Enforcing US Outsourcing Customer's Rights and Remedies in India

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Outsourcing Contracts With Indian Suppliers: What to Expect When Enforcing US Customer’s Rights and Remedies in India

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In any offshore outsourcing transaction, the enforcement of the US customer's rights and remedies is always a vital concern, and those concerns can be exacerbated when dealing with an Indian supplier with few or no meaningful assets in the US against which any judgment or arbitral award could be executed. If the Indian supplier has meaningful assets located in the US and a US plaintiff-customer successfully obtains a judgment in a court of competent jurisdiction, the judgment can be enforced against those US assets. However, even if a dispute with an Indian supplier is adjudicated in the US, if the Indian supplier's primary assets are located in India and not in the US, the US customer must still seek redress within the Indian legal system to obtain and enforce a judgment against the Indian supplier's India-based assets, which can present significant challenges as described below. Therefore, a US customer should understand upfront the Indian supplier's corporate structure, including the location of assets within the supplier's corporate family, and structure the dispute resolution provisions in a manner that will maximize the possibility of the US customer's recovery against the Indian supplier's assets in the event of a dispute. If the Indian supplier has assets in multiple jurisdictions outside the US, the US customer should seek recovery against the Indian supplier's assets in a jurisdiction that would be most effective. For example, if the Indian supplier has assets both in the U.K. and India, it may be prudent for the US customer to seek enforcement of a US judgment against the Indian supplier's UK-based assets as the enforcement of US judgments by the UK courts is relatively routine. Where possible, the US customer should consider additional mechanisms beyond the operative contract to guarantee performance and payment from the Indian supplier through requiring parent or affiliate guarantees, letters of credit, payment escrow accounts, product liens and security interests and insurance, as applicable.

Enforcing US Judgments in India

Under Indian law, a US judgment is not directly enforceable in India. Rather, it can only be enforced by filing a fresh lawsuit in an Indian court based on the US judgment, which will be treated as evidence, among other evidence, against the Indian defendant. The lawsuit could require years before any relief is actually awarded by the Indian court. Furthermore, the US judgment will not be enforceable in India if it is determined by the Indian court that (i) the judgment was not issued by a court of competent jurisdiction, (ii) the judgment was not issued on the merits of the case, (iii) the judgment appears to be founded on an incorrect view of international law or a failure to recognize Indian law if such law is deemed to be applicable, (iv) principles of natural justice were ignored by the US court, (v) the judgment was obtained by fraud, or (vi) the judgment sustained a claim founded on a violation of any law in force in India. Only once a judgment is obtained from the Indian court in this proceeding may the US customer seek to attach the Indian

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supplier’s assets in India. This also applies to any injunctive relief issued by a US court that will need to be enforced against a defendant in India. This process is much more simplified and streamlined with respect to certain countries designated as “reciprocating territories” by the Indian government. Foreign judgments passed by courts of these “reciprocating territories” can be directly enforced in India by filing execution proceedings and are deemed to be decrees of the Indian courts for enforcement purposes, thereby considerably speeding up the process. The “reciprocating territories” include the UK, Singapore, Hong Kong, Malaysia, Canada, New Zealand, to name a few, but not the U.S.

Because seeking to enforce a foreign judgment in India can be arduous, time consuming, expensive, and unpredictable, jurisdiction and enforcement provisions in the operative outsourcing contract should be carefully considered and crafted so as to provide the US customer with adequate and flexible rights and remedies keeping in view the nature and scope of the services outsourced to the Indian supplier, including any IP or sensitive data being transferred to India.

**Enforcing Governing Law and Forum Selection Provisions**

Indian courts recognize private international law principles and will generally enforce choice of law clauses agreed upon by the parties, except under very limited circumstances, such as, for example, if the chosen governing law would violate public policy in India in some way. Thus, in the operative outsourcing contract between an Indian supplier and a US customer, the US customer must always unambiguously require a particular state’s law as the governing law of the contract. A US customer should be aware, however, that Indian courts may nonetheless apply Indian law to adjudicate disputes in certain fields, including disputes involving IP, real property, labor issues, and insolvency, for example, regardless of the governing law stipulated in the contract, thereby limiting the practical realization of the contract’s intended protections should the Indian supplier seek protection in an Indian court. Therefore, a US customer should be cognizant of the effect Indian laws might have on the contract terms agreed upon by those parties.

