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BILATERAL INVESTMENT TREATIES: THE CHANGED INDIAN PERSPECTIVE

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Abstract

A country, in order to prosper, requires economic growth as the key factor for growth. For economic growth, the business has to be feasible not only at the national level but also at the international level which includes a proper cooperation between the business houses and state authorities. One of the key results of this relationship is the emergence of bilateral investment treaties (BIT). With the advent of globalization, the role foreign investors have to play in the business /economic scenario of any country cannot be ignored. BITs play an instrumental role in looking after the foreign investment and the risks that come along with it. The new times have changed the outlook towards such investments and have led to devising new alternatives and dispute resolutions like arbitration. This paper shall be a comparative analysis between the old and new BIT and what impact globalization has had on the framing of the latest BIT. It shall also dwell deeper into the solutions that can be suitable for the benefit of both the investors and the state.
Keywords: Globalization, investment, arbitration.

1.Introduction

The aims of having a better (stable) economy is something every nation aspires to have and policies are also made keeping this agenda in mind. The economy is one of the basic factors that indicate any country's development. The Bilateral Investment Treaties are tools in the hands of the states and companies to negotiate a midway to keep both the parties' interests at an equal level, investor protection being the most important reason behind the introduction of these treaties. The Indian economy has seen a boom after the economic reforms of liberalization of 1991. Hence, the relationship between the state and investors was different before and after the year 1991. The BITs were a necessity to provide assurance to the foreign investors of a safeguard and to give the country the impression of being investor-friendly. As time progressed, this protection has been modified by the investors as to their benefits, hence, showing that the deficiency lies in the way the treaties are framed. This led to some introspection on the part of the Government which has since led to the making of a new model draft BIT in 2015.

2. Research Problem

This paper shall dwell deeper into the evolution in the investment law strategies taken up by the Indian Government and the conditions which led to it along with the comparison of the old and the new draft BIT.

3. Review of the Relevant Literature

The article titled "India and Bilateral Investment Treaties- A Changing Landscape" by Dr. Prabhash Ranjan was of great help in writing this paper. The 32-page text gives a complete chronological study of the investment law regime of India and how it has evolved. It also looked into the most important case named *White Industries v. Union of India* that has been responsible in changing the Indian perception towards the policy making related to foreign investments.

The paper "Comparing Investment Provisions in India's FTAs with India's Stand-Alone BITs-Contributing to the Evolution of New Indian BIT Practice" by Dr. Prabhash Ranjan contains the important research related to the various provisions of the BITs and how they have been dealt with related to India's FTAs and BITs.
The paper 'The politics of corporate taxation in the European Union" by Radaelli gives a thorough research on the subject of tax treaties and how the BITs are not directly responsible for the foreign direct investments (FDI) but are more often a means of tax-evasion through the various clauses of the BIT.

4. Methods

The method adopted by the research paper is qualitative in nature and secondary data has also been used.

4.1 The Indian Economy- Policy Outline

The change in the perspective of the investment law strategies has a link with the governmental economic policy reforms. The times before the 1990s in the Indian economy were such that they were not welcoming for foreign investors, as the main focus of the economic policy then was to encourage the functioning of the industries at the national level before competing with the international ones. The ideology at that time while forming the reforms was that the Indian economy needed to have a strong base of the national industry and hence, there were limitations if anyone from outside India invested. Laws having a detrimental impact on foreign investment were enacted such as the Foreign Exchange Regulation Act (FERA) (Chaudhary, 1979), which required a foreign company to convert foreign equities into minority holdings. Only if a foreign company diluted its equity to a minority holding of 40 percent would it get national treatment.[1]
This led to transnational corporations such as IBM and Coca Cola exiting India (Kumar, 1998).
Low economic growth in the 1970s led to limited liberalization and deregulation in 1980s (Virmani, 2005). Somewhat receptive attitude towards FDI was adopted by introducing flexibility in foreign ownership and exceptions to the 40 percent ceiling rule (Kumar, 1998).
There was paradigm shift from this nationalistic view to a more liberalized mindset of the government after the 1990s. There was a severe economic crisis which led India to the opening of the economy at an international level. Bold measures aimed at liberalizing FDI included: automatic approval of FDI up to 51 percent in high priority industries and 100 percent foreign equity in the energy sector; setting up of a Foreign Investment Promotion Board (FIPB) to act as a single window clearance for foreign investment proposals; opening up new sectors such as mining and telecommunications for foreign investment, and; amending the foreign exchange regulation act to treat foreign companies with more than 40 percent ownership on par with fully owned Indian companies (Kumar, 1998).

