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UNCTAD's REFORM PACKAGE FOR THE INTERNATIONAL INVESTMENT REGIME

2018 EDITION

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NOTE

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The Division provides, among others,

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FOREWORD

UNCTAD's Reform Package (2018) is the result of a collective effort, led by UNCTAD, pooling global expertise in the investment and sustainable development field from international organizations and numerous international experts, academics, business, practitioners and other stakeholders in the field of investment law and policy. UNCTAD's Reform Package has been designed as a "living document" for regular updates, in light of the new developments and advocacy for reform, with a standing invitation to the international community to exchange views, suggestions and experiences.

The Reform Package combines the research and policy analysis from the World Investment Report 2015 (*WIR15*) (the Road Map for international investment agreement (IIA) Reform), the World Investment Report 2017 (*WIR17*) (the 10 Options for Phase 2 of IIA Reform) and the World Investment Report 2018 (*WIR18*) (the guidance for Phase 3 of IIA Reform) into one single document.

Various elements of the Reform Package were peer-reviewed at numerous high-level intergovernmental meetings, including UNCTAD's Ministerial Conferences, UNCTAD's Trade and Development Board, its Commission on Investment and Development, the World Investment Forums 2012, 2014 and 2016, as well as several of UNCTAD's Annual High-level IIA Conferences.

UNCTAD's tools for IIA reform also received significant attention from numerous international organizations and groups. They were discussed at the African, Caribbean and Pacific (ACP) Group of States, Investment and Private Sector Subcommittee meetings, the Asia Pacific Economic Cooperation (APEC) Investment Expert Group (IEG) meetings, the Islamic Development Bank (IDB) and Organisation of Islamic Cooperation (OIC) IIA Conferences, the Organisation for Economic Co-operation and Development (OECD) Freedom of Investment (FoI) Roundtables, the United Nations Commission on International Trade Law (UNCITRAL) Commission sessions and Working Group meetings, sessions at the Meeting of the Energy Charter Conference, the Annual Forum on Business and Human Rights and the International Institute for Sustainable Development (IISD)-South Centre Annual Forums of Developing Country Investment Negotiators. Informal discussions among the Friends of Investment Facilitation for Development in the World Trade Organization (WTO) also referred to elements of UNCTAD's Reform Package.

Different parts of the Reform Package have been field-tested in beneficiary countries and regions (including through UNCTAD's advisory services and its Investment Policy Reviews) and have formed the basis of numerous regional training courses organized or co-organized by UNCTAD, including for countries in Africa, Asia, Latin America and for economies in transition.

Now consolidated into one comprehensive Reform Package, UNCTAD makes available a coherent, sequenced and user-friendly set of options for countries engaging in IIA reform. This comes at a time when IIA reform has entered the mainstream of international investment policymaking.

Over the past years, UNCTAD's policy tools have generated significant impact. The Road Map for IIA Reform and subsequent guidance have spurred global reform efforts and actions. Numerous countries have used them to review their treaty networks and to design new model treaties with innovative features. Today, most new treaties contain key reform elements as set out in UNCTAD's Road Map, as do important regional investment policy initiatives, such as the 2016 Amendments to the SADC Protocol on Finance and Investment, the Pan-African Investment Code and the Intra-MERCOSUR Cooperation and Facilitation Investment Protocol. Some parts of the Reform Package have shaped global reform efforts, such as efforts to foster transparency in investment dispute settlement or initiatives for an international investment court system/multilateral investment court.

They have also found reflection in key investment policy instruments, such as the G20 Guiding Principles for Global Investment Policymaking, the draft Joint ACP-UNCTAD Guiding Principles for Investment Policymaking, or the draft Guiding Principles for Investment Policymaking for OIC countries.

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TABLE OF CONTENTS

EXECUTIVE SUMMARY

In the last ten years, the need for systematic reform of the global international investment agreements (IIA) regime has become increasingly evident. Heated public debate, parliamentary hearing processes and demonstrations on the street have been taking place in many countries and regions. A shared view has emerged on the necessity to ensure that the international investment treaty regime works for all stakeholders. The question is not about whether to reform, but about the substance of such reform (the what), as well as the process and mechanisms of reform (the how).

