

*Sumeet Kachwaha on*

## The New Challenges and Opportunities for India in Bilateral Investment Treaties

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In the early 1990's India was confronted with a very bleak fiscal scenario. It took a bold decision to move away from its socialist path and embrace economic reform, liberalise the economy and attract foreign investment. As part of this effort, India entered into a host of BITs. Recently this has gone into rough weather and India is faced with a spate of high stake BIT disputes. The country is at the cross-roads and needs to consider afresh its BIT arrangements and explore alternatives which balance investors concerns and the country's sovereign rights and expectations.

**Background:** India is not a signatory to the ICSID Convention<sup>1</sup>. This is for historical reasons as it has always been of the view that the supremacy of its courts cannot be compromised by allowing an ICSID arbitral tribunal decision finality and immunity from challenge.

In the absence of BITs India did experiment with individual / ad hoc State support agreements / guarantees (as it did for instance with Enron in relation to the Dabhol Power Project) but this was essentially a stop gap arrangement as it lacked transparency and consistency. Entering into BITs was seen as the way forward and India got about in right earnest. Beginning from 1994 the country has entered into 72 BITs with 82 countries, which make it one of the largest portfolios globally. Additionally the country has four comprehensive economic co-operation agreements with investment protection provisions.

**Reckoning with reality: The White Industries Award:** While more and more treaties were being negotiated India got a reality check when an ad hoc BIT arbitral tribunal in *White Industries Australia Limited versus the Republic of India* rendered an Award dated 30<sup>th</sup> November 2011 against it. White Industries (White), an Australian Company had an ICC Award in its favour against an Indian Public Sector Undertaking (PSU) called Coal India. White had been trying to enforce the award in Indian courts since September 2002. However the matter got embroiled on a jurisdictional issue (relating to Indian courts powers to set aside a foreign award), which ended up and remained unresolved in the Supreme Court.<sup>2</sup> In December 2009 White invoked the Australia – India BIT arbitration *inter alia* contending that it was denied "effective means of asserting claims and enforcing rights" - an obligation contained in the Kuwait - India BIT, which White (though an Australian Company) contended it could take advantage of relying on the most favoured nation (MFN) clause in the bilateral investment treaty between Australia and India. The White Tribunal

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1 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (Washington Convention, 18 March 1965).

2 Judicial delays are common in India. The chief reason for delay was that the Supreme Court felt that the matter raised an important issue which should be decided by a Five Judge (Constitution) Bench and it took time for the Court to constitute a Five Judge Bench. In the meanwhile White invoked the Australia- India BIT. The author has criticized the White Award (see *Arbitration International*, Volume 29 Issue 2, page 275).

*inter alia* held that the ICC Award which White had in its favour would be an “investment” under the BIT. It held that the Indian judicial system’s inability to deal with White’s jurisdictional appeal for over nine years amounted to an undue delay and constituted a breach of India’s obligation to provide White with “*effective means of asserting claims and enforcing rights*”. On this basis the BIT Tribunal awarded White damages (representing the sums awarded to it under the ICC Award along with costs). Essentially India had to suffer due to its general court delays even though it was not guilty of any specific act or omission in relation to White as an investor.

*Children’s Investment Fund Management case:* This UK based hedge fund procured 1.01 per cent of equity in Coal India (a leading PSU) after the Government decided to offload 10 per cent of its shares in 2010. Soon thereafter, the investor objected against governmental influence on the PSU requiring it to sell cheap coal to power plants and others, which the investor said impacted the dividend payout.

The basis of the case seems questionable. It is a matter of public knowledge that PSUs in India serve social objectives (indeed this – and not profit making – is the rationale for their existence). The investor could not have been oblivious of the realities. Besides it would seem that the investor did in fact earn 39 per cent return on its equity – (far better than the market average).<sup>3</sup>

*The Vodafone controversy:* The Vodafone controversy was somewhat unnecessarily called upon itself by India. The Vodafone Group had purchased shares in a Mauritius based entity, which in turn held 66% interest in an Indian telecom company. The Indian Government sought to impose a capital gains tax on the transaction. The amounts involved were large (over US\$2 billion). The High Court of Bombay held the transaction to be taxable but the Indian Supreme Court ruled in Vodafone’s favour and held it to be non-taxable. The Government of India did not accept this as the final word and introduced retrospective legislation in Parliament sidestepping the dicta of the Supreme Court and holding Vodafone liable to tax. This provoked a sharp reaction not only from Vodafone but from the political and international business community at the highest level. Vodafone has served a Notice of Dispute under the India - Netherlands BIT, threatening India with arbitration if India’s retrospective amendment to its law is not abandoned. A Conciliator has been appointed and efforts are afoot to settle the matter.

