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PUBLIC POLICY: THE DOUBLE EDGED SWORD IN ENFORCEMENT PROCEEDINGS

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ABSTRACT
The pre- dominant view taken by international jurists is that Article V (2) of the New York Convention refers to the concept of international public policy, the scope of which is narrower than domestic public policy. In other words, what is considered as public policy in domestic matters is different from public policy in international matters. In the context of enforcement of arbitral award, international public policy is increasingly referred to in legislations and court judgments. However, what constitutes international public policy is a matter to be decided by a national judge.

1. Introduction

***"Public Policy is an unruly horse, and when you get astride it you never know where it will carry you."*- Mr. Justice Burrough**

The pre- dominant view taken by international jurists is that Article V (2) of the New York Convention refers to the concept of international public policy, the scope of which is narrower than domestic public policy. In other words, what is considered as public policy in domestic matters, is different from public policy in international matters. In the context of enforcement of arbitral award, international public policy is increasingly referred to in legislations and court judgements. However, what constitutes international public policy is a matter to be decided by a national judge.

While the definition of international or transnational public policy is not necessarily the same as domestic public policy, the purpose of making such a distinction is always to narrow down the scope of the public policy which must be considered for assessing whether the enforcement of a foreign award is compatible or not.

The principal surrounding the violation of public policy have been differently expressed by courts depending on whether they are in civil law or common law jurisdictions. In the former, the definitions of public policy generally refer to the basic principles or values upon which the foundation of society rests, without precisely naming them. In common law jurisdictions, on the other hand, the definition often refers to more precisely identified, yet very broad, values, such as justice, fairness or morality.

In India, public policy has been given a much broader interpretation, and the enforcement of a foreign award may be refused by an Indian court on

the ground of public policy if such enforcement would be contrary to:

(a) Fundamental policy of Indian law; or

(b) The interests of India; or

(c) Justice or morality

Domestic public policy consists of principles of morality and justice that are reflected in the constitution or other legal sources of a country. On the other hand, international public policy is a reflection of the justice seeking sentiment of a society and is a collection of values of a country and their violation cannot be tolerated by the society even in international public policy in relation to enforcement cases. Usually, the fundamental or basic principles constituting public policy are those as existing in the country where enforcement is sought. This is explicitly stated in Article V (2) (b) of the New York Convention which refers to a situation where the recognition or enforcement of the award would be contrary to the public policy of "that country". Countries like France and Switzerland, differentiate between international and domestic public policy and consider international arbitral awards as part of international public policy.

The District Court of Columbia in recent proceedings between *Hardy Exploration & Production (India) Inc. ("**HEPI**") v. Government of India (Ministry of Petroleum and Natural Gas)*,[1] have witnessed fervent debates on enforcement of arbitral award and its far-reaching impact across jurisdictions.

2. Factual Background

Contractual relationship between the parties, HEPI and Union of India ("**UOI**") was governed through a production sharing contract ("**PSC**") entered in November, 1996 for the extraction, development and production of hydrocarbons in a geographic block in India ("**Block**").

Disputes arose between the parties, which were subsequently referred to arbitration pursuant to the clauses in PSC. The arbitration clause in the PSC recorded the venue of arbitration as Kuala Lumpur, unless otherwise agreed.[2] The arbitral tribunal rendered its final award in favour of HEPI, signed and delivered in Kuala Lumpur in February 2013 ("**Award**"), upholding that:

- Hydrocarbons discovered by HEPI was natural gas and not crude oil. HEPI was denied the contractual period prescribed under the PSC to determine the commerciality of the discovery;
- UOI's relinquishment of HEPI's rights to the Block was null and void. The parties were to be put in the position they stood prior to the termination of rights, granting HEPI three more years to ascertain the commerciality of the natural gas;
- UOI to pay interest on HEPI's investment of INR. 500 crore at the rate of 9% per year until the date of the award and 18% per year until the final payment after the award as damages.

3. Court Proceedings in India

A. Proceedings before the High Court of Delhi[3]

UOI filed an application for setting aside of the Award and HEPI filed application for enforcement before the Delhi High Court ("**Delhi HC**") in 2013. HEPI opposed the setting aside proceedings on two grounds:

- Award was a '*foreign award*', therefore an application for setting aside under Section 34 of Part-I of the Arbitration and Conciliation Act, 1996 ("**Act**") would not be maintainable; and
- Assuming the application was maintainable, it would not lie within the territorial jurisdiction of the Delhi HC.

