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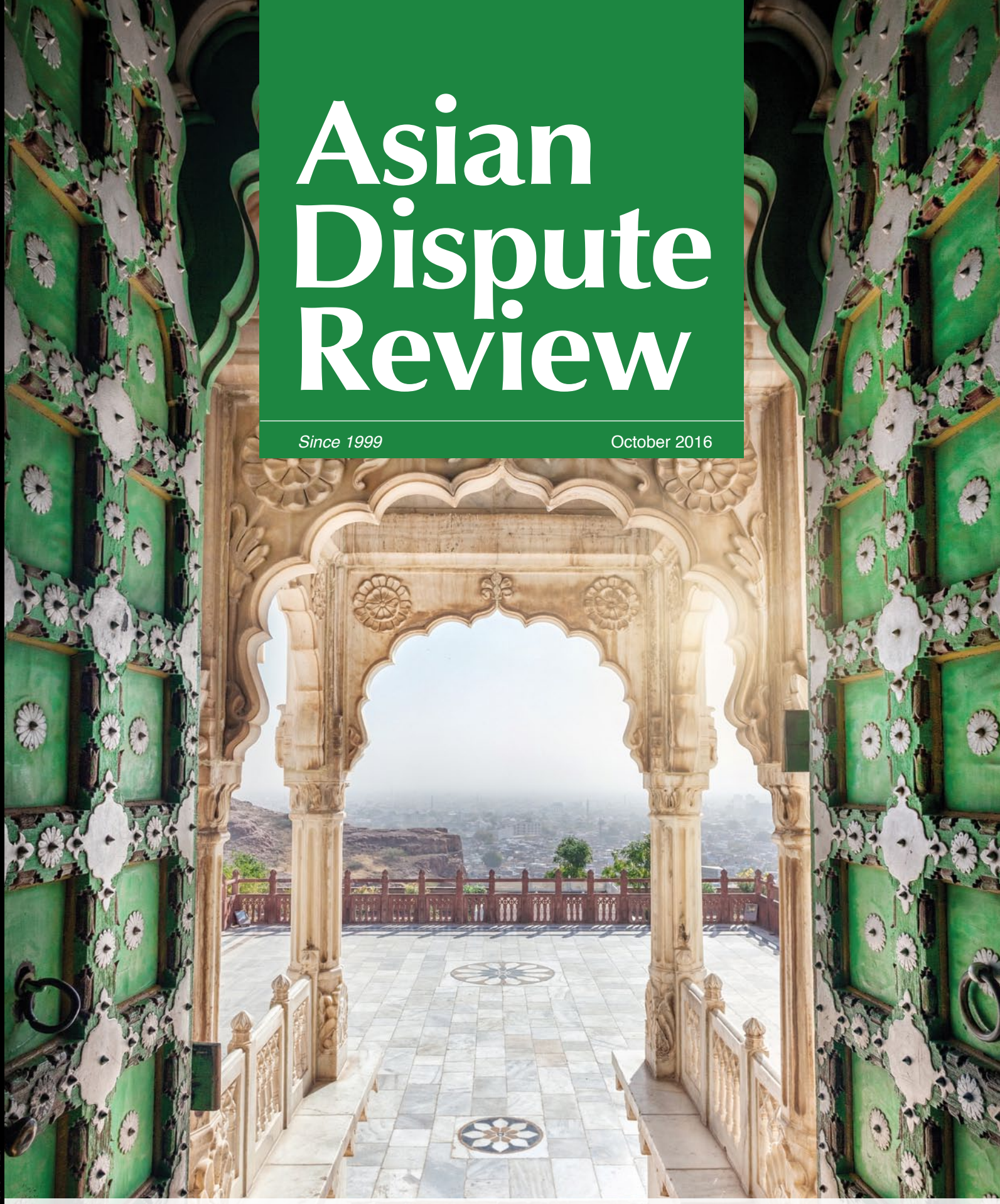

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CONTENTS

October 2016

India's New Approach to Investment Treaties

Nish Shetty & Romesh Weeramantry

This article focuses on a new phase in India's investment treaty programme, which involves the formulation of a new Model Bilateral Investment Treaty and the termination of old BITs. It concludes by assessing what effect the new Model BIT may have on India's future investment treaty negotiations.

