
(2018) 12 BOM CK 0156

In the Bombay High Court

Case No : Commercial Arbitration Petition No. 18 Of 2015, Notice Of Motion No. 2334 Of 2018, Arbitration Petition No. 1267 Of 2015

Reach Cargo (Movers) Pvt.Ltd. & Ors

APPELLANT

Vs

Global Asia Venture Company

RESPONDENT

Date of Decision : 11-12-2018

Acts Referred:

Arbitration and Conciliation Act, 1996 — Section 4, 4(b), 16, 16(5), 34
Indian Contract Act, 1872 — Section 23

Citation : (2018) 12 BOM CK 0156

Hon'ble Judges : S.C.Gupte, J

Bench : Single Bench

Advocate : Gaurav Joshi, Jyoti Sinha, Devangshu Nath, Khaitan, Sharan Jagtiani, Vyapak Desai, Siddharth Ratho, Nishikant Desai

Final Decision : Dismissed

Judgement

S.C.GUPTE, J.

1. Heard learned Counsel for the parties.

2. This arbitration petition (Commercial Arbitration Petition No.18 of 2015) challenges a majority award passed by an arbitral tribunal of three arbitrators. Disputes between the parties arise out of a share subscription and shareholders agreement.

3. Initially, by a term sheet dated 17 March 2007, the parties recorded terms for a proposed investment to be made by the Respondent, who is a 'foreign venture capitalist', in Petitioner No.1 company, an 'Indian venture capital undertaking' as defined under the applicable foreign investment policy. The term sheet provided for broad commercial terms of the transaction. It appears that keeping in view the proposed investment, the Respondent even proceeded to secure a certificate of registration as a 'Foreign Venture Capital Investor' from the Securities and Exchange Board of India ('SEBI'). On 18 September 2007, a proper agreement,

termed as a 'share subscription and shareholders agreement', was executed between the parties in pursuance of the term sheet. Under this agreement, the Respondent made an investment of USD 5 Million in Petitioner No.1 company against the issuance of 5,00,000 shares of the face value of Rs.10/- each. One of the main commercial terms of this investment was that in the event Petitioner Nos.2 to 4 herein, referred to in the agreement as 'promoters' or 'sponsors', were not able to make the first Petitioner company public within 24 months from the date of closing (as defined in the agreement), they would be under an obligation to ensure that the Respondent, referred to as the 'investor' in the agreement, exited at a minimum IRR of 25% or the fair value of the shares issued to it, as determined by an independent accounting firm to be appointed jointly by the parties, whichever was higher. The agreement also had a performance clause, which inter alia required the investor to be compensated by way of additional equity shares or cash from the sponsors in the event the company was unable to meet at least 85% of the target profit as provided in the business plan (defined in the agreement) within two years from the date of closing; this was to be based on a formula (as provided in an annexure to the agreement), which enabled the investor to earn an IRR of at least 25% of the investor's contribution. The agreement provided for a put option on the part of the Respondent for enforcement of its exit entitlement with an IRR of at least 25 per cent.

4. It is not in dispute that the stated performance was not achieved and that, as a result, the Respondent became entitled to exercise the put option provided for in the agreement. It is also not in dispute that the option was in fact exercised by the Respondent but was not fulfilled by the Petitioners and as a result, dues were owed by the latter to the former. What was in dispute, and what led to the present reference to the arbitral forum, was the conformity of the put option exercised by the Respondent with the Foreign Exchange Management Act ('FEMA') and the RBI Policy and Guidelines framed thereunder. It was submitted by the Petitioners before the arbitral tribunal that the Petitioners had written to RBI seeking a clarification in that behalf and that, in response, RBI had made it clear that the put option exercised by the Respondent, and return of its investment demanded by it with an IRR of 25%, was in contravention of law and could not be enforced. There was one more controversy which the arbitral tribunal had to decide and that pertained to the alleged termination of its mandate on account of overshooting or breaching of the time-line provided in the arbitration agreement for making of an award. The arbitral tribunal, by its majority award, held in favour of the Respondent on both counts. The majority held that it had the requisite mandate to declare its award and was not functus officio. (This order was passed by the tribunal in an application under Section 16 of the Arbitration and Conciliation Act, 1996, which preceded the making of the final award; under Sub-section (5) of Section 16, this part of the award has been challenged in the present arbitration petition.) The minority held that the tribunal had indeed become functus officio. The majority award, on merits, did not find

fault with the stipulation of return of investment with a fixed IRR of 25 per cent with reference to the law of FEMA and regulations framed thereunder. The minority, since it held the tribunal to be functus officio, did not go into the merits of the reference.

