India Unleashed

May 2016

Dear Readers,

The NDA Government completed two years in office on 26 May this year. To expect a new regime to wave a magic wand to solve all problems, transient and endemic, is unrealistic. However, two years is good enough to assess the direction of economic policy and the spirit of a Government's endeavours. Naysayers will not agree, but this Government has taken steps in the right direction. Even if one discounts the din of frequent grandstanding, the very fact that the Government has managed to transact significant legislative business in two years is a sound indicator of its performance.

Amendment to arbitration laws, unveiling of the new regime on insolvency and bankruptcy, and law on regulation of real estate sector are few examples of how the Government has been able to push legislation despite being in minority in the Upper House.

In the third edition of 'India Unleashed' we examine the recent amendments in the arbitration laws. Quicker, efficient and cost-effective resolution of disputes is the bedrock of every business friendly jurisdiction and arbitration is the most preferred mode of dispute resolution for businesses. The Arbitration and Conciliation (Amendment) Act, 2015 is a significant step in the attempt of the lawmakers to heal the cracks in the edifice of arbitration in India.

We hope you find India Unleashed useful. Please feel free to provide your feedback at indiaunleashed@khaitanlegal.com.

We also propose to bring out a special mid-quarter edition of India Unleashed on the Insolvency and Bankruptcy Code, 2015, next month. So watch this space!

Warm Regards,

Sakate Khaitan
Senior Partner

In Brief

FDI in E-Commerce : More Questions than Answers!

Until recently, 100% Foreign Direct Investment ("**FDI**") in Business to Business e-commerce was permitted under the automatic route. However, the FDI policy was silent on FDI in Business to Consumer e-commerce ("**B2C e-Commerce**"). Press Note No. 3 of 2016 dated 29 March 2016 ("**Press Note**") has clarified the Government's position with respect to FDI in B2C e-Commerce.

The Press Note divides B2C e-Commerce into inventory based model (where goods and services owned by the e-commerce entity are sold directly to consumers) and marketplace based model (where the e-commerce entity only provides an IT platform to act as facilitator between buyer and seller).

Subject to certain conditions, 100% FDI under the automatic route has been allowed in the marketplace based model. FDI is not permitted in the inventory based model.

The conditions for e-commerce entities carrying on business under the marketplace model *inter alia* permit them to provide support services, such as warehousing, logistics, order fulfilment, call centre, payment collection, etc. to the sellers. However, such e-commerce entities are restricted from exercising ownership over inventory; effecting sales of more than 25% through one vendor or its group companies; and influencing, either directly or indirectly, the sale price of goods or services to ensure a level playing field is maintained. Further, post-sales, delivery of goods to the customers, customer satisfaction and warranties/ guarantees on goods and services sold have been expressly stated to be the responsibility of the seller.

Some of the restrictive conditions do not appear to be in line with the market practices of existing Indian e-commerce entities and has lead several of them to re-think their business models and strategies.

It remains to be seen whether the market practices force the Government to re-think their policy with respect to FDI in e-commerce entities, or whether the e-commerce entities in India are forced to reorganise their business to ensure they can access FDI.

Big Reform Push: New Insolvency Regime to become a reality soon!

The much awaited revamp of the insolvency and bankruptcy regime is finally taking shape. Indian Parliament approved the Insolvency and Bankruptcy Code, 2016 (**"Code"**) in May 2016. When enforced, the Code will act as the consolidated legislation for insolvency and bankruptcy in India.

The primary objective of the Code is to consolidate and amend the laws relating to reorganisation and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner and maximisation of value of their assets. It also aims to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders.

Currently, bankruptcy and insolvency is governed by multiple laws with different agencies having overlapping jurisdictions resulting in the process becoming time consuming, complex and expensive.

The Code envisages a resolution plan to be approved for a company undergoing insolvency and also addresses the issue of efficiency by mandating a formal corporate insolvency resolution process, which can be initiated by financial creditor, operational creditor or corporate debtor itself. Time line of 180 days has been set out to complete the process, extendable for another 90 days. If within the stipulated timeline no resolution plan is achieved, the company is directed to be liquidated. The Code also allows for a fast track insolvency process, to be completed within 90 days, extendable for 45 days.

The National Company Law Tribunal would adjudicate insolvency resolution for companies and the Debt Recovery Tribunal would adjudicate insolvency resolution for partnership firms and individuals.

