
THE RELATIONSHIP BETWEEN NATIONAL FDI LAWS AND THE IIA FRAMEWORK

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ABSTRACT

India as part of the overall regulatory framework for Foreign Direct investment (FDI) in India, in addition to India's domestic FDI laws. The researcher aims to clarify this concept at the beginning, which examines India's current Investment Agreements (IIA) framework. With the adoption of the new Model Bilateral Investment Treaty (BIT) 2015, India is undergoing a regulatory shift in terms of its IIA programme. Consequently, it has already terminated 54 BITs and plans to renegotiate existing BITs in accordance with the 2015 Model BIT¹. In light of the current situation, the research will study and examine India's IIA Framework solely in terms of the Model BIT 2015, with IIAs.

¹ International Investment Navigator, Investment Policy Hub, UNCTAD, <https://investmentpolicyhub.unctad.org/IIA/CountryBits/96> (last visited: Feb. 12, 2023)

INTRODUCTION

According to the UNCTAD report, the international community has given the national investment laws little consideration², a similar circumstance exists in India. A report found that 108 countries had adopted national investment laws to promote and regulate foreign investment³. National investment laws and bilateral investment treaties (IIAs) should form the country's fundamental legal framework for foreign investment.

However, two distinct approaches can be distinguished: the adopting national investment laws and adopting multiple investment laws or regulations based on government policies. In order to align the national regime with the IIA framework and vice versa, however, both must undergo extensive review and reform.

Although it is commonly believed that national investment laws and IIAs are entirely distinct, it is undeniable that they share-related policy instruments⁴. With globalisation and increased cross-border investment, the majority of nations started to rebalance the IIA structure (by adopting new model BITs and renegotiating the same). Common objectives of such changes include the treatment of foreign investment, the rights and responsibilities of investors, the pursuit of sustainable development objectives, and the resolution of investment disputes. In recent years, changes have occurred in the national policy framework regarding foreign investment. In the majority of instances, however, it was observed by UNCTAD that the national investment laws of the countries shared similar goals and objectives with their respective IIA framework.

It was also discovered that the majority of foreign investment laws in Asian nations share common policy goals. Moreover, while national investment laws and the IIA framework share similarities, the two instruments differ significantly in their approach to incorporating specific laws and drafting particulars.

National investment laws typically focus solely on foreign investment, whereas the IIA framework must consider a vast array of international obligations. Consequently, it becomes

² World Investment Report, 2017, UNCTAD, https://unctad.org/en/PublicationChapters/wir2017ch3_en.pdf#page=9

³ Id. See also, Investment Laws, Investment Policy Monitor, UNCTAD, Special Issue (2016), https://unctad.org/en/PublicationsLibrary/webdiaepcb2016d5_en.pdf.

⁴ Id.

more crucial to advocate for parallel reform measures in the two instruments. If provisions of national investment laws are not reflected in international investment agreements (IIAs), or vice versa, this can result in costly (contentious) outcomes between contracting nations. Consequently, contracting nations should collaborate to evaluate the content of the IIA and national investment, and reforms are required to align the two instruments in terms of investment-related policies.

Investment Agreements

IIAs establish a regulatory framework that is distinct from the domestic regulatory framework for foreign investments. IIAs could be viewed as a means for the host nation to channel foreign investment. These indicate that the host nation is prepared to protect the investments of foreign investors. Consequently, the IIA regime should complement the domestic regulatory structure. The IIA regime must be followed as part of the overall FDI regulatory framework.

Any inconsistency between the provisions of an international investment agreement and the domestic regulatory framework would be a violation of investment protection. Consequently, it is necessary to put the IIA provisions to the test in order to identify any gaps between domestic laws and the IIAs and to examine individual provisions in order to comprehend the investment protection offered by the IIA regime.

In the early days of foreign investment, when it was primarily viewed as an extension of trade, a normative approach to protecting foreign investors in times of crisis was neglected. Since the post-colonial era, this area of law has undergone significant evolution, and IIAs have emerged as a structured framework for providing a normative approach to foreign investment and its protection. The inclusion of a clause prohibiting discrimination guarantees both national treatment and most-favored nation (MFN) treatment. Pessimists argue that international law already contains such safeguards in the form of private and public investment insurance and guarantees.

A counterargument to such a claim could be that these protections are not always available in the absence of an agreement to that effect. Since public investment guarantees are contingent on the policies of the host country, which are in turn contingent on development objectives, and private insurance is typically expensive.

The total number of international investment agreements has reached 3,322 (including 2,200 bilateral investment treaties and a variety of other regional, bilateral, and interregional agreements), and the number of cases referred to international investment tribunals has increased dramatically in recent years⁵.

