The Indian EXPRESS
JOURNALISM OF COURAGE

Next generation treaty

India's new model BIT makes it clear that its goal is to accomplish more than investor protection.

Written by Lisa Sachs , Lise Johnson , Sudhanshu Roy | Updated: November 12, 2015 5:41 pm

The April release of India's draft model bilateral investment treaty 1(BIT), which is expected to be approved by the cabinet soon, has generated a rich public debate on its international investment regime. There are important questions about the purpose and content of investment treaties, both in India and other countries. However, some reactions — like August's Law Commission report suggesting that the model BIT was not sufficiently investor-friendly — frame the discussion too narrowly, ignoring key questions and objectives behind India's transitioning investment policy regime.

India has close to 90 international investment agreements, either as BITs or as investment chapters in free trade agreements; for the most part, they are similar to the BIT models developed by capital-exporting countries in Europe and North America. The release of the comprehensive model BIT earlier this year indicates that, for the first time, Indian policymakers have been proactively taking steps to formulate a policy that ensures that BITs advance India's needs and interests, and not just the interests of their treaty partners and investors from those countries. Countries throughout the world, including India, are grappling with two key questions about investment treaty policy: First, the economic justifications for those treaties and second, their costs.

Until recently, it was simply assumed that the investor protection regime enshrined in BITs would lead to increased foreign investment and that foreign investment, in turn, would produce economic development benefits in both the host and home countries. Yet, within the past decade, several empirical studies have raised doubts about the accuracy of that assumption; investors are driven by important factors like market size, availability of skilled labour, infrastructure and quality of domestic governance institutions, and not so much by the existence of a BIT. Moreover, it is now clear that not all investment leads to development. So the underlying promise of BITs has not been realised.

Second, the costs of BITs are becoming harder to ignore. An increasing number of disputes have been brought against states to challenge good-faith measures taken in the public interest, such as anti-tobacco legislation, phase-out of nuclear power, environmental regulations, restrictions on development of hazardous waste facilities, domestic decisions regarding the scope of intellectual property rights, and efforts to regulate tariffs for electricity and water in concessions operated by private investors. These disputes are costly to litigate and even more costly to lose, and threaten states' ability to regulate in the public interest.

The backlash has already begun. In recent years, countries such as Bolivia, South Africa and Indonesia have either stopped signing new treaties or have announced their intention to withdraw from existing treaties. Others, like Australia, view the regime with scepticism and are reluctant to sign treaties with investor-state dispute settlement (ISDS) mechanisms. In a major shift in policy, Germany, which had been one the earliest proponents of the investment treaty system, now opposes the inclusion of ISDS in the investment chapter of the Transatlantic Trade and Investment Partnership with the United States. Leading economists such as Joseph Stiglitz and Jeffrey Sachs have similarly raised concerns about the potential impact of traditional BITs on governments' ability to regulate in the public interest.

Brazil has adopted a new model agreement that not only rejects investor-state arbitration but also excludes more traditional investment protections, such as the guarantee against indirect expropriation. Instead, it focuses on state-to-state cooperation and dispute settlement, and includes important provisions on investment facilitation as well as corporate social responsibility.

India’s revised model BIT is consistent with these trends. The new model clarifies that it only covers investments that have a physical presence and substantial business activities in the territory of the host state. This means that the investments represent long-term commitments of capital and resources to the local economy and can facilitate crucial transfers of technology. These types of beneficial investment are still afforded guarantees of fair treatment, protections against discrimination, expropriation and a right to freely transfer returns on investments. Moreover, they get the significant benefit of ISDS — but not before pursuing prior remedies before domestic courts, endorsing the customary rule applicable in other international regimes that a violation of international law can only be found after there has been an exhaustion of domestic remedies.

Critics of the new model should think more broadly than how investors and arbitrators may react to changes from the previous model. India should be commended for taking a step back to reevaluate the purpose and objectives of signing investment treaties to begin with. India’s new model BIT makes clear that its goal is to accomplish more than mere investor protection. Recent trends suggest that governments are wisely transforming BITs into tools of good governance with carefully calibrated rights and obligations. The model BIT is a step in the right direction. The next challenges include a comprehensive review of India’s many existing treaties, negotiations with strategic partners in Asia, Africa and Latin America that share similar objectives, and joint authoritative interpretations of treaty provisions to ensure the treaties are applied as the parties intend.

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