# TREATY EXCLUSIONS AS THE UNTAPPED INSURANCE POLICIES FOR STATES AGAINST INVESTORS: DEVELOPMENT IN INDIAN MODEL

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**Abstract**

International Investment Agreements have mostly revolved around protecting the rights of the investors. In a bid to balance investor's rights and public interests, there has been a shift towards enhancing the powers of the state. Beyond its regulatory powers, the state requires to take measures 'necessary' for their 'essential security interests'. Such requirement has been enabled by the Treaty exclusions. An overview of India's model Bilateral Investment Treaties explain the modern trend of having diverse exceptions, demarcated as general exceptions, security exceptions as well as carve-outs. These exclusions have a common precondition of necessity that brings objectivity in the use of more than regular power. By analysing the state's perspective vis-a-vis India-investor dispute, this essay explores the state's failure to tap the insurance cover provided by the treaty exclusions and how they are amending their past mistakes.

Keywords: necessary, essential security interest, Bilateral Investment Treaty, investor obligations

## Part I: Introduction

International Investment Agreements ("**IIA/IIAs**") are the confluence of promises to and expectations from the international investors by contracting parties. States promise maintenance of four pillars of international investment- Fair and Equitable Treatment ("**FET**"), Full Protection and Security ("**FPS**"), National Treatment ("**NT**") and Most-Favoured Nation Treatment ("**MFN**"). These pillars are in tandem with the regulatory powers of the states, that are exercised non-discriminatorily and proportionately to meet the state's public policy objectives without violating the legitimate expectations of the investors.[1]

In return, IIAs provide for minimal expectations from investors to observe the law of the land. The Arbitral Tribunals have not shown much emphasis on the investor obligations. The trend in investor disputes with India has mostly tilted in favour of investors. There are two probable reasons: first, India's conduct that would be expropriatory, discriminatory, or in violation of any of the four pillars; second, India was devoid of enough treaty exclusions to defend their cause.

This essay focuses on the second leg of reasoning for India's inability to safeguard its policy objectives. This would prompt analyses of the *Deutsche Telekom v India* ("**DT**") where State argument for "national security" defence failed.[2] However, 2015 model Bilateral Investment Treaty ("**BIT**") has been the advent of new insurance policies in favour of the State as provisions of Exceptions.[3] This essay aims to explore the treaty exclusions in the latest Indian IIAs and comprehend how these exclusions could change the dynamics in India-investor disputes.

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[1] Brazil-India BIT, art. 6.4, Direct Expropriation.

[2] Deutsche Telekom v. India, PCA Case No. 2014-10, Interim Award, 13 December 2017, ¶¶288-291.

[3] India Model BIT 2015, ch. 6.

Firstly, this essay will provide a basic overview of the treaty exclusions- general exceptions and security exceptions, carve-outs and other types. It will include the discussion on the shift in the provision of non-precluded measure to defence of necessity. Since this discussion would be incomplete without interpreting the Tribunal decisions in Argentine disputes, this essay will analyse the application of NPMs or defence of necessity in Indian disputes vis-a-vis Argentine disputes. Secondly, it will highlight that treaty exclusions and regulatory powers of the state are a pair of scales that needs to be balanced to sprout the best possible combination of investor's rights and obligations.

## Part II: Types of exclusions catering to State's diverse regulatory purposes

### A. Structure of the General Exception, Security Exceptions and Carve-outs

Treaty exclusions are defences to host states against any liability towards foreign investors. They are the last line of defence to states that shield them in the event of failure of their regulatory powers. When the state's conduct is proved to be in breach of any of the clauses of an IIA, exclusions or exceptions provide the last resort within the IIA to protect state's regulatory conduct. There are three distinct kinds of exceptions available in an IIA, i.e., General Exceptions, Security Exceptions and Carve-Outs. Post-2018, tax measures and provisional measures are being added generally to the BITs.[4]

General Exceptions apply when a measure is deemed necessary to protect- "public morals", "public order"; "human, animal or plant life or health"; or "to secure compliance with laws or regulations which are not inconsistent with the Agreement".[5]

Security Exceptions is a more vital defence to protect host states' "essential security interests", "public order" or obligations towards "international peace or security". It can either be in the form of NPM or as a customary international law defence of necessity under Article 25 of International Law Commission ("**ILC**") Draft Articles. In Indian model, there has been a shift from NPM to necessity within the BIT.