*The 2G license controversy:* Almost in parallel another major controversy has erupted. This arose out of allocation of spectrum licenses to 122 Indian and foreign telecom companies on a ‘first-come-first-serve’ basis. The Government of India announced a policy in 2008 allocating telecom spectrum to applicants, taking a deliberate decision not to maximise profit for the State, but to allow licenses to be allocated on a fixed (low) license fee on a ‘first-come-first serve’ basis. The policy was sanctified at the highest level - endorsed by the Attorney General of India, the Telecom Regulator as well as the office of the Prime Minister. However the Comptroller & Auditor General of India came down heavily, stating that the public exchequer had been severely compromised, whereupon a Public Interest Litigation was filed in the Supreme Court *inter alia* challenging the allocation of licenses. The Supreme Court upon being seized of the matter held the ‘first come first serve’ policy adopted by the Government to be unconstitutional. The court held that the Government could not have given away precious natural resources on an arbitrary and non-

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3 A treaty too many: 15<sup>th</sup> May 2013; <http://www.downtoearth.org.in>.

transparent basis. It ought to have proceeded through public auction. As a corollary the Supreme Court struck down all 122 licenses that had been granted under the impugned policy. While the Indian telecom companies affected by this decision had no legal remedy (the decision being of the highest court of land), the foreign investors have not passively accepted the decision. They have threatened India with BIT arbitrations for very large amounts claiming reimbursement / compensation for their lost investment.

Amongst the companies involved are Russia's Sistema JSFC, Norway's Telenor ASA, Loop Telecom U.K, Axiatic Group Malaysia and Mauritius based Capital Global & Kaif Investment. Telenor's claim alone is reported to be US\$ 14 billion.

**The dilemma for India:** India seems to have got caught on the wrong foot. At one level it has exposed itself to a criticism of not being an investment friendly destination (an image it can ill afford given the enormous task the country has to pull its millions out of poverty). On the other hand there are legal issues which it must now face with billions at stake. Then there are cases like the Children's Investment Fund which impact the country's social agenda and sovereign functions.

**Lessons for India:** There is now (somewhat all of a sudden) a new dimension to Bilateral Investment Treaties (and indeed the picture is unfolding the world over).

To begin with, India needs to examine if its current BITs need to be modified or refined in any manner in light of the recent global experience. What are the legitimate rights which a foreign investor must be assured of and where does a country need to draw the line.

Secondly, India must realise that there is an inherent disadvantage it faces in BIT investment arbitrations. It is generally recognized that investment arbitrations are skewed in favour of foreign investors.<sup>4</sup> A disadvantage that is further fueled by the limited pool of investment arbitrators and lawyers and the negligible participation of Indians in it.<sup>5</sup> As a result India is driven to appoint non-Indians as arbitrators or lawyers in most of its BIT disputes.

It should be a legitimate expectation of a nation as vast and commercially significant as India to participate in the decision-making process where it is involved. India thus needs to take vigorous steps to train and upgrade the skills of its law officers; focus on giving arbitrations / arbitral institutes a boost so that locally grown talent is nurtured and emerges.

Third, India needs to seriously consider whether it should accede to the Washington Convention. Over 149 countries have ratified the Convention as of now (more have signed and are in the process of ratification). Can India afford to sit outside this community of nations?

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4 See Gary Born, Duke Journal, Volume 61, Number 4, January 2012, page 775 at 842.

5 According to an in-depth study by CEO and Transnational Institute dated November 2012 - 'Profiting from Injustice' - three US and UK firms have been involved in 130 investment treaties between them in 2011 alone. Further just 15 arbitrators from Europe, US and Canada have decided 55 per cent of investment dispute arbitrations. Further, as per the study, investment dispute lawyers have "a firm grip on academic discourse on investment law and arbitration" which may well compromise "academic balance and independence."