This led to the enactment of the Foreign Exchange Management Act (FEMA) in order to look into the foreign investments. The various economic legislations were the amendment of the Indian Patent Act introducing product patent regime for pharmaceuticals due to WTO obligations; amendment of the Customs Tariff Act 1975 in order to introduce WTO-consistent provisions on anti-dumping; enactment of a Competition Act in 2002 replacing the out-dated Monopolies and Restrictive Trade Practices Act; the enactment of the Special Economic Zone (SEZ) Act in 2005 aimed at the establishment of special economic zones in order to boost exports; the enactment of a new Arbitration and Conciliation Act in 1996 aimed at consolidating and amending the law related to domestic arbitration, international commercial arbitration and enforcement of foreign arbitral awards (Ranjan, 2014).

[1] Department of Industrial Development, Ministry of Industry, 'Industrial Policy' (23 December 1977) <http://www.dcmsme.gov.in/policies/iip.htm#Indus3>

4.2 The Indian Model BIT

The Indian Model BIT 2003 had the main objectives of:

"Desiring to create conditions favourable for fostering greater investment by investors of one State in the territory of the other State; Recognising that the encouragement and reciprocal protection under International agreement of such investment will be conducive to the stimulation of individual business initiative and will increase prosperity in both States;" (India's Model BIT, 2003)

It can be clearly seen that the definition of investment is asset-based which includes:

"(i) movable and immovable property as well as other rights such as mortgages, liens or pledges;
(ii) shares in and stock and debentures of a company and any other similar forms of participation in a company;
(iii) rights to money or to any performance under contract having a financial value;
(iv) intellectual property rights, in accordance with the relevant laws of the respective Contracting Party;
(v) business concessions conferred by law or under contract, including concessions to search for and extract oil and other minerals."[2]

Article 4 of the BIT discusses about the most-favoured nation (MFN) clause which states that the contracting parties shall not give a treatment less favourable than the one given to a third State although the exception being of any benefit of treatment resulting from any matter existing or future customs, union or similar international agreement to which it is or may become a party, or any matter pertaining wholly or mainly to taxation.[3] An important aspect of the MFN provision in Indian BITs is its limitation to applying to the post-establishment phase. This is evident from the fact that granting MFN treatment is not linked to 'establishment', but only to those stages of investment, which follow after an investment has been made. In other words, at the stage of entry or admission, India has the policy space of treating different foreign investments in a different manner without violating the MFN provision (Ranjan, 2015).

Article 5 discusses the concept of expropriation-both direct and indirect. Article 9 discusses about the Settlement of Disputes between an Investor and a Contracting Party. It is mentioned in the BIT that "in case any dispute cannot be settled within six months from the time the dispute arose, it shall upon the request of either Contracting Parties be submitted to an arbitral tribunal."[4]

4. 3 White Industries v. Union of India

Prominent companies like Cairn Energy, Vodafone UK and Nokia have raised investment-related disputes under the respective BITs signed by India, with the home countries.[5] So, far in the Indian context, investment treaty arbitrations have been instituted, or considered as legal recourse in response to cancellation of telecom licenses and imposition of retrospective taxes.
White Industries is an Australian Company which entered into a mining contract with Coal India Ltd. in 1989. In 1999, various disputes pertaining to mining were referred to arbitration.

