DISCERNING THE COMPLIANCE CALCULUS: WHY STATES COMPLY WITH INTERNATIONAL INVESTMENT LAW

Christopher M. Ryan*

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* Christopher M. Ryan is an attorney in the International Arbitration and Litigation groups at Shearman & Sterling, LLP. Mr. Ryan is also a lecturer at the University of Virginia School of Law and The George Washington University School of Law, teaching courses on International Investment Law and International Commercial Arbitration. The views in this Article are solely those of the author and do not reflect the views of Shearman & Sterling, LLP or its clients.
I. INTRODUCTION

Over the past twenty-five years, global foreign direct investment (FDI) inflows increased from approximately $200 billion to $1.5 trillion. During that same period, the scope of the legal protections accorded to foreign investments has grown at an equally extraordinary rate. Today, international investment law consists of almost 2,600 treaties among approximately 180 countries. The system of law codifies the obligations that States owe to private investors and gives investors a direct right of action against host governments for breaches of those obligations.

Unlike other areas of international law, where many obligations are perceived as aspirational and where the prospect of enforcement varies, international investment law imposes concrete obligations on the participating States. Enforcement is neither limited to diplomatic or economic sanctions nor tempered by the political sensitivities of the day. Rather, the law is enforced by private actors and imposes the very real threat of forcing governments to defend their sovereign actions before an international arbitral tribunal.

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2 See R. Doak Bishop et al., FOREIGN INVESTMENT DISPUTES: CASES, MATERIALS AND COMMENTARY 1 (2005) (stating that, in the past forty years, 2,200 bilateral investment treaties (BITs) involving 176 countries have come into existence).

3 Sachs & Sauvant, supra note 1, at xxxiv.

4 See Bishop et al., supra note 2, at 1–2 (explaining historical problem of sovereign immunity and the positive effect of States increasing consent to arbitrate as manifested in BITs and private agreements).

It has been assumed that formal acceptance of international investment law—through a bilateral or multilateral investment treaty—was a precondition to foreign investment in many developing States. \(^6\) Individual governments historically have balanced their need for foreign investment against the potential limits that international investment law might impose on them. To the extent the need for foreign investment outweighed concerns over potential limits on, or liability for, sovereign action, States generally elected to enter into bilateral or regional investment treaties with the expectation that foreign investment would follow. Studies, however, have questioned the relationship between investment treaties and foreign investment. \(^7\) At the same time, some government officials and scholars have argued that the scope of international investment law has been expanded beyond the participating States’ original intent. Thus, while the vast majority of participants in the international investment law system abide by their obligations, a number of States have begun to recalculate the costs and benefits of international investment law. Some States, like the United States, have tried to clarify the limits of international investment law through the adoption of new, more balanced investment treaties. Others, mainly in Latin America, have overtly repudiated the system or, at least, have expressly questioned whether continued participation in the system is in their long-term interest.

In light of the compliance costs associated with international investment law and the challenges to the system evidenced by a number of States, it is important to understand why States accept, adhere to, breach, or repudiate the system. To better understand that issue, Part II of this Article discusses the historical

\(^6\) See Andrew T. Guzman, *Why LDCs Sign Treaties that Hurt Them: Explaining the Popularity of Bilateral Investment Treaties*, 38 VA. J. INT’L L. 639, 669–70 (1998) (noting that developing countries are better able to compete for foreign investment by signing a BIT because it increases the credibility of their commitments).

evolution of international investment law. Part III explores alternative theories for why States have bound themselves to international investment law and the varied expectations of the constituencies served by the system. Finally, Part IV explores various factors that influence a State to comply with, breach, or repudiate international investment law in an effort to understand the relative importance of those factors in the compliance calculus.

II. THE ORIGINS OF INTERNATIONAL INVESTMENT LAW

International law is a “construct of norms, standards, principles, institutions and procedures” that serve the purposes of the international community. It is designed to “establish and maintain order and enhance reliable expectations, to protect ‘persons,’ their property and other interests, [and] to further other values.” Historically, the “persons” subject to international law were not natural persons, but States. As such, the rights and obligations imposed by international law typically run from State-to-State, and could be enforced only by States.

International investment law fundamentally differs from traditional or customary forms of international law in several respects. First, unlike customary international law, international investment law does not principally derive its authority from the measure of “consistent State practice” and opinio juris. Rather, while customary international law is relevant to the interpretation of international investment law’s substantive obligations, the willingness of States to follow international investment law is reflected in the approximately 2,600 bilateral investment treaties (BITs) and several multilateral investment treaties currently in force. Such uniformity of consent is rare within the international community and has been characterized as one of the “more remarkable developments in international law in the past 40 years.”

Second, the substantive protections found in international investment law are directed towards private actors. Thus, while States are the formal parties to

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9 *Id.*

10 *See, e.g.*, Frank J. Garcia, *Globalization and the Theory of International Law*, 11 INT’L LEGAL THEORY 9, 10 (2005) (“[I]nternational law exists to order a community in which States are the members.”).


investment treaties, private investors are the principal beneficiaries of the system. By signing investment treaties, States commit to treat foreign investors in accordance with the substantive protections set forth therein. As a “third-party beneficiary,” however, investment treaties (and, indeed, international investment law as a whole) do not impose reciprocal obligations on foreign investors.\(^{13}\)

Third, international investment law provides investors the ability to directly prosecute their own claims against a host government through international arbitration. Investors are no longer forced to choose between litigating investment-related claims in the courts of a host State or seeking diplomatic protection from their home governments. International investment law, therefore, has greatly depoliticized the dispute-resolution process by placing the enforcement decision entirely within the hands of the investor.

The modern form of international investment law can be traced to the post-World War II reconstruction era.\(^{14}\) The system was proposed as a means of substituting private investment into developing States as the bulk of sovereign aid began to wane. The countries—that needed private investment the most, however, typically posed the highest investment risks. Frequently, such countries did not have adequate means of protecting property rights, either because their legal systems did not recognize such rights or because their judiciaries were either incapable or unwilling to enforce them.\(^{15}\) Critical to the development of the international investment law system, therefore, was the creation of two elements: international protections that could supplant the seemingly inadequate domestic regimes of many target States, and adequate incentives that would persuade States to provide foreign investors with higher standards of property rights than were otherwise available in their domestic laws.

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\(^{13}\) The International Institute for Sustainable Development (IISD) has prepared a model investment agreement that would impose social obligations on foreign investors. For a copy of the model agreement, see Int’l Inst. for Sustainable Dev., IISD Model International Agreement on Investment for Sustainable Development (Apr. 2005), available at http://www.iisd.org/pdf/2005/investment_model_int_agreement.pdf.

\(^{14}\) See id. at 4 (stating that “[e]fforts to organize both international protection for foreign investment and methods for resolving disputes began in earnest after World War II”).

\(^{15}\) Zachary Elkins et al., Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960–2000, 2008 U. ILL. L. REV. 265, 277 (2008) (“[G]overnments with little inherent credibility are more likely to sign BITs than are governments known for their fair treatment of foreign capital.”).
A. The Pre-BIT Era

Prior to the modern BIT era, international investment law was predicated largely on customary international law and its contours had not developed very far. Although foreign investments had played a prominent role in international affairs for centuries, the legal protections accorded such investments were extremely slow in developing. The difficulty in creating a universal system of international investment law was predicated largely on three factors.

