

72 *Id.* ¶¶ 46-49.

provisions. Under Article V, the exception referred the "contrary to the public policy of that country" where the award's enforcement was being sought.[73] Differing from this wording, the Foreign Awards Act simply stated that a "contravention of public policy" could be used as a reason by a court to withhold a foreign award's enforcement in India. This raised a question about the scope of public policy under the Foreign Awards Act, specifically whether section 7 was referring to public policy in the context of international private law or the public policy of India.

The party opposing the enforcement of the foreign arbitral award contended that the text of section 7 of the Foreign Awards Act needed to be interpreted as conferring an expansive definition to the phrase "public policy" and one that would go beyond the public policy of India. Article V of the New York Convention clearly stated that an award contravening the public policy of the enforcing jurisdiction need not be enforced by the respective court. Section 7 did not have such a qualification for its public policy exception and only referred to public policy as an exception without specifying whether it was referring to the public policy of India. The Supreme Court rejected this argument and held that the intention behind not explicitly stating which public policy comprised an exception under the Foreign Awards Act could not have been to deviate from the New York Convention. The Foreign Awards Act was enacted with the objective of enforcing the provisions of the New York Convention.[74] Hence, an assumption that an absence of a qualification of public policy was intended to go against the provisions the New York Convention would be untenable. The Supreme Court also referred to the United Kingdom Arbitration Act of 1975 which was also enacted to enforce the New York Convention. The public policy exception in the UK Arbitration Act also did not explicitly refer to the public policy of England. However, the interpretation and application of the provision was still limited to the public policy of the England. A key reason for this was that courts in the UK were not adequately equipped to inquire into the public policy of other jurisdictions.[75] In *Renusagar*, the court also found practical difficulties in using the standard of international public policy, because it would be more difficult to

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73 New York Convention, *supra* note 46, art. V(2)(b).

74 Awards Act, *supra* note 66, at Preamble.

75 Renusagar Power Co. v. General Electric Co., (1993) 3 SCR 22, ¶ 44 (India).

define and prone to subjective interpretation by different states.[76] Based on all these reasons, the Supreme Court in *Renusagar* confirmed that the public policy exception was concerned with contraventions of India's public policy.

After resolving the question of which public policy could be a consideration for refusing to enforce an award, the *Renusagar* bench determined the manner in which the public policy exception should be applied. Precedent from England showed that there were two approaches to construing the exception: the broad view and the narrow view.[77] The key distinction between the two views is the level of judicial intervention permissible under each of them. The narrow view requires courts to be judicious in their application of the exception and refrain from adding to the constituents of public policy.[78] The broad view allows courts more latitude to include different heads under the public policy exception.[79] When *Renusagar* was being decided, the Supreme Court had already criticised the broad view of the exception because it enabled judicial activism and allowed for the courts to decide the contents of the law rather than interpret it.[80] However, the Supreme Court's position was not consistent; some decisions prior to *Renusagar* did not ascribe to the narrow view and preferred the broad view.[81] The *Renusagar* court decided to adopt the narrow view and held that the design of the Foreign Awards Act was meant to facilitate the smooth enforcement of foreign arbitral awards. In order to reach its conclusion, *Renusagar* referred to precedent from the United States[82] which emphasised the pro-enforcement framework of the New York Convention.[83] The U.S. Supreme Court had concluded that countries cannot expect to access the benefits of international trade and foreign markets (and capital) based on their own terms and laws

76 *Id.* ¶¶ 62-63.

77 *Id.* ¶ 48.

78 *Id.*

79 *Id.*

80 *Id.*; *see* Gherulal Parakh v. Mahadeodas Maiya, AIR 1959 SC 781, 22-23 (India); Egerton v. Brownlow (1853) 4 H.L.C. 1.

81 Renusagar Power Co. v. General Electric Co., (1993) 3 SCR 22, ¶ 49; *see* Murlidhar Agarwal v. State of Uttar Pradesh, AIR, 1974 SC 1924 (India).

82 Renusagar Power Co. v. General Electric Co, (1993) 3 SCR 22, ¶ 59 (India); *see* Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974).

83 Scherk v. Alberto-Culver Co., 417 U.S. 506 (1974).

alone.[84] The same rationale would apply to the dispute resolution mechanism for matters related to international trade; a country could not have all disputes relating to it or its residents decided based on its own domestic laws.[85]

The Supreme Court then turned to the question of the implications of a foreign arbitral award violating Indian laws. In *Renusagar* the Supreme Court compared the Foreign Awards Act to the Geneva Convention of 1927 and the Protocol & Convention Act of 1837. The public policy exception in these laws differentiated between a country's public policy and its laws; either could be independently used as a basis to refuse the enforcement of an award by a court. Contrastingly, the Foreign Awards Act referred to public policy "and" the law of India.[86] In *Renusagar,* the Supreme Court held that because public policy was not equivalent to the law of India, a violation of a law alone will not warrant the application of the public policy exception.[87] Importantly, the public policy exception could not be used to replicate the result of a domestic adjudication. Even if the foreign award reaches a different conclusion than a domestic court would have, this cannot be the basis for rejecting the enforcement of the arbitral award.[88] In order to add more clarity to the limits of the public policy exception, *Renusagar* provided three instances when an award could be set aside on the grounds public policy:

1. when it contravenes the fundamental policy of Indian law; or
2. the interests of India; or
3. justice and morality.

The *Renusagar* case, and its three-pronged conceptualisation of the public policy exception, have reverberated through India's commercial arbitration jurisprudence for over two decades. As already discussed, the Arbitration Act treats domestic awards and foreign seated awards differently. The counter part of section 48 (foreign arbitral awards) for the purpose of domestic arbitral awards

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[84] *Id.*; Renusagar Power Co.v. General Electric Co., (1993) 3 SCR 22, ¶ 59 (India); *see* Eyongndi, *supra* note 68, at 103.

[85] Renusagar Power Co. v. General Electric Co., (1993) 3 SCR 22, ¶ 59 (India).

[86] *Id.* ¶ 66.

[87] *Id.* ¶ 65.

[88] *Id.* ¶ 60; *see* Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614 (1985).

is section 34. When the Act was introduced in 1996, sections 34 and 48 contained the same provisions, seemingly implying that domestic seated and foreign seated arbitral awards would be enforceable based on the same criteria. Despite *Renusagar*, the broad view for the application of the public policy exception started taking root in the context of foreign arbitral awards on account of the similarities between sections 48 and 34.

b. Fluctuations in the Conception of Public Policy Under the Arbitration Act, 1996

The *Renusagar* case has been applied by the Supreme Court in subsequent decisions to support both the broad and narrow views for the application of the public policy exception. This itself is a testament to the unpredictability of the reach of public policy in the context of international commercial arbitration. The judiciary's reins on the concept of public policy were first relaxed in the case of *ONGC v. Saw Pipes*.[89] Oil and Natural Gas Corporation (ONGC), an Indian corporation majority owned by the government, had issued a tender for the supply of pipes for one of its projects. Saw Pipes, also an Indian corporation, was selected to supply these pipes to ONGC, but because of a general steel workers' strike across Europe, Saw Pipes was unable to procure the raw material to supply ONGC with the pipes on time. ONGC granted Saw Pipes a forty-five-day extension to make their delivery provided that liquidated damages for the delay in supply (per the contract) were deducted from the consideration payable by ONGC. Saw Pipes disputed this deduction and the matter was referred to domestic arbitration.

The domestic arbitral tribunal found that there were other causes to the delay experienced by ONGC in its project and that it had suffered no losses from Saw Pipes' late delivery. The tribunal used the Indian Contract Act, 1872 and case laws to hold that ONGC had to show that it had suffered damages in order to claim the liquidated damages, which it had not done. Accordingly, it held that the deducted amount from Saw Pipes' consideration had to be returned with an interest of twelve percent. The enforcement of this award was challenged before the Supreme Court. The Supreme Court reviewed the decision of the arbitral tribunal and held that it had erroneously applied Indian law and the terms of the contract to

[89] Oil & Nat. Gas Corp. v. SAW Pipes Ltd., (2003) 5 SCC 705 (India).

make its award and held the award to be "patently illegal." It was stated that the illegality must go to the root of the matter and not simply be an erroneous application of the law. Further, the enforceability of liquidated damages is also not a settled question under Indian law.[90] The Supreme Court here was making an active choice to prefer its application and interpretation of the law over that of the arbitral tribunal. However, before the Supreme Court could act on its finding that the award was patently illegal; it had to establish that public policy under section 34 of the Arbitration Act permitted the inclusion of new categories under it.

On the question of the scope of public policy under section 34, the Supreme Court differentiated it from section 48 of the Arbitration Act and section 7 of the Foreign Awards Act. By doing this, the *ONGC* court restricted the application of *Renusagar*'s ruling that the public policy exception ought to be applied narrowly to foreign arbitral awards alone. The basis of this distinction was that foreign awards are brought before Indian courts only for the purpose of deciding their enforcement and not their validity, "in foreign arbitration, the award would be subject to being set aside or suspended by the competent authority under the relevant law of that country whereas in the domestic arbitration the only recourse is to Section 34."[91]

A foreign award's validity can be challenged before the foreign court which has jurisdiction at the relevant seat of arbitration. However, for domestic awards, Indian courts are the only fora where the award can be challenged both in the context of their enforcement and their validity.[92] Accordingly, the Supreme Court added "patent illegality" as the fourth category to *Renusagar's*

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[90] T.T. Arvind, *The 'Transplant Effect' in Harmonization*, 59 INT'L & COMPAR. L.Q. 65, 76 (2010).

[91] Oil & Nat. Gas Corp. v. SAW Pipes Ltd., (2003) 5 SCC 705, ¶ 11 (India). Although the drafting of section 34 and 48 of the Arbitration Act is almost identical, there is nevertheless a basic and, indeed, a very vital difference between 'refusing enforcement' and 'setting aside' of an arbitral award. Enforcement, be it of a court decree or an award, is a stage which comes after a decree or an award has attained finality. Section 34 deals, not with enforcement, but setting aside of an award. It is Section 36 of the Arbitration Act which deals with enforcement of a domestic award *after* it has become final. This difference between 'refusing enforcement' and 'setting aside' of an arbitral award can also be noted from the Explanatory Note prepared by UNCITRAL to the Model Law. *See* Sidharth Sharma, *Public Policy Under the Indian Arbitration Act: In Defence of the Indian Supreme Court's Judgment in* ONGC v. Saw Pipes, 26 J. INT'L ARB. 133 (2009).

[92] Oil & Nat. Gas Corp. v. SAW Pipes Ltd., (2003) 5 SCC 705, ¶ 11 (India).

existing three categories of public policy. In *ONGC v. Western Geco*,[93] the scope of public policy was further expanded to include the reasonableness of an award under it. This was done by broadly interpreting the first category of public policy (fundamental policy of India) under *Renusagar*.[94] The cases of *Saw Pipes* and *Western Geco* were in the context of domestic arbitration and did not venture into interpreting the scope of the public policy under section 48 (enforcement of foreign arbitral awards).