[2] Article I (b) of the Indian Model BIT 2003
[3] Article 4 (3) (a) & (b) of Indian Model BIT 2003
[4] Article 10(2) of Indian Model BIT 2003
[5] 'Vodafone turns to Arbitrators in Seven-Year Old Indian Tax Dispute', Financial times, May 7, 2014, available at http://www.ft.com/intl/cms/s/0/21f91f9c-d5fa-11e3-a017 00144feabdc0.html#axzz3nslIpyCe accessed on December 25, 2015.

The arbitral tribunal issued the award in favour of White Industries for approximately four million Australian dollars.[6]

This award was challenged before the Calcutta High Court by Coal India, while parallel proceedings for the enforcement were instituted by White Industries in the Delhi High Court. The Delhi High Court stayed the enforcement proceedings in view of the proceedings pending before the Calcutta High Court.[7] This interim order was appealed before the Supreme Court of India. Failing to achieve an expedited adjudication of its issues either before the Supreme Court, or the two High Courts, White Industries invoked the dispute resolution clause under the BIT signed between India and Australia. White Industries inter alia claimed violation of the Most Favourable Nation clause in the India-Australia BIT.[8]

The arbitral tribunal gave the award in favour of the claimant only on its claim of violation of the MFN clause. The main reason being that the effective means of asserting claims and enforcing rights, has been denied to the investor. This could be seen as there was a delay in the proceedings pending before the Supreme Court. The tribunal, using the MFN clause, incorporated an 'additional' liability of providing effective means; an obligation imposed on India under another BIT entered with Kuwait (Ranjan, 2012).

This award is significant because it is the first known ITA-adverse award against India. It was followed by a number of foreign corporations slapping ITA notices against India[9] Vodafone under the India-Netherlands BIT for a retrospective taxation measure; Deutsche Telekom under the India-Germany BIT over a cancelled satellite venture; ByCell under the India-Cyprus BIT for withdrawal of the approval to grant telecom licenses; and Devas multimedia under the India-Mauritius BIT.[10] On the basis of these notices, India concluded that the current investment treaty regime unfairly restricts her sovereign right to regulate (Mayaram, 2014).

4.4 The Draft Model BIT 2015

Contrary to the notion that the actual role of the BIT is to promote foreign investment, various scholars have stated that BITs do not have much impact on investments. For instance, Dagan asserts that the use of treaties to promote foreign direct investment is "a myth". He claims that since a parent country could unilaterally adjust its tax policy to eliminate distortions caused by differing parent and host country tax policies, promotion of efficiency plays little role in treaty formation. Instead, Dagan suggests that treaties are intended to reduce administration costs, reduce tax evasion, and to extract tax concessions from treaty partners (Dagan, 2000). The double taxation objective has been dismissed in favor of the view that tax treaties are geared towards reducing tax evasion (Radaelli, 1997).

The new draft model of the Indian BIT has been more inclusive of definitions given out in a more lucid way. It has been divided into six chapters which include (1) Preliminary, (2) Obligation of Parties, (3) Investor, Investment and Home State Obligations, (4) Dispute Settlement, (5) Exceptions and (6) Final Provisions respectively. These sections include a total of 24 articles.

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[6] Bilateral Investment Treaty Awards- The Indian Context,2005 Background Paper of International Conference on Arbitration in the Era of Globalization, Indian Council for Arbitration, New Delhi, December 11-12, 2015
[7] Ibid.
[8] Ibid.
[9] For a list of cases, see 'Investment Treaty Arbitration, Respondent State, India' <http:// www.italaw.com/cases-by-respondent?field_case_respondent_tid=622>
[10] JWIT_RANJAN_2015

The Preamble states the main objective to be that of :

