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Analyzing the Role of State Immunity in Cairn Energy's Enforcement Lawsuit: Can India Successfully Invoke State Immunity in Defense?

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ABSTRACT

Last year in December while deciding an investment dispute related to the sovereign right to tax, a PCA tribunal at The Hague, ruled in Cairn Energy's favour an award of $1.72 bn. against India. However, India is determined to protect her sovereign right to tax and vowed not to accept the arbitral award. In these circumstances, the British Oil giant Cairn Energy Plc. has started locating Indian assets in different countries and moved courts in several jurisdictions under the international treaty for the enforcement of the arbitral award. It is reported that Cairn Energy has registered the arbitral award in more than ten countries including the US, France, the UK. Recently, a Paris based court has ordered to freeze Indian government assets valued at around $20 mn. In this background, I will argue that how far the doctrine of state immunity help India to protect her assets in foreign countries.

I. INTRODUCTION

On Tuesday (29/07/2021) the Indian government has confirmed in its Upper House the news of the Paris court's order to freeze certain estates of the government of India. Last month, the French court has accepted the application from the British oil giant Cairn Energy Plc, seeking to recover an arbitral award of $1.72 bn. ordered by The Hague based tribunal against the Indian government. Although the news of freezing assets is confirmed, the government has not identified the assets so far. However, it is believed that assets are mostly included residential real estate located in Paris, owned by the government valued at around 20 mn. euro. The Minister of State for Finance has also confirmed an appeal against the award has also been filed at the seat of arbitration, before the Court of Appeal, in The Hague. Additionally, after locating substantial assets in the New York, Cairn Energy has also moved a court in the South District of New York against India's national carrier Air India to enforce the arbitral award.

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 [ISSN 2581-5369]

The Indian government has determinedly asserted that they would contest every enforcement proceeding before the national courts in which enforcement lawsuit is filed. State-owned entities such as national airline companies, shipping lines, commercial enterprises, property used for commercial activity are very lucrative assets in terms of recovery of an arbitral award in the hands of the winning party. Predominantly, this is the only reason Cairn Energy is going for those assets. In this write-up, examining the present state of the law on state immunity, I will analyse the possibility of the Indian government for taking up the defence of state immunity in such cases.

II. INDIA'S RETROSPECTIVE TAX DISPUTE WITH CAIRN ENERGY

The Cairn-India dispute goes back to Cairn Energy's corporate reorganisation year 2006. At the time Cairn UK had transferred its shares in Cairn India Holding to Cairn India. Subsequently, in the year 2011, Cairn energy sold almost its entire shares in the Indian unit to Vedanta Resources. In 2012, the Indian Parliament introduced an amendment in her tax laws with retrospective effect. The said amendment made any capital gains arising out of the transfer of shares from a foreign entity whose assets were located in India taxable retrospectively, which means from the year 1962. Interestingly, the amendment was introduced to invalidate the Supreme Court's dictum in the Vodafone case where the apex court had ruled against India's income tax department's move to slap capital gains tax on Vodafone for overseas sale of share transaction. Under the new retrospective law, the tax Indian department slapped capital gains tax on Cairn energy and enforced the dues by selling shares, withholding refunds, seizing dividends etc. In March 2015, Cairn Energy initiated international arbitration under the auspices of the Permanent Court of Arbitration invoking the India-UK Bilateral Investment Treaty saying the actions of India caused significant loss in Cairn's investment. The Cairns argument was premised on the violation of fair and equitable treatment standards under India-UK BIT. The PCA tribunal held by striking capital gains tax based on the 2012 amendment and enforcing the same against assets of Cairn Energy, the Indian government treated the oil giant unfairly and inequitably which breached Article 3(2) of the India-UK BIT. Specifically, Cairn Energy contended that the Indian government was at fault in retroactively applying the capital gains tax on a transaction that was not taxable at the time it was carried out. Last year December a Permanent Court of Arbitration tribunal had found the Indian government guilty of violating India-UK BIT and ordered it to pay $1.2 bn. in damages to Cairn Energy. State practice shows that in most investment disputes, losing states conform with the arbitration award willingly. However, sometimes they do not, compelling the award-creditor to initiate enforcement proceedings in the national courts of the States where award-debtors assets are

 [ISSN 2581-5369]

located.