In 2011, the Supreme Court, in the case of *Phulchand v. O.O.O. Patriot*,[95] held that the broad view of the public policy exception under section 34 could be expanded and applied to section 48 of the Arbitration Act.[96] This meant that a foreign arbitral award could be set aside if a court found that it was patently illegal. In *Phulchand* the Supreme Court probed the merits of the award and ultimately found that it was not patently illegal.[97] However, by giving itself the liberty to consider setting aside a foreign arbitral award on the grounds of patent illegality, the *Phulchand* court set a dangerous precedent. This decision emboldened parties to object to the enforcement of foreign arbitral awards on the grounds that they contravened the terms of the underlying contract between parties. This would make awards patently illegal as the Arbitration Act requires that tribunals decide cases while considering terms of the contract.[98] An attempt to set aside a foreign arbitral award based on patent illegality was made in the case of *Shri Lal Mahal v. Progetto*.[99] The appellant had asked the Supreme Court to set aside a foreign arbitral award based on the *Phulchand* and *Saw Pipes* decisions.[100] Though the judge who authored the *Phulchand* decision was on the *Progetto* bench, the Supreme Court in *Progetto* overruled *Phulchand*.[101] The *Progetto* court held that the law laid down by

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[93] Oil & Nat. Gas Corp. v. Western Geco Int'l Ltd., (2014) 9 SCC 263 (India).

[94] Varuna Bhanrale, Ashish Kabra & Vyapak Desai, *India: Widened Scope Of "Public Policy" Leaves Arbitral Awards Susceptible To Further Scrutiny By Courts*, MONDAQ (Oct. 15, 2014), https://www.mondaq.com/india/trials-appeals-compensation/347164/widened-scope-of-public-policy-leaves-arbitral-awards-susceptible-to-further-scrutiny-by-courts [https://perma.cc/R4YU-N2UG].

[95] Phulchand Exps. Ltd. v. OOO Patriot, (2011) 10 SCC 300, ¶ 12-13 (India).

[96] *Id.*

[97] *Id.* ¶ 22.

[98] Arbitration Act, *supra* note 24, at 28(3).

[99] Shri Lal Mahal Ltd. v. Progetto Grano SPA, (2014) 2 SCC 433, ¶ 69 (India).

[100] *Id.* ¶¶ 27, 30.

[101] *Id.* ¶ 30.

Phulchand was incorrect and that the narrow interpretation mandated by the *Renusagar* court would apply to the public policy exception under section 48.[102] Thus, the broad approach to interpreting the public policy exception was once again restricted to the context of enforcing domestic awards. This also meant that patent illegality would only be a ground to reject the enforcement of domestic arbitral awards and not foreign ones.[103]

The judicial developments discussed above drew attention to the public policy exception and the enforcement of arbitral awards in India. The Law Commission of India, in its August 2014 Report (and a Supplementary Report which was published shortly thereafter),[104] agreed with the Supreme Court decision in *Progetto* and stated that increased court intervention is only legitimate in arbitration that is purely domestic in nature, i.e., where there is no international party involved. In other words, the Law Commission favoured a narrower application of the public policy exception to enforcement of arbitral awards in India-seated international commercial arbitrations[105] which are considered to be domestic awards under the Arbitration Act.[106] The Report noted that the judiciary's approach prior to *Progetto* in cases such as *Saw Pipes* and *Phulchand* was not arbitration friendly and went against the ethos of the New York Convention. The Law Commission Report recommended amendments to sections 34 and 48 to streamline the use of the public policy exception. Both sections were amended to include *Renusagar's* three-pronged enumeration of public policy except for the category referring to "the interests of India." The Law Commission found that this category was vague and amenable to broader application and interpretational misuse.[107] The final three

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102 *Id.* ¶¶ 27, 30.

103 *Id.*

104 LAW COMMISSION REPORT, *supra* note 47; LAW COMM'N OF INDIA, SUPPLEMENTARY TO REPORT NO.246 ON AMENDMENTS TO ARBITRATION AND CONCILIATION ACT, 1996: "PUBLIC POLICY," (2015) [hereinafter SUPPLEMENTARY REPORT].

105 Arbitration Act, *supra* note 24, § 2(1)(f) (defining "international commercial arbitration").

106 Arbitration Act, *supra* note 24, § 2(7), provides that ". . . [a]n arbitral award made under this Part [Part I of the Act] shall be considered as a domestic award." Section 2(2) states that Part I ". . . shall apply where the place of arbitration is in India."

107 SUPPLEMENTARY REPORT, *supra* note 104, at 7 ("…in its 2003 decision . . . the Supreme Court opened the floodgates so far as judicial interference in arbitrations was concerned.").

enumerations of the public policy exception under sections 34 and 48 proposed by the Report included an award effected by (1) fraud and corruption; or (2) against the fundamental policy of Indian law; or (3) in contravention to the basic principles of morality and justice.[108] The proposed amendment was meant to make the definition of public policy exhaustive. A contravention of public policy could occur only if the award met any of the three criteria mentioned above. As for the "patent illegality" criteria added by *Saw Pipes,* the Report recommended that the same be retained but decoupled from the notion of public policy. It was suggested that patent illegality be added to section 34 through a separate provision and applied as a ground to set aside arbitral awards arising out of arbitrations other than international commercial arbitrations. This would prevent any misconception that patent illegality falls under the public policy exception or that it can be used to set aside a foreign award under section 48. The Supplementary Report went one step further and recommended that section 34 should explicitly state that courts are not allowed to review an award on its merit to decide whether it falls within the "fundamental policy of Indian law" category of the public policy exception.[109] This recommendation was made to directly address the expansive interpretation *Western Geco* had given to the fundamental policy of Indian law under the public policy exception. By prohibiting the review of an award's merits, the Report intended to prevent courts from setting aside awards on the grounds of unreasonableness or any other disagreement with the approach taken by the arbitral tribunal.[110]

The Government of India accepted all the recommendations of the Law Commission Report and Supplementary Report, which were followed by Parliament's enactment of the Arbitration and Conciliation (Amendment) Act, 2015.[111] Parliament's amendment went one step further and applied the Supplemental Report's recommendation for section 34 to section 48 as well.[112] As the law currently stands, the public policy exception is exhaustively defined through three headings recommended by the Report under section 34 and section 48, and patent illegality is a separate ground under section 34 to set aside an arbitral award passed in India-seated

108 SUPPLEMENTARY REPORT, *supra* note 47, at 14.

109 SUPPLEMENTARY REPORT, *supra* note 104, at 19-20.

110 SUPPLEMENTARY REPORT, *supra* note 104, at 14-15, 19-20.

111 Arbitration Amendment, *supra* note 64.

112 Arbitration Amendment, *supra* note 64, § 34, § 48.

arbitrations (domestic arbitral awards) other than international commercial arbitrations.[113] Enforcement of a foreign arbitral award can now be refused under section 48 on the grounds of violating the public policy of India only if the award:

1. is a result of fraud or corruption; or
2. contravenes the fundamental policy of Indian law; or
3. opposes the most basic notions of justice or morality.[114]

Finally, the amendment ensured that the court cannot review the merits of an award in order to decide whether or not it is in contravention to the fundamental policy of India. A bare reading of the amended text of the Arbitration Act conveys an expectation of judicial restraint, especially in the context of setting aside foreign arbitration awards. The Amendment Act was considered a step towards a pro-enforcement direction for commercial arbitration in India.[115]

c. Regressive Currents in India's Arbitration Waters: NAFED v. Alimenta

The mandate of the amended Arbitration Act greatly clarified the standard by which foreign arbitral awards based on put options are enforced in India by the judiciary. Before looking at the evolution of the judicial interpretations of the public policy exception in the context of the foreign exchange law, this Part will conclude with an overview of the Supreme Court's recent decision in *National Agricultural Cooperative Market Federation in India ("NAFED") v. Alimenta*.[116] This case is important as it marks yet another turn in the Indian judiciary's approach to the public policy exception and could potentially make courts regress to the broad approach of the exception's application.

NAFED (an Indian canalizing agency) entered into a contract with Alimenta (a U.S. company) to ship 5,000 metric tonnes of groundnuts (commodity). Only 1,900 metric tonnes of the

113 Arbitration Act, *supra* note 24, § 34(2A).

114 Arbitration Act, *supra* note 24, § 48(2).

115 Tercier & Devitre, *supra* note 55, at 25.

116 Nat'l Agric. Coop. Mktg. Fed'n of India v. Alimenta S.A., (2020) SCC Online SC 381 (India).

commodity could be shipped in the time period stipulated in the contract. The shipment of the remaining 3,100 tonnes was delayed on account of cyclones in India that affected crop yield.[117] After a series of addendums, it was agreed that the remaining 3,100 tonnes would be shipped by NAFED in the year 1980-81, instead of 1979-80 as initially envisioned by the contract.[118] NAFED was prevented from shipping the commodity as agreed to in the addendum because of a government prohibition in place. The prohibition prevented carrying over exports for one year into another after 1980 without government permission. NAFED stated that it did not realise that it required government permission to enter into the addendum where it committed to ship the commodity in the year 1980-81. NAFED had assumed that the permission granted to it in the period of 1977-80 would be carried over to the next year as it was the same contract being executed.[119] When NAFED was unable to deliver the remaining amount of the commodity, Alimenta opted for arbitration (seated in London) and was awarded damages payable by NAFED.[120]

When the Supreme Court of India considered the enforcement of the arbitral award in *NAFED*, it had to do so under the Foreign Awards Act, as the case arose before the Arbitration Act was enacted. Despite using the provisions of the Foreign Awards Act, *NAFED* remains relevant because previous Supreme Court decisions have used case laws under the Foreign Awards Act to interpret the public policy exception under section 48 of the Arbitration Act.[121] It has been held that the public policy exception under the Foreign Awards Act is *pari materia* or substantially similar to those under section 48 of the Arbitration Act.[122] In *NAFED,* the Supreme Court did not restrict itself to precedent relating to the Foreign Award Act and traversed cases from *Renusagar* to *Progetto*. *NAFED*'s final interpretation of the public policy exception is thus an authoritative application of the precedent it has relied on. Even though the Foreign Award Act is no longer applicable, *NAFED*'s

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117 *Id.* ¶ 3.

118 *Id.* ¶ 6-7.

119 *Id.* ¶ 8.

120 *Id.* ¶ 22.

121 Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177 (India); Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810 (India).

122 Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, ¶¶ 34, 39 (India); Nat'l Agric. Coop. Mktg. Fed'n of India v. Alimenta S.A., (2020) SCC Online SC 381, ¶ 67 (India).

interpretation of Supreme Court precedent on the Arbitration Act (to support the broad approach taken by it) can be used in the context of other cases under the Arbitration Act.[123] Accordingly, *NAFED* has the potential to influence the application of the public policy exception under section 48 in future cases.

When the Supreme Court considered the enforcement of the arbitral award in favour of Alimenta, it took an approach that was closer to the *Saw Pipes* decision (which permitted courts to broadly construe the public policy exception) than the *Progetto* decision (which required courts to narrowly apply the public policy exception). Going against its own precedent, the Supreme Court in *NAFED* reviewed the facts of the case and the merits of the award. It used the Indian Contract Act and Indian case laws to state that the conclusion reached by the arbitrator that NAFED owed damages to Alimenta was untenable and incorrect. This was despite the fact the law applicable to the construction of the contract based on the agreement between the parties (and quoted by the Supreme Court) was English contract law.

