INSIGHTS

SYNERGIA FOUNDATION

MAY 2021 | EDITION V | WEEKLY

TAXING THE PAST

LESSONS FOR THE ROAD AHEAD

EXPERT INSIGHTS

Mary Kavita Dominic
Policy Research Associate, Synergia Foundation

Arijit Prasad
Senior Advocate at the Supreme Court of India

Dr Crina Baltag
Senior Lecturer in International Arbitration at Stockholm University

Kiran Nasir Gore
Counsel in the Law Offices of Charles H. Camp, Washington

Steven Finizio
Partner at WilmerHale London

Shwetha Bidhuri
South Asia head at the Singapore International Arbitration Centre

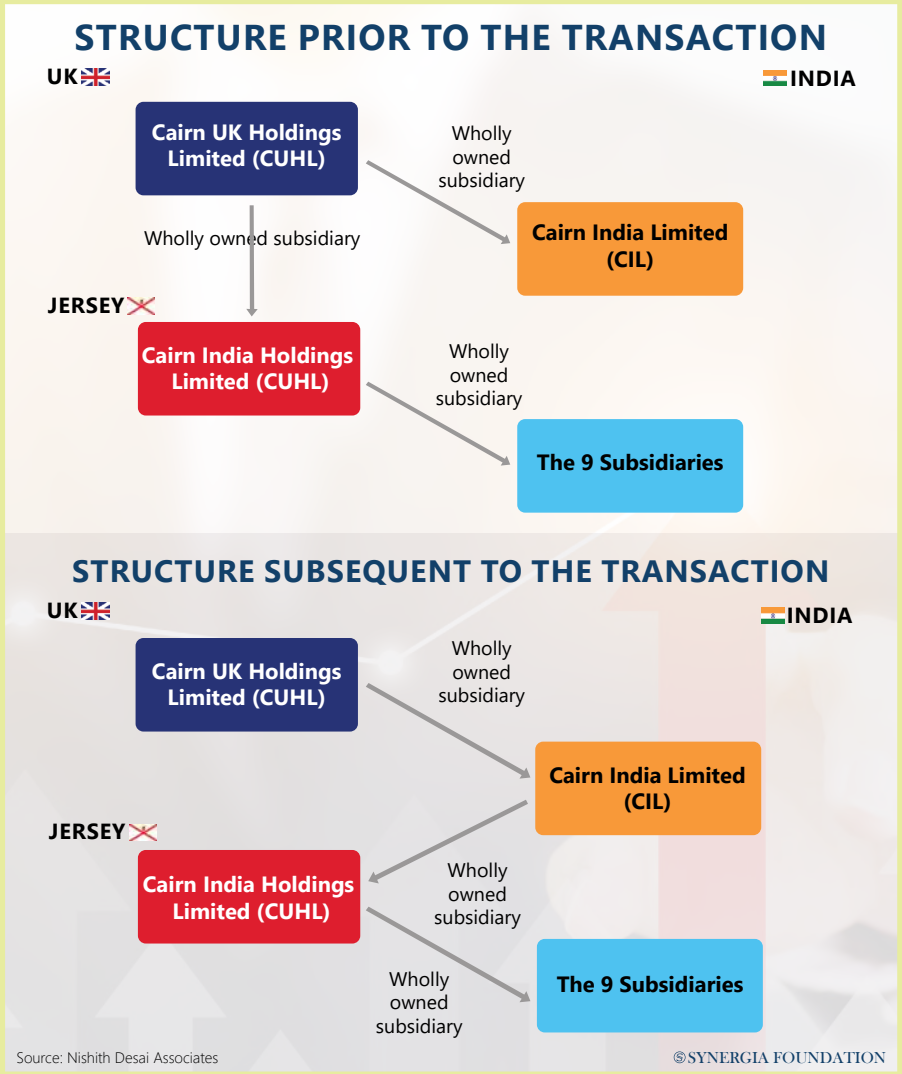
Ajar Rab
Rab & Rab Associates LLP

SYNERGIA FOUNDATION

THE INVESTMENT-TAX BINARY

The Cairn and Vodafone cases have opened a pandora's box of tax-related investment disputes that lie at the intersection of international laws and municipal governance

Mary Kavita Dominic, is a Policy Research Associate with the Synergia Foundation. She has completed her masters in law (BCL) and South Asian Studies (MSc.) from the University of Oxford.



Following a significant setback in the case of Cairn Energy Plc and Cairn UK Holdings Limited versus the Republic of India, the Indian government has challenged its arbitration penalty at the Hague Court of Appeal. According to the Union Finance Ministry, the $1.2 billion award is liable to be set aside, as the country had never agreed to arbitrate a national tax dispute.

This development comes at a time when Cairn Energy has identified around $70 billion of overseas Indian assets for potential seizure and enforcement of the arbitral award. In fact, the company has already moved a court in the United States to sue India's national carrier 'Air India' and recover part of the damages awarded to it. It remains to be seen whether the two sides can reach an amicable settlement before relevant foreign jurisdictions decide on the matter of enforcement.

THE RETROSPECTIVE DEBATE

At the heart of this arbitration dispute lies a 2012 legislative amendment to the Indian Income Tax Act, 1961, which effectively permits tax authorities to investigate transactions from 2006 for the evasion of capital gains tax. By virtue of this amendment, any transfer of shares between entities registered or incorporated outside India could be deemed taxable if the same derives value from underlying assets in the country.

This retrospective provision was enacted by the Indian Parliament to reverse the effects of a Supreme Court decision in the Vodafone tax dispute. As evident from the facts of that case, the Indian government had sought to raise a demand of Rs 7,990 crore in capital gains, owing to Vodafone's purchase of 67 per cent stake in Hutchison Whampoa. According to the taxman, Vodafone ought to have deducted the tax at source before making a payment to Hutchison, as the transaction had involved assets based in India. This argument, however, was categorically rejected by the Apex Court.

To circumvent this judicial verdict, an amendment was brought in through the Finance Act, which conferred power on the Income Tax Department to retrospectively tax such deals. However, the retroactive application of this provision to Vodafone was deemed to be a violation of the guarantee of fair and equitable treatment, as enshrined under the India-Netherlands Bilateral Investment Treaty (BIT), by an arbitration tribunal at Hague.

The same amendment has now stirred controversy in the Cairn dispute. Under scrutiny is a 2006 internal restructuring of the company,

through which Cairn UK Holdings Limited transferred its Indian assets to a wholly-owned subsidiary incorporated in India, namely Cairn India Limited. According to the tax authority, this transaction is subject to a capital gains tax under the 2012 retrospective amendment.

Cairn, however, has argued that this levy constitutes a 'manifest breach' of the UK-India BIT. This position has also been upheld by the arbitration tribunal at Hague, which views the imposition of ex post facto laws as violative of international principles like 'legal certainty' and 'fair and equitable treatment'. As a result, India has been ordered to pay $1.2 billion in damages, apart from other legal costs.

COMPETING INTERESTS

Implicit in the Vodafone and Cairn cases are larger questions pertaining to base erosion and profit shifting (BEPS). While countries like India argue that corporates evade taxes by transferring shares through shell corporations and complex webs of subsidiaries, others contend that these transactions amount to nothing more than prudent tax planning. In other words, there is an apparent clash between the sovereign's right to tax and the companies' right to use tax-saving devices.

With studies suggesting that governments lose 4-10 per cent of their revenue to BEPS practices, governments around the world are keen to reform their tax structures. For example, the Biden administration has recently pushed for a global minimum corporate tax that prevents the shifting of profits to low tax jurisdictions.

In altering such laws, however, the interests of foreign investors have been critically implicated. If the country that seeks to revise its tax regulations has signed an investment protection pact with the investor's home country, then there may be sufficient grounds for alleging a breach of treaty protection. When combined with retrospective measures, as seen in the case of India, investors can potentially claim that their legitimate expectations about a stable regulatory environment were impinged upon. This is precisely the line of argument that was adopted in the Vodafone and Cairn arbitration cases.

Against this backdrop, the utility of stability clauses that seek to maintain the status quo in investment protection agreements have been vigorously debated in policy circles.

ARBITRABILITY OF TAX

In investment disputes, the arbitrability of tax matters has proven to be legally contentious. Given their potential overlap with international tax treaties as well as domestic statutes of host countries, there are several questions that need to be addressed. In the absence of explicit 'conflict avoidance' clauses between tax treaties and investment protection agreements, it is important to determine the regime that prevails. Similarly, states must decide whether the exhaustion of local statutory remedies is essential before tax disputes are arbitrated under investment pacts.

As far as India is concerned, it has unilaterally revoked its previous BITs and propounded a new model in 2015 that excludes all tax matters from investment arbitrations. Meanwhile, other states have carved out specific aspects of taxation that can be arbitrated under an international investment agreement. The language of these treaty instruments will, therefore, be key over the coming years.

