Arbitration and Exchange Control Laws of India

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Abstract

*Freedom of contract is an essential pillar of transnational contract law. The corollary to this is that a party which freely enters a contract should honour its commitments—often encapsulated in the Latin maxim "*pacta sunt servanda*". However, in the context of investments in India, a practice of reneging on freely entered contractual obligations, by way of invoking the exchange control laws of India, has emerged. For foreign investors, this practice has become a cause of concern. In this article, we explore a series of judgments of Indian courts, including a recent judgment of the Supreme Court, which demonstrates a positive trend towards enforcement of foreign arbitral awards in India.*

Freedom of contract is an essential pillar of transnational contract law. The corollary to this is that a party that freely enters a contract should honour its commitments—often encapsulated in the Latin maxim "*pacta sunt servanda*". However, in the context of investments in India, this does not always seem to be followed, considering that a practice of reneging on freely entered contractual obligations by way of invoking the exchange control laws of India has emerged. For foreign investors, this practice has become a cause of concern. However, a series of judgments of Indian courts, and a recent judgment of the Supreme Court of India, will most likely provide some comfort to foreign investors.

In this article, we explain the nature of exchange control laws and analyse judgments of Indian courts which indicate a positive trend towards enforcement of foreign arbitral awards in India. We conclude that international arbitration has come to the aid of foreign investors such that the exchange control laws of India are not unfairly used to disavow contractual obligations.

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Currency convertibility and exchange control laws

It is important first to understand the concept of currency convertibility and the impact of exchange control laws on currency convertibility. Currency convertibility is the ability to freely convert a national currency at the going exchange rate into any other currency.[1] However, the concept goes beyond the simple ability to exchange currency, i.e. merely a financial transaction of exchanging one currency into another. Convertibility issue also arises in form of exchange of any other goods, services or capital across borders. A currency may be convertible at a given exchange rate, but practically its convertibility is often restricted through trade and capital controls.[2] Exchange control laws impose limitations on free convertibility of currency. Thus, exchange control laws regulate how transactions such as the exchange of goods or the acquisition of assets across borders would take place. In a way, such laws create certain barriers against free movement of capital and goods across borders, usually with the intent to protect the domestic market or players.

India, post its independence in 1947, started out as a closed economy and did not permit free movement of goods and capital across its border. Soon after independence, the Foreign Exchange Regulation Act 1947 (FERA 1947) was enacted, imposing severe restrictions on all forms of cross-border transactions. FERA 1947 was subsequently replaced by the Foreign Exchange Regulation Act 1973 (FERA 1973). As per its preamble, FERA 1973 was enacted to regulate: "certain payments, dealing in foreign exchange and securities, transactions indirectly affecting foreign exchange and the import and export of currency, *for the conservation of the foreign exchange resources of the country* and the proper utilisation thereof in the interest of the economic development of the country" (emphasis added). FERA 1973 was a strict statute providing for imprisonment as a consequence of its violation, and its focus was on preserving foreign exchange.[3]

However, in the year 1990, India began a gradual process of deregulation and liberalisation. As part of this process, it was noted that FERA 1973 had become an archaic piece of legislation hindering growth and foreign investment. In 1997, the Tarapore Committee on Full Capital Account Convertibility recommended the replacement of FERA 1973 with a Foreign Exchange Management Act.[4] Subsequently, the Foreign Exchange Management Act 1999 (FEMA) was enacted on 1 June 2000[5] and FERA 1973 was repealed.

Through FEMA, the approach towards exchange control shifted from conservation and control to management of foreign exchange.[6] FEMA removed criminal consequences for a breach of exchange control laws (which were provided under FERA 1973), and also introduced provisions for compounding of offences under the statute.[7] Notably, the preamble of FEMA provides that: "it is an Act to

[1] Manuel Guitian, "Concepts and Degree of Currency Convertibility", in Manuel Guitian and Saleh M. Nsouli (eds), *Currency Convertibility in the Middle East and North Africa*, pp.22–23.

[2] See fn.1 above.

[3] *Life Insurance Corporation of India v Escorts Ltd* (1986) 1 SCC 264.

[4] Press Release of the Reserve Bank of India on the Report of the Committee on Capital Account Convertibility, 3 June 1997.

[5] Notification No.GSR 371(E), 1 May 2000.

