



## Bombay High Court rejects objections to enforcement of foreign award and upholds legality of put option under SCRA AND FEMA<sup>1</sup>

### Brief Facts

On 12 September 2008, Banyan Tree Growth Capital LLC (“**Petitioner**”) and Respondent Nos. 2 and 3 entered into a Share Subscription Agreement (“**SSA**”) whereunder the Petitioner made an initial investment of USD 50 million in return for equity shares and convertible debentures in Axiom Cordages Ltd. (“**Respondent No. 1 Company**”). The parties also entered into a put option deed on the same date (“**Put Option Deed**”) whereunder Respondent Nos. 2 and 3 were required to buy the Petitioner’s shareholding in Respondent No. 1 (“**Put Securities**”) to secure its exit. However, upon the exercise of the put option right by the Petitioner in 2015, Respondent Nos. 2 & 3 refused to purchase the Put Securities and stated that the Put Option Deed was void *ab initio* under Indian law. The dispute was referred to arbitration at the Singapore International Arbitration Centre. The arbitral tribunal held the Put Option Deed to be a valid and legal contract under Indian law and awarded damages to the Petitioner based on the fair market value of the Put Securities, which remained uncontested by the Respondents (“**Award**”).

The Respondents opposed the petition for enforcement of the Award filed before the Bombay High Court (“**Court**”) and contended that the Award was against the public policy of India, and for the first time, raised an objection that the Put Option Deed was inadequately stamped.

### Issues:

**Issue (i):** Whether the Put Option Deed is inadequately stamped, resulting in the illegality of the contract?

**Issue (ii):** Whether the Put Option Deed is unenforceable under the Securities Contracts (Regulation) Act, 1956 (“**SCRA**”)?

**Issue (iii):** Whether the Put Option Deed is unenforceable under the Foreign Exchange Management Act, 1999 (“**FEMA**”)?

**Issue (iv):** Whether the Award is contrary to the fundamental policy of Indian law?

### Judgment

**Issue (i):** The Court observed that the Put Option Deed was accepted in evidence before the arbitral tribunal and such admission of the document precluded the Respondents from challenging the document subsequently for insufficient stamping under Section 35 of the Maharashtra Stamp Act, 1958. The Court also noted that the obligation of adequately stamping the Put Option Deed was upon the Respondents who, for a period of ten years, took the position that the Put Option Deed was adequately stamped. The Court held that the Respondents were estopped in law to challenge their own actions and conduct in contending that the document is not adequately stamped.

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While enforcing a foreign award under Sections 47 and 48 of the Arbitration & Conciliation Act, 1996 (“Act”), the Court is precluded from adjudicating any factual dispute. The Court noted that accepting the contentions of the Respondents, especially after the parties had admitted the document in the arbitral proceedings, would tantamount to reopening the trial on factual issues, which was beyond the jurisdiction of the Court.

**Issue (ii):** Relying on *Edelweiss Financial Services Ltd. v. Percept Finserve Pvt. Ltd.*,<sup>2</sup> the Court reiterated that a contract containing a put option cannot be termed as a contract in derivatives and held to be illegal under Section 18A of the SCRA. Since the option in favour of the Petitioner was a buyback arrangement, it could neither be dealt nor traded on the stock exchange, and would not attract the SCRA.

In any case, the Court also held that the contract for the sale or purchase of securities came into existence in 2015 only after the Petitioner exercised its option under the Put Option Deed.<sup>3</sup> The Court recognised that the Put Option Deed was governed by the SEBI notification dated 3 October 2013 (“SEBI Notification”), which provided statutory recognition to shareholders contracts for purchase or sale of securities, with a put option, even if entered prior to the issuance of the SEBI Notification. Therefore, the Put Option Deed was permissible under the SCRA.

**Issue (iii):** The Respondents contended that the Put Option Deed was in contravention of the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000 (“FEMA Regulations”), and in particular, in contravention of Regulation 5(1), which permitted optionality clauses only from 2013 onwards and Regulation 10, which mandated valuation of unlisted shares as per the fair market value. The Court held that the Put Option Deed could only be exercised under certain conditions and did not guarantee assured returns to the Petitioner. The Put Option Deed provided that if the put option price exceeded the FMV valuation, the excess amount was not to be remitted to the Petitioner, but

was to be repatriated to a nominee’s account in India, which is not prohibited under the FEMA Regulations.<sup>4</sup>

The Court relied on *Vijay Karia v. Prysmian Cavi E Sistemi SRL & Ors.*<sup>5</sup> and held that enforcement of the Award cannot be refused on the ground of violation of the FEMA Regulations. This is because the provisions of the FEMA and the regulations thereunder do not deal with the legality of contracts and are concerned only with the manner in which contracts are to be performed with respect to foreign exchange.

**Issue (iv):** The Court relied on the decision in *Shri Lal Mahal Ltd. v. Progetto Grano SPA*<sup>6</sup> to interpret ‘public policy’ and its applicability in enforcement of a foreign award, as well as the rationale espoused in *Vijay Karia (supra)* to reject a challenge to an award argued to be contrary to the FEMA. In light of upholding the legality of the Put Option Deed under the FEMA, the SCRA and the regulations and notifications thereunder, the Court held that the grounds raised to challenge enforcement of the Award did not fall within the ambit of fundamental policy of Indian law. Resultantly, the Award was held to be in consonance with the public policy of India.

## Analysis

The present case is an addition to the precedents set by Indian courts recognising the concept of put options, which is one of the most prevalent exit mechanisms for foreign investors. Courts have granted interim reliefs in disputes involving exercise of put options and not interfered with awards granting reliefs based on put options.

On the issue of inadequate stamping, the Court interestingly distinguished the position laid down by the Supreme Court that an arbitration clause contained in an agreement, which is inadequately stamped, cannot be acted upon, by differentiating the jurisdictions of the court under Section 11 and Sections 47-48 of the Act.

The concept of fundamental policy of Indian law has been interpreted to mean compliance of statutes and judicial precedence, need for

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judicial approach, natural justice compliance and standards of reasonableness. Even if the law laid down in **SMS Tea Estates Pvt. Ltd. v. Chandmari Tea Co. Pvt. Ltd.**<sup>7</sup> and **Garware Wall Ropes Ltd. v. Coastal Marine Constructions and Engineering Ltd.**<sup>8</sup> is made applicable to the present case, it would still

be difficult to refuse enforcement of the foreign award on the ground of inadequate stamping, as the said ground is technical in nature, which can be easily cured and rectified. Therefore, such ground will not fall under the scope of fundamental policy of Indian law.

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1 Authored by Nitesh Jain, Partner and Shambhavi Pandey, Associate; *Banyan Tree Growth Capital LLC v. Axiom Cordages Ltd.*, Commercial Arbitration Petition No. 476/2019, Bombay High Court, judgment dated 30 April 2020.

**Coram:** G.S. Kulkarni, J.

2 2019 SCC OnLine Bom 732.

3 *MCX Stock Exchange Ltd v. Securities & Exchange Board of India & Ors.*, 2012 SCC OnLine Bom 397.

4 *IDBI Trusteeship Services Ltd. v. Hubtown Ltd.*, 2018 SCC OnLine SC 2795.

5 2020 SCC OnLine SC 177.

6 (2014) 2 SCC 433.

7 (2011) 14 SCC 66.

8 (2019) 9 SCC 209.

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