The Delhi HC held:

- The PSC did not specifically mention the place or seat of arbitration; therefore, it was necessary to ascertain *the place of arbitration* to decide on the maintainability of the application.

- Relying on Article 31.3 of the Model Law,[4] as the award was pronounced and signed at Kuala Lumpur, the 'place' of making the award, was Kuala Lumpur.
- The arbitration agreement was entered prior to September 6, 2012. Relying on *Reliance Industries*,***[5]*** since seat of arbitration is outside India, Part I of the A&C Act will not apply and Section 34 application is not maintainable.

B. Proceedings before the Supreme Court of India [6]

- UOI appealed before the Supreme Court of India ("**Supreme Court**"). The Supreme Court referred the appeal to a larger bench before the Chief Justice of India to decide the law applicable to post arbitral award proceedings when the 'seat' is not expressly specified. The appeal is pending.

4. Proceedings before the United States District Court of Columbia

During the pendency of proceedings in India, HEPI approached the District of Columbia ("**US Court**") in January 2016 seeking confirmation of the arbitral award under the Federal Arbitration Act.

Based on objections raised by UOI, the issues before US Court were:

- Whether confirmation of Award seeking specific performance and interest would violate US public policy;
- In the alternative, if the Award is confirmed, whether the US Court should stay the enforcement of the Award in the US considering that the challenge and enforcement proceedings are pending in India.

5. Decision

A. Stay on Enforcement Proceedings in the US:

UOI sought a stay on the proceedings in the US, pending the challenge to the Award before Indian courts. UOI relied upon Article V and VI of the New York Convention [7] and the doctrine of *forum non conveniens* and international comity.

HEPI argued that conditions under Article VI of the New York Convention were not met as the Award was not challenged before the competent authority (Malaysian court).

It is well settled that a district court has the inherent authority to issue a stay but such authority should be used judiciously.[8] Even in circumstances where the Indian courts do have the jurisdiction to set aside the award, the US Court noted that a stay on confirmation should not be lightly granted, defeating the purpose of arbitration.

The US Court relied on the six criteria set out in *Europcar Italia, S.p.A v. Maiellano Tours, Inc.****[9]*** To ascertain if a stay should be granted.[10] Considering the factors laid down in *Europcar*, the US Court acknowledged that the proceedings before Indian courts have suffered inordinate delays. The US Court held that there is no clarity on timelines for completion of the setting aside and enforcement proceedings, considering it has been pending for more than five years. Therefore, the first two criteria laid down in *Europcar* do not favour a stay.

With respect to the third factor, UOI submitted that the Award will be subjected to higher scrutiny in India due to the existence of a broader scope of '*public policy*' as compared to the US. The US Court ruled that this factor favoured a stay, as Indian courts can evaluate if an arbitral award complies with Indian law even during enforcement proceedings, a power that US courts do not possess.

In the US, public policy is defined narrowly and the only ground for refusal for enforcement of arbitral awards is under Article V (2)(b) of the New York Convention. In the US, the defence is available when the arbitral award clearly tends to undermine the public interest, the public confidence in the administration of the law, or security for individual rights of personal liberty or of private

property,[11]whereas in India, public policy has a much wider umbrella.[12]

Further, considering UOI had contributed to the delays in the proceedings, the US Court noted that the fourth criterion did not favour a stay. The US Court keeping in mind the fifth and sixth criterion with respect to balancing hardship amongst parties, held that HEPI had already suffered severe hardships given the fact that the contract was breached nine years ago and the Award was rendered five years back. Any further delay would burden HEPI. Based on the above findings, the US Court concluded that a stay on the proceedings was not warranted.

B. Public Policy Concerns:

HEPI urged that two portions of the arbitral award should be confirmed, *i.e.*, specific performance allowing HEPI to re-enter the Block for a period of three years and UOI's payment of interest on HEPI's original investment.

6. Specific Performance

UOI argued that an order of specific performance should not be granted:

- Specific performance would be against the US public policy of respecting the sovereignty of foreign nations, including their right to be in possession and control of their own land and national resources.
- Specific performance of the Award would violate Indian law, which permits such specific performance only in limited circumstances.
- Confirming the arbitral award would be difficult to enforce and supervise and would go against international comity.