ENFORCEMENT DILEMMA

Even if the first hurdle of arbitrating tax matters can be overcome, the enforcement of investment arbitral awards in India remains a sticking point. The country is not a party to the International Convention on Settlement of Investor Disputes (ICSID), which provides facilities for conciliation and arbitration of investment disputes between contracting states and nationals of other member-nations.

Therefore, it is not bound to recognise and enforce the pecuniary obligations that accompany an investment award.

Although India is a signatory to the New York Convention, it has availed itself of the reservation clause under Article I (3), which exempts disputes pertaining to non-commercial relationships. The domestic Arbitration and Conciliation Act, 1996 (Arbitration Act) has further entrenched this position, raising critical questions about the enforcement of investment arbitral awards.

If investment treaties are indeed deemed to be commercial in nature, then the Arbitration Act can seamlessly pave the way for enforcement. However, the Calcutta and Delhi High courts have adopted conflicting positions about the applicability of this statute to investment relationships. Unless this vital issue is resolved by a judgement of the Supreme Court, the enforceability of investment arbitral awards in India will continue to remain uncertain.

Alternately, the Parliament can introduce an amendment that clarifies the scope of the Arbitration Act.

DE-ESCALATING TENSIONS

As India suffers a spate of losses in international arbitral tribunals, there are concerns that its protectionist image may hamper further investments. By declining to enforce the award, the country has joined the likes of Pakistan and Venezuela, which have faced similar actions in foreign jurisdictions against their overseas assets.

Unless a robust framework is put in place for deescalating investor-state disputes, the South Asian giant's ambitious plans to conclude free trade and investment agreements with jurisdictions like the European Union may come to nought.

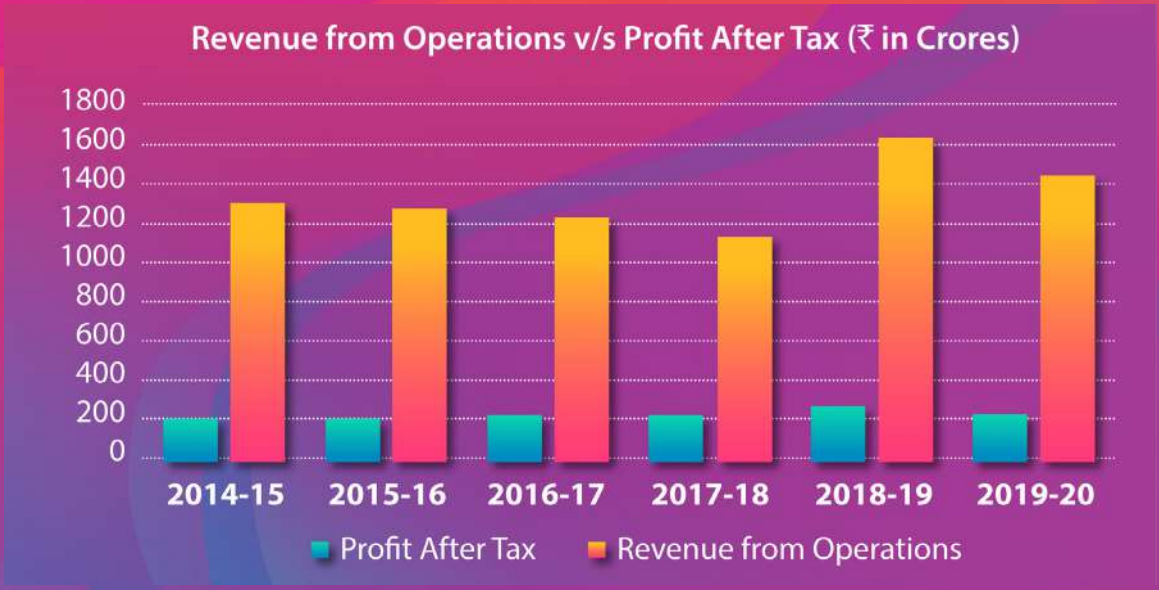
CORRECTION

• The May IV Insights edition, which featured an article on the Israel-Palestine conflict, had misstated the number of Israeli casualties. The correct number is 12, which includes two children.

ANTRIX CORPORATION LIMITED

Incorporated on 28th September, 1992 under the Companies Act 1956, Antrix Corporation Limited is a wholly owned Government of India company under the administrative control of the Department of Space. The mandate of the company has been to market the products and services emanating from the Indian Space Program. Antrix has remained profitable every year right from its inception. Antrix was awarded Miniratna-Category 1 status in 2008.

Access to a wide spectrum of Indian industries, a proven track record of delivering turnkey space solutions and a strong technical backing collectively have helped Antrix carve a unique industry positioning and shall also serve as bedrocks and beacon lights for the company to continually strive towards realizing its vision of maximizing the potential of Indian Space Technology by creating a robust space ecosystem in India and emerge as a globally significant space company.



INSIGHTS
SYNERGIA FOUNDATION

A 'LOOK THROUGH' PROVISION

By retrospectively amending the Income Tax Act in 2012, the Indian Parliament sought to clarify its legislative intention

Arijit Prasad, is a Senior Advocate at the Supreme Court of India, with extensive experience in corporate tax and commercial arbitration. This article is based on his views at the 102 nd Synergia Forum on 'Retrospective Tax Law and India's Global Road Ahead'.

LONG AND TAXING

- **May 2007:** Vodafone buys Hutchison Whampoa's controlling stake in Hutchison Essar for $10.9 billion
- **Sept 2007:** The I-T Department serves a notice to Vodafone International Holdings BV, citing alleged failure to deduct withholding tax from Hutchison Telecommunications International Ltd. The Uk firm later moves Bombay High Court
- **Sept 2010:** The Bombay High Court rules in favour of the I-T Department, stating it has jurisdiction over the deal. Vodafone challenges the ruling in the Supreme Court
- **Jan 2012:** The Supreme Court rules in favour of Vodafone, saying the transaction is not taxable in India and hence the company is not responsible for deduction of withholding tax
- **April 2012:** George Osborne, UK's Chancellor of the Exchequer, raises the issue with then Finance Minister, Pranab Mukherjee
- **April 2014:** Vodafone Group moves the Permanent Court of Arbitration in The Hague
- **Sept 25, 2020:** The arbitration tribunal rules in favour of Vodafone in ₹20,000-crore tax case

Source: DrishtiIAS

The root of the debate on retrospective tax and international investment law can be traced to the Vodafone case, which was decided by the Indian Supreme Court in 2011. This case pertained to a transaction between two non-resident companies, which was subsequently sought to be taxed by the Indian government. Vodafone had acquired shares in a company in the Cayman Islands, which was essentially a paper enterprise without business operations. On acquiring that upstream company, downstream companies which had their asset base in India were automatically transferred to Vodafone. Against this backdrop, the question that emerged was whether this particular transaction could give rise to capital gains tax in India under section 9 of the Income Tax Act, 1961. After all, its value derived from underlying assets in the country, represented by the Hutchinson company's operations in the telecom sector.

CONFLICTING POSITIONS

Vodafone argued that the relevant shares were located in a Cayman Islands company, and therefore if any tax had arisen, it was liable to be levied in this British overseas territory. Meanwhile, the Indian Revenue Department pointed out that the structure in the Cayman Islands had been created for the sole purpose of dodging tax. There was a very fine line between tax avoidance and tax evasion, with the latter being strictly prohibited by the law. Given that capital assets in India had been transferred and payment made to a non-resident entity, Vodafone was required to deduct tax at its source.

Clearly, therefore, there were diverging interpretations about the import of section 9. While Vodafone believed that taxes had to be levied in accordance with the structure of the transaction, the government reasoned that the veil of the corporate structure had to be pierced in order to ascertain the substance of that transaction. In other words, the two sides disagreed whether section 9 was a 'look at' stipulation or a 'look through' provision.

APEX COURT VERDICT

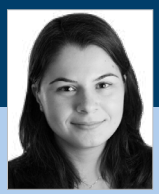
Ultimately, this case was brought before the Indian Supreme Court, which had to assess various legal doctrines to arrive at a decision. The Westminster principle that entitles every taxpayer to arrange his affairs within the limits of the law was particularly noted during the course of the proceedings. The Ramsay principle was also touched upon, given that it allows transactions to be taxed if they have pre-arranged artificial steps that serve no commercial purpose other than the saving of tax. Even the McDowell case (CTO v. McDowell and Co. Ltd.), which upholds the right of companies to maintain a tax-efficient system within the framework of the law, was referred to. Eventually, after hearing the case for around 32 days, the Apex Court upheld the interpretation by Vodafone.