III. LAW OF STATE IMMUNITY IN INTERNATIONAL INSTRUMENTS

One of the difficulties in the enforcement proceedings in the investor-state dispute settlement system is the defence of the doctrine of state immunity. The norm of state immunity is premised on the sovereign equality and independence of States. Fundamentally, the doctrine prevents States and their authorised agents from prosecution in foreign courts. In turn, such protection from foreign jurisdiction enables and facilitates public functions of States and their agents. The sources of rules on state immunity may be found in customary international law, treaty law, domestic law, and treaty practise to some extent. Almost every State affords protection of state immunity from attachment and execution of sovereign assets of other States located in their jurisdiction. It has been universally accepted that waiver of State immunity from the jurisdiction of international tribunal does not automatically renounce state immunity from execution of the arbitral award in domestic courts. The very first attempt was made to codify the law on state immunity is the European Convention on State Immunity (ECSI); adopted by the Council of Europe in 1972. The major international instrument related to state immunity is the UN Convention on Jurisdictional Immunities of States and Their Property 2004; a major contribution of the International Law Commission. Both international instruments have incorporated the approach that general immunity from jurisdiction is distinct from the immunity from enforcement or execution. The UN Convention of State Immunity could have outshined the ECSI but in the absence of sufficient ratification, the Convention is yet to make a mark. Yet, the International Court of Justice and European Court of Human Rights have indicated that some provisions of the treaty have the status of customary international law and are applicable independently.

IV. DEFENCE OF STATE IMMUNITY IN INVESTMENT ARBITRATION

Finality of the arbitral award and the efficient enforcement are the two topmost features of international arbitration; investment arbitration is no exception. Essentially, investment awards are recognised and enforced under two principal international instruments; those are ICSID Convention of 1965 and the New York Convention of 1958. Both documents have recognised the state immunity rule and the rule is a potent defence in the hand of a losing party against an arbitral award. ICSID Convention is a special self-contained regime for investment arbitration. Even though the Convention does not allow the national courts to interfere with the ICSID awards, the Convention has saved the state immunity exception in Article 55 of the ICSID Convention. Article 55 specifies that the arbitral award during enforcement proceedings in a

State is subjected to the laws on state immunity of that State. The role of national courts is significant in case of enforcement proceedings under the New York Convention. Article III of the Convention is vital here; it provides, the contracting States shall recognise and enforce arbitral awards under the laws prevailing in the State where the arbitral award is sought to enforce. Though the rule of state immunity has not been explicitly mentioned in Article V as one of the grounds under which an award could be challenged, many believe Article III has impliedly allowed national courts to apply the rules of state immunity. The phrase "in accordance with the rules of procedure of the territory where the award is relied upon" in Article III supports such interpretation. Moreover, some national courts consider the term "rules of procedure" to embrace principles of international law such as the doctrine of state immunity. It is to be noted that these two principle international documents have waived the immunity from jurisdiction and not immunity from enforcement or execution. Thus, a recalcitrant State may well invoke the state immunity exception in the national courts during the enforcement proceedings.

V. NATIONAL LAWS ON STATE IMMUNITY AND JUDICIAL TRENDS

As the law of state immunity has evolved from the different sources, sources vary for customary international law to national statutes; we can well characterise it as a hybrid law. Mainly, international norms of state immunity are applied in two diverse techniques; first national courts may directly apply the rules as a part of their legal order or the norms have been transposed into national legal order through legislative actions. Which of these two approaches a State chooses, basically depends on whether a particular State follows dualism or monism. It is observed while common law jurisdictions are working on the Domestication of the state immunity doctrine started with the US codified Foreign Sovereign Immunities Act (FSIA) 1976. This trend was followed by the UK legislating State Immunity Act (SIA) 1978. We have put a limit by discussing only these two states approaches and judicial trends relating to state immunity. Generally, the US courts under FSIA 1976 provides both immunities from jurisdiction and immunity from execution to States and their properties respectively subject to international agreements the US has signed. It is to be noted that the immunity extends to the State agency or instrumentality. Nonetheless, the general protection to the State and its instrumentality or agency can be avoided if a State or its assets fall one of the exceptions provided under the FSIA 1976. Such exceptions include explicit or implicit waiver of immunity, commercial nature of the activity, admiralty suit etc. That said, central bank, property used by or under the authority of foreign army is immunised and exempted from execution and attachment under FSIA 1976. Unlike FSIA 1976 the SIA 1978 affords

 [ISSN 2581-5369]

protection of immunity from jurisdiction only, perhaps immunity from execution is left for the judiciary to decide. The foreign states are immune from the courts of the UK subject to the provisions of the SIA 1978. Some exceptions under the SIA 1978 are – when State waived immunity, commercial activity by State, commercial vessels etc. Moreover, State immunity is afforded to the head of the State, government, department of the government, central bank under provisions of the SIA 1978.