The next form of exclusion is a carve-out wherein a specific field may be excluded from observance of general obligations while exercising regulatory powers of the state. The Energy Charter Treaty in its Part IV have carve-outs for environment, taxation, and other specific measures.[6]

### B. Good Faith doctrine raises the threshold for the satisfaction of an exception

In *Antin v Spain*, the Tribunal in reference to a tax carve-out held that the state can benefit from such carve-out when it demonstrates good faith.[7] The same is true for general and security defences as well. The Tribunal in *LG&E v Argentina* accepted the economic necessity defence

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[4] Crina Baltag et al., *Recent Trends in Investment Arbitration on the Right to Regulate, Environment, Health and Corporate Social Responsibility: Too Much or Too Little?,* ICSID REVIEW - FOREIGN INVESTMENT LAW JOURNAL, Volume 38, Issue 2, Spring 2023, at 381–421,

[5] Asean Comprehensive Investment Agreement 2009, art. 17, General Exceptions;

[6] ECT, part IV.

[7] Infrastructure Services Luxembourg S.à.r.l. and Energia Termosolar B.V. (formerly Antin Infrastructure Services Luxembourg S.à.r.l. and Antin Energia Termosolar B.V.) v. Kingdom of Spain, ICSID Case No. ARB/13/31, Award, 15 June 2018, ¶314.

raised by the host state for a specific period when extremely severe crises reached its culmination point, threatening a total collapse of the government.[8]

Test of good faith does not render the exclusions as an unbridled defence. As per *Renergy v Spain*, there exists a presumption of bona fide measure while the Claimant must disprove that presumption.[9] *Renergy* failed to cross the higher evidentiary threshold.[10] Even in customary law the defence of necessity has a high threshold since the measure taken should be the only means to prevent a grave and imminent peril from threatening the essential security interest of the state. Contrary to *LG&E*, Argentina in *CMS* failed to show that measure was the only means to thwart the economic crises.

The threshold of necessity for an IIA provision differs from that of customary law necessity. The DT Tribunal in explains that requirements depend upon the text of the provision. India traditionally has NPMs in their IIAs. Article 12(2) of the 2003 model BIT used the phrase "nothing in this Agreement precludes the host Contracting Party from taking action" while Article 33 of the 2015 model BIT uses the phraseology "Nothing in this Treaty shall be construed". India following the post-2018 trend to make of its regulatory powers.

### C. Customary Law Necessity v. Lex Specialis Necessity

The conundrum around defence of necessity between customary international law and an IIA has always been a tough nut to crack for the Tribunals. Both the defences have antithetically been treated as similar and dissimilar in different cases. Argentina raised it in both ways in the cases of *CMS*,[11] and *Sempra*[12]to protect their national economic interest. In *CMS* and *Sempra*, no such difference was made out but, in *El Paso*,[13] and *Continental Causualty*,[14] the Tribunals did not keep the two necessities on the same pedestal.

Preliminary, the DT tribunal identified the two defences to be 'substantially different' because their requirements are not the same. Referring to *Sempra*'s ad hoc committee,[15] the Tribunal said that Article 25 of ILC Draft Articles cannot be used to define necessity for the purpose of the concerned BIT (which was US-Argentina BIT in that case). Article 25 states that the necessary measure taken must be the 'only means' to protect the 'essential security interest' against a 'grave and imminent peril'. Article 12 of the Germany-India BIT had comparatively milder terms since the Tribunal entertained that State may meet the requirements of an exception clause without satisfying essentials of Article 25.[16]

Article 12 of this BIT being a non-self-judging clause, the Tribunal does determine if there is an actual threat requiring the measure challenged or not. The clause contextually did not

[8] LG&E v Argentina, ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006.
[9] RENERGY S.à r.l. v. Kingdom of Spain, ICSID Case No. ARB/14/18, Award, 6 May 2022, ¶¶478-480.
[10] *Id.*
[11] CMS Gas Transmission Company v. The Republic of Argentina, ICSID Case No. ARB/01/8, Award, 12 May 2005, ¶353.
[12] Sempra Energy International v. The Argentine Republic, ICSID Case No. ARB/02/16, Award, 28 September 2007, ¶388.
[13] El Paso Energy International Company v. The Argentine Republic, ICSID Case No. ARB/03/15, Award, 31 October 2011, ¶553.
[14] Continental Casualty Company v. The Argentine Republic, ICSID Case No. ARB/03/9, Award, 5 September 2008, ¶167.
[15] Deutsche Telekom v. India, PCA Case No. 2014-10, Interim Award, 13 December 2017, ¶228.
[16] Deutsche Telekom v. India, PCA Case No. 2014-10, Interim Award, 13 December 2017, ¶229.

express the measure to be what the party considers necessary but to the extent necessary. While articulating this contextual difference between a self-judging clause and a non-self-judging clause, India convincingly argued that the Tribunal must pay deference to the State's decision about a looming threat towards their 'essential security interest'. Like a mother to a child, a State would be the best assessor of what is necessary for its national interests.