First, the international community was “divided over what law governed the treatment of foreign investment.” Historically, developed States had accepted international law’s role in governing the treatment of foreign nationals and thus readily accepted that international law should also regulate their treatment of foreign investments. Developing States, by contrast, traditionally had fought against the expansion of international law into areas that they considered to be solely within their domestic purview. Indeed, throughout the 1950s and 1960s, developing States waged a sustained campaign against creating a higher standard of protection for foreign investors and sought to retain absolute sovereignty over their own natural resources, including the right to regulate those resources as they saw fit and the exclusive right to adjudge claims brought by companies benefiting from those resources.

The campaign was fought on both the domestic and international fronts. On the domestic front, many States took measures to solidify their control over foreign investments. For example, a number of Latin American countries adopted the position articulated by the Argentine jurist Carlos Calvo and enacted measures intended to codify the equality of domestic and foreign investors and prohibit foreign investors from claiming rights and remedies that were more extensive than those available to domestic investors. Some countries even incorporated such provisions into their constitutions.

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17 Id.
18 Id.
19 Id. at 27–28. This campaign led the U.S. Supreme Court to observe in 1964 that “there are few issues in international law today on which opinion seems to be so divided as the limitations on a State’s power to expropriate the property of aliens.” Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398, 428 (1964).
21 See id. at 127–28 (quoting Constitución Política de la República del Perú [1933...
On the international front, the emerging socialist States of Eastern Europe and the newly developed States that were formed after the post-World War II collapse of colonialism adamantly sought to establish their economic independence and to insulate themselves from the reaches of international law. The international efforts reached their pinnacle with the passage of the 1962 United Nations General Assembly Resolution on Permanent Sovereignty over Natural Resources, which, in case of nationalizations, purported to allow individual States to determine the amount of "appropriate compensation, in accordance with the rules in force in the State taking such measures in the exercise of its sovereignty and in accordance with international law." A decade later, the United Nations Commission on Trade and Development (UNCTAD) issued a resolution reiterating the sovereign right of States to nationalize companies to "recover their natural resources" and affirming the sole right of the States to adjudicate disputes relating to such actions. However, because neither the General Assembly nor the UNCTAD resolution carried any force of law, they were largely seen as aspirational in nature.

By the mid 1970s, the momentum behind the international campaign waned. In 1974, the United Nations passed the Charter of Economic Rights and Duties of States, which purported to give every state the right to (i) "freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources, and economic activities," (ii) "nationalize, expropriate or transfer ownership of foreign property," and (iii) settle questions of compensation "under the domestic law of the nationalizing State and by its tribunals." Despite the seemingly concrete terms set forth in the Charter, the document was adopted without the support of a single developed State. Since

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26 See RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 reporters' notes 1 (1987) (stating that "[t]he Charter was adopted 120 in favor, 6 against, and 10 abstentions, the vote reflecting the views of the majority as developing States, with the United States among the dissenters and the other developed Western States either dissenting or abstaining").
the Charter had no legal force on its own, the failure of a single developed State to support it confirmed the lack of defined customary international law standards and only served to highlight the disagreement between developed and developing States.\textsuperscript{27} The gap between these divergent perspectives would have to be bridged before a modern system of international investment law could be developed.

Second, the difficulty in creating a universal agreement on international investment law was exacerbated by the fact that the international community could not agree on the content of the law governing foreign investments. Although many Friendship, Commerce, and Navigation Treaties generally referenced property rights and prohibitions against uncompensated expropriation, the specific protections they accorded the property of foreign aliens were ill defined and were largely predicated on customary international law.\textsuperscript{28} As a result, it was believed that such standards were incapable of adequately protecting foreign investors or providing States with certainty as to the scope of their obligations.\textsuperscript{29} To the extent that articulable standards had developed, there was significant disagreement as to their applicability. For example, one of the earliest protections provided to foreign investors was the prohibition against uncompensated expropriation. While the notion that some compensation must be paid was beyond doubt, significant disagreement existed over the standard of compensation. Customary international law simply required expropriating States to provide full compensation.\textsuperscript{30} The United States defined the term "full" compensation to mean "prompt, adequate, and effective" compensation.\textsuperscript{31} Known as the Hull Formula, this standard was widely adopted by developed States and became synonymous with the idea of full compensation.\textsuperscript{32}

\textsuperscript{27} Id.

\textsuperscript{28} See, e.g., W. Michael Reisman & Robert D. Sloane, \textit{Indirect Expropriation and its Valuation in the BIT Generation}, in \textit{74 BRIT. Y.B. INT'L L.} 115, 116 (James Crawford et al. eds., 2003) (noting that "the prototypical FCN treaty did little more than impose upon the host State an obligation not to expropriate covered foreign investments without paying compensation for them").

\textsuperscript{29} For example, there was significant concern that customary law standards "failed to take account of contemporary investment practices and to address important issues of investor concern, such as their rights to make monetary transfers from the host country." Salacuse, \textit{supra} note 11, at 155.


\textsuperscript{31} \textit{GREEN H. HACKWORTH, DIGEST OF INTERNATIONAL LAW} 658–59 (1942).

Developing States vehemently opposed the Hull Formula on the grounds that it impermissibly infringed on their sovereign authority. The United Nations attempted to mediate the dispute by passing General Assembly Resolution 3171, which declared that a State expropriating foreign property "is entitled to determine the amount of possible compensation and the mode of payment, and . . . any disputes which might arise should be settled in accordance with the national legislation of [that] State." As with the Charter of Economic Rights and the Permanent Resolution on Sovereignty over Natural Resources, General Assembly Resolution 3171 had little practical affect. While arbitral tribunals subsequently spoke in terms of "just," "appropriate," or "equitable" compensation, those terms were little more than euphemisms for the Hull Formula.

Third, there was little evidence of the tangible benefit developing States would receive by adopting a formal system of international investment law. The

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33 See, e.g., Gloria L. Sandrino, The NAFTA Investment Chapter and Foreign Direct Investment in Mexico: A Third World Perspective, 27 Vand. J. Transnat'l L. 259, 318 (1994) (asserting that "[m]ost Third World States oppose such high standards of valuation, and instead argue for ‘appropriate compensation . . . taking into account . . . all circumstances that the State considers pertinent’").


35 Libyan American Oil Co. (LIAMCO) v. Libya, reprinted in 20 I.L.M. 1, 79 (1981) (arbitration award of Apr. 12, 1977) (Mahmassani, sole arbitrator) (deeming the award to be "just and equitable compensation").

36 See, e.g., American Independent Oil Co. (AMINOIL) v. Kuwait, reprinted in 21 I.L.M. 976, 1033, ¶ 144 (1982) (final arbitration award of Mar. 24, 1982) (finding that the claimant was entitled only to "appropriate" compensation following the lawful expropriation of its investment by the Kuwait government); Shahin Shaine Ebrahimi v. Iran, 30 Iran-U.S. Cl. Trib. Rep. 170, ¶ 88 (final arbitration award of Oct. 12, 1994) ("The gradual emergence of this rule aims at ensuring that the amount of compensation is determined in a flexible manner . . . taking into account the specific circumstances of each case. The prevalence of the ‘appropriate’ compensation standard does not imply, however, that the compensation quantum should be always ‘less than full’ . . . .")