After detailing why the award was incorrect, the Supreme Court set it aside on the grounds that it was opposed to the fundamental policy of India relating to exports. This conclusion was reached based on the apparent infirmities of the award as identified by NAFED and the fact that shipping a regulated commodity would contravene the government's export regulations.[124] This is another instance of where the fundamental policy of India has been applied broadly. The Supreme Court identified export policy and laws as being a part of the fundamental policy of India.[125] However, it remains unclear what separates this policy from others. As mentioned above, this judgement was rendered under the Foreign Awards Act and some writers have stated that for this reason, it will not be binding on future benches of the Supreme Court.[126] Others

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[123] Shaneen Parikh & Surya Sambyal, *Enforcement of Foreign Awards in India—Have the Brakes been Applied?*, CYRIL AMARCHAND MANGALDAS: INDIA CORP. L. (Apr. 27, 2020), https://corporate.cyrilamarchandblogs.com/2020/04/enforcement-of-foreign-awards-in-india-have-the-brakes-been-applied/ [https://perma.cc/AA4U-T92T].

[124] Nat'l Agric. Coop. Mktg. Fed'n of India v. Alimenta S.A., (2020) SCC Online SC 381, ¶¶ 68-69 (India).

[125] *Id.*

[126] S. Sreesh, *India: Enforcement Of Foreign Arbitral Awards—Scope Of Public Policy And Recent Developmental Perspectives*, MONDAQ (Sept. 2, 2020), https://www.mondaq.com/india/trials-appeals-

suggest that the case can be used to justify a broader application of the public policy exception when deciding on the enforcement of foreign arbitral awards.[127] *NAFED* thus gives rise to legitimate concerns. At the very least, it is safe to say that *NAFED* demonstrates the malleability of the Supreme Court's pro-enforcement approach.[128]

Having discussed the scope and limitations of the public policy exception and the Indian judiciary's approach to enforcing foreign awards, this Article now turns to the question of foreign arbitral awards that deal with put options. The Indian Supreme Court and High Courts have successfully kept such awards out of the reach of the public policy exception, but there are unique challenges to enforcing awards relating to put options in India. The next Part discusses all of these issues in detail.

IV. ENFORCING PUT OPTIONS THROUGH FOREIGN ARBITRAL AWARDS

The approach taken by the High Courts and the Supreme Court in enforcing arbitral awards relating to put option clauses has been a liberal one that has deferred to the reasoning of arbitral tribunals and strictly applied the public policy exception. This has been grounded in the permissive nature of India's current foreign exchange regulatory regime (as discussed below) and the courts' refusal to interfere with the enforcement of foreign arbitral awards,

compensation/981256/enforcement-of-foreign-arbitral-awards--scope-of-public-policy-and-recent-developmental-perspectives?type=mondaqai&score=74 [https://perma.cc/N9EZ-4BM2]; Sathvik Chandrashekar, *The Indian Supreme Court's Judgment in NAFED v. Alimenta S.A.: Retrogressive or Wholly Irrelevant? Implications for India's Pro-Arbitration Project*, AM. REV. INT'L ARB.: BLOG (July 21, 2020), http://aria.law.columbia.edu/the-indian-supreme-courts-judgment-in-nafed-v-alimenta-s-a-retrogressive-or-wholly-irrelevant-implications-for-indias-pro-arbitration-project/ [https://perma.cc/E48L-8PZG].

127 *See* Parikh & Sambyal, *supra* note 123; R. Harikrishnan, *NAFED v. Alimenta S.A.: Has the Indian Supreme Court Opened a Pandora's Box on Enforcement of Foreign Awards?*, KLUWER ARB. BLOG (July 11, 2020), http://arbitrationblog.kluwerarbitration.com/2020/07/11/nafed-v-alimenta-s-a-has-the-indian-supreme-court-opened-a-pandoras-box-on-enforcement-of-foreign-awards/ [https://perma.cc/K6SD-7FUP].

128 Parikh & Sambyal, *supra* note 123; Harikrishnan, *supra* note 127.

especially after the 2015 amendment of the Arbitration Act.[129] Despite the courts' pro-enforcement approach, challenges to ensuring a stable and predictable regulatory environment for investors remain. This Part examines these challenges through important case laws decided by the High Courts and the Supreme Court of India. Before delving into individual cases, the following discussion outlines the foreign exchange laws governing put options exercisable by foreign investors in India.

a. Regulatory Framework Under the Foreign Exchange Management Act

India's parent foreign exchange law is the Foreign Exchange Management Act, 1999 (FEMA).[130] FEMA is principally administered by the RBI which is endowed with delegated legislative powers to frame regulations and issue directions under the Act; on certain aspects, the power vests with the Central Government which makes rules.[131] Accordingly, put options are governed by provisions under FEMA and delegated legislations such as rules, regulations and circulars as issued thereunder and amended from time to time (collectively referred to as FEMA Regulations). The following discussion maps current laws and regulations governing put options exercisable by foreign investors in India.

The current scheme of regulation[132] under FEMA is that a transaction is prohibited unless (i) it is covered by a general

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[129] The current regulatory regime does not impose absolute prohibitions and retains a room for discretionary approvals by the Central Bank. "Permissive" in the context of India's foreign exchange regime, therefore, does not refer to leniency. Rather it is a key feature of India's foreign exchange regulations which do not declare all transactions that contravene it to be void. The RBI has the ability to permit a transaction that goes against foreign exchange regulations.

[130] Foreign Exchange Management Act, 1999 [hereinafter FEMA].

[131] *See id.* Sections 11 and 47 deal with powers of the RBI to issue directions and frame regulations. The Central Government has powers to make rules under § 46 of FEMA.

[132] This regulatory scheme can be gathered from the express provision under FEMA §3(a)-(c), which states:

> Save as otherwise provided in this Act, rules or regulations made thereunder, or with the general or special permission of the Reserve Bank, no person shall–(a) deal in or transfer any foreign exchange or foreign

statutory or regulatory permission or (ii) the RBI gives special permission for the transaction. Thus, under FEMA there are three permissible means of dealing in foreign exchange, the first is through any transaction that has been allowed by FEMA itself, the second is through transactions that are covered by the general permission under FEMA Regulations, and the third is through transactions for which special permission of the RBI has been obtained.

Furthermore, there is an important distinction between the regulatory approach under FEMA to a capital account transaction and a current account transaction. Section 2(e) of FEMA defines "capital account transactions" to include "a transaction which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of persons resident outside India." Section 2(j) of FEMA defines "current account transactions" generally as "a transaction other than a capital account transaction" including some illustrative transactions specified in the section.

Section 5 of FEMA permits dealings in foreign exchange which are a part of current account transactions, subject to "such reasonable restrictions for current account transactions as may be prescribed" by the Central Government in consultation with the RBI and in the public interest.[133] Therefore, the regulatory approach to current account transactions appears to be more liberal inasmuch as they are permissible as long as they are not prohibited. In contrast, capital account transactions are more closely regulated by FEMA. Section 6 of FEMA allows dealing in foreign exchange for a capital account transaction. The class or classes of capital account transactions which are *permissible* have to be specified by the RBI and the Central Government in consultation with each other. Until October 2019, the RBI was empowered to frame regulations to allow, in consultation with the Central Government, the classes of capital

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> security to any person not being an authorised person; (b) make any payment to or for the credit of any person resident outside India in any manner . . . ."

Accordingly, the RBI has an overarching, discretionary power to grant special permission for any dealing in, or transfer of, foreign exchange or of a foreign security or payment to any person resident outside India that falls within FEMA and is not generally permitted under FEMA, its rules or any of the regulations framed by the RBI. The Indian Supreme Court has recognized that special permission can be given by the RBI even *ex post facto*. *See* Life Ins. Corp. of India v. Escorts Ltd., (1986) 1 SCC 264, ¶ 65 (India).

133 FEMA, *supra* note 130, § 5.

account transactions along with conditions such as the set limit up to which they are permissible.[134] Pursuant to certain amendments to FEMA notified in October 2019, the power to specify permissible capital account transactions involving "debt instruments" now vests in the RBI whereas those involving non-debt instruments (e.g., equity instruments) rests with the Central Government which has to consult with the RBI.[135] Thus, in so far as capital account transactions are concerned, unless the RBI and the Central Government have specified them to be permissible, they are considered to be prohibited, except where a special permission is sought and granted. Prior to the 2019 Amendments to FEMA, Section 6(3) of FEMA gave an illustrative list of the classes of capital account transactions that the RBI is empowered to prohibit, restrict or regulate. One such class of capital account transaction was "transfer or issue of any security by a person resident outside India."[136] Under Section 47 of FEMA, the RBI had the general power to make regulations in relation to, inter alia, "the permissible classes of capital account transactions, the limits of admissibility of foreign exchange for such transactions . . . and the prohibition, restriction or regulation of such capital account transactions under Section 6."[137]

Put options contemplate capital account transactions because, when exercised by the foreign investor, they result in a transfer of security (shares) by the non-resident shareholder, thereby constituting a transaction that alters the assets or liabilities in India of persons resident outside India. Since they are capital account transactions, the RBI (prior to the 2019 Amendments) had the authority to regulate them under FEMA. The RBI regulated each class of permissible capital account transactions by way of separate regulations made for the class. Using its power to regulate "transfer or issue of any security by a person resident outside India" under the then in force Section 6(3)(b) and Section 47 of FEMA, the RBI

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134 FEMA, *supra* note 130, § 6.

135 Ministry of Finance, S.O. 3715(E) (Notified on October 15, 2019) [hereinafter 2019 Amendments] (India). Consequent to the 2019 Amendments, sections 6, 46, and 47 of FEMA stood amended to provide for the powers of the RBI and the Central Government to make regulations and rules concerning capital account transactions involving debt and non-debt instruments respectively. *See* FEMA, *supra* note 130, § 6(2)(a), (2A), read with § 46(2)(a)-(b) and § 47(2)(a).

136 FEMA, *supra* note 130, § 6(3)(b).

137 FEMA, *supra* note 130, § 47 (2)(a). After the 2019 Amendments, the RBI's power is restricted to debt instruments only; with respect to non-debt instruments, for example, equity instruments, the regulatory power now vests in the Central Government.

regulated the transfers of securities by a person resident outside India to a person resident in India through the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations (commonly referred to as FEMA 20).[138] FEMA 20 contained RBI's regulations on foreign investment. From time to time, the RBI also issued Master Directions,[139] which compiled various instructions issued to Authorised Persons (i.e., persons such as banks who are authorized to deal in foreign exchange) on specific regulations, including foreign investment.[140]

FEMA 20 permitted investment by persons resident outside India subject to certain conditions. One such condition was that the investment and any subsequent share transfer transaction (between a person resident in India and a person resident outside India) have to conform to prescribed pricing guidelines.[141] The pricing guidelines were amended from time to time; the underlying principle of the pricing guidelines being that the shares, in case of transfer from a resident to a non-resident should not be less than their fair market value; and in case of transfer from a non-resident to a resident should not exceed the fair market value.

The policy objective behind RBI's pricing guidelines, particularly in the context of put options, is evident from FEMA 20 itself. *First*, this is evident in the definition of "capital instruments" which, under FEMA 20, were eligible for investment by a foreign investor. The definition of capital instruments, which includes "equity shares," recognised that such instruments "can contain an optionality clause" but should be "without any option or right to exit at an assured price."[142] *Second*, a specific "explanation" that was added to the pricing guidelines in case of transfer of a capital instrument (e.g., share) from a foreign investor to an Indian party. The explanation stated that the "guiding principle" for pricing of the share transfer transaction would be that the person resident outside

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138 FEMA 20 was originally framed and notified by the RBI in the year 2000—"Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, May 2000," as later amended from time to time. These regulations were substituted by the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017, FEMA 20(R)/2017-RB (Nov. 7, 2017) [hereinafter FEMA 20].

139 *See, e.g.*, Reserve Bank of India, Master Direction on Foreign Investment in India, RBI/FED/2017-18/60 (Issued on January 4, 2018) [hereinafter Master Direction].