VI. CAIRN ENERGY'S LAWSUIT AGAINST INDIA – CAN INDIA SUCCESSFULLY INVOKE STATE IMMUNITY DEFENCE?

In practice, the US Courts presume that state instrumentalities are separate and distinct from the State itself. The Act's legislative history indicates the term has received a wide interpretation and is intended to include a broad range of entities such as corporations, associations, state trading corporations, mining enterprise airline or shipping company etc. who can sue and be sued, hold property, contract in its own name under the law of the State it is established. As such the legislation manifests an essential policy of respecting distinction between the State and its separate agencies or instrumentalities. Generally, US Courts abide by the policy and attach assets of the state instrumentality and the State is regarded as single. However, if the state instrumentality enjoys a separate legal status, then its assets are protected. This was expounded in the seminal case of First National City Bank v. Banco Para El Comercio Exterior de Cuba (BANCEC) in the year 1983, the US Supreme Court held, "duly created instrumentalities of a foreign state are to be accorded a presumption of independent status". Thus, a state-owned entity such as Air India normally would be treated as a separate independent and distinct entity from India. However, such presumption is not final, it comes with some exceptions. In BANCEC, the court held the presumption can be overcome when it is shown that the instrumentality is so extensively controlled by the State….that a relationship of principal-agent is created, and the instrumentality is nothing but an alter ego of the State. The court laid down a five-aspect test to decide an instrumentality is really an alter ego of the State. These are as follows - i) the level of economic control by the government; b) whether the entity's profits go to the government; c) the degree to which government officials manage the entity or otherwise have a hand in its daily affairs; d) whether the government is the real beneficiary of the entity's conduct; e) whether adherence to separate identities would entitle the foreign state to benefits in United States' courts while avoiding its obligations. In the same manner, the Indian national carrier Air India would be accorded a separate legal status or the Indian government can advance such an argument before the US court. Albeit such argument

is refutable with counter-argument based on a five-factor test developed in BANCEC. Once again, in Mckesson Corp v. the Islamic Republic of Iran, the US court held that presumption was rebutted when Iran controlled the instrumentality's routine business decisions such as honouring contract commitments and declaring and paying dividends to shareholders. Cairn Energy has argued before the US Court that the Indian government extensively controls Air India which created a principal-agent relationship. Indian government appoints and removes high-level officers of Air India, it can tailor the airline's policy, determines the salary of its employees, supports financially through loans, capital, favourable tax treatment etc. Essentially, this kind of wide control over Air India's business activities makes the instrumentality nothing but an alter ego of the Indian government. Accordingly, Cairn Energy is one step ahead of India in winning the case and attaches the assets to recover the arbitral award. Another very interesting case is LR Avionics Technologies Limited v. The Federal Republic of Nigeria (2016) where the English High Court set aside an order for enforcement of an arbitral award and a similar foreign judgment issued against property owned by Nigeria. Such property was leased to a private company for processing visa and passport applications on behalf of the government of Nigeria. Although the operation carried out by the private company is purely commercial, an exception under the SIA 19978, the activity was consular activity and protected as sovereign purpose. The UK Court noted, "the primary consideration must be the nature or character of the relevant activity". The consular function is public function as such whether it is performed by the government itself or by a private entity for commercial purposes. Consequently, India could save her residential properties located in Paris, a subject of an enforcement proceeding, if India shows that the property is not used for commercial purposes, rather used for public purposes such as consular functions or used as residential apartments for officers engaged in sovereign functions.

VII. CONCLUSION

Cairn Energy has the arbitration award registered in more than ten different countries such as in the UK, the US, France, Singapore, Canada etc. The Scottish oil giant has already located Indian assets worth $70 bn. for recovering its $1.72 bn. arbitral award against India. The battle for the recovery of debt will be time-consuming and the burden of proof is on the applicant; that is Cairn Energy. The analysis unravels that Cairn Energy has a good chance to recover the debt what it needs to do a careful examination of the nature and the function of the Indian assets. A well-researched strategy is very much essential in this respect. On the other hand, the Indian government needs to build up a solid case against the attachment and execution which needs a stratagem of meticulous study on law and practice on state immunity in those

 [ISSN 2581-5369]

jurisdictions in which she has to fight a lawsuit.

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 [ISSN 2581-5369]