37 LIAMCO, 20 I.L.M. at 76–77 ("[I]t would be reasonable and just to adopt the formula of ‘equitable compensation’ as a measure for the estimation of damages in the present dispute. This formulation is certainly in complete harmony with the general trend of international theory and practice on the concepts of sovereignty.").

38 Shahin Shaine Ebrahimi, 30 Iran-U.S. Cl. Trib. Rep. 170 ¶ 88 (effectively restating the Hull Formula in holding "while international law undoubtedly sets forth an obligation to provide compensation for property taken, international law theory and practice do not support the conclusion that the ‘prompt, adequate and effective’ standard represents the prevailing standard of compensation . . . [r]ather, customary international law favors an ‘appropriate’ compensation standard").
stated goal was to foster private foreign direct investment in developing States. Private investment lagged dramatically behind sovereign aid, however, and it was unclear whether the business community could or would generate sufficient investment to materially affect a country’s development. At the same time, many developing States were wary of any encroachment on their sovereign authority.

In the face of these three factors, it is hardly surprising that international investment law’s development was stymied during the pre-BIT era.

B. The BIT Era

While the international community could not agree on an overarching paradigm for international investment law, individual States began exploring the potential benefits of bilateral investment relationships. The first BIT was signed in 1959 by Germany and Pakistan. Since that time, over 180 countries entered into more than 2,500 investment treaties, approximately 75% of which have entered into force. These treaties are “truly universal in their reach and essential provisions,” and have “become an integral part of international relations.”

Investment treaties, whether bilateral or multilateral, establish the standards that governments commit to apply to foreign investments. The vast majority of BITs provide investors broad protections against uncompensated expropriation, discriminatory treatment, the inequitable or arbitrary application of the law, and the right to convert local currencies and repatriate profits.

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44 See Schwebel, supra note 16, at 27 (noting that “[c]ustomary international law . . . embod[i]es the principles . . . found in more than two thousand concordant [BITs]).
45 Historically, the major differences among BITs centered around three areas: (a) the types of activities that constituted an investment; (b) when a venture qualified as an “investment” and, therefore, fell within the protections of the treaties; and (c) whether the treaties applied to investments that were made prior to the entry into force of the treaty. See Tobin & Rose-
In addition, investment treaties almost universally give investors the right to submit disputes to international arbitration. This is arguably the most significant right given by investment treaties. Under traditional international law, individuals and corporations did not have standing to bring claims directly against foreign governments. Aside from bringing suit in the domestic courts of the host State (a thoroughly disfavored option), the only recourse available to investors was to request that their home government take up their cause and espouse their claim through either diplomatic negotiations or formal suit at the International Court of Justice. Espousal is equally disfavored by investors because of the political obstacles and loss of control involved. Indeed, the decision to espouse a claim is entirely discretionary. Moreover, before a government can espouse a claim on behalf of one of its nationals, the national must have exhausted its local remedies. Thus, as a precondition to espousal the foreign investor must litigate against the host government in its domestic courts unless the investor can show that there is no reasonable prospect of obtaining an effective remedy in the host State’s courts. Finally, if the investor’s home government elects to espouse its claim, the investor is required to cede all

Ackerman, supra note 7, at 7 (explaining that BITs are intended to “secure the legal environment for foreign investors”).

46 See, e.g., Richard B. Lillich et al., Recent Developments in State Responsibility, 83 AM. SOC’Y INT’L L. PROC. 224, 244–46 (1989) (discussing the Iran-U.S. Claims Tribunal as evidence of how the concept of State responsibility has broadened).

47 See id. at 245 (discussing the historical impossibility of individual actions against sovereign powers).

48 See The Foreign Sovereign Immunities Act: Hearing on S. 825 Before the Subcomm. on Cts. and Admin. Prac. of the S. Comm. on the Judiciary, 103d Cong. 83–84 (1996) (testimony of Abraham D. Sofaer, former Legal Advisor to U.S. Dep’t of State) (stating that “the Department [of State]’s decision with respect to espousal is likely to be influenced, not only by the merits of the case, but by the Department’s concern for offending a foreign State and creating a potential irritant in its dealings with that State”); David J. Bederman, International Law Advocacy and Its Discontents, 2 CHI. J. INT’L L. 475, 484 (2001) (“Individual grievances have tended to be subordinated to the greater good of the nation in its pursuit of common foreign policy objectives.”); see also KENNETH J. VANDEVELDE, UNITED STATES INVESTMENT TREATIES: POLICY AND PRACTICE 160–62 (1992) (stating that “the government may be reluctant to espouse because of a fear that the investment dispute could damages [sic] its relations with the expropriating country and interfere with other foreign policy objectives”).

control over that claim. The government is free to settle or abandon the claim as it sees fit.

III. WHY STATES ENTER INTO BILATERAL INVESTMENT RELATIONSHIPS

The impetus driving developed States to seek out bilateral investment relationships is understandable. Such relationships allow them to selectively choose which countries they grant investment protections, thereby establishing a measure of political, diplomatic, and economic leverage, while at the same time creating mechanisms for protecting their nationals' foreign investments against adverse government action. In addition, developed countries, in particular the United States, viewed bilateral relationships as a means of fostering increased property protections around the world. The United States Trade Representative's office commented that the three goals of the U.S. BIT program were to "1) protect U.S. investment abroad...; 2) encourage adoption in foreign countries of market-oriented domestic policies that treat private investment fairly; and 3) support the development of international law standards consistent with these objectives." The motivation for developing States to enter into such bilateral relationships is often harder to discern. Investment treaties are effectively contracts that oblige governments to treat foreign investments according to international standards. Like contracting parties, States that enter into BITs do so with clear expectations as to the attendant costs and benefits.

As noted, developing States objected to an overarching paradigm for international investment law because the costs were too high; in particular, the system was seen as an unacceptable intrusion on sovereign authority and the standards were vague and ill-defined. In spite of those objections, developing States began entering into bilateral treaties that contained far greater investor

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50 See K. Scott Gudgeon, United States Bilateral Investment Treaties: Comments on Their Origin, Purposes and General Treatment Standards, 4 INT'L TAX & BUS. L. 105, 105 (1986) (noting that the United States created the U.S. BIT program as a "mechanism for protecting U.S. foreign investment in the Third World from unfair or discriminatory treatment").

51 Id. (noting that the U.S. viewed the system as a means of "promoting treatment standards compatible with U.S. policies and principles of international law"); see also Salacuse & Sullivan, supra note 7, at 76 ("In addition to protecting the investments of their nationals, some countries, especially the United States, have had another objective in negotiating BITs: to facilitate the entry and operation of these investments by inducing host countries to remove various impediments in their regulatory systems. They have sought to encourage or induce investment and market liberalization within their negotiating partners.").


53 See supra Part I.
protections than the multilateral treaties that had been rejected. For example, most BITs between developed and developing States formally incorporate the "prompt, adequate, and effective" compensation standard that was rejected by General Assembly Resolution 3171. In addition, BITs typically require host States to provide "fair and equitable" treatment, "full protection and security," and adhere to a "minimum standard of treatment." The general nature of those terms has led to varied and, occasionally, inconsistent interpretations by arbitral tribunals. Finally, a number of BITs contain "umbrella clauses," which require States to adhere to their obligations and thus arguably elevate mere contractual breaches to breaches of international law that, in turn, may give rise to an investor-State dispute.