Indian courts also generally recognize forum selection clauses, including clauses that require the parties to litigate disputes in a foreign jurisdiction. To avoid becoming embroiled in litigation in Indian courts, a US customer should require that the parties adjudicate any dispute arising from the licensing or technology transfer transaction exclusively in a US jurisdiction or a “neutral” non-Indian jurisdiction. To be enforceable in India, exclusive foreign venue provisions should be carefully crafted in accordance with Indian law requirements and include express waivers. One exception to an exclusive venue provision that may be beneficial to a US customer would be to retain the right of the US customer to seek injunctive relief in a local court in India under appropriate circumstances, such as to stop an Indian party from the unauthorized use or disclosure of the US customer’s IP in India.

It is important to note that the enforcement of venue selection clauses is not without limitation in an Indian court. Even if an outsourcing contract contains an exclusive non-India venue provision, if the Indian supplier seeks protection in an Indian court an Indian court may elect, in its discretion, not to enforce the venue provision but instead to adjudicate the lawsuit in India if it determines that justice will be better served. For example, a US customer could find itself involuntarily in an Indian court if the Indian
supplier, notwithstanding the agreement to submit to foreign jurisdiction, initiates an action in an Indian court or seeks an “anti-suit” injunction against the proceedings initiated by the US customer in a foreign court. In such a situation, the Indian court could decide to assume jurisdiction or stay the action, depending on the circumstances of the case.

**Arbitration Preferred Over Litigation**

To best mitigate the risk of an Indian supplier seeking refuge in an Indian court and being mired in prolonged litigation and subject to unfamiliar procedures, private arbitration is the preferred means of dispute resolution in commercial transactions involving India. The benefits of confidentiality of arbitral proceedings and the relative ease of enforcing in India both foreign and India-based arbitral awards further provide compelling reasons for adopting arbitration as the formal dispute resolution mechanism in India.

India is a signatory to the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Awards, commonly referred to as the “New York Convention,” which makes a foreign arbitral award rendered in a “convention” country far easier to enforce in India than comparable court judgments. However, a foreign arbitral award may be challenged or refused enforcement in India on certain limited grounds which include (i) the incapacity of any of the parties to the contract, (ii) the invalidity of the arbitration agreement under the law governing the dispute, (iii) a lack of due process afforded to either party, (iv) if the award is beyond the arbitration clause’s scope, (v) the subject-matter is not subject to resolution by arbitration under India’s laws, or (vi) if enforcement would be contrary to public policy in India. If an Indian court is satisfied that the foreign arbitral award is

In an outsourcing transaction, therefore, the operative contract should unequivocally specify that all disputes relating to the transaction must be arbitrated and require the arbitration to be conducted preferably in the US, but at the least in recognized neutral, non-India venues, such as Paris, London, or Singapore, for example. The US customer should consider whether to preserve the right to seek injunctive relief in India depending on the circumstances specific to the transaction.

On January 10, 2008, the Supreme Court of India issued an important decision in the case *Venture Global Engineering v. Satyam Computer Services, Ltd.*, 2008 (1) CTC 348, regarding the enforcement in India of foreign arbitration awards. The decision paves the way to challenge foreign arbitral awards in an Indian court based on broad public policy grounds and has important implications for any US customer that may find itself involved in an arbitration proceeding involving a supplier located in India. Specifically, the Supreme Court upheld a challenge in India to a foreign arbitration award on the grounds that the relief contained in the award violated certain Indian statutes and was therefore contrary to Indian public policy pursuant to Part I of India’s Arbitration and Conciliation Act, 1996 (the “Arbitration Act”). As a result of the *Venture Global* decision, new risks exist with respect to the impact of Part I of India’s Arbitration Act on contract parties’ rights and expectations in agreements involving India and that contain arbitration clauses. The Supreme Court’s decision did recognize, however, the right of contract parties to exclude the application, in whole or in part, of Part I of the Arbitration Act in their contracts. Accordingly, these new risks arising from the Supreme Court’s decision may be addressed
and minimized by analysis of Indian law concerning the rights and interests involved in a particular transaction and by carefully drafted provisions in the underlying contract that expressly address the issues raised by the Supreme Court’s holding.

**Unpredictable Consequences of Indian Supplier Bankruptcy**

As is the case when doing business in any number of other jurisdictions, including the United States, an Indian supplier’s bankruptcy can have a catastrophic effect on the US customer and can significantly impact the enforceability of the operative outsourcing contract. This is because a party’s bankruptcy can significantly alter the relationship of the parties by operation of law to effectuate the purpose of bankruptcy laws which is to maximize the value of the debtor’s estate. The outcome of bankruptcy proceedings in India can be unpredictable and can have dramatic impact on the US customer. If the Indian supplier becomes a debtor in bankruptcy, a key question concerns the status of the outsourcing contract, including any IP or proprietary technology that may have been licensed, assigned or otherwise transferred to or from the Indian debtor in bankruptcy. Can a US customer unilaterally terminate the outsourcing contract and all underlying licenses to customer IP or proprietary technology once the Indian supplier files for bankruptcy in India? If not, what rights and duties will the Indian debtor-supplier continue to have with respect to the outsourcing contract and any US customer’s IP? Can the Indian debtor-supplier unilaterally terminate the outsourcing contract or otherwise cut off the US customer access to the supplier’s IP that might be critical for the US customer’s operations? What legal recourse is available to a non-debtor contract party in India? These are important considerations from a US customer’s perspective that must be assessed and addressed beforehand to try to mitigate the unpredictable consequences of an Indian supplier’s bankruptcy.