IIA FUNDAMENTAL PRINCIPLES

Typical IIAs consist of three sections, one of which is the "substantive clause." This section contains the protection standard for foreign investors, also known as the fundamental principles of international investment law⁶.

Protection against indirect expropriation, discrimination against domestic foreign investors (most favoured nation and national treatment), fair and equitable treatment (FET), full protection and security, and proper capital flow management are the most important fundamental principles of international investment law⁷. The researcher endeavours to explain the principles of international investment law so as to provide context for the study of the relationship between the two coexisting legal frameworks, namely IIAs and the domestic FDI regulatory framework. Rudolf Dolzer and Christoph Schreuer independently elaborated and explained the aforementioned principles in their work⁸.

The researcher has emphasised 'indirect expropriation,' 'FET,' 'most favoured nation,' and 'transfer of funds.' Given that the study is predominately based on Indian FDI laws, only those principles whose violations frequently occur in Indian investment disputes are selected. In the context of foreign investment, expropriation has traditionally been regarded as one of the most important protection standards⁹. It has become one of the most essential principles of international investment law over time¹⁰.

In recent years, however, the concept of expropriation has become gradually more indirect. Indirect expropriation occurs when the host state seizes the investor's property without

⁵ Yong Kyun Kim, States Sued: Democracy, the Rule of Law, and Investor Settlement (ISDS), INTERNATIONAL DOI: 10.1080/03050629.2016.1173546

⁶ DOLZER & SCHREUER, (2016).

⁷ Id.

⁸ Id.

⁹ D. W. Bowett, State Contracts with Aliens: Contemporary Developments on Compensation for Termination or Breach 59 BYIL (1988)

¹⁰ DOLZER & SCHREUER, (2016), at 102.

compensation through regulatory means¹¹.

According to Schreuer, it is difficult to establish indirect expropriation before the court. Although the early cases of Norwegian Shipowners' Claims and Case Concerning Certain German Interests in Polish Upper Silesia acknowledged the concept of indirect expropriation, with the emergence of new economic orders, the list of elements that could qualify as indirect expropriation grew longer and more contentious. Under the BLEU (Belgium-Luxembourg Economic Union) - Burundi BIT, the ICSID tribunal deemed such activities as indirect expropriation in the Goetz case¹², where the revocation of a free zone certificate by the concerned Ministry forced the investors to cease their activities, thereby preventing them from benefiting from their investment.

ADOPTION OF THE 2015 MODEL BIT

In 2015, the Indian government made public its new model Bilateral Investment Treaty (BIT), a framework for independently negotiated accords that regulate private investments from one nation to another. As a strategy for economic liberalisation, India began signing BITs in 1991, according to previous research. India has made it clear that it intends to welcome foreign investment into its market¹³.

In 1994, it signed its first bilateral investment treaty with the United Kingdom¹⁴. This laid the groundwork for the Model BIT of 2003, and since then India has negotiated BITs with nearly 84 nations.¹⁵ These treaties included broad provisions that arbitral tribunals could interpret harshly, and they gave investment protection precedence over a host state's right to regulate.

Despite India's launch of a massive BIT project, the BIT programme in India failed to attract

¹¹ Id. 101

¹² Antoine Goetz et consorts v. République du Burundi, ICSID Case No. ARB/95/3 (1998)

¹³ Prabhash Ranjan, India and Bilateral Investment Treaties – A Changing Landscape 29 ICSID REV.- FOREIGN INV. L.J. 419 (2014) [hereinafter Ranjan, Changing Landscape]; See also Niti Bhasin & Rinku Manocha, Do Bilateral Investment Treaties Promote FDI Inflows? Evidence from India, 41(4) Vikalpa: J. Decision Makers 275-287 (2016), (claiming that BITs signed by India have contributed to rising FDI inflows 'by providing protection and commitment to foreign investors contemplating investment in India'); Luke Nottage & Jaivir Singh, Does ISDS Promote FDI? Asia-Pacific Insights from and for Australia and India, Asia Pacific Forum for International Arbitration (AFIA) (Nov. 17, 2016), <http://afia.asia/2016/11/does-isds-promote-fdi-asia-pacific-insights-from-and-foraustralia-and-indi a/>.

¹⁴ Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of India for the Promotion and Protection of Investments, Mar. 14, 1994, entered into force Jan. 6, 1995. [India-UK BIT].

¹⁵ Dev Krishan, India and International Investment Law, India and International Law 277 (Bimal Patel ed., 2008)

much attention between 1994 and 2014¹⁶. According to Prabhas Ranjan, the reason could be India's absence from the Investor-State Dispute Settlement (ISDS) mechanism¹⁷.