EX POST FACTO LAW

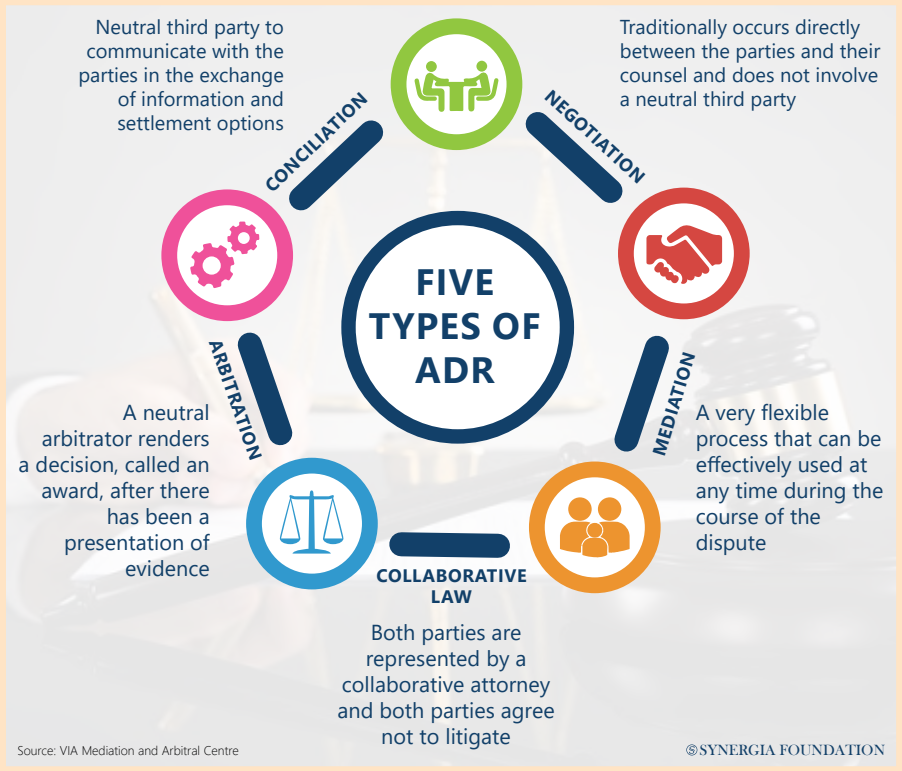
Circumventing this judgement, however, an amendment was brought in through the Finance Act by the Indian Parliament, which conferred the Income Tax Authority with the power to retrospectively tax such deals. It is pertinent to note that there are several judgements passed by the Supreme Court that uphold this sovereign right to amend tax laws, including Rai Ramkrishna and Others v. The State of Bihar (1963 AIR 1667) as well as Calcutta Division v. National Tobacco Ltd. (1972 AIR 2563). In the instant case, however, it is vital to understand that the amendment to section 9 was essentially clarificatory in nature. Instead of imposing a new tax, the legislature sought to confirm that the provision always had a 'look through' approach built into it.

RECONCILING FRAGMENTED LAWS

The nature of the interaction between taxation regimes and investment agreements have evolved over time, with new generation treaties envisaging specific carve-outs for tax



Dr Crina Baltag, is a Senior Lecturer in International Arbitration at Stockholm University and qualified attorney-at-law since 2004. This article is based on her views at the 102nd Synergia Forum on 'Retrospective Tax Law and India's Global Road Ahead'.



In public international law, the right of a state to regulate taxes is undisputed. What is contested, however, is the manner in which it seeks to do so. In the Cairn and Vodafone cases, for instance, the matter under scrutiny was the way in which the Indian government implemented amendments to section 9 of the Income Tax Act. According to the arbitration tribunals in each of the two cases, the enforcement of a capital gains tax with retrospective effect had contravened the guarantee of 'Fair and Equitable Treatment' (FET), as enshrined in India's Bilateral Investment Treaties (BITs) with the United Kingdom and the Netherlands.

Implicit in this issue are larger questions about the relationship between domestic law, taxation treaties and international investment agreements. The underlying complexities of these applicable regimes and their mutual interaction pose a dilemma for host states and foreign investors.

EVOLVING TREATY REGIMES

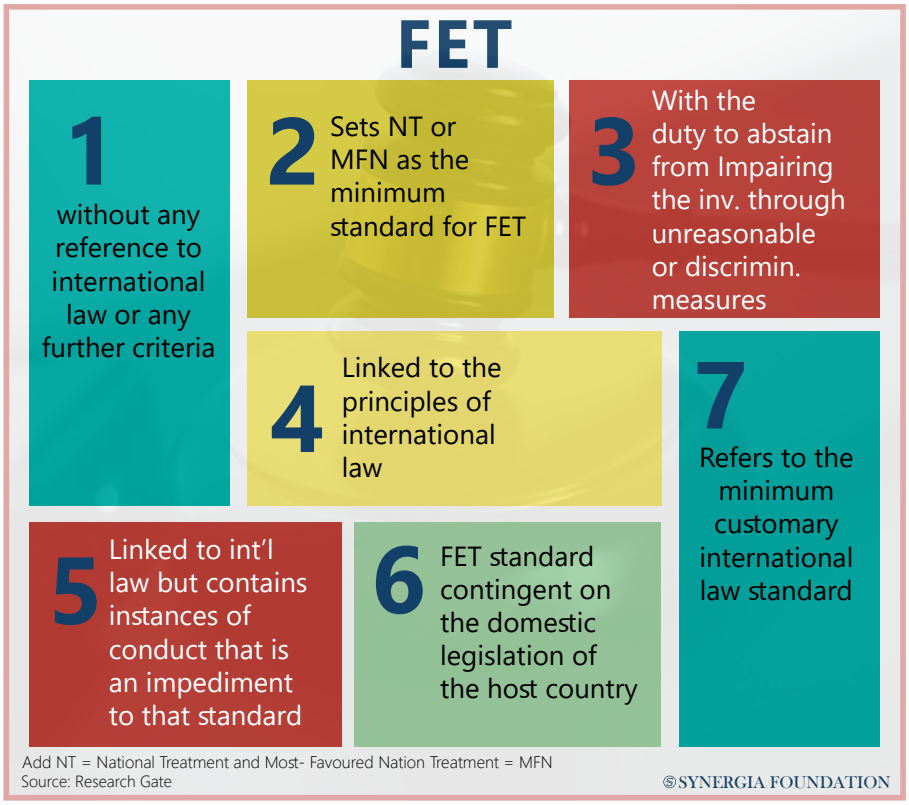
As far as international investment agreements are concerned, there are discernible differences between old generation and new generation treaties. Depending on where one sits in time, the approach to taxation measures may be distinct under these regimes. For example, old generation treaties do not generally exclude tax disputes from their ambit. They also rarely address the interaction between double taxation treaties (DTT) and investment treaties in the event of a discrepancy between the two. Finally, the relevance of any prerequisite criteria for accessing the DTT or an investment treaty in local administrative courts and authorities remains unclear.

Meanwhile, some of the newer investment pacts have a tendency to overregulate. They not only specify the relationship between tax treaties and investment treaties but also have explicit carve-outs that elucidate the taxation measures covered within their scope. For instance, the Canadian model BIT has a long provision on taxation measures as well as an obligation to approach local tax authorities for a certain period of time.

With the exception of these latest agreements, however, most investment treaties have failed to define 'taxation measures'. It is unclear whether they relate to the actual imposition of taxes or the interpretation of laws concerning taxes. Attaining definitional clarity on this front is the first step towards fixing the jurisdictional limits of an investment tribunal.

ARBITRABILITY OF TAXES

The Organisation for Economic Cooperation and Development (OECD) and the International Chamber of Commerce (ICC) have made significant contributions to



the debate on the arbitrability of tax matters. Following several studies and reports published by them, the OECD Model Tax Convention has recommended arbitration as the preferred mechanism for dispute resolution.