Introduction

Two significant developments have recently taken place in India's investment treaty programme: the formulation of a new Model Bilateral Investment Treaty (BIT) and a policy aimed at terminating its old BITs. These twin developments are part of a new phase in India's approach to investment treaties which appears to have been triggered by numerous investment arbitrations filed against India.

Background

Since India's independence in 1947, three main phases have been relevant to its investment treaty programme.[1] The first, from 1947 through to 1990, saw India giving priority to its national laws to regulate and protect foreign investments. During this period, India did not enter into a single investment treaty.[2]

The second phase, from the 1990s to 2011, involved a seismic shift in policy. A balance of payments crisis in 1990-1991 gave rise to a major reversal of India's inward-looking economic policies. The new outlook embraced BITs to attract foreign investors into India, which was in line with a global BIT boom that had been taking place, especially in the 1990s.

However, cracks in India's confidence in investment treaties started to emerge in 2011, particularly after the *White Industries v India* award,[3] which gave rise to a third phase. Efforts to re-evaluate India's treaty programme gained considerable momentum during this phase, leading to the drafting of a new Model BIT and the adoption of a new policy of terminating India's existing open-textured BITs.

> "Efforts to re-evaluate India's treaty programme gained considerable momentum … [following the White Industries arbitration], leading to the drafting of a new Model BIT and the adoption of a new policy of terminating India's existing open-textured BITs."

It should also be borne in mind that India is one of the few Asian nations not to have signed the ICSID Convention.[4] Investment arbitrations against India have therefore been typically instituted under the UNCITRAL Arbitration Rules, which provide a far more confidential process than that found in ICSID arbitration. Consequently, much of what is known about the existence, content and outcome of investment arbitrations brought against India are, in the majority of cases, based on news reports rather than arbitral tribunal decisions themselves.

India's investment treaties

India's BIT programme commenced in 1994, when it signed its first BIT with the UK. This treaty was based on the capital exporting model developed by the UK in the 1970s and was a far cry from the inward-looking, nationalistic approach to foreign investment that India had espoused prior to the 1990s. India's recalibration of its investment policies was clear: it strived to gain investor confidence and increase volumes of private capital inflows. This approach had a one-dimensional focus – the promotion of investment – with little thought given to India's power to regulate. Since 1994, India has signed more than 80 BITs and ratified over 70.[5]

From 1994 to 2011, India signed an average of four to five investment treaties per year. However, this trend ended after 2011. UNCTAD's investment treaty database shows that from 2012 to date, only one BIT (with the United Arab Emirates) and an Investment Agreement with ASEAN had been signed by India.[6] Most recently, India signed a BIT with Cambodia in 2016 (which is not, however, indicated in the UNCTAD database). The slowdown in concluding BITs has been attributed to India's loss in the *White Industries* case, pursuant to which India was held responsible for court delays in enforcing an international commercial arbitration award.[7] Since the *White Industries* award, there have been a number of other investment treaty claims made against India, which are discussed below.

The most frequent investment treaty invoked against India is the Mauritius-India BIT, pursuant to which six investment arbitration cases appear to have been launched. The explanation why this BIT is the most popular relates to the use of Mauritius as the main channel of foreign direct investment into India (due to tax and other advantages[8]). Other BITS that have been used more than once against India include those with the UK, France, the Netherlands and the Russian Federation. BITs with Austria, Australia, Cyprus, Germany, the Russian Federation and Switzerland have been invoked one time each.[9]

> "India is one of the few Asian nations not to have signed the ICSID Convention. Investment arbitrations against India have therefore been typically instituted under the UNCITRAL Arbitration Rules, which provide a far more confidential process than that found in ICSID arbitration."

