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## India's bilateral investment treaty negotiations – the stalemate and the way forward

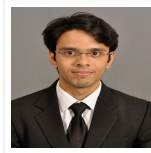
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Recently, India [announced](http://pib.nic.in/newsite/PrintRelease.aspx?relid=147849) (<http://pib.nic.in/newsite/PrintRelease.aspx?relid=147849>) that its Union Cabinet had approved signing of a new Bilateral Investment Treaty [BIT] with Cambodia, another South-Asian country. The IA Reporter also reported that India and Brazil have also concluded (referring to finalization of draft) the much-anticipated BIT. These are important events as the new BIT with Cambodia as well Brazil is supposedly based on the controversial Model Bilateral Investment Treaty 2015 ([Model BIT](http://indiainbusiness.nic.in/newdesign/upload/Model_BIT.pdf) ([http://indiainbusiness.nic.in/newdesign/upload/Model\\_BIT.pdf](http://indiainbusiness.nic.in/newdesign/upload/Model_BIT.pdf))). However, while the both the BITs are yet to be signed (no press release by Indian Government yet confirming that they have been signed), many developed or capital-exporting nations have shown reluctance in agreeing to the clauses as contained in the Model BIT citing the low level of protection offered to investments and high threshold of compliance before bringing a dispute before an international tribunal. While such reluctance on the part of developed countries is not surprising, it is important to acknowledge the merit in some of these concerns.

India has been reevaluating its BIT's since 2012 when India started receiving large number of arbitration notices due to retrospective taxation and cancellation of 2G licenses by the apex court. Last year, after much discussion and debate, India released the new Model BIT replacing the 2003 Model Bilateral Investment Promotion Agreement (**Model BIPA**). Subsequently, India gave a notice of termination of the existing BIPAs to 57 Countries and also requested 25 others for joint interpretational statements. India started its renegotiation for new BITs with a number of countries including US, Canada, Australia, Brazil & Cambodia and also with EU based on its Model BIT.

### What has changed in the 2015 Model BIT?

The new Model BIT, as per the government, balances the protection given to the foreign investments with the sovereign right of the country to take fiscal and regulatory measures. However, while the revision of the Model BIPA was necessary, the contents of the BIT have been a subject of unending controversy.

The first major change is the complete **exclusion of taxation measures** from the BIT. The blanket and absolute exclusion of taxation measures from the scope of the BIT has not gone down well with many countries. While most of the treaties exclude tax measures from the scope of treaty but make an exception for expropriation and national treatment clauses. However, there is no such exception in this model BIT. It has also been noted that India is not agreeable to any deviation from this position, probably, due to the large number of claims it had to face due to the retrospective tax amendments.

Further, the **threshold of protections** has also been substantially altered. Instead of the vague (and avoidable) standard of Fair & Equitable Treatment (F&ET), the Model BIT provides for protection of investments against denial of justice, fundamental breach of due process and manifestly abusive treatment. The latter two protections are merely corollary of the protection against denial of justice. While the omission of F&ET is acceptable, its replacement with protection against denial of justice is not. The protection against denial of justice has a very high threshold of breach which is evident from the *White Industries* award where a delay of 9 years in enforcement of an award was considered not to be a denial of justice. Therefore, the

developed countries argue that it would be very difficult for an investment to remain reasonably protected when the standard of breach by the host state is exceptionally high.

Also, the clause of **Full Protection & Security (FPS)** has been explained to be limited to physical security of the investments and investors in relation to those investments. There have been cases in past where such a clause has been expansively interpreted to include all kind of vague and unintended protections.

On the issue of **expropriation**, there has been conflict of views between the countries regarding the clause which requires the investor to approach domestic courts before moving to an international tribunal. It also keeps the judgements of courts having expropriating effect excluded from the scope of the BIT.

The **dispute resolution** clause has also been a bone of contention. The requirement that investors must pursue the domestic remedy for at least five years before bringing a claim has not gone down well with other countries. This is a very high threshold of compliance that nearly defeats the purpose of the treaty.

The Model BIT also excludes **Compulsory licensing & revocation of Intellectual Property Rights (IPR)** from the scope of BIT i.e. a foreign investor against whom such an action is taken by the government will not have a recourse to international arbitration under the BIT. This is one of the biggest concerns raised by foreign investors and nations.

The **Most Favoured Nation (MFN)** clause has also been omitted. This provision provides protection to investments against discrimination by the host state. However, in past, this provision has been used extensively and successfully by investors to engage in treaty shopping. There has been a movement away from this provision as more and more developing countries oppose the clause for its rampant misuse.

Before we highlight the concerns or suggest any way forward, it is important to acknowledge that India is not alone in its quest to limit the protections offered to foreign investors or move towards a BIT mechanism that considerably asserts the nation's sovereign right to regulate. Many nations in Latin America, Africa and Asia-Pacific have made their intentions to go the same path. It has been argued, quite successfully, that developing countries require a higher degree of regulatory discretion to govern their resources equitably and therefore, a higher threshold of protection to foreign investors may not be the best option.