In light of the broad protections found in most BITs and the objections that developing States raised against granting such protections, it is important to understand why developing States would enter into bilateral investment relationships. Reasons vary; however, explanations typically fall into two categories: the "positive correlation theory" and the "coercion theory."

A. A Perceived Correlation Between BITs and Foreign Direct Investment

One reason why developing States began entering into bilateral relationships is that they believed a direct relationship existed between signing a BIT and increased foreign direct investment. As stated, the countries that need foreign investment the most often provide the least amount of property rights protections. It was perceived, therefore, that foreign investors would be unwilling to risk their capital in a country that did not have well-defined protections for property, either because such rights were not recognized or the country's judicial infrastructure was incapable or unwilling to enforce those rights.

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55 Id. art. 5(1), (2).
57 See, e.g., Elkins et al., supra note 15, at 277 (stating that "[g]overnments with little inherent credibility are more likely to sign BITs than are governments known for their fair treatment of foreign capital"); Tobin & Rose-Ackerman, supra note 7, at 5 (finding that
A BIT was supposed to offset that risk factor by allowing States to publicly commit to treat foreign investments according to international standards.58 From an investor’s perspective, BITs were supposed to increase the credibility of a State’s commitment by “reducing the ambiguity of the host government’s obligations,” including the “investor’s government as a treaty party,” and providing for a direct right of action.59 Thus, by entering into BITs it was thought that developing States could mitigate systemic deficiencies in their legal systems that increase the perceived risk of investing in that State,60 and in doing so, increase their standing in the international community.61

In light of this belief, many developing States felt they faced a Hobson’s choice—either accept international investment law and reap the benefits of increased investment that were supposed to come with it, or reject the system and be placed at a competitive disadvantage with other countries vying for a limited pool of foreign investment. As a result, while developing States publicly reeled against the perceived diminution of sovereign authority that accompanied the acceptance of international investment law, a great number of them elected to embrace the system in the hope that the increased foreign investment would offset any concerns about the potential loss of sovereignty. As explained by a former judge on the Court of Appeals of Sri Lanka “developing countries, beset developing countries frequently “cannot make credible commitments not to violate their own country’s rules”).

58 Professor Andrew Guzman states that BITs help developing countries overcome the problem of “dynamic inconsistency,” whereby they would like to assure investors of their respect for property rights and their willingness to provide investment protections but are unable to give such assurances because of the inherent risks associated with investing in developing countries. By signing a BIT, governments are able to publicly affirm their commitment to international standards and, thus, overcome their inherent structural deficiencies. Guzman, supra note 6, at 658–59.

59 Elkins et al., supra note 15, at 278.

60 See Tobin & Rose-Ackerman, supra note 7, at 5 (noting that “most developing country governments do not have the legal systems and institutional structures in place to adequately enforce laws”). Interestingly, however, at least one empirical study has shown that “developing countries that have signed a BIT tend to be richer, larger, and more democratic” than developing countries that have not signed any BITs. Tom Ginsburg, International Substitutes for Domestic Institutions: Bilateral Investment Treaties and Governance, 25 INT’L REV. L. & ECON. 107, 114 (2005).

61 See, e.g., Beth A. Simmons & Lisa L. Martin, International Organizations and Institutions, in HANDBOOK OF INTERNATIONAL RELATIONS 192 (Walter Carlsnaes et al. 2002) (discussing the impact of international institutions and regimes on domestic behavior and international cooperation); Elkins et al., supra note 15, at 277 (“BITs give host governments a competitive edge in attracting capital if doubts otherwise exist about their willingness to enforce contracts fairly.”).
with economic difficulties, have come to realize that one of the best ways in which their economies can be developed is by encouraging foreign investments, and that the bilateral investment treaty is a fine instrument to achieve that objective.” While facially appealing, this explanation has four principal flaws. First, if a critical mass of developing States were willing to bind themselves to international investment law—as is reflected by the number of developing States that have entered into investment treaties—it makes little sense to reject an overarching paradigm in favor of bilateral relationships. By coming together, developing States could have acted as a unified negotiating block, thereby reducing the costs associated with negotiating individual treaties and maximizing their collective bargaining power. In addition, the adoption of an overarching paradigm governing international investment law would have provided developing States with the largest pool of potential investors because of the multilateral nature of the resulting investment treaty.

Second, a critical aspect of the positive correlation theory is the belief that developing States are able to realistically calculate the costs and benefits of entering into an investment treaty. That belief necessarily assumes that developing States fully understood the scope of obligations they were assuming. Many developing States, however, were unaware of the obligations they were undertaking. For example, Makhdoom Ali Khan, the Attorney General of Pakistan, commented in 2006 that Pakistan entered into dozens of BITs because they presented “photo-opportunities.” At the time, the treaties were “signed without any knowledge of their implications.” Consequently, the “full import of Pakistan’s substantive obligations] became clear only after foreign investors began to invoke the treaty rights in the course of initiating investor-State arbitrations against Pakistan.” According to Mr. Ali Khan, “when you are hit by the first investor-State arbitration you realize what these words mean.”

Third, questions exist regarding the extent to which BITs truly increase (or are perceived to increase) the costs of making commitments. While BITs define a government’s obligations toward a foreign investor, an investor’s willingness to enforce those obligations depends upon a number of factors. For example, if

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64 Id.
65 Id.
66 Id.
67 Elkins et al., supra note 15, at 278.
an investment is impaired, but not destroyed, a foreign investor must balance the possibility of recouping its past losses against the potential revenues it might forego if it can no longer do business in the host State. Hence, a number of investors who initiated arbitration against Argentina for losses incurred during the 2000–2001 economic crisis withdrew their claims in exchange for an opportunity to renegotiate the terms of their concessions.\(^6\) Other companies elected not to initiate arbitration out of concern for the potential adverse effect that the arbitration would have on their future business opportunities in Argentina. Such decisions are made every day by investors around the world.

Similarly, while some have argued that the presence of the investor's home government as a party to a BIT helps ensure the host government's compliance by raising the cost of a breach,\(^6\)\(^9\) the process for resolving investment disputes was designed to remove the home State from the equation. Private investors were given a direct right of action against host governments largely to depoliticize the dispute resolution process. By granting investors a private right of action against governments, BITs were intended to remove the home government from the enforcement equation.\(^7\) Thus, it would appear that the home country's presence in the equation is, at most, a neutral factor.\(^7\)

Fourth, there is limited evidence showing a direct correlation between signing a BIT and increased foreign investment. Indeed, "[t]he most sophisticated analyses to date have found that BITs have had little effect on increasing FDI."\(^7\)\(^2\) For example, a 1998 United Nations study found only a marginal positive relationship between signing a BIT and increased foreign direct investment.\(^7\)\(^3\) Almost a decade later, a leading study determined that


\(^{69}\) Elkins et al., *supra* note 15, at 278.

\(^{70}\) See Convention on the Settlement of Investment Disputes Between States and Nationals of Other States art. 27(1), opened for signature Mar. 18, 1965, 17 U.S.T. 127, 575 U.N.T.S. 159 [hereinafter Washington Convention] ("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 have consented to submit or shall have submitted to arbitration under this Convention . . . .").

