Bilateral Investment Treaties: Concept and History

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Abstract

Bilateral Investment Treaties (BITs) are a policy tool for promoting and protecting foreign direct investment (FDI). FDI is simply defined as a type of investment by a resident of one country in an enterprise in another country, indicating a significant influence and long-term interest. In the age of globalisation, FDI is regarded as an essential component of a free and prosperous global economic system and a key development tool[1]. The proposed study will investigate these treaties and their impact on policy space, focusing on the BITs signed by India. It is argued that BITs limit sovereign governments' ability to take policy measures to promote and protect domestic development goals. Policy space is defined as an autonomous decision-making space that a host country government considers essential for promoting and protecting its citizens' basic needs[2].

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[1] *India and Bilateral Investment Treaties*, PRS Legislative research, available at: https://prsindia.org/policy/report-summaries/india-and-bilateral-investment-treaties#:~:text=BITs%20establish%20minimum%20guarantees%20between,protection%20from%20expropriation%20(limiting%20each (last visited on 01-03-2023)
[2] *Bilateral treaty*, Britannica, available at: https://www.britannica.com/topic/bilateral-treaty
(last visited on 01-03-2023)

I. Introduction

Bilateral Investment Treaties (BITs) are a policy tool for promoting and protecting foreign direct investment (FDI). FDI is simply defined as a type of investment by a resident of one country in an enterprise in another country, indicating a significant influence and long-term interest. In the age of globalisation, FDI is regarded as an essential component of a free and prosperous global economic system and a key development tool[3].

According to popular belief, FDI brings a package of capital, skills, technology, marketing capabilities, management know-how, and access to foreign markets. These assets can help to build local capacity, consumer welfare, industrial change, employment and income, higher labour and environmental standards, and higher living standards. Because of the benefits associated with FDI, developed and developing countries have opened their economies and implemented FDI-friendly policies to attract more foreign investment. However, the impact of BITs on a country's policy space requires scholarly investigation.

The proposed study will investigate these treaties and their impact on policy space, focusing on the BITs signed by India. It is argued that BITs limit sovereign governments' ability to take policy measures to promote and protect domestic development goals. Policy space is defined as an autonomous decision-making space that a host country government considers essential for promoting and protecting its citizens' basic needs[4].

It is argued that BITs emerged as a key instrument of international investment law for promoting and protecting global investment movement. BITs have traditionally been used by Capital Exporting Countries (CECs) to legally and financially protect their nationals in host countries. As a result, the vast majority of investment treaties are concluded between developing and developed countries.

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[3] *India and Bilateral Investment Treaties*, PRS Legislative research, available at: https://prsindia.org/policy/report-summaries/india-and-bilateral-investment-treaties#:~:text=BITs%20establish%20minimum%20guarantees%20between,protection%20from%20expropriation%20(limiting%20each (last visited on 01-03-2023)

[4] *Bilateral treaty*, Britannica, available at: https://www.britannica.com/topic/bilateral-treaty (last visited on 01-03-2023)

Capital flows into and out of India have both increased steadily since the liberalisation regime of 1991. Investors, scholars, and corporations alike have taken notice of India's recent surge in FDI abroad. Most current theories of FDI focus on the flow of money from developed to less developed nations. So far, the phenomena of OFDI from emerging countries like India has been understudied. Current theories of foreign direct investment focus extensively on the Firm Specific Advantages (FSAs) garnered by MNCs based in the developed world. These ideas are grounded in corporations from developed countries, but they are insufficient to explain the increase in OFDI from developing countries like India, which do not have the same FSAs as their counterparts in the developed world. In addition, there is a lack of theoretical grounding with regard to (w.r.t.) emerging countries like India in the extant literature on OFDI from developing countries like India, both at the macro and firm level.

II. History

Pakistan and Germany signed the first BIT in the world in 1959. At the end of the 1980s, the total number of BITs in the world was 371. Their number skyrocketed during the 1990s, at the height of the FDI liberalization era, reaching 1,862 by the end of the decade. By the end of 2016, that figure had risen to 2,960[5]. The primary function of BITs is to protect investors' interests in order to encourage them to invest in other countries, particularly developing ones. BITs are based on mutually agreed-upon principles.

The main provisions of BITs that contribute to a long-term investment environment are clauses such as Full Protection and Security (FP&S), Fair and Equitable Treatment (FET), Most Favored Nation (MFN), national treatment, expropriation, and, most importantly, Investor State Dispute Settlement (ISDS) - the right of an investor to approach an international investment tribunal in the event of a dispute with the host State.