#### **What are the concerns?**

Coming back to the Model BIT, there is no doubt that it has been a subject of worry for both- domestic and foreign investors. The foremost concern among domestic investors is that the Model BIT fails to contemplate India's position as a capital exporting nation. Indian companies are expanding and investing significantly in markets such as Africa, Iran, middle-east and other smaller countries. These countries are plagued with recurrence of political instability, civil uprisings and in some cases, even armed rebellions. With a BIT that substantially reduces the protection available to investments, they will find themselves in a relatively inferior position to enforce their claims against such countries in case their investment is harmed. For instance, recently, an Indian company- Fleming, won an investment [claim](http://www.italaw.com/sites/default/files/case-documents/italaw7709_3.pdf) (http://www.italaw.com/sites/default/files/case-documents/italaw7709\_3.pdf) of €20 Million against Poland for breach of the requirement to treat its investment fairly & equitably and for unlawful expropriation. If the claim was under a new BIT on the lines of Model BIT, it would have been difficult for Fleming to receive compensation for denial of justice because of the high threshold of breach it requires. Even compensation under the Expropriation clause may have been limited. Therefore, smaller countries like Cambodia and struggling economies such as Brazil which are capital importing in nature will be more than willing to sign such a treaty that gives them more regulatory freedom while putting less burden on them.

Similarly, the developed countries and investors thereof are apprehensive about the Model BIT and the lower threshold of protection it offers. For instance, there have been strong reactions to the five year period required to exhaust domestic remedies. Similarly, as per these countries, the blanket exclusion of the taxation measures is unwarranted, in all reasonableness. They are not pleased with most of the alterations in the standard of protections- omission of MFN & F&ET and the limitation placed on FPS clause. They are also unhappy with the exclusion of compulsory licensing and revocation of IPR from the scope of the BIT (something India says is non-negotiable).

#### **The way Ahead**

It must be clarified at the outset that there is no need for a total reconsideration by India of its position based on Model BIT. The reluctance of these developed nations to accept the omission of MFN and limiting of FPS to physical security of investors and investments is unwarranted. There is no need for India to reconsider its position on the MFN clause as the omission was required as it had become a means of treaty shopping whereby the notion of *bilateralism* in a bilateral treaty was rendered useless. The limiting of FPS clause to physical security is in line with the awards of various tribunals. While there is some conflicting jurisprudence, but India is well within its right to put a limitation on it. That said, India needs to recalibrate its position with its intention to provide a stable and secure environment to foreign investments. One suggestion which has been consistently offered to government is to link and limit the protections to international law or customary international law to be precise instead of incorporating extreme thresholds like denial of justice. This should be acceptable to US and other developed countries as such a clause is present in North American Free Trade Agreement ([NAFTA](http://www.sice.oas.org/trade/nafta/chap-111.asp) (http://www.sice.oas.org/trade/nafta/chap-111.asp)) to which US is a party. Secondly, it would be justified and reasonable for India to assure foreign nations that their investments will not be subject to expropriation by taxation measures and therefore, a clause to that effect can be incorporated. Further, the dispute resolution clause needs to be made less onerous and more pragmatic. It is futile to seek avoidance of claims by creating onerous or difficult pre-requisite to claims. Instead, Indian government should seek to avoid claims by providing a stable and robust legal and business environment through domestic reforms which are implemented at a steady pace. While there have been steps to that effect, one is yet to see the promised results.

With India and Iran contemplating signing of a BIT by the year end, it is expected that India will amend its stance to protect its own investments flowing into Iran- a relatively volatile jurisdiction. If that happens, the developed countries may expect India to alter its position. However, the onus is also on developed countries to accept and recognize the relatively higher bandwidth of regulatory discretion needed by developing countries, especially India. Being a developing country, it needs the right to regulate investments in its territory in accordance with its evolving commercial environment. And with India's share in international trade growing steadily, it is time for these countries to sit down with India and find a mutual ground.

However, before we conclude, it needs to be reasserted here that the Model BIT and the strong position of India on it merely highlights the growing opposition among developing countries to the present regime of BITs or the higher threshold of protections that these BITs offer to foreign investments. The authors believe that this signals a possible movement towards the revival of Calvo Doctrine- *foreign investors shall get the same protection that is available to the domestic entities*. Clearly, while we see the world turning into a global village, the geo-political and the socio-economic realities differ in

every state. Such geo-political and socio-economic realities play a significant role in the conduct of the state and level of protections it wishes to offer. While the present BIT regime, on the face of it, may sound an attractive proposition, considering the need of each individual state, going forward, the authors see marked resistance to such treaties, if not in their entirety, then at least to the level of protection they offer to foreign investments.

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