

# ARBITRATION IN INDIA: DISPUTE RESOLUTION IN THE WORLD'S LARGEST DEMOCRACY

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Legal Briefings

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'Incredible India' (as the tourist marketing campaign describes it) has an economy growing at 7% a year, a population of 1.2 billion of whom some 65% are below the age of 35, and an outward-facing, English speaking business community boasting international players in steel, manufacturing, pharmaceuticals, telecoms, IT consultancy, to name but a few. No wonder India remains high on the list of cross-border traders and investors. But challenges go hand in hand with opportunities, especially when it comes to enforcing legal rights and resolving disputes. Where does international arbitration sit in this, and what is best practice for resolving India-related commercial disputes?

**Nick Peacock, Donny Surtani and Kritika Venugopal of Herbert Smith Freehills' India Disputes group explain the options.**

## THE DISPUTE RESOLUTION AND ARBITRATION LANDSCAPE IN INDIA

### DISPUTE RESOLUTION OPTIONS FOR FOREIGN COMPANIES IN INDIA

Indian litigation - patience required

The Indian judiciary is vast at some 17,000 judges, and while it boasts many professional and diligent judges, the system is under strain. With almost 24 million cases currently pending in the system,<sup>1</sup> the courts are understaffed, meaning bottlenecks and delays are endemic. Depending on the court, commercial cases may take in the region of 5, 10 or 15 years to reach judgment. In such an environment, commercial cases may even be abandoned as they eventually approach trial, as the pace of development, inflation, and the passage of time render the original dispute no longer relevant or economic to contest. Such distant trials render the question of 'interim' relief all important. Indian court litigants fight with aggression and creativity to achieve interim injunctions pending trial which can often effectively decide a dispute for all relevant commercial purposes.

The principles of Indian commercial law will be familiar to many common law practitioners, albeit that outside the main commercial hubs, the depth of experience of complex and strategic commercial or financial disputes can be limited. So too can familiarity with international arbitration and investment treaty arbitration.

Reform is underway although headline initiatives can sometimes be harder to see in practice on the ground. The government of Narendra Modi has embraced the long-debated concept of a 'Commercial Court' in India. The Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts Act was passed in 2015 with the objective of creating Commercial Divisions with the High Court and Commercial Courts at a District level. However, while some judges have been designated to hear commercial cases, there is little sign of extra personnel or resources. The practicality is that rather than easing the burden of the courts, it is the same heavily-burdened courts which have been repackaged to hear commercial cases; which practitioners on the ground believe do not really help the base issue.

In the meantime, the Indian courts are widely watched and widely accessed including by public interest litigants who file suits to challenge the acts of government, individuals, and corporations, creating further obstacles to action in a country already replete with bureaucracy.

All of this means that Indian courts are ideally admired from a distance or with the curiosity of a disinterested observer. The objective of many international commercial parties will be to stay out of the Indian courts, meaning making use of arbitration whenever possible.

## **The arbitration landscape - an emerging independence**

The arbitration landscape in India is defined by the Arbitration and Conciliation Act 1996<sup>4</sup> (the Arbitration Act). The Arbitration Act is made up of two parts:

- **Part I** which applies to disputes with their seat of arbitration in India and gives the Indian courts significant powers to appoint or replace arbitrators, hear procedural appeals,

grant interim measures, and set aside arbitral awards. This is often termed "*onshore arbitration*".

- **Part II** applies to disputes where the seat of arbitration is outside of India and incorporates the New York Convention and the Geneva Convention into Indian law. This is often termed "*offshore arbitration*".

## **Onshore arbitration**

Historically, the great majority of arbitration cases seated in India have been ad hoc arbitrations; that is, arbitration conducted under the framework of the Arbitration Act, but with no supervision by an arbitral institution. A 2013 PwC study found that 47% of Indian companies that had chosen arbitration as their preferred method of dispute resolution chose *ad hoc* proceedings.<sup>5</sup> The predominant choice of arbitrator in such cases has been, and remains, retired court judges. As a result, domestic arbitration has developed the characteristic of 'after hours' litigation with advocates conducting short hearings after the court closes in front of retired judges who bring many of their past practices (such as pleadings and rules of evidence) from the courtroom into the arbitration chamber.