140 *Id.*

141 *See* FEMA 20, *supra* note 138, § 11.

142 FEMA 20, *supra* note 138, § 2(v)(a).

India (i.e., the foreign investor) is "not guaranteed any assured exit price at the time of making such investment/agreement" and "shall exit at the price prevailing at the time of exit."[143]

These provisions in FEMA 20 (notified in November 2017) followed from their predecessor regulations (FEMA 20 notified in May 2000, and as amended from time to time). The erstwhile FEMA 20 as originally notified in May 2000 did not specifically deal with transfers pursuant to put options. However, the regulations mandated compliance with pricing guidelines.[144] These guidelines were notified by the RBI by way of a circular, which set the price for transfer of shares at fair market value.[145]

Restrictions on put options were first specifically imposed by the RBI in December 2013 by amending FEMA 20 (as was in effect at the time).[146] By this amendment (the 2013 Amendment), the RBI provided that only shares or convertible debentures "without any option/right to exit at an assured price" would be recognised as eligible instruments for investment by non-residents under the automatic route (without requiring RBI's prior approval).[147] These restrictions were further reaffirmed and reiterated by the RBI in amendments to FEMA 20 issued on May 23, 2014 which laid down the new pricing regulations.[148] The new pricing regulations reiterated that a foreign investor could exit under a put option clause provided the exit price did not exceed the fair market value. It further added that the "guiding principle" would be that the foreign investor is "not guaranteed any assured exit price at the time of making such investment/agreements and shall exit at the price prevailing at the time of exit . . . ."[149] This regulatory approach by

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143 FEMA 20, *supra* note 138, § 11(3).

144 *See* FEMA 20 (as originally notified by the RBI in May 2000), *supra* note 138, § 11.

145 Reserve Bank of India, FEMA—Foreign Direct Investment in India—Transfer of Shares/Convertible Debentures by Way of Sale—Simplification of Procedures, A.P. (DIR Series) Circular No. 16 (Issued on October 4, 2004).

146 Reserve Bank of India, Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) (Seventeenth Amendment) Regulations, 2013, FEMA. 294/2013-RB (Issued on November 12, 2013).

147 *Id.* § 2.

148 *See* Reserve Bank of India, Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) (Seventh Amendment) Regulations, 2014, FEMA. 306/2014-RB (Issued on May 23, 2014).

149 Reserve Bank of India, Foreign Direct Investment—Pricing Guidelines for FDI Instruments with Optionality Clauses, A.P. (DIR Series) Circular No. 86 (Issued on Jan. 9, 2014) [hereinafter 2014 Amendment].

way of a guiding principle added through the 2014 Amendment was reiterated in the 2017 version of FEMA 20.[150]

All this while, the mode or methodology of calculating fair market value kept changing.[151] Under FEMA 20 (as notified in November, 2017) the valuation could be done as per any "internationally accepted pricing methodology for valuation of shares on an arm's length basis" duly certified by a Chartered Accountant or a Securities and Exchange Board of India registered Merchant Banker or a practicing Cost Accountant, in case of an unlisted Indian company.[152] In case of a listed company (i.e., a company whose shares are quoted on the stock exchange), the pricing had to be worked out as per the guidelines prescribed by the Securities and Exchange Board of India (SEBI), which is a statutory body that regulates the securities market in India.[153]

As mentioned above, after the 2019 Amendments to FEMA[154] the powers of the RBI and the Central Government have been bifurcated. RBI's power to regulate capital account transactions are now limited to "debt instruments" only. For capital account transactions involving non-debt instruments (such as equity), the regulatory power is given to the Central Government. In exercise of

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150 *See* FEMA 20, *supra* note 138; *see also* Master Direction, *supra* note 139. The Master Direction, at ¶ 7.8.1 states: "A person resident outside India holding capital instruments of an Indian company containing an optionality clause in accordance with FEMA 20(R) and exercising the option/right, can exit without any assured return." At ¶ 8.3.2, it is provided that "the guiding principle would be that the person resident outside India is not guaranteed any assured exit price at the time of making such investment/agreement and shall exit at the price prevailing at the time of exit."

151 In the 2013 Amendment, the valuation methodology was changed to be based on the 'Return on Equity'. In the 2014 Amendment, the methodology for calculation of fair market value was changed to "any internationally-accepted pricing methodology for valuation of shares on an arm's length basis, duly certified by a chartered accountant or a Security and Exchange Board of India-registered merchant banker." This is the methodology which was followed in FEMA 20 (as notified in November 2017) and now the extant rules notified in October 2019 also provide. Prior to these amendments, the regulations required determination of fair market value using the Discounted Cash Flow method of valuation. *See* Res. Bank of India, Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) (Amendment) Regulations, 2010, FEMA 205/2010-RB (Issued on April 7, 2010); *see also* Reserve Bank of India, Foreign Direct Investment (FDI) in India—Transfer of Shares/Preference Shares/Convertible Debentures by Way of Sale: Revised Pricing Guidelines, A.P. (DIR Series) Circular No. 49 (Issued on May 4, 2010).

152 *See* FEMA 20, *supra* note 133, § 11(1)(b).

153 *See* FEMA 20, *supra* note 133, § 1.

154 *See* 2019 Amendments, *supra* note 135.

this power, the Central Government of India has, in consultation with the RBI, notified the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 (Non-Debt Rules 2019).[155] The Non-Debt Rules 2019 have superseded FEMA 20 which governed the field earlier. However, it is not that the Non-Debt Rules 2019 have completely overhauled the existing regime. In so far as treatment of put options and pricing rules are concerned, the regulatory regime remains the same as it was under FEMA 20. The Non-Debt Rules 2019 reiterate the earlier position that a foreign investor holding any equity instruments of an Indian company containing an optionality clause may, in exercise of the option, exit "without any assured return." The pricing guidelines contained in these new rules continue to retain the same valuation methodology and reiterate the same "guiding principle" that ". . . the person resident outside India is not guaranteed any *assured exit price* at the time of making such investment or agreement and shall exit at the price prevailing at the time of exit"[156] (emphasis added).

From the above, it is evident that the RBI, and now the Central Government, while allowing put options, continues to keep a tight control on the price at which the put options can be exercised. This regulatory approach emanates from concerns, which are understandable, that put options of equity securities with guaranteed internal rates of return, as opposed to fair market value valuations, would have impermissible characteristics of debt. The concern with non-residents owning and exercising such options arose from requirements governing incurrence by residents of "external commercial borrowings," or "ECB," which have a number of conditions attached to them including end-use restrictions, minimum average maturity, all-in-cost ceilings, etc.[157]

As stated above, from a policy standpoint the underlying rationale for the restriction on the price payable by the Indian party to the foreign investor under put options was that investors should not be guaranteed any assured returns.[158] However, a dichotomy arises when put options which offer no return and are there only to provide to the foreign investor a downside risk protection are also

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155 Ministry of Finance, S.O. 3732(E) (Notified on October 17, 2019) [hereinafter Non-Debt Rules].

156 *See* Non-Debt Rules, *supra* note 155, §§ 9(5), 21(2)(c)(iii).

157 Reserve Bank of India, Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000, FEMA. 3/2000-RB (Issued on May 3, 2000).

158 *See* 2014 Amendment, *supra* note 149, § 2(b)(iii).

made impermissible. By using the expression "assured exit price" while explaining the guiding principle (both under FEMA 20 and under the extant Non-Debt Rules 2019) the pricing guidelines effectively prevent the exercise of put options where the sale price is different from the fair market value of the securities.[159] This approach fails to differentiate between put options with sale prices guaranteeing assured returns and those that only offer downside protection that cap the extent of an investor's losses without guaranteeing any profits.[160] The pricing guidelines make it technically impermissible for foreign investors to sell their shares at anything above the prevailing stock exchange price in a listed company or, in the case of unlisted companies, at a price not exceeding the fair market value. Though the mode of calculating fair value has been changed from time to time,[161] the implication is the same—exit at predetermined prices remain impermissible. It is in this regulatory backdrop that several cases regarding the enforceability of arbitral awards based on put option clauses were decided by the High Courts and Supreme Court. The following discussion will trace the status of India's foreign exchange laws within the public policy exception and then examine individual cases of High Courts.

b. From Renusagar to Vijay Karia: Decoupling Public Policy and Foreign Exchange Laws

The Supreme Court decision in *Renusagar* has been discussed in Part II in light of its importance for the interpretation of the public policy exception. The narrow view laid down by it continues to be prevalent today to the extent that it has been codified in the Arbitration Act. Despite its restrained approach to the public policy exception, *Renusagar* had held that an award whose enforcement would require a violation of India's foreign exchange laws would contravene public policy.[162] This portion of the *Renusagar* ruling was determined by the facts of the case and the foreign exchange law in force in India at the time.

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159 *See* Non-Debt Rules, *supra* note 155.

160 *See* Makkar & Jain, *supra* note 13, at 400.

161 *See supra* note 151 and accompanying text.

162 *See* Renusagar Power Co.v. General Electric Co., (1993) 3 SCR 22, ¶ 73-83 (India).

General Electric, a company incorporated in New York, entered into a contract with Renusagar to supply equipment for a thermal power plant that Renusagar was constructing.[163] The contract stipulated that Renusagar would pay ten percent of the consideration through cash or a Letter of Credit, the remaining ninety percent was to be paid in sixteen installments (each installment becoming payable every six months) at an interest rate of 6.5 percent. This contract required the approval of the Government of India (as it would entail the outflow of foreign exchange through payments to General Electric) which was granted.[164] The contract also stipulated the reduction of the interest from 6.5 to 6 percent if the Government of India would exempt General Electric from paying taxes on the interest paid to it by Renusagar.[165] The Government of India granted this exemption, but it was withdrawn two years later and cancelled retrospectively; this meant that Renusagar had to pay an interest of 6.5 percent on principle amount.[166] Renusagar approached the Delhi High Court to cancel the Government's revocation of the exemption. Granting Renusagar's request, the Delhi High Court effectively restored the Government of India's tax exemption towards General Electric, thus reducing the interest payable by Renusagar to six percent once again.[167] Despite the Delhi High Court's order, Renusagar did not complete the payments of its due installments. Meanwhile, there were some delays from General Electric's side for the supply of equipment. A revised payment schedule was arrived at by the parties based on which the capitalized interest was calculated using a longer period of time than what was initially decided.[168] Both parties agreed to these revised terms but the Government of India refused to approve the new payment schedule as it would imply an increased outflow of foreign exchange than the original payment schedule.[169] Renusagar did not make further payments to General Electric and the latter decided to file for arbitration on account of not

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163 *Id.* ¶ 32.

164 *Id.* ¶ 33.

165 *Id.*

166 *Id.* ¶ 34.