[6] Address by Ms Shyamala Gopinath, Deputy Governor of the Reserve Bank of India, at the Conference organised by the Forum for Free Enterprise, Mumbai, 25 January 2005.

[7] See fn.6 above.

consolidate and amend the law relating to foreign exchange with *the objective of facilitating external trade and payments* and for promoting the orderly development and maintenance of foreign exchange market in India" (emphasis added). Over the years, through regulations framed under FEMA, there has been a gradual and steady reduction in the degree of limitations which are imposed on cross-border transactions.

However, despite gradual liberalisation in India, certain cross-border transactions have continued to be regulated through FEMA and the regulations framed thereunder. For example, the Foreign Exchange Management (Non-debt Instruments) Rules 2019 (NDI Rules 2019), which have been issued under the FEMA, inter alia, regulate the price at which equity instruments may be transferred between residents and non-residents. Rules 21(2)(b)(iii) and (c)(iii) provide that equity instruments transferred by an Indian resident to a person residing outside India should not be less than the valuation of equity instruments done as per any internationally accepted pricing methodology for valuation on an arm's length basis (Fair Value) of the instrument; similarly, equity instruments transferred by a person resident outside India to an Indian resident shall not exceed the Fair Value of the instrument.[8]

It must be noted that FEMA provides that no person shall deal with foreign exchange except as provided under the FEMA, rules or regulations framed thereunder or with the general or special permission of the Reserve Bank of India (RBI).[9] The NDI Rules 2019 provide that the RBI may, on application made to it for sufficient reasons and in consultation with the Central Government, permit a person resident outside India to make any investment in India subject to such conditions as may be considered necessary.[10] Thus, transactions which are not expressly authorised under the FEMA may be carried out with permission from the RBI.

In light of the continued regulation of transactions, non-Indian parties often encounter situations where a counter-party would assert that due performance of its contractual obligation would be contrary to the Indian exchange control laws. As we will show, the same objection is also invoked at the stage of enforcement of foreign awards in India by asserting that the award is contrary to the "public policy of India".

[8]

"21. Pricing Guidelines

…

(2) Unless otherwise prescribed in these rules, the price of equity instruments of an Indian company—

…

(b) transferred from a person resident in India to a person resident outside India shall not be less than

…

iii. the valuation of equity instruments done as per any internationally accepted pricing methodology for valuation 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.

(c) transferred by a person resident outside India to a person resident in India shall not exceed …

iii. the valuation of equity instruments done as per any internationally accepted pricing methodology for valuation 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 … ."

[9] Foreign Exchange Management Act 1999 s.3.

[10] Foreign Exchange Management (Non-debt Instruments) Rules 2019 r.3.

Genesis of the public policy objection

The Indian Arbitration and Conciliation Act 1996 (A&C Act) is based on the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention). The A&C Act stipulates that the enforcement of a foreign arbitral award may be refused if the Court finds that the enforcement of the award would be contrary to the public policy of India.[11]

One of the earliest challenges to an arbitral award on the basis of exchange control laws in India occurred in the case of *Renusagar Power Co Ltd v General Electric Co*[12] (*Renusagar*). In *Renusagar*, the enforcement of a foreign arbitral award in India was resisted on the basis that the award was contrary to the public policy of India as its enforcement would amount to a violation of the FERA 1973. The Supreme Court noted in an *obiter dictum* that the FERA 1973 prohibited parties from entering into agreements contrary to its provisions and that conservation of foreign exchange was vital for the Indian economy. In effect, the Supreme Court stated that the enforcement of an award which would result in the violation of provisions of the FERA would be contrary to the public policy of India.[13] However, since the challenge pertained to, inter alia, whether an award for interest for delayed payment of instalments of a loan violated the provisions of the FERA 1973, the Supreme Court held that since the original contract had been approved by the Government of India, the award of interest for delayed payment of instalments does not violate the provisions of FERA 1973.[14] Thus, whilst ultimately the enforcement of the foreign arbitral award was permitted, the findings of the Supreme Court in *Renusagar* on the exchange control law and the public policy of India became the basis for numerous attempts by parties to resist enforcement of arbitral awards.