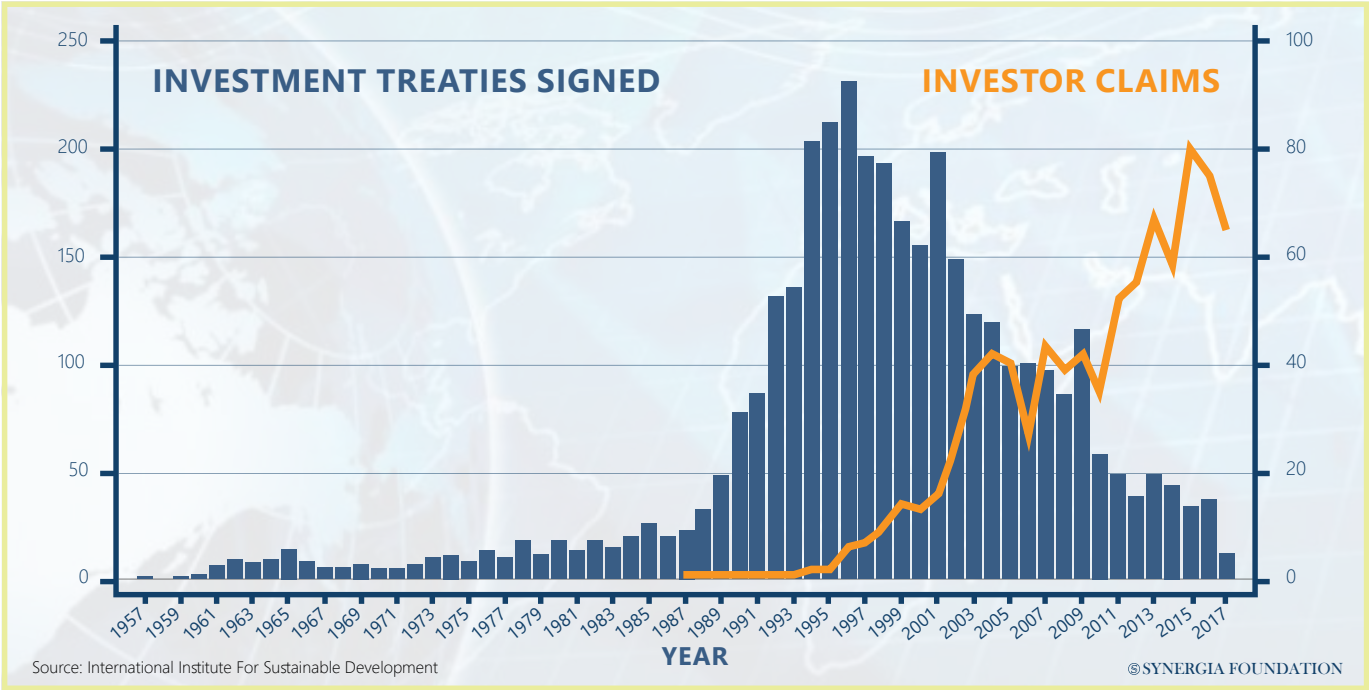
With respect to investment regimes, the arbitrability of tax disputes is also predicated on the specific carve-outs within the treaty. The definition of 'investments' and 'investors' are equally critical. In the specific cases of Vodafone and Cairn, for example, the arbitrability of retrospective tax law will depend on the portfolio of shares covered within the definition of investment. In other words, the language of the instrument will be key in determining the types of disputes that are arbitrable in the investment tribunal.

CONDUCT OF STATES

In tax-related investment disputes, it is important to situate the investor within different frameworks of state behaviour. In this regard, there are two kinds of cases that need to be distinguished. The first type relates to cases where existing tax laws are imposed by administrative authorities without any modification. Yukos Shareholders v. Russia is a prominent example. The second type includes cases where retrospective taxes are levied, with implications for principles like stabilisation, legitimate expectations, and transparency. The Cairn and Vodafone disputes fall within this category.

The FET standard is critical in assessing the conduct of states. It probes whether the implementation of a tax measure is unreasonable, arbitrary, abusive, discriminatory or a violation of due process. Although this principle is constantly evolving, it primarily interrogates whether the legitimate expectations of an investor have been met by the host state.

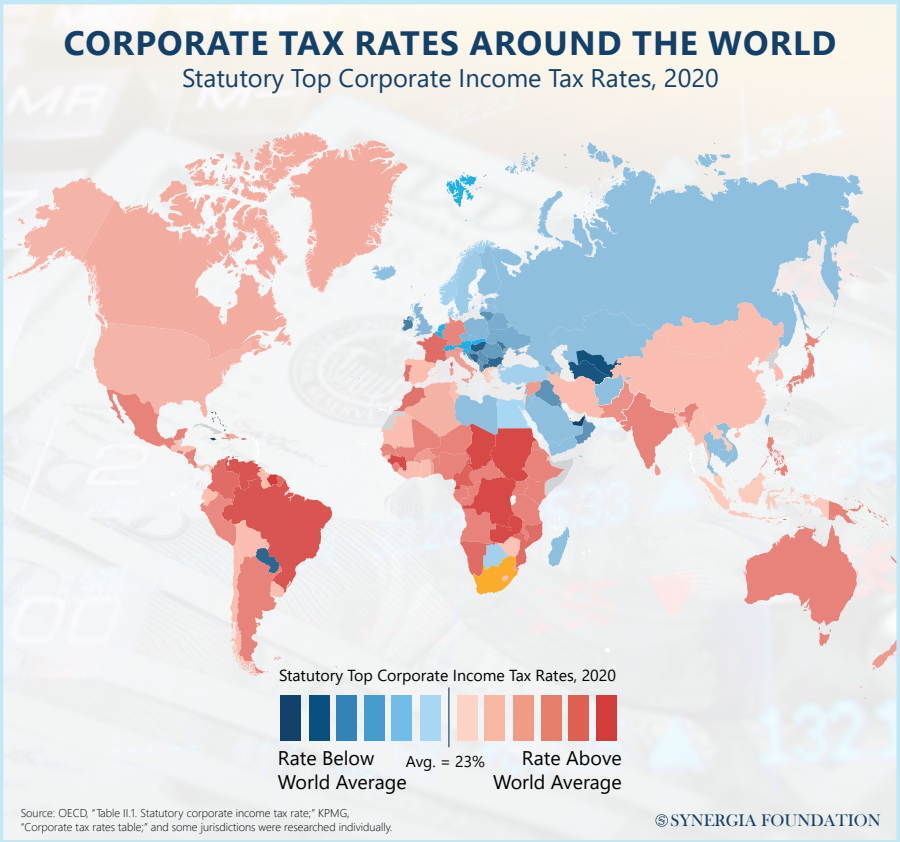
Other substantive standards of treatment like the expropriation principle or 'most favoured nation' status can also come into play, as has been seen in numerous cases pertaining to the non-payment of Value-Added Tax (VAT) refunds, withholding of tax etc. Ultimately, therefore, the manner in which the state imposes tax obligations on its investors will be the object of inquiry in investment arbitrations.



A BALANCING ACT

It is critical to maintain an equilibrium between the regulatory powers of a sovereign and the legitimate interests of a foreign investor

Kiran Nasir Gore, is a Counsel in the Law Offices of Charles H. Camp, Washington, with expertise in public and private international law, foreign investment strategies, and international dispute resolution. This article is based on her views at the 102nd Synergia Forum on 'Retrospective Tax Law and India's Global Road Ahead'



Taxation must be viewed in the experiential reality or practicality of how multi-national corporations and foreign investors operate. More often than not, they are looking for favourable tax scenarios by incorporating pass-through entities or paper companies. Indeed, this is the nature of international business today, and nefarious intentions do not necessarily accompany it.

For example, there are some states in the United States which are more predisposed to taxation on corporate affairs, as opposed to others. Bearing this in mind, many companies have structured their corporate existence in more advantageous jurisdictions.

SOVEREIGN CHALLENGES

Studies by the Organisation for Economic Co-operation and Development (OECD) have demonstrated that states lose almost 4-10 per cent of their global corporate income tax on an annual basis, owing to corporate restructuring practices. Given that billions of dollars are at stake, most governments are keen to regulate and exercise their sovereign right to tax. This is, however, riddled with several practical challenges, which was most recently observed in the case of ConocoPhillips and Perenco v. Vietnam. The facts were very similar to the Vodafone dispute in India, whereby ConocoPhillips had sold its U.S.-based subsidiaries in Vietnam to an entity in the United Kingdom. Given that the names of the subsidiaries were changed, and the entire transaction was carried out in the U.K., it was unclear whether Vietnam had the right to levy a capital gains tax. Clearly, it is not easy for governments to investigate transactions, identify taxable income and value the transfer of shares in such corporate restructuring case. It is no surprise, therefore, that tax matters have been implicated in the corpus of many investor-state disputes.

COMPETING INTERESTS

Ultimately, it is important to strike a balance between the competing interests of host states and foreign investors. Many of the new generation Bilateral Investment Treaties (BIT) have taken that into account by clearly defining the taxation measures that are included within their ambit. The Canadian model BIT is a case in point. Similarly, the United States-Mexico-Canada Agreement (USMCA), which has replaced the North American Free Trade Agreement (NAFTA), has permitted member-states to issue binding clarificatory documents about the interpretation of their treaties. With a heavy inflow of Foreign Direct Investments (FDI), the nexus between tax law and investment agreements will become more apparent over the coming days.

Against this backdrop, the international sphere is likely to witness a more sophisticated generation of investment treaties that lay down global best practices on conflict avoidance and dispute resolution.