167 *Id.*

168 *Id.*

169 *Id.*

having received the payment installments. The Arbitral Tribunal gave an award granting General Electric's claims.[170]

The enforcement of the foreign arbitral award was challenged before the Supreme Court on the grounds that it contravened India's public policy by violating its foreign exchange laws. At the time, the Foreign Exchange Regulation Act, 1973 (FERA) was in force.[171] The objectives of FERA were contained in its Preamble and they were unequivocal in prioritizing the conservation of India's foreign exchange reserves. A country's right to protect its economic interests through the use of foreign exchange laws is a recognized principle in private international law,[172] and it is also a prevalent practice.[173] The Supreme Court in *Renusagar* found that all countries, at some point of their history controlled the flow of their foreign exchange to cater to their economic interests;[174] for instance, England did this through the Exchange Control Act, 1947 (suspended in 1979).[175] Informed by this context, *Renusagar* held that any award that would require a violation of FERA would contravene India's public policy. This finding gave the *Renusagar* court the imperative to examine whether the foreign award violated FERA. The Supreme Court found that though the revised payment schedule was not approved by the Government of India (which was required under FERA),[176] the original payment schedule was approved and Renusagar had defaulted in its installment payments even under that schedule.[177] Accordingly, the arbitral tribunal had correctly awarded damages to General Electric. The Supreme Court also made use of section 47 of FERA which allowed damages and debts to be recovered pursuant to a judgment irrespective of the permissibility of the recovery under the general scheme of FERA. However, the Government of India needed to approve the recovery of a sum through a judgement before it could be remitted.[178] The

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[170] *Id.* ¶ 40.

[171] The Foreign Exchange Regulation Act, 1973, No. 46, Acts of Parliament, 1973 (India) [hereinafter FERA].

[172] *See* Renusagar Power Co.v. General Electric Co., (1993) 3 SCR 22, ¶ 74 (India).

[173] *See id.*

[174] *See id.*

[175] *See id.*

[176] *See id.* ¶ 80; FERA, *supra* note 171, § 9.

[177] *See* Renusagar Power Co.v. General Electric Co., (1993) 3 SCR 22, ¶ 83 (India).

[178] *Id.* ¶ 84.

Supreme Court noted that the Government's refusal to approve a revised schedule cannot be assumed as a refusal to enforce any judgement relating to the case as well. Based on this reasoning, it held that the arbitral award did not violate FERA. Though a violation of FERA would have amounted to a contravention of public policy according to *Renusagar*, no such violation was found and this allowed the Supreme Court to enforce the foreign arbitral award.

The portion of the *Renusagar* award which held that a contravention of India's foreign exchange laws would amount to a violation of public policy has been overruled by the Supreme Court through its recent judgment in *Vijay Karia v. Prysmian Cavi*.[179] While the case did not directly relate to put options, the Supreme Court used a Delhi High Court decision on put options to substantiate its judgement.[180] *Vijay Karia* dealt with the enforcement of an award relating to a call option or the right to require shares to be sold at the sale price.[181] Call options are the flip side of put options and confer a right to require shares to be sold at the sale price.[182] In *Vijay Karia*, the foreign investors exercised their right to buy shares of an Indian corporation from an Indian shareholder (Vijay Karia) at the discounted price.[183] Call options, like put options, are also governed by pricing guidelines. The Foreign Exchange (Non-Debt Instrument) Rules of 2019[184] require that transfers of shares from a resident to a non-resident are made at a price that is prevalent in the stock exchange or at an arm's length price as determined through international pricing methodologies by a Chartered Accountant.[185] The sale price explicitly provided for the sale of shares to Prysiman Cavi at a discount and thus did not meet the requirements of the pricing guidelines under the Non-Debt Rules of FEMA.

Beyond the permissibility of call options under the Non-Debt Rules of 2019, the rationale behind objecting to the exercise of this call option was that lesser foreign exchange would be entering the

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179 *See* Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177 (India).

180 *Id.*; *see also* Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810 (India).

181 *See* Makkar & Jain, *supra* note 13, at 401.

182 *See* Makkar & Jain, *supra* note 13, at 401.

183 *See* Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177 (India).

184 *Id.*; *see also* Non-Debt Rules, *supra* note 155, § 9(5).

185 *See* Non-Debt Rules, *supra* note 155, § 21(2)(b)(iii).

country as the shares were being bought by the foreign investor at a discounted price (the sale price). However, the imperative to regulate call options appears to be a less urgent matter from a foreign exchange policy perspective as irrespective of the amount, call options bring some foreign exchange into the country; this was one of the arguments put forth by Prysmian Cavi, the corporation which wanted the arbitral award to be enforced.[186] Nonetheless, the Supreme Court used this case to examine the validity of the claim that any contravention of FEMA would be opposed to the public policy of India.

Referring to *Renusagar*, the Supreme Court pointed out that the objective of India's foreign exchange laws had changed after the enactment of FEMA. Foreign exchange control under FEMA is strict but also permissive. Unlike FERA, there is no provision under FEMA which states that any contract that violates the Act will be automatically void.[187] Rather, the scheme of FEMA allows for violations to be rectified *post-facto* by seeking permission from the

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[186] *See* Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177 (India).

[187] *Id.* ¶ 88. *See also* The Foreign Exchange Regulation Act, 1973, § 47 (Sept. 19, 1973) (India). It is relevant to mention here that in an earlier judgment, which the Supreme Court noted in *Vijay Karia*, the Supreme Court had emphasised that

> insofar as conservation and/or augmentation of foreign exchange is concerned, the restrictions in FEMA continue to be as rigorous as they were in FERA. FEMA continues with the regime of rigorous control of foreign exchange and dealing in the foreign exchange is permitted only through authorised person . . . The conservation and augmentation of foreign exchange continues to be as important as it was under FERA. The restrictions on the dealings in foreign exchange continue to be as rigorous in FEMA as they were in FERA and the control of the Government over foreign exchange continues to be as complete and full as it was in FERA.

Dropti Devi v. Union of India, (2012) 7 SCC 499, 529 (India). In *Vijay Karia*, the Supreme Court did not disagree with these observations but contextualised them by stating that they were made "in the context of preventive detention of persons who violate foreign exchange regulations." The court held that

> to contend that any violation of any FEMA Rule would make such violation an illegal activity does not follow. In fact, even if the reasoning contained in this judgment [*Dropti Devi*] is torn out of its specific context and applied to this case [*Vijay Karia*], there being no alleged smuggling activity which involves *depletion* of foreign exchange, as against foreign exchange coming into the country as a result of sale of shares in an Indian company to a foreign company, it does not follow that such violation, even if proved, would breach the fundamental policy of Indian law.

Id.

RBI.[188] If a transfer of securities (for instance, through a put option) results in a breach of any FEMA regulations, the RBI has the power to condone this breach.[189] Thus, impermissible transactions under FEMA are not inherently violative of its provisions as they can all be potentially permitted by the RBI after they have been carried out.[190] Based on this change in India's foreign exchange regime (from FERA to FEMA), the Supreme Court held that a violation of FEMA can never be a ground to refuse the enforcement of a foreign arbitral award.[191]

The *Vijay Karia* decision has laid to rest the question of the role of India's foreign exchange laws vis-à-vis the public policy exception. There will always be some amount of uncertainty when it comes to the judiciary's approach, and the *NAFED* case is evidence of this as it was rendered amidst a pro-enforcement ethos in the Supreme Court and High Courts. Whether the *NAFED* decision will be an anomaly or used as grounds to challenge *Vijay Karia's* approach cannot be conclusively determined at this stage. However, the *Vijay Karia* decision in addition to the 2015 amendment are likely to maintain the pro-enforcement approach in courts for the future. Part V provides a detailed analysis of the *Docomo* case and uses this as a template to explain the High Courts' approach to put options in the context of foreign arbitral awards. These High Court decisions are also used to explain the limitations faced by investors despite the current pro-enforcement approach taken by the judiciary and establish the urgent need to rationalize India's regulations on put options at the policy level.

V. HIGH COURT DECISIONS: A STEP IN THE RIGHT DIRECTION

a. The Docomo Case

The Delhi High Court decision in *NTT Docomo, Inc. v. Tata Sons Ltd.*[192] is particularly significant because it made a conclusive

[188] *See* Vijay Karia v. Prysmian Cavi e Sistemi, (2020) SCC Online SC 177, 18 (India).

[189] *See id.*

[190] *See id.* at 88.

[191] *See id.* at 90.

[192] *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078 (India).

pronouncement about RBI's role in the enforcement of foreign arbitral awards. The *Docomo* case dealt with the enforceability of a foreign arbitral award made by the London Court of International Arbitration (LCIA).[193] NTT Docomo Inc, a company incorporated in Japan (Docomo), and Tata Sons, Ltd. (Tata) and Tata Teleservices Limited (TTSL), each incorporated in India, had entered into a Shareholders Agreement (SHA) in 2009.[194] The SHA outlined the terms of Docomo's investment in TTSL's business through the purchase of its shares. One of the clauses in the SHA (the sale option clause) provided Docomo with an exit option in case TTSL did not meet certain performance indicators prescribed in the SHA.[195] The sale option clause was, at the minimum, in the nature of a stop-loss provision which permitted Docomo an exit while limiting the extent of its losses. As described in more detail below, the exit option clause provided that Tata would be required to find a buyer for Docomo's shares at a price equivalent to the fair value of the shares on July 7, 2014, or fifty percent of the price at which Docomo purchased TTSL's shares (the sale price), whichever was higher. If Tata could not find a buyer willing to purchase Docomo's shares at the sale price, the clause required Tata to purchase the shares or procure their purchase at any price and indemnify Docomo for the shortfall. This clause essentially performed the functions of a put option for downside protection but was structured to provide Tata with at least with one alternative means to perform its obligations in a manner (by finding a non-resident buyer for the Docomo shares) in which the restrictions imposed by the RBI's pricing guidelines would not apply.[196]

Due to market factors, TTSL was not able to meet the SHA's performance indicators. Consequently, Docomo invoked its right under the sale option clause through a trigger notice on May 30, 2014, and requested Tata to find a buyer for its shares in TTSL.[197] At

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[193] *See* NTT Docomo, Inc. v. Tata Sons Ltd., LCIA Case No. 152896, Final Award (June 22, 2016).

[194] *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 2 (India).

[195] *See id.*

[196] *See* NTT Docomo, Inc. v. Tata Sons Ltd., LCIA Case No. 152896, Final Award (June 22, 2016), ¶ 36; *see also* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 10-11. The LCIA found that the put option clause was drafted in the way that it was because "the Parties knew that exchange control regulations and other considerations might prevent performance under a simple put."

[197] *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 2-3 (India).

that time, the Tata-determined fair value of Docomo's shares in TTSL was INR 23.34 per share which was substantially lower than the sale price of INR 58.045 per share.[198] Upon receiving Docomo's trigger notice, Tata attempted to find a buyer for Docomo's shares but without success. Tata then approached the RBI seeking special permission to remit the price of TTSL's shares to Docomo per the sale option clause, i.e., fifty percent of the price Docomo had paid when it had initially purchased them. The RBI ultimately denied Tata permission to purchase Docomo's shares at the sale price.[199] Unable to reach a resolution through negotiations with Tata, Docomo commenced arbitration proceedings before the LCIA on January 3, 2015.[200]

In the case before the LCIA, Docomo claimed damages from Tata in lieu of its performance of its obligations under the sale option clause. Tata argued that the sale option clause was a "waterfall" clause involving different stages of sequential performance.[201] This meant that Tata's obligation was a qualified one and would be considered as fulfilled once Tata had attempted to fulfill it using the alternative means provided under the SHA. The sale option clause contemplated that Tata would first attempt to find a buyer for Docomo's shares at the sale price. If no such buyer was found, then Tata could acquire or procure the acquisition of Docomo's share at any price and indemnify Docomo for the remaining amount.[202] Tata argued that it had tried to find non-resident buyers and then approached the RBI for permission to purchase the shares itself.[203]

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198 *See id.* at 31; *see also* NTT Docomo, Inc. v. Tata Sons Ltd., LCIA Case No. 152896, Final Award (June 22, 2016), at ¶ 50; *see also* Anandita Singh Mankotia & Deepshika Sikarwar, *RBI eases fair value buyout norm, allows Tatas to pay DoCoMo previously agreed price for Tata Tele stake*, ECON. TIMES (last updated Jan. 14, 2015, 08:19 AM IST), https://economictimes.indiatimes.com/news/economy/policy/rbi-eases-fair-value-buyout-norm-allows-tatas-to-pay-docomo-previously-agreed-price-for-tata-tele-stake/articleshow/45879202.cms?from=mdr [https://perma.cc/9VHK-TUCW].