\(^{71}\) One area where home-government pressure may play an important role is in cases where a host government refuses to pay an arbitration award. See *infra* notes 87–91 and accompanying text for a discussion of Argentina's refusal to pay adverse awards stemming from its 2000–2001 economic crisis.

\(^{72}\) Ginsburg, *supra* note 60, at 117.

\(^{73}\) U.N. CONF. ON TRADE AND DEV. [UNCTAD], BILATERAL INVESTMENT TREATIES IN THE
although "the presence of a U.S. BIT has a large, positive, and significant association with a country's overall FDI inflows," the presence of BITs from other developed States had a very weak positive effect on the level of FDI.\textsuperscript{7} Factors such as a country's rate of economic growth, population, inflation levels, and market size, and adherence to the rule of law each had statistically more significant effects on FDI inflows.\textsuperscript{74}

By contrast, Brazil, which has not ratified any bilateral or multilateral investment treaties, has seen FDI inflows steadily increase from $1.9 billion in 1980\textsuperscript{76} to approximately $45 billion in 2008.\textsuperscript{77} Similarly, U.S. investment in China has increased dramatically over that same period, despite the fact that the United States and China have not signed a BIT. While arguments can be made that Brazil and China are poor examples because of their size and abundant resources, it is precisely those and other factors that demonstrate the complexity of the investment decision.

\textbf{B. Developing States were Compelled to Enter into BITs}

International investment law is predicated on a tripartite system of consent: (1) States must consent to be bound by the substantive obligations of the system; (2) States must consent to allow investor-State disputes to be resolved by arbitration; and (3) investors must consent to submit disputes to international arbitration. Some have argued, however, that the first two prongs of this system are not truly consensual and that many developing States were in fact coerced into signing BITs.

The coercion argument takes two forms. First, developed States have used BITs as a point of leverage for extracting political, economic, military, or other forms of cooperation from developing States. An example in support of this argument is the BIT negotiations between the United States and Pakistan. Although the United States publicly stated that "Pakistan's 150 million people ... offer a large and potentially valuable market for U.S. exporters and

\textsuperscript{74} Salacuse & Sullivan, \textit{supra} note 7, at 105.

\textsuperscript{75} \textit{Id.} at 99; \textit{see also} Tobin & Rose-Ackerman, \textit{supra} note 7, at 22 (noting importance of economic growth, population, and market size to determining FDI).

\textsuperscript{76} FDI statistics for Brazil may be accessed from the UNCTAD Website by visiting the following web address, clicking on the "FDI Country Profiles" dropdown box, and selecting Brazil, http://www.unctad.org/Templates/Page.asp?intItemID=3198&lang=1.

investors,\textsuperscript{78} the United States' dominant motivation in entering into a BIT with Pakistan appears to have been Pakistan's continued support in "combating global terrorism."\textsuperscript{79} It is clear, therefore, that factors other than a desire to stimulate and protect bilateral investment can drive a developed State's decision to enter into a BIT.

Although developed and developing States may have unequal bargaining power in BIT negotiations, and developed States have almost certainly used BITs as a diplomatic or political carrot, it cannot fairly be said that international investment law is not based on the consent of the parties. Many developing States have actively sought, and continue to seek, bilateral investment relationships in an effort to stimulate foreign direct investment. While a disparity in relative bargaining power may leave developing States at a disadvantage in their ability to negotiate away from the model BITs used by many developed States, their willingness to enter into bilateral relationships can hardly be questioned. Moreover, the coercion argument fails to account for the significant (and growing) number of BITs between developing States. If developing States were truly coerced into signing BITs with developed States, it is unclear why they would voluntarily seek out such treaties with other developing States—particularly in light of the public concerns regarding the international investment law system that a number of developing States have raised. The relatively equal bargaining power among developing States severely reduces the likelihood that one party would have the political, diplomatic, or economic clout to coerce another into signing a BIT.

The second form of the coercion argument is effectively a "race-to-the-bottom" theory. It posits that once one developing State enters into a BIT, others were required to follow suit so as not to be placed at a comparative disadvantage in the competition for foreign capital. Interestingly, the "race" theory creates the prospect for a two-tiered "bottom." At first, investment protections would plateau at the levels established by the relevant BITs. As the number of developing States that sign BITs increases, however, the comparative advantage obtained by signing any one BIT diminishes. Because foreign investors often view potential host States as interchangeable, developing countries would feel pressure to provide incentives beyond those contained in the investment treaties.\textsuperscript{80} The capital that developing States can trade to attract investment is


\textsuperscript{79} Id.

\textsuperscript{80} See, e.g., Yoram Margalioth, \textit{Tax Competition, Foreign Direct Investments and Growth}:
limited, often involving access to raw materials and labor, and promises regarding the stability of the regulatory or tax environments. Thus, the incentives that developing States may be pressured to provide can be at odds with the long-term development goals associated with foreign investment because they either reduce the economic value of the investment to the host State or impose significantly greater regulatory constraints on the host government.

IV. DISCERNING WHY STATES COMPLY WITH INTERNATIONAL LAW

The consensual nature of international investment law means that States must affirmatively elect to participate in the system. It also means that States may affirmatively elect to withdraw from the system. It is important, therefore, to discern what factors influence a State’s decision to comply with, breach, or withdraw from the system.

Existing compliance theories attempt to explain why States adhere to international law generally and, as such, are focused on compliance and enforcement at the State-to-State level. Within that context, the theories show that, to a greater or lesser degree, States balance factors such as their self-interest, the prospect of enforcement, the potential reputational and collateral

Using the Tax System to Promote Developing Countries, 23 VA. TAX REV. 161, 169 (2003) (positing that offering substantial corporate tax incentives will increase FDI into developing countries); Avi Nov, The “Bidding War” to Attract Foreign Direct Investment: The Need for a Global Solution, 25 VA. TAX REV. 835, 835 (2006) (claiming that, in the tax context, “an ‘incentive competition’ or ‘bidding war’ between countries takes place” in an attempt to induce FDI).

While states would continue to be bound by customary international law norms governing foreign investment, such norms do not provide investors with a private right of action against a host government.

affects of a breach, and the costs or benefits of compliance when deciding a particular course of conduct.

States must make a similar calculation when deciding whether to comply with international investment law. The variables in the equation are slightly different, however, because of international investment law’s unique aspects:


See Andrew T. Guzman, *A Compliance-Based Theory of International Law*, 90 Cal. L. Rev. 1823, 1825 (2002) (“This Article . . . puts forward a theory of international law in which compliance comes about in a model of rational, self-interested States. International law can affect State behavior because states are concerned about the reputational and direct sanctions that follow its violation.”); see also Hathaway, *supra* note 83, at 473 (emphasizing the effect of legal enforcement and collateral consequences).
These variables fundamentally alter the costs and benefits of the system and force States to apply a different calculus when determining whether to accept and ultimately comply with international investment law.

A. Legal Liability

International investment law permits investors to bring claims directly against States. As such, a breach of international investment law carries with it the prospect of significant financial liability. A recent study shows that, as of 2006, the amount of quantified damages claimed in investment treaty arbitrations ranged from $155,314 to $9.4 billion, with an average claim of approximately $345 million. The same study, however, shows that successful claimants are often awarded substantially less than their claimed damages, with the average award totaling $10.4 million.

