

Governing Globalization: International Law, Foreign Investment, and the Emerging System of Investor-State Arbitration

How do rules emerge to govern various aspects of increasingly globalized relationships and transactions? This project examines the development of the growing system of law designed to govern and to protect cross border direct investments.

Despite the fact that net global flows of foreign direct investment are huge and generally growing, there is no focal regime for governing FDI as there is in the case of international trade. Instead, agreements on how governments will treat foreign investments within their jurisdictions take the form of bilateral investment treaties (BITs). These agreements typically are designed to protect foreign investments, by for example requiring national or most favored nation treatment of FDI, barring performance requirements, and mandating the availability of hard currency for purposes of repatriation. One of the most important provisions of most of these treaties, however, is the obligation to accept international arbitration in the event of an investment dispute. The purpose of arbitration is to help potential hosts make credible commitments to be fair to foreign investors, thereby making some investments attractive that otherwise might be perceived as too risky. Arbitration also presents the opportunity for rule elaboration and law development, which is the focus of this project.

I am ultimately interested in saying something about the normative implications of the international investment regime. But to do so, a few empirical facts are useful. The number of BITs exploded in the 1990s, and I have done empirical modeling this phenomenon that shows this burst of treating was driven at least in part by competitive pressures among potential host (developing) countries. In fact, one of the most reliable predictors of whether a developing country will sign a BIT with another country is that their close competitor(s) have done so. This competitive pressure raises the issue as to whether all of these agreements were entirely well-considered (fully understood?) by the developing countries who entered into them. The econometric evidence that BITs actually end up attracting much foreign capital is fairly weak at best. But one sure consequence of the spread of BITs in the 1990s was the explosion of litigation in the late 1990s and 2000s, especially in Latin America, with the fallout from Argentina's financial crisis of 1997-98.

These disputes are interesting because they involve asymmetrical adversaries: investors and states. This potentially means that a lot of law is developing in this area that arises from cases initiated by a special category of private actors: private foreign investors. And yet the issues raised are very public in nature: they involve regulatory policies, taxation, labor and environmental issues, and indeed the very appropriateness of governmental interventions in an (alleged) economic emergency. Big public policy issues are being challenged in some of these arbitration cases, yet only recently have decisions been made public, and only in some instances have proceedings opened up to broader participation in the form of amicus briefs.

As the number of arbitrations has increased, a few interesting trends are apparent. The few cases that were arbitrated before the 1990s typically involved autocratic regimes, who we may suppose often reneged on agreements with investors for reasons that had little to do with the public good. By the 2000s, however, the defendants were typically highly democratic states, whose legitimacy and accountability to their publics is pretty strong. Moreover, many of the newer arbitration cases involve very sensitive issues – possibly areas not even intended to be governed by a bilateral investment treaty. Water, power, and electricity are now the largest category of cases that go to arbitration under ICSID rules; these are areas that affect the basic well-being of citizens in their daily lives.

Another interesting trend is that despite new rules under ICSID that decisions are to be made public, more cases referred initially to this venue are being settled “out of court.” Completely appropriate in cases involving two private parties, it raises some issues when one of the parties is a public authority and it is not clear what settlement has been reached or why. Finally, a very crude observation about the arbitrators: they are overwhelmingly – more than 75% from the OECD countries. This despite the fact that only about one-third of defendant countries are members of the OECD. Special mention should be made of a select group of arbitrators from the US, UK, France, Switzerland and Canada who have officiated in about half of the cases. Their governments on the other hand have only been defendants about 2% of the time.

None of this constitutes a huge indictment of the system of investor-state arbitration. But it does comport with a view voiced by Benedict Kingsbury and others that the system may be “brittle” in important ways. We do not currently have much of a systematic empirical basis to say a whole lot more than this at the present. The four papers I am proposing would probe this system of investor-state arbitration more deeply in hopes of describing and theorizing its actual operation. Every paper will be empirical; I am hoping in particular to take advantage of being in New York to do surveys/interviews of arbitrators, government officials, and counsel.