[5] Vandevelde, Kenneth J., *Bilateral Investment Treaties: History, Policy and Interpretatio*n,Thomas Jefferson School of Law Research Paper No. 3022249, Available at SSRN: https://ssrn.com/abstract=3022249 (last visited on 01-03-2023)

III. Indian Aspect

India is the country with the second-largest population and seventh-largest landmass in the world. One of the economies that could expand the fastest is this one. Nonetheless, FDI is viewed as a key conduit for promoting quicker economic growth in the age of economic globalization[6]. In order to welcome FDI, India, like other developing nations, signed multiple BITs. The World Bank and the International Monetary Fund (IMF) provided support for the structural adjustment and macroeconomic stabilization program that the Indian government launched in July 1991.

The same year saw the promulgation of the New Industrial Policy (NIP), which paved the way for extensive liberalization and accelerated India's economic integration with the rest of the world. The NIP and subsequent policy updates had loosened FDI limitations. India was further compelled to adopt trade liberalization by allowing FDI into a number of its economic sectors by the Balance of Payments (BoP) crisis of 1991. India quickly overtook China as the second-largest recipient of FDI after that country with 84 countries, India has signed BITs, 72 of which are already in effect. Moreover, India is currently negotiating new BITs with a select group of nations, including the US and Canada. In addition to BITs, India has also ratified Comprehensive Economic Cooperation Agreements (CECAs) with a select group of nations, which include investment-related chapters.

India is also experiencing significant difficulties as a result of its BITs, just like many other nations. Early in the 1990s, the Indian government signed a series of BITs to liberalise its economy without considering any potential risks. It has taken two decades, but people are finally realizing how risky the BITs India signed are. It is stated that the majority of India's conflicts resulted from its BITs' vaguely written, unconditional, and unspecific terms.

[6] Tracing the History, and Impact, of India's Bilateral Investment Treaties, The wire, Available at https://thewire.in/books/prabhash-ranjan-bilateral-investment-treaties, (last visited 01-03-2023)

IV. Relationship Between FDI And Development

Based on their findings, studies on the connection between FDI and development can generally be categorized into four groups. One perspective holds that FDI has a good impact on the economic development of host countries, whereas the other holds that FDI has a detrimental impact. The third perspective holds that FDI has no effect on development, while the fourth holds that FDI only has a beneficial influence if the host country has met certain requirements[7].

Both FDI and BITs received increasing attention with the rise of globalization and the integration of the world's markets. Most emerging nations significantly changed their perspectives as they adopted a liberal approach to international investment. Developing nations implemented policies to allow foreign investment to play a larger role in their economies because they believed it was essential for strengthening their macroeconomic foundation and hence improving economic performance. In order to attract and approve FDI, they, therefore, changed their development strategies to place a greater emphasis on outward orientation, competitiveness, and privatization. FDI is mostly from the developed world and is channelled through MNEs. China Construction Bank, Toyota Motor, Verizon Communications, Wal-Mart Stores, PetroChina, Samsung Electronics, Volkswagen Group, Microsoft, Nestlé, Ford Motors, IBM, Pfizer, Siemens, Deutsche Telekom, and many others are among the largest MNEs in the world and key providers of FDI. Asia continued to receive the most FDI at the end of 2016, totalling around $500 billion[8]. The bulk of BITs was finished in the 1990s. This decade drastically altered the BITs landscape. BITs quickly spread over the globe during this time. By the end of the 1990s, there was 1,857 BITs total, up from 385 at the end of the 1980s.

Basically, BITs are reached based on a set of agreed-upon principles, which include demands that the host State gives the foreign investor FET, MFN treatment, FP&S, national treatment, etc. Even amongst BITs signed by the same country, the specific content of the provisions may noticeably vary within these general terms, indicating different methodologies and negotiating stances.

[7] Sarker, B., Khan, F. *Nexus between foreign direct investment and economic growth in Bangladesh: an augmented autoregressive distributed lag bounds testing approach.* Financ Innov Available at: https://doi.org/10.1186/s40854-019-0164-y (last visited on 01-03-2023)
[8] Ibid.

These responsibilities are enforced via a special investor-state dispute settlement (ISDS), which provides the foreign investor with the right to challenge a sovereign host country in international arbitration in the event of a dispute under a BIT[9].

V. Problems With BITs

A new trend in investment agreements has emerged during the past few years. It has been observed that these agreements, particularly the BITs, which were originally signed to encourage FDI are now generating disputes as a result of the large number of foreign investors who have brought legal claims against sovereign States utilizing the BITs. Whenever foreign investors discover that any government policy or action has a negative impact on their investment, they can use several BIT clauses to sue the sovereign governments. By the end of 2016, there were 767 known ISDS cases involving foreign investors who had used various arbitral procedures. Of these, 63% were brought by the International Centre for Settlement of Investment Disputes (ICSID), 26% by the United Nations Commission on International Trade Law (UNICITRAL), and 4% by the Stockholm Chamber of Commerce[10].