**Lessons for the investors:** Fighting a legal battle against a host country should not be an ideal situation for any long term investor. Hence an investor's focus must be on moulding its business plans to fit in with realities on the ground, taking the thick with the thin (just as any domestic investor would). A foreign investor's interest would be equally well served (and foreign investment not suffer) if the treaty in question is confined to protecting against seriously inequitable or unfair treatment. Too expansive a treaty, its interpretation or application is not in the best interest of investors or the future of BITs. There is a case for restraint. The next section touches on this.

**The global picture:**

India is not alone at the cross roads. The number of investment claims registered up to 1996 was only 38. By 2011 this number had increased to 450 and 62 new cases were filed in 2012 alone.<sup>6</sup>

Bolivia, Venezuela and Ecuador have denounced the ICSID Convention. Venezuela is currently renegotiating 25 BITs. Argentina is faced with more than 40 BIT arbitrations with mind-boggling sums involved. Several of these concerned Argentina's financial crisis of 2001 and the consequent (deliberate) decision of the Government to allow its currency to devalue against the dollar. Certain investors claim that they suffered a loss as a result. Australia is faced by claims brought by tobacco companies alleging indirect expropriation of their trade marks and other intellectual property rights as a result of plain packaging legislation.

UNCTAD has called for a 'public debate' and mechanism to reform investor – State dispute settlement. On 10 April 2013, it issued a press release dated stating *"the number of investment disputes brought to international arbitration reached a new peak in 2012, amplifying the need for public debate about the efficacy of the investor-State dispute settlement (ISDS) mechanism and ways to reform it, a new UNCTAD report says"*.<sup>7</sup>

Australia has come out strongly indicating its intent to limit the scope of future BITs including doing away with the Dispute Resolution procedures envisaged therein. A Trade Policy statement issued in April 2011<sup>8</sup> *inter alia* states that while the government will ensure that foreign and domestic businesses are treated equally under the law, *"the Government does not support provisions that would confer greater legal rights on foreign businesses than those available to domestic businesses. Nor will the Government support provisions that would constrain the ability of Australian governments to make laws on social, environmental and economic matters in circumstances where those laws do not discriminate between domestic and foreign businesses[...]. In the past, Australian Governments have sought the inclusion of investor-state dispute resolution procedures in trade agreements with the developing countries at the behest of Australian businesses. The Gillard Government will discontinue this practice. If Australian businesses are concerned about sovereign risk in Australian trading partner countries, they will need to make their own assessments about whether they want to commit to investing in those countries."*

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6 UNCTAD Press Release No. PR/2013/007 dated 10<sup>th</sup> April 2013.

7 See footnote 6, *supra*. The United Nations Conference on Trade and Development (UNCTAD) publishes an annual Report on Recent Developments in Investor State Dispute Settlement (ISDS) highlighting the developments during the previous year.

8 Gillard Government Trade Policy Statement: Trading our way to more jobs and prosperity.

Has the pendulum begun to swing the other way? Clearly neither the developing nor the developed economies seem happy with the current state of affairs. There are no doubt challenges but equally opportunities to charter a mutually nurturing relationship. The experience of the past can serve to build a better future.

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**About the Author.** **Sumeet Kachwaha** has over three decades experience, primarily in Dispute Resolution (Litigation and Arbitration). He figures in Band One in the Arbitration Section of Chambers Asia from 2009 onwards. He also figures in Asia Pacific Legal 500 in the Dispute Resolution Section as a “Leading Individual”.

Mr. Kachwaha recently completed a three year term as Chair of the Dispute Resolution & Arbitration Committee of the IPBA (Inter-Pacific Bar Association). He currently serves as a Member, Advisory Board, KLRCA (Kuala Lumpur Regional Centre for Arbitration) and as Vice President, APRAG (Asia Pacific Regional Arbitration Group).

Mr. Kachwaha founded the firm Kachwaha & Partners in 2002 with its offices in New Delhi and Mumbai.

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