199 *See* NTT Docomo, Inc. v. Tata Sons Ltd., 2017 SCC Online Del 8078, 10 (India).

200 *See id.* at 3.

201 *See* NTT Docomo, Inc. v. Tata Sons Ltd., LCIA Case No. 152896, Final Award (June 22, 2016), ¶ 89(1) (India).

202 *See id.*

203 *See id.* ¶ 89(5). Tata argued that if FEMA required special permission for Tata to purchase Docomo's shares at the sale price then it meant that the sale option clause was subject to a condition that RBI granted that permission.

These attempts meant that Tata had fulfilled its obligations towards Docomo.[204]

The LCIA was unpersuaded by this reasoning and found in a unanimous decision that the sale option clause contained an unqualified and absolute obligation on Tata's part to secure Docomo's exit at the sale price.[205] The LCIA held that the sale option clause was neither illegal under FEMA nor did it require RBI permission to be obtained. Tata was free to find a non-resident buyer for Docomo's shares and no RBI approval was required under FEMA for the transfer of shares in an Indian company from a non-resident to another non-resident. However, no non-resident was willing to purchase Docomo's shares in TTSL at the sale price given that their fair market value was well below such price. Furthermore, no non-resident was willing to purchase the shares at any price. Accordingly, the impediment Tata faced in fulfilling its obligations under the exit option clause, the LCIA held, was a factual one (inability to find a non-resident buyer) and not a legal one.[206] The need for RBI permission to enable Tata itself to purchase the shares from Docomo and its denial were consequences of this factual impossibility and did not affect the validity of the sale option clause or the nature of Tata's unqualified obligation towards Docomo under it to find a buyer willing to purchase the shares.[207] Accordingly, Tata was obligated to indemnify Docomo for the full amount of the obligation as provided in the contract (of course, if a willing buyer had been found at an amount below the floor price, Tata's indemnification obligation would have been limited to the shortfall). The LCIA disagreed with Tata's "waterfall" analogy and agreed with Docomo's interpretation of the SHA and held that Tata's inability to fulfill its obligation through the alternative routes described would not discharge Tata of these obligations

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204 *See id.* ¶ 89. In support of its "waterfall" analogy, Tata had also relied upon a clause in the SHA which provided that no party would take any action or have any right that would violate applicable law. The parties were then required to negotiate in good faith an alternative structure which would give to Docomo the substantial benefits intended by the sale option clause. However, the parties could not agree upon such an alternative structure. Since Tata claimed it had attempted to perform at each stage of the sequential performance with reasonable diligence, it argued that it was discharged by law; therefore, there was no breach.

205 *See id.* ¶ 121.

206 *See id.* ¶ 139-40.

207 *See id.*

altogether.[208] Once it was held that Tata's primary obligation (the obligation to find a buyer) was an unqualified one, the LCIA found that the question whether a contractual obligation remains enforceable if it is subject to a requirement for special permission under the FEMA Regulations does not arise. Nor was it necessary for the LCIA to decide whether special permission was required in order for Tata to make payment under the indemnity in the sale option clause, or the effect in law of RBI's refusal of special permission.[209] Based on this reasoning, the LCIA awarded damages to Docomo equivalent to the sale price under the exit option clause together with interest. Docomo and Tata eventually entered into consent terms based on the award.[210]

When Docomo approached the Delhi High Court to enforce the LCIA award the RBI filed an application to intervene in the case before the court. The RBI disagreed with the LCIA's reasoning and filed an application to be impleaded in the enforcement proceedings before the Delhi High Court. Given that Tata had already agreed to comply with the award and had agreed on consent terms, the main opposition to the award's enforcement came from the RBI.[211] It was argued that the award overlooked FEMA regulations and that because of this, its enforcement would be against the public policy of India.[212] The High Court rejected the RBI's argument and found

[208] *See id.* ¶ 120-21. The LCIA held that Tata's primary obligation—to find a buyer for Docomo's shares at the sale price—was absolute. Tata might have been able to avoid a breach of its primary obligation by availing itself of one of the alternative methods of performance provided for in the second part of the sale option clause; but if Tata was not able to do so, it remained in breach and was liable to pay damages to Docomo. *See also* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 11 (India).

[209] *See* NTT Docomo, Inc. v. Tata Sons Ltd., LCIA Case No. 152896, Final Award (June 22, 2016), at ¶ 140 (India).

[210] *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 17-21 (India). Tata had initially contested enforcement of the LCIA Award but subsequently agreed to withdraw its objections to enforcement and pay to Docomo the entire amount due under the award, subject to the Delhi High Court ruling on the objections raised by the RBI in its intervention application.

[211] Tata did not contest the validity per se of the put option or the agreement on the price that was payable to Docomo under the put option; Tata claimed that its obligations were subject to the RBI's approval. In the enforcement proceedings before the Delhi High Court after the RBI had intervened, Tata consented to pay the amount under the award if the court rejected the objections raised by the RBI, which the court ultimately did. For Tata, its reputation and record of adherence to contractual commitment was also important, NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078 at 62-64 (India). *See id.* at 21-25.

[212] *Id.* at 22.

that the award had adequately dealt with the legality of the SHA in the context of FEMA regulations and that the arbitral tribunal's decision would be binding, even on the RBI. The case did not require the court to go as far as to explain why the public policy exception cannot be invoked solely on the basis of any illegality. This is because the LCIA had found, and the court agreed, that the structure of the transaction and the design of *Docomo's* exit rights did not contravene the RBI's regulations per se simply because they guaranteed to Docomo a minimum assured exit price. The court held that the SHA between Tata and Docomo "could not be said to be void or opposed to any Indian law including the FEMA".[213] The court noted, "FEMA contains no absolute prohibition on contractual obligations. It envisages grant of special permission by RBI" and agreed with the LCIA that "Clause 5.7.2 of the SHA always was legally capable of performance without the special permission of RBI, using the general permission under sub-regulation 9(2) of FEMA 20," which permitted a transfer of shares from one non-resident to another non-resident at any price.[214] The court was referring to the reasoning given in the LCIA Award that the put option was structured keeping in mind implications under the FEMA, and that Tata was under an unqualified obligation to perform. The LCIA Award held that performance did not necessarily require special permission from the RBI because certain methods of performance (e.g., Tata finding a non-resident buyer for Docomo shares) were already covered by general permissions.

Further, the RBI's case that its permission was required for Tata to transfer any money to Docomo was not cognizant of the fact that the award did not enforce the put option per se, rather, it awarded damages to Docomo payable by Tata. Accordingly, the question of seeking the RBI's permission did not arise as no such permission is required for the payment of damages.[215] The court also ruled that

> [A]s long as the Award stands, there is no need for any special permission of RBI for remission by Tata of the amount awarded thereunder to Docomo as damages. The refusal by RBI of such permission which is not required in the first place, or the fact that such refusal has not been

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213 *Id*. at 36.

214 *Id.*

215 *Id.* at 33 (noting that the RBI had "not placed before the Court any requirement for any permission of RBI having to be obtained for Docomo to receive the money as damages in terms of the Award").

challenged, would therefore not affect the enforceability of the Award.[216]

Through this reasoning, the court addressed the RBI's objection to enforcement based on public policy which was premised on the alleged illegality of the SHA and the need for the RBI's permission for Tata to transfer the award amount to Docomo. Thus, the award of damages by the LCIA was the necessary element for true enforcement of Docomo's contractual rights. However, this required a litigated outcome. The Delhi High Court also noted that the present case had an effect on the goodwill and reputation of Indian entities that entered into contracts with foreign entities.[217] Seeing as the present contract was not entered into under any duress, it was in the interest of public policy that the contracting parties be allowed to honor it by the judiciary.[218]

The Delhi High Court took a strict approach to the RBI's *locus standi* or basis to intervene in the case. Section 48 of the Arbitration Act does not allow third parties to implead themselves when the enforcement of an award is being challenged.[219] On the contrary, it specifies that only a party in the award which is aggrieved by it has the right to challenge the award based on the grounds provided in

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[216] *Id.* The LCIA had not expressed any view on the question whether or not special permission of the RBI is required before Tata can perform its obligation to pay Docomo damages in satisfaction of the Award. *See* LCIA Award, *supra* note 193, at 171. Tata had sought special permission of the RBI to make payment under the Award but the same was rejected. The Delhi High Court held that no special approval of the RBI was required in this case.

[217] NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 38 (India).

[218] *Id.*

[219] *Id.* at 25. It is important to note here that in the Docomo case, the court was not examining whether the RBI should have granted special permission when Tata first sought it prior to the commencement of arbitration proceedings. The court's examination was in the context of objections raised by the RBI in enforcement proceedings under the Arbitration Act. In this sense, the court's judgment in the *Docomo* case is not a precedent for enforcement of fixed price put options per se and it is unlikely that courts will rule on this issue, for it's a matter of regulatory policy on which courts would defer to RBI's discretion instead of directing it to grant approvals. Courts' deference to RBI on policy matters is reflected in the Indian Supreme Court's observations in an earlier case that once the RBI has taken a view it is not "open to the company or any other authority or individual to take upon itself or himself, thereafter, the task of deciding whether the permission was rightly granted by the Reserve Bank of India." Life Ins.e Corp. of India v. Exps. Ltd., AIR 1986 SC 1370, 12 (India). In the Docomo case and other cases discussed in this Article, the courts have examined the issue on a narrow basis—whether enforcement of foreign awards for payment of damages, for example, could be refused by the Indian courts or objected to by the RBI.

section 48.[220] The RBI was not a party to the award and consequently could not use the Arbitration Act as the basis to implead itself. The RBI turned to India's Civil Procedure Code of 1908 (hereinafter "CPC") which gives courts the discretion to not enforce any compromise that furthers an unlawful objective;[221] the RBI was referring to the consent terms between Tata and Docomo which it considered unlawful. Notwithstanding the High Court's decision that the award and consent terms were lawful , it also held that even the CPC did not contemplate the intervention of a third party in such cases.[222] The CPC only gave courts the discretion not to enforce unlawful compromises but did not empower third parties to intervene in these cases.[223] Importantly, it held that the RBI could not use issues decided by the arbitral tribunal as the basis for its intervention in the present case. For instance, the RBI claimed that by virtue of the fact that the case involved money leaving India, the RBI had an inherent right to implead itself. The High Court responded to this argument by referring to the LCIA decision that had already assessed the role of the RBI in the case. Though the RBI was not a part of those proceedings, the High Court noted that it was argued by Tata that the RBI's permission was required for it to comply with the exit option. The LCIA had held that there was no need to obtain RBI permission based on the nature of the amount awarded (in the form of damages).[224] The High Court concluded that the LCIA award would bind the RBI as if it were a pronouncement of any civil court: " . . . RBI will, just as any other entity, be bound by an Award interpreting the scope of its powers or any of its regulations subject to it being upheld by a Court when challenged by a party to the Award."[225] This is an important finding of the Delhi High Court as it deferred to the arbitral authority to not only direct the parties in the dispute but to conclusively determine

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[220] NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, ¶ 36 (India).