Investment-based disputes are currently on the rise. According to UNCTAD, 70 new ISDS claims were made against various nations in 2015 alone, making it the year with the most disputes reported. The 767 cases have been made publicly known as at this point, as detailed in section 3.3. At the end of 2016, 444 ISDS cases had been resolved, with 36% of cases going in the States' favor, 26% going in the investors' favor, 26% being settled, 10% being abandoned, and 2% going in neither party's favor (responsibility identified but no damages paid). Moreover, 57 rulings were rendered by various IATs in 2016; only 41 of those decisions were made public.From a level of roughly 50 claims in total in 2000, cases have grown rapidly over the following 15 years to reach a total of 696 instances in 2015. The vast number of claims made by foreign investors, which place host countries in precarious situations, illustrates the seriousness of the situation.

[9] UNCTAD Press Release No. PR/2013/007 dated 10th April 2013.
[10] Summeet Kachwaha, *India: The New Challenges And Opportunities For India In Bilateral Investment Treaties*, Mondaq, available at: https://www.mondaq.com/india/fiscal--monetary-policy/1165638/the-new-challenges-and-opportunities-for-india-in-bilateral-investment-treaties (last visited on 01-03-2023)

Since 1994, India has begun to finalize investment agreements as a participant in the global economy. BITs, also known as Bilateral Investment Promotion and Protection Agreements (BIPA) in India, are the most popular type of investment agreement that India enters into. The founding of the British East India Company is where foreign investment in India first began. During her reign in India, the British provided India with the first and most significant foreign money. Nonetheless, a small number of other MNCs, mostly from Japan, entered the Indian market after India gained independence from British Control. Moreover, MNEs and foreign investment were the emphasis of the administration during this time. As a result, the Indian government's industrial strategy of 1965 allowed foreign MNEs to engage in technical collaboration.

The Indian government has provided many incentives for foreign MNEs to attract more foreign investment, including simplified licensing procedures and tax breaks. Unfortunately, India encountered a formidable in early 1990s Balance of Payments (BoP) crisis India lacked the foreign exchange reserves necessary for imports. In response, the Indian government began economic reforms in 1991[11].In July 1991, the Indian government began a structural adjustment and macroeconomic stabilization program supported by the World Bank and the International Monetary Fund (IMF). The same year, the "Statement on Industrial Policy" (also known as the "New Industrial Policy (NIP)"), which provided the foundation for extensive liberalization and accelerated India's path of economic integration with the rest of the world, was promulgated. The NIP and subsequent policy changes introduced the FDI regime and the State's industrial policy structure.

The 1991 BoP crisis made it easier for India to accept trade liberalization by allowing FDI into a number of its economic sectors. India quickly overtook China as the second-most popular location for FDI inflows. Prior to 1991, Indian policymakers had placed tight regulatory restrictions on the economy and guided it toward a centralized economic system.The administration used an import substitution strategy. Nonetheless, the Indian government created and carried out its infrastructure and investment program based on the five-year plans after the country gained its independence in 1947. As a result, the administration was able to build its policies around short-term objectives and analyze the nation's economic performance using macroeconomic indexes.

[11] *Why developing countries are dumping investment treaties*, The conversation, available at: https://theconversation.com/why-developing-countries-are-dumping-investment-treaties-56448 (last Visited on 27-03-2023)

Trade liberalization, the structure of the state's currency rate system, and the size of its fiscal deficit are all considered macroeconomic indexes. Also, when assessing the state of the economy, the number of natural resources and infrastructure was taken into account[12].

India engaged into a number of BITs to encourage and safeguard foreign investments and to facilitate the influx of FDI. India and the UK signed their first BIT in 1994. At the end of 2016, India had signed a total of 84 BITs, of which 72 are still in effect. India is now negotiating a number of new BITs with nations like the US and Canada. India has also inked a few CECAs (comprehensive economic cooperation agreements) in recent years that include chapters on investment. Like the BITs of other nations, those of India are likewise based on a few fundamental principles, including the provision of ISDS, Full Protection and Security (FP&S), National Treatment, Most Favoured Nation (MFN) Treatment, and Fair and Equitable Treatment (FET) for foreign investors.