LANGUAGE IS THE KEY

While determining the arbitrability of tax disputes under investment protection laws, the devil lies in the details of the treaty instrument

Steven Finizio, is a Partner at WilmerHale London, with experience in general commercial litigation, international arbitration, and alternative dispute resolution. This article is based on his views at the 102 nd Synergia Forum on 'Retrospective Tax Law and India's Global Road Ahead'.

KEY DISPUTES INVOLVING INDIA

Foreign Investor	*Date Of Dispute Notice*	*Indian Company concerned, If any*	*Applicable BIPA*
White Industries Australia	Jul 27, '10	Coal India Limited	India-Australia
(i) CC/Devas (Mauritius), (ii) Devas Employee Mauritius, (iii) Telecom Devas (Mauritius)	Dec 13, '11	Antrix Corporation	India-Mauritius
Deutsche Telecom	May 15, '12	Antrix Corporation	India-Germany
Vodafone International Holdings	Apr 17, '12	Vodafone India	India-The Netherlands
Sistema Joint Stock Financial Corporation	Feb 28, '12	Sistema Shyam Teleservices (SSTL)	India-Russia
M/s Khaitan Holdings (Capital Global, Mauritius & Kaif investment, Mauritius, original claimants)	Apr 16, '12	Loop Telecom	India-Mauritius
(i) Axiata Investment I & Axiata Investment 2, Mauritius (ii) Axiata Berhad Group	Jun 6, '12 Jul 5, '12	Idea Cellular Idea Cellular	India-Mauritius India-Malaysia
Children's Investment Fund Management (UK) & ICI Cyprus Holdings	May 16, '12	Coal India Limited	India-Cyprus
Tenoch Holdings, Cyprus	Jun 18, '12	ByCell Telecom India	India-Russian Federation & India-Cyprus

Source: Ministry of Finance through RTs filed by trade activists

Under international law, as a general principle, tax matters are considered to be arbitrable. In investor-state disputes, however, specific questions pertaining to their admissibility will depend on the language of the treaty.

ADMISSIBILITY OF TAX DISPUTES

Historically, most international investment agreements have not created any exceptions for tax disputes. Over the years, however, many of them evolved to incorporate provisions that wholly exempt tax matters or carve out specific parameters for their application. Defining the scope of 'tax' was another way of putting limitations in place.

Such 'exceptions' and 'exceptions-to-exceptions' have created multiple layers of complexity, which must be deftly manoeuvred by an arbitral authority while determining the scope of its jurisdiction. However, if a tribunal determines that the dispute is not really about the imposition of tax but is about an abuse of power by the government, it may nevertheless proceed to arbitrate such matters. This is where principles like Fair and Equitable Treatment (FET) and non-discrimination assume special relevance.

Some regimes have additionally dealt with the intersection of double taxation treaties, domestic statutes, and investment laws by requiring the exhaustion of particular remedies before availing other dispute resolution mechanisms. In other words, matters of admissibility under an investment treaty is determined by what the state parties have consented to, at the time of entering the treaty or through subsequent joint interpretative statements.

ENFORCEMENT OF ARBITRAL AWARDS

Apart from the admissibility phase of investor-state disputes, arbitrability of tax matters may arise at the enforcement stage. For instance, when investors approach a foreign court to enforce an arbitral award under the New York Convention, governments may argue that tax disputes are not arbitrable under the laws of that particular jurisdiction. While there does not appear to be any data on the success of this strategy, as a matter of principle, it is possible to bring such issues of arbitrability at the time of enforcement.

Of course, this would not apply in the context of the International Convention on Settlement of Investment Disputes (ICSID), where the right to arbitrate treaty claims has no effect on enforcement mechanisms.

A TWO-WAY STREET

When nation-states become protectionist and over-regulate through new generation treaties, there may be ramifications for their own investors. For example, if a government enters a treaty that limits protections for foreign investors, similar treatment may be meted out to its outbound investments.

Therefore, before implementing any measures that completely exclude tax disputes from investor treaties, as India has sought to do with its model Bilateral Investment Treaty (BIT), states must evaluate all long-term consequences.

THE ENFORCEMENT PREDICAMENT

The enforcement of an investment treaty award is a layered issue and needs to be deconstructed step by step

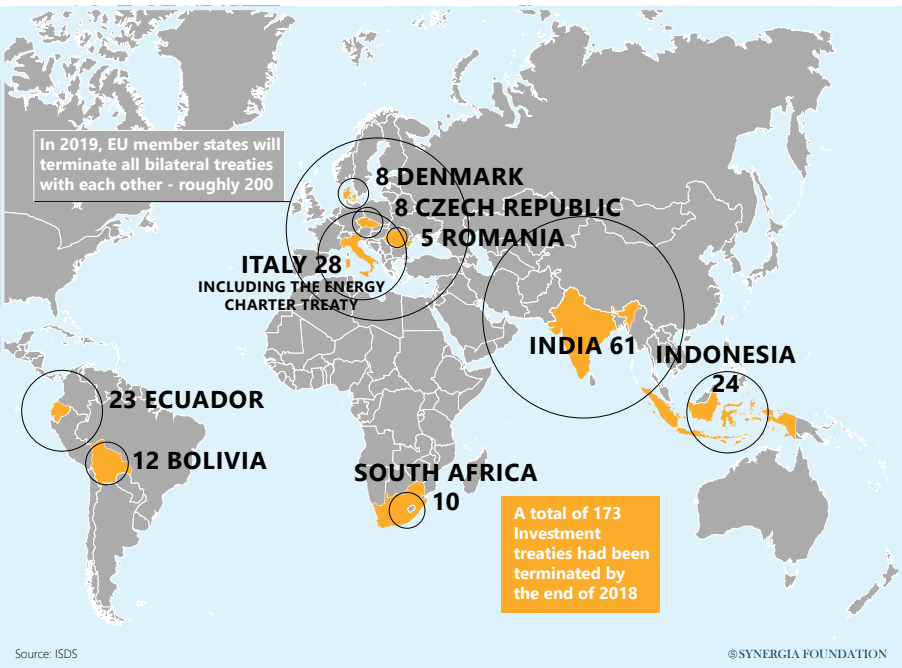
Shwetha Bidhuri, is the South Asia head at the Singapore International Arbitration Centre. This article is based on her views at the 102nd Synergia Forum on 'Retrospective Tax Law and India's Global Road Ahead'.

In India, the enforcement of arbitral awards under an investment treaty remains legally murky.

CLARIFYING THE ENFORCEMENT TERMS

Under ordinary circumstances, after securing an investment award in its favour, a company would seek to enforce the same in a jurisdiction where the respondent state has maximum assets. In the Cairn arbitration case, therefore, the natural choice would have been India. However, the country's high courts have adopted conflicting positions about the applicability of the Arbitration and Conciliation Act 1996 (Arbitration Act) to investment treaty awards, thereby raising doubts about their enforceability.

For example, in Board of Trustees of the Port of Kolkata v. Louis Dreyfus Armatures, the Calcutta High Court seems to have operated under the presumption that investment awards are enforceable under the Arbitration Act. However, in Union of India v. Khaitan Holdings (Mauritius) and Union of India v. Vodafone Group plc, the Delhi High Court has remarked that arbitral awards under an investment agreement are not in the nature of commercial awards and therefore, should ordinarily be governed by a regime that is different from the Indian arbitration act. While this might have been in the nature of 'obiter', it still leaves a big vacuum for foreign investors, in terms of enforcing the awards that are granted in their favour.



Given this legal uncertainty, India will need to clarify its position. Until the Supreme Court adjudicates on this issue, the Parliament should bring in a legislative amendment that clarifies the import of the Arbitration Act and its applicability to foreign investment awards. In fact, there are many who argue that investment treaties are not strictly outside the commercial regime, given that their premise is somewhat similar.

TREATY LANGUAGE

In both the Vodafone and Cairn cases, the government had contested the arbitrability of tax disputes. While resolving such admissibility and enforcement matters, the simple solution is to defer to the language of the treaty. If nothing indicates that India had agreed to exclude tax-related matters or taxation measures from the scope of its Bilateral Investment Treaty (BIT), then an investor would be justified in resorting to arbitration or other mechanisms of dispute resolution, as provided under its ambit.

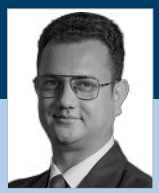
For example, while the India-Russia BIT has completely excluded taxation matters, the India-UK BIT has made a mention of tax in the context of the 'Most Favoured Nation' status.

