What’s in a Meme? The Truth about Investor-State Arbitration: Why It Need Not, and Must Not, Be Repossessed by States

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The current discourse on international investment law and investor-State arbitration is replete with inaccuracies and hypothetical fears. Certain quarters are clamoring for sweeping changes that would undermine the effectiveness of foreign investment protection by politicizing the existing neutral, juridical system for resolving investor-State disputes. With the impending expiration of over 1,000 investment treaties and the negotiation of two trade and investment treaties that would cover 65% of the world economy, the system stands at a watershed moment, calling for a comprehensive rebuttal to critics. We argue that proposals to politicize dispute settlement—by giving states control over adjudicators, introducing self-judging defenses, permitting retroactive treaty amendment through state practice, or relaxing the rules of treaty interpretation—should be rejected. The evidence demonstrates

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that investment treaties and arbitration benefit poor states, are even-handed, enhance transparency, allow states ample regulatory leeway, and promote the rule of law.

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Words ought to be a little wild for they are the assault
of thoughts on the unthinking.¹

John Maynard Keynes

INTRODUCTION

In 1998, the book Dealing in Virtue chronicled the rise of international arbitration and a corps of arbitrators who, through private ordering and intense competition, established themselves as trustworthy to resolve high-stakes cross-border disputes with integrity and rigor.² Nearly fifteen years after that study quietly noted incipient antipathy to international arbitration, a non-governmental organization (NGO) report entitled Profiting from Injustice broadcast its hostility to investor-State arbitration through an earsplitting bullhorn. The cover of that recent “exposé” features a group of faceless “suits” popping a bottle of champagne atop one side of the balance scale of justice as dollar signs waft up from a nearby briefcase; far overhead on the scale’s other pan perches a tiny white courthouse, evidently grossly outweighed by the sinister doings below. Driving home that graphic depiction of injustice, the report’s introduction quotes an Irish folk epigraph: “There is little use in going to law with the devil while the court is held in hell.”³

This propagandistic screed is but one of the current assaults on international investment arbitration by NGOs, press, popular media, academics, and various states, to wit:

- Bolivia, Venezuela, and Ecuador have denounced the

¹. John Maynard Keynes, National Self-Sufficiency, 22 YALE REV. 755, 768 (1933).


ICSID Convention\(^4\) or reduced the scope of their consent to settle disputes thereunder.\(^5\)

- The previous Australian Government adopted a policy (now abandoned) of no longer agreeing to arbitration with foreign investors.\(^6\)

- The then-Attorney General of Singapore (now its Chief Justice) opened the June 2012 conference of the International Council for Commercial Arbitration with a speech stating that international investment arbitration “has the potential to constrain the exercise of domestic public authority in a manner and to a degree perhaps not seen since the colonial era” and characterized international arbitrators as “modern-day uber-sophisticated ambulance-chasing plaintiffs’ lawyers . . . [because] rul[ing] in favor of investors from traditionally capital-exporting countries [is] the ‘price’ that has to be paid to gain credibility and access to the privileged club of elite international arbitrators.”\(^7\)

- South Africa has announced it will renegotiate or terminate its “first wave” investment treaties and will only enter into new treaties if there are “compelling

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reasons” to do so.8

- Ecuador is in the process of auditing its 25 BITs in the wake of several investor claims against it.9

- On April 22, 2013, the Hugo Chavez-inspired Bolivarian Alliance for the Peoples of the Americas (ALBA) declared its support for the project of the Union of South American Nations (UNASUR)10 to establish its own arbitration center for trade and investment cases. The declaration’s preamble states that “recent events in various countries of Latin America, concerning disputes between states and transnational corporations have shown that there are still cases where the judgment violates international law and the sovereignty of the states as well as its legal institutions, due to the economic power of certain companies and deficiencies of the international systems of dispute settlement on

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9. Mercedes Alvaro, Ecuador Plans to Audit Bilateral Investment Treaties, WALL ST. J. (Mar. 11, 2013), http://online.wsj.com/article/BT-CO-20130311-708469.html. This appears to be a softening of its position several years ago that it would withdraw from all of its BITs, see Ecuador to Denounce Remaining BITs, GLOBAL ARBITRATION REVIEW (Oct. 30, 2009), http://www.globalarbitrationreview.com/news/article/19251/.

10. UNASUR is an organization created in 2008 to encourage South American integration in various policy areas. See Historia [History], UNASUR, http://www.unasursg.org/ (last visited July 17, 2013).
investment.”11

- In 2011, Ecuador initiated state-to-state arbitration seeking a binding interpretation of its bilateral investment treaty (BIT) with the United States, in order to undermine, if not effectively nullify, an unappealable partial award that had been issued against it by a sitting tribunal established under the same BIT.12

- The Director of Public Citizen’s Global Trade Watch argued at an April 2013 meeting at the Council on Foreign Relations that BITs, “which aim to protect foreign investors from unfair and inequitable treatment by governments, are themselves arbitrary and unfair.”13

- Relying on Profiting from Injustice, the UN Conference on Trade and Development (UNCTAD) published a report advocating reform of investor-State dispute settlement, citing concerns including “a perceived deficit of legitimacy and transparency” and “questions about the independence and impartiality of arbitrators.”14

- Ecuador announced a plan to publish a blacklist of arbitrators who allegedly “have engaged themselves in

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destroying our nations.”

- The President of the Center for International Environmental Law testified before Congress urging the rejection of investor-State arbitration in the Transatlantic Trade and Investment Partnership, a treaty currently under negotiation between the United States and the European Union. He argued, “there is no pretext for granting foreign investors superior rights to domestic firms or subjecting our judicial systems to tribunals empowered to put the American public in a lose-lose situation. The inclusion of such provisions would have a chilling effect on the future development of regulations for public health, safety and the environment in the EU and U.S.”

The unfortunate result of such attacks is that states are increasingly working to constrain investment tribunals’ adjudicative role through back door channels. The most striking of these efforts are calls for states’ control over the selection of all investment dispute arbitrators. Thus, at the same time that the Government of Singapore has been promoting that country as a desirable venue for arbitrations, its Chief Justice has called for global regulation that effectively permits states to vet the arbitrators that investors can choose. There even have been proposals to return to diplomatic protection.

15. See Ecuador contactará con países para crear una “lista negra” de árbitros extranjeros [Ecuador contracted countries to create a “blacklist” of foreign arbitrators], FOX NEWS (July 6, 2013), http://latino.foxnews.com/latino/espanol/2013/07/06/ecuador-contactara-con-paises-para-crear-una-lista-negra-de-arbitros/.


18. See Menon, supra note 7. Menon was the Attorney General of Singapore when he made the abovementioned speech. He is now the Chief Justice of Singapore.

19. See, e.g., M. Sornarajah, Columbia FDI Perspectives no. 74: Starting Anew in International Investment Law, VALE COLUM. CTR. ON SUSTAINABLE INT’L INVESTMENT (July 16, 2012), http://www.vcc.columbia.edu/content/starting-anev-international-investment-law. Under diplomatic protection, investments are protected only by the diplomatic efforts of the
A wave of recent academic writings proposes various means by which states would exert greater control over the investment dispute resolution process to correct alleged flaws in the system. The most extreme proposals are appeals to eliminate investor-State arbitration entirely. Some suggest new rules of treaty interpretation that would effectively allow states to amend treaties retroactively, while others propose structures that would give states control over the eligibility of arbitrators who decide disputes, in line with the position taken earlier by the then Attorney General of Singapore. Still others propose rules of interpretation that give states heightened deference when they invoke particular values as the motivation for their actions. What all of these proposals by states, academics, and NGOs have in common is the urge to return investment dispute settlement to the control of states and thereby dispense with the present rule-based system of independent and impartial, hence apolitical, investment dispute resolution.

The issue is far from academic. Negotiations are underway for two multilateral treaties that, if concluded, will govern the investment relations of 65% of the world economy. The investment protections and investor-State dispute settlement provisions in those treaties—the Trans-Pacific Partnership and the Transatlantic Trade and Investment Partnership—therefore have the potential to immediately impact global governance of relations between foreign investors and host states as well as to influence future treaty negotiators.


Moreover, as of the end of 2013, an estimated 1,300 bilateral investment treaties are eligible for renegotiation or termination under their sunset clauses, with a further 350 treaties becoming eligible by 2018.24

At this watershed moment, calls to turn back the clock on investment dispute resolution should give particular pause. Over fifty years ago, states recognized that the political elements inherent in then-existing avenues of investment dispute resolution—domestic courts and diplomatic protection—inhibited vital capital flows and unduly strained international relations.25 Therefore, they created ICSID and other neutral fora for resolving investor-State disputes directly between host states and alien investors. The innovation of investor-State arbitration has fulfilled its promise of increasing foreign direct investment where it has been most acutely needed and curbing gunboat diplomacy. Reverting to a politicized system threatens such critical advances.

As against that great cost, the supposed benefits of repolitization, or “re-statification,” are illusory.26 The alleged faults that re-statification seeks to remedy—the purported sacrifice of poor countries, bias, and threats to public interest regulation—are supported by little more than endless repetition. What began as the refrain of New International Economic Order (NIEO)27 revivalists and globalization


26. For an extended discussion of the concept of re-statification, see Brower & Blanchard, supra note 2.

opponents has pervaded the conversation so thoroughly that many accept the criticisms as gospel. In its most extreme form, the argument made against international investment arbitration is that it is “poisoned at the root,” a farce that promotes entrenched capitalist interests at the expense of host states.  

A group of law professors issued a public statement on August 31, 2010 castigating foreign investment treaties and investor-State arbitration on the same basic grounds, but more subtly recording their “shared concern for the harm done to the public welfare by the international investment regime, as currently structured, especially its hampering of the ability of governments to act for their people in response to the concerns of human development and environmental sustainability.” Further along the continuum, UNCTAD baldly asserts that investor-State arbitration is antithetical to sustainable development. More recently, a group of “100 jurists” published an “Open Letter . . . to the Negotiators of the Trans-Pacific Partnership Urging the Rejection of Investor-State Dispute Settlement” expressing “concerns about how the expansion of this regime threatens to undermine the justice systems in our various countries and fundamentally shift the balance of power between investors, states and other affected parties in a manner that undermines fair resolution of legal disputes.” This vein of

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rhetoric relies on ideological assumptions and hypotheticals rather than demonstrating any actual harm from international investment law.32

Despite overwhelming counterevidence, this “meme” (to borrow Richard Dawkins’s term) of a broken system continues to proliferate, with assorted variations.33 Through that process, objections that began as ideologically driven polemics have come to be widely, but inaccurately, presumed as truths. Some international lawyers have advocated treating such uninformed and unsubstantiated claims with the seriousness they warrant—namely by ignoring them.34 In the process of communication that undergirds international lawmaking,35 however, memes can be powerful.

The objective of this Article is to destroy the meme that international investment law is deeply flawed and in need of reform, so that misguided reform proposals will not destroy the beneficial mechanisms of international legal cooperation desired by much of the community of nations. We do not seek to argue that the current system is perfect, but rather to provide context and balance to a very skewed conversation, and therefore to provoke deeper thought and discussion. We do so primarily by shifting the focus from unexamined, meme-engendered fears of hypothetical eventualities to observed experience with the existing system.

The Article proceeds as follows: Parts I through VII respond to the most pervasive memes about the international investment law regime. Part I counters the argument that the international investment legal regime furthers the interests of multinational corporations at the expense of poor states. It does so by reference to the most recent and sophisticated empirical research, which shows that credibly

32. See infra text accompanying notes 128–141; James D. Fry, International Human Rights Law in Investment Arbitration: Evidence of International Law’s Unity, 18 DUKE J. COMP. & INT’L L. 77, 79 & n.8 (2007) (also observing that such arguments typically “rely[] on hypothetical situations and weak counterfactual reasoning” and listing examples).

33. A “meme” is a unit of cultural transmission that replicates itself through individuals by inducing repetition. RICHARD DAWKINS, THE SELFISH GENE 192 (2d ed. 1989). A meme’s success does not depend on its truth or on whether it improves the long-term welfare of its hosts. See generally AARON LYNCH, THOUGHT CONTAGION: HOW BELIEF SPREADS THROUGH SOCIETY (1996).


35. Reisman, supra note 27, at 113.
binding investment treaties increase inbound investment for states that need it most. Part II addresses the critique that the current regime is one-sided by examining the outcomes of actual arbitrations. Part III responds to the argument that investment treaty arbitration is opaque. Part IV disputes the contention that such arbitration unduly constrains state policy discretion, by assessing what BITs and arbitral awards actually say, and Part V addresses the related contention of “regulatory chill.” Part VI counters the argument that investment treaties and arbitration contravene the rule of law. Finally, Part VII responds to the argument that some states’ recent rejection of the current system demonstrates its crumbling legitimacy, through both a rational choice analysis and a comparison with states’ behavior toward other international adjudicatory mechanisms. Part VIII assesses several proposed reforms of the international investment law system in light of the foregoing analysis.

I. THE MEME THAT INVESTMENT TREATIES AND ARBITRATION ARE HARMFUL OR INEFFECTIVE

To a great extent, the debate over BITs and investor-State arbitration is a debate about fundamental issues of political economy. It is a clash over the appropriate roles of the state and the private sector, played out in NGOs, the media, and the academy. NGOs opposed to globalization and international corporations publish polemics like Profiting from Injustice.36 The common message is encapsulated in the opening sentence of that paper: “The last two decades have witnessed the silent rise of a powerful international investment regime that has ensnared hundreds of countries and put corporate profit before human rights and the environment.”37 Sensationalist exposés such as this appeal to mistrust of markets in order to

36. EBERHARDT & OLIVET, supra note 3.
37. Id. at 7; cf. Chimni, supra note 28, at 1 (“[A] growing network of international institutions . . . constitute[s] a nascent global state, whose current task is to realize the interests of an emerging transnational capitalist class in the international system to the disadvantage of subaltern classes in the third and first worlds.”); Sornarajah, supra note 19 (arguing that the current system is “geared to promote the narrow interests of the rich,” rather than being a “truly justice-centered regime that shows concern for the interests of the poor,” ostensibly because it “restrict[s] the regulatory space of governments to take measures for the advancement of its people, their environmental and human rights interests and their economic development”).
Impugn the integrity of the international investment law system. States seeking to roll back foreign investment protection by denouncing BITs, exiting ICSID, or taking other measures within their sovereign prerogative adopt and perpetuate this rhetoric to legitimize their actions.38

Underpinning this foundational critique is the belief that foreign direct investment harms host states and is forced upon them for the advantage of rich states and multinational enterprises.39 It has been argued that international law is “the means by which hegemonic States impose principles on the basis of a pretense such as a higher standard of civilization or better standards of governance.”40 The evidence is overwhelming, however, that the current system of international protection for foreign investment benefits developing states.

One powerful indicator is the continuing growth in the number of intra-South BITs, which now number over 1,000.41 Not only do intra-South BITs proliferate, but with the benefit of decades of experience with investment treaties and arbitration, developing countries continue to enter into new treaties offering greater protection to foreign investors than their first-generation treaties. For example, in 2012, China concluded a trilateral investment agreement with Korea and Japan that promises stronger protection of foreign investment and strengthens its commitment to international arbitration for resolving disputes with foreign investors.42 China had previously conclud-

38. See, e.g., Ecuador/Chevron dispute enters a new chapter: Correa calls for Latam support, MERCOPRESS (Feb. 26, 2013), http://en.mercopress.com/2013/02/26/ecuador-chevron-dispute-enters-a-new-chapter-correa-calls-for-latam-support (quoting President Correa of Ecuador as saying, “It’s the end of sovereignty, the end of our independence; we have become colonies with these rulings from international courts.”).


ed a 1988 bilateral investment treaty with Japan and a 1992 treaty with Korea with more circumscribed rights. Under China’s former treaties with Japan and Korea, investors could submit claims to international arbitration only in the case of expropriation and then only for a determination of compensation owed under national law. The new trilateral treaty firmly relinquishes national jurisdiction over investment claims by Japanese and Korean nationals and prescribes independent standards of compensation. Similarly, the 2009 ASEAN Comprehensive Investment Agreement provides for investor-State arbitration under ICSID or other institutional rules, at the investor’s option. Intra-South BITs as a whole are as protective of foreign investors as older generation North-South BITs, typically offering foreign investors access to arbitration through ICSID or equivalent channels. In addition, in response to criticism from first-world academics of investor-State arbitration provisions in the Trans-Pacific Partnership (TPP), Malaysia issued a statement expressing its support of investor-State dispute settlement in the TPP and more generally as an important tool for its economic development. Developing states in general recognize that inbound foreign direct investment is to their benefit, and they go to great lengths to attract it, including


47. See supra text accompanying note 31.

by entering into investment treaties that provide for mandatory investor-State arbitration.

In addition to the evidence of states’ behavior, empirical research confirms the economic benefits to poor states of the international regime of foreign investment protection. There has long been consensus that foreign direct investment increases national income and employment and accelerates development and modernization, including by establishing valuable tangible assets within the host country, promoting the development of human capital, facilitating the acquisition of technical knowledge, and creating network effects that create opportunities for future market access abroad.49 Thus, to the extent that international investment law provides foreign direct investment, it contributes to those positive consequences.