A US customer should be aware that India’s bankruptcy laws are antiquated, complex and inefficient compared to the US bankruptcy laws. For example, India’s bankruptcy laws do not provide any specific guidance as found in Section 365 of the US Bankruptcy Code with respect to the respective legal obligations and rights of licensors and licensees of IP in bankruptcy. Lack of available protections or predictability for non-debtor contract parties under Indian bankruptcy laws, therefore, can potentially create real vulnerabilities for the US customer.

The unanticipated consequences of the Indian counterparty’s bankruptcy may be avoided if the US customer is able to timely terminate the operative outsourcing contract pre-bankruptcy, which of course is usually practically feasible only if the US customer remains vigilant about the Indian supplier’s performance and financial health on a routine basis. Care should be taken in drafting the outsourcing contract to include effective mechanisms to provide early warning signs to the US customer, such as performance benchmarks, periodic financial reporting and “no material adverse change” certification requirements, as well as escrow arrangements and security interests in critical licensed IP, as applicable and appropriate. In addition, payment terms, licenses and any on-going obligations of the parties under the operative contract should be structured in a manner so as to minimize the impact of the Indian counterparty’s bankruptcy on the US customer’s interests.

**Enforceability of Third Party Beneficiary Rights**

Unlike the US, India does not expressly recognize any established “third
party beneficiary” law that entitles a third party to enforce contract terms that exist in contracts to which it is not a party but which are either expressly or implicitly for such third party’s benefit. A third party beneficiary means an intended, and not just an incidental, beneficiary of a contract. While there is no statute in India that expressly permits or prohibits an intended third party beneficiary from enforcing such a contract, the general rule under Indian law to date is that no right under a contract may be enforced by a person who is not a party to the contract unless certain established exceptions apply. In other words, Indian courts have adopted a rather strict interpretation of the doctrine of privity of contract based on English common law that entitles only contracting parties to enforce rights, and hence recover damages, under the contract. Indian courts have, however, acknowledged certain exceptions to the privity doctrine based on the principles of equity but these exceptions are very limited and narrow in scope.

This somewhat strict application of the privity doctrine in India can potentially create a significant enforcement gap from a US customer’s perspective. To illustrate this point, consider an R&D services outsourcing contract between a US company (“US Co.”) and an Indian supplier pursuant to which the supplier will provide services to US Co. and US Co.’s affiliate (“US Affiliate”) and the supplier’s indemnities will extent to both US Co. and US Affiliate receiving the services under the outsourcing contract. In this hypothetical, US Affiliate would be deemed an intended third party beneficiary under the contract. If US Affiliate were to end up in a legal proceeding in an Indian forum, voluntarily or involuntarily, to independently enforce a supplier indemnity for the affiliate’s benefit, it could well be deemed not to have legal standing or sufficient rights or interests to sue under the contract. Furthermore, for the same reasons relating to standing, rights in interest, actual damages, and so forth, it is equally as questionable whether US Co., although a party to the contract, could enforce the contractual supplier indemnity for the benefit of US Affiliate in an Indian forum.

It is therefore prudent to determine upfront the intended third party beneficiaries and where feasible, structure the contractual relationship in a manner that would adequately equip such beneficiaries with direct enforcement rights in India. Alternatively, the operative outsourcing contract could be assigned to a third party beneficiary in which case the assignee beneficiary would be able to directly enforce the contract.

Conclusion

While outsourcing to India can be a powerful means of streamlining IT and business functions that can yield enormous cost savings, increased efficiencies and improved service quality, it also demands more complex and robust risk assessment and management because of the unique and heightened risks inherent in cross-border outsourcing arrangements and the potential challenges of enforcing rights and remedies in foreign jurisdictions with different legal systems. These risks and challenges can be managed, however, with thorough due diligence, objective supplier selection, and the careful assessment and treatment of the issues discussed above in an outsourcing contract that memorializes all underlying business terms and provides real and practical protections and enforcement mechanisms to a US customer.