TREATY VIS-À-VIS PUBLIC POLICY

Lastly, the question of public policy is critical. India has the undeniable right to tax private parties, whether retrospectively or not. India has the undeniable right to tax private parties, whether retrospectively or not. Sometimes, it ends up reversing the effect of an SC judgement, as was seen in the Vodafone case, which left the investor feeling cheated. Treaty regimes embody a guarantee by the country that it has willingly decided to undertake the conditions accompanying them. On occasions, where a government decides to not have treaties, and an arbitral tribunal gives a decision against it, the country can question the ruling on the grounds of public policy.

NAVIGATING THE TERRAIN OF PUBLIC POLICY

States need to clearly delineate the contours of public policy, before claiming it as an exception in investment arbitrations



Ajar Rab, is a Partner, Rab & Rab Associates LLP, based out of Dehradun. He is also an International Policy Consultant at Lexidalean, an international policy consulting firm. He has published several articles on international arbitration, and has authored books on real estate law and drafting of commercial contracts. This article is based on his views at the 102nd Synergia Forum on 'Retrospective Tax Law and India's Global Road Ahead'.

The Cairn arbitration case has once again thrown the limelight on issues surrounding India's tax laws, with a primary focus on the 'retrospective' aspect of taxation. Ensuring the State's right to rightfully tax private companies while safeguarding the investors' rights is by itself a balancing act.

Currently, when one thinks of India and investment arbitration, there appears to be a sense of cynicism, which needs to be dispelled. India certainly suffers from various arbitration concerns. Having been under media scrutiny due to the Vodafone and Cairn disputes, the problem that seeks urgent attention is the matter of retrospective tax.

With regard to the Cairn issue, actions are being currently taken to seize Indian assets on foreign soil to recover the amount awarded by the international arbitration tribunal. There have also been other cases, such as the 2G spectrum dispute, with its various corruption charges, that have led India to respond in a threefold manner.

Firstly, India has terminated its Bilateral Investment Treaties (BITs). Secondly, it has proposed a new model BIT, which specifically excludes taxation measures. Thirdly, India has defended its actions under the wide ambit of public policy.

Since public policy brings within its fold the question of arbitrating disputes, India has taken the position that tax disputes are non-arbitrable.

PUBLIC POLICY EXCEPTION

There is a legitimate expectation on the part of investors that laws would not be changed to their detriment. While the way forward in the new Indian model BIT is to exclude taxation measures, the question remains whether this can be retrospectively done under the garb of national interests, security concerns and the public policy of a

State. This, in turn, begs the question – 'what is public policy'?

Most developing countries, when faced with an arbitration claim, tend to mix up domestic policy with public policy qua domestic policy, and public policy with respect to international law.

All attempts to generate an international or a transnational public policy till date, have been unsuccessful. Hence, the line between public policy and political interests is often blurred.

States ought to take into consideration the real intent behind the public policy exception in international law, and more specifically, in international arbitration. In arbitration, the public policy exception extends to violations of the most fundamental notions of justice, morality and ethics or such violations that strike at the root of the sovereignty of a country.

Therefore, the public policy defence extends to mandatory law or lois de police and not to actions taken under the garb of public policy.

WHAT SAYS INDIA?

Recently, the Supreme Court, in the case of Vidya Drolia v. Durga Trading, for the first time, clearly laid out what it considers as public policy. This is relevant for two reasons. Firstly, it helps decide whether the issue is arbitrable or not. Secondly, it clarifies whether you can resist enforcement on the grounds of public policy. On the one hand, that which is arbitrable under domestic law automatically becomes arbitrable under international law. However, the reverse scenario is unclear, muddying the position on public policy exceptions. For instance, when something is non-arbitrable under Indian domestic law, but is arbitrable in the US such as competition law, where does one draw the line?

The question that needs to be addressed at the policy level is whether there exists any solution to prevent States from claiming public policy as an excuse to justify their taxation measures.

In the Devas Multimedia case, India cancelled telecom licenses citing security concerns. While one tribunal agreed with this interpretation and reduced India's liability, under the German BIT, it was held that there were no security concerns involved and that this was simply an inequitable treatment being meted out to the investor. Indian policymakers need to decide whether the State is willing to distinguish between domestic public policy and international public policy. In the absence of such clarity and much-required certainty, neither can investors be adequately protected nor can India successfully defend its actions as a sovereign.

This distinction will also bolster the confidence of other nations to reciprocate protections for Indian investors. Furthermore, a clear legislative intent that delineated the contours of public policy will make enforcement of arbitral awards easier.

POTENTIAL TRAJECTORIES

If domestic remedies have not been exhausted, can the entire arbitrable process be completely thwarted, given the lingering option of public policy? Should stabilization clauses be reintroduced to prevent actions such as the nullification of Supreme Court judgements? One can also debate if the solution lies in having joint committees between states, before an investor claim is brought for arbitration, as India has sought to do in recent times.

Expert Q&A

Q Following a favourable award in its tax-related investment dispute with India, Cairn Energy has threatened to takeover Air India's assets in the United States. To what extent is this enforcement strategy viable?

A Ajar Rab: The reason why Air India was picked was because of its distress sale. If the same can be effected, Cairn would potentially be able ask the government for a settlement. Therefore, over the coming days, the question of viability will not be as relevant as the success of this strategy.

A Shwetha Bidhuri: For any company that gets an award in its favour, the obvious reaction would be to enforce it in a place where the respondent has maximum assets. In the Cairn arbitration case, the relevant jurisdiction would be India. However, given the uncertainty about the application of the Arbitration and Conciliation Act, 1996 to investment arbitral awards, Cairn has identified jurisdictions around the world where the Indian government may have overseas assets.

A Arijit Prasad: Even in a foreign court, the enforceability of this award will depend on the interpretation of Indian laws. For instance, there was a recent judgement in Malaysia where the Supreme Court interpreted Indian laws and public policy, before determining the enforceability of a particular award.

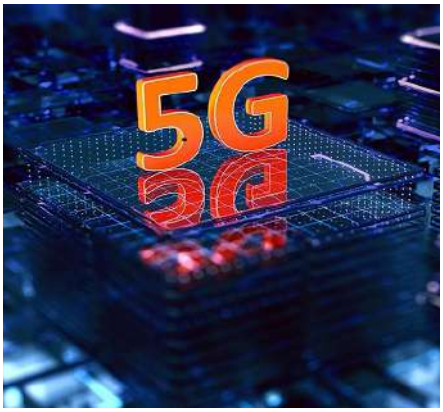
Q If the Parliament or the Supreme Court proceeds to clarify the applicability of the Arbitration and Conciliation Act (1996) to investment arbitrations, will India reconsider its decision to not be a party to the International Convention on Settlement of Investment Disputes (ICSID)?

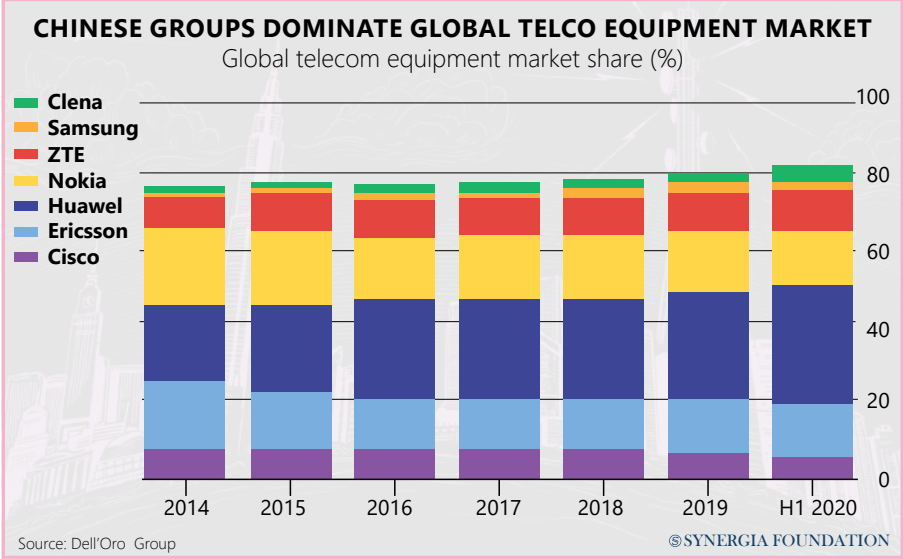
A Shwetha Bidhuri: This is a slightly different issue. The reason why India chose to not be a signatory to the ICSID convention was driven by public policy considerations. In particular, it had objected to the provisions of the Convention that limited its ability to challenge an arbitral award before its own national courts.

INDIAN 5G SANS HUAWEI

The Huawei controversy raises the questions of whether India can envision a future without Chinese venture capital

SYNERGIA FOUNDATION
RESEARCH TEAM





In the first week of this month, the Indian Department of Telecom (DoT) released permissions for 5G trials. The selected network providers such as Sweden's Ericsson, Finland's Nokia, South Koreas Samsung, and State-owned C-DOT were asked to work with Indian mobile operators. Reliance Jio was accorded permission to conduct trials with its own 5G technology.