Paper #1:

The Ascent of Arbitration:

Explaining the Boom in Investor-State Arbitration

1. *Why do states and firms end up in litigation?*
 - a. Information asymmetries.
 - b. Political constraints (note the growth in *democracies* being sued over time)
 - c. Unanticipated shocks (economic crises)
2. Empirics:
 - a. Chart & quantify the relationship between economic crisis and arbitration
 - b. choose a subset of cases (10-12)
 - c. Information asymmetries: Interviews (state actors):
 - i. How salient was the arbitration provision at time of negotiation?

- ii. How likely did you think arbitration was when you ratified the BIT?
- iii. On what did you base your assessments ex ante?
- iv. How likely do you think it is that [your country] end up in arbitration in the future? What affects the likelihood of arbitration?
- v. Research domestic cases of investor complaints against the government (none – probably did not have information/experience)
- d. Political constraints:
 - i. Subjective: interview government officials: did you feel it was possible political to make concessions that would satisfy the investors?
 - ii. Research the media (L-N, FBIS) for domestic resistance to concessions to an investor – how politicized?
- 3. Conclude: Arbitration is booming because of information asymmetries or because of domestic political constraints, or some combination.

Paper #2

Increasing Returns to Power?

Legal Snowballs in International Arbitration

1. *What is the evidence that the development of international investment law is dominated by investor perspectives?*
2. Empirics:
 - a. Arbitrators
 - i. Nationality
 - ii. Commercial v PIL background
 - iii. Who are the “repeat players”
 - iv. Does a “pro-state” (or “pro-investor”) decision affect changes of being selected to arbitrate in future?
 - v. Subjective evidence from interviews: what are the most important characteristics in choosing an arbitrator? (Experience? A winning record?)
 - b. Counsel – domicile
 - i. Who are the “repeat players”
 - ii. Material incentives to work for state v investor (compare hourly rate and probability of getting paid)
 - c. Citations:
 - i. Western v. non-western sources of law
 - ii. Western v. non-western Arbitrators
 - iii. Cases won by state or investor
 - iv. “pro-state” v “pro-investor” principles
3. Conclusion: Is there evidence of a pro-investor legal snowball in international arbitration of investor-state disputes, and why this is normatively important.

Paper #3:
Dispute Settlement or Law Development?
Four Decades of International Investor-State Arbitration

1. *Is international arbitration of investment disputes evolving away from dispute settlement and toward law elaboration?*
2. Empirics:
 - a. Arbitrators:
 - i. Objective: Commercial arbitrators v PIL background
 - ii. Subjective: interviews: (How do you view what you are doing?)
 1. is it more important to settle a dispute or to make a broader point about law?
 2. More important to be consistent with existing law, or to reach a decision that is acceptable to both parties?
 3. Is it important that decisions are made public?
 4. Is it important to allow non-litigants to participate?
 - b. Decisions:
 - i. Longer, better reasoned, more “justified”
 - ii. More citations – concerned with precedent
 - c. Other participants (amicus):
 - i. More, and more varied (including NGOs and PIL-types)
 - d. Process
 - i. Share of decisions that are public
 - ii. Share of proceedings that are public
3. Conclude: whether there has been change over the past 4 decades in law-development qualities of international arbitration; reflect on the significance for the parties, for investment/development, and for IL.

Paper #4:
The Consequences of Arbitration: Law, Politics, and Economics

1. *What are the consequences for a state, its leaders and its economy of being involved in an international investment dispute?*
2. Empirics:
 - a. Legal consequences:
 - i. BIT revisions: look at amendments post-decision
 - ii. Revisions to national investment laws post-decision
 - b. Political consequences:
 - i. polls, media, elections: does the government/governing party suffer political costs if they concede? lose?
 - c. Economic consequences:
 - i. Budget impact of awards
 - ii. impact on net FDI flows, especially in disputed sector
3. Conclusion: weigh these consequences, come to a normative conclusion.