[221] *Id*. at 38. *See* The Code of Civil Procedure, 1908, Order XXIII § (5)(3) (India) (stating that "[a]n agreement or compromise which is void or voidable under the Indian Contract Act, 1872 (9 of 1872), shall not be deemed to be lawful within the meaning of this rule.").

[222] NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 26-27 (India).

[223] *Id*. at 26.

[224] *Id*. at 27.

[225] *Id*.

the applicability of their findings on statutory bodies such as the RBI.

b. Treatment of Downside Protection on Par with Assured Returns

The *Docomo* case was the last of a series of similar decisions rendered by the Delhi High Court in 2017. *Shakti Nath v. Alpha Tiger*[226] and *Cruz City v. Unitech*[227] were cases which also concerned the enforcement of foreign arbitral awards based on put option clauses and were decided by the Delhi High Court just before the *Docomo* case. An important difference between *Cruz City* and *Docomo* is that in the former, the put option agreement was not simply for the purpose of downside risk protection but guaranteed an assured return to the investor. The put option stipulated that the price at which the foreign investor's shares are purchased must be equivalent to their initial capital commitment and a fifteen percent post-tax internal rate of return (IRR).[228] This was a put option that guaranteed an assured return. Another distinction between the two cases is that in *Cruz City*, the LCIA award did not provide for the payment of damages to the foreign investor (Cruz City). Rather it directly enforced the put option requiring the respondent (Unitech, an Indian corporation) to pay Cruz City the purchase price of its shares against delivery.[229] While the LCIA award for *Cruz City* is not available, a decision of the Mauritius Supreme Court (before whom the enforcement of the same award was sought but against another party) confirms that the relief in the award was in the form of a direction to purchase shares and not an award of damages.[230] In *Cruz City* the Delhi High Court acknowledged that the agreement sought to be enforced may be invalid under FEMA but this would not be the basis to deny the enforcement of an arbitral award based

[226] Shakti Nath v. Alpha Tiger Cyprus Inv., (2017) SCC Online Del. 6894 (India).

[227] Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810 (India).

[228] *Id*. at 5. For further discussion, see Makkar & Jain, *supra* note 13, at 408-09.

[229] Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810, 4-5 (India).

[230] Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2014) SCJ 100, 12-13, 26 (India).

on the agreement, given the narrow scope of section 48.[231] The court concluded by stating that Unitech may be proceeded against under FEMA as a result of entering into the put option agreement with Cruz City, but this cannot be the basis on which it can escape liability under the same agreement.[232] This approach allows foreign investors to use India's pro-enforcement stance in the context of international commercial arbitration to effectively maneuver around regulatory uncertainty. However, this would be achieved at the cost of the Indian party being made subject to regulatory action. Courts in India have not allowed parties to do indirectly what they cannot do directly.[233] This principle can be equally applied to transactions that are structured around the FEMA regulations. While the scope of judicial review is limited in the context of enforcing the arbitral award, the same restraint need not be exercised when taking action against the Indian party for any regulatory violation. Thus, the lack of a more nuanced policy on put options not only affects foreign investors but also increases the risk faced by Indian parties when they enter into agreements that are structured around foreign exchange regulations.

This distinction is important to understand the full scope of an arbitral tribunal's powers to make awards based on put options. In the *Docomo* case the Delhi High Court did not find the award or its enforcement in contravention of public policy, and added that factors such as impact on the foreign direct investment inflows and strategic relations between the countries where parties are located will have to be kept in mind while examining whether enforcement of an award would be consistent with the public policy of India.[234] However, the actual enforcement of the LICA award in *Docomo* did not require any FEMA regulations to be violated as the award characterized Tata's obligation to pay Docomo as damages and not as consideration for the transfer of securities.[235] By contrast, in *Cruz City*, the High Court was dealing with an award which would be impermissible under FEMA but nevertheless decided to enforce the

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231 Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810, 42 (India).

232 *Id.* at 70-71.

233 *See* Singh v. Singh, (1979) 2 SCR 282, ¶ 5 (India) (explaining that to permit a party to do indirectly what a statute forbids them from doing directly would be tantamount to permitting parties to evade the statute).

234 NTT Docomo, Inc. v. Tata Sons Ltd., 2017 SCC Online Del 8078, 30 (India).

235 *Id.* at 32-33.

award.[236] In *Shakti Nath* the Delhi High Court dealt with a domestic arbitral award and an application to set it aside under section 34 of the Arbitration Act. In this case, the SHA gave the foreign investor the option to either trigger the put option or claim damages under the Indian Contract Act, 1872. The investor had chosen the former and the arbitral award provided the relief of damages.[237] The arbitral award was challenged for giving effect to a put option by disguising its exercise as a claim for damages. The High Court dismissed this challenge and held that in the event of a breach, the contract allowed the investor to exercise the put option or claim damages. Given that the claim and arbitral award were for damages, the question of RBI approval or their prohibition of put options would not arise in the first place. This decision was upheld by the Supreme Court[238] and is encouraging for investors as it represents a pro-enforcement stance even for domestic-seated arbitration.[239]

VI. GAPS IN THE CURRENT APPROACH

High Court decisions have made it clear that the judiciary will not intervene in the enforcement of arbitral awards even if they contravene provisions of FEMA. While this is a step in the right direction, the lack of regulatory certainty has created hurdles for foreign investors who have legitimate business interests in managing their investment risks through freely negotiated exit rights. Relying on judicial enforcement increases the time taken to exercise put options and imposes additional financial strain on the party that loses the case before the arbitral tribunal. Even after parties successfully enforce a foreign arbitral award, the freedom with which they can use the proceeds of the award could be constrained. For example, in some cases exit options are structured

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[236] Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810, 52, 55-56 (India).

[237] Shakti Nath v. Alpha Tiger, (2017) SCC Online Del., 6894, ¶¶ 52-53, 58-63 (India).

[238] *Id.* ¶ 63.

[239] *Claim for Damages for Breach of Contract under Section 73 of the Contract Act, 1872 by a non-resident does not violate the RBI guidelines*, AZB & PARTNERS: ADVOCS. & SOLICS. (Apr. 1, 2017), https://www.azbpartners.com/bank/claim-of-damages-for-breach-of-contract-under-section-73-of-the-contract-act-1872-by-a-non-resident-does-not-violate-the-rbi-guidelines/ [https://perma.cc/5E6T-J2F9].

to address FEMA regulations by retaining a portion of award proceeds in India. The following discussion explains these implications in detail.

a. Forcing Parties into Arbitration Proceedings

In the context of put options exercisable by foreign investors, the uncertainties created by the regulatory regime place Indian residents in a position that drive foreign investors to arbitration not only as a dispute resolution mechanism but as a necessary means to enforce their contractual rights. The severe penal consequences that follow under FEMA for any violation[240] prevents an Indian party from honoring non-market value-based put options irrespective of whether or not it is willing to do so. Litigation then is the safest and perhaps the only means to a resolution. However, an award for damages for breach of contract brings with it reputational issues which, as the *Docomo* case has shown, is not a desirable outcome for Indian parties who are ready and willing to honor their contractual commitments. This is because the RBI thus far has not granted permission to transfer securities to a non-resident for consideration that is noncompliant with the prescribed pricing guidelines. In the *Docomo* case, a two-step process was followed by the RBI. The RBI first carried out its own evaluation, which was in favor of granting an exception, and then made a recommendation to the Ministry of Finance, Government of India, which, having the power to take the final call on the request, denied the recommendation.

Based on correspondence cited in the *Docomo* case, it appears that the RBI is cognizant of the difference between put options designed to secure assured returns (as in *Cruz City*) and those designed to reduce downside risk (as in *Docomo*). When considering Tata's request to buy Docomo's shares at the sale price, RBI officials

240 Section 13 of FEMA prescribes the penalties for violations of the Act and contravention of any rule, regulation, notification, direction or order made thereunder. The amount of the fine could be up to three times the sum involved in the violation where such amount is quantifiable, or up to two lakh Indian Rupees where the amount is not quantifiable, and a further penalty that may extend up to five thousand Indian Rupees for every day after the first day during which the contravention continues. Under Section 42 of FEMA, directors and other persons in management of a company in contravention of FEMA will be personally liable for the consequences of such violations. Additionally, the provisions of Section 37(1) of FEMA stipulate that the Directorate of Enforcement shall investigate any person/entity for the alleged contraventions referred to in Section 13 of FEMA.

had stated that the exit option clause did not guarantee an assured return.[241] Assured returns are characterized by the investor recovering its entire investment *plus* a certain return on that investment. Under the sale option clause, the investor was only recovering fifty percent of its own investment; the clause was thus intended to provide downside protection and a fair arrangement.[242] The RBI was cognizant that a bare reading of FEMA regulations would come in the way of enforcing this exit option; however, it also noted the importance of India's strategic relationship with Japan with respect to foreign direct investment inflows.[243] In conclusion, the RBI had initially found that the request to honor the exit option had merit and that it should be granted in this case and future cases having similar circumstances.[244] When the request was referred to the Ministry of Finance, Government of India, it stated that an exception could not be made for one case.[245] The Ministry of Finance stated that the present FEMA regulations had to be applied to the case. It also suggested that if the RBI believed some deviation from the present regulations were warranted then it should present a

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241 *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 29-31 (India).

242 *See id.* at 29-31, 35-36 (explaining the RBI's internal correspondence claimed that the "intention" behind the regulation was to disallow exit with assured return, which was not the case in Docomo).

243 *See id.* at 31 (explaining that the RBI stated that

> [h]owever, the larger issue here is of a fair commitment in the contracts in relation to an investment and a downside protection of an investment, rather than an assured return. Besides our strategic relationship with Japan in recent times in relation to FDI flows is also a matter to be kept in view.

In the Letter of Reserve Bank of India to Department of Economic Affairs, Investment Division, Ministry of Finance, dated December 22, 2014 [hereinafter RBI Letter]); *see also* NTT Docomo, Inc. v. Tata Sons Ltd., LCIA Case No. 152896, Final Award, ¶ 68 (June 22, 2016).

244 *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 31 (India) ("In view of this, we are inclined to accept the proposal and in future, in all such case, similar principle shall be applied."); *see also* Vijay Sambamurthi, *Recent Developments in Indian Law: Impact on Private Equity Transactions*, 28 NAT'L L. SCH. INDIA REV. 44, 49 (2016).

245 *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 31 (India) (sharing that the Ministry of Finance stated that "[t]he proposal needs to be examined by RBI per its extant regulations. An individual proposal cannot be considered in exception of such regulations."); *see also* NTT Docomo, Inc. v. Tata Sons Ltd., LCIA Case No. 152896, Final Award, ¶ 69 (June 22, 2016).

proposal for their change to the Ministry for its consideration.[246] It was consequent to this communication by the Ministry of Finance that the RBI finally refused Tata's request to transfer money to Docomo for its shares for the predetermined price under the SHA.

