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India Considers Qualified MFN in Revised Investment Treaty Framework to Balance Investor Protection with Regulatory Autonomy

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Recent Developments:

- India is reviewing its **Bilateral Investment Treaty (BIT) framework** to make it more attractive to foreign investors while retaining adequate **regulatory policy space** for the State.
- As part of the proposed overhaul, India is reportedly considering a **limited or Qualified Most-Favoured Nation (MFN) provision** instead of restoring an unrestricted MFN clause.
- The review follows concerns that India's existing investment-treaty framework may be relatively restrictive for foreign investors, particularly regarding access to **international arbitration**.
- The Government is also examining the requirement under the existing framework that investors pursue domestic remedies before initiating international arbitration, with the present **five-year period** reportedly under review.
- The reform has wider significance because India is simultaneously seeking greater **foreign direct investment** , negotiating investment treaties and expanding opportunities for Indian companies investing abroad.

Bilateral Investment Treaties:

Meaning and Purpose:

- A **Bilateral Investment Treaty** is an agreement between two countries that establishes rules for the protection and treatment of investments made by investors of one country in the territory of the other.
- BITs generally seek to reduce investment-related uncertainty by establishing standards concerning **non-discrimination, fair and equitable treatment, expropriation, transfer of funds, protection and security, and dispute settlement**.
- Many BITs provide an **Investor-State Dispute Settlement mechanism**, under which an eligible foreign investor may bring certain claims against the host State before an international arbitral tribunal.
- BITs are therefore intended to create a more **predictable and rules-based investment environment** while balancing the interests of investors and host States.

India's Model BIT Approach:

- India adopted its **Model BIT in 2016**, following concerns arising from investment disputes and international arbitration involving the country.
- The Model BIT adopted a relatively cautious approach towards investor protection and sought to preserve greater **policy and regulatory autonomy** for India.
- The framework did not retain a broad, open-ended **MFN clause**, reflecting concerns about investors importing favourable provisions from India's treaties with third countries.
- The current review therefore represents an attempt to recalibrate the framework rather than simply return to the earlier unrestricted approach.

Most-Favoured Nation Principle in Investment Treaties:

Meaning of MFN:

- In an investment treaty, the **MFN principle** generally requires a State to provide investors from one treaty partner treatment that is **no less favourable** than the treatment provided to investors from another treaty partner.
- For example, if India grants investors from Country A a particular investment protection under a later treaty, an applicable MFN clause could potentially allow investors from Country B to seek similar treatment under India's treaty with Country B.
- The underlying objective is to prevent **discriminatory treatment among foreign investors** from different treaty partners.

Why MFN Became Controversial for India:

- An unrestricted MFN clause can potentially allow an investor to rely on provisions negotiated by the host State with a **third country**, even when those provisions were not included in the investor's own treaty.
- This can create uncertainty regarding the actual obligations that a State accepted during the original treaty negotiations.
- Investment tribunals have differed in their interpretation of the scope and application of MFN clauses, particularly concerning whether MFN provisions can be used to import **substantive protections or procedural rights**.
- India therefore moved away from a broad MFN approach in its revised investment-treaty policy.

Qualified MFN:

Concept:

- A **Qualified MFN provision** would preserve the principle of non-discrimination while imposing clearly defined limitations on its operation.
- Instead of allowing investors to automatically claim every favourable provision available in another treaty, the clause could specify **which provisions may be imported, which treaties may be considered and under what circumstances MFN treatment may apply**.
- The approach could also clarify whether MFN treatment applies **retrospectively**, whether previously settled disputes can be reopened and which categories of investment protection are covered.

Why India May Prefer Qualified MFN:

- Qualified MFN can provide greater **investor confidence** without creating an unlimited mechanism for importing provisions from unrelated treaties.
- It can reduce interpretational uncertainty and help India maintain greater **regulatory autonomy**.
- It can also become a negotiating instrument because India could seek comparable treatment for its own investors in major overseas markets.
- A carefully drafted MFN clause can therefore attempt to balance **investment protection, treaty certainty and sovereign policy space**.

MFN under Investment Treaties versus WTO:

Key Difference:

- The **MFN principle in investment treaties** concerns the treatment of foreign investors and investments under bilateral or regional investment agreements.
- The **WTO MFN principle** is a core principle of the multilateral trading system and generally requires a WTO member to extend trade advantages granted to one member to other WTO members on a non-

discriminatory basis.

- Under the **General Agreement on Tariffs and Trade**, MFN is contained in **Article I**, while the **General Agreement on Trade in Services** contains MFN treatment in **Article II**, and the **TRIPS Agreement** contains it in **Article 4**.
- Therefore, the two applications share the broader idea of **non-discrimination**, but operate within different legal frameworks and cover different subject matter.

UPSC Distinction:

- **Investment-Treaty MFN:** Protects investors from discriminatory treatment vis-à-vis investors of third countries, subject to the wording of the particular treaty.
- **WTO MFN:** Promotes non-discrimination among WTO trading partners in the treatment of goods, services and intellectual-property-related trade obligations.
- **Important:** MFN does not mean giving a country a uniquely preferential status; within the WTO system, it principally means extending comparable trade treatment to members without discrimination.