HEPI's arguments

- UOI has overstated the implication of the enforcement of Award on its sovereignty and the US hesitancy to hold foreign governments accountable when they harm private parties.
- UOI attempted to re-argue the merits of the case by raising grounds of public policy;
- Courts in the US have, in the past, enforced arbitral awards for specific performance and such extra-territorial performance does not violate public policy.

The US Court discussed the concepts of sovereignty, independence, and dignity of each foreign State[13] which includes respect for *territorial integrity*. Despite the Foreign Sovereign Immunities Act, 1976 ("**FSIA**") not granting immunity to states from US courts in case of confirmation of foreign arbitral awards,[14] nothing in the statute suggests that US Court's jurisdiction extends to awarding *extra-territorial specific performance* against a foreign State.

HEPI relied on *Chabad v. Russian Federation**[15]*** and *NML Capital v. Argentina*,[16] where US courts had granted specific performance against sovereign nations, though outside the scope of international arbitration. The US Court differentiated both cases and held that an order for enforcement in the present case had far more serious implications and would deprive a foreign nation of the ability to decide who will be able to extract and utilize its natural resources. Confirmation of the Award would encroach upon the territorial integrity of India, which is against the US public policy. The US Court held:

- Confirmation of the Award would be invasive in nature and that *forced interference with India's complete control over its territorial waters violate public policy.* Separately, the US Court disagreed that the enforcement was too complicated for it to oversee.
- While the US Court has jurisdiction over the case, ordering specific performance may not be in the spirit of the US policy preference against specific performance as is clear from the exclusion from the statutory text of the FSIA.
- Given that the US has not waived its sovereign immunity in its own courts against specific performance in contract cases, the US Court noted that it would be against US public policy to create a situation in which a foreign court

could order the US to specifically perform its portion of a contract.

C. Awarding Interest:

UOI submitted that awarding interests would be both coercive and punitive in nature and against the public policy of US. HEPI argued that interest was compensatory in nature. The US Court held that since the primary component of the award is not being enforced, *i.e*, return of the Block to HEPI, allowing payment of interests would in effect coerce a foreign state into complying with an order the US Court cannot issue. The payment of interest is inextricably linked to the specific performance of the Award, thus confirmation of the interest portion of the Award would also violate the US public policy. India may ultimately need to pay HEPI millions once the award attains finality, but only when a competent authority permits specific performance of the award.

7. Analysis

This judgment has dealt with certain critical concepts in the realm of international commercial arbitration. It raises a larger issue on the sanctity of arbitral awards and eventual enforcement in disputes involving States. The New York Convention, as well as Model Law[17], are silent on whether the defense of sovereign immunity can be raised by States during enforcement proceedings.

However, there is a school of thought which believes that the since sovereign immunity has not been listed as a specific ground of defense to recognition and enforcement, States have implicitly consented to not raising such a defense in international commercial arbitration.[18]

The United Nations Convention on Jurisdictional Immunities of States and their Property[19] draws the distinction with respect to commercial and non-commercial transactions entered by states. Therefore, if a State enters an arbitration agreement pursuant to a commercial transaction, immunity cannot be invoked at the stage of confirmation or setting aside of the award.[20]

The US Supreme Court has interpreted the phrase "*commercial*" in the context of S. 1611 of the FSIA (which discusses the commercial activity exception to sovereign immunity). Commercial functions rendered by the State are deemed to be non-sovereign. There is no provision on sovereign immunity under Indian arbitration regime and follows the distinction laid down by US.

It is interesting to note that the US Court did not even delve into whether the nature of the relationship between the parties or the ultimate specific performance was *commercial or non-commercial* in nature. The US Court held that the mere fact that granting specific performance would impact the natural resources of the country was sufficient to invoke the public policy defence and refuse confirmation of the Award.

While the ruling of the US Court is beneficial for UOI at this stage, given the delays in court processes in the Indian legal system, it is possible that UOI will be mandated to pay enormous sums to HEPI as interest at the colossal rate of 18% in the event of failure of challenge to the execution of arbitral award.

With this recent ruling, it remains to be seen how concepts of sovereignty, read into the defence of public policy, will be interpreted and impact it would have for future cases of enforcement of arbitral awards against States. Undoubtedly, interest of States will need to be balanced with commercial rights that accrue to private enterprises. It is hoped that with the passage of time, a balance will be struck between these two competing interests.