However, at least one critic of the foreign investment legal regime argues that it does not generate capital flows to poor countries. He argues that BITs are unnecessary because states will treat investors fairly irrespective of such agreements in order to attract future foreign investment.50 But in practice, reputational effects and community pressure have proven inadequate against hostile actions of host states against foreign investors.51 While expropriation events became less frequent over the 1980s and early 1990s,52 the last five to ten years have seen an increase in both direct and indirect expropriations against foreign investors.53 Experience thus shows that


51. See ANDREW T. GUZMAN, HOW INTERNATIONAL LAW WORKS: A RATIONAL CHOICE THEORY 88–90 (2008) (describing how in the 1970s and 1980s states expropriated foreign investment without regard to reputational effects because their governments were pursuing policies hostile to foreign investment anyway, making large future inflows of foreign investment unlikely). See generally id. at 71–117 (describing the complexity of the impact of reputation on State behavior, involving cost-benefit calculations of reputational versus non-reputational payoffs, the importance of the obligation at stake, and current reputation).


reputational effects alone cannot ensure legal stability and certainty. More importantly, the specter of reputational effects gives would-be investors no legal recourse if the reputational threat fails, and therefore no certainty of protection. Thus, investors remain deeply concerned about political risk and expropriation abroad and actively seek ways to reduce their exposure. In 2011, at least 38% of respondents to the Multilateral Investment Guarantee Agency’s annual political risk survey had withdrawn existing investments or cancelled planned investments because of political risk in the previous twelve months.54

Of course, it is one thing to show that political risk hinders capital flows and another to demonstrate that the existing international legal regime for foreign investment effectively mitigates political risk. Evidence also supports the latter proposition, however. Companies such as Dow Chemical identify investment treaties as the foundation of their foreign direct investment strategy.55 While one unreliably small survey of multinational companies and political risk insurers concluded that many do not take BITs into account,56 in a much larger survey, 67% of executives of multinational enterprises said that the existence of an investment treaty influenced their company’s decisions on where to invest.57 That study discovered that investors considered the existence of a BIT important when deciding whether to invest in developing countries, and considered it among the most significant factors when deciding whether to invest in transitional economies.58

54.  Id. at 22, fig. 1.11.
Other evidence supports this finding. The government political risk insurers of France and Germany refuse to underwrite investments that are not covered by BITs.\textsuperscript{59} Other countries’ public political risk insurers take the existence of a BIT into account as part of their risk assessments.\textsuperscript{60} The World Bank Group’s Multilateral Investment Guarantee Agency considers the existence of an investment protection treaty a sufficient condition for coverage and factors it into its premium calculation.\textsuperscript{61} Some private political risk insurers consider BITs as relevant factors when assessing very risky countries.\textsuperscript{62} One writer downplays the importance of BITs to political risk insurers on the basis of a survey he conducted, drawing the conclusion that BITs are usually not dispositive to private political risk insurers when setting premiums “for developing countries that treat foreign investors fairly and in a non-discriminatory way.”\textsuperscript{63} However, that the results had to be conditioned on that expansive caveat in fact demonstrates the value of BITs to countries facing reputational hurdles.

A related argument is that BITs are not the only way for states to make a credible commitment to protect foreign investment, and that other means of protection that offer recourse to international arbitration might be equally effective.\textsuperscript{64} While some early studies showed weak or no correlation between BITs and foreign direct investment,\textsuperscript{65} the majority of published studies find a positive correla-


\textsuperscript{61} Poulsen, supra note 59.

\textsuperscript{62} See id.

\textsuperscript{63} See id.


tion between foreign direct investment (FDI) and international investment agreements (IIAs). The most sophisticated studies con-


66. See, e.g., Todd Allee & Clint Peindhardt, Contingent Credibility: The Impact of Investment Treaty Violations on Foreign Direct Investment, 65 INT’L ORG. 401 (2011) (finding that entering into BITs significantly increases FDI unless the state is then charged with breaching the BIT by an investor in arbitration); Rashmi Banga, Do Investment Agreements Matter?, 21 J. ECON. INTEGRATION 40 (2006) (finding that signing BITs with developed countries increased FDI inflows); Matthias Busse, Jens Koniger & Peter Nunnenkamp, FDI Promotion Through Bilateral Investment Treaties: More than a Bit?, 146 REV. WORLD ECON. 147 (2010) (controlling for endogeneity and other statistical artifacts and finding that BITs increase FDI, with evidence that they may substitute for weak domestic institutions); Tim Büthe & Helen V. Milner, Bilateral Investment Treaties and Foreign Direct Investment: A Political Analysis, in THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT, supra note 57, at 171, 213–14 (finding a statistically significant increase in FDI as a percentage of GDP with each standard deviation in the number of BITs signed); Peter Egger & Michael Pfaffermayr, The Impact of Bilateral Investment Treaties on Foreign Direct Investment, 32 J. COMP. ECON. 788, 790 (2004) (finding a 30% increase in capital flows from a capital-exporting to a capital-importing country after they enter into a BIT); Kevin P. Gallagher & Melissa B.L. Birch, Do Investment Agreements Attract Investment? Evidence from Latin America, in THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT, supra note 57, at 295, 296–99 (2009) (finding a positive correlation between the number of BITs signed and foreign investment inflows to Latin American countries); Robert Grosse & Len J. Trevino, New Institutional Economics and FDI Location in Central and Eastern Europe, in THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT, supra note 57, at 273 (finding a significant positive correlation between BITs and inward FDI); Andrew Kerner, Why Should I Believe You? The Costs and Consequences of Bilateral Investment Treaties, 53 INT’L STUD. Q. 73, 82–98 (2009) (controlling for endogeneity and finding that ratifying a BIT can result in a $600 million increase in foreign direct investment); Eric Neumayer & Laura Spess, Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?, 33 WORLD DEV. 1567, 1568 (2005) (finding that concluding BITs with a number of capital-exporting states could result in a near doubling of FDI, but that the effect diminishes as domestic legal institutions improve); Clint Peindhardt & Todd Allee, Devil in the Details? The Investment Effects of Dispute Settlement Variation in BITs, in YEARBOOK ON INTERNATIONAL INVESTMENT LAW AND POLICY 2010–2011, at 837, 854–56 (Karl P. Sauvant, ed. 2012) (finding that, controlling for country-specific characteristics that impact treaty negotiations and thus treaty language, international investment agreements that more strongly commit to investor-State arbitration by omitting reference to domestic dispute resolution are correlated with higher foreign direct investment inflows); Susan Rose-Ackerman, The Global BITs Regime and the Domestic Environment for Investment, in THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT, supra note 57, at 311 (finding that BITs have a positive impact on FDI flows to developing countries in interaction with domestic political and economic factors); Jeswald W. Salacuse & Nicholas P. Sullivan, Do BITs Really Work?: An Evaluation of Bilateral Investment Treaties and Their Grand Bargain, 46 HARV. INT’L L.J. 67, 95–115 (2005) (finding that concluding a BIT with the United States correlated with increased incoming investment of 77 to 85%, but with other OECD countries had no significant effect); Kim Sokchea, Bilateral Investment Treaties, Political Risk and Foreign Direct Investment, 11 ASIA PAC. J. ECON. & BUS. 6
sider possible alternative explanatory variables and still find that IIAs that provide for investor-State arbitration are correlated with increased investment. These findings line up with the ways that one would expect investment treaties to operate. The strength of the correlation varies for a state according to factors such as its internal economic and political conditions, its economic characteristics relative to those of its treaty partners, the contents of the treaty, and the procedural conditions it places on investor-State arbitration. The most sophisticated empirical analysis available thus confirms that strong BITs—particularly those with arbitration clauses that omit any references to local dispute resolution—are the most likely to increase foreign direct investment. Thus, the weight of available empirical evidence bears out Wälde’s assessment:

It is the ability to access a tribunal outside the sway of

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67. See Busse, Koniger & Nunnenkamp, supra note 66; Kerner, supra note 66; Peinhardt & Allee, supra note 66; Sokchea, supra note 66.

68. See Peinhardt & Allee, supra note 66, at 837, 854–56.

69. Id.
the host State which is the principal advantage of a modern investment treaty. This advantage is much more significant than the applicability to the dispute of substantive international law rules. The remedy trumps in terms of practical effectiveness the definition of the right.\textsuperscript{70}

The available data decidedly fails to support the claims that IIAs and investor-State arbitration do not increase capital flows or that the benefits accrue solely to rich-country foreign investors.\textsuperscript{71} Instead, it suggests that poor countries—in particular those with high levels of perceived political risk—stand to make large gains from IIAs and investor-State arbitration.\textsuperscript{72} The results of empirical studies of FDI flows comport with the findings of surveys of international investors discussed above.\textsuperscript{73} Interestingly, such investors are not concerned about political risk in stable non-democratic countries, which tend to have the lowest levels of political risk insurance coverage for foreign investors. During the 2011 Arab Spring, many investors in the Middle East and North Africa that had gone without coverage sought to obtain it.\textsuperscript{74} That dynamic illustrates the potential for IIAs with investor-State arbitration to play a powerful role at this critical point in history in helping those countries in transition to establish political stability and realize economic growth.

In addition, these studies do not consider the additional effect of BITs and consent to arbitration on the cost of foreign capital, and consequently on domestic prices for the foreign investor’s goods and services as well as the portion of project costs that the host state pays. While political risk insurance may in some cases be an alternative to

\textsuperscript{70} Thomas W. Wälde, The “Umbrella” Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases, 6 J. WORLD INVESTMENT & TRADE 183, 190 (2005).

\textsuperscript{71} See Somarajah, supra note 28, at 203; Yalkin, supra note 28.

\textsuperscript{72} Berger et al., supra note 66, at 272 (finding that the positive effect of the existence of a BIT disappears when Eastern and Central European transitional economies are removed); Busse, Koniger & Nunnenkamp, supra note 66, at 168 (finding that the positive effect of the existence of a BIT decreases, but is still significant, when transitional economies are removed); Sokchea, supra note 66, at 7 (finding that the correlation between BITs and FDI strengthens as a country’s political risk increases).

\textsuperscript{73} See supra notes 54–57 and accompanying text.

\textsuperscript{74} MULTILATERAL INVESTMENT GUARANTEE AGENCY, WORLD BANK GROUP, WORLD INVESTMENT AND POLITICAL RISK 2012, at 8 (2013).
a BIT, the investor bears the cost of that insurance, which in turn translates into requiring more subsidies, tax breaks, or other concessions from the host state, and/or higher prices for the end product. The host state will bear part of the cost of its political risk in one way or another. Promising legal security enforced by neutral dispute resolution should be a way for a state committed to protecting foreign investment to reduce its financial contribution to development projects.

II. THE MEME THAT INVESTMENT ARBITRATION IS ONE-SIDED

There are two variants of the argument that investor-State arbitration is one-sided: one contends that arbitrators are biased and the other that treaty protections and investor-State arbitration structurally favor investors. Neither stands up to the evidence.

Bolivia and Venezuela denounced ICSID in the late 2000s, and Ecuador reduced the scope of its consent to arbitrate disputes under the convention,75 alleging that ICSID arbitration is biased against developing states. Bolivian President Evo Morales charged, “Governments in Latin America and I think all over the world never win the cases. The transnationals always win.”76 Venezuelan President Hugo Chávez characterized his country’s withdrawal as a refusal to “bow down to imperialism and its [sic] tentacles.”77 His government issued a press release contending that ICSID tribunals harbored a pro-investor bias, having decided “232 times in favor of corporate interests in the 234 cases it has known throughout its history.”78 Other groups and individuals have claimed that “ICSID represents the inequities of an international system biased against the developing countries”79 and that “[i]nvestment treaty arbitration as currently

75. See supra note 5.
79. Bolivia Withdraws from World Bank Investment Court, FOOD & WATER WATCH (June 21, 2007), http://www.foodandwaterwatch.org/global/latin-america/bolivia/bolivia-
constituted is not a fair, independent, and balanced method for the resolution of investment disputes and therefore should not be relied on for this purpose.”

Such assertions have no discernible basis in reality. One of the authors has already thoroughly refuted contentions of systematic arbitrator bias, and we will not repeat that analysis here. Other points, however, remain to be made. First, Venezuela’s statistics are flat wrong. Tribunals convened under the ICSID Convention and Additional Facility Rules have upheld investor claims in part or in full in 46% of cases (far from 232 out of 234 cases, as Venezuela has declared). In 23% of cases, ICSID tribunals declined jurisdiction altogether; in 30%, they dismissed all claims; and in 1%, they concluded that the claims were “manifestly without legal merit.” Further, in a rigorous analysis of fifty-two investment arbitration awards finally resolving treaty claims, Susan Franck found that of the twen-

withdraws-from-world-bank-investment-court/ (“On May 1, 2007, the government of Bolivia took a bold step and withdrew from the World Bank’s undemocratic court for investment disputes. The International Centre for the Settlement of Investment Disputes, or ICSID, is an undemocratic institution that allows the world’s largest corporations to sue poor countries for millions of dollars.”). See also Christian Tietje et al., *Once and Forever? The Legal Effects of a Denunciation of ICSID*, 6 TRANSNAT’L DISP. MGMT. 1, 5 (Mar. 2008) (reporting that Bolivia cited ICSID’s bias as a reason it withdrew from ICSID); Steve Josselson, *Pro-North Bias Seen at ICSID*, (June 19, 2007), http://www.troubledtimesblog.com/2007/06/pro-north-bias-seen-at-icsid.html (“[ICSID] is biased toward corporation[s] based in the Developed World.”).


83. *Id.*
ty-one cases that investors won on the merits, damages were not high: thirteen resulted in damages being awarded between $1 and $5 million; in four cases, investors were awarded between $5 and $10 million; and in only four others were investors awarded more than $10 million. Furthermore, awards typically are well below the amount claimed: more than 80% of awards granted less than 40% of the damages sought. Two analyses by Franck revealed no statistically significant relationship between a country’s development status and its likelihood of success in an investor-State arbitration or the amount of damages a losing state is ordered to pay. These statistics give the lie to the endlessly repeated bias argument.

Another approach of critics is to argue that the outcomes of particular arbitrations evidence bias. Taking this approach, Sornarajah contends that tribunals expansively interpret their jurisdiction to favor investors. He singles out the Tokios Tokelès v. Ukraine award for its definition of “investment,” Maffezini v. Spain for its interpretation of a most-favored nation (MFN) clause, Aguas del Tunari v. Bolivia for disagreeing with the respondent’s argument that a clause in a concession contract precluded changes in upstream ownership of the concession company, and Fedax v. Venezuela for its finding that the claimant’s acquisition of a promissory note issued by the state constituted an investment. Declining to analyze the reasoning of the awards, Sornarajah does nothing more than assert his

89. See id. at 279–81, n.26 (citing Tokios Tokelès v. Ukraine, ICSID Case No. ARB/02/18, Award, ¶¶ 41–49 (July 26, 2007); Maffezini v. Kingdom of Spain, ICSID Case No. ARB/97/7, Decision of Tribunal on Objections to Jurisdiction, ¶¶ 38–64 (Jan. 25, 2000); Aguas del Tunari, S.A. v. Republic of Bolivia, ICSID Case No. ARB/02/3, Decision on Respondent’s Objection to Jurisdiction, ¶¶ 156–80 (Oct. 21, 2005); Fedax N.V. v. The Republic of Venezuela, ICSID Case No. ARB/96/3, Decision of the Tribunal on Objections to Jurisdiction, ¶¶ 18–29 (July 11, 1997)).
disagreement with the result and conclude bias therefrom. 90 Without addressing those four cases, it should be obvious that a handful of individual cases does not establish a pattern of bias. For that matter, mere disagreement with the results of a line of cases that similarly decide a legal issue also does not indicate bias; it may demonstrate nothing more than a consensus on the correct legal analysis of that issue. More is required to evidence bias than disagreement with the outcomes of arbitrations.

Arguments that the investment law regime is asymmetrical are similarly ill-conceived. “Foreign investors,” the argument goes, “are being accorded substantive rights under these treaties without being subject to any specific obligations.” 91 While it cannot be denied that an investor might renege on its promises or break the law of the host state, there is no institutional gap to be filled by memorializing such obligations in a treaty or granting a state a treaty right to enforce them. Investors are bound by the law of the host state and by their contractual obligations. As sovereigns, host states have many tools at their disposal for responding to investor breaches, including civil and criminal penalties, legal actions for breach of contract in their own courts, and political pressure. The very nature of the relationship means that the foreign investor will typically have assets in the host state, guaranteeing enforcement leverage. Further, investment contracts almost universally provide for international arbitration of any dispute relating thereto, which provisions have been interpreted broadly to include not only breach of contract but also torts and violations of domestic law. 92 If successful in such an international arbitration, a state can reach the investor’s assets abroad under the New York Convention. 93 By contrast, resort to treaty-based arbitration is often the sole lever available to an investor to enforce its rights if a host state treats it inequitably once the investor has expended

90. See id.


substantial resources in the host state’s territory.94 Given that the actual power imbalance inherent in this institutional arrangement so glaringly favors host states, the persistence of the asymmetry argument is baffling. One might just as well criticize the “asymmetry” of international human rights courts.

What is more, states are not excluded in principle from bringing either claims or counter-claims in investor-State arbitration.95 The ICSID Arbitration Rules do not preclude a state from bringing a claim against an investor if it has concluded an agreement (in a contract or a treaty) providing for two-way international arbitration.96 Indeed, ICSID has registered four claims initiated by states and state entities against foreign investors.97 That number makes up only a tiny


95. See generally Hege Elisabeth Veenstra-Kjos, Counter-Claims by Host States in Investment Dispute Arbitration “Without Privity,” in NEW ASPECTS OF INTERNATIONAL INVESTMENT LAW 597 (Philippe Kahn & Thomas W. Wälde eds., 2006).

96. See ICSID Convention, supra note 4, art. 36; ICSID, REPORT OF THE EXECUTIVE DIRECTORS ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES, ¶ 13 (2006), https://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/basic-en.htm (“[T]he Convention maintain[s] a careful balance between the interests of investors and those of host States. Moreover, the Convention permits the institution of proceedings by host States as well as by investors, and the Executive Directors have constantly had in mind that the provisions of the Convention should be equally adapted to the requirements of both cases.”); Tanz. Elec. Supply Co. Ltd. v. Indep. Power Tanz. Ltd., ICSID Case No ARB/98/8, Final Award, ¶ 1 (June 22, 2001), available at https://icsid.worldbank.org/ICSID/FrontServlet (follow “cases” hyperlink; then follow “search cases” hyperlink; then sort by “view concluded cases”; then follow “ARB 98/8” hyperlink on page twelve) (claim by a State-owned power company against a foreign investor).