Investment arbitrations against India

Among States in the Asian region, India has had, by far, the greatest number of investment treaty claims filed against it. According to UNCTAD, it ranks as the twelfth most frequent investment treaty arbitration respondent State in the world,

with 17 investment treaty cases instituted against it.[10] These UNCTAD statistics do not, however, appear to be complete. There may be as many as eight more claims reported to have been filed against India.[11] The next most frequent Asian respondent State is Indonesia, which is the respondent in six investment treaty arbitrations.[12]

The relatively high number of treaty claims against India may be explained to some extent by its first nine investment treaty arbitrations. They were all initiated in 2003-2004 and related to one project, the Dabhol power project in Maharashtra. The nine claimants in these arbitrations alleged the reversal of energy policy by the local government. All these claims were settled.[13] Another point that has been made to explain the number of arbitrations against India is that they are filed for tactical reasons: to obtain leverage in negotiations with the government.

Reported claims pending against India include:

- *Satellite lease annulment cases*: In a decision issued on 25 July 2016 in *Devas v India*,[14] an UNCITRAL tribunal held that India had breached the India-Mauritius BIT's expropriation and fair and equitable treatment provisions by annulling Deva's lease of two satellites owned by Antrix, an arm of the country's space programme. A majority dismissed part of the claim, upholding one of India's defences which was based on an exception in the BIT for measures to protect "essential security interests".[15] Subject to any challenge by India, the case will now proceed to the damages phase. Another investment arbitration related to this satellite deal has also been brought by Deutsche Telekom under the Germany-India BIT.[16]
- *Retrospective tax cases*: Two claims have been made under the UK-India BIT relating to Vedanta Resources' acquisition from Cairn Energy UK of a stake in the oil company Cairn India. The claims concern the retrospective imposition of billions of dollars in taxes. India is arguing that the BIT does not permit the arbitration of tax disputes.[17] A case brought by Vodaphone under the Netherlands-India BIT is also reported to relate to back taxes involving billions of dollars.[18]
- *2G spectrum licence cases*: Two UNCITRAL claims have been brought under the UK-India BIT and the Mauritius-India BIT by Astro All Asia Networks and South Asia Entertainment Holdings, respectively. The claims relate to criminal investigations in India relating to the 2G spectrum scandal, in which government ministers are accused of accepting bribes in return for awarding discounted licences to mobile phone operators. The claimants allege that India breached its BIT obligations by subjecting them to an unfair and biased investigation and that the Indian Supreme Court had wrongly assumed the role of investigator, prosecutor and adjudicator in violation of fundamental rules of procedural fairness. Khaitan Holdings Mauritius has also launched a US$ 1.4 billion claim following the Indian Supreme Court's decision to cancel mobile operator licences in the wake of the 2G scandal.[19]

It can be seen that the investment claims pending against India are significant in terms of the players involved and their factual content, as well as the magnitude of the amounts in dispute. India's reaction to these cases in the form of a re-evaluation of its BIT programme is therefore not altogether surprising.

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The new Model BIT

As mentioned previously, the first decision in an investment arbitration against India in the *White Industries* case appears to have been a tipping point and has led to a dramatic slowdown in the conclusion of its investment treaties. However, the rethink that India went through after this case and the others mentioned in the previous section went further than this: it led to the drafting of a new Model BIT, a draft of which was circulated for public consultation in early 2015. This draft addressed concerns that India's existing BITs unduly favoured protecting investor interests and failed to strike the required balance between the rights and obligations of a foreign investor and the host State.[20] The draft of the Model BIT came under some criticism and was revised significantly before the final version was approved by the Indian Cabinet on 16 December 2015 (the 2015 Model BIT).

Listed below are some notable observations that arise from a comparison between the 2015 Model BIT and India's BITs signed in the 1990s.

- *What's not changed*: (i) the obligation to accord national treatment to foreign investors (art 4); (ii) the prohibition against nationalisation or expropriation of an investment except for a public purpose, in accordance with due process, and payment of the fair market value of the investment before the expropriation (art 5); (iii) free movement of the investor's capital (art 6); and (iv) subrogation (art 8).
- *What's not there*: (i) a most favoured nation provision; (ii) a fair and equitable treatment provision; (iii) a full protection and security provision that relates to non-physical security of investors and investments; and (iv) the right to commence arbitration without exhausting local remedies (although art 15.2 permits arbitration to be commenced after five years of seeking local remedies).
- *What's new*: (i) an 'investment' is defined using the criteria adopted in *Salini v Morocco*;[21] (ii) provisions that exclude liability for expropriation where judicial bodies impose measures "designed and applied to protect legitimate public interest or public purpose objectives" (art 5.5); (iii) requirements that the parties' pleadings, transcripts of hearings and awards be public (art 22); (iv) the ability of State parties to make a joint interpretation of the BIT that is binding on tribunals established under that BIT (art 24); (v) general exceptions for measures to protect public morals, maintain public order, protect human, animal or plant life or health, protect and conserve the environment and protect national treasures or monuments (art 32); and (vi) denial of benefits to an investment or investor owned or controlled by persons of a State that is not a party to the BIT (art 35).