Importantly, the absence of a supervising institution also means that disputes between the parties on matters such as challenges to arbitrators and default selection of arbitrators need to be referred to the Indian court for resolution. Given the delays in obtaining such decisions, this often extends a commercial dispute far beyond the 1-2 years it may take under institutional arbitration (but see below regarding the new 12 month time limit for all onshore arbitrations).

This practice is gradually changing with the emergence of a body of full-time arbitration counsel who do not spend days in court, and so expect their arbitrators to hear cases during office hours in substantial hearings, rather than spread out in short sessions over a longer period. Doing so also means that no longer is the pool of arbitrators limited to retired High Court or Supreme Court judges and notable practitioners have begun hearing cases as arbitrators.

At the same time, institutional arbitration is also growing. Prime Minister Modi addressed the "Global Conference on Strengthening Arbitration and Enforcement in India" held in October 2016<sup>6</sup> and declared that a "vibrant ecosystem for institutional arbitration" was one of his government's priorities.<sup>7</sup>

Foreign arbitral institutions such as the ICC and LCIA have long been used in India. More recently, SIAC has emerged as the number one choice for many parties arbitrating India-related disputes offshore. Foreign institutions within India have fared less well. LCIA India was set up in New Delhi with high hopes in 2009, but closed its doors only seven years later in 2016. SIAC has established a marketing office in Mumbai, but has not opened an Indian branch.



### India

Population: 1,200,000,000

Judges: 18 per million



### UK

Population: 65,000,000

Judges: 56 per million



### US

Population: 320,000,000

Judges: 102 per million

## Judge/population ratio

India has a vast population and a vast judiciary, yet statistics showing the ratio of judges per million of population show the difference between the US and the UK.<sup>2</sup>

The Law Commission of India in its 120th Report (1987) recommended a judge per capita ratio of 50 judges per million people.<sup>3</sup> The Chief Justice of India in April 2017 said that some 70,000 more judges were needed.

Meanwhile, there are various domestic institutions such as the Indian Council of Arbitration (ICA), the Delhi International Arbitration Centre (DAC), the Indian Merchant Chamber (IMC) in Mumbai, and the Nani Palkhivala Arbitration Centre (NPAC) in Chennai. Most recently, these have been joined by the Mumbai Centre for International Arbitration (MCIA) (see below).

## **Offshore arbitration**

Opting for arbitration with a seat outside India has the advantage of avoiding the delays associated with interaction with the Indian courts, at least until enforcement. Parties may still wish to approach the Indian courts for interim relief in support of arbitration (under section 9 of the Arbitration Act), or for assistance in collecting evidence (section 27), assuming they can be obtained in sufficient time to be useful to the ongoing arbitration.

There had historically been the risk that arbitrations taking place outside India may nevertheless be susceptible to Indian court action (including challenges to the award), save where the jurisdiction of the Indian court under Part I of the Arbitration Act was explicitly or implicitly excluded. This led to a generation of arbitration agreements in cross-border contracts which contained exclusions of Part I of the Arbitration Act (save sometimes for sections 9 and 27). This risk was resolved by the Indian Supreme Court in its 2012 BALCO decision<sup>8</sup> which held that the Indian courts had no supervisory jurisdiction over arbitrations held outside India.<sup>9</sup> However this decision was stated to be prospective only, leaving a prior batch of arbitrations cases working their way through the Indian courts under the old law. The BALCO situation also confirmed the existence of a lacuna in that interim relief under section 9 (found in Part I of the Arbitration Act) was not available to parties with arbitrations seated outside India. The Supreme Court noted the lacuna but held that it was for the Indian legislature to resolve. This left parties with a difficult choice of whether to opt for offshore arbitration, but accept that they would have no ability to seek interim relief inside India, or choose onshore arbitration with the additional issues of Indian court supervision and award challenge.

That lacuna has now been filled with the 2015 Arbitration Act amendments (see below), meaning parties once again have a straightforward choice of onshore and offshore arbitration, based on the needs, dynamics and bargaining positions of the parties to the transaction.

Thus, while onshore arbitration is growing, a number of offshore seats in particular Singapore and London, plus also Hong Kong, Kuala Lumpur, Dubai and Paris, remain common and sensible choices.