97. See Case Details, Republic of Peru v. Caraveli Cotaruse Transmisora de Energia S.A.C., ICSID Case No. ARB/13/24 (Dec. 26, 2013), https://icsid.worldbank.org/ICSID/FrontServlet (follow “search cases” hyperlink; then follow “select all” hyperlink; then follow “ARB/13/24” hyperlink); Case Details, Gabon v. Socié té Serete S.A., ICSID Case No. ARB/76/1 (Feb. 28, 1977), https://icsid.worldbank.org/ICSID/FrontServlet (follow “search cases” hyperlink; then follow “select all” hyperlink; then follow “ARB/76/1” hyperlink); Case Details, Government of the Province of East Kalimantan v. PT Kaltim Prima Coal and others, ICSID Case No. ARB/07/3 (Dec. 28, 2009), https://icsid.worldbank.org/ICSID/FrontServlet (follow “search cases” hyperlink; then follow “select all” hyperlink; then follow “ARB/07/3” hyperlink) (provincial government in Indonesia against an Anglo-Australian joint venture); Case Details, Tanzania Elec. Supply Co. Ltd. v. Indep. Power Tanzania Ltd., ICSID Case No. ARB/98/8 (Mar. 24, 1999), https://icsid.worldbank.
proportion of all ICSID cases, but as explained above, that is likely because states prefer to avail themselves of one of the other avenues available to them for resolving foreign-investor disputes.

Few current investment treaties explicitly provide for counterclaims, but the language of many is broad enough to encompass jurisdiction over counterclaims. So far only one tribunal is known to have found that a treaty excluded counterclaims in ICSID arbitration. In that case, however, W. Michael Reisman issued a Dissenting Opinion based on Article 46 of the ICSID Convention, which provides:

Except as the parties otherwise agree, the Tribunal shall, if requested by a party, determine any incidental or additional claims or counterclaims arising directly out of the subject-matter of the dispute provided that they are within the scope of the consent of the parties and are otherwise within the jurisdiction of the Centre.

Professor Reisman argued that when a host state offers con-

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98. One that does is the Investment Agreement for the COMESA (Common Market for Eastern and Southern Africa) Common Investment Area, which provides, “A Member State against whom a claim is brought by a COMESA investor under this Article may assert as a defence, counterclaim, right of set off or other similar claim, that the COMESA investor bringing the claim has not fulfilled its obligations under this Agreement, including the obligations to comply with all applicable domestic measures or that it has not taken all reasonable steps to mitigate possible damages.” Investment Agreement for the COMESA Common Investment Area, art. 28(9), May 23, 2007, available at http://vi.unctad.org/files/wksp/iawks08/docs/wednesday/Exercise%20Materials/invagreecomesa.pdf. The COMESA treaty also expressly requires investors to comply with domestic law, which makes it clear that a host State may raise counter-claims for domestic law breaches; see id. art. 9.

99. See Roussalis v. Romania, ICSID ARB/06/01, Award, ¶¶ 868, 872 (Dec. 7, 2011), available at http://www.italaw.com/sites/default/files/case-documents/ita0723.pdf (refusing to hear a counterclaim under a BIT that provided for arbitration of “[d]isputes between an investor of a Contracting Party and the other Contracting Party concerning an obligation of the latter under this Agreement,” reasoning that the treaty imposed no obligations on the investor) (emphasis added). We refer of course to publicly available ICSID awards and those that have been summarized by ICSID. As explained below, we believe that universe to include virtually all ICSID treaty-based arbitrations. See infra notes 106–109 and accompanying text; note 142.

100. ICSID Convention, supra note 4, art. 46.
sent to ICSID arbitration through a BIT, the consent to arbitrate ancillary claims set out in Article 46 is automatically imported into any ICSID arbitration brought against it. 101 Just a few months later, Professor Reisman was vindicated when the ICSID tribunals in *Inmaris v. Ukraine* and *Goetz v. Burundi* reached the same conclusion as he had, finding that they had jurisdiction to hear the state’s counterclaims. 102 It is thus somewhat premature to argue that investment arbitration is one-sided as permitting only investor claims.

Even where states may not bring counterclaims, they may—and often do—raise investors’ alleged violations of domestic law and breaches of contract before investment tribunals in their defense, and tribunals consider violations of legal obligations in deciding whether treaty breaches occur. For example, tribunals have rejected investors’ contract and treaty claims on the grounds that the investments were secured by corruption in violation of domestic law and international public policy or that the investor violated its contractual obligations to the host state. 103 States can also argue “set-off” claims,

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101. *Roussalis*, ICSID ARB/06/01, Partial Dissent of Michael Reisman.

102. See Antoine Goetz & Consorts et S.A. Affinage des Metaux v. Republique du Burundi, ICSID Case No. ARB/01/2, Sentence, ¶ 278–79 (June 21, 2012), available at http://www.italaw.com/sites/default/files/case-documents/italaw1086.pdf (reasoning that the absence of an explicit provision in the BIT for counterclaims is irrelevant because, by agreeing to the ICSID Convention, Burundi accepted the possibility of counterclaims, and by accepting the State’s offer to arbitrate before ICSID, the investor also agreed); Inmaris Perestroika Sailing Maritime Services GmbH v. Ukraine, ICSID Case No. ARB/08/8, Award, ¶ 431–32 (Mar. 1, 2012), available at https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC3296_En&caseId=C320 (basing its decision on the breadth of the BIT’s dispute resolution clause, which covered disputes “with regard to investments between either Contracting Party and a national or company of the other Contracting Party,” similar language is found in many BITs); cf. Metal-Tech Ltd. v. Republic of Uzbekistan, ICSID Case No. ARB/10/3, Award, ¶¶ 391–413 (Oct. 4, 2013), available at http://italaw.com/sites/default/files/case-documents/italaw3012.pdf (relying on *Goetz* and *Roussalis* and holding that in principle the tribunal would have jurisdiction over the State’s counterclaims if it had jurisdiction over the investor’s claims, but because the investment was “tainted by corruption,” the tribunal lacked jurisdiction over the entire dispute).

103. See Metal-Tech Ltd., Award, ¶¶ 278–390, 422–23 (rejecting an investor’s claims for lack of jurisdiction on the basis that the investment was “tainted by corruption” and thus violated Uzbek law); Vannessa Ventures v. Venezuela, ICSID Case No. ARB(AF)/04/6, Award, ¶¶ 52–71 (Jan. 16, 2013), available at http://www.italaw.com/sites/default/files/case-documents/italaw1250.pdf (holding that Venezuela’s actions were justified by the claimant’s breaches of the parties’ contract); World Duty Free v. Kenya, ICSID Case No. ARB/00/7, Award, ¶¶ 137–88 (Oct. 4, 2006), available at http://italaw.com/documents/WDFv.KenyaAward.pdf (rejecting an investor’s claims on the basis of international and
which reduce the value of any award rendered in the investor’s favor by amounts owed by the investor to the state for contractual or domestic law breaches. The ICSID tribunal in *Occidental Petroleum v. Ecuador*, for instance, reduced the damages awarded to the claimant on the basis that a breach by the claimant of Ecuadorian law had contributed to its losses.\(^{104}\)

Thus, the contentions that investment arbitrators and the system of investor-State arbitration are biased against respondent states are nothing more than empty rhetoric.

### III. The Opacity Meme

Contrary to the frequent charge that treaty-based investor-State arbitrations are secret,\(^{105}\) investor-State arbitration today increasingly shines the light of transparency not only on dispute resolution, but also on the actions of foreign investors and host states. Investor-State treaty arbitration ceased to be hidden from public view long ago. Most awards are public and readily found on the internet and, increasingly, so are hearings, party submissions, and other data from proceedings.\(^{106}\) Browsing of any one of a number of websites\(^{107}\) that exhaustively collect publicly available investor-State ar-

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107. See *supra* note 106 (listing several websites which provide access to investor-State
arbitration documents dispels the myth of secrecy. Further, ICSID publishes, at a minimum, excerpts of the legal reasoning of all awards, even if the parties do not agree to publish pleadings, tribunal decisions, or awards.\textsuperscript{108} A growing number of investor-State arbitrations involve open hearings, sometimes live-streamed on the internet.\textsuperscript{109} These features make the proceedings more transparent than investor-State disputes played out in domestic courts, whose decisions typically are not publicly accessible worldwide.

Even where the parties have not agreed to publish documents from the arbitration, the existence of the case, the parties’ identities, and the subject matter of the dispute are usually reported in the press. The prevalence of reporting by both popular media and specialist arbitration news outlets of the existence of formally confidential treaty arbitrations and details about the underlying disputes demonstrates just how infrequently investment treaty arbitrations remain truly “secret.”\textsuperscript{110}

\textsuperscript{108.} See ICSID ARB. R. 48(4) (“The Centre shall . . . promptly include in its publications excerpts of the legal reasoning of the Tribunal.”); ICSID Cases, supra note 106.

\textsuperscript{109.} Luke Eric Peterson, The Expanding Audience for Open Arbitration Hearings, KLUWER ARB. BLOG (Feb. 6, 2012), http://kluwerarbitrationblog.com/blog/2012/02/06/the-expanding-audience-for-open-arbitration-hearings/.

Nonetheless, even formal confidentiality is decreasingly common. A growing number of states have publicly affirmed their support for publishing arbitration documents, opening hearings, and including explicit transparency provisions in their treaties. In July 2013, United Nations Commission on International Trade Law (UNCITRAL) adopted Transparency Rules for treaty-based investor-State arbitration and a corresponding amendment to the UNCITRAL Arbitration Rules. Under the new rules, party submissions and tribunal decisions and awards must be published, hearings must be open to the public, and non-disputing parties must be permitted to make submissions.

Like other international tribunals, investor-State tribunals amplify the reputational effects of treaty breaches, making it easier to detect and make known both investor and state violations. States and investors that behave badly may therefore be internationally exposed as a result of an arbitration. The transparency benefits accrue not only to other states and foreign investors; international tribunals that are directly accessible by non-state actors also provide infor-

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mation to domestic political actors. In addition, many investment treaties expressly require—and tribunals have interpreted the fair and equitable treatment obligation to require implicitly—that states be transparent in governance and decision-making. Such commitments benefit domestic actors as well as foreign ones. In short, the opacity meme, too, is simply that and no more.

IV. THE SOVEREIGNTY MEME

The most recent wave of criticism objects to the imposition of international discipline on states’ politico-economic decisions. This view seeks to chip away at investment protections by expanding the availability of self-judging exceptions for claimed public interest objectives. The argument has been formulated as an objection to interference with state sovereignty, democratic decision-making, public interest regulation, human rights protection, and environmental preservation. For example, it has been argued that arbitration awards are affronts to sovereignty, that they threaten the right of self-determination, and that investment treaties undermine the ability of states to promote life, liberty, and equality.


116. See generally VAN HARTEN, supra note 21.

117. See id.


This Part points out the hidden assumptions underlying this critique and offers countervailing evidence. First, a number of features of international investment law that are criticized are not limited to this legal regime but are features of international law generally. Second, the posited conflict between the current system of foreign investment protection and the public interest is largely illusory; it stems from ignorance of how international arbitration operates, of the nature of the substantive obligations to which states agree in investment treaties, and of the actual holdings of investment treaty arbitrations.

A. Limiting Political Discretion Is What Treaties Do

The broadly stated objection that investment treaties limit state discretion or “reduce sovereignty” \(^{120}\) is actually a challenge that applies against the whole of international law. In the international investment regime, states agree to limit their discretion in the treatment of foreign investors in exchange for benefits that include increased attractiveness to foreign capital, a stable economic and legal environment, improved infrastructure and services to citizens, and more efficient and environmentally sound manufacturing and energy production. Similarly, via treaties, states have agreed to restrict their handling of environmental pollutants in exchange for a cleaner planet, to compel certain treatment of aliens within their borders in exchange for reciprocal treatment of their own citizens abroad, and to improve the treatment of their own citizens by promoting human rights and the rule of law.

Thus, the voluntary acceptance of binding international obligations that constrain domestic actors is a basic principle of international law. The International Court of Justice (ICJ) held in the Nicaragua case that a state may bind itself internationally to install a

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\(^{120}\) See, e.g., Elizabeth May, *Presentation to Trade and Environment Consultations of Canadian Government: Examining Canada’s Priority Interests at the WTO/FTAA Negotiations: Or, How Not To Promote Environmental Protection*, SIERRA CLUB OF CANADA (July 8, 1999), http://www.sierraclub.ca/national/programs/sustainable-economy/trade-environment/wto-brief-jul99.html (“The essence of trade liberalization agreements is a reduction of domestic sovereignty. As the state’s ability to protect its citizens is reduced, we need not cast those peoples and the biosphere to the faceless mercies of the global free-market free for all.”).
democratic government domestically:

[T]he assertion of a commitment raises the question of the possibility of a State binding itself by agreement in relation to a question of domestic policy, such as that relating to the holding of free elections on its territory. The Court cannot discover, within the range of subjects open to international agreement, any obstacle or provision to hinder a State from making a commitment of this kind. A State, which is free to decide upon the principle and methods of popular consultation within its domestic order, is sovereign for the purpose of accepting a limitation of its sovereignty in this field. 121

Further, it is a fundamental rule of international law that states may not override their international obligations by contrary national law. 122 The Permanent Court of International Justice (PCIJ) and the ICJ have affirmed repeatedly that treaty obligations should not be interpreted to permit a state party to be the judge of its own case. 123 Some ICJ judges even have suggested that explicitly self-judging treaty clauses are legally ineffective. 124 The rule that states cannot, absent rare circumstances, invoke even the most laudable domestic interests to override their international obligations is not

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unique to international investment law and was not formulated by investment arbitrators.\textsuperscript{125} The increasing use of “sovereignty-constraining” rhetoric should concern international lawyers generally, because it is in fact a challenge to foundational principles of international law that is the handmaiden of popular suspicions of international cooperation, “globalization,” and multilateralism.

On closer examination it becomes apparent that many “sovereignty-constraining” objections are actually objections not to the fact of binding international obligations, but to the content of those obligations. Thus, when environmental NGOs criticize BITs and investor-State arbitration as “reduc[ing] . . . domestic sovereignty,” their actual objection is that they believe those policy tools threaten environmental values.\textsuperscript{126} This is clear from the fact that the same NGOs support treaties that bind states to particular environmental obligations—thereby constraining their sovereignty.\textsuperscript{127} Looking past the red herring that IIAs and investor-State arbitration are “sovereignty-constraining,” the next Section considers whether they compromise the values that are actually at stake.

\textbf{\textit{B. Fear and the False Claim that International Investment Law Is Incompatible with the Public Interest}}

In December 1999, the Canadian chemical company Methanex initiated arbitration under NAFTA’s investment chapter challenging a state of California ban of MTBE, a gasoline additive that was feared to contaminate drinking water. The media reaction was acerbic. On-air personality Bill Moyers aired a documentary called \textit{Trading Democracy}, branding NAFTA Chapter 11 a “sophisticated extortion racket” that permits foreign companies to say to the United States, “If you regulate me and make me less profitable, pay me

\textsuperscript{125} The doctrine of necessity elucidates the rare circumstances under which a State’s domestic interests may be invoked to override its international commitments. See JAMES CRAWFORD, THE INTERNATIONAL LAW COMMISSION’S ARTICLES ON STATE RESPONSIBILITY: INTRODUCTION, TEXT AND COMMENTARIES 174 (2002).

\textsuperscript{126} See, e.g., May, \textit{supra} note 120.

\textsuperscript{127} See, e.g., \textit{id.} (Expressing tacit approval of multilateral environmental agreements including the Convention on the Trade in Endangered Species, the Basel Convention, the Montreal Protocol to protect the Ozone Layer, and the Kyoto Protocol, while criticizing NAFTA as constraining sovereignty).
The Moyers documentary featured an NGO lawyer who stated, “Essentially we see Chapter Eleven operate to reverse the globally accepted ‘polluter pays’ principle and we see it being turned into a ‘pay the polluter’ principle.”

There was a flurry of political response to Methanex and two other NAFTA claims against the United States. Methanex garnered particular attention because the claimant challenged California’s enactment of a generally applicable environmental law. In response, members of Congress introduced an amendment to an appropriations bill reacting against the NAFTA arbitrations and blasted investor-State arbitration in floor debates. The United States reportedly suspended its trade and investment negotiations. After finding itself as respondent in several claims, it made major changes reducing the interpretive authority of investor-State arbitral tribunals in its 2004 model BIT. After the uproar subsided, the United States quietly won the Methanex arbitration, and Methanex

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129. Id.

130. The first three NAFTA Chapter 11 claims against the United States were Methanex, Mondev, and Loewen. See Methanex Corp. v. United States, Final Award on Jurisdiction and Merits (Aug. 3, 2005), 44 I.L.M. 1345 (2005); Loewen Grp., Inc. v. United States, ICSID Case No. ARB(AF)/98/3, Award (June 26, 2003), 7 ICSID Rep. 421 (2005); Mondev Int’l Ltd. v. United States, ICSID Case No. ARB(AF)/99/2, Award (Oct. 11, 2002), 6 ICSID Rep. 192 (2004).

131. 145 CONG. REC. H20151 (1999) (“If [Methanex] prevails, an important environmental protection would be overturned and U.S. taxpayers would have to foot the bill for any damages awarded.”).

