

INDIA AND INTERNATIONAL ARBITRATION: THE DABHOL EXPERIENCE

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Fali Nariman notes that India ratified the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention)¹ quite early and, in 1996, adopted a new Arbitration and Conciliation Act² that is, for the most part, in conformity with the United Nations Commission on International Trade Law (UNCITRAL) Model Law.³ He says that the new Act “limits court intervention in domestic and international arbitration,” unlike in the “old days” where “the [Indian] courts frequently interfered with arbitration proceedings and awards, international and domestic, on the judge-based notion that it was the duty of courts to keep arbitrators within the law.”⁴ Moreover, Mr. Nariman argues that the Indian courts have no anti-foreigner bias, and that if one has sufficient patience to await the outcome of court challenges to the enforcement of arbitral awards, “the foreigner can justifiably rely upon the arbitral process when dealing with India.”⁵ The implication is that India now provides a suitable location for international commercial arbitration.

But, the experience of the Dabhol project suggests otherwise.⁶

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1. Fali S. Nariman, *India and International Arbitration*, 41 GEO. WASH. INT'L L. REV. 367, 371 (2009).

2. *Id.* at 372.

3. Convention on the Recognition and Enforcement of Foreign Arbitral Awards, June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 38.

4. The Arbitration and Conciliation Act, No. 26 of 1996, INDIA CODE (2000), *available at* <http://www.ficci-arbitration.com/htm/acts.pdf>.

5. UNCITRAL Model Law on International Commercial Arbitration, G.A. Res. 61/33, U.N. Doc. A/RES/61/33 (Dec. 18, 2006), *available at* http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html.

6. The author, then–Deputy Legal Adviser at the Department of State, was involved in the 2004-05 phase of the Dabhol dispute, when the United States initiated arbitration against India under an Overseas Private Investment Corporation (OPIC) investment guaranty agreement. *See generally* United States v. India, Request for Arbitration, Nov. 4, 2004 [hereinafter U.S. Request for Arbitration], *available at* <http://www.opic.gov/sites/default/files/docs/GOI110804.pdf>.

This project spawned a large number of arbitration cases in many venues, under multiple contracts and several bilateral investment treaties. Perhaps more significant than the number of cases is the fact that at every turn, despite the 1996 Act and the New York Convention, the Indian government, the Maharashtra state government, and both central and state governmental entities refused to honor payment guarantees and sought to avoid the commitments in the relevant agreements to settle the disputes by international arbitration. Intervention by India's courts was not limited by the new 1996 Act: the Indian courts collaborated in the effort by enjoining international arbitration of the disputes at the behest of Indian government entities. The series of events, which are described below, casts serious doubt as to whether one can rely on the Indian government and Indian courts to comply with arbitration commitments.

The facts underlying the Dabhol matter are extremely complex.⁷ The brief summary here only skims the surface of the myriad entities, contracts, events, and arbitration and court cases that flowed from the Dabhol investments.

In the 1990s, India had begun to encourage foreign investment and established a fast-track process for investment approval. In this environment, the Dabhol Power Corporation (the Corporation), a local corporation owned by General Electric (10 percent), Bechtel (10 percent), and Enron (80 percent), entered into an agreement with the Maharashtra State Electricity Board (the Board) for a two-phase project. The first phase was for the construction of an approximately 700-megawatt distillate fuel power plant. The second was for an approximately 1400-megawatt gas-fired power plant, which would depend on the import of liquid natural gas through the Dabhol port and gasification of the imported liquefied natural

7. General information about what happened may be found in Preeti Kundra, Note, *Looking Beyond the Dabhol Debacle: Examining its Causes and Understanding its Lessons*, 41 VAND. J. TRANSNAT'L L. 907 (2008). Relevant information may also be found in the American Arbitration Association (AAA) arbitration award in the case brought by the investors against OPIC. See *Bechtel Enterprises Int'l Ltd. vs. Overseas Private Inv. Corp.*, No. 50 T195 00509 02, at 3-24 (2003) [hereinafter AAA Award], available at http://www.opic.gov/sites/default/files/docs/2294171_1.pdf. For further factual background, see generally *Expropriation Claim of Bank of America*, OPIC Memorandum of Determinations (2003) [hereinafter OPIC Memorandum] and *Capital India Power Mauritius I v. Maharashtra Power Dev. Corp. Ltd.*, No. 12913/MS (2004) [hereinafter ICC Award], available at http://ita.law.uvic.ca/documents/Dabhol_award_050305.pdf (International Chamber of Commerce (ICC) award in the investor-state arbitration brought by a Bechtel subsidiary under the Mauritius bilateral investment treaty with India). The factual summary herein draws on information in Kundra's Note, the OPIC Memorandum, the AAA and ICC Awards, and the U.S. Request for Arbitration, *infra* note 6.

gas (LNG). The Dabhol project was India's largest investment project to date, with over \$2 billion in secured loans.