> "Desiring to promote bilateral cooperation between the Parties with respect to foreign investments; and
>
> Reaffirming the right of Parties to regulate Investments in their territory in accordance with their Law and policy objectives including the right to change the conditions applicable to such Investments; and
>
> Seeking to align the objectives of Investment with sustainable development and inclusive growth of the Parties"[11]

The Definition of "Investment" in the BIT is enterprise-based[12] rather than being asset based. It excludes the assets of the enterprise which include:

"(i) any interest in debt securities issued by a government or government- owned or controlled enterprise, or loans to a government or government owned or controlled enterprise;
(ii) any pre-operational expenditure relating to admission, establishment, acquisition or expansion of the Enterprise that is incurred before the commencement of substantial and real business operations of the Enterprise in the Host State;
(iii) portfolio investments;
(iv) claims to money that arise solely from commercial contracts for the sale of goods or services;
(v) Goodwill, brand value, market share or similar intangible rights;
(vi) claims to money that arise solely from the extension of credit in connection with any commercial transaction referred to in (v) above;
(vii) an order or judgment sought or entered in any judicial, regulatory, administrative, or arbitral proceeding;
(viii) any other claims to money that do not involve the kind of interests or operations set out in the definition of Investment in this Treaty."[13]

The Law Commission's report reviewed the draft Model BIT[14] and noticed the absence of the MFN clause in the draft Model. The Commission released this to be an intentional step after the White Industries case where under the MFN clause, the foreign investor was able to read additional favourable standards into the India- Australia BIT which were not negotiated before or agreed upon. It is an intentional step by the Government to reduce the chances of 'treaty shopping', simultaneously it shall protect the Indian as well as the foreign investor from being exposed to the discriminatory treatment from the host state. Since Indian BITs contain very limited exceptions,[15] an important question is whether a foreign investor can rely on these broadly worded MFN provisions to borrow beneficial substantive provisions from another BIT. Indeed this is what happened in *White Industries*. The tribunal allowed White Industries to rely on the MFN provision to import a more favourable substantive provision related to 'effective

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[11]Draft Model BIT 2015 available at https://mygov.in/sites/default/files/master_image/Model%20Text%20Text%20for%20the%20Indian%20Bilateral%20Investment%20Treaty.pdf accessed on October 15, 2015.

[12] Article I (1.6) of the Draft Model BIT 2015
[13] Article I (1.5) of Draft Model BIT 2015
[14]Draft Model BIT 2015 available at https://mygov.in/sites/default/files/master_image/Model%20Text%20Text%20for%20the%20Indian%20Bilateral%20Investment%20Treaty.pdf accessed on October 15, 2015.
[15] Some Indian BITs have narrower or broader exceptions than the two exceptions pertaining to customs union and taxation. For instance, the India-Russia BIT does not contain the exception related to taxation.

means of asserting claims and enforcing rights' given in the India- Kuwait BIT into the India-Australia BIT.[16]

The 2015 draft Model BIT does not contain a Fair and Equitable Treatment (FET) provision. Instead, it contains a provision titled 'Standard of Treatment', which puts the host State under an obligation not to subject foreign investment to measures which constitute a denial of justice under customary international law, to un-remedied and egregious violations of due process, or to 'manifestly abusive treatment involving continuous, unjustified and outrageous coercion or harassment'. The absence of an FET provision will safeguard India's right to regulate by minimizing the possibilities of unexpected restrictions on its regulatory power that can be brought about by broad interpretations of an undefined FET (Ranjan, 2014).

The 2015 draft Model BIT, on expropriation, provides that an indirect expropriation requires evidence that there has been permanent and complete, or near complete, deprivation of the value of the foreign investment and of the investor's right of management and control over investment.[17] Thus, the treaty not only provides for the 'substantial deprivation'-test to determine indirect expropriation, but also requires in Articles 5.2 (i) and (ii) that this deprivation should be both economic and legal.[18]This solves one key problem related to the method of determining 'substantial deprivation' (Ranjan, 2014).