132. See S. EXEC. REP. NO. 106-23, at 21 (2000) (“Some members of the [Senate Foreign Relations] Committee have expressed concern over the possibility that . . . the North American Free Trade Agreement may make it more difficult for the United States to protect itself from exposure to unforeseen claims under investor-state dispute resolution provisions.” Nonetheless, the committee recommended that the Senate advise and consent to ratify the treaties.); Kenneth J. Vandeveld, A Comparison of the 2004 and 1994 U.S. Model BITs, 2008–2009 Y.B. ON INT’L INVESTMENT L. & POL’Y 283, 283–85 (2009).

133. The 2004 BIT restricts arbitrators’ authority by, inter alia, setting out more precisely defined standards of treatment than in the 1994 Model BIT. For example, it specifies that fair and equitable treatment under Article 5 requires only the minimum standard under customary international law. It expressly states that expropriation is limited to interference with property rights or an interest in an investment, asserts that a mere loss is insufficient to show that expropriation has occurred, and specifies that generally applicable regulatory actions will rarely give rise to an expropriation claim (Annex B). See generally Vandeveld, supra note 132, at 290–98 (comparing 1994 and 2004 U.S. Model BITs).
was ordered to reimburse all of the United States’ legal costs and the entire cost of the arbitration. The award revealed that the tribunal had accorded expansive deference to the environmental interests and policy discretion of the state of California and the United States. Indeed, the fears prompted by the first wave of claims proved to be greatly exaggerated when the United States succeeded in all three of those initial NAFTA arbitrations against it. Years later, the United States still has not been found liable in an investment treaty arbitration, despite being a party to investment treaties with at least one-third of the world’s states and hosting foreign direct investment valued at $11.7 trillion.

Nonetheless, the vein of rhetoric that surfaced with early NAFTA claims grew and spread throughout the media, Capitol Hill, the halls of academia, and the platforms of NGOs, much of the discourse assuming, rather than even attempting to prove, that there is a conflict between the system of foreign investment protection and values such as environmental protection. Similar movements have occurred elsewhere. In 2012, the same group of law professors that opposed the inclusion of investor-State arbitration in the Trans-Pacific Partnership Treaty argued that arbitrator “interpretations have prioritized the protection of the property and economic interests of transnational corporations over the right of states to regulate and the sovereign right of nations to govern their own affairs.” In its 2012 World Investment Report, UNCTAD lists, without explanation, the absence of a “provision for investor-State arbitration” as a way to make an investment treaty “[s]ustainable-development-friendly.” Another section of that publication offers the following explanation for the presumed conflict between sustainable development and investment treaties:

[A]s the number of ISDS [(investor-State dispute set-

138. UNCTAD, supra note 30, at 90.
tlemen] cases increases, questions have arisen with regard to the effectiveness and the [sustainable development] implications of ISDS. Many ISDS procedures are very expensive and often take several years to resolve. ISDS cases increasingly challenge domestic regulatory measures implemented for public policy objectives. Almost all ISDS cases lead to the breakdown of the relationship between the investor and the host State. Due to the lack of a single, unified mechanism, different tribunals have issued divergent interpretations of similarly worded treaty provisions, resulting in contradictory outcomes of cases involving identical/similar factors and/or treaty language. Many ISDS proceedings are conducted confidentially, which has raised concerns when tribunals address matters of public policy.139

The UNCTAD report fails, however, to point to a single instance in which an investor-State tribunal thwarted a legitimate environmental measure or to explain precisely how investor-State arbitration undermines sustainable development.140 Instead, it merely reiterates the standard list of criticisms of investor-State arbitration: that it is expensive, confidential, and yields inconsistent decisions. We are not the first to observe that such arguments “rely[] on hypothetical situations and weak counterfactual reasoning.”141

As against hypotheticals and bald assertions that investment tribunals are pro-polluter, a review of actual arbitral awards reveals great respect for environmental protection efforts and national policy

139. Id. at 152.

140. See generally id.; see also Luke Eric Peterson & Kevin R. Gray, International Human Rights in Bilateral Investment Treaties and in Investment Treaty Arbitration 5 (2003) (“[H]ost states may wish to regulate the economy, including foreign investors embedded therein, in a manner which seeks to promote or protect certain human rights interests . . . . Where bilateral investment treaties are in place, foreign investors will often enjoy the ability to challenge these human-rights inspired measures through international arbitration.”); Ursula Kriebaum, Privatizing Human Rights: The Interface Between International Investment Protection and Human Rights, in The Law of International Relations: Liber Amicorum Hanspeter Neuhold 165, 177 (August Reinisch & Ursula Kriebaum eds., 2007) (“[A]n investor may use BIT provisions to challenge human rights-inspired regulations that interfere with its investment.”).

141. Fry, supra note 32, at 79.
Moreover, there is much actual evidence that international investment protection complements and promotes values such as human rights, environmental protection, and the rule of law. Therefore, states should think carefully before permitting inflammatory rhetoric and unrealized fears to drive their policies toward international investment law.

C. Reality Check: Case Study of Environmental Measures

The argument that BITs and investor-State arbitration undermine environmental and other values is grounded in a misspecification of the rights the treaties guarantee and the way they have been interpreted. Contrary to some popular and academic characterizations, BITs do not grant investors the right to recover damages from a host state every time an investment is merely “interfered with” or to “demand compensation when a government-initiated change lowers the value of their assets.” Nor, as has been asserted, do investment tribunals “[strike] down host states’ environmental regula-

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142. This analysis includes all publicly available investment treaty arbitration awards addressing measures that states have defended by invoking environmental protection concerns. As explained above, the incidence of truly confidential investment treaty arbitrations is rare, and even where the documents from an investment treaty arbitration are non-public, details about the case usually enter the public domain. That is especially true where the arbitration concerns politically sensitive matters that arouse the interest of the public, such as environmental disputes. It is thus possible to proceed with reasonable confidence that the publicly known environmental arbitrations comprise most or all such arbitrations. See supra notes 105–110 and accompanying text. Besides the awards analyzed here, press reports cover only one other concluded investment treaty arbitration concerning an environmental dispute. A claim by a Spanish investor against Mexico arising out of a planned waste management facility, it is factually nearly identical to the Metalclad and Tecmed cases discussed here. The investor was granted authorization to build and operate a waste management facility but was subsequently thwarted by local opposition, leading the investor to initiate the treaty claim alleging that its authorization to operate was arbitrarily revoked. The tribunal upheld at least some of the investor’s claims. See Katia Fach Gomez, *ICSID Claim by Spanish Companies Against Mexico over the Center for the Integral Management of Industrial Resources, 2010 Spain Arb. Rev., no. 8, at 129*; *Mexico Is Found Liable for Breach of Investment Treaty in Dispute with Spanish Owners of Waste Management Facility, Investment Arb. Rep. (Apr. 23, 2013),* http://www.iareporter.com/articles/20130423_3.

143. Kriebaum, supra note 140.

tions”—not “on many occasions,”145 and to date, not ever. Moreover, investment treaties do not protect against all changes in the host state’s law. Investors are not guaranteed a particular level of profit, protected from their own bad business decisions, or promised an absence of regulation.146 Rather, in a typical BIT a host state promises not to discriminate against foreign investors and their investments,147 to treat them fairly and equitably,148 to refrain from expropriating without prescribed compensation,149 and to provide full protection and security.150 Those guarantees stop far short of promising that the state will not change the law, regulate the environment, or protect human rights.

Because much of the opposition to BITs and arbitration focuses on environmental concerns, it is instructive to examine the investment treaty arbitrations to date in which investors have challenged measures defended by states by reference to environmental protection. All publicly available151 investment treaty awards concerning environmental disputes to date have acknowledged that states have wide leeway to regulate the environment. In no case has a state been ordered to compensate an investor for enacting a generally applicable environmental law or legitimately enforcing an environmental regulation that caused an investor a loss.

1. Environmental Measures and Indirect Expropriation

Much of the concern surrounding IIAs and investor-State arbitration has centered on the fear that tribunals might use the doctrine of indirect expropriation to require states to compensate investors for generally applicable environmental regulations that cause a loss.152

148. See, e.g., id. art. II, ¶ 2.
149. See, e.g., id. art. IV.
150. See, e.g., id. art. II, ¶ 2.
151. See supra note 142.
152. See, e.g., Deborah Sy, Warning: Investment Agreements Are Dangerous to Your
This has never happened, and an analysis of existing arbitral decisions gives no reason to believe that it will. The three identifiable doctrines of indirect expropriation are discussed in turn below.

\textit{a. Sole Effects}

Particular concern has been raised that an investment tribunal might use the so-called “sole effects” doctrine to require a state to compensate an investor for an environmental regulation.\footnote{See, e.g., Rudolph Dolzer, \textit{Indirect Expropriations: New Developments?}, 11 N.Y.U. \textit{Envtl. L.J.} 64, 79–80, 91 (2002).} To determine whether an expropriation has taken place, this doctrine places less weight on the intention of the state than on the impact of its actions on the property or investment.\footnote{See Certain German Interests in Polish Upper Silesia (Ger. v. Pol.), 1926 P.C.I.J. (ser. A) No. 7, ¶ 44 (May 25).} Courts and tribunals have invoked the doctrine almost exclusively in cases where the state’s actions at issue, although not formally seizing legal title, were targeted specifically against the foreign investment and severely interfered with its ownership or control. Resort to the doctrine has been quite infrequent in recent decades.\footnote{See \textit{Sy}, supra note 152, at 637. Dolzer’s detailed historical tracing of a handful of international court and arbitral decisions that he construes as having applied this doctrine makes its narrow application apparent. See \textit{Dolzer, supra} note 153, at 81–90. An exception is the NAFTA tribunal’s decision in \textit{Pope & Talbot}, which did not concern an environmental dispute, stated that the “sole effects” doctrine applied to a generally applicable regulatory measure. However, in applying the standard to the facts, the tribunal hewed to established jurisprudence in reasoning that the required interference would have to be quite egregious. It held that there was no expropriation because the investment was not nationalized, the regulatory regime was not confiscatory, the investor retained day-to-day control of the assets because they allegedly reduce their anticipated profits”).} No arbitral tribunal addressing


\footnote{154. See Certain German Interests in Polish Upper Silesia (Ger. v. Pol.), 1926 P.C.I.J. (ser. A) No. 7, ¶ 44 (May 25).}

\footnote{155. See \textit{Sy}, supra note 152, at 637. Dolzer’s detailed historical tracing of a handful of international court and arbitral decisions that he construes as having applied this doctrine makes its narrow application apparent. See \textit{Dolzer, supra} note 153, at 81–90. An exception is the NAFTA tribunal’s decision in \textit{Pope & Talbot}, which did not concern an environmental dispute, stated that the “sole effects” doctrine applied to a generally applicable regulatory measure. However, in applying the standard to the facts, the tribunal hewed to established jurisprudence in reasoning that the required interference would have to be quite egregious. It held that there was no expropriation because the investment was not nationalized, the regulatory regime was not confiscatory, the investor retained day-to-day control of the assets because they allegedly reduce their anticipated profits”).}
measures defended by reference to environmental concerns has ever based a finding of expropriation on the sole effects doctrine. The tribunals in Unglaube v. Costa Rica and Santa Elena v. Costa Rica—both considering situations in which it was uncontested that an expropriation had occurred, and the dispute was over what compensation was due—focused on the effects of various actions of the state to determine when the admitted expropriation took place and thus from what point to calculate damages. It was in response to that question that the tribunals placed their focus on the effect of the measures rather than on the state’s intention or the form of its actions.

As an interesting point of contrast, the Unglaube tribunal also considered whether various administrative and regulatory actions affecting different plots of the investor’s land amounted to expropriation. Those actions included the introduction of new permit requirements, suspension of a permitting process, and a court decree temporarily prohibiting the claimants from developing those plots. Unlike with the other plots, Costa Rica did contest that it had expropriated these plots and argued that it had only taken bona fide regulatory measures to protect the environment. The tribunal found that Costa Rica had not expropriated the plots. In considering judicial establishment of a “buffer zone” around a wildlife preserve, the tribunal examined the process by which the deprivation had been effected and expressed concern that there had been no scientific or technical basis given for the decision, particularly in light of the claimant’s investment, no officers or employees had been detained, and the State did not supervise the work of employees or take any of the proceeds of company sales apart from taxes, interfere with the appointment of management, or take “any other actions ousting the Investor from full ownership and control of the Investment.”

156. See Santa Elena v. Republic of Costa Rica, ICSID Case No. ARB/96/1, Final Award, ¶¶ 76–81 (Feb. 17, 2000), 15 ICSID Rev. 169 (2000); see also Unglaube v. Republic of Costa Rica, ICSID Case Nos. ARB/08/1, ARB/09/20, Award, ¶¶ 128, 135–37, 209–21 (May 16, 2012), available at http://www.italaw.com/sites/default/files/case-documents/ita1052.pdf (“Expropriatory environmental measures . . . are, in this respect, similar to any other expropriatory measures that a state may take in order to implement its policies.”) (quoting Santa Elena, ¶ 72) (emphasis added).


158. Id. ¶¶ 138–40, 144.
careful adherence to applicable regulations in developing its property. It was also concerned that the court had issued a declaration creating the “buffer zone” “without any attempt to obtain evidence or comment from the affected landowners.” However, the tribunal did not conclude that those defects rendered the acts expropriatory. Most importantly, the tribunal did not apply the “sole effects” doctrine in its analysis of those environmental regulatory measures.

In Metalclad v. Mexico, the tribunal stated obiter dicta that the issuance of an ecological decree creating a preserve for a rare cactus, which prohibited the operation of claimant’s landfill lying within the new reserve, would amount to an expropriation regardless of the motivation for the decree. However, as will be discussed in detail below, like the tribunal in Unglaube, the Metalclad tribunal applied a more nuanced test—decidedly not “sole effects”—when considering other regulatory actions that involved alleged environmental interests of the state.

These three cases highlight the instinctively differential treatment of regulatory acts as opposed to paradigmatic takings, particularly of real property. In Santa Elena and Unglaube, the state acknowledged that it had expropriated the properties and that it was obligated under both national and international law to compensate. In Metalclad, with respect to the ecological decree, Mexico did not deny that the decree would be expropriatory if it had the effect of foreclosing forever the operation of the landfill. Instead, Mexico argued that the decree did not foreclose the operation of the landfill. While it is understandable that earlier in the development of the law of expropriation some writers worried that the analysis for paradigmatic takings—and particularly the “sole effects” doctrine—might be transposed to regulatory actions taken in the public interest, that has not proven to be the case. The next two sub-Parts examine the distinct way in which tribunals have treated regulatory acts when considering whether they gave rise to indirect expropriation.

159. Id. ¶¶ 227, 231–34.


161. See infra text accompanying notes 172–176.

162. Id. ¶¶ 110–12.
b. The Carveout for Regulatory Actions

The predominant view holds that it is a principle of customary international law that where economic injury results from a bona fide regulation within the police powers of a state, no compensation is required.\textsuperscript{163} As the tribunal in \textit{S.D. Myers v. Canada} reasoned,

Expropriations tend to involve the deprivation of ownership rights; regulations [are] a lesser interference. The distinction between expropriation and regulation screens out most potential cases of complaints concerning economic intervention by a state and reduces the risk that governments will be subject to claims as they go about their business of managing public affairs.\textsuperscript{164}

That tribunal looked to the “real interests involved and the purpose and effect of the government measure” to determine whether an indirect expropriation had occurred and observed that “[t]he general body of precedent usually does not treat regulatory action as amounting to expropriation. Regulatory conduct by public authorities is unlikely to be the subject of legitimate complaint under Article 1110 of the NAFTA . . . .”\textsuperscript{165} Even though Canada’s purportedly environmental regulatory actions were pretextual, as they were actually motivated by protectionist objectives, the tribunal declined to find that they resulted in an indirect expropriation.\textsuperscript{166}

One variation of the basic view carves out an exception where the state has made particular representations to a foreign investor to induce it to make an investment:

[A]s a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, \textit{inter alios}, a foreign investor or investment is


\textsuperscript{164} \textit{S.D. Myers}, ¶ 285.

\textsuperscript{165} \textit{Id.} ¶ 281.