India has undertaken a number of projects over the past 20 years to offer adequate infrastructure, including public roads, railway lines, cutting-edge technology, and irrigation, in an effort to stay up with international standards. Due to numerous policy changes that have been implemented since 1991, India currently relies on FDI to achieve its infrastructure goals and targets. For the Indian economy to grow at a rate that is sustainable, significant foreign investment in infrastructure has been deemed essential. Due to this desire, a number of public infrastructure projects have changed their regulatory framework to allow for private sector participation and competition.The latest surge of investment conflicts, which contested the state's legislative, executive, and even judicial activities, however, demonstrated that all is not well with the Indian BITs. It is clear that all complaints based on BITs against India are a result of the BITs' general and ambiguous language.

The almost 84 accords that make up the Indian BIT regime. All of these agreements were signed within the last 20 years, which was also the time when investment agreements proliferated internationally. With economic changes implemented in 1991, India opened its economy to global businesses. Inviting FDI was the main goal of the economic reforms.

[12] Kinda Mohamadieh, *Challenges of Investment Treaties on Policy Areas of Concern to Developing Countries,* available at: https://www.g24.org/wp-content/uploads/2019/03/Challenges_for_developing_countries_in_IIAs.pdf (last visited on 27-02-2023)

India, like a number of other nations, is dealing with many difficulties as a result of its BITs. The BITs signed by India contain a number of flaws. Early in the 1990s, India signed a series of BITs to liberalise its economy without taking any potential risks into account. However, after twenty years, it is now recognized that India's BITs are risky. While examining the problems in India's BITs, one can discover that the majority of the issues India encounters are caused by the unconditional, vague, and broadly drafted clauses in India's BIT.

ISDS is a feature of every BIT that India has signed. The ISDS was established to resolve investor-State disputes resulting from BITs, but governments of several States, including India, are increasingly gradually questioning it. MNEs have recently started exploiting the ISDS mechanism's international arbitration clauses to challenge governments in nations where they invest, undermining host States' national policy decisions. Since foreign investors can directly challenge host States at an international level thanks to the ISDS provision, rather than bringing lawsuits in the host State's national courts, the majority of BIT have an influence on the sovereignty of host governments. Recent BIT disputes cost the host States millions of dollars in compensation. In IATs, India is also dealing with a number of ISDS-related dispute cases[13]. Due to the presence of ISDS, foreign investors have the ability to address their concerns to a global organization that has the power to resolve them by levying severe penalties against sovereign States and paying out significant settlements[14].

VI. Conclusion

By the end of 2016, there had been a $1.52 trillion global FDI inflow. At the end of 2016, there were 2,953 BITs in existence worldwide. India signs its first BIT with the UK in 1994 following the economic changes of 1991. At the moment, India has 84 BITs overall. It is now understood, nevertheless, that there are a number of gaps in these agreements that must be filled. The provisions concerning investor and investment definitions, MFN, FET, national treatment, and ISDS are the most open to various interpretations by investors and IATs. The Indian government adopted a new model BIT in 2015 in an effort to address its shortcomings[15].

[13] http://www.nishithdesai.com/fileadmin/user_upload/pdfs/Bilateral_Investment_Treaties_and_India.pdf
[14] Ibid.
[15] DAS, K. (2014). *Dispute Settlement in Bilateral Investment Agreements: Whither India*? Economic and Political Weekly, 49(28), 22–25. http://www.jstor.org/stable/24480295 (Last visited on 01-03-2023)

A firm or other body with its headquarters in one nation may invest in the territory of another nation. Most FDI is channeled through MNEs. The earlier imperialist and colonial periods can be used to track the history of MNEs in India. In the age of globalization, FDI is viewed as the primary tool for accelerating development[16].Yet, how much FDI can be utilized relies on the policies of the host nation. Such policies should be able to direct FDI in accordance with the host country's development priorities, which require an independent policy space.

After nearly 21 investment disputes, India began to examine its previous BIT framework in 2012. A draft of a model BIT was made available for public comment in April 2015. New concept was accepted by Union Cabinet in December 2015. The public's response to the new model BIT was unresolved. The new model BIT has a lot of improvements. For instance, its numerous sections now have more precise meanings than they had in the past, which were more general. With a few minor tweaks, the most contentious component of the new BIT regime—ISDS—remains in place. Foreign investors can continue to use IATs for any BIT-based dispute in the future despite the small amendments to ISDS, which can only postpone their use.

[16] Egger, P., & Merlo, V. (2012). *BITs Bite: An Anatomy of the Impact of Bilateral Investment Treaties on Multinational Firms.* The Scandinavian Journal of Economics, 114(4), 1240–1266. http://www.jstor.org/stable/23356956 (Last visited on 01-03-2023).