The prospect of such liability—be it either the claimed amount or the awarded amount—can be daunting, particularly to developing States. The affect that such liability can have on States and the international arbitral process is reflected in two examples. First, Argentina is a respondent in over forty cases stemming from its response to the country's 2000–2001 economic crisis. To date, nine awards on the merits, totaling over $1 billion in damages, have been issued against Argentina. Arbitrations against Argentina have also produced

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86 Id. at 58.


some of the largest awards ever issued in an investment dispute, including the $132.3 million award to CMS Gas Transmission Company\(^9\) and the $165 million award in favor of Azurix Corporation.\(^9\)

Argentina, however, has refused to pay any of these awards. Indeed, CMS Gas Transmission Company, one of the first investors to obtain a ruling against Argentina, transferred its award of $133.2 million to a subsidiary of Bank of America that specializes in collecting distressed debt.\(^9\)

Second, in *Himpurna California Energy Ltd. v. PT (Persero) Perusahaan Listruik Negara*\(^9\) and *Patuha Ltd. v. PT (Persero) Perusahaan Listruik Negara*,\(^9\) foreign investors entered into agreements with Indonesia to construct power plants and to sell the power generated by those plants back to the government. Although the investment was not protected by a BIT or other treaty, Indonesia contractually assumed international investment law’s substantive obligations and provided the investors the right to submit investment disputes to international arbitration. A dispute arose and the government refused to purchase power as required by the agreement. The claimants submitted their disputes to arbitration, seeking billions of dollars in damages for both wasted costs and lost profits. Although the arbitral tribunals ultimately determined that Indonesia was liable, they awarded the claimants only 10% of their claimed lost profits on the grounds that awarding the full amount would constitute an “abuse of right.”\(^9\)

The Himpurna tribunal noted that the claimants’ damages must be curtailed so as “to prevent the claimant’s undoubtedly legitimate rights from...
being extended beyond tolerable norms, and failure to do so would impose on Indonesia “ever-increasing losses” that “would be ruinous to the respondent.”

The tribunals’ reliance on the “abuse of right” doctrine met with significant controversy. What is notable, however, for purposes of this analysis is that the tribunal explicitly recognized the fact that the legal liability attendant to international investment law has the potential to have a ruinous effect on host governments.

B. Scope of Obligations

States must understand the scope of their obligations to determine the relative costs and benefits of compliance in any given case. This understanding comes from the fair and uniform application of clearly defined standards. A culture of compliance cannot emerge unless States see and believe that the law has been applied neutrally and consistently.

Investment treaties are constitutive in nature and, as such, generally use broad terms when describing the host government’s obligation. For example, virtually all investment treaties prohibit uncompensated expropriations and require governments to treat foreign investments “fair[ly] and equitab[ly].” Most treaties require that governments provide investors “fair and equitable treatment” and “full protection and security.” In many respects, the use of such broad language is beneficial because it allows for greater flexibility. From the

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95 Himpurna, 25 Y.B. Com. Arb. at 93.
96 Id. at 90.
97 A full discussion of this doctrine is not within the scope of this Article. For more information, see Irina Petrova, “Stepping on the Shoulders of a Drowning Man” The Doctrine of Abuse of Right as a Tool for Reducing Damages for Lost Profits: Troubling Lessons from the Patuha and Himpurma Arbitrations, 35 GEO. J. INT’L L. 455, 463–69 (2004); Louis T. Wells, Double Dipping in Arbitration Awards? An Economist Questions Damages Awarded to Karaha Bodas Company in Indonesia, 19 ARB. INT’L 471 (2003) (providing economic argument that another arbitral award was excessive).
99 See, e.g., Model BIT, supra note 54, art. 5.
100 Id.
101 See, e.g., LG&E Energy Corp. v. Argentina, ICSID Case No. ARB/02/1 (decision on liability, Oct. 3, 2006), 21 ICSID Rev.-Foreign Inv. L.J. 203, 234, ¶ 123 (2006), available at http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc &docId=DC627_En&caseId=C208. The decision notes that the fair and equitable standard was initially articulated in the 1920s and required that “state conduct be deemed outrageous, wrongful, open injustice, an atrocity, bad faith or voluntary negligence of duty for a violation to be found.” Id. ¶ 123 n.29. However, “[t]hat interpretation is not the same that is given today. What was considered an ‘atrocity’ in 1926 might not be so today, and what may be considered
perspective of certainty, however, generalized obligations of this type offer States little comfort.

Where constitutive documents do not provide clear standards, clarity must come from arbitral or judicial bodies charged with interpreting those documents. In the United States, for example, the courts are charged with interpreting the Constitution and statutes, many of which are as broadly worded as investment treaties. In the international investment context, arbitral tribunals should provide the same clarity with respect to the obligations set forth in investment agreements. Some critics, however, have questioned whether the arbitral system has provided the necessary certainty.

The criticism stems, at least in part, from two factors. First, the modern system of international investment law is relatively young. The first BIT was signed in 1959 and the majority of arbitral decisions have been issued in the past ten years. As such, the substantive norms are still being developed.

Second, there is no stare decisis within the investment arbitration system. Although the public nature of International Centre for Settlement of Investment Disputes (ICSID) awards has led to a greater reliance on prior awards by parties and arbitrators alike, tribunals need not follow those awards and are free to decide each case on its own merits. For example, over forty arbitrations have been brought against Argentina stemming from the passage of certain laws in 2000 and 2001. Each of those cases involved the same time period, facts, and allegations. In defense of these cases, Argentina has consistently argued that its actions should be excused as a matter of “necessity” under international law because of the economic crisis it faced at that time. To date, five tribunals have ruled on the merits of Argentina’s necessity defense. Four of the five tribunals rejected the defense and held Argentina fully liable notwithstanding the occurrence of the economic crisis.102 One tribunal, however, accepted the

argument and excused Argentina from liability during the peak months of the financial crisis.\textsuperscript{103}

The uncertainty created by the lack of precedent in international arbitration affects both investors and States alike. Such uncertainty increases the difficulty in counseling investors on their international treaty rights and predicting how arbitral tribunals will rule on particular issues. From the State perspective, the uncertainty makes it difficult for governments to know what regulatory measures are permissible under international investment law. To offset the risks inherent in this uncertainty, some countries have elected to limit their consent to international arbitration. For example, the Philippines and Japan omitted a provision allowing investors to submit investment disputes to arbitration from their 2003 Economic Partnership Agreement.\textsuperscript{104} Similarly, while the Russia-Venezuela bilateral investment agreement (which was ratified by the Russian Federation in September 2009) permits investors to submit disputes to arbitration, it limits their choice of forum.\textsuperscript{105} Although both countries are signatories to the ICSID Convention, the treaty omits ICSID as a forum to which disputes could be submitted. Instead, investors may submit disputes to courts in the host State, ad hoc arbitration under the UNCITRAL rules, or arbitration pursuant to the Stockholm Chamber of Commerce rules.\textsuperscript{106}

Some countries have tried to reduce the uncertainty by minimizing ambiguities within their investment treaties. For example, the United States' BITs are based on model agreement that was first drafted in 1982.\textsuperscript{107} At the time, it provided broad investor protections that were intended to reflect both U.S. and international law standards.\textsuperscript{108} In 2004, the United States substantially revised its model Bilateral Investment Treaty. In so doing, it precisely defined and, in some cases, narrowed the substantive protections accorded to investors.\textsuperscript{109}

\textsuperscript{103} See LG&E, 21 ICSID Rev.-Foreign Inv. L.J. at 267–68, ¶ 267 (dismissing claim because "Argentina was in a state of necessity").