\textsuperscript{166} \textit{Id.} ¶¶ 194–95, 281.
not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation.\textsuperscript{167}

The preservation of that principle permits states to retain the capacity to make credible promises. In both of the cases in which an investor has challenged truly generally applicable regulatory measures as expropriatory, the tribunals applied this principle and declined to find that the state’s environmental regulation gave rise to any treaty breach.\textsuperscript{168}

c. The European Court of Human Rights Approach

Another approach adopts the more investor-protective stance of the European Court of Human Rights (ECtHR), stating that there is no principle of customary international law that exempts regulatory action \textit{per se} from giving rise to expropriation if “the economic value of the use, enjoyment or disposition of the assets or rights affected by the administrative action or decision have been neutralized or destroyed.”\textsuperscript{169} Thus, even this more protective approach sets the very high bar of neutralization or destruction of the investment to ground an indirect expropriation claim. It also imposes a second hurdle: even if the investment has been destroyed, a proportionality test (also adopted from the European Court of Human Rights) then examines whether there is a “reasonable relationship of proportionality between the means employed and the aim sought to be realized.”\textsuperscript{170}

\begin{footnotesize}
\begin{enumerate}
\item\textsuperscript{167} Methanex, pt. IV, ch. D, ¶¶ 7–9 (emphasis added); see also Waste Management v. Mexico, ICSID Case No. ARB(AF)/00/3, Award, ¶ 98 (Apr. 30, 2004), 15 ICSID Rev. 214; Revere Copper & Brass, Inc. v. Overseas Private Investment Corp., 17 I.L.M. 1321, 1331 (cited in \textit{Waste Management}).
\item\textsuperscript{168} Methanex, pt. IV, ch. D, ¶ 7; Chemtura, ¶ 266.
\item\textsuperscript{169} Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 116 (May 29, 2003), \textit{available at} \url{http://italaw.com/sites/default/files/case-documents/ita0854.pdf}.
\end{enumerate}
\end{footnotesize}
d. A Second Look at Metalclad

Metalclad v. Mexico has been identified as an example of an expansive new interpretation of expropriation\(^{171}\) because of the following passage:

\[\text{[E]xpropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.}^{172}\]

Actually, however, Metalclad’s approach to regulatory takings stands comfortably within both of the two approaches discussed above: the “carveout” approach and the ECtHR approach. The above-quoted passage, on which other writers have zeroed in, only sets out the longstanding and uncontroversial principle affirmed in NAFTA that there are two forms of expropriation: direct and indirect.\(^{173}\) While the passage addresses the “taking” element of expro-

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173. NAFTA Article 1110, quoted immediately prior to the above-quoted passage, states, “No party shall directly or indirectly . . . expropriate an investment . . . or take a measure tantamount to expropriation . . . except . . .” See id. ¶ 102 (emphasis added); see also Rudolf Dolzer & Christoph Schreuer, Principles of International Investment Law 101–03 (2d ed. 2012); Rosalyn Higgins, The Taking of Property by the State: Recent
puration, it does not deny that other factors are part of the consideration, including the purpose of the state’s action and whether it was taken in accordance with due process. It is therefore incorrect to characterize Metalclad as creating an expansive strain of the “sole effects” doctrine, as some have done. In the very next paragraph, the tribunal weighs the nature and the purpose of the challenged measures. It explicitly relies on their unlawful purpose and pretextual nature to reach its finding that they were expropriatory:

By permitting or tolerating the conduct of Guadalcazar in relation to Metalclad which the Tribunal has already held amounts to unfair and inequitable treatment breaching Article 1105 and by thus participating or acquiescing in the denial to Metalclad of the right to operate the landfill, notwithstanding the fact that the project was fully approved and endorsed by the federal government, Mexico must be held to have taken a measure tantamount to expropriation in violation of NAFTA Article 1110(1).

Metalclad’s finding of expropriation thus relied on the fact that, in response to political opposition, the challenged governmental measures sought to force the closure of the landfill, without any lawful regulatory purpose and in spite of the operation’s compliance with the law.

e. What Constitutes an Expropriation?

Tribunals’ reasoning on whether a deprivation has occurred is also noteworthy. In Chemtura, the tribunal held that the deprivation was not substantial even though Canada had effectively banned the investor’s product. Similarly, it is hard to imagine a more severe

Declarations in International Law, 176 Recueil des Cours 259, 324 (1982).


175. Metalclad, ¶ 104 (emphasis added).

176. Id. ¶ 106. This discussion excludes the tribunal’s obiter dicta conclusion that an environmental decree issued after the series of acts that amounted to the expropriation also constituted an expropriation.

generally applicable environmental regulatory measure than the one at issue in Methanex: an outright ban on the foreign investor’s product. Nonetheless, the tribunal did not find that an expropriation had occurred. It acknowledged the reasoning in Pope & Talbot v. Canada that “property” could not be construed in an outdated fashion as referring only to tangible assets. However, it rejected the notion that expropriation could be vastly expanded beyond its original understanding:

Certainly, the restrictive notion of property as a material “thing” is obsolete and has ceded its place to a contemporary conception which includes managerial control over components of a process that is wealth producing. In the view of the Tribunal, items such as goodwill and market share may . . . “constitute[] an element of the value of an enterprise and as such may have been covered by some of the compensation payments.” Hence in a comprehensive taking, these items may figure in valuation. But it is difficult to see how they might stand alone, in a case like the one before the Tribunal.178

The Tecmed tribunal articulated an even stricter standard, requiring that any business activity must have “disappeared” and the “economic value of the use, enjoyment or disposition of the assets or rights affected . . . [have] been neutralized or destroyed.”179

f. Two Awards Finding Indirect Expropriation

Applying the aforementioned standards, tribunals have held states liable for expropriation for purportedly environmental measures only where the environmental rationale was pretextual or government officials violated domestic law. Neither of the two cases imposing liability on a state involved a bona fide environmental regu-


179. See Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 116 (May 29, 2003). Similarly, the tribunal in LG&E v. Argentina held that there is no indirect expropriation “where the investment continues to operate, even if profits are diminished.” LG&E Capital Corp. v. Argentina, ICSID Case No. ARB/02/1, Decision on Liability, ¶ 191 (Oct. 3, 2006) available at http://italaw.com/sites/default/files/case-documents/ita0460.pdf.
lation. In both cases, no governmental organ had identified any threat to the environment or public health that would have justified the impugned action.

In *Metalclad*, provincial and municipal officials took a number of actions outside of their authority under Mexican law to thwart the investor’s continued operation of a landfill, despite the investor’s receipt of all required environmental approvals, compliance with environmental laws, and repeated endorsements from the federal government.\(^\text{180}\) The state did not even contend that the landfill posed any risk of environmental degradation; to the contrary, all investigations undertaken in response to local opposition showed the operation to be “consistent with, and sensitive to, [Mexico’s] environmental concerns.”\(^\text{181}\)

Similarly, in *Tecmed v. Mexico*, the claimant had purchased a landfill that had previously been run by a municipality for years without incident. It acquired all necessary environmental permits to operate the landfill. Shortly thereafter, newly elected local officials mounted a campaign against the landfill that resulted in such local opposition that the investor agreed to move it to a different location, despite the acknowledgment of the municipality and the federal government that there was no “evidence of any risk to health and the ecosystem” and no “legal, ethical, or logical arguments” in favor of its closing.\(^\text{182}\) Thus, in response to purely political pressure, the claimant and the local and federal governments agreed to cooperate to relocate the landfill at substantial cost to the investor. Several months later, while steps were being taken to carry out that agreement, pressure from local authorities led the federal government to issue a resolution on pretextual grounds ordering the immediate closure of the existing site.\(^\text{183}\) Throughout the entire process, the landfill operated in accordance with applicable laws and regulations with only minor regulatory infractions, and no government authority had made any finding of a risk to human health or the environment that


\(^{181}\). *Id.* ¶¶ 76–105.

\(^{182}\). *Tecmed*, Award, ¶ 110.

\(^{183}\). *Id.* ¶¶ 127–32, 151.
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justified a serious sanction, much less closure of the site.184

Thus, the jurisprudence emphatically does not support the contention that investment tribunals have expanded the interpretation of expropriation so as to enable investment dispute tribunals “to order compensation for regulatory measures that incidentally reduce the value of investor assets.” 185 In contrast to the paradigmatic case of a taking of real property, the hurdles to establishing regulatory expropriation are difficult for an investor to clear: either bona fide regulations do not give rise to expropriation, or they do so only where the investment is destroyed and that destruction is disproportionate to the interest pursued, or where the regulation contravenes an existing agreement of the state with the investor.

2. Environmental Measures and Fair and Equitable Treatment

Given the near impossibility of successfully challenging an environmental regulation of general application as expropriatory, fair and equitable treatment (FET) is the treaty standard most relevant to the impact of treaty protection and arbitration on states’ regulatory space.186 An examination of the FET standard and how it has been applied gives the lie to the claim that treaties and arbitration restrain states from taking legitimate regulatory measures.187

What is fair and equitable is difficult to ascertain in the abstract; the jurisprudence demonstrates, and at times states expressly, that the determination is highly dependent on the facts of the case.188 While that apparent indeterminacy has been cited as a basis for con-
cern vis-à-vis future environmental regulation, in practice, when
the facts of the case do involve regulation in the public interest, FET
has uniformly been interpreted to give states very broad leeway. The
very expansive deference that has been accorded to states is evident
in both the legal doctrines that tribunals have employed and the way
they have applied them to the facts.

a. On Fears of Freezing the Regulatory Framework

Statements of the FET standard in three arbitral awards—
Metalclad v. Mexico, Tecmed v. Mexico, and Occidental v. Ecuador—are frequently cited as examples of expansive interpretations
that risk preventing states from altering their regulatory frameworks. Tecmed states, and Occidental relies on, the following exp-
lication of FET:

[T]he foreign investor expects the host State to act in a
consistent manner, free from ambiguity and totally
transparently in its relations with the foreign investor,
so that it may know beforehand any and all rules and
regulations that will govern its investments, as well as
the goals of the relevant policies and administrative
practices or directives . . . .

Metalclad states:

[All] relevant legal requirements for the purpose of in-
itiating, completing and successfully operating in-
vestments made, or intended to be made, under the
Agreement should be capable of being readily known
to all affected investors of another Party. There
should be no room for doubt or uncertainty on such

189. See Open Letter, supra note 20, at 2. See generally Roberts, supra note 21, at 179,
190–91.

190. See, e.g., Roberts, supra note 21, at 214–15; Open Letter, supra note 20, at 2;
Zachary Douglas, Nothing if Not Critical for Investment Treaty Arbitration: Occidental,
Eureko and Methanex, 22 ARB. INT’L 27, 28 (2006) (“The Tecmed ‘standard’ is actually not
a standard at all; it is rather a description of perfect public regulation in a perfect world, to
which all states should aspire but very few (if any) will ever attain.”).

ARB(AF)/00/2, Award, ¶ 154 (May 29, 2003); Occidental v. Ecuador, LCIA Case No.
UN3467, Final Award, ¶¶ 190–91 (July 1, 2004), available at http://www.italaw.com/sites/
matters. Once the authorities of the central government of any Party . . . become aware of any scope for misunderstanding or confusion in this connection, it is their duty to ensure that the correct position is promptly determined and clearly stated so that investors can proceed with all appropriate expedition in the confident belief that they are acting in accordance with all relevant laws.192

Roberts argues regarding these three awards that:

[S]ome tribunals have adopted idealized standards of perfect governmental conduct and regulation divorced from any real consideration of state practice. Scrutiny of the internal practices of the treaty parties or states as a whole would demonstrate that these standards are unrealistic and inappropriate for use as the threshold for review.193

Notwithstanding that just three cases provide a thin basis at best for assertions of systemic overreach,194 the discussion of these cases has divorced these individual paragraphs from the context of the facts at issue. In each case, the state made specific promises or assurances directly to the investor to induce the investment and then violated them. In Metalclad, the investor worked with the Federal Government of Mexico, which assured it that Federal officials had exclusive regulatory authority over its planned activities and that Metalclad possessed all necessary permits.195 In Tecmed, the investor had purchased a landfill from a municipality and relied on its representations and the license it granted the investor to operate the landfill for an indefinite term. Thereafter, the license was revoked without explanation and replaced with a one-year, renewable license, and then renewal was refused on a pretextual basis discordant with

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193. Roberts, supra note 21, at 223 (footnote omitted).
Mexican administrative law and without due process.\textsuperscript{196} In \textit{Occidental}, the state negotiated an oil production-sharing contract with the investor on the express basis of the existing tax regime. The contract included a tax stabilization clause promising that any change in the VAT tax regime would be offset by amendments to the contract to protect the investor’s expectations. The breach of FET was found in Ecuador’s breach of those express contractual promises.\textsuperscript{197} Thus, as broadly as the FET standard may appear to be articulated in these three cases, the actual holdings of the awards are not expansive. It is instructive to compare their reasoning in the factual scenario of specific promises and assurances to the reasoning of tribunals considering general regulatory measures. The remainder of this Section does so.

\textit{b. Due Consideration of the Public Interest}

While some have characterized investment arbitrators as narrow-minded commercial lawyers incapable of giving or unwilling to give thought to public interest considerations,\textsuperscript{198} this contention is empirically questionable.\textsuperscript{199} The jurisprudence also shows this characterization to be false, as arbitral tribunals considering environmental regulatory matters have consistently demonstrated an understanding of public interest concerns and a commitment to giving them due weight. A clear example of this is the regulatory carve-out for bona fide regulation in the doctrine of expropriation, discussed above.\textsuperscript{200} The reasoning of awards addressing FET provides further illustrations.

\footnotesize{\textsuperscript{196} \textit{Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, \textsuperscript{¶} 123–32, 154–66 (May 29, 2003).}


\textsuperscript{198} See, \textit{e.g.}, Suzanne Spears, \textit{Quest for Policy Space in New-Generation International Investment Agreements}, 13 \textit{J. INT’L ECON. L.}, 1037, 1073 (2010); Menon, supra note 7, at 32.

\textsuperscript{199} For instance, the list of elite investment arbitrators in the anti-investment arbitration pamphlet \textit{Profiting from Injustice} have among them extensive experience working in and advising governments and international institutions. \textit{See EBERHARDT & OLIVET, supra} note 3, at 38–41.

\textsuperscript{200} \textit{See supra} notes 163–168 and accompanying text.}
In *Chemtura v. Canada*, which involved a challenge to restrictions imposed on lindane, a commercial pesticide, the tribunal began by affirming its deference to public concerns, regardless of their factual validity: “Irrespective of the state of the science . . . the Tribunal cannot ignore the fact that lindane has raised increasingly serious concerns” among the public.201 It listed countries in which public concerns resulted in restrictions on lindane, noted its inclusion on the list of substances designated for elimination in an international convention, and continued to recall these “public concerns” throughout the entire award.202

Similarly, in *Unglaube v. Costa Rica*, after paying tribute to the importance of the turtle-nesting habitat at issue, the tribunal affirmed the state’s authority to take measures to protect the habitat:203

> [T]he Claimants do not question the authority of the sovereign government of Costa Rica to expropriate land, pursuant to Costa Rican law provided that such action and its effects are also in conformity with Costa Rica’s obligations under the Treaty. Certainly this Tribunal is not empowered, nor does it have any intention, to question or weaken the appropriate use of this authority by the government—an authority which has long been established and recognized by international law.204

As the following sub-Parts will show, the homage paid to public concerns has been put into practice. The FET standard has not been used to second-guess states’ policy decisions and has been particularly deferential to state acts relating to environmental interests.

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202.  *Id.* ¶¶ 134–36, 184.  Canada received a unanimous award dismissing Chemtura’s claim.  See *id.* pt. V.


204.  *Id.* ¶ 166 (citing *Santa Elena* v. Republic of Costa Rica, ICSID Case No. ARB/96/1, Final Award (Feb. 17, 2000), 15 ICSID Rev. 169 (2000)).  Costa Rica had conceded, as it had in *Santa Elena*, that it in fact had expropriated the property.
c. The Investor Takes the Host State as He Finds It

It is a widely recognized principle that an investor takes the regulatory and legal framework of the host state as it stands when the investment is made. This principle has been interpreted quite broadly to include the assumption that the investor takes an uncertain regulatory framework as given. As the tribunal in Methanex recognized:

Methanex entered a political economy in which it was widely known, if not notorious, that governmental environmental and health protection institutions at the federal and state level, operating under the vigilant eyes of the media, interested corporations, nongovernmental organizations and a politically active electorate, continuously monitored the use and impact of chemical compounds and commonly prohibited or restricted the use of some of those compounds for environmental and/or health reasons. Indeed, the very market for MTBE in the United States was the result of precisely this regulatory process. Methanex appreciated that the process of regulation in the United States involved wide participation of industry groups, nongovernmental organizations, academics and other individuals, many of these actors deploying lobbyists. Methanex itself deployed lobbyists.205

Similarly, in Unglaube, the tribunal gave weight to the fact that although “the workings of the courts and administrative agencies of Costa Rica surely involve noticeable differences from those with which Claimants may be more familiar,” “governments are accorded a considerable degree of deference regarding the regulation/administration of matters within their borders”206 and are required only to refrain from actions that are arbitrary or discriminat-


ry, lack due process, or violate “elemental fairness.”

Similarly, the tribunal in Chemtura v. Canada stated that it must “take into account the obvious fact that the operation of complex administrations is not always optimal in practice and that the mere existence of delays is not sufficient for a breach.” The tribunal considered the “fact that certain agencies manage highly-specialized domains involving scientific and public policy determinations.” Similarly, other tribunals have asked only whether a state action bears a reasonable relationship to some rational policy.

Thus, the standard that has been applied to regulatory measures in general stands in stark contrast to the reasoning applied where specific assurances have been given. Notwithstanding the language of a few arbitral awards, tribunals have not required unrealistic levels of bureaucratic competence and stability.

d. Very High Deference to Domestic Policy and Processes

The way FET has been interpreted tells an entirely different story from that recounted by critics about the way investment treaties and arbitration constrain state discretion. When assessing whether a state’s regulatory actions have breached FET, tribunals have declined to question the wisdom of policies or the efficiency of bureaucratic processes. Instead they have asked whether the state acted in good faith and in accordance with the rule of law, recognizing states’ substantial leeway in the legislative, administrative, and judicial processes through which environmental interests are pursued.

As a threshold matter, FET does not permit arbitrators to impose their own personal conceptions of fairness on the host state.
Rather, widely accepted administrative law doctrines such as legitimate expectations have been employed to assess state actions toward foreign investors.\textsuperscript{213} One tribunal explained FET as follows:

[L]eadin\textsuperscript{g} authorities indicate that to prove a breach of the standard, a claimant must show more than mere legal error. Instead, as stated by the Saluka Tribunal, the evidence must establish actions or decisions which are manifestly inconsistent, non-transparent, [or] unreasonable (i.e., unrelated to some rational policy)\ldots Where, however, a valid public policy does exist, and especially where the action or decision taken relates to the State’s responsibility “for the protection of public health, safety, morals or welfare, as well as other functions related to taxation and police powers of states,” such measures are accorded a considerable measure of deference in recognition of the right of domestic authorities to regulate matters with their borders.\textsuperscript{214}

The limit of that deference is that “[e]ven if such measures are taken for an important public purpose,” “governments are required to use due diligence in the protection of foreigners and will not be excused from liability if their action has been arbitrary and discriminatory.”\textsuperscript{215}

While adherence to domestic law is insufficient to establish that the state acted in accordance with international standards, tribunals accord domestic law and political structures substantial respect. For example, in \textit{Unglaube}, the tribunal noted:

[T]he Tribunal would, without hesitation, have found that, under the Constitution and laws of Costa Rica, it

\textsuperscript{213.} See generally Daphne Barak-Erez, \textit{The Doctrine of Legitimate Expectations and the Distinction between the Reliance and Expectation Interests}, 11 EUR. PUB. L. 583 (2005) (discussing the doctrine in various European jurisdictions).