Significant changes have therefore been made. Most of these changes are not novel, however, and have been seen before in treaties concluded between other States. Some have become common features in the current generation of investment treaties or free trade agreements (FTAs) with investment chapters that aim to strike more of a balance between the sovereign right to regulate and the rights of investors. The requirement that local remedies be exhausted as a precondition to instituting arbitration is, however, a major change that will be subject to much comment.

India's BIT termination policy

The 2015 Model BIT was a prelude to India's BIT termination notices sent to 57 countries earlier in 2016. Further, it is reported that the remaining 25 countries having BITs with India have been requested to sign joint interpretative statements with India to prevent expansive interpretations by arbitral tribunals on key substantive principles. For example, where treaties are silent as to whether tax measures are within their scope, the interpretation apparently requires the State parties to agree that those measures are outside the scope of the relevant BIT. [22]

The terminations, when implemented, will not automatically do away with the old style BITs, however, as they have so-called 'sunset' provisions which ensure that investors who made investments before termination are protected for periods of up to 10 years or more. For example, the Netherlands-India BIT provides that: "In respect of investments made before

the date of the termination of the present Agreement the foregoing Articles shall continue to be effective for a further period of fifteen years from that date." To avoid this type of post-termination application, the 2015 Model BIT does not include a sunset provision.

> "Most of … [the new provisions of the 2015 Model BIT] are not novel … and have been seen before in treaties concluded between other States. The requirement that local remedies be exhausted as a precondition to instituting arbitration is, however, a major change that will be subject to much comment."

Conclusion

The foregoing discussion demonstrates that India has adopted a far-reaching new approach toward investment treaties, which has been triggered by the investment arbitrations filed against it. The 2015 Model BIT has adopted many provisions not found in India's old generation of BITs. A number of these new provisions will have a significant impact on future investment arbitrations instituted against India under treaties that follow that model.

A provision expected to raise considerable debate, especially in India's BIT negotiations with developed States, is the requirement that an investor must exhaust local remedies as a pre-condition to arbitration. In the event India considers including such a provision, due regard must also be given to the increase in the number of its own nationals or companies who are becoming major investors outside India, and who may one day need access to international arbitration rather than having to fight their investment dispute before the domestic courts of the host State. A good example of this type of Indian investor is India Metals & Ferro Alloys Ltd, which commenced an investment arbitration in 2015 against Indonesia pursuant to the India-Indonesia BIT with regard to its rights under a coal mining licence in Indonesia. Going forward, the authors expect that Indian investors will encounter many more disputes with foreign States and this reality should not be overlooked in India's investment treaty negotiations.

India is currently negotiating investment treaties or FTAs containing investment chapters with developed countries such as the United States and Canada, and with the European Union. It is also participating in the negotiation of the Regional Comprehensive Economic Partnership, a multilateral investment treaty that involves all ASEAN nations plus six more States, including Japan and China. None of these States currently show a preference in their investment treaties for the exhaustion of local remedies as a condition to commencing investment arbitration. The authors consider that while a number of the provisions in the 2015 Model BIT may be accepted in negotiations with these States, an agreement to adopt the exhaustion of local remedies provision will prove difficult to achieve. It is, however, noteworthy that the BIT signed with Cambodia earlier in 2016 adopts virtually all of the Model BIT's text, including the requirement to exhaust local remedies prior to arbitration.

The new approach taken by India in respect of its investment treaties is a bold one. For this to be successful, however, the country must proceed in a nuanced manner that strives to balance the competing interests of its right to regulate and the protection of both foreign investors in India and Indian investors abroad.