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# **A DEVELOPING PICTURE**

## **ARBITRATION ACT REFORMS**

Reform of the Arbitration Act had long been discussed in India, with various proposals and draft Bills having been produced over the last 10 years. The aftermath of the BALCO decision, the imperative to take further pressure off the Indian court system, and the stated desire of the Modi government to encourage greater foreign investment into India, finally led to amendments to the Arbitration Act being passed in 2015, first as an Ordinance and then as the Arbitration and Conciliation (Amendment) Act, 2015<sup>10</sup> (Arbitration Amendment Act) which came into force on 23 October 2015.<sup>11, 12</sup> Some of the key reforms made by the Arbitration Amendment Act were:

- Resolving the lacuna left by the BALCO decision by providing that sections 9 and 27 of the Arbitration Act would, subject to contrary agreement, apply to arbitrations with a seat outside India. Once more, parties arbitrating in Singapore, London or elsewhere are able to approach the Indian courts for interim relief in support of the arbitration.
- Addressing delays in the conduct of onshore arbitration, by providing that all Indian-seated arbitral tribunals must render their award within 12 months from the date of appointment. This period can be extended by a further six months by agreement of the parties, after which the mandate of the arbitrators will automatically terminate, unless an extension is allowed by the Indian court. The Arbitration Amendment Act having been passed only at the end of 2015, the question of whether the deadline will produce a flurry of extension applications to the courts will only now start to be answered, along with the attitude of the courts to such applications. This in turn, will indicate whether accepting an appointment to an onshore Indian arbitration will be more or less attractive for arbitrators in the future.
- Attempting to narrow the definition of "public policy" as an exceptional ground for setting aside arbitral awards in the Indian courts (in line with the New York Convention). Consistent with recent case law, the Arbitration Amendment Act now states that the exception will only apply where an award (i) has been obtained fraudulently, (ii) contravenes the fundamental policy of Indian law, or (iii) conflicts with the most basic notions of morality or justice. While the scope for ambiguity to the public policy exception remains in India (as it does in most jurisdictions), the legislative intent to narrow the exception appears clear and, it is hoped, will be followed by Indian judges.
- Importantly, the amendments removed the automatic stay previously applied under section 36 of the Arbitration Act which prevents enforcement while an onshore award is subject to set-aside proceedings. This had produced an obvious incentive for any losing party to an onshore arbitral award to challenge in the Indian courts (which challenges could take upwards of 5 years to be decided) in order to frustrate enforcement. Now the Indian courts have a discretion to stay enforcement, but no obligation to do so. Moreover, the Arbitration Amendment Act now also fixes a one year time limit for the decision on a challenge application (under section 34 of the Arbitration Act). It is likely that a combination of these provisions will considerably reduce the number of awards

being challenged in the Indian courts.

## **A TREND TOWARDS INSTITUTIONAL ARBITRATION?**

The current support for institutional arbitration from the Indian government may owe as much to the desire to take a load away from the Indian courts, as to improve the working of the onshore arbitration system. In any event, it is welcome. Despite the demise of LCIA India, the increased support for institutional arbitration in India is palpable.

One embodiment of this is in the creation and the promotion of the MCIA launched in Mumbai in 2016.<sup>13</sup>

The MCIA is supported by the Government of Maharashtra as part of its wider initiative to develop an international financial centre in Mumbai. Parallels may be drawn in this regard with the creation of financial centres, and associated arbitration institutions, in Middle Eastern cities such as Dubai, Qatar and Bahrain. Taking its support one step further, the Maharashtra Government recently announced<sup>14</sup> that all cases of a value of more than five crore INR (approx. US\$770,000) will have to compulsorily contain institutional arbitration clauses as the mode of dispute resolution.

The MCIA has emerged from a joint initiative between the State Government and the domestic and international business and legal communities. It now has a full set of institutional rules, a Council composed of Indian as well as overseas members, and a first class arbitration centre with hearing facilities in Mumbai. Herbert Smith Freehills Partner and Head of the India Disputes Practice Nicholas Peacock was part of the Rules Committee and in 2016 joined the founding MCIA Council.<sup>15</sup>

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***"It is an interesting time for arbitration in India and the MCIA is well-placed to take advantage of growth in the market"*** Neeti Sachdeva, MCIA Registrar

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## **MIXED MESSAGES: CANCELLATION OF INVESTMENT TREATIES**

While the past few years have seen encouraging trends for commercial arbitration in India, the Indian Government's treatment of its bilateral investment treaties (BITs) has created uncertainty for investors into and out of India.<sup>16</sup>

In 2016, the Government reported that it had sent notices to terminate BITs with 58 countries. While no definitive list of which BITs have been cancelled has been produced, it is known that the BIT between India and the Netherlands was terminated with effect from December 2016,<sup>17</sup> while the BIT with the UK was terminated from the end of March 2017.<sup>18</sup> The BIT with Australia also terminated in March 2017.<sup>19</sup> For its remaining 25 BITs which are still in their initial term and not yet capable of termination, the Indian Government has instead proposed 'Joint Interpretative Statements'<sup>20</sup> to the counterparties of these BITs seeking to restrict the scope of the protections under those ongoing BITs, in line with a recast Model BIT which India adopted in December 2015.