The Code also paves way for Insolvency Practitioners who would ensure completion of the insolvency process, and also for establishment of information utilities to collect, collate and disseminate financial information to facilitate the insolvency resolution. Insolvency and Bankruptcy Board will be established for the purpose of regulating insolvency and bankruptcy processes and insolvency professionals and agencies.

After Amendment...
Will the Game Change for Arbitration in India?

With "ease of doing business in India" as its mantra, the current Government has taken several measurers to enhance the attractiveness of India as a business destination.

The much anticipated amendments to the Indian arbitration law is one among many such initiatives. Indian Government passed the Arbitration and Conciliation (Amendment) Act, 2015 ("**Amendment Act**"), which was notified on 1 January 2016. It is expected that the Amendment Act, which is effective from 23 October 2015, will address the concerns of international business community that is often apprehensive of arbitrating in India. It also bolsters Government's attempts at increasing the "ease of doing business in India".

The Amendment Act brings about much needed changes to the Arbitration and Conciliation Act, 1996 ("**Act**"), by offering clarity with respect to interim relief for foreign seated arbitrations, judicial intervention and independence of the arbitral tribunal; and introduction of measures to make arbitration in India time and cost efficient.

We examine some of the key changes brought about by the Amendment Act that is intended to make Indian arbitration a more effective and efficient dispute resolution mechanism and position India as an arbitration friendly jurisdiction.

INTERIM RELIEFS

Interim Measures and Appeals from Certain Orders Permitted in Foreign Seated Arbitration

After years of debate and conflicting judgements, the question of applicability of Part I of the Act to foreign seated arbitrations was finally put to rest by the Supreme Court, in *Bharat Aluminium Company v. Kaiser Aluminium Technical Services*[1], by holding that Part I of the Act is not applicable to foreign seated arbitrations arising from arbitration agreements entered into after 6 September 2012. Although this verdict reduced interference of the Indian judiciary in foreign seated arbitral proceedings, it also restricted the ability of parties to seek interim reliefs in India.

Inapplicability of Part I of the Act put foreign seated arbitrations at a significant disadvantage as a party's only chance of interim relief was reduced to an order from the arbitral tribunal or an order from a court outside India and in both cases the enforceability remained uncertain. Therefore, if an arbitral tribunal was not yet formed, a party in a foreign seated arbitration would be left without any urgent remedy in India. This lacuna has been recognised and remedied by the law makers in the Amendment Act, by making the provisions with respect to interim relief, court assistance in taking evidence and appeal from an order of interim relief passed by a court, under Part I of the Act, applicable to foreign seated arbitrations as well.

Supremacy of Arbitral Tribunal in Granting Interim Reliefs

Before the Amendment Act came into effect, the Act conferred jurisdiction to both, courts as well as the arbitral tribunal, to pass orders for interim measures during the pendency of arbitral proceedings.

Recognising the problems of delay that such parallel jurisdiction created, the Amendment Act prevents courts from accepting any application for interim measures once the arbitral tribunal is already constituted; with a caveat that the courts could exercise this power *if circumstances exist which may not render the remedy provided by the arbitral tribunal efficacious*.

The Amendment Act also addresses the issue of enforceability of interim orders passed by the arbitral tribunal by clarifying that such orders shall be deemed to be an order of the court and would be enforceable accordingly. This change brings the Indian regime in line with the international best practices, ensuring that once an arbitral tribunal is constituted, it has almost exclusive jurisdiction to grant effective interim reliefs.

REDUCED CHALLENGES

Public Policy

The Act allowed both domestic awards and foreign awards to be set aside if they were in conflict with the 'public policy' of India and the interpretation of this term has been the subject of much judicial debate over these years. In *Oil & Natural Gas Corporation Ltd. v. Saw Pipes Ltd.* , the Supreme Court held that an arbitral award could also be set aside if it was 'patently illegal', on the ground that it was against the 'public policy' of India which includes patent illegality. However, in the case, *Shri Lal Mahal Ltd. v. ProgettoGrano Spa*[3] ("**Shri Lal Mahal Case**"), the Supreme Court restricted the scope of the defence of 'public policy' in case of foreign awards and clarified that 'patent illegality' would not be recognised within the scope of 'public policy' as a ground to refuse enforcement of a foreign award.

The Amendment Act gives legislative force to the decision of the Apex Court in Shri Lal Mahal Case, by restricting the scope of 'public policy', and recognising 'patent illegality' as a defence against enforcement of only domestic arbitral awards, and not foreign awards.