\textsuperscript{105} Acuerdo Entre el Gobierno de la Republica Bolivariana de Venezuela y el Gobierno de la Federacion de Rusia Sobre la Promocion y Proteccion Reciprocas de Inversiones, 369 GACETA OFICIAL DE LA REPUBLICA BOLIVARIANA DE VENEZUELA 439, 440, art. 9(2) (June 2, 2009).

\textsuperscript{106} Id.

\textsuperscript{107} Model BIT, supra note 54.


\textsuperscript{109} See Model BIT, supra note 54. For a critique of the new model BIT, see Stephen M.
These revisions were made in an effort to create more certainty and predictability in how tribunals would interpret and enforce U.S. BITs and have been incorporated in subsequent BITs and Free Trade Agreements signed by the United States.

In 2008, Norway proposed a new model BIT that would have resulted in several major substantive changes.10 In particular, the new BIT would have included an exhaustion-of-local-remedies requirement and would have narrowed the definition of "investor" so as to limit the ability of so-called "mailbox" companies from using the treaty's protections.11 Notably, the proposed BIT also emphasized the importance of corporate social responsibility, human rights, and sustainable development, and as such, sought to impose basic duties on investors as a precondition to obtaining protections under the treaty.12 In June 2009, Norway abandoned its efforts to adopt the proposed model BIT after receiving considerable resistance from a number of nongovernmental organizations and business groups, who claimed that the proposed model both failed to provide enough substantive protections to investors and unduly restrained the government's ability to regulate in the public interest.13 According to one government official, the prospect of "achieving a proper balance was too difficult" to justify moving forward with the proposed model.14 As a result, Norway has questioned whether it will enter into future BITS. For the moment, Norway has indicated that it would consider including investment provisions in the context of a free trade agreement.15 Thus, Norway's dissatisfaction with the current BIT system and its inability to create increased certainty has called into question the country's future participation in the system.

Still other countries have tried to eliminate the uncertainty altogether by moving away from the international investment law system. For example, the Bolivarian Alternative for Latin America and the Caribbean was created in 2006


12 Id. art. 23(3)(viii).


14 Id.

15 Id.
as a means of fostering economic integration among the countries of Latin America. Unlike other similar organizations, the Bolivarian Alliance explicitly rejects the notion of bilateral or regional investment treaties. The Alliance was initially proposed by Venezuela and Cuba, but today includes ten Latin American countries. As evidence of the Alliance’s hostility to international investment law, two members—Bolivia and Ecuador—have withdrawn from the ICSID Convention, and others have threatened to follow suit.

While the actions of countries that have moved away from the international investment law system have resulted in substantial debate within the legal and academic community, they remain outliers within the system as a whole. Nevertheless, while the utility and impact of each country’s response can be debated, it is clear that a need for greater certainty exists and that the desire for such certainty is a driving force behind the actions of many countries. It is also clear that greater certainty is essential for the system’s long-term growth and legitimacy.

C. Domestic Expectations/Demands

States must balance their international obligations against the needs and demands of various domestic constituencies. Achieving that balance within the context of international investment law can be difficult. International investment law creates a two-tiered system of protections that intentionally advantages foreign investment over domestic investment. Although international investment law does not replace the host country’s entire domestic regime, it does provide foreign investments a higher standard of property rights protections than are typically available to domestic investors. In many cases, this disparity is meaningless because foreign investment exists in sectors where there is little or no domestic competition. In some cases, however, domestic and foreign investments coexist and the increased protections available to foreign investments could create resentment by domestic investors.

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118 See infra notes 124–33 and accompanying text.
Moreover, foreign investment and international investment law are often closely intertwined with politically sensitive issues of State sovereignty. Foreign investment in many States—particularly developing States—is directed principally at infrastructure and natural resources—two sectors that are embedded with nationalistic sentiment and perceptions of sovereign authority. Developing States, therefore, must balance the need for foreign investment in those sectors against the perception that foreign investors may exploit their dependence on such investment.

The necessary balance is not always easily achieved. Even when it is, the balance can shift over time as governments and public sentiment change. Recent events in Bolivia and Ecuador illustrate the tensions that can exist between a State’s international obligations and domestic demands.

1. Bolivia

Bolivia is one of the poorest countries in Latin America, with an economy that is principally tied to its natural resources. Due to its poverty and lack of industry, Bolivia has long needed foreign investment to benefit from those resources.

In the early 2000s, Bolivia underwent a political shift that saw an increase in nationalistic sentiment and a push for increased sovereign control over the country’s natural resources. In 2005, Evo Morales was elected President of Bolivia and undertook to regain control over privatized natural resources. Within the first 100 days of his term, President Morales moved to nationalize the nation’s oil and gas sector, transferring majority control in the industry to the State oil company, Yacimientos Petrolíferos Fiscales Bolivianos. At the time, Bolivia was a party to BITs with Argentina and Spain, both of which had investors who were adversely affected by Bolivia’s actions.

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120 Id.

121 See, e.g., Paulo Prada, Bolivian Nationalizes the Oil and Gas Sector, N.Y. Times, May 2, 2006, at A9, available at http://www.nytimes.com/2006/05/02/world/americas/02bolivia.html (stating that Morales ordered private foreign producers to forfeit control of oil fields, providing 180 days to renegotiate contracts). At the time, Bolivia was party to nineteen BITs. A full list of the BITs to which Bolivia is a party can be found at U.N. Conf. on Trade and Dev. [UNCTAD], Total Number of Bilateral Investment Treaties Concluded, 1 June 2009, http://www.unctad.org/sections/dite_pcbb/docts/bits_bolivia.pdf.

122 Prada, supra note 121; see also U.S. Dep’t of State, Bureau of Econ., Energy and Bus.
Bolivia has been named as a respondent in three investor-State arbitrations brought to ICSID. Based largely on that experience and a concern over the perceived disadvantages faced by developing States in investment arbitrations, Bolivia notified ICSID in May 2000 that it would withdraw from the Convention on the Settlement of Investment Disputes between States and Nationals of Other States effective November 3, 2007. At the time of its notification, two cases against Bolivia were pending before ICSID tribunals.

Membership in the Washington Convention is a precondition to accessing the ICSID arbitral process. By withdrawing from the Washington Convention, Bolivia has removed the prospect of ICSID arbitration as a means of resolving investment disputes with future investment partners. At the same time that Bolivia denounced the Washington Convention, it announced a systematic process of renegotiating concession and foreign investment agreements with the goal of restoring the purported economic equilibrium of the agreements and creating terms more favorable to Bolivia.