\textsuperscript{214.} \textit{Unglaube}, \textsection 246 (internal quotation omitted) (footnote omitted).

\textsuperscript{215.} \textit{Id.} \textsection 247.
is the Attorney General and the Supreme Court who are empowered to give authoritative and final interpretation of the law. The construction of the 1995 National Park Law is a matter of Costa Rican law, and it is not appropriate for this Tribunal to substitute an opinion of its own or make any finding of liability unless the Attorney General and the Court are found to have acted in a manner which is arbitrary, discriminatory or otherwise shocking to the conscience.216

Similarly, the tribunal in S.D. Myers confirmed ample leeway for states in their treatment of foreign investors, finding that a breach occurs only when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective. That determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders.217

In Chemtura v. Canada, an arbitration in which the claimant challenged an environmental review and eventual phase-out of a pesticide, the tribunal showed similar deference to Canada. It focused on whether Canada had acted in bad faith, unfairly, or without due process.218

216. Id. ¶ 253.

217. S.D. Myers v. Canada, Partial Award, ¶ 263 (Nov. 13, 2000), available at http://italaw.com/sites/default/files/case-documents/ita0747.pdf. This decision was rendered before the NAFTA parties issued their Note of Interpretation seeking to limit the NAFTA to protecting the international minimum standard of treatment. See Notes of Interpretation of Certain Chapter 11 Provisions, supra note 111.

218. See Chemtura Corp. v. Canada, Award, ¶¶ 123–47 (Aug. 2, 2010), available at http://italaw.com/documents/ChemturaAward.pdf. Like S.D. Myers, Chemtura cannot be distinguished as applying a more restrictive standard than that applied in most bilateral investment treaties pursuant to the NAFTA parties’ Note of Interpretation. The tribunal considered whether, through a most favored nation clause, Canada could be said to have breached a more rigorous FET standard and found that it could not. Id. ¶¶ 236–37.


e. The Precautionary Principle

Most national environmental regulatory frameworks incorporate the precautionary principle in weaker or stronger forms.219 Before many treaty challenges to environmental actions had been decided, it was an open question how arbitrators would evaluate whether a state using the precautionary principle had violated its treaty obligations, and there was understandable wariness about how arbitrators would assess “the reasonableness of the risk analysis used to justify regulatory action.”220 However, the development of the jurisprudence discussed above, with its emphasis on good faith and due process, shows deference to the precautionary principle in that tribunals have declined to assess the scientific foundation or wisdom of a state’s environmental policy decisions.221 In Chemtura v. Canada, the tribunal noted that “it is not its task to determine whether certain uses of lindane are dangerous . . . the role of a Chapter 11 Tribunal is not to second-guess the correctness of the science-based decision-making of highly specialized national regulatory agencies.”222 Applying a good faith standard, the tribunal also rejected the claimant’s contention that the review of the pesticide did not afford due process because it began with a foregone conclusion that it would be banned.223 Similarly, in Methanex v. United States, the tribunal applied a good faith standard and declined to assess the scientific evidence, which was controversial even within the United States.224

S.D. Myers is the only award that has held a state liable for breaching FET through a measure the state characterized as a generally applicable regulatory measure. Canada banned the export of a

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220. Gantz, supra note 219, at 657.


222. Chemtura, ¶ 134.

223. Id. ¶¶ 145–46.

class of industrial waste chemicals called PCBs destined to be remediated at a facility just across the U.S. border. As in the two cases discussed above, the tribunal in S.D. Myers also applied a good faith test. It found overwhelming evidence that the ban was not imposed on legitimate grounds provided for under Canadian law but instead was motivated by a “desire and intent to protect and promote the market share of enterprises” that could carry out such remediation in Canada. The evidence included internal communications of environmental regulators showing that they believed that the export of the chemical posed no significant environmental risk, that export was supported by all jurisdictions within Canada, and that the Minister of the Environment had nonetheless promised certain companies that had lobbied her that she would close the border.

In Unglaube v. Costa Rica, the tribunal held that the requirement of fair and equitable treatment was not violated by a Supreme Court order suspending development of property for nine months, despite the tribunal’s finding that the order had no basis in the applicable law or any scientific evidence. To assess the claimants’ allegation that it was treated unfairly and inequitably, the tribunal applied a denial of justice standard, requiring the claimants to prove that “the laws of Costa Rica, taken as a whole, did not afford them an adequate opportunity, within a reasonable time, to vindicate their rights.” That standard required claimants to show procedural unfairness, such as a failure to ensure “reasonable advance notice, a fair hearing and an unbiased and impartial adjudicator.” Similarly, the tribunal rejected the claimant’s argument that it was denied justice by a delay of nearly four years in developing its previously approved project caused by two actions brought by environmental groups. The tribu-

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226. Id. ¶¶ 162–89.
227. Id.
229. Id. ¶ 272.
nal reasoned that the cases had been conducted in accordance with Costa Rican law and there was no evidence of “impropriety, corruption or discrimination.”  

In summary, investment tribunals assessing environmental regulations have carefully limited their inquiry to the scope of the guarantees states have made to foreign investors in their treaties. Opponents of investor-State arbitration have made sweeping arguments that investment treaty protections and consent to arbitration constrain states’ “policy space.” For example, Van Harten argues that consent to arbitration allows a wide range of regulatory issues to be resolved through private arbitration, giving arbitrators the power to decide upon the permissible scope of public powers to tax business, deliver public services, establish regulatory standards, control land use, and so on.  

As the discussion above shows, that characterization is wholly misleading. Arbitrators have nothing to say about the “permissible scope of public powers.” The authority to regulate remains intact, and arbitrators decide only whether an investor is entitled to compensation because a state breached an obligation it undertook—in an exercise of its sovereign capacity—by concluding a treaty. There is no foundation for the characterization that investment tribunals are a back door to dismantling environmental regulations or that they substitute their own policy judgment for that of democratically elected governments.  

231. Id. ¶ 286.
232. Van Harten, supra note 185, at 608–12.
234. See Michelle Sforza & Mark Vallianatos, Chemical Firm Uses Trade Pact to Contest Environmental Law, GLOBAL POLICY FORUM (Apr. 1997), available at http://www.globalpolicy.org/component/content/article/212/45381.html (“If Ethyl wins its case, a precedent will be set whereby the legal right of corporations to be compensated when public health regulations affect a company’s bottom line is given the same weight as the public’s right not to be harmed by industrial toxins. This could send the message to investors that seeking compensation from the public for the cost of complying with
V. RECONSIDERING “REGULATORY CHILL”

The previous Part analyzed the content of specific investment treaty awards addressing purported environmental measures to show that tribunals have not demanded that states freeze their regulatory frameworks as of the time of investment in order to avoid liability. This Part responds more generally to the argument that the mere possibility of a future investment treaty claim will discourage states from making policy changes in the public interest, leading to regulatory chill.\(^{235}\) That argument is made in the abstract and is based on untested assumptions. It is mere speculation that the specter of damages claims by foreign investors on balance negatively impacts the quality of host state regulation rather than improving it. After all, that specter could stop a government from enacting misguided, discriminatory, and harmful policies.

Advocates of the regulatory chill critique contend that even if investors have been unsuccessful in challenging environmental regulation, they have proven willing to use treaty arbitration as a weapon to challenge states’ authority to enact legitimate environmental regulation if such regulation causes them any loss. For example, a recent call for papers stated:

> [T]he rapid growth in the number of treaty-based claims filed by investors reflects investors’ increased willingness to safeguard their investments from *any adverse state conduct* . . . . [A] wide variety of domestic measures relevant to sustainable development . . . have also been challenged under the agreements. Such claims by investors, whether successful or not, can cause a state to think twice before adopting environmental regulations constitutes a legitimate business strategy. Thus, in pacts like NAFTA, groups opposed to strong environmental regulation may find an effective mechanism for advancing the radical ‘takings’ agenda for which they have not been able to build public or legislative support.”); see also discussion of *Ethyl v. Canada*, infra notes 241–243 and accompanying text.

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235. See Bruno Simma & Theodore Kill, *Harmonizing Investment Protection and International Human Rights: First Steps Towards a Methodology*, in *INTERNATIONAL INVESTMENT LAW FOR THE 21ST CENTURY: ESSAYS IN HONOUR OF CHRISTOPH SCHREUER* 678 (Christina Binder et al. eds., 2009); Sforza & Vallianatos, supra note 234 (“If such cases were to become commonplace, governments would have to give due consideration to the potential fiscal costs before passing needed regulations.”).
legitimate regulations, suggesting that treaties may in fact impede states’ policy space to promote sustainable development domestically.\footnote{\textit{Call for Papers}, supra note 152 (emphasis added).}

Given states’ hitherto undefeated record in arbitrations challenging bona fide environmental regulations, it is understandable that criticism has shifted focus to the very incubation of regulations. However, it is quite a stretch to characterize the challenges that have been made as opposing any adverse state conduct. Successfully arbitrating investors have uniformly had to make out a case that the state’s actions were pretextual, discriminatory, or lacking in due process.\footnote{\textit{See supra} text accompanying notes 153–185.} The clear message of cases decided so far has been that an investor challenging public interest regulatory action faces a forbidding, if not impossible, climb. The high cost of pursuing an arbitral claim\footnote{\textit{See} \textit{Susan D. Franck, Rationalizing Costs in Investment Treaty Arbitration}, 88 \textit{WASH. U. L. REV.} 769, 774 n. 21, 785 (2011); John Y. Gotanda, \textit{Note, Consistently Inconsistent: The Need for Predictability in Awarding Costs and Fees in Investment Treaty Arbitration}, 28 ICSID REV. 420, 420, 423 (2013).} will tend to deter resort to arbitration where the probability of success is low. As if to further drive the point home, some tribunals have required the unsuccessful claimant to bear the entire cost of the arbitration and some or all of the state’s fees for defending against the claim.\footnote{\textit{See} Methanex Corp. v. United States, Final Award on Jurisdiction and Merits (Aug. 3, 2005), 44 I.L.M. 1345, pt. VI (2005) (ordering the claimant to pay the United States $2.9 million for its legal costs and to bear the entire cost of the arbitration itself); Chemtura Corp. v. Canada, Award, pt. V (Aug. 2, 2010), \textit{available at} \textit{http://italaw.com/documents/ChemturaAward.pdf} (ordering the claimant to bear the costs of the arbitration and 50% of Canada’s legal costs).} The possibility of settlement does not significantly alter the analysis. Where the environmental measure is not pretextual, discriminatory, or lacking in due process, a state is unlikely to settle a claim challenging the legitimate measure by taking a step as drastic and politically difficult as reversing its laws or regulations.

\textit{Ethyl v. Canada} has been a favorite example of critics, who argue that Ethyl successfully used an arbitration claim to coerce Canada to revoke an environmental law.\footnote{\textit{See} \textit{PUBLIC CITIZEN, NAFTA Chapter 11 Investor-to-State Cases: Bankrupting Democracy} 9–10 (2001), \textit{available at} \textit{http://www.citizen.org/documents/ACF186.PDF}; Connie de la Vega, \textit{Human Rights and Trade: Inconsistent Application of...}
ingly different.

In Ethyl, a NAFTA investment tribunal found it had jurisdiction to hear a claim challenging a Canadian statute that prohibited (1) imports of the gasoline additive MMT and (2) the interprovincial transportation thereof. (The only source of MMT was in the United States and only one Canadian Province had any related MMT facility.) The claimant alleged that the challenged statute was a discriminatory trade measure because it did not outlaw the production and sale of MMT, but only banned its importation into Canada and any interprovincial movement.

While the NAFTA arbitration was pending, and before a hearing on the merits, four Canadian provinces succeeded in a challenge against the legislation before a Canadian public interprovincial tribunal. That Canadian tribunal held that the legislation was invalid under Canadian law as an illegitimate restraint on interprovincial trade unjustified by the environmental interests invoked. Thus, Canada repealed the legislation and settled the NAFTA arbitration only after the MMT trading ban had been invalidated domestically, and it was not Ethyl’s NAFTA claim that pushed Canada to change its law.

Moreover, while Canada has been the most frequent respondent in treaty claims arising out of purportedly environmental regulations, there is no indication that the challenges have chilled environ-

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242. Id. ¶¶ 5–6.

243. See Report of the Article 1704 Panel Concerning the Dispute Between Alberta and Canada Regarding the Manganese-Based Fuel Additives Act, 3 ASPER REV. INT’L BUS. & TRADE L. 347, 361 (1998) (holding in favor of complainants Alberta, Quebec, Nova Scotia, and Saskatchewan that the MMT legislation is inconsistent with Canadian law because it creates barriers to internal trade not justified by the applicable “legitimate objectives” test and recommending that Canada remedy the inconsistency and suspend the legislation in the meantime).
mental regulation there. After Dow AgroSciences notified Canada of its intent to seek arbitration under NAFTA in 2009 because the province of Quebec banned a chemical used for cosmetic lawn care, five other provinces enacted similar bans.244 Additionally, Canada has enacted several new federal environmental laws in recent years.245 Thus, past awards indicate that if the specter of investor challenges risks “chilling” anything, it is the misuse of regulatory authority.246 Indeed, a recent study of all concluded ICSID arbitrations found that investors have rarely challenged legislative acts; over 90% of cases involved challenges to executive branch measures.247 It is also to be expected that future claims will be even more circumscribed

244. See David Suzuki Foundation, Pesticide Free? Oui!: A Comparison of Provincial Cosmetic Pesticide Bans 4 (2011), available at http://www.healthyenvironmentforkids.ca/sites/healthyenvironmentforkids.ca/files/pesticide-free-oui-2011.pdf. Dow AgroSciences instituted NAFTA arbitration against Canada after the province of Quebec banned the chemical 2,4-D, used in cosmetic lawn care. Dow pointed out that the government had itself concluded after a review that there was no evidence that the chemical was harmful to the environment or humans. Ultimately Canada settled the claim quite favorably to itself, paying Dow no compensation and maintaining the ban. Canada’s only concession in the settlement was to acknowledge publicly its finding that products containing the chemical do not pose an unacceptable risk to the environment or human health as long as the instructions on the label are followed. See Canada Welcomes Agreement with Dow AgroSciences, FOREIGN AFFAIRS, TRADE AND DEVELOPMENT CANADA (May 27, 2011), http://www.international.gc.ca/media_commerce/comm/news-communicues/2011/145.aspx?view=d.


246. Others analyzing this issue have concluded that there is no reason to expect that any impact on regulation will be negative. See Vicki Been, NAFTA’s Investment Protections and the Division of Authority for Land Use, 20 PACE ENVTL. L. REV. 19, 59–60 (2003) (“Each of these potential implications—towards greater centralization and less localism, and towards more comprehensive and less discretionary regulatory regimes—carries both risks and benefits. There is enormous controversy about the benefits of more decentralized regimes, and about the tradeoff between flexibility and comprehensiveness. The implications of NAFTA’s investor protection provisions upon the distribution of authority between the federal, state and local governments and between environmental and land use regulatory schemes therefore are not necessarily undesirable.”).

247. Jeremy Caddel & Nathan M. Jensen, Columbia FDI Perspectives No. 120: Which Host Country Government Actors Are Most Involved in Disputes with Foreign Investors?, VALE COLUM. CTR. ON SUSTAINABLE INT’L INVESTMENT (April 28, 2014), http://www.vcc.columbia.edu/content/which-host-country-government-actors-are-most-involved-disputes-foreign-investors. Among the fourteen concluded ICSID arbitrations in which investors have challenged legislative actions, many were initiated in response to the same legislative changes, indicating an even lower likelihood of an investor challenge to any one change in the law.
given that tribunals have been so firm in confirming states’ authority to regulate environmental issues (and considering the high cost of initiating an arbitration), further reducing the risk that even unsuccessful claims will deter beneficial regulation.

Luke Nottage offers an instructive example of a rashly enacted policy change toward solar energy in New South Wales (NSW), Australia. In 2011, the NSW government announced that it would not honor its promise to ensure electricity providers a particular feed-in tariff on electricity generated by solar panels installed by householders. It cut the price offered by one-third, upending the expectations of householders who had invested in solar panels in reliance on the promised rate.248 Popular outcry ultimately led to the restoration of the originally promised tariff. The government had failed even to consider the potentially devastating impact of its hasty policy change on foreign (not to mention domestic) investment in the fledgling solar power industry. To flourish, the industry required a clear, predictable legal and political environment, not one in which “government-backed contracts can be reneged on at will.”249 The NSW policy shift caused at least one major foreign investor in solar power to postpone planned expansion in Australia.250 Nottage observes that if an international investment treaty had been applicable, the government may have more carefully considered the impact of its actions, thereby potentially improving the quality of regulation not only for foreign investors but also for domestic investors and consumers.251 Thus, the discipline imposed by international obligations can help even a generally well-governed state to institutionalize a forward-looking, long-term view of governance that inoculates domestic political institutions against shortsighted or populist proclivities.252 The granting of privately enforceable rights against states has been shown

249. Id. at 9 (internal quotation omitted).
250. Id.
251. Id. at 9–10.
to improve domestic governance. The positive impact would only be amplified in countries with histories of poor governance.