5. The impugned award is challenged by the Petitioners mainly on the ground that it is in breach of public policy of India, since, in contravention of clear provisions of law contained in FEMA and RBI guidelines framed thereunder, it recognises and enforces a contract which is contrary thereto. It is also submitted that the award exhibits an impossible view or a view which no fair or judiciously minded person could have taken. It is submitted that the arbitrators failed to take into account the agreement between the parties as also the applicable regulations relating to foreign investment in India and the response of RBI based thereon. It is also submitted that for the very reason, the award can be said to be vitiated by a patent illegality appearing on the face of the award.

6. The chief controversy before the arbitral tribunal concerned the nature of the investment involved in the present case and particularly, whether it was a Foreign Venture Capital Investment ('FVCI') or a Foreign Direct Investment ('FDI'). The relevant regulatory provisions of FEMA read with the regulations and guidelines framed thereunder reserve two separate routes for foreign investment in Indian undertakings and funds. One is the FDI route and the other the FVCI route. It is not in dispute that if the investment in the present case were to be treated as an investment through the FVCI route, there is nothing wrong with either the agreement between the parties providing for a fixed minimum IRR or the demand by the Respondent in exercise of its put option for return of investment at such IRR. It is equally clear that were it to be reckoned as an FDI, it would be an impermissible transaction and its enforcement could not have been ordered. The whole controversy, thus, turns on whether the investment was an FDI or an FVCI. The Petitioners claimed that it was the former, whilst the Respondent's case was that it was the latter. That is what the arbitrators were called upon to decide.

7. After construing the relevant clauses in the agreement and in particular, Clauses 11.5, 13 and 16.2 thereof, the arbitrators accepted the contention of the Respondent (original claimant) that the parties had clearly understood, having regard to the nature of the transaction, that it was the requirements of FVCI which were to be complied with and were in fact complied with in the present case. The arbitral tribunal inter alia considered the relevant regulatory provisions in this behalf and noted that the case of the Petitioners mainly turned on filing of what is known as "FC- GPR form" with RBI. Filing of this form, so to say, distinguishes an FVCI from an FDI, since it is only an investment through FVCI route which requires this form to be filed. The Petitioners' case that the investment contemplated under the agreement was an FDI was based on the fact that the agreement provided for filing of this form, and which was purportedly done in the present case. (Other than the provision for filing of such form to be

found in the agreement between the parties, there is nothing in the agreement or in any other document or circumstance of the case to suggest that the investment here was through the FDI route.) The arbitral tribunal noted that filing of the FC-GPR form was provided in the agreement by way of caution keeping in view the prevailing uncertainty around the time about the requirement of such form in case of an FVCI, whereas actual filing of the FC-GPR form in the present case was a unilateral act on the part of the Petitioners, and which was much after the disputes arose between the parties. The Petitioners' explanation in their evidence that this form was prepared contemporaneously when the investment was made, that is to say, in 2007, but was not filed then in the circumstances narrated in their evidence, was not accepted by the tribunal. The arbitrators found the Petitioners' endeavour to file the form under an old date to be a malafide exercise, aimed at supporting their case of the investment being through the FDI route. Even the response of RBI was considered by the arbitrators in the backdrop of the Petitioners' attempt to support its case in a surreptitious manner. The arbitrators noted that a distorted portrayal of the real transaction between the parties by the Petitioners was responsible for securing RBI's opinion in the matter. The sole witness of the Petitioners was extensively cross-examined in this behalf. After referring to the questions posed to the witness in the course of his cross-examination, the arbitrators held that the whole attempt of the witness, and through him of the Petitioners, was to dodge the return of the Respondent's investment. The explanation was held to be of no avail; in the arbitrators' opinion, filing of the relevant FC-GPR form was merely with a view to create evidence to show that the investment was through the FDI route so as to invite contravention of law and invalidity of the transaction based on such contravention. These are all clearly possible views which are supported by evidence. These are not views which can be termed as views, which no fair or judiciously minded person could have arrived at or views, which would shock the conscience of the court. The arbitrators have merely construed the agreement between the parties, considered the relevant regulations applicable to the transaction and taken into account the response of RBI in the light of the portrayal of the transaction by the Petitioners. Once the arbitrators are shown to have applied their mind to all this material placed before them, construed the agreement and appreciated the evidence led the parties, and the findings arrived at by the arbitrators are shown to be possible views, there is nothing further for the challenge court to consider under Section 34 of the Arbitration and Conciliation Act, 1996. The Supreme Court has made this amply clear in its judgment in *Associate Builders vs. Delhi Development Corporation* (2015) 3 SCC 49.