Conspicuous by their absence from the list were Chinese telecom giants Huawei and ZTE. Coming in the wake of the ban on Chinese apps imposed during the Ladakh border faceoff and growing allegations of cyber-attacks on Indian systems by Chinese hackers, the news did not come as a surprise. It only further substantiated the Indian government's policy to reduce the Chinese footprint in developing its critical cybersphere.

In this context, the Telecom infrastructure on which most of our digital atmosphere exists, has come under the intense scrutiny of the Indian government. 5G technology or fifth-generation mobile network is going to revolutionise the digital landscape as we know it. With a speed of almost 100 times that of existing 3G/4G technology, it will facilitate much larger data transfers, cyber intelligence, A.I., financial transactions, etc. It will also be much more efficient in connecting autonomous cars, smart cities, and smart industry. It is set to completely change and re-shape our economies, societies, defence mechanisms, and much more. Thus, it becomes imperative who and what interests are defining and controlling this game-changing technology.

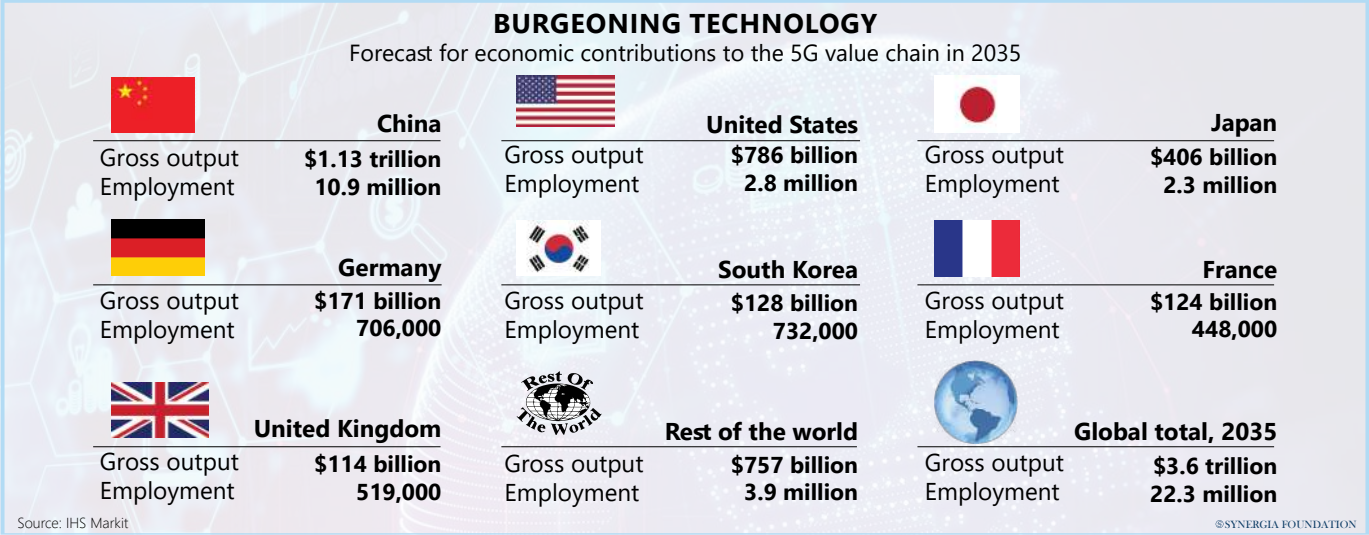
5G TECH: WHO IS IN CHARGE?

With Huawei leading 5G technology, China aims to make almost 13 trillion dollars in new value globally by 2035. The only other companies which are in the same league are Nokia and Ericsson. China's long-term thinking has given them an upper hand and a lead to market such disruptive technologies.

The common concern is that through these technologies, Beijing seeks strategic control of global supply chains. They range from critical raw materials up to semi-finalised products and, finally, worldwide installation and application of these new technologies. The Chinese fusion model of integrating civilian and military efforts for technological innovation makes sure that the government controls how the technology is used and sold.

With 5G technology, China and Huawei have proposed new standards for core network technology (called 'I.P.') at the U.N.'s International Telecommunication Union (ITU). They claim that current global networks are "unstable" and would be "vastly insufficient" for the future digital world they hope to build by 2030. These proposals have been perceived as a move by Beijing to seek control over the use of the internet on its citizens and also globally via U.N. institutions with the support of other like-minded nations.

Huawei is already viewed with suspicion. It has had accusations of breaching data privacy and thus threatening national security levied against it. In 2019, the U.S. Department of Commerce put Huawei on its 'Entities List' which identifies companies and individuals that the U.S. government deems a threat to national security. Since then, it has continued imposing sanctions on technological exports and imports to and from China, such as semiconductor chips, to halt and hamper its growth within the larger global economy. The U.S. is also coercing its allies to withhold technology or outright ban Huawei and its related services, citing a lack



of data privacy and its ambiguous connection with the CPC (Communist Party of China). The EU has also expressed concern in enrolling Huawei for its 5G rollout. The UK government excluded Huawei from its 5G rollout in 2020 and has asked the company to remove existing equipment from the country by 2027. It seems that India has taken a leaf out of their book and taken the first step in the Indo-Pacific region by adopting a hard-line stance against China, at least in the technological dimension.

DIGITAL DISTANCING, A VIABLE OPTION?

While a potential 'digital de-coupling' from China is desirable from a cybersecurity point of view, it begs the question of whether it would be economically viable.

India's cyberspace is relatively open, fluid and largely dependent on foreign funds and investments. The internet app-based start-up industry depends on a heavy influx of Chinese venture capital. Even if the GOI bans another 100 China-based apps, it might not be enough to counter Chinese presence in the Indian Internet space. The heavy influx of Chinese funding, technology, and equipment needs to be regulated. Alibaba and Tencent were the major companies leading the way in flowing Chinese venture capital to India, totalling $4.3 billion between 2017 and 2020. Following the crackdown on China-based apps, the Indian government seeks to regulate Chinese and other foreign investment in the country. The introduction of a new law known as the 'Consolidated FDI Policy', announced in October 2020, forces countries that share a land border with India, such as China, to invest in India solely through government channels. Therefore, investments from China will be examined on a case-by-case basis by government agencies. This move may severely restrict the free flow of venture and other forms of capital into the Indian economy from China.

While this may be a huge step towards regulating Chinese money and income into its domestic economy, it is a devasting blow to the Indian start-up industry, which is heavily dependent upon FDIs. With hundreds of new start-ups being rolled out, there is a survival rate of less than a per cent, those being able to withstand the withering competition and make a profit.

Venture capital investments are extremely risky and need a continuous flow of capital and cheap equipment to sustain themselves. China provides both. In contrast, the western flow of capital into India's domestic economy has always been towards established companies and private entities that ensure profit. Western investors tend to invest less as venture capital and target areas and business, generating high profit or royalties.

WAY OUT OF STALEMATE

One of the main reasons most free-market entities and states are irked with China is that it does not offer a reciprocal market.

The fundamental principle of a global free market is the idea that one should have the freedom to mutually invest in each other's domestic economies.

Using their hold over private players and companies, the CPC government channelises the profit made from other markets towards their internal domestic infrastructure, thus ensuring that it sustains itself without foreign capital.

Considering the heavy pushback against Huawei technology in its most profitable markets, will the CPC offer levy in these restrictions? Or will they hand over more control over the technology to the buyers? Or can they incorporate cybersecurity mechanisms of other governments to build trust and ensure transparency? These are some questions which CPC need to answer.

Despite the LAC de-escalation announced by India and China, it is unlikely that diplomatic engagements will return to the 2019-2020 levels. However, India will continue to seek an interaction that rebalances a large trade deficit with China.

Limiting and regulating its investment, and presence, should also not be read as a complete rejection of Chinese financing in India. Such an outright distancing is not possible for the present situation. India's existing 4G networks itself have trouble earning a profit, and even then, it relies heavily on Chinese equipment to sustain itself.

FOURTH ESTATE UNDER SIEGE

Reporters across the globe are witnessing an increase in threats, arrests, and censorship

SYNERGIA FOUNDATION
RESEARCH TEAM

Nothing could have illustrated the threat posed to journalists better than the utter disregard shown for world opinion and international law by Belarusian strong man Alexander Lukashenko when he diverted Ryanair flight from Athens to Vilnius, Lithuania's capital, to the Belarusian capital Minsk on the pretext of a "potential security threat on board." Upon landing, Pratasevich, the former editor in chief of one of the most popular Telegram news channels in Belarus, was promptly arrested.