Under a late 1993 agreement, the Board undertook to purchase power from the Corporation. In early 1994, the Board, the government of Maharashtra state, and the government of India each gave payment guarantees. The government of Maharashtra state also agreed to support the project. Later, an escrow agreement was established to ensure the availability of funds, and Canara Bank, an Indian bank, provided a letter of credit as a further guaranty. The U.S. Overseas Private Investment Corporation (OPIC) lent about \$160 million for the project and provided the U.S. private corporations that owned the Corporation political risk insurance. Both Indian financial institutions and offshore lenders, including Bank of America, made loans to the project.

The first series of disputes arose in 1995. After an election, a new Maharashtra state government, which had campaigned against the project and alleged corruption was involved in the contracting, ordered that the newly initiated construction be terminated. The Corporation commenced arbitration in London against Maharashtra state for breach of contract. The state challenged the jurisdiction of the tribunal and filed suit in Bombay High Court seeking to void the contract, alleging fraud and misrepresentation. But the parties reached a negotiated settlement, and this arbitration and litigation was terminated.

Five years later, after a year and a half of operation, the Board defaulted on its payment obligations. In January and March 2001, the Corporation demanded payment under the Maharashtra state and Indian government guarantees, respectively. In April 2001, the Corporation commenced arbitration proceedings against the Board, the state government, and the central government.

In response, the Board asked the Maharashtra State Regulatory Commission (the Commission) to enjoin the Corporation from pursuing international arbitration, which the Commission did, finding that it had exclusive jurisdiction over the dispute between the Corporation and the Board. This was appealed to the Bombay High Court, which ruled that the Commission had authority to determine its own jurisdiction. The Indian Supreme Court reversed, instructing the Bombay High Court to make a finding on whether the Commission had exclusive jurisdiction. The Bombay High Court then held that the Commission had such jurisdiction, and the case again went to the Indian Supreme Court, where it remained pending when the parties resolved the disputes in 2005.

In addition, the government of Maharashtra obtained an injunction from the Bombay High Court against the Corporation pursuing international arbitration against the government under its guaranty. And the government of India obtained an injunction from the Delhi High Court against the Corporation pursuing international arbitration against that government under its guaranty.

The next series of arbitrations occurred from 2003 to 2005. On the one hand, the U.S. companies sought to collect on their political risk insurance from OPIC, arguing that the Indian governments and courts had taken away the arbitration remedy provided in the relevant contracts. When OPIC did not pay the companies' claims, the companies instituted arbitration proceedings under the auspices of the American Arbitration Association against OPIC.⁸ The panel found that the Board, the government of Maharashtra, and the government of India each violated the relevant agreements for political reasons and without any legal justification. The panel also found that the Board, the Maharashtra State Regulatory Commission, and the Indian courts had enjoined and otherwise taken away the claimants' international arbitration remedies in violation of established principles of international law and in disregard of India's commitments under the New York Convention and the Indian Arbitration Act. As a result, the panel ordered OPIC to pay the companies.⁹ Thereafter, the U.S. government instituted arbitration proceedings against the government of India for claims to which OPIC was subrogated under the U.S. investment guaranty agreement with India.¹⁰

At the same time, the U.S. companies, which had channeled their investments through subsidiaries in Mauritius and the Netherlands, brought separate arbitration cases directly against India under bilateral investment treaties (BITs) India had with those two countries.¹¹ The International Chamber of Commerce (ICC) case resulted in a decision against India in April 2005.¹²

8. See AAA Award, *supra* note 7, at 22-23.

9. *Id.* at 24, 30.

10. See U.S. Request for Arbitration, *supra* note 6, at 2.

11. See Press Release, Bechtel, Bechtel Wins Court Order to Seize Indian Assets; Maharashtra Defaults on \$123 Million International Arbitration Award (May 31, 2005), <http://www.bechtel.com/2005-05-31.html>; Press Release, Bechtel, Arbitration Tribunal Rules for Bechtel In India's Dabhol Power Project (May 3, 2005), <http://www.bechtel.com/2005-05-03.html>. See generally ICC Award, *supra* note 7.

12. See ICC Award, *supra* note 7, at 30-31. The proceedings under the Dutch bilateral investment treaty (BIT) were still pending at the time the Dabhol matter was settled.