Independence and Impartiality of Arbitrator

With the introduction of the Fifth Schedule, which lists the grounds giving rise to justifiable doubts as to the independence or impartiality of arbitrators; and the Seventh Schedule, which lists the relationships between an arbitrator and the parties or counsel, that would make the arbitrator ineligible to be appointed as an arbitrator, except when expressly waived by the parties after the dispute has arisen; the Amendment Act seeks to assist arbitrators and parties to ascertain the independence of arbitrators, and limit the scope of challenging their appointment.

This change is in line with international best practices, and the Schedules have been modelled on the basis of the Guidelines on Conflicts of Interest in International Arbitration, issued by the International Bar Association.

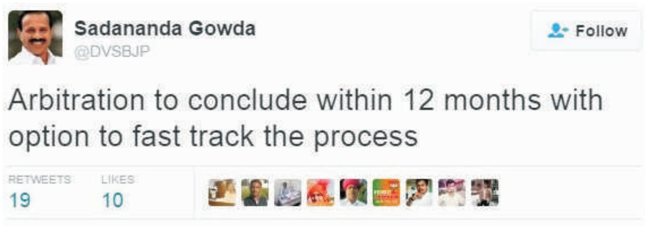
TIME CONSIDERATIONS

One of the main concerns parties usually have, while deciding whether to subject their disputes to Indian arbitration, is that arbitration in India is sometimes long-drawn and there is no time guarantee for resolution of disputes. To address this concern, the Amendment Act has introduced the following amendments:

Time Limit

Once a court passes an order for interim measures before the commencement of the arbitral proceeding, the arbitral proceeding ought to commence within ninety days from the date of the order. However, the court would have the discretion to determine a longer time for commencement of the arbitration.

Further, the Amendment Act also requires an arbitral proceeding under Part I of the Act to complete and award to be passed within a period of twelve months from the date of receipt of notice of appointment by the arbitrators. This period can only be extended for a maximum period of up to six months, with the consent of the parties. Upon failure to pass an award within the time prescribed, the mandate of the arbitrators automatically terminates. A further extension can only be permitted by court for sufficient cause.



Courtesy: Twitter

Efficient Hearings

The Amendment Act encourages an arbitral tribunal to hold oral hearings for evidence and arguments on a day to day basis and to limit adjournments only to cases of sufficient cause. It also empowers the arbitral tribunal to order costs, including exemplary costs, on a party that seeks unnecessary adjournments.

Monetary Incentive

The Amendment Act links the arbitrator's fee to the time taken to pass the final award and entitles the arbitrators to additional fees if the award is made within a period of six months. Further, the courts have also been empowered to order a reduction of fees if there is a delay beyond eighteen months in passing the final award, for reasons attributable to the arbitrators.

Expedited Procedure

The Amendment Act also introduces a fast-track arbitration procedure to resolve disputes provided such option is exercised prior to or at the time of appointment of the arbitral tribunal. Under the fast-track process, the arbitral tribunal would decide disputes based on written pleadings, documents and submissions filed by the parties. An oral hearing would be held only if all parties request it or if the arbitral tribunal considers it necessary in order to clarify certain issues. The award ought to be passed within 6 months from the date of reference.

Although expedited arbitration is recognised by the rules of several arbitral institutions, including the International Chamber of Commerce, which have seen successful implementation thereof in many cases, it was not recognised under the Act earlier. This amendment is expected to provide some relief to parties who face tremendous commercial impact due to time lag and delay in dispute resolution.

PRACTICAL CONSIDERATIONS

Judicial Support in International Commercial Arbitration

The definition of the word 'court' has been revised to ensure that in case of international commercial arbitrations, seated in India or outside, the court approached is only a High Court. This is expected to expedite the court process in such arbitrations since High Courts have more experience in dealing with international issues.

Arbitrator's Fees

The Amendment Act has empowered the High Court to frame rules for determination of the fees of the arbitral tribunal and the manner of its payment to the arbitral tribunal. Further, a 'model' fees structure for arbitrators has also been included in the Fourth Schedule to the Act, for the consideration of the High Court. The Amendment Act prevents the applicability of this fee structure to institutional arbitration and international commercial arbitration.

Procedural Flexibility

The Amendment Act has also brought significant procedural flexibility by expressly recognising arbitration agreements concluded via electronic communication, enabling respondents to file a counter-claim or set off and allowing a party to appeal against an order refusing to refer parties to arbitration.