The 2015 draft Model BIT also maintains a balance between the host State's right to regulate (adverse economic harm will not be enough to constitute expropriation) and investment protection (the host State is prohibited from transferring the cost of pursuing a public purpose on to foreign investors if the regulatory measure results in substantial deprivation of foreign investment). This is yet another example of India emerging as a 'rule-maker' in international investment law.[19]

Furthermore, the 2015 draft Model BIT also exempts non-discriminatory regulatory measures designed and applied to protect legitimate public welfare objectives, such as public health and the environment from the ambit of expropriation. This is too sweeping and tilts the balance in favour of the host State's right to regulate. This provision is subject to abuse by the host State by, for example, structuring all regulatory measures as measures aimed at the fulfillment of public welfare objectives, thus avoiding a finding of indirect expropriation notwithstanding the impact of the measure on foreign investment.[20].

Another interesting point to be noted is any kind of tax related issues have been left out in the draft Model 2015 and the biggest reason behind it can be the Vodafone case[21] which is still pending before the arbitration tribunal. It was filed against India for retrospective taxation.

The 2015 draft Model BIT contains a separate chapter on exceptions covering both general and security exceptions. Article 16 contains general exceptions with a long list of permissible

[16] *White Industries Australia Limited v Republic of India*, UNCITRAL, Final Award (30 November 2011). paras 11.2.2 – 11.2.8

[17] 2015 draft Model BIT (n 14) art 5.2 (i) and (ii).

[18] See *Chemtura Corporation v Government of Canada,* UNCITRAL, Award (2 August 2010) para 247.

[19] Ibid.

[20] On this point also see *Azurix Corp v The Argentine Republic*, ICSID Case No ARB/01/12, Award (14 July 2006) para 310.

[21] Vodafone News Release, 'Vodafone Serves Notice Against Indian Government Under International Bilateral Investment Treaty', (17 April 2012) <http://www.vodafone.com/content/index/media/group_press_releases/2012/bit. html> accessed 18 December 2015.

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objectives, which includes not just health, environment, public order, public morals but also measures 'improving working conditions'[22] and 'ensuring the integrity and stability of its financial system, banks and financial institutions'.[23]

India's stand-alone BITs do not provide an exhaustive NPM provision and thus do not present an adequate textual basis to balance investment protection with the host country's right to regulate for non-investment issues such as health, environment etc. (Ranjan, 2014)
The Report also mentions that there is no provision of the appellate review of the award in the draft Model BIT. This might pose difficulties for Indian investments abroad. The Commission has brought forth its concerns and also recommended various amendments that should be taken into view for an overall better prospective. Article 14.3 mandates the pre-condition of exhaustion of all domestic remedies present in the host country; Article 14.2 (ii) (a) disallows such claims to be adjudicated by arbitration. The Commission has also recommended the removal of certain provisions which cause unfair partiality against the investor.[24]

Conclusion

The paper has been written with an intention to see the evolution of Indian investment law pertaining to bilateral investment treaties. As nothing is static, the economic, political conditions also evolve. These changes show the change in the mindset which in this case related to a change in the Government's outlook towards foreign investment. The complete change of thinking from inward protection of business to the liberalized nation which is investor friendly was a great step towards a change. Now, with such change come certain dangers and the BIT is the tool that has been instrumental with the intention to solve a purpose to attract more foreign investments but it should be seen that it should not be done at the pretext of making the country itself vulnerable in any way. The proper balance needs to be struck between the investor's suitable conditions and the host nation's sovereignty. An equation where both of them are at the same grounds is idealistic but it surely is a direction towards which we can move. The changes that have occurred completely show that the Indian Government has learnt from its mistakes and the result can be seen in the draft Model of 2015.

[22] 2015 draft Model BIT (n 14) art 16.1 (vi).
[23] ibid art 16.1 (ii).
[24] Ibid.

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