Finally, in January 2009, Bolivia ratified a new constitution that, among other things, subjected foreign investors to Bolivian sovereignty, Bolivian law, and Bolivian authorities with respect to any activity carried out in the hydrocarbons sector. As such, all disputes in that sector shall be resolved exclusively by the


123 Washington Convention, supra note 70.
126 Bolivia’s withdrawal from the Washington Convention does not vitiate its consent to ICSID jurisdiction for investment disputes submitted to ICSID prior to the date of withdrawal. Similarly, strong arguments can be made that Bolivia’s withdrawal does not affect the consent to ICSID jurisdiction contained in any of Bolivia’s existing BITs. Article 72 of the Washington Convention provides that withdrawal from the Washington Convention “shall not affect the rights or obligations under this Convention [of the withdrawing State] arising out of consent to the jurisdiction of the Centre given . . . before such notice was received by the depositary.” Washington Convention, supra note 70. An arbitral tribunal has clearly held that a state’s consent to ICSID jurisdiction is found in the language of a BIT permitting an investor to submit disputes for resolution to the Centre and becomes irrevocable at the time the BIT is ratified. Lanco Int'l Inc. v. Argentina, ICSID Case No. ARB/97/6 (Preliminary Decision on Jurisdiction of Dec. 8, 1998), reprinted in 40 I.L.M. 457 (2001).
127 Constitución de 2009 arts. 351, 359–68 (Bol.), available at http://pdba.georgetown.edu/
Bolivian courts. Foreign investors are prohibited from submitting such disputes to international arbitration and from seeking the diplomatic protection of their home governments. Moreover, foreign arbitral awards involving Bolivia’s hydrocarbon sector will no longer be recognized or enforced, and existing foreign arbitration awards may be annulled by the Bolivian courts.

2. Ecuador

Over the past two years, Ecuador has incrementally withdrawn its consent to the international investment law system. In December 2007, Ecuador notified the ICSID Secretariat that, pursuant to Article 25(4) of the Washington Convention, it no longer consented to ICSID’s jurisdiction over disputes regarding oil, mining, and other natural resources. Then, in October 2008, Ecuador notified the governments of Cuba, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, the Dominican Republic, and Uruguay that it was denouncing the BITs it had signed with each country. Ecuador’s reason for terminating the treaty relationships was that Ecuador had reviewed “its domestic as well as international policies in the matter of investments,” evaluated “the impact of the BITs on the national economy,” and concluded that those treaties have “not reached [their] fundamental objective, that is, to motivate the attraction of capitals.”

Finally, on July 6, 2009, Ecuador formally notified ICSID that it was withdrawing from the ICSID system effective January 7, 2010. At the time, Ecuador was a named respondent in six ICSID cases and is facing billions of

Constitutions/Bolivia/bolivia09.html.

128 Id. art. 366.
129 Id.
dollars in potential liability. Ecuador’s president announced that its actions were necessary to further “the liberation” of Ecuador because ICSID “signifies colonialism, slavery with respect to transnationals, with respect to Washington, with respect to the World Bank and we cannot tolerate this.” Ecuador has a long record of questioning ICSID’s impartiality and objecting to what it perceives as unfairness in the international investment law system.

3. Reputation/Investment Climate

A State’s reputation exists at both the investment and systemic levels. At the investment level, countries seeking foreign investment attempt to create a stable and transparent investment environment that has the “appropriate legal, administrative, and regulatory framework” that “modern investment theory has come to recognize as a *conditio sine qua non* of the success of” private investment. The investment-level reputation, therefore, bears directly on a State’s attractiveness to potential investors.

By contrast, a State’s reputation at the systemic level bears on its attractiveness as a treaty partner to other States. The greater a State’s reputation for compliance, the greater the likelihood other States would be willing to enter into treaties with it. States that are interested in expanding their participation in the investment treaty system, therefore, have a vested interest in taking actions that do not undermine their commitment to the system.

State action can affect its reputation in different ways. At the investment level, directed action against a single or small number of investors will be perceived differently than acts that cut across entire industries. While potentially giving rise to legal liability, such directed actions do not necessarily call into question the State’s commitment to the international investment law.

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134 ICSID, List of Pending Cases, *supra* note 87. In total, Ecuador has been named as a respondent in thirteen ICSID arbitrations since 2001.


136 *Id*.


138 See, e.g., Andrew T. Guzman, *The Design of International Agreements*, 16 EUR. J. INT’L L. 579, 596 (2005) (“A state that violates an international commitment signals . . . that it does not take its international promises seriously and . . . is willing to ignore its obligations. When that state seeks to enter into agreements . . . its potential partners will take into account the risk . . . and will be less willing to offer concessions . . . in exchange for promises from that country. If there is enough suspicion, potential partners may simply refuse to deal with the state.”).
system as a whole. As in other areas of law, individual instances of breach do not necessarily reflect a repudiation of the law per se. While directed action may tarnish the perception of the State’s investment environment or cause subsequent investors to price investments differently—i.e., seek greater incentives or guaranteed returns on their investment—they likely would not diminish the State’s prospects of entering into other investment treaties.

At the systemic level, a State’s reputation can be harmed by actions that call into question its commitment to the international investment law system. Such actions can take several forms. As described above, Argentina has refused to pay valid ICSID awards issued in favor of foreign investors. Argentina’s position is notable in that it is the first time that a government has refused to pay an adverse award issued by an ICSID tribunal, overtly calling into question Argentina’s willingness to comply with a system that it voluntarily adopted.\textsuperscript{139} Thus, given their wide-ranging implications, Argentina’s actions necessarily have a direct effect on its systemic reputation.

Similarly, the withdrawal from ICSID by Bolivia and Ecuador, coupled with Ecuador’s Article 25 notice and denunciation of various BITs, severely undermine their commitment to the system. Such actions not only affect their investment-level reputations, but also their systemic reputations and, thus, could have an effect on the willingness of other States to enter into future treaties with either country.

V. CONCLUSION

States must balance multiple variables when determining whether to accept, breach, or repudiate international investment law. Recent events have shed light on the various factors that underlie a State’s decision-making process and are useful in discerning trends. For example, the most vocal opponents of the international investment law system—Argentina, Ecuador, Bolivia—have been respondents in multiple investment disputes and have recently undergone substantial internal political upheaval. Their perspective, therefore, appears to be heavily influenced by the prospect of substantial financial liability and the desire to appease domestic pressures by reasserting control over natural resource and infrastructure sectors—areas that are closely tied with notions of sovereignty and national pride. Similarly, while the United States was one of the principal architects of the current international law system, it entered into the

\textsuperscript{139} For a discussion regarding the enforceability of ICSID awards and the affect of Argentina’s actions, see High Noon a Round Table over Unpaid ICSID Awards, GLOBAL ARB. REV., Dec. 1, 2008.
majority of its investment treaties at a time when there was little prospect of substantial reciprocal investment from its treaty partners. Thus, the broad constitutive language used in its early BITs was intended principally to protect U.S. investors without regard to the possibility that the United States may actually be named as a respondent in an investment dispute. Times have changed, however, and the United States has been hailed before NAFTA tribunals on several occasions. Although the United States has never lost an investment dispute, it is clear that the uncertainty surrounding the scope of international investment law’s substantive obligations has caused the United States to modify its approach to the area of law. Thus, its revised Model BIT is intended to provide greater certainty and to more clearly limit the scope of potential liability.

Over time, as more data becomes available, it should be possible to assess the relative weight the above-mentioned variables play in the State decision-making process. At the moment, however, the identification of these variables should allow existing and potential investors to discern trends in State conduct and may help predict how States will react to changes in their political, economic, or social conditions.