For a measure to be necessary, time is always of the essence.[17] To India's dismay, the Tribunal observed that the measure did not target its 'essential security interests' since the debate regarding the correct course of action would not have taken four years had the measure remained necessary. One of the primary learnings India should imbibe is an understanding of their security interests that are 'essential'. This requires a diversion from the concept of necessity. *Devas v India* refreshens the perspective over an 'essential' interest because the objective precondition of necessity was omitted in the Mauritius-India BIT.[18]

Indian government has attempted to diversify its defences in line with the 2015 model BIT by adopting carve-outs like tax measures and provisional measures. They terminated more than 75 BITs[19] and are forging new reciprocal agreements with better insurance policies to balance public interest.

**Part III: India's brand-new tools that revamp its regulatory power**

In the latest Brazil - India BIT (2020), India has prima facie improvised since the clause text includes an objective perception of an 'essential security interest'. Actions relating to nuclear items, wars, ammunitions, critical public infrastructure as well as security clearances to a company are sitting on the front row while the gate for wider interpretation is kept open.[20] There are reservations regarding the misuse of these defences, but the Arbitral Tribunals shall always protect the investor's rights without compromising the powers of the states.

As held in *Copper Mesa v Ecuador*, it is not the Tribunal but the State who has "*sovereign rights, as regulator, to determine what lies within its national interests*."[21] The focal point of a State's measure should be upon a non-discriminatory, reasonable and proportionate measure unless and until exceptional circumstances exists. However, the state should not use treaty exclusions to justify its arbitrary actions since they would fail to pass the assessment by the Tribunal as happened in *Deutsche Telekom*.

The presence of objective precondition of necessity along with an understanding on the state's 'essential security interest' enhances the regulatory power while reducing the scope of misuse. They supplement the investor's obligations articulated as Compliance with laws and Corporate Social Responsibility in Chapter III of the 2015 model BIT.[22] Not only will the state be able to keep their powers within reasonable bounds but also impress upon the obligations of an investor. As the Hohfeld's theory provides that rights are coupled with duties, an investor must be obligated to support a state's regulatory measure.

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[17] Deutsche Telekom v. India, PCA Case No. 2014-10, Interim Award, 13 December 2017, ¶¶290-291.

[18] CC/Devas v. India (I), PCA Case No. 2013-09, Award on Jurisdiction and Merits, 25 July 2016, ¶¶229-242.

[19] Mauritius-India BIT 1998,

[20] Brazil-India BIT, art. 24, Security Exceptions.

[21] Copper Mesa v. Ecuador, PCA Case No. 2012-02, Award, 15 March 2016, ¶6.64.

[22] India Model BIT 2015, ch. 3.

Diversification of treaty exclusions indirectly enables acknowledgement of investor obligations as an investor would have to cooperate with the state. Cases like *Bear Creek v Peru*[23] and *SAS v Bolivia*[24] evince the difficulty in balancing investor's obligations with that of the state to compensate. Treaty exceptions help to avert the problem by listing the conditions when a state shall not be held liable to compensate for the damage caused to the investor.

**Part IV: Conclusion**

The past BITs included the most generic exceptions which rendered the usage of these defences by the states frivolous and arbitrary. With the instance of India in *Deutsche Telekom*, it is crystallised that State's lacked the basic understanding of either what is 'necessary' or what is there 'essential security interests'. However, it is undeniable that India has developed upon its knowledge reflective in the 2015 model BIT and being incorporated in the newly crafted BITs like one between Brazil and India.

The new reciprocal agreements would not just focus on the rights of investors but also create their obligations. Redefining the treaty exceptions may potentially allow India and similar states to protect their 'essential' national interests as well as help gain the Arbitral Tribunals deference for state's necessary measure.

[23] Bear Creek Mining Corporation v. Peru, ICSID Case No. ARB/14/2, Award, 30 November 2017
[24] South American Silver ( SAS ) v. Bolivia, PCA Case No. 2013-15, Award, 22 November 2018.