Almost eleven BIT claims were filed against India in various arbitral forums during this time period. Nine of these eleven claims were related to the Dabhol Power Project¹⁸, and, surprisingly, none of them were resolved by ISDS.

Investment Protection Requirement Under The Model Bit Of 2015

A chapter on "protection standards" is included in nearly all BITs. This serves as the basis of investment protection in a concerned BIT. Fundamental principles of investment protection standards include the presence of well-defined FET, non-discrimination clauses such as MFN-national treatment, full protection and security clause, umbrella clause, transfer of funds provision, and 'access to justice, fair procedure, and denial of justice' Occasionally, however, treaties contain expansive language that permits arbitral tribunals to interpret treaty clauses against the host state.

Previously, India adhered to this practise; however, the new model BIT departs from this practise. The escalation of India's treaty claims has prompted a shift in strategy. It was essential for India to acknowledge that the practise of relying on broad investment standards was no longer acceptable. In light of the growing debate over how to strike a balance between Sovereign hegemony and investment protection, the host state cannot have unchecked regulatory autonomy over investment protection. Using this guiding principle as a guide, a draught Model was developed, and the new 2015 Model BIT was eventually developed to fulfil the lost hopes of foreign direct investment in India.

¹⁶ Ranjan, Changing Landscape, supra note 57. This is confirmed by three Indian government officials who recently wrote that "until the White Industries award, there had been little debate about the investment regime" in India. SAURABH GARG ET AL., supra note 39, at 71. It has been found that until countries are hit by BIT claims, it may be difficult for the country concerned to fully appreciate the cost of the BIT – Lauge N. Skovgaard Poulsen & Emma Aisbett, When Claim Hits: Bilateral Investment Treaties and Bounded Rational Learning 65:2 WORLD POL. (2013).

¹⁷ India – as Respondent State, Investment Policy Hub, UNCTAD
<http://investmentpolicyhub.unctad.org/ISDS/CountryCases/96?partyRole=2>

¹⁸ VAND. J. TRANSNAT'L L. 908 (2008). Also see GE settles Dabhol Issue, THE INDIAN EXPRESS (Mumbai, July 3, 2005), <http://www.indianexpress.com/oldStory/73760/>. Capital India Power Mauritius I and Energy Enterprises (Mauritius) Company v. India, ICC Case No. 12913/MS, Award, (Apr. 27, 2005); Bank of America, Memorandum of Determinations, OPIC, IIC 25 (2003), <https://www.opic.gov/sites/default/files/docs/BankofAmerica-September30-2003.pdf>.

Contrary to common belief, the new Model BIT may contain several temporal gaps, rendering it ineffective and reverting it to the same primitive document of regulatory dominance. In spite of this, non-discrimination clauses such as 'Most Favored Nation' (MFN) and 'Fair and Equitable Treatment' were in place (despite the existence of arbitral awards, but not ISDS)¹⁹.

Investment Protection Standards Taken From The Bit 2015 Model

Every BIT has a section on "protection standards." There wouldn't be any investment protection in a BIT without this. The presence of clearly defined FET, non discrimination clauses, such as the MFN-national treatment clause, the full protection and security clause, the umbrella clause, the funds transfer provision, and the "access to justice, fair procedure, and denial of justice," determine the basic principles of investment protection standards²⁰.

However, some treaties have vague provisions that allow the arbitral tribunal to interpret treaty sections in a way that is detrimental to the host state. While India had previously followed this practise, the new model BIT breaks away from it. Constant Indian treaty claims prompted the new approach. Realizing that the time for depending on general investing guidelines has passed was crucial for India. Given the growing discussion about how to find a happy medium between Sovereign hegemony and investment protection, the host state cannot have complete regulatory autonomy over investment protection. Using this as a compass, a Model was drafted, and the 2015 Model BIT was finalised to restore faith in FDI in India. If so, does the new BIT provide a clear and comprehensive solution to the problems?

Yet, a closer look reveals that the new Model BIT may contain a few temporal gaps, which could render the new Model ineffectual and relegate it to the same rudimentary document of regulatory domination. The Model no longer includes the non-discrimination clauses of "Most Favoured Nation" (MFN) and "Fair and Equitable Treatment" (FET), but "National Treatment" is still present. Provisions for expropriation, transfer of cash, and full protection and security are all part of the new model, which should reassure investors. However, it lacks key safeguards that should be included, such as provisions relating to tax measures, the restriction on arbitrariness, the umbrella clause, legitimate expectations of investment protection, etc. Hence,

¹⁹ Capital India Power Mauritius I and Energy Enterprises (Mauritius) Company v. India, ICC Case No. 12913/MS, Award, (Apr. 27, 2005); Bank of America, Memorandum of Determinations, OPIC, IIC 25 (2003), <https://www.opic.gov/sites/default/files/docs/BankofAmerica-September30-2003.pdf>.