Based on its extensive policy analysis and work over the past years, UNCTAD's World Investment Report 2015 (*WIR15*) on Reforming Global Investment Governance provided a Road Map for IIA Reform focusing mainly on the substance of reform. UNCTAD's subsequent stocktaking of reform efforts showed that while key reform options were increasingly being incorporated in new treaties, urgent action was required on the stock of old treaties. *WIR17* responded with the recommendation to move to Phase 2 of the reform process (modernizing the stock of over 2,500 old-generation treaties currently in force) and provided policy options. Finally, as reform efforts increasingly brought to light inconsistencies in national and international investment policy frameworks, *WIR18* presented policy options as part of Phase 3 of the reform process to enhance coherence of IIAs with each other, with national investment policies and with other bodies of international law affecting investment.

The updated Reform Package (2018) presents a consolidated version of UNCTAD's research and policy guidance on IIA reform derived from these publications.

Phase 1 of IIA Reform concerns the substance of IIAs and addresses five priority areas for reform. IIA reform should aim at (i) safeguarding the right to regulate in the public interest while providing protection; (ii) reforming investment dispute settlement to address the legitimacy crisis of the current system; (iii) promoting and facilitating investment; (iv) ensuring responsible investment to maximize the positive impact of foreign investment and minimize its potential negative effects; and (v) enhancing the systemic consistency of the IIA regime so as to overcome the gaps, overlaps and inconsistencies of the current system and establish coherence in investment relationships (figure 1).

In recent years, IIA reform has made significant progress and entered the mainstream of international investment policymaking. Since 2012, over 150 countries have undertaken at least one reform action in the pursuit of sustainable development-oriented IIAs, and most new treaties contain key reform elements as set out in UNCTAD's Road Map. Dispute settlement is high on the agenda, with concrete steps undertaken, including at the multilateral level (e.g. reform-oriented clauses in new treaties, work on the establishment of an international investment court). Investment facilitation has become an area of increased interest in IIA making, and UNCTAD's Global Action Menu on Investment Facilitation has obtained strong support from all investment-development stakeholders. Moreover, recent treaties include new language that preserves host States' right to regulate or fosters responsible investment.

But more needs to be done. Phase 2 of IIA Reform envisages modernizing the existing stock of old-generation treaties. Old treaties abound: more than 2,500 IIAs (95 per cent of all treaties in force) were concluded before 2010. Old treaties "bite": all of today's

known investor-State dispute settlement (ISDS) cases are based on those treaties. And old treaties perpetuate inconsistencies: their continued existence creates overlaps and fragmentation in treaty relationships and interaction challenges. IIA reform requires a two-pronged approach: improving new treaties and modernizing existing ones.

Phase 2 of IIA Reform presents and analyses 10 policy options: (1) jointly interpreting treaty provisions; (2) amending treaty provisions; (3) replacing "outdated" treaties; (4) consolidating the IIA network; (5) managing relationships between coexisting treaties; (6) referencing global standards; (7) engaging multilaterally; (8) abandoning unratified old treaties; (9) terminating existing old treaties; and (10) withdrawing from multilateral mechanisms. Countries can adapt and adopt these options to pursue the reforms set out in the Road Map. Global policy debate on Phase 2 of IIA Reform culminated at UNCTAD's October 2017 High-level IIA Conference, when more than 350 experts shared their experiences, identified best practices and charted the way forward towards the third phase of reform.

Phase 3 of IIA Reform, finally, focuses on improving coherence, consistency and interaction between different levels and types of policymaking. In particular, shaping the interaction of national and international dimensions of investment policymaking requires a solid understanding of the different objectives, functions and natures of the legal instruments involved. At the country level, an incoherent IIA network can expose the host State to undesirable effects. IIA reform should also take into account the interaction between IIAs and other bodies of international law affecting investment.