However, recently, in the case of *Vijay Karia v Prysmian Cavi E Sistemi Srl*,[15] (*Vijay Karia*), the Supreme Court upheld the enforcement of a foreign arbitral award as the Court found that a violation (if any) of reg.21(2)(b)(iii) of the NDI Rules 2019 (issued under the FEMA) would not constitute a violation of the fundamental policy of Indian law. This position was reiterated by the Bombay High Court recently while enforcing two Singapore International Arbitration Centre (SIAC) foreign arbitral awards.[16]

The judgments discussed below, including the recent Supreme Court ruling in *Vijay Karia*, reveal that courts usually reject "exchange control objections" and permit enforcement of contractual obligations recognised in arbitral awards. This is in light with a general trend over the last decade which saw Indian courts and legislation become more arbitration friendly.

A move towards a pro-arbitration approach

Over the years, the Indian arbitration regime has undergone various changes. In 2012, the Supreme Court of India in *Bharat Aluminium Co v Kaiser Technical*

[11] Arbitration and Conciliation Act 1996 (India) s.48.
[12] 1994 Supp. (1) SCC 644.
[13] 1994 Supp. (1) SCC 644 at [76].
[14] 1994 Supp. (1) SCC 644 at [79].
[15] Civil Appeal Nos 1544 and 1545 of 2020.
[16] *Banyan Tree Growth Capital LLC v Axiom Cordages Limited*, Commercial Arbitration Petition No.476 of 2019 and Commercial Arbitration Petition No.475 of 2019.

Services[17] (overruling its earlier judgment *Bhatia International v Bulk Trading SA*[18] held that Part I of the A&C Act is not applicable to foreign-seated arbitrations. This judgment stopped Indian courts from entertaining challenges for setting aside foreign arbitral awards under the regime applicable to domestic arbitral awards. In 2013, the Supreme Court in yet another landmark ruling[19] (overruling its earlier judgment *Phulchand Exports Ltd v OOO Patriot*[20]) held that the scope of the public policy exception is narrower when applied as a ground for resisting enforcement of foreign arbitral award as against when it is applied as a ground for setting aside a domestic arbitral award.

In 2015, the A&C Act was amended to implement further important changes.[21] One of the key amendments was the introduction of an explanation to the meaning of "public policy".[22] "Public Policy" includes, inter alia, (i) a contravention of the "fundamental policy of Indian law"; or (ii) "the most basic notions of morality or justice".

Prior to the amendments, Indian courts could set aside arbitral awards on the ground of "patent illegality" being against public policy, whether arbitrations were seated within or outside of India. Patent illegality refers to an illegality which is not trivial and goes to the root of the matter[23]—but in essence allowed the setting-aside for, albeit serious, breaches of national law. The amendments in 2015 clarified that the ground of "patent illegality" is available *only* as a ground for challenge of awards rendered in domestic arbitrations seated in India.[24]

This pro-arbitration approach has had a marked impact on the arbitration regime in the country. Lately, foreign arbitral awards rarely have been refused enforcement in India. This has also had a positive effect on "exchange control objections". We now look at the most pertinent judgments where the issue recently has been addressed by the Indian courts.

1. Noy Vallesina Engineering Spa v Jindal Drugs Ltd[25]

In the *Noy Vallesina* case, enforcement of a foreign arbitral award was challenged on the basis that it would be contrary to FERA 1973. It was argued that the payment based on a contract that had not been approved by the RBI, as required under FERA 1973, would be contrary to India's public policy. The Bombay High Court held that an award cannot be refused enforcement for the reason that at the time of execution of the contract, the permission of the RBI was not obtained.

The Court held that if permission of the RBI is required, it could be obtained before actual payment. Thus, while the Court permitted enforcement, there remained

[17] (2012) 9 SCC 552.
[18] (2002) 4 SCC 105.
[19] *Shri Lal Mahal Ltd v Progetto Grano Spa* (2014) 2 SCC 433.
[20] (2011) 10 SCC 300.
[21] Arbitration and Conciliation (Amendment) Act 2015.
[22] Public policy is defined as: "Explanation 1.—For the avoidance of any doubt, it is clarified that an award is in conflict with the public policy of India, only if,—(i) the making of the award was induced or affected by fraud or corruption or was in violation of section 75 or section 81; or (ii) it is in contravention with the fundamental policy of Indian law; or (iii) it is in conflict with the most basic notions of morality or justice"; see Explanation 1 and Explanation 2 to s.34(2)(b), and Explanation 1 and Explanation 2 to s.48(2)(b) of the Arbitration and Conciliation Act 1996.
[23] *ONGC Ltd v Saw Pipes Ltd* (2003) 5 SCC 705 at [31].
[24] Arbitration and Conciliation Act 1996 s.34(2A).
[25] (2006) 3 Arb. L.R. 510.

a requirement of obtaining RBI permission before the foreign investor could receive any money pursuant to the arbitral award.