1 See Prabhash Ranjan, 'India and Bilateral Investment Treaties: From Rejection to Embracement to Hesitance?', in R Babu & S Burra (Eds), *Locating India in the Contemporary International Legal Order* (2016, Springer), forthcoming.

2 During this period, India was a strong proponent of the UN General Assembly's 1974 Charter of Economic Rights and Duties of States (UN Doc A/RES/29/328), art 2(2)(a) of which provided that each State had the right "[t]o regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its laws and regulations in conformity with its national objectives and priorities. No State shall be compelled to grant preferential treatment to foreign investment."

3 *White Industries Australia Ltd v Republic of India*, Final Award, UNCITRAL, 30 November 2011.

4 Other Asian nations that have not signed the ICSID Convention include Bhutan, Laos, Myanmar and Vietnam.

5 See http://investmentpolicyhub.unctad.org/IIA/CountryBits/96#iiaInnerMenu .

6 See http://investmentpolicyhub.unctad.org/IIA/CountryBits/96#iiaInnerMenu and http://investmentpolicyhub.unctad.org/IIA/CountryOtherIias/96#iiaInnerMenu .

7 For commentary on this case, see Sumeet Kachwaha, *The White Industries Australia Limited-Indian BIT Award – A Critical Assessment* (2013) 29 Arb Int'l 275.

8 India has recently amended its tax treaty with Mauritius, imposing a capital gains tax on short-term investments into India. See Amy Kazmin & Simon Mundy, *India closes tax loophole with Mauritius*, Financial Times, 11 May 2016. The impact of this change on the use of Mauritius as the route for making investments into India is yet to be seen.

9 See http://investmentpolicyhub.unctad.org/ISDS/CountryCases/96?partyRole=2 (accessed on 4 September 2016).

10 UNCTAD, *IIA Issues Note, Investor-State Dispute Settlement: Review of Developments in 2015*, (No 2, June 2016), p 3. India lies in between the Ukraine (19 claims) and Kazakhstan (15 claims). See also http://investmentpolicyhub.unctad.org/ISDS/CountryCases/96?partyRole=2.

11 See the table in Prabhash Ranjan, 'India and Bilateral Investment Treaties: From Rejection to Embracement to Hesitance?', in Babu & Burra (Eds), *op cit* (note 1 above).

12 See http://investmentpolicyhub.unctad.org/ISDS/CountryCases/97?partyRole=2 (accessed on 4 September 2016). On a global basis, Indonesia is ranked the 33rd most frequent respondent State.

13 Data compiled from http://investmentpolicyhub.unctad.org/ISDS/CountryCases/97?partyRole=2 (accessed on 4 September 2016).

14 *CC/Devas (Mauritius) Ltd, Devas Employees Mauritius Pte Ltd, and Telcom Devas Mauritius Ltd v Republic of India*, PCA Case No. 2013-09.

15 Douglas Thomson, *India Found Liable in Satellite Case*, Global Arbitration Review, 26 July 2016.

16 *Deutsche Telekom v Republic of India*, ICSID Additional Facility (details not public).

17 *Vedanta Resources v Republic of India*, and *Cairn Energy UK v Republic of India*. See Lacey Yong, *Panels in Place for Indian Back Tax*, Global Arbitration Review, 15 August 2016.

18 Kavaljit Singh, *Treaties that gave away the store*, The Hindu, 27 April 2012.

19 Lacey Yong, *2G Spectrum Scandal Leads to Claims against India*, Global Arbitration Review, 15 March 2016.

20 See Law Commission of India, *Analysis of the 2015 Draft Model Indian Bilateral Investment Treaty*, Report No 260 (August 2015) and Anirudh Krishnan, *A bit for the state, a bit for the investor*, The Hindu, 8 September 2015.

21 *Salini Costruttori SpA and Italstrade SpA v Kingdom of Morocco*, ICSID Case No ARB/00/4, Decision on Jurisdiction, 31 July 2001.

22 Kavaljit Singh & Burghard Ilge, *Remodeling India's Investment Treaty Regime*, Global Arbitration Review, 18 July 2016.

23 See Ayomi Amindoni, *Indian mining co sues Indonesia for $581 million*, The Jakarta Post, 18 November 2015.