The NSW case study illustrates that the posited dichotomy between the public interest and the protection of investment is a misconception. Rather than facing a tradeoff between “corporate profit” and “human rights and the environment,” States must balance various objectives that serve the public interest, including the maintenance of a stable legal environment necessary for healthy economic functioning and other political and regulatory objectives. Beyond discouraging foreign investment, an unstable political and legal environment hampers domestic development and the ability of citizens to plan their futures. It is no accident that economic development is strongly and positively correlated with all major indicators of human well-being and other fundamental values, including health, education, social welfare, environmental protection, and respect for human rights.

It also should not be overlooked that creating a predictable environment for foreign direct investment has helped developing states to advance other values such as environmental protection. Inflows of foreign capital and know-how—which depend on a stable legal and economic environment—have been crucial to reducing environmental degradation in manufacturing and mining and a driving force behind adoption of greener technologies.


255. Eberhardt & Olivet, supra note 3, at 7.


257. See, e.g., Turkey’s Energy Reforms Make Way for Renewable Future, World Bank (Mar. 29, 2010), http://www.worldbank.org/en/news/feature/2010/03/29/turkeys-energy-reforms-make-way-for-renewable-future (reporting that by opening energy production to foreign investment Turkey has reduced blackouts by more than half, improved access to power for 4.6 million households, and through renewable energy generation averted emissions of 1.01 million tons of carbon dioxide per year). Turkey’s reform of its
VI. ON THE RULE OF LAW

Some opponents of investment treaties and investor-State arbitration have argued that these institutions are “corrosive of the rule of law,” although this objection has been made less frequently than the others considered so far. 258 Because investment treaties and arbitration are in fact powerful tools for advancing the rule of law, both internationally and domestically, this argument calls for a brief rebuttal.

Domestically, developing countries use investment and trade agreements as mechanisms for improving human rights and entrenching democracy. 259 Investment treaties can work complementarily with a stable political environment and respect for human rights to create a welfare-enhancing virtuous circle. 260 The mechanism has been explained as follows:

[T]he increased number of arbitrations may also motivate developing host countries to improve domestic administrative practices and laws in order to avoid future disputes; this would further strengthen the predictability and stability of the legal framework that the conclusion of IIAs was supposed to produce in the


258. See Open Letter, supra note 20 (“The current regime’s expansive definition of covered investments and government actions, the grant of expansive substantive investor rights that extend beyond domestic law, the increasing use of this mechanism to skirt domestic court systems and the structural problems inherent in the arbitral regime are corrosive of the rule of law and fairness.”).


Moreover, in contrast to international arbitration, “internal” political methods for resolving disputes, whether through recourse to dependent judicial systems or attempts to settle with domestic political actors, open doors for the entrenched corruption that exists in many states with weak rule of law. There is occasionally a fine line between a state’s offer to settle a politically driven dispute with a foreign investor and a demand for a bribe. During the 2011 Egyptian revolution, foreign investors were notified, at times through unofficial channels, that they were under criminal investigation for allegedly underpaying for land; although the charges against them remained secret, they could settle their cases by agreeing to make large payments to the extant ruling authorities (who were ostensibly tackling past corruption).  

When investors have recourse solely through domestic dispute settlement, only domestic constraints stand in the way of officials imposing new hurdles at will and then demanding extra-contractual payments from investors to “settle” resulting disputes.

Internationally, investor-State arbitration frees up diplomatic channels for higher concerns and has replaced gunboat diplomacy with formalized legal dispute resolution. That objective was a foundational goal of the ICSID Convention, as expressed in Article 27. Similarly, a stated objective of the U.S.-Argentina BIT was to eliminate the need for the United States to intervene to protect U.S. nationals as it had done repeatedly in the face of Argentina’s frequent declaration of national emergencies. Before the advent of investment arbitration by consent, states occasionally took truly sovereign-

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263. “No Contracting State shall give diplomatic protection, or bring an international claim, in respect of a dispute which one of its nationals and another Contracting State shall have consented to submit or shall have submitted to arbitration under this Convention, unless such other Contracting State shall have failed to abide by and comply with the award rendered in such dispute.” ICSID Convention, supra note 4, art. 27.

ty-threatening actions against other states to protect the interests of their nationals abroad. In spite of its recent criticisms of investor-State arbitration, UNCTAD has expressed its support for this mechanism as a development that has contributed to the international rule of law, to the benefit of less powerful states:

[S]ince most developing countries lack the economic and political power of developed countries, they should be particularly interested in pursuing the further legalization of the international investment system. They benefit from further strengthening of the rule of law at the international level.

Another way that investor-State arbitration has enhanced the international rule of law is that the grant of an enforceable right directly to the foreign investor decouples his ability to obtain redress for a wrong from his influence within his home state. Investors have no right to the diplomatic protection of their home state. Thus, under diplomatic protection, unpopular or powerless persons such as ethnic minorities and aboriginal tribes, or simply those who had no sway with their governments, were left without a remedy.

Investment tribunals further contribute to international and domestic rule of law by relying on and developing human rights jurisprudence when interpreting treaties. To offer just a few exam-


266. See supra notes 14, 30, 138, and accompanying text.

267. INVESTOR-STATE DISPUTE SETTLEMENT, supra note 261, at 93. Since its inception as part of the NIEO movement, UNCTAD appears to have evolved ideologically to recognize at least some of the benefits of international protection of investment for poor States. See supra note 27.


269. Cf. Cayuga Indians (Great Britain) v. United States, 6 Rep. Int’l Arb. Awards 173 (U.S.-Brit. 1926). During the American Revolution, the property of the Cayuga tribe had been confiscated by the political entity that would become the United States. The tribe was dependent on Great Britain and then Canada to espouse its claim and was unable to persuade either State to do so for 150 years.

270. See Sadie Blanchard, State Consent, Temporal Jurisdiction, and the Importation of
ples: The tribunal in *Lauder v. Czech Republic* relied on European Court of Human Rights (ECtHR) cases to determine the content of indirect expropriation, and the tribunal in *Tecmed* relied on Inter-American Court of Human Rights cases for the same purpose. The tribunal in *Saipem v. Bangladesh* looked to ECtHR jurisprudence to determine whether a judicial act could be expropriatory.

The characterization of foreign investors’ rights as being opposed to human rights ignores the fact that the rights protected in BITs overlap substantially with the rights protected in human rights treaties. Some investor-State disputes could just as fittingly be heard by a human rights tribunal as by an investment tribunal (and some claims have indeed been brought in both types of forum). For example, in *Sovtransavto Holding v. Ukraine*, the ECtHR heard claims of violations of due process, protection of property, and discriminatory treatment arising out of the treatment of a corporation operating in the transport sector. The corporation alleged that the Ukrainian President had pressured a local arbitration tribunal to “defend the interests of Ukrainian nationals” in the dispute. More recently, foreign investors have pursued similar claims against Russia relating to its treatment of the corporation Yukos before both investor-State and human rights tribunals. Before the European Court of Human Rights, investors have alleged that Russia violated the European Convention’s prohibitions on unlawful expropriation, arbitrary treatment, and denial of justice by instigating tax and criminal investigations to destroy and eventually nationalize Yukos. They have alleged

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Continuing Circumstances Analysis into International Investment Arbitration, 10 WASH. U. GLOBAL STUD. L. REV. 419, 441 (2011); Fry, supra note 32, at 83.


similar breaches under investment treaties.275

The present system of international investment law therefore complements and builds on international human rights law and strengthens the rule of law domestically and internationally. As Wälde explains, it is part of a shift from “pressure, power, politics, and corruption” as the major tools of dispute resolution to “juridified and heavily ritualized procedures.”276

VII. THE MEME ARISING FROM SOME STATES’ REACTIONS

A final meme about IIAs and investor-State arbitration is that the recent behavior of some states demonstrates that it is time to abolish or fundamentally reform the current system of foreign investment protection. For example, arguing that “[t]he legitimacy of investment arbitration becomes increasingly questioned, with liberal states like Australia moving away from the regime,” Sornarajah has proposed that the existing regime should be scrapped and an entirely new one created.277 The argument that Australia stopped agreeing to investor-State arbitration because it questioned the regime’s legitimacy is a facile characterization of how states decide whether to participate in international adjudicatory mechanisms. The truth is that state behavior toward such mechanisms is complex, depending on a number of fluctuating international and domestic political factors. First, states sometimes make decisions based on short-sighted considerations or on unique domestic factors. (For its part, Australia abandoned after only two years the policy of not agreeing to investor-


277. Sornarajah, supra note 19.
State arbitration, signing a free trade agreement with Korea in late 2013 that grants recourse to arbitration.)\textsuperscript{278} Second, the actions of a minority of States do not necessarily justify dismantling or radically altering a widely used legal mechanism. It should not be thoughtlessly concluded that the actions of a few states call for structural changes to the existing investment law regime that would impact all states.

A state may exhibit reticence about the investment law regime based on fear of hypothetical outcomes. Australia’s recent short-lived pivot away from investor-State arbitration evokes the similar risk aversion that surfaced in the United States when the first NAFTA claims were initiated.\textsuperscript{279} The previous Australian Government’s Trade Policy Statement announcing a decision to “discontinue [the] practice” of agreeing to investor-State dispute arbitration specifically cited concern that its anti-tobacco initiatives would subject the state to liability, stating, “The Government has not and will not accept provisions that limit its capacity to put health warnings or plain packaging requirements on tobacco products.”\textsuperscript{280} Australia is a party to twenty-one bilateral investment treaties containing investor-State arbitration clauses going back as far as twenty-five years,\textsuperscript{281} but it has only recently become a respondent in an investment treaty arbitration for the first time. The tobacco company Philip Morris has brought a claim objecting to the country’s new plain tobacco packaging law,\textsuperscript{282} but it remains to be seen whether the company will prevail.

States also express their displeasure with international adjudicatory mechanisms when those bodies reach decisions with which states are dissatisfied. The most notorious instances of this dynamic


\textsuperscript{279.} See supra text accompanying notes 131–136.


\textsuperscript{281.} See generally Investment Instruments Online, Australia Bilateral Investment Treaties, UNCTAD, http://www.unctadxi.org/.

have been state reactions to decisions of the International Court of Justice. As a prominent example, the Israeli Prime Minister made public statements against the ICJ’s advisory opinion holding that Israel’s security fence violates international law. Before that, the United States had issued statements condemning the International Court’s decision to accept jurisdiction in the Nicaragua case over what it called an inherently political problem and then terminated its acceptance of the court’s compulsory jurisdiction. Similarly, France revoked its consent to compulsory jurisdiction in 1974 when the Nuclear Test Case was decided against it, as did South Africa in 1967 in anticipation of feared further ICJ involvement in its refusal to abide by international law in its control over and governance of South West Africa (now Namibia). States have engaged in similar signaling with respect to the WTO Appellate Body. While a state’s withdrawal or criticism of an international institution may be an occasion for examination, it is by no means a clear signal that the institution or mechanism is in crisis. To the contrary, as of this writing the ICJ docket lists eleven cases, as compared to a maximum of three in 1967 and five in 1974.

Indeed, states, such as Ecuador and Argentina, that have experienced repeated claims or dramatic losses in investment treaty arbitrations have an especially strong incentive to vocalize their dis-


287. Argentina is the most frequent respondent in investment treaty arbitrations, having been the subject of fifty-two claims as of the end of 2012. IIA Issues Note, Recent Developments in Investor-State Dispute Settlement (ISDS), UNCTAD 4 (May 2013), http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d3_en.pdf. While it has fared
satisfaction. Losing an investment arbitration reduces a state’s attractiveness to foreign investors to a level lower than it would have been had the state never signed a BIT.288 States that have lost arbitrations therefore may conclude that they have nothing to lose by attacking the system’s credibility.

Another factor is that capital-importing states with well-developed and trusted legal institutions, such as Australia and the United States,289 likely do not attract significant additional inbound investment by agreeing to arbitration.290 The United States and Australia invoked the mutual credibility of their respective legal systems as the reason they chose not to include investor-State arbitration in their free trade agreement.291 Moreover, given the broad coverage of today’s network of BITs, highly developed states that are home to significant volumes of outbound investment (which includes the United States and Australia despite their status as net capital importers)292 have less reason than they did historically to be concerned


290. Cf. Sokchea, supra note 66 (finding that the correlation between BITs and FDI weakens as a country’s political risk decreases); Neumayer & Spess, supra note 66 (finding that the positive effect of BITs diminishes as domestic legal institutions improve).

about the treatment of their nationals abroad, since would-be investors can structure their investments to take advantage of a prospective host state’s BITs with other countries. For example, an Australian national that wished to invest in Malaysia would not benefit from the protection of a bilateral investment treaty if it makes its investment directly. However, the Australian individual or company could establish and execute its investment through a corporation in the United Kingdom and thereby gain the protection of the UK-Malaysia investment treaty, which provides for ICSID arbitration.293

The increase in criticism of the investment law regime has occurred in tandem with a cyclical cooling of certain states’ attitudes toward foreign direct investment generally. That trend suggests that opposition to investor-State arbitration and BITs is driven not by objections to the way the investment law regime functions specifically, but rather by other factors that are causing some states to shift their positions on foreign investment. After decades of nearly universally increasing openness toward foreign investment, the last several years have brought an uptick in investment protectionism and a return to the discourse from the 1960s and 1970s about a “New International Economic Order” and “permanent sovereignty over natural resources.”294 Sauvant has documented a movement of nationalistic opposition to foreign direct investment in a number of more developed states over the past five years. This trend has manifested itself in coercive attempts to regain control over previously privatized natural resources and nationalistic protectionism.295 In the face of economic downturn, the political rhetoric in developed countries reveals an increased hostility towards capital, spurring calls for restrictions on offshoring and other forms of outbound investment.296 Domestic

293. See United Kingdom of Great Britain and Northern Ireland and Malaysia: Agreement for the Promotion and Protection of Investments, Gr. Brit.-Malay., art. 1(4), May 21, 1981, 1579 U.N.T.S. 11 (defining “companies” that are “nationals” of the United Kingdom as “corporations, firms or associations incorporated or constituted under the law in force in any part of the United Kingdom”).


296. Id. at 256–58.
forces such as these may also be driving states’ rhetoric and policy decisions toward international investment law.

In contrast to states with strong positive reputations for governance, other states face the prospect that watering down their treaty protections will render them comparatively less desirable for foreign investors than competitor states that are otherwise similarly attractive investment destinations but are willing to make more credible promises. Such a state will be loath to proclaim that it is cutting back on investor protection in order to reclaim its sovereign prerogative to treat foreign investors as it sees fit. If a state decides, for whatever reason, to shift its policy toward less protection for foreign investment, it may seek to avoid or offset adverse signals by calling for a change to the entire investment arbitration regime. If it succeeds in diminishing not only its own commitment but also that of other participants, a state may reduce its perceived costs of participation in the system without jeopardizing its position relative to competitor states as a desirable investment location in the short term.297

If a state’s domestic political dynamics lead it to pull out of investor-State arbitration or sign treaties that expressly reduce the discretion of arbitrators, that is its sovereign prerogative. However, in light of research showing that countries with less credible domestic institutions stand to receive the greatest benefits from the credibility commitment offered by investor-State arbitration, movements to weaken the entire system are troubling.298 As discussed above, Allee and Peinhardt found that transitional economies may benefit from BITs by signing stronger treaties than their peers.299 Other studies confirm that BITs are most valuable for countries that face the highest barriers to investor trust, such as those that have recently experienced regime change.300 That unsurprising but little-noted dynamic has important implications for international investment policy. States with little at stake should not destroy a valuable tool available to

298. Neumayer & Spess, supra note 66; see also supra Part I.
299. See Allee & Peinhardt, supra note 66.
emerging economies by undermining their ability to commit to protect foreign investors. Proposals to politicize the appointment of arbitrators, to universally restrict the scope of their adjudicative authority, and to develop rules of treaty interpretation that give states wide or self-judging discretion to derogate from their commitments all threaten the efficacy of arbitration as a tool of credible commitment. The next Part will consider several proposed reforms in light of these dynamics.

VIII. ASSESSING PROPOSED REFORMS

The memes discussed above have spurred a number of reform proposals designed to resolve presumed problems with the current system.301 While most of those proposals have not progressed beyond academic journals and conferences, opportunities to advance them are in view. As noted above, over 1,000 BITs are eligible for renegotiation as of the end of 2013, and negotiations are underway for two trade and investment treaties that together would govern 65% of the world economy.302 Further, as the European Commission implements a “comprehensive E.U. investment policy,”303 which includes the current and pending negotiations of a number of E.U.-wide investment treaties with non-E.U. countries, it has stated that future investment agreements should “better balance . . . the right of states to regulate and the need to protect investors.”304 Based on the current state of investment arbitral jurisprudence,305 it is not obvious that such an objective would indicate a shift in priority or necessitate any departure from past treaty standards. Nonetheless, based on the con-
cern about policy space, the Commission has proposed a number of new features that it will seek to include in future E.U. investment treaties. 306

Proposed reforms should not undermine the efficacy of investor-State arbitration as a tool for demonstrating credible commitment to protecting foreign investment. States delegate lawmaking authority to international courts and tribunals as trustees to make their treaty commitments credible. Thus the key feature of international tribunals is that they be independent and impartial. Independent tribunals raise the real possibility that a state’s violation of its promise will result in material and reputational harm “where compliance generates short-term political losses but long-term political gains.” 307 With that principle in mind, the remainder of this Part will assess three recent reform proposals.

A. Proposals to Select Investment Arbitrators Through Political Channels

Proposals to politicize the selection of those who decide investor-State disputes include the creation of an official panel of investment arbitrators from which not only states but also investors must choose and the establishment of a permanent court for deciding investor-State disputes. 308 Sornarajah proposes a dispute settlement system “manned by designated government lawyers” and through which foreign investors could “plead . . . through a nominated body of lawyers.” 309 Van Harten advocates for the creation of an international investment court staffed by state-appointed judges. 310 These proposals would give states substantial control over the body of investment dispute adjudicators.