2. *Vitol SA v Bhatia International Ltd*[26]

The case of *Vitol SA v Bhatia International Ltd* involved the enforcement of an arbitral award rendered in a London-seated arbitration. Vitol had entered into an agreement to supply coal to Bhatia in four instalments. Under the contract between the parties, Vitol could exercise a buy back right on the coal it was due to supply, in which case a certain charge was required to be paid by Vitol to Bhatia. Regarding the first instalment, Vitol exercised this right and consequently was liable to pay the charge to Bhatia. However, subsequently the market for coal collapsed and Bhatia was not able to accept the remaining three instalments. While the parties made attempts to negotiate a fresh price for supply of coal, Vitol required a guarantee from Bhatia that it would accept the delivery of goods. Bhatia accordingly agreed to Vitol retaining the money payable towards the first charge as guarantee. Ultimately, the negotiations between the parties failed. In the arbitration, an award for damages was issued in favour of Vitol after adjusting the charge due in favour of Bhatia.

Bhatia resisted enforcement of the award in India on the ground of it being against public policy. It argued that under s.8 of the FEMA, a person resident in India had an obligation to take all reasonable steps to realise the foreign exchange which had become due and could not take any step which resulted in delaying the receipt of foreign exchange. Accordingly, Bhatia argued that the award recognising such an arrangement between Vitol and Bhatia, whereby the payment of the charge was delayed was against FEMA, and thereby public policy.

The Bombay High Court rejected Bhatia's argument and found that the provisions of FEMA were not violated. The Court specifically took note of the fact that Bhatia had benefited from having the charge held as security. Withholding the payment of the charge had allowed Bhatia to negotiate a possible agreement and keep in abeyance any liability arising from its inability to accept subsequent shipments. The Court further recognised that a violation of FEMA, if any, is by an act of Bhatia itself and not pursuant to or under the order of the arbitral tribunal. The Court accordingly recognised and enforced the foreign arbitral award.

3. *POL India Projects Ltd v Aurelia Reederei Eugen Friederich Gmbh*[27]

The case of *POL India Projects v Aurelia Reederei* involved a party resisting the enforcement of an arbitral award on the ground that the award enforced a contract of guarantee which was executed in violation of FEMA. POL India Projects had provided a guarantee in favour of Aurelia Reederei, securing the performance of a voyage charter party contract. Due to default in performance of the voyage charter party agreement, Aurelia Reederei invoked the guarantee. The arbitral tribunal found POL India Projects liable towards Aurelia Reederei pursuant to the guarantee. POL India resisted the enforcement of the award on the basis that the guarantee

[26] (2015) 1 Bom. C.R. 100.
[27] (2015) 7 Bom. C.R. 757.

agreement was not in accordance with the Foreign Exchange Management (Guarantee) Regulations 2000 (Guarantee Regulations). It argued that the enforcement of an award based on such contract of guarantee would be in violation of India's public policy.

The Bombay High Court rejected this defence on multiple grounds. The Court, relying on various judgments,[28] held that:

i. the approval of RBI could be obtained even post execution of the guarantee agreement. Such permission could be obtained before receipt of the actual payment;
ii. it was not open to the award debtor to take advantage of its own wrong to avoid liability;
iii. if such defence raised by a company which voluntarily gave the guarantee was accepted, it would undermine the credibility of Indian companies and thereby affect the role of India in international trade and commerce;
iv. the award debtor, being aware of the regulatory requirements, only chose to raise this defence at a belated stage and thus it could not be accepted;
v. a mere contravention of Indian law does not attract the bar of public policy. A simple violation of FEMA would not attract the bar of public policy;
vi. unlike s.47 of the FERA 1973, there was no provision in FEMA which declared a transaction in contravention of the FEMA as void.