While contempt for the media may be the cornerstone for authoritarian regimes, it is a sad commentary that there is an increasing trend among democracies to subvert the autonomy of the media.

GROWING HOSTILITY

One of the most critical threats is geopolitical, where leaders of democratic, authoritarian, and dictatorial dispensations attempt to suppress the circulation of fair and transparent information. They impose their visions of a world without pluralism and independent journalism.

Compared to 2019, arrests of journalists shot up by 1200 per cent in the U.S. Recent reports uncovering seized phone records of journalists further reveal the intrusion on U.S. media's First Amendment rights. Half of Eastern Europe is witnessing an increase in authoritarian regimes, with a matching rise in cases of state ownership and extensive censorship protocols. In Israel, four high-profile journalists have been assigned private security over receiving death threats, while more journalists have faced on-ground attacks over their reporting.

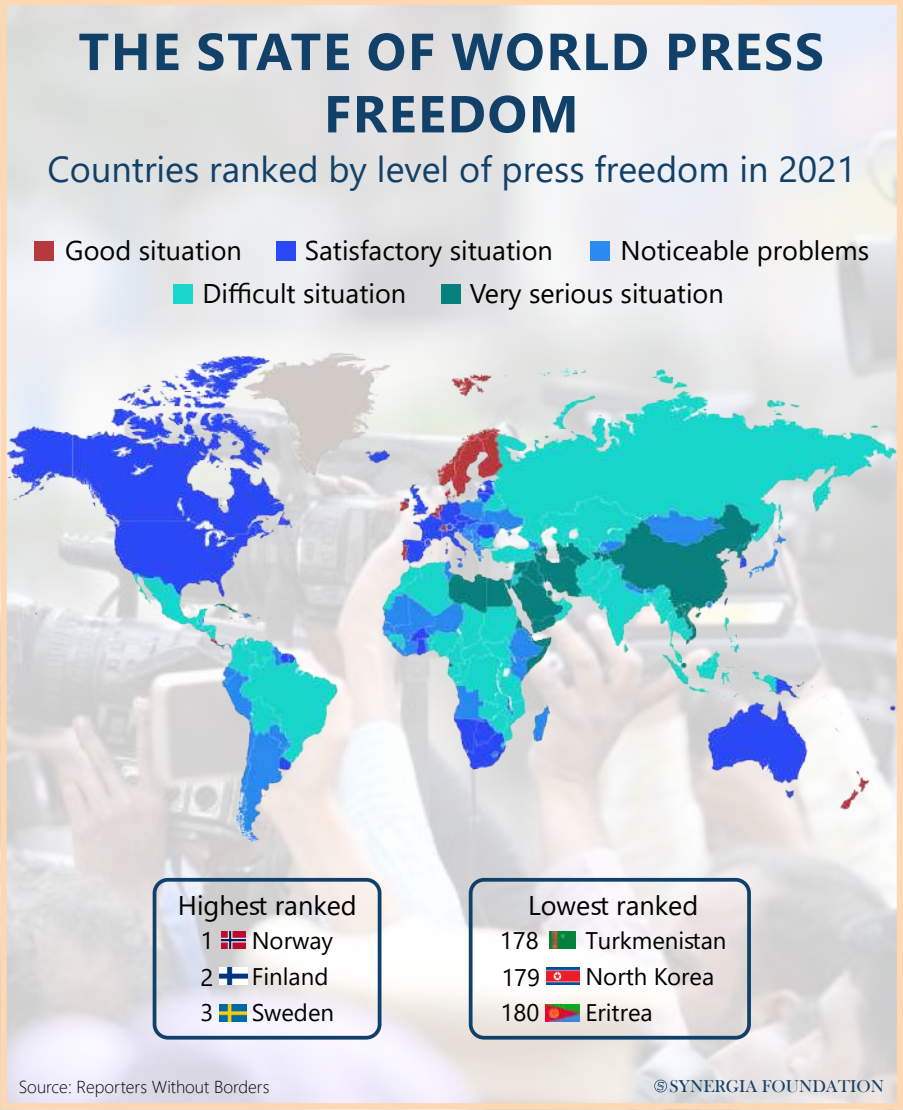
The digitisation of media comes with its own share of threats. Since 2013, the U.S. National Security Agency has used its sprawling 1.5million sq ft Utah Data Centre to store and analyse data captured from around the globe. This surveillance data can enable the government to dig deep into a reporter's research, trace the sources and, if found worthwhile, enable real-time eavesdropping. The sanctity of source protection, so essential for investigative journalism, has been torn asunder by this capability. In fact, in a 2013 scoop, using documents provided by Snowden, the German Der Spiegel magazine broke a story on NSA breaking into the internal communication system of Al Jazeera broadcaster.

The unprecedented rise in digital media and especially social media has blurred the lines for gathering fact-checked information and creating a culture of clickbait and fake news. The lack of appropriate regulations in the digitalised and globalised platforms has contributed to an environment of disinformation. This, in turn, has been grasped by regimes of all sorts to pass laws, which, on the pretext of curbing fake news, enable tougher crackdowns on journalists and independent media houses.

The Digital Security Act 2018 passed in India, for example, curbs the freedom of the press. It allows forces to carry out arrests, without a warrant, of those who criticise the government online. Singapore introduced a similar law that undemocratically restricts the freedom to inform on the pretext of combating cybercrime and disinformation. Of even greater concern is the Indian Information Technology (Intermediary Guidelines and Digital Media Ethics) Rules, 2021. Although mainly focusing on online platforms like Facebook, YouTube, Amazon, and Netflix, it also covers "publishers of news and current affairs content." It grants the government the power to remove any online content in news articles, a kind of censorship unimaginable in the printed media in normal times.

CAPITALISATION OF MEDIA

Media undoubtedly is a big business. The capitalist model in the media sector dates to the first few decades of the twentieth century, where the emergence of newspaper industries dominated the market, catalysing the potential of profitability, and attracted advertisers to the industry. Consequently, the consolidation and decline of



newspaper diversity were perceived as the early threats to press freedom.

The financial capability of media outlets is a crucial factor that determines their ability to resist pressure and engenders the phenomena of ownership concentration. This also triggers conflicting ideas concerning journalistic ethics by putting business or national interests first, which further causes public distrust of media.

Today, Hungary, Serbia, Poland, and the Czech Republic are few countries that have recently witnessed a shift in the ownership and consolidation of media outlets to state-owned or owned by wealthy individuals. When media houses become state-owned, they lose the ability to provide non-partisan news and merely function as a medium that furthers totalitarian propaganda. The ability to hold governments accountable to truth is weakened. Not only does it ossify a culture of impunity, but it also weakens the informed voting processes in a democracy.

THE COVID PROTOCOL

Since 2013, Reporters Without Borders (RSF), a media watchdog organisation, has globally recorded a 12 per cent decline in press freedom. In 2020, the list of countries offering a suitable environment for free journalism shrunk to less than a dozen. RSF's Press Freedom Index revealed that the coronavirus pandemic had exacerbated the repression of free media.

A poll commissioned by the Alliance of Democracies Foundation finds that 'citizens rate their democratic countries' handling of the COVID crisis poorer than other less democratic countries (among 50,000 respondents in 35 countries)'. Several leaders promoted unproven COVID-19 remedies and false claims about the virus – from Asia to America. Some countries took a step further to track down journalists who were reporting on infection rates, death tolls, and covering live demonstrations on the ground and either denied access to the report or were the primary targets for arrest.

Disregarding the RSF rankings before 2020, there is a notable decline in the number of countries enlisted in the 'white zone' of the index in the wake of the global health crisis. The common sentiment that has accelerated official limitations on media journalists and proved to be detrimental to the freedom of the press globally is the fear of damage to one's reputation.

Assessment

Quality and unbiased news is an indispensable right imperative to uphold the pillars of democracy. Certainly, pecuniary consideration is a crucial element that enables news organisations to maintain their independence and autonomy and thus do their job – to find, report, and defend the truth with integrity.

There is a need for media publications and organisations to come together and develop blueprints to ensure the future of the free media taking on board multilateral agencies like the UN, who on their part must ensure press freedom and protection of journalists.

Passing legislations like the shield laws is key to protect journalists and their sources. Although they are present in many countries, there is a lack of regulation. Leaders must step up as the bulwarks of democracy and ensure that media freedom remains unscathed. UK's D10 initiative and Biden's Summit for Democracy may be important alliances to address threats to press freedom as press freedom alone cannot produce a democratic media without the will of its leaders.

SYNERGIA FOUNDATION

SYNERGIA FOUNDATION

34, Vittal Mallya Road, Bengaluru, Karnataka 560001, India
+91 80 4197 1000
info@synergiagroup.in

@SynergiaFoundation
@SynergiaImpact
www.synergiafoundation.org
www.synergiaconclave.org