²⁰ DOLZER & SCHREUER, (2016).

the following paragraphs make an effort to discuss the key aspects of the Model BIT, which can have a substantial influence on foreign investment protection and so restrict capital flow. With MFN in place, there is no room for bias in global trade²¹.

The Model BIT has been criticised for not including a most-favored-nation clause; this was highlighted in the White Industries case⁴¹⁵. India's FDI openness was severely harmed by the presence of white-collar industries. Since the award's enforcement was significantly delayed, White Industries lost its entire investment in India. Due to the absence of an effective means standard in the India-Australia BIT, the tribunal applied the effective means standard from the India-Kuwait BIT and rendered a 4,08,000,000 USD award against India. This was made possible by the comprehensive MFN clause in the India-Australia BIT.

The Indian government was already on edge because of the 22 treaty claims that had been made against it in the years following the end of the White Industries era. It is acceptable to use MFN clauses for treaty shopping on occasion, but this practise is best avoided if possible. So, investors will have an advantage in settling conflicts that aren't covered by an existing treaty. However, the BIT would revert to a protectionist era if non-discrimination clauses like MFN were removed. It would be quite difficult for a foreign investor to fight discrimination if he or she encountered it. If this clause is not included, the Model BIT's credibility will deteriorate.

Actions Taken By Local Governments

Considering India's quasi-federal structure, the State Governments have a great deal of discretion and authority on state-level matters of policy. Many of the items on the Concurrent List are delegated to the discretion of individual state governments under the State and the Concurrent List. Although if foreign direct investment (FDI) is on the residual list and FDI policy choices are made at the federal level, international investors may still be subject to regulations enacted by the states. As a result, actions performed by local governments (and mistakenly attributed to the state government) can have severe consequences for foreign

²¹ See Rudolf Dolzer & Terry Myers, *After Tecmed: Most Favoured Nation Clauses in International Investment Protection Agreements*, 19 ICSID Rev. Foreign Inv. L. J. 49 (2004); Stephen Fietta, *Most Favoured Nation Treatment and Dispute Resolution under Bilateral Investment Treaties: A Turning Point?* 8 Int'l. Arb. L. Rev. 131 (2005);

investors²².

FINAL REMARKS

While trying to entice foreign direct investment (FDI), BITs are a crucial component. Although India had success with the BIT regime in 1994, the investor-friendly model from 2003 was the driving force behind the country's continuing development. Nevertheless, things changed in 2011 after a treaty claim was filed by Australia's White Industries. A record \$3.5 million was levied against India because it did not adhere to the "effective methods" criteria. Contrary to popular belief, the aforementioned clause was not originally included in the India-Australia BIT but was instead lifted wholesale from the India-Kuwait BIT's generalised Most Favored Nation (MFN) provision. It was during this frenzy that a paradigm change occurred, marking the end of the 2003 Model and the beginning of the 2015 Model. While the danger persisted and grew more severe, arbitration notifications demanding billions of dollars were repeatedly sent to India over a period of four to five years.

After ratifying the revised Model BIT in December 2015, India will no longer be party to it after 2018. Over 58 bilateral investment treaties (BITs) exist to shield companies from litigation. India's Foreign Direct Investment (FDI) strategy has changed, however, because only Belarus has signed a BIT based on the revised Model BIT in 2018. The dynamic shift in India's attitude is the simplest explanation. The 2015 model is a highly pro-state BIT, which is different from the investor-centric 2003 model. The Model BIT 2015 provides substantial protections for the Indian government. Such restrictions could include, for instance, a definition of "enterprise-based" investments that is significantly narrower than the definition contained in domestic regulations.

As an added stipulation, the foreign investor must show that his or her capital commitment, made without assurance of a return for a set length of time, contributed to the expansion of India's economy. The regulatory space has been expanded by the abolition of the taxation clause, MFN, and FET. Without MFN and FET, India may treat foreign investors very unfairly. In addition, the Indian government is not prohibited from acting arbitrarily, and there are no laws for the protection of investments or the expectations of such protection. Without these

²² Local Government includes urban, rural and other local governments within its ambit. Definition of State in turn includes 'Local Government' with its scope. The Constitution of India, art. 12, 1950. Thus an act of the Local Government can be attributed to the State Government under Article 12 of the Constitution.

cornerstones, the model collapses even further. Finally, foreign investors are deterred from investing in India due to the roughly six-year waiting period between the exhaustion of local remedies and the initiation of arbitration.