4. Cruz City 1 Mauritius Holdings v Unitech Ltd[29]

The case *Cruz City 1 Mauritius Holdings v Unitech Ltd* (*Cruz City*) dealt with an application for enforcement of a London-seated LCIA arbitration award filed by Cruz City against Unitech Ltd before the Delhi High Court. The award arose out of an agreement where Unitech had agreed to ensure that its subsidiary has sufficient funds to meet its obligations towards Cruz City. The award eventually required Unitech to pay certain sums against delivery of shares of a company.

Unitech claimed that the award cannot be enforced as it is against public policy of India on account of being contrary to provisions of FEMA. It argued the following four separate FEMA contraventions:

i. the agreement was in effect a guarantee and was issued without adhering to the Guarantee Regulations;
ii. the award directed Unitech to pay amounts against delivery of shares of a foreign company, which required prior approval of RBI;
iii. that no such investment could have been made by Unitech in pursuance of the award without appropriate valuation; and

[28] *Videocon Industries Ltd v Intesa Sanpaolo SPA, Renusagar Power Co Ltd v General Electric Company*, AIR 1985 SC 1156; *Shri Lal Mahal Ltd v Progetto Grano SPA* (2014) 2 SCC 433; *Penn Racquet Sports v Mayor International Ltd*, ILR (2011) Delhi 181; *Vitol SA v Bhatia International Ltd* (2015) 1 Bom. C.R. 100; *SRM Exploration Pvt Ltd v N & S & N Consultants SRO* (2012) 4 Comp. L.J. 178 (Delhi).
[29] (2017) 239 DLT 649.

iv. that the agreements were structured in such manner that it provided an assured return to Cruz City, which was prohibited under FEMA.

At the outset, the Delhi High Court made two key observations. First, it noted that there is a policy in favour of enforcing foreign arbitral awards. Accordingly, after referring to various international decisions,[30] the court observed that:

> "… even in cases where it is found that the enforcement of the award may not conform to public policy, the courts may evaluate and strike a balance whether it would be more offensive to public policy to refuse enforcement of the foreign award—considering that the parties ought to be held bound by the decision of the forum chosen by them and there is finality to the litigation—or to enforce the same; whether declining to enforce a foreign award would be more debilitating to the cause of justice, than to enforce it. In such cases, the court would be compelled to evaluate the nature, extent and other nuances of the public policy involved and adopt a course which is less pernicious."[31]

Secondly, the Court noted that a mere contravention of a provision of law is not synonymous to contravention of fundamental policy of Indian law. The Court noted that fundamental policy of Indian law refers to the principles and the legislative policy on which Indian statutes are based.

The Delhi High Court found that unlike its predecessor statute, i.e. FERA 1973, FEMA did not proscribe foreign exchange transactions. The policy behind FEMA is to manage foreign exchange transactions as opposed to the policy under FERA 1973, which was to preserve foreign exchange. FEMA itself neither prohibited foreign exchange transactions, nor did it render them void in cases of any procedural non-compliances (such as failure to seek government/RBI approval). Therefore, the Court ruled that a simple violation of a provision of FEMA would not be contrary to the fundamental policy of Indian law. The Court, however, did observe that any remittance of the money recovered from Unitech in enforcement of the award would necessarily require an RBI approval.

Further, the Court found that Unitech had provided clear representations that the agreement was in accordance with applicable laws. Accordingly, to allow Unitech's arguments based on provisions of FEMA would be manifestly unjust. The Court also noted that Unitech had not raised these arguments before the arbitral tribunal and therefore was precluded from raising it at the enforcement stage.

The Supreme Court, in the case of *Vijay Karia*, recently affirmed the findings of the Delhi High Court in *Cruz City*.[32]

5. NTT Docomo Inc v Tata Sons Ltd[33]

The case of *NTT Docomo Inc v Tata Sons Ltd* (*Docomo*) arose from Docomo filing an application before the Delhi High Court for enforcement of an award rendered

[30] *Westacre Investments Inc v Jugoimport-SDRP Holding Company Ltd* [1999] App. L.R. 05/12; *Dallah Real Estate and Tourism Holding Company v The Ministry of Religious Affairs, Government of Pakistan* (2011) 1 A.C. 763; *Yukos Oil Company v Dardana Limited* [2002] EWCA Civ 543.