8. In the present case, it is clear firstly from the very agreement between the parties, which refers to FVCI registration of the Respondent and a fixed IRR payable to it as a foreign venture capitalist after stating the transaction to be foreign investment policy compliant that the investment contemplated was through the FVCI route. Even the correspondence placed on record before the

learned arbitrators, some of it by the Petitioners themselves, made it clear that contemporaneously with its proposal to invest in the Petitioner company, the Respondent had applied for SEBI registration as also RBI permission as an FVCI in keeping with the nature of the investment in the present case, namely, as an investment through the FVCI route. There are documents on record in the form of letters addressed by HSBC, who was the custodian of the subject shares, to the first Petitioner company itself and the latter's own response to such correspondence, which unequivocally support the Respondent's case. The first Petitioner company has acknowledged in this correspondence that the investment strategy involved a foreign venture capital investment (FVCI) and steps taken by the parties in compliance with the relevant regulatory requirements were towards such FVCI. It is clear from the correspondence that the investment was in unlisted equity shares of an Indian company, which was not within the negative list, that is to say, an Indian Venture Capital Undertaking, and such investment was made by a Foreign Venture Capital Investor. The Investor had the requisite registration with RBI, which was the only requirement under the applicable regulatory mechanism. The investment, in other words, was nothing but Foreign Venture Capital Investment (FVCI).

9. Nothing much can be made of the fact that the share subscription and shareholders agreement refers to "the conditions currently applicable under FDI Policy" as "have been satisfied"; and filing of form FC- GPR with the RBI within 30 days of issuance of the Investor shares. The foreign investment policy of India has been broadly known as 'FDI Policy'. The reference to applicable 'FDI Policy' in the agreement does not suggest that what was contemplated by the parties was the FDI route as against the FVCI route of investment; both FDI and FVCI routes come under the FDI policy of India. As for the reference to the FC-GPR form, it is on record that prior to June 2013, there was some confusion as to the requirement of filing of FC-GPR form by a Foreign Venture Capital Investor even for an FVCI investment. A clarification was issued thereon by the RBI in June 2013. The RBI circular of June 2013 explains that filing of FC-GPR form was necessary for a SEBI registered FVCI only when it acquired shares of an Indian company under the FDI scheme and not when it went by the FVCI route. (A Foreign Venture Capital Investor could invest both by FDI and FVCI routes.) It has been brought out by the Respondent in its evidence that the reference to the FC-GPR form in the agreement was only by way of abundant caution in the light of the then obtaining ambiguity. The RBI circular of June 2013 has been duly considered by the arbitrators in this context.

10. The majority award cannot, thus, be faulted under any of the grounds of challenge available under Section 34 of the Act.

11. Coming now to the objection to the jurisdiction of the arbitrators on the ground of expiry of their mandate, it is important to note that the parties actually went ahead with the arbitration reference even after the expiry of the period provided for making of an award. The invocation of the arbitration agreement

was as of 1 February 2010. The six months' period prescribed under the agreement for making of an award, thus, expired on 31 July 2010. The first or preliminary meeting before the arbitral tribunal itself was held on 11 October 2010; neither party raised any objection to the arbitrators entering upon the reference. The statement of claim and defence were, respectively, filed on 7 December 2010 and 31 January 2011. Further pleadings and documents were filed thereafter. A substantial part of the cross-examination of the Petitioners' witness was conducted thereafter, by which time one of the three arbitrators died and a substitute arbitrator was appointed in his place by the Petitioners. The Petitioners' witness was thereafter discharged from further cross-examination. All this happened on or before 8 April 2013. It was only thereafter, i.e. on or about 13 August 2013, that the Petitioners for the first time raised a ground of termination of the arbitrators' mandate on account of expiry of the period of six months originally reserved under the arbitration agreement for making of an award. The majority arbitrators rejected the objection and the reference continued with the Petitioners participating in it under protest. These facts unequivocally go to the show that there was a clear waiver on the part of the Petitioners herein of the alleged termination of the arbitrators' mandate. Section 4(b) of the Act provides for a deemed waiver of objections in a case where a party, despite knowing about non-compliance with any requirement under the arbitration agreement which is derogable, proceeds with the arbitration without stating his objections to such non-compliance without undue delay or, if a time limit is provided for stating such objection, within that period of time. That has clearly happened in the present case and there has been deemed waiver of the objection on the part of the Petitioners.