Investment Dispute Settlement and India's Approach:

Investor-State Dispute Settlement:

- **Investor-State Dispute Settlement** allows qualifying foreign investors to challenge certain State measures through international arbitration under the applicable investment treaty.
- India has historically become more cautious about ISDS because investment disputes can involve substantial financial claims and questions concerning the balance between **investor protection and sovereign regulatory powers**.
- India's Model BIT therefore sought to strengthen the requirement for investors to first use **domestic judicial remedies** before accessing international arbitration.
- The current review reportedly considers shortening the existing domestic-remedy period, reflecting concerns that prolonged pre-arbitration requirements can reduce India's attractiveness to foreign investors.

Why India Is Reconsidering the BIT Framework:

Need to Attract Foreign Investment:

- India seeks to make its investment regime more **predictable, competitive and investor-friendly** while retaining safeguards against excessive treaty claims.
- India's net FDI inflows reportedly declined to approximately **USD 7.7 billion in FY 2025–26**, significantly below the levels seen in some competing Asian economies.
- A more predictable investment-treaty framework could strengthen investor confidence, particularly among investors from developed economies.

Protection of Indian Investors Abroad:

- The reform is not only about attracting foreign capital into India.
- A carefully designed MFN provision could strengthen India's bargaining position when negotiating investment treaties with major economies such as the **United States and European Union**.
- Indian companies investing abroad could potentially benefit from **non-discriminatory treatment** and comparable investment protections in partner countries.
- MFN could therefore operate as both an **investor-protection mechanism and a diplomatic negotiating instrument**.

Advantages of Qualified MFN for India:

Balancing Competing Objectives:

- **Investor Protection:** Qualified MFN can provide foreign investors with greater certainty regarding non-discriminatory treatment.
- **Regulatory Autonomy:** Explicit limitations can prevent investors from automatically importing every favourable provision from unrelated treaties.
- **Treaty Predictability:** Clear drafting can reduce disputes over the scope and interpretation of MFN provisions.
- **Negotiating Leverage:** MFN can strengthen India's position while seeking reciprocal protections for Indian investors abroad.
- **Investment Climate:** A balanced framework can improve India's attractiveness without substantially weakening the State's ability to regulate in the public interest.

Potential Challenges:

Drafting and Interpretation:

- The effectiveness of Qualified MFN will depend heavily on **precise treaty drafting**.
- Ambiguous language could recreate the very interpretational disputes that India sought to avoid through its restrictive Model BIT approach.
- India will need to clearly define the **scope, exceptions, temporal application and procedural consequences** of MFN treatment.

Balancing State and Investor Interests:

- Excessively restrictive provisions may discourage foreign investment by reducing the practical value of treaty protection.
- Excessively broad provisions may expose India to extensive claims and reduce regulatory flexibility.
- The central policy challenge is therefore to establish an appropriate balance between **investor confidence and sovereign regulatory space**.

Broader Significance for India's Economic Diplomacy:

Investment Treaty Network:

- India's BIT policy is increasingly important because the country is negotiating and updating investment agreements with multiple economic partners.
- Recent developments, including India's willingness to advance **BIT negotiations with Canada**, demonstrate the continuing importance of investment treaties in India's external economic strategy.
- The revised framework could therefore become a common negotiating template for India's future investment agreements.

Integration with FDI Policy:

- BIT reform should complement India's domestic efforts to improve the **ease of doing business, investment facilitation and regulatory predictability**.
- The Government has also recently revised aspects of its FDI framework, with the revised regime facilitating certain investments involving **non-controlling beneficial ownership from land-bordering countries**.
- A coherent combination of domestic investment reforms and modern BITs can strengthen India's position in global investment flows.

Way Forward:

Policy Priorities:

- India should adopt a **clearly defined Qualified MFN clause** that identifies the provisions capable of being imported from third-country treaties.
- The framework should specify the treatment of **retrospective claims, settled disputes, procedural provisions and treaty exceptions**.
- Domestic dispute-resolution institutions should be strengthened so that investors have access to **efficient, credible and time-bound remedies**.
- India should pursue greater **reciprocity** so that stronger protection for foreign investors in India is accompanied by meaningful protection for Indian investors overseas.
- BIT reform should remain consistent with India's wider objectives of **FDI attraction, economic security, regulatory autonomy and global economic integration**.

Value Addition for UPSC:

Prelims Pointers:

- **MFN in investment treaties:** A non-discrimination principle concerning investors from different treaty partners.
- **WTO MFN:** A core multilateral trade principle reflected in **GATT Article I, GATS Article II and TRIPS Article 4**.
- **India's Model BIT:** Published by the **Department of Economic Affairs in 2016**.
- **Qualified MFN:** A restricted MFN mechanism subject to specifically negotiated conditions and safeguards.
- **ISDS:** A mechanism through which eligible foreign investors may pursue treaty-based claims against host States through international arbitration.

Potential UPSC Mains Question: *“India's reconsideration of a Qualified Most-Favoured Nation provision reflects an attempt to reconcile foreign-investor protection with regulatory autonomy. Examine the opportunities and challenges associated with this approach.”*

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