[31] *Cruz City 1 Mauritius Holdings v Unitech Ltd* (2017) 239 DLT 649 at [39].

[32] *Vijay Karia v Prysmian Cavi E Sistemi Srl*, Civil Appeal Nos 1544 and 1545 of 2020 at [83].

[33] (2017) 241 DLT 65.

by an arbitral tribunal seated in London. The dispute pertained to enforcement of a put option which required Tata to find a buyer for shares held by Docomo at 50 per cent of the price at which Docomo had purchased the shares. The award required Tata to make payment to Docomo upon tendering of the shares.

In the proceedings before the Court, Tata initially resisted the enforcement of the arbitral award. However, the parties arrived at a settlement which led to Tata agreeing to withdraw all its objections to the enforcement of the award. Accordingly, a joint application was filed by Docomo and Tata to place on record the "Consent Terms" arrived at between the parties, in terms of which Tata agreed to pay the amount awarded by the arbitral tribunal to Docomo. However, the RBI intervened, opposing the enforcement of the award and contended that it was illegal and opposed to public policy. The RBI argued that the clause in the shareholder agreement pursuant to which the award was rendered was in contravention with the provisions of the FEMA which prohibited transfer of shares at a price higher than the fair market value.

At the outset, the court ruled that the RBI did not have the ability to intervene in the application for enforcement of the award as it was not a party to the arbitration agreement. Interestingly, the Court further went on to hold that RBI would 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. With this backdrop, the Court observed that since the tribunal had ruled that no RBI permission was required as the sum awarded to Docomo was in nature of damages and not the sale price for shares, RBI would be bound by the determination of the arbitral tribunal and could not refuse permission. The Court further observed that RBI had not placed on record anything to suggest that permission was to be obtained in case of payment of damages. The fact that the put option was only in the nature of a downside protection, and did not provide an assured return, was also a factor which downplayed the objection against enforcement of the award.

The Delhi High Court also found that the provisions of the shareholder agreement could not be said to be void as the FEMA does not contain any absolute prohibition on contractual obligations. The Delhi High Court held that such a transaction merely requires the permission by RBI. Thus, the put option could be performed within the scope of the general permission granted by RBI.

6. Vijay Karia v Prysmian Cavi E Sistemi Srl[34]

The Supreme Court of India was recently faced with the question of whether a foreign arbitral award ought to be refused enforcement as it violates the FEMA, which may result in a violation of public policy under s.48 of the A&C Act.

In this case, a foreign arbitral award directed the petitioners to transfer their shareholding in an Indian entity to the respondent (a foreign entity) at a 10 per cent discount to the fair market value of the shares. The petitioners argued that the NDI Rules do not permit a person resident in India to transfer shares to a person resident outside India at a price below the fair market value.[35] The petitioners

[34] Civil Appeal Nos 1544 and 1545 of 2020.
[35] Regulation 21(2)(b)(iii) of the Foreign Exchange Management (Non-Debt Instruments) Rules 2019.

sought to refuse the enforcement of the foreign arbitral award on the basis that a violation of the NDI Rules and the FEMA results in a violation of the fundamental policy of Indian law, and thereby, the public policy of India.

The Supreme Court, however, rejected the petitioners' arguments and held:

(i) The FEMA refers to the nation's policy of managing foreign exchange, unlike the erstwhile FERA which pertained to policing foreign exchange.
(ii) The FEMA does not contain a provision equivalent to s.47 of the FERA, which rendered transactions that violated the FERA void.
(iii) Further, if a particular act violates any provision of the FEMA or Rules framed thereunder, the permission of the RBI may be obtained post-facto if such violation can be condoned. Thus, a rectifiable breach under the FEMA cannot be considered as a violation of the fundamental policy of Indian law.
(iv) Even if there is a breach of the NDI Rules, it is the RBI's prerogative to step in and direct that the shares are to be sold only at the fair market value (and not the discounted value); or to condone such a breach.

The Supreme Court held that a breach of FEMA does not render the award void, and thereby its enforcement cannot be resisted on this ground. The Supreme Court reiterated its holding in *Renusagar*, and stated that a violation of the fundamental policy of Indian law must amount to a breach of a legal principle or regulation which is so basic to Indian law that it is not susceptible to being compromised. The Supreme Court further ruled that "'Fundamental Policy' refers to the core values of India's public policy as a nation, which may find expression not only in statutes but also in time-honoured, hallowed principles which are followed by the Courts".[36]

Consequently, the Supreme Court upheld the enforcement of the foreign arbitral award.