When their interests are at stake, there is evidence that states tend to select officials for international adjudicatory mechanisms who

306. See EUR. COMM’N, TRADE, FACT SHEET, supra note 304, at 2.
308. See, e.g., Menon, supra note 7.
309. Sornarajah, supra note 19, at 2.
310. VAN HARTEN, supra note 21, at 180.
have demonstrated reliability and government-friendly attitudes. Where the dispute at issue is between two states, there is less of a concern because each party’s appointee will balance the other one out. However, that dynamic does not carry over to investor-State dispute settlement where only one party to the dispute—the state—is given a gatekeeper role. Helfer and Slaughter have explained the credibility problem thereby posed:

It is states who create the tribunal, define its jurisdiction, appoint and reappoint its members, fund its operations, and decide whether it will continue to exist. Aware of these retained powers, a decision maker serving on a dependent tribunal can anticipate a negative reaction from states if she consistently rules in favor of private parties, even assuming their claims are meritorious. An independent tribunal, by contrast, faces far fewer pressures “to pander to the governments at whose sufferance it exists.”

Thus any proposal to “regulate” arbitrators in a manner that makes states the gatekeepers of who is eligible for appointment will undermine the very purpose of investor-State arbitration and should be rejected.

B. Post Hoc Interpretative Statements and De Facto Amendments

Some have advocated wider use by states of—and deference by arbitral tribunals to—mechanisms to remove issues from the consideration of investor-State tribunals post hoc. Two paths have been proposed for reaching this objective. The first is through express provisions found in recent model investment treaties that would permit the contracting states to agree to remove an issue from an arbitral

311. SHABTAI ROSENNE, THE WORLD COURT: WHAT IT IS AND HOW IT WORKS 44 (1995). Although defenders of the ICJ argue that states have shielded the process of choosing judges from politics by having candidates nominated by national groups of the Permanent Court of Arbitration, others argue that the process is highly political; see STEPHEN M. SCHWEBEL, THE CREATION AND OPERATION OF AN INTERNATIONAL COURT OF ARBITRAL AWARDS, IN JUSTICE IN INTERNATIONAL LAW: FURTHER SELECTED WRITINGS OF STEPHEN M. SCHWEBEL 246 (2011).

312. See Brower & Rosenberg, supra note 81, at 642–49.

313. Helfer & Slaughter, supra note 283, at 940.
tribunal’s consideration during an investor-State dispute. The second, at least equally insidious, path seeks universal shifts in treaty interpretation under which arbitral tribunals would be required to accept as retroactively effective states’ post hoc expressions of opinion as to how their treaties should be interpreted, even if the ostensible interpretations are really de facto amendments. Ecuador has attempted (and failed) to pioneer an offshoot of this approach that would permit a state to use state-to-state arbitration to obtain a binding interpretation of a provision contradictory to the interpretation already made in an award by a tribunal established under the treaty being interpreted.

The argument attempts to find grounding in Article 31(3) of the Vienna Convention on the Law of Treaties, which requires that states’ subsequent agreements and practice on interpretation be taken into consideration when a treaty is interpreted. Article 31(3) provides that in interpreting a treaty,

[t]here shall [also] be taken into account, together with the context:

(a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;

(b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;

(c) any relevant rules of international law applicable in the relations between the parties.

The Methanex tribunal and the ICJ have reasoned that such an agreed

314. See U.S. MODEL BIT art. 30(3) (2012) (“A joint decision of the Parties, each acting through its representative designated for purposes of this Article, declaring their interpretation of a provision of this Treaty shall be binding on a tribunal, and any decision or award issued by a tribunal must be consistent with that joint decision.”); CANADA MODEL FOREIGN INVESTMENT PROMOTION AND PROTECTION AGREEMENT arts. 40(2), 51 (2004). The European Commission has announced its intention to negotiate for such provisions in future E.U. investment treaties, and states that a recently concluded free trade agreement with Canada includes such a provision. See EUR. COMM’N, TRADE, FACT SHEET, supra note 304, at 9.

315. See VAN HARTEN, supra note 21, at 131–32; Roberts, supra note 21, at 210.

316. See supra note 6.

interpretation by the state parties does not require any particular method of agreement.318

However, Roberts seeks to expand subsequent agreement and practice “regarding interpretation” or “application” to permit de facto amendments, “interpretations” that in fact change the meaning of the treaty.319 To further lower the systemic barriers to authoritative interpretation and amendment, she advocates expanding the range of expressive acts that would constitute an interpretive agreement, arguing that “joint statements and actions are not required.”320 Relevant acts would thus include not only issuing NAFTA-style joint interpretive statements but also pleading as a respondent in an arbitration, publishing a new model treaty, and making public statements about the state’s view of treaty provisions.321

Roberts offers three primary arguments in defense of accepting after-the-fact state actions, loosely defined, as authoritative interpretations and even amendments of investment treaties. First, she observes that investment treaties do not include explicit exceptions to the Vienna Convention’s provision on subsequent practice as a means of interpretation.322 Second, to the objections based on the rule of law and predictability, she asks the following rhetorical question: Why should states be prevented from retroactively amending their treaties when they can withdraw from them?323 Third, she argues by analogy that international law permits states to revoke or modify rights they have granted through a treaty to third states unless it is established that it was intended that they not be able to revoke or modify those rights.324

The recommended expansion should be rejected. First, the

320. Id. at 217.
322. Roberts, supra note 21, at 208.
323. Id. at 211.
324. Id.
Vienna Convention treats amendments and interpretations differently, and for good reason. Unlike amendments, interpretations are within the realm of reasonable understanding of a treaty and thus are less likely to frustrate the reliance of third parties and the principles of notice and legality. For that reason, amendments have only prospective effect, while interpretations may be retroactively effective.\textsuperscript{325} That is also why the Vienna Convention sets out no specified form for an agreement on treaty \textit{interpretation} but requires the same formalities to amend a treaty as to conclude one.\textsuperscript{326} Dispensing with the formal requirements for treaty amendment would dramatically lower the transaction cost of amending a treaty, undermining the principle of legality and encouraging short-term thinking by states, particularly where the treaty grants rights to third parties.

Second, most investment treaties include a sunset clause that maintains the treaty’s applicability to investments made while it was in force for some time period after a state withdraws. However, even absent a sunset clause, withdrawing from a treaty and negotiating an amendment are formal, recognizable state acts that differ in critical ways from the acts of pleading as respondent in a dispute or publishing a new model treaty. Political, institutional, and diplomatic barriers are in place to make amending or withdrawing from a treaty difficult and rare. Thus, while it is correct to say that foreign investors “cannot legitimately expect that their treaty rights will be absolute and irrevocable,”\textsuperscript{327} they must expect better than absolute subjection to the whims of the treaty parties.

Particularly where a treaty includes mechanisms that make it difficult or even temporarily impossible for a state to revoke the promises made therein, it is legally unsound to interpret the treaty so as to contravene those mechanisms. The very existence of a sunset clause for the benefit of existing investors evidences an intent to permit them to rely on the treaty, including, if applicable, a commitment therein to dispute resolution unfettered by state interference.

\textsuperscript{325} Id. at 201–02; see also Access to German Minority Schools in Upper Silesia, Advisory Opinion, 1931 P.C.I.J. (ser. A/B) No. 40, at 19 (May 15) (interpretations by courts have retrospective effect).

\textsuperscript{326} See Vienna Convention on the Law of Treaties, art. 39, May 23, 1969, 1155 U.N.T.S. 331 (providing that a treaty may be amended or modified under the rules in Part II of the Convention for concluding a treaty unless the treaty itself provides otherwise).

\textsuperscript{327} Roberts, \textit{supra} note 21, at 210.
Apart from including a sunset clause, states may express their intentions to impede the easy disposal of their agreements by setting out an amendment or withdrawal process. Further, by expressly delegating the interpretation of a treaty to a tribunal in a matter of dispute with a foreign investor, treaty parties can be said to have evidenced an intention to restrict their ability to modify or revoke rights granted therein. Thus, when a treaty grants rights to third parties, imposes barriers to revoking those rights, and omits any explicit reference to binding subsequent agreement and practice, recognizing subsequent agreements, loosely defined, as binding risks undermining predictability and the rule of law.

That is particularly so when a wide range of possible state actions are accepted as grounds for finding a subsequent agreement. Roberts’ threshold for the scope of official acts that can justify subsequent agreements is excruciatingly low. For example, she criticizes one investment tribunal for declining to find that a single response by a government minister to an internal query evidenced an interpretive agreement.328

Roberts also places much emphasis on the idea that states, as sovereigns, retain a right to change their minds, unlike commercial parties, which are more definitively bound when they induce third parties to rely on their promises.329 However, the very reason states enter into treaties is to be bound in exchange for some value they wish to promote. To cavalierly wave aside that function of treaties by invoking sovereign prerogatives is to replace international law with pure politics. The potential impact of such a rule of interpretation does not stop at investment treaties.

Roberts proposes a framework for assessing the authoritative-ness of subsequent practice and agreements, based on when they are issued in relation to the commencement of the arbitration and how reasonable they are.330 In principle those are sensible criteria that may be capable of balancing stability with states’ ability to steer the interpretations of their treaties. However, many of the proposed applications of this framework are problematic.

For instance, she and others argue that tribunals should give

328. Id. at 216–17.
329. Id. at 209–15.
330. Id.
special weight to state interventions in ongoing arbitrations as a means of interpreting the treaty retroactively.\textsuperscript{331} There are a number of issues with this proposal. It reintroduces the problems associated with diplomatic protection, allowing states to use their international political power either in favor of their nationals or, potentially, in favor of the disputing state party to further other political objectives. Additionally, a state may advance an interpretation as a disputing party that is in its short-term interest as a respondent in other arbitrations rather than its long-term interest in the development of international law and in furthering the interests of its own nationals abroad. The lawyers who plead for a state in a dispute are frequently not the officials authorized to represent the state’s international lawmaking position.

More generally, attempts by states such as the NAFTA Parties and the European Union to issue binding interpretations in pending and even concluded disputes compromise “fundamental tenets of procedural justice: (1) equal treatment of the parties, and (2) the principle that ‘no one may be the judge of his own cause.’”\textsuperscript{332} State interventions in ongoing arbitrations have low credibility as actual “interpretations” and can too easily devolve into political interference that undermines the purpose of investor-State arbitration.

C. Proposals to Relax the Rules of Treaty Interpretation

Some states have advanced the position that “necessity” or “essential security” provisions in bilateral investment treaties are self-judging.\textsuperscript{333} Others have argued for something approaching a

\textsuperscript{331} Id. at 219; \textit{Van Harten}, supra note 21, at 131–32. The NAFTA tribunal in \textit{ADF Group v. United States} adopted this approach, giving special weight to the United States’ interpretation because the other NAFTA parties had agreed with the United States in interventions. \textit{ADF Grp. Inc. v. United States}, ICSID No. ARB(AF)/00/1, Award, ¶ 177, (Jan. 9, 2003), 6 ICSID Rep. 470 (2004).


self-judging exception, under which a state could invoke fundamental values such as human rights to justify derogating from the obligations of other treaties to which it is party. 334 A related approach would depart from the rules of interpretation set out in the Vienna Convention and aspire to “reach compromise policy solutions that are acceptable to all” when interpreting investment treaties. 335 However, changes that introduce vague or self-judging public interest, environmental, human rights, or necessity carve outs risk making states’ obligations illusory and undermining the effectiveness of investor-State arbitration.

As Alvarez and Khamsi point out, proposals to rely on preambular text referring to values such as “economic development,” and “effective use of economic resources” take these concepts out of context. 336 The concepts are mentioned as the consequences of achieving the treaty’s object and purpose of protecting foreign investment rather than as freestanding objectives. 337 They thus cannot be legitimately employed to override substantive treaty obligations.

The dangers of self-judging treaty provisions are obvious, particularly where the beneficiaries of the treaty are not other states but individuals, with limited means of redress, who have accepted the treaty’s invitation to rely on its guarantees. 338 Self-judging exceptions certainly should not be recognized where they are not expressly provided for in a treaty, and in a treaty providing for international adjudication, the question has been raised whether such exceptions are legally effective. 339 Self-judging exceptions open the door to abuse, as states inevitably assert that their human rights or other international law obligations excuse or justify their breaches of the investment treaty. Thus, we stand with Sloane in calling for “sustained reflec-

335. Stern, supra note 22, at 185–86.
336. See Alvarez & Khamsi, supra note 123, at 469–70.
337. See id.
338. See supra Part IV.A.
339. See supra note 124 and accompanying text.
tion before general international law adopts [defenses] authorizing exceptions to international obligations in what is, already, a characteristically unstable legal system.”

Some academics and arbitrators, however, propose interpretive devices that would favor such arguments, such as a rule that treats human rights obligations as taking “priority” over obligations to foreign investors. For instance, it has been argued that “while human rights are ‘fundamental’ to human dignity, investment rights are ‘instrumental’ to the achievement of certain policy objectives which, presumably, are not indispensable for human dignity.” Contrary to that breezy dismissal of their significance, investment treaties and neutral international arbitration promote the rule of law and other fundamental values. More importantly, it is questionable how often there will be a true conflict between a state’s obligations to an investor under a BIT and its human rights obligations. An investment treaty will not bar a state from taking actions necessary to fulfill its human rights obligations, but it will require that, if those actions violate the specific obligations the state has undertaken in the treaty toward a foreign investor, it compensate the investor for its consequent loss. As with the doctrine of necessity, the question is who should bear the cost.

Two hypotheticals begin to clarify the picture. First, imagine that a foreign investor commits acts against the domestic population which violate the latter’s human rights. A failure of the state to respond—to stop and punish the actions—would violate its human rights obligations. The state responds appropriately by terminating the investment contract, imposing sanctions, and pursuing criminal charges. The investor’s violation of the law justified the state’s response. The result is that the investor pays for the loss it caused by

341. See, e.g., Simma, supra note 334, at 591.
343. See supra Part VI.
344. Cf. Sloane, supra note 340, at 506–07 (demonstrating that the underlying question where necessity is raised in a dispute between states is which state bears the loss).
345. Cf. Vannessa Ventures v. Venezuela, ICSID Case No. ARB(AF)/04/6, Award, at 52–71 (Jan. 16, 2013), available at http://www.italaw.com/sites/default/files/case-documents/italaw1250.pdf (holding that Venezuela’s actions were justified by the claimant’s
its unlawful actions.

We borrow the second scenario from Simma, who observes that according to the comments to the International Covenant on Economic, Social and Cultural Rights (ICESCR), a state could violate its obligations under the right to water by failing “to effectively regulate and control water services providers” or failing “to take into account its international legal obligations regarding the right to water when entering into [international] agreements.”\(^\text{346}\) If, in entering into an investment contract with a foreign investor, a state has disregarded its obligations under the ICESCR (to which all but a handful of states are already party) or promised substandard regulation to induce the investment, should the investor then be required to bear the loss of its expected return if the state later decides to abide by its obligations? The state, not the investor, is in the best position to assess whether its regulatory framework complies with its human rights obligations, and the investor is entitled to rely on the state’s representations in that regard. If, on the other hand, the investor violates the regulatory framework, resulting in an appropriate state response that results in a loss to the investor, current rules of interpretation would not hold the state liable. Finally, as discussed in detail above, bona fide regulatory changes will not subject a state to liability under existing rules and jurisprudence.\(^\text{347}\) As these examples help demonstrate, it is unclear what is sought by expanding deference to states beyond that already afforded. Indeed, holding states accountable for both their promises to foreign investors and their human rights obligations incentivizes them to ensure that their regulatory framework is human rights compliant at the time a foreign investment is made and thus that the investment operates compatibly with human rights from the outset. Such planning and transparency eliminate the risk of claims arising from later breaches of the investor’s legitimate expectations created by host state misrepresentations.


\(^{347}\) See supra Part IV.C.
CONCLUSION

In the discussion of the current investment protection regime, certain criticisms have been repeated so often that they have come to be accepted by many as fact. We have sought to challenge untested assumptions and show that criticisms are by turns exaggerated, one-sided, and based on inaccurate information. They all drive a movement away from international discipline on state relations with foreign investors, largely targeted at eradicating or eviscerating investor-State arbitration. That movement threatens to undermine the continuing economic development, improved governance, and enhanced rule of law promoted by investment treaties that allow for investor-State arbitration.

There is not a single, monolithic international investment law regime. Instead, over 3,000 bilateral investment treaties and additional regional trade agreements with investment chapters form a network that promotes foreign investment and protects it once made. In addition to choosing the substantive standards to which they wish to bind themselves, states can agree to arbitrate under any of various institutions and rules and can specify particular procedural mechanisms in their investment treaties. Competing regimes offer the benefit of experimentation that can lead to best practices over time or, more likely, various options suitable to certain states. For this “competing systems” approach to work, however, states must be aware that one size does not fit all. A more contingent commitment to arbitration that works for a well-governed state will not be effective for a country facing reputational hurdles to attracting foreign investment. For many of the neediest states, neutral arbitration is indispensable to the efficacy of foreign investor protection, whether through treaties, contracts, or host state law. The impact on such states should thus be a central consideration in assessing any proposed reform of arbitration.

A number of states are actively engaged in reviews and renegotiations of their BITs, and many more have the opportunity to

amend, replace, or even exit existing BITs. Some of those states might curtail the investor-State arbitration clauses and narrow the substantive protections in their treaties, changes that will, for some, increase the cost of capital or shrink investment flows. However, those are policy changes the contracting states to each treaty are free to adopt. The three systemic reform proposals discussed above, by contrast, risk destroying for all states the availability of a credible commitment to neutral dispute resolution by permitting states to interfere politically with the arbitration process.

350. See supra note 315 and accompanying text.