Prospective Applicability

Unless specifically made applicable by parties through agreement, the Amendment Act applies only to arbitrations that commence after 23 October 2015. Arbitrations that have commenced prior to 23 October 2015 would continue to be governed by and be subject to the provisions of the Act, as existed prior to the amendments.

CONCLUSION

The Amendment Act is certainly a welcome step and will go a long way in positively impacting the arbitration landscape in India. Not only has it made the Indian legal regime more pro-arbitration, it has also brought clarity in provisions which were subject to frequent judicial review and has attempted to align the statute with international best practices.

The proactive stance taken by the law makers with respect to the maintenance of strict time limits and reduced judicial intervention would, in our view, ensure that arbitral proceedings are not unnecessarily derailed by dilatory tactics. Further, by clarifying the role of the arbitral tribunal in granting interim relief, the Act ensures that arbitration would be a one-stop solution for resolution of commercial disputes. We believe that the greater power given to the arbitral tribunal coupled with strong judicial backing, will further the cause of arbitration in India.

[1] 2012 (3) ARBLR 515 (SC).
[2] AIR 2003 SC 2629.
[3] (2014) 2 SCC 433.

Doors of "Haven" to Close? India-Mauritius Tax Treaty Amended

India and Mauritius have recently signed a protocol (**"Protocol"**) amending the India-Mauritius Double Taxation Avoidance Agreement (**"DTAA"**). The DTAA, first negotiated in the 80s, famously exempted capital gains arising to a Mauritius resident from Indian income tax charge, and has been the root of significant controversy in an Indian tax context. India attracts maximum foreign direct investment via the Mauritius route, however concerns regarding money laundering and tax evasion have gathered momentum in recent times, prompting a renegotiation of the DTAA.

As per the terms of the Protocol, India will tax capital gains arising from the transfer of shares of an Indian company, acquired on or after 1 April 2017. During a transition period of 1 April 2017 to 31 March 2019 (**"Transition Period"**), capital gains will be taxed at 50% of the Indian domestic tax rates, subject to fulfilment of conditions in the Limitation of Benefits (**"LOB"**) article. From financial year 2019-20 onwards, capital gains will be subject to tax at full rates. However, investments in shares made prior to 1 April 2017 are grand fathered and any income arising in this regard will not be subject to tax in India.

Courtesy: Google Images

The LOB article ensures that the lower tax rates during the Transition Period are not abused by mere shell and conduit companies by limiting eligibility in this regard to companies resident in Mauritius that satisfy the 'main purpose' and 'bonafide business' tests.

The Protocol has far reaching consequences on current and future investment structures into India, and would also have to be analysed in the context of the domestic anti-avoidance rules (that come into force from 2017) and the overall climate of measures against base erosion and profit shifting (BEPS). Further, benefits under the India-Singapore DTAA would be impacted, given that capital gains related exemptions available under the India-Singapore DTAA, are contingent on exemptions under the India-Mauritius DTAA.

In Other News...

Unravelling D&O Liability and Claims Handling:

In the first week of May, Khaitan Legal Associates co-hosted a series of workshops on D&O Liability and Claims handling in Mumbai, Pune and New Delhi along with India Insure, a composite Insurance broking company. The workshop was facilitated by Nilam Sharma, a well-known D&O insurance/reinsurance expert from London. The event witnessed active participation from general counsels, risk managers, claim handlers and experts who brainstormed on various relevant and practical issues concerning the area of D&O insurance. A glimpse from the workshop in Mumbai: L to R: Deepali Rao (India Insure), Sakate Khaitan (Senior Partner, Khaitan Legal Associates), Sushant Sarin (Tata AIG) and Nilam Sharma.

Panel discussion organised by Khaitan Legal Associates:

On 16 March, Khaitan Legal Associates conducted a panel discussion on 'Doing Business in India 2016 - Latest Trends and the Road Ahead'. The panel discussion turned out to be an exhilarating evening with distinguished guest speakers from Securities and Exchange Board of India, Reserve Bank of India and from the industry. The esteemed panel discussed the changing regulatory landscape of India, the emerging trends in economic reforms, the outlook for 2016 and how regulators and businesses can work together towards the creation of a conducive regulatory environment. It was a highly interactive session with the audience getting an opportunity to communicate with the panellists and experts.

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