7. Banyan Tree Growth Capital LLC v Axiom Cordages Limited

Recently, in the case of *Banyan Tree Growth Capital LLC v Axiom Cordages Limited*,[37] the Bombay High Court enforced two foreign arbitral awards issued in an arbitration administered by the Singapore International Arbitration Centre (SIAC) in 2019. The respondents raised objections to the enforcement of the foreign arbitral award on the following grounds:

(i) The underlying put option deed was unenforceable and illegal under the provisions of the FEMA and the notifications thereunder. In 2008, the petitioner had made an investment in the respondent, and the share subscription agreement contemplated an exit for the petitioner pursuant to a put option deed. The respondents contended that the right to exercise a put option was allegedly impermissible

[36] *Vijay Karia v Prysmian Cavi E Sistemi Srl*, Civil Appeal Nos 1544 and 1545 of 2020 at [83].
[37] Commercial Arbitration Petition No.476 of 2019 and Commercial Arbitration Petition No.475 of 2019.

under the FEMA at the time. It was only in 2013 that the FEMA was amended to permit optionality clauses.

(ii) The put option clause provides for guaranteed assured return which is not permissible as the price of transfer of equity instruments under the FEMA must be at the fair market value.

Relying upon on several judgments including *Cruz City* and *Vijay Karia*, the Bombay High Court rejected the respondents' contentions and enforced the SIAC arbitral awards. The Court concluded that a challenge to the enforceability of a foreign award on the ground that the contract violates the provisions of FEMA cannot be sustained.

Conclusion

The judgments discussed demonstrate that so far objections raised pursuant to exchange control laws have not stood in the way of enforcement of foreign arbitral awards. Pertinently, the Supreme Court has held, in unequivocal terms, that a violation of the FEMA does not render an arbitral award unenforceable. Further, even in *Cruz City*, which was affirmed by the Supreme Court in *Vijay Karia*, the Supreme Court dismissed the petition challenging the order of the Delhi High Court.

Initially, the courts had side-stepped allegations of contravention of exchange control laws by asserting that ex-post facto permission could be obtained. However, the recent judgments demonstrate that a pro-arbitration policy is of greater importance than the policy to manage foreign exchange under FEMA. It has been held in the case of *Vijay Karia* that a mere violation of the FEMA does not violate the fundamental policy of Indian law. Thus, a mere violation of FEMA is not a sufficient ground to refuse the enforcement of an arbitral award.

Another question which had remained unresolved until the Supreme Court's decision in *Vijay Karia* pertained to whether an RBI approval would still be required prior to remittance of the funds outside India pursuant to a direction in an arbitral award. In the *Docomo* case, the Delhi High Court interestingly noted that the RBI would be bound by the determination of the arbitral tribunal.[38] However, in the case of *Vijay Karia*, the Supreme Court has held that it would be in the realm of the RBI's powers to either direct a compliance with the FEMA or condone a breach of the FEMA. The Supreme Court also held that post facto approval may be obtained from the RBI for an act or a transaction which breaches the FEMA and the rules framed thereunder. The Supreme Court has clarified that an objection to resist the enforcement of an arbitral award on this ground alone would not sustain. However, it remains to be seen how the RBI will respond to such transactions.

The age-old debate on the interplay between foreign exchange laws and enforceability of arbitral awards, for now, appears to be settled by the Supreme Court. Foreign investors can now take comfort from the general pro-enforcement and minimal intervention approach that Indian courts have followed. From the *Docomo* case it would appear that Indian courts may also extend the

[38] On 31 October 2017, NTT Docomo issued a press release stating that the payment of the award amount in accordance with the Delhi High Court's ruling was received, "Payment Received in Respect of Arbitration Award Regarding Stake in Tata Teleservices", 31 October 2017, Press Releases, NTT Docomo, available at: *https://www.nttdocomo.co.jp/english/info/media_center/pr/2017/1031_00.html* [Accessed 12 February 2021].

pro-enforcement approach to the residual power of the RBI—which might become subject to further limitations should the RBI be seen as exercising it in an overly strict or unreasonable manner.