The terminations are an apparent reaction to the wave of recent BIT claims against India brought by investors. The first of these recent claims was the case brought by White Industries of Australia which concerned allegations of excessive judicial delays in enforcing a commercial arbitration award through the Indian courts.<sup>21</sup> An award was made against India in 2011 (which it duly honoured), resulting in a notable backlash by India against the current mechanism of BIT protections. In the meantime more claims were filed with the result that, by 2016, India was one of the most frequently named respondent states, with four claims brought against it by foreign investors that year. The current number of BIT claims against India is understood to be around 17.

The Government's first response was to re-issue its Model BIT which explicitly reduced the scope of protections available to foreign investors into India (and at the same time, to Indian investors into the counterparty state), including specially targeting matters such as the provision of non-commercial services by a state (ie court services) and the levying of (retrospective) tax which had formed the basis of prior or existing BIT claims.<sup>22</sup>

While the Model BIT retained the use of arbitration for the settlement of investor claims, it included a new requirement for investors to exhaust local remedies (for a minimum five year period from the date on which the investor first acquired knowledge of the state action in question) prior to initiating arbitration, unless the investor can demonstrate that there are no available local remedies reasonably capable of providing any relief.

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***"The institution's offering has been well-received by commercial parties and, although in its infancy, the MCI A has already been delegated the power of an appointment of an arbitrator by the Indian Supreme Court under s11 of the Act"*** Neeti Sachdeva, MCI A Registrar

It remains unclear which BIT terminations are pending and what protections will remain in place for investments already underway. For those BITs that are not yet terminated it remains to be seen if the relevant governments will agree with India's proposed joint interpretative statement and what impact the statement has on future investment and claims brought against India based on the ongoing BITs.

India having served notice to terminate its existing BITs with the seeming objective of adopting new BITs based on its Model BIT, investors into India are now faced with an absence of BIT protections for new investments, and no sense of when any new investment protection regime will be put in place. For example, the EU counterparties to terminated BITs are unable to negotiate new BITs with India, and must await the EU Commission to negotiate on behalf of all member states (including, for now, the UK).

While investments made before the termination of the BITs may be protected under the 'sunset' clauses in the relevant BIT, new investors into India, and Indian investors into counterparty states, will no longer benefit from treaty protections. This lack of previously available protections, together with the message sent by the Indian Government in removing these protections, must inevitably give prospective investors some degree of unease as they consider India as an investment destination.

Therefore, while there appear to be strides of development in the domestic arbitration landscape, when it comes to international arbitration, and in particular, investment treaty arbitration, there still appears to be a long road ahead before India can be touted as being a secure investor-friendly destination.

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***"MCIA is the first of its kind arbitral institution in India providing dedicated arbitration hearing facilities and has conducted over 100 arbitrations at its premises" Neeti Sachdeva, MCIA Registrar***

We will be publishing the sixth edition of our well-regarded Guide on Dispute Resolution and Governing Law Clauses in India-related Commercial Contracts in August. The Guide is intended to assist in-house counsel who handle India-related commercial contracts on behalf of non-Indian companies and who need to have a practical understanding of the nuances of drafting dispute resolution and governing law clauses in the Indian context. If you would like to request a copy please email [asia.publications@hsf.com](mailto:asia.publications@hsf.com) and we will send you an electronic copy as soon as it is available.

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## FOOTNOTES

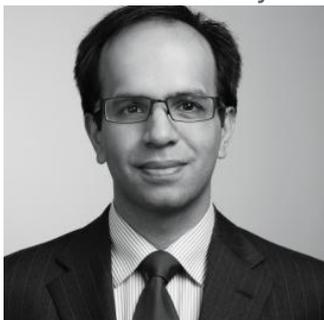
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