Though the present foreign exchange regime is a permissive one as held by the Supreme Court in *Vijay Karia*, permission for transactions are granted based on the discretion of the RBI and the Ministry of Finance. The preceding cases have shown that the norm is not to permit such transactions even though their fairness has been acknowledged by the RBI.[247] This makes the exercise of put options without an arbitral award subject to regulatory hurdles unless the put option complies with FEMA Regulations. As seen from *Docomo* and *Cruz City*, put options exist to mitigate an investor's losses or secure assured returns; investors thus have an incentive to exercise put options only when the sale price cannot be obtained through the sale of shares at their fair market value. The effect of the pricing guidelines under the erstwhile regulations (FEMA 20) framed by the RBI was that put options could operate exclusively in situations where they are least likely to be used by investors. The RBI's policy, and now the Central Government's Non-Debt Rules, 2019 that continue that policy, have created an avoidable clog in the wheels of international business requiring parties, even when there may be no genuine dispute, to arbitrate, obtain an award, and have their rights enforced through the judiciary (the High Courts and Supreme Court). Foreign investors may still be willing to invest in India and structure transactions to try to address the restrictions. However, from the Supreme Court's decision in *Cruz City*, it would appear that the party in India will continue to remain subject to regulatory action.[248] Relying on the judiciary is thus not an optimal solution as it increases the cost of enforcing a simple contractual right. Some of the ways in which this happens are explained below.[249]

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246 *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 31 (India) ("In case, RBI is of the opinion that the existing regulations need modification, a detailed proposal on the subject along with justification and rationale may be forwarded in the Government for taking a view in the matter.").

247 *See id.*

248 *See* Cruz City 1 Mauritius Holdings v. Unitech Ltd., (2017) SCC Online Del 7810, ¶¶ 100-03 (India).

249 *See* HSA Advocates, *India: RBI On Downside Protection—Are We Set for Course Correction?*, MONDAQ (June 1, 2017), https://www.mondaq.com/india/shareholders/598944/rbi-on-downside-

b. Costs of Enforcing Put Options Through Arbitration

The first cause of increased costs arises from the uncertainty created by enforcing a contractual right through arbitration. Though arbitral tribunals have been allowing foreign investors to benefit from put options either directly or through the award of damages, parties should not have to subject themselves to this process in the first place. The second issue is that arbitration is a costly process. The process of completing the arbitration and subsequent enforcement in the *Docomo* case was expensive. The award of costs in the arbitration alone, as cited in the arbitral decision, constituted approximately GBP 120,000 in arbitration costs and over JPY 1,000,000,000 by way of legal costs.[250] It is pertinent to note that the aforesaid figures do not include other costs which were incurred by Tata.

The often-cited advantages of arbitration include its ability to provide speedy dispute resolution, with confidentiality and at low cost. As seen in the *Docomo* case, none of these tenets are true in large commercial arbitrations. When one adds the costs of pre-arbitration negotiation and preparation (including extensive and voluminous document requests and review) and post-award enforcement action, the time and costs involved can significantly exceed the award of costs (award of costs usually only cover costs from the time after filing through award; post-award interest covers the period after award to payment—the costs of enforcement litigation are not included). Put options are meant to be a tool to manage the risks of, and thereby attract, foreign investment by providing for reasonable exit terms. If the cost of their enforcement is too high, their use will be restricted only to larger corporations which will be able incur such expenses.

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protection-are-we-set-for-course-correction [https://perma.cc/5QZU-Y6ED]; *see also* Radhika Pandey & Bhargavi Zaveri-Shah, *Policy Implications Of The Tata-Docomo Order*, BLOOMBERG QUINT (May 9, 2017, 12:20 PM IST), https://www.bloombergquint.com/opinion/policy-implications-of-the-tata-docomo-order [https://perma.cc/9VNS-UJ7A]; Makkar & Jain, *supra* note 13, at 407-08, 413.

[250] *See* NTT Docomo, Inc. v. Tata Sons Ltd., (2017) SCC Online Del 8078, 15 (India). The awarded costs did not include pre-arbitration preparation and negotiation costs. In addition, enforcement actions were commenced in the United States District Court for the Southern District of New York and the London Commercial Court in addition to the Delhi High Court, and were stayed pending the case before the Delhi High Court.

In the same vein, companies may have to pay increased damages in the form of interest due to delayed regulatory approval or simply due to the length of the proceedings involved to secure an arbitral award and then enforce it in India. During the LCIA proceedings, Tata requested that the LCIA refrain from providing for the payment of post award interest. This was on account of the fact that Tata's ability to pay the awarded damages was contingent on approval from the RBI. The LCIA rejected this contention and only allowed a twenty-one-day grace period, after which Tata was required to pay interest on the damages. Not all corporations may be able to incur such costs, and regardless of the Indian entity's relative ability to bear such costs, it is certainly not a desirable situation if the dispute could be avoided in the first place.

The third issue relates to the characterization of the relief in the award as damages, and the reputational implications for the losing party. A breach of contract and consequent damages carries negative associations. The implication is that a party was either unwilling or unable to honor a contract. When it comes to the current tenuous route to enforce put options, this is not necessarily the case. In *Docomo*, it was the RBI's refusal to grant permission that created the ultimate basis for Docomo to argue non-performance of an obligation by Tata. While context will help dispel any adverse implications one may draw from an award of damages, there is always an underlying and unnecessary risk posed to a non-performing party's reputation. Finally, even if the RBI and Ministry of Finance were to approve requests to honor put options on a case-by-case basis, the very fact that such approvals are discretionary will result in uncertainty. One may legitimately ask whether Tata's request to purchase Docomo's shares merited the grant of any special permission, especially when the norm was to strictly apply the RBI policy against put options. In the absence of clear and deliberate guidelines upon which such discretion would be exercised, it is difficult to convince investors that it will be exercised without any arbitrariness.

c. Remittance – the Last Yard of Enforcement

A review of the High Court decisions conveys the limitations of their pro-enforcement stance. High Courts have consistently and unequivocally held that awards based on put option clauses ought to be enforced. However, the enforcement of an award does not automatically guarantee the right to remit the award amount. In *Cruz City*, the Delhi High Court enforced the arbitral award but held that any money recovered from Unitech (the Indian resident) could be remitted only after following FEMA Regulations and the pricing guidelines. In a recent case decided by the Bombay High Court, *Banyan Tree v. Axiom Cordages*,[251] a pronouncement to this effect was made. In *Banyan Tree,* the put option guaranteed the foreign investor an assured return of fifteen percent when exercised (target value). The Bombay High Court allowed the enforcement of the foreign arbitral award providing for the performance of the put option clause, citing precedent such as *Vijay Karia* and *Cruz City* in its judgment. However, it noted that the put option was legal because it stipulated that only the fair market value of the shares will be remitted through foreign exchange (not requiring special permission of the RBI) and the difference between the fair market value and target value will be deposited in Indian Rupees to a nominee account in India as appointed by the foreign investor.[252] In *Docomo*, the requirement of RBI permission did not arise ultimately because RBI's intervention and objections were rejected and the award's relief was in the form of damages, payment of which, as the court held, was not prevented under any express provision of FEMA or FEMA Regulations.[253] Thus, the parties' ability to fully realize the relief granted to them depends on how it is characterized. The present policy also reduces investor freedom. To the extent that parties are required to leave proceeds in India for the purpose of complying with FEMA Regulations, it constrains the investor's freedom to use the proceeds as it sees fit. For instance, all the investment in the *Banyan Tree* case was made in U.S. Dollars, but the proceeds were recovered in Indian Rupees (amounts constituting interest payments were retained in India to meet RBI pricing requirements) and U.S. Dollars (to the extent of the amounts that were remitted outside of India). Investor freedom is also curtailed when the attempt to work within FEMA Regulations results in remittance of put option proceeds to a nominated account in India for use within the country. These limitations on the use of proceeds from put options effectively reduce their value and consequently their ability to attract foreign investments in India.

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251 *See* Banyan Tree Growth Cap. L.L.C. v. Axiom Cordages Ltd., (2020) SCC Online Bom 781 (India).

252 *See id.* ¶ 91; *see also* Kazi & Agarwal, *supra* note 44.

253 *See supra* Part V(A).

The correspondence between the RBI and the Ministry of Finance regarding the *Docomo* case took place in 2014-2015 but no changes were subsequently made to FEMA 20. Rather, they have been incorporated by the Central Government in the Non-Debt Rules of 2019 that replaced FEMA 20. The recent Supreme Court pronouncement in *Vijay Karia* and cases such as *Banyan Tree* have renewed discussions on India's policy towards put options. By removing the blanket ban on put options the Central Government and the RBI may be able to better regulate them. In the status quo, put options designed for assured returns and downside protection are being treated in the same manner. Since the enforcement of these put options will happen through the same route, corporations will not be deterred from entering into put options providing assured returns. By recognizing (and permitting) downside protection in foreign investment, the Central Government and the RBI can differentiate it from assured returns and regulate the two practices differently. For instance, proceeds of assured returns could be taxed at a higher rate than downside protection in order to disincentivize the former.

Put options are extensively used in India because of a lack of investor confidence, accordingly, they play a crucial role in attracting investments in India.[254] Downside protection offered by put options allow investors to venture into unfamiliar markets with more confidence because the extent of their losses will be capped. At the same time, this Article acknowledges the RBI's interest in ensuring the stability of India's monetary reserves and ensuring that debt instruments are not disguised as equity. An investor ought to assume some risk, and this is where the distinction between assured returns and downside protection becomes significant. At present, it is only the judiciary that seems to recognize the need for Indian residents to uphold their contractual obligations to foreign investors. However, when the judiciary enforces put options through arbitral awards, it follows a policy of non-interference with the award; meaning that different treatment of downside protection and assured returns is not judicially imposable. Rather, the judiciary asserts its doctrinal approach to the issue through holdings that subject India's regulators to the findings of the arbitral tribunals. Further, despite the pro-enforcement trend in the context of

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[254] *See* Makkar & Jain, *supra* note 13, at 414; *see also* Shilpa Mankar Ahluwalia & Kushagra Priyadarshani, *Enforcing put options as a method of investor exit*, INDIA BUS. L.J. (June 24, 2012), https://law.asia/enforcing-put-options-as-a-method-of-investor-exit/[https://perma.cc/GV53-NPHT].

commercial arbitration, the fact that investors need to look to arbitration and the judiciary and not the other contracting party for the enforcement of their rights in the first instance is not emblematic of an investment-friendly environment. Parties' desires for a neutral venue under neutral rules is a key driver for their decision to initiate arbitration. Thereafter, enforcement actions of favorable awards are commenced through courts in India, thus relying on the judiciary to enforce the award. Such courts' willingness to narrowly construe the public policy exception gives foreign investors comfort, but it doesn't obviate the need to first resort to arbitration and then go through a lengthy enforcement process.

VII. CONCLUSION

There are clear limitations to the present regime governing the enforcement of put options exercisable by foreign investors. The current approach is heavily reliant on foreign arbitral awards and their enforcement by courts. While courts have steadfastly enforced these awards when required, parties should not have to rely on litigation as a first resort to fulfill contractual obligations. Despite the current pro-enforcement stance of Indian courts towards foreign arbitral awards, the lack of a responsive regulatory framework poses several challenges to foreign investment. These include high costs of litigation and the inability to remit proceeds of put options outside India, unless structured as an award of damages. Irrespective of whether an investment is structured as providing for an assured return or downside protection, in order to realize the full amount and use it outside India, it would have to be characterized as damages by the foreign arbitral award. In cases where the award does not characterize the awarded amount as damages, the party desiring to enforce the award would have to retain any amount above fair market value in India. In order to increase investor freedom and confidence, India will need to rationalize its policy towards downside protection of foreign investment. The RBI seemed to have been inclined to allow put options guaranteeing downside protection. Given this inclination, the RBI should persuade the Central Government to leverage the present judicial momentum and frame a more nuanced regime governing optionality clauses; one that distinguishes between assured returns and downside protection.