While the ability of corporations subject to their jurisdiction to pursue international arbitration had been effectively thwarted by Indian courts and state entities, they could not prevent international arbitration brought by foreign governments or by offshore corporations under applicable BITs. Thus, while international arbitration had failed effectively to resolve any Dabhol dispute since 1995, in 2005, the commencement of arbitration by the United States under the Investment Incentive Agreement and the International Chamber of Commerce (ICC) award under the Mauritius BIT seemed to have a significant impact. At this point, the parties had reached an overall settlement of the matter, and the various still-pending arbitration and court proceedings were terminated.¹³

This review of the Dabhol matter demonstrates that India was not yet ready to play by the rules of commercial international arbitration, despite its membership in the New York Convention and despite the 1996 Indian Arbitration and Conciliation Act. On paper, it may look as if a business partner or investor may rely on India having attuned itself to a modern international arbitration system, but the Dabhol experience suggests that such reliance is not warranted.

Although India solicited foreign investment in the power section and provided every imaginable sort of guaranty that the terms of the relevant contracts would be honored, the project became an issue in local politics and, with a change in government, no effort was spared to undercut it. When a new coalition took control of the state government in Maharashtra, the government, rather than abide by its commitment to support the project, sought to terminate it. This was a policy decision by the state government, not made because of a shortage of funds but made with an understanding that it was contrary to Maharashtra's contractual obligations. The Finance Minister of the State of Maharashtra said:

We have refused to honor our contractual obligations by choice. It is our strategic decision not to pay [on the guaranty agreement] . . . as we want to scrap the power purchase agreement the state has with [the Corporation] Our decision not to pay has nothing to do with the state's finances.¹⁴

Moreover, the Maharashtra state regulatory authorities and government took active steps to thwart the agreed mechanism of inter-

13. See Press Release, Bechtel, Statement by Bechtel on Dabhol Settlement (July 12, 2005), <http://www.bechtel.com/2005-07-12.html>; Press Release, GE, GE Announces Comprehensive Settlement on Dabhol Power Project (July 2, 2005).

14. ICC Award, *supra* note 7, at 27.

national arbitration. As recounted above, each took steps to prevent entities subject to its jurisdiction from pursuing arbitration. The Commission asserted jurisdiction to resolve any disputes to the exclusion of international arbitration, and litigated that through the Indian court system, twice reaching the Indian Supreme Court. The state sought to enjoin arbitration in the courts. And the central government of India sought to enjoin arbitration on the enforcement of the guaranty it had provided.

Thus, it was clear in this case that Indian politicians and governmental authorities had not accepted that international arbitration was the appropriate way to settle this major dispute. Moreover, these events created doubts about the reliability of Indian government financial guarantees and increased the foreign investors' wariness about investing in India.¹⁵

But, it was not Indian politicians alone who rejected international arbitration as the appropriate way to settle a major dispute. The courts were complicit in the effort to prevent international arbitration. Both the Delhi High Court and the Bombay High Court granted injunctions precluding companies subject to their jurisdiction from pursuing international arbitration. It appears that Indian courts remained unwilling to cede jurisdiction to international arbitral tribunals situated outside of India. There is no evidence to suggest that the Indian courts were subject to political influence on the matter. However, it is clear that the Indian courts had not really come to accept that international arbitration was the appropriate—and contractually required—method of resolving the disputes in question.

In the future, this situation may of course change. In the power sector, in 2003, India enacted a new electricity act, consolidating previous electricity laws and decreasing the power of Indian states in the field; in 2005, India established a new electricity policy to encourage foreign investment.¹⁶ The 2003 law also created a new appellate tribunal to hear appeals from of the central and state electricity regulatory commission decisions.¹⁷

But the problem appears to be one that is broader than the electricity field. It implicates the attitudes of both Indian politicians and courts more generally. In 2005, the Indian authorities recognized that they could no longer prevent the resolution of the Dabhol dispute by arbitration and may have recognized that

15. See Kundra, *supra* note 7, at 930-31.

16. See *id.* at 933.

17. See *id.*

India's reputation was also at stake. In any event, they decided it was time to reach an overall settlement. It is impossible to conclude from this, however, that there has been a fundamental shift in attitudes of the Indian state authorities and courts. Thus, for the present, it would seem that reliance on Indian's New York Convention status, the 1996 Act, and the Indian courts would be misplaced. Rather, foreign entities that wish to invest and conduct business in India and do not wish to have disputes settled in the Indian court system will likely want, to the extent feasible, to structure their transactions to bring them under the coverage of a BIT (or other international agreement) that offers the possibility of off-shore arbitration against the government of India and is not subject to disruption by actions of local governmental authorities or the Indian courts.