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[1] United States District for the District of Columbia, Civil Action No. 16-140 (RC)

[2] The UNCITRAL Model Law on International Commercial Arbitration, 1985.

"33.12. The venue of conciliation or arbitration proceedings pursuant to this Article unless

the parties otherwise agree, shall be Kuala Lumpur and shall be conducted in English language. Insofar as practicable the parties shall continue to implement the terms of this contract notwithstanding the initiation of arbitration proceedings and any pending claim or dispute."

[3] Union of India v. Hardy Exploration & Production (India) Inc. FAO (OS) 59/2016 and CM Nos. 7062-63/2016 and 7066/2016

[4] Article 31. Form and contents of award

(3) The award shall state its date and the place of arbitration as determined in accordance with article 20(1). The award shall be deemed to have been made at that place.

[5] Union of India v. Reliance Industries Limited, 2015 (10) SCC 213.

[6] Union of India v. Hardy Exploration and Production (India) Inc. Civil Appeal No. 4628 of 2018

[7] Article VI of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of June 10, 1958 ("**New York Convention**") states "if an application for the setting aside or suspension of the award has been made to a competent authority referred to in article V(1)(e), the authority before which the award is sought to be relied upon may, if it considers it proper, adjourn the decision on the enforcement of the award." Article V(1)(e) of the New York Convention states that a competent authority is one "of the country in which, or under the law of which, that award was made."

[8] Cf. Four Seasons Hotels & Resorts B.V. v. Consorcio Barr S.A. 377 F.3d 1164 and Hewlett-Packard Co. v. Berg 61 F. 3d 101, 106

[9] 156 F.3d 310, 317 (2d Cir. 1998).

[10] (1) the general objectives of arbitration—the expeditious resolution of disputes and the avoidance of protracted and expensive litigation; (2) the status of the foreign proceedings and the estimated time for those proceedings to be resolved; (3) whether the award sought to be enforced will receive greater scrutiny in the foreign proceedings under a less deferential standard of review; (4) the characteristics of the foreign proceedings including (i) whether they were brought to enforce an award (which would tend to weigh in favor of a stay) or to set the award aside (which would tend to weigh in favor of enforcement); (ii) whether they were initiated before the underlying enforcement proceeding so as to raise concerns of international comity; (iii) whether they were initiated by the party now seeking to enforce the award in federal court; and (iv) whether they were initiated under circumstances indicating an intent to hinder or delay resolution of the dispute; (5) A balance of possible hardships to the parties. .. and (6) Any other circumstance that could tend to shift the balance in favor of or against adjournment.

[11] Enron Nigeria Power Holding, Ltd. v. Fed. Republic of Nigeria, 844 F.3d 281, 289 (D.C. Cir. 2016).

[12] Section 48(2), Arbitration and Conciliation Act, 1996.In India, the enforcement of an arbitral award can be refused:

1. If the arbitral award is induced or affected by fraud or corruption or is in violation of the clauses on confidentiality and admissibility of evidence in other proceedings; ii. The arbitral award is in contravention of the fundamental policy of India; or (iii) is in conflict with the most basic notions of morality or justice. Further to be in confirmation with public policy in India, the criteria of compliance with Indian statutes and judicial precedents, reasonableness, adherence to judicial approach and compliance with natural justice needs to be met.

[13] Bolivarian Republic of Venezuela v. Helmerich & Payne Intern. Drilling Co., 137 S. Ct. 1312, 1319 (2017).

[14] Foreign Sovereign Immunities Act, 28 U.S.C. § 1605(a)(6).

[15] 915 F. Supp. 2d 148, 150–52 (D.D.C. 2013).

[16] 699 F.3d 246, 261–65 (2d Cir. 2012).

[17] The UNCITRAL Model Law on International Commercial Arbitration, 1985.

[18] Rajesh Sharma, *Enforcement of Arbitral Awards and Defence of Sovereignty: The Crouching Tiger and the Hidden Dragon*, Lapland Law Review, Vol. 1, No. 1, pp. 252-264.

[19] United Nations Convention on Jurisdictional Immunities of States and Their Property, 2004.

[20] Article 17, United Nations Convention on Jurisdictional Immunities of States and Their Property, 2004. While India has signed this Convention, it has not ratified it yet. The United States is not a signatory to this Convention.