12. Learned Counsel for the Petitioners submits that at any rate, more than six months have passed even after the Petitioners raised an objection to the continuation of the reference. That is neither here nor there. It is not as if a fresh period of six months would start from the date when the objection is raised after waiving it initially. The submission has no support either in law or in the agreement between the parties. Alternatively, learned Counsel submits that the six months' period originally provided for could not have been waived, whether as a matter of fact or as a matter of law based on the deeming fiction of Section 4(b).

Learned Counsel submits that the agreement between the parties clearly provides (Clause 21.6 of the shareholders agreement) that the terms of the agreement could only be waived by a written instrument duly executed by or on behalf of each of the parties. There is no substance even in this submission. In the first place, it is doubtful whether clause 21.6 applies to the arbitration agreement, which, as the courts have time and again explained, stands as an independent and stand-alone contract separate from the underlying contract of which it is but a part. Secondly, and more importantly, the clause refers to a waiver by volition; it cannot possibly apply to a waiver by a fiction of law, namely, in this case, the effect of Section 4(b). Section 4, which provides for

wavier of right to object, is, by its very nature, a non-derogable provision. Grave anomalies may result, if the provision were to be construed as a derogable provision. It effectively rules on what should happen in case the parties proceed with the reference in the face of non-compliance with any derogable provision of Part I. This rule itself cannot be derogated from by the parties by their agreement. The rule exists as a matter of public policy, which is to encourage and facilitate alternative dispute resolution inter alia through arbitration. No party can contract out of such provision. Under Section 23 of the Contract Act, an agreement is void not only when it is forbidden by law but also when, if permitted, it would defeat the provisions of any law. The Privy Council decision in *Moti Chand vs. Ikram-ullah Khan* (1917) ILR 39 All 173 is a case in point. That was a case where provisions of Agra Tenancy Act preserved the right of occupancy of an ex-proprietor of a mahal to lands cultivated personally for twelve years in a case where his proprietary rights in the mahal or a portion of it were transferred otherwise than by gift or exchange between co-sharers in the mahal. This was so whether he wished the rights to be so preserved or not and notwithstanding any agreement to the contrary between him and the transferee. By a deed, the defendants, who were proprietors within the meaning of the Act, purported to sell to the Plaintiffs their zamindari property together with the land of which they were in cultivation for the statutory period of twelve years. The Privy Council held that the policy of the Act was not to be defeated by any ingenious devices, arrangements or agreements between a vendor and a vendee for the relinquishment by the vendor of his land which he had cultivated continuously for twelve years at the date of the transfer; for a reduction of purchase money on the vendor's failing or refusing to relinquish such lands; or for the vendor being liable to a suit for breach of contract on his failing or refusing to relinquish such lands. All such devices, arrangements, and agreements were in contravention of the policy of the Act and contrary to law and were illegal and void and could not be enforced by the vendee in any civil or revenue court.

13. In the premises, there is no merit in the challenge to the impugned award. The arbitration petition is, accordingly, dismissed. The Petitioners shall pay the costs of this arbitration petition quantified at rupees one lakh to the Respondent.

14. Learned Counsel for the Petitioners applies for stay for a limited period in terms of the interim order passed by this court on 18 April 2018. The petition having been comprehensively heard and decided against the Petitioners, there is no question of granting of any such stay. The application is rejected.

15. In view of the dismissal of the arbitration petition, Notice of Motion No. 2334/2018 does not survive and is dismissed.

16. The connected petition, i.e. Arbitration Petition No.1267 of 2015, which has been filed by the original Respondent, seeks interim reliefs pending the hearing of the main petition, i.e. Commercial Arbitration Petition No.18 of 2015. There has been an ad-interim order operating in this petition, restraining the original

Petitioner from alienating assets otherwise than in usual course of business against a corresponding stay of execution of the award impugned in the main petition. Now that the main petition has been decided in favour of the Respondent and stay of execution of the award has been refused even for a limited period, further reliefs will have to be sought by the original Respondent from the executing court. Commercial Arbitration Petition No.1267 of 2015 is disposed of accordingly.