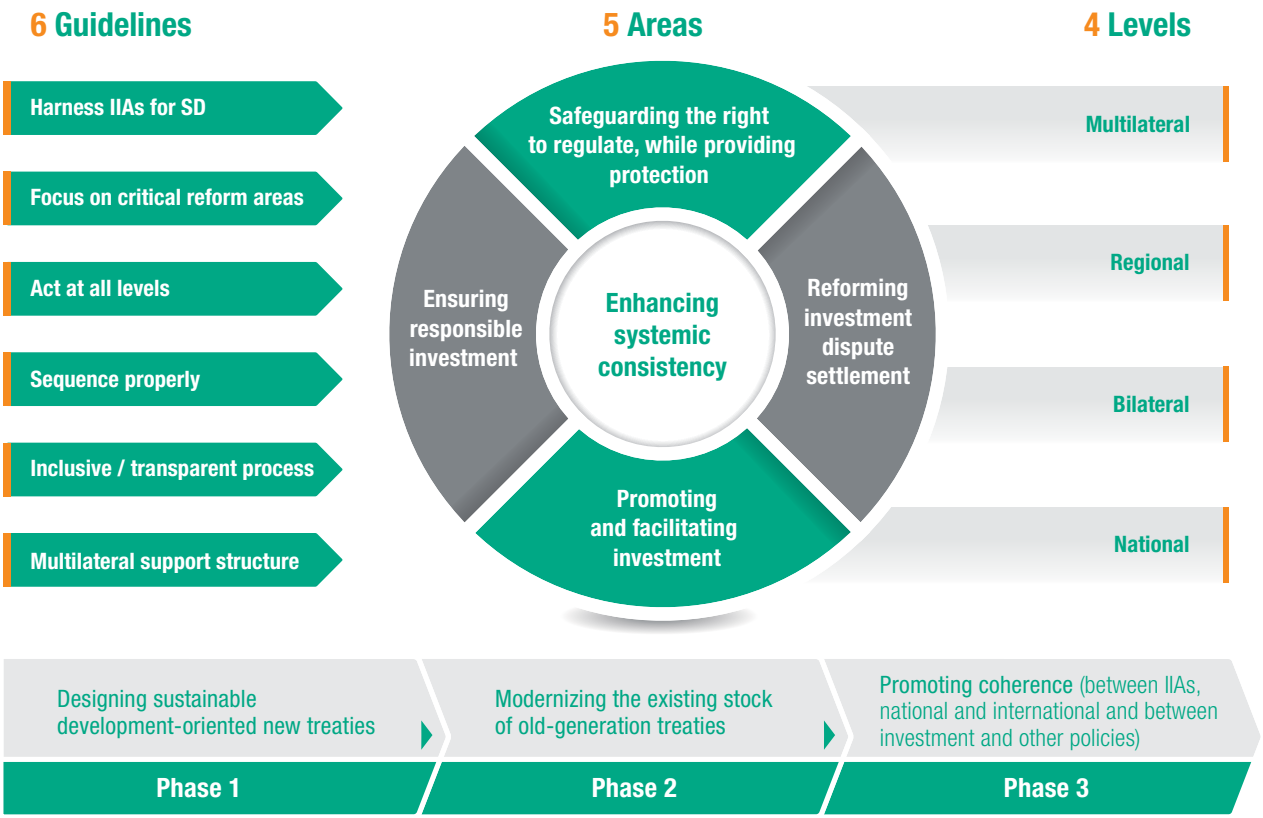
Although the term "phase" suggests a temporal element in the sense of successive reform actions, UNCTAD's "Phases of IIA Reform" refer to different conceptual stages that are inter-related and that countries should consider at the same time when planning IIA reform. The implementation of the reform steps may well be gradual and staged over time, and the substance of Phase 1 of IIA Reform, notably the policy options for the five priority areas of reform, is equally relevant for Phases 2 and 3. In other words, "Phase 1 options" inform policy makers' decisions on whether and how to modernize existing old-generation IIAs and whether and how to improve coherence, consistency and interaction between different levels and types of policymaking.

Successfully reforming IIA rule-making is not an easy task. Design criteria can help in this challenge. The UNCTAD Reform Package offers six Guidelines for IIA Reform: (i) harness IIAs for sustainable development; (ii) focus on critical reform areas; (iii) act at all levels; (iv) sequence properly for concrete solutions; (v) ensure an inclusive and transparent reform process; and (vi) strengthen the multilateral supportive structure (figure 1).

Comprehensive reform requires synchronizing reform actions at four levels of policymaking: at the national, bilateral, regional and multilateral levels. In each case, the reform process includes: (i) taking stock and identifying the problems; (ii) developing a strategic approach and an action plan for reform; and (iii) implementing actions and achieving the outcomes.

Determining which policy options are right for a country in a particular situation requires a careful and facts-based cost-benefit analysis, while also addressing a number of broader challenges. Strategic challenges include preventing "overshooting" of reform, depriving the IIA regime of its purpose of protecting and promoting investment. Systemic challenges arise from gaps, overlaps and fragmentation that create coherence and

Figure 1. UNCTAD's Road Map for IIA Reform



Source: ©UNCTAD.

consistency problems. Coordination challenges require prioritizing reform actions, finding the right treaty partners to implement them and ensuring coherence between reform efforts at different levels of policymaking. Capacity challenges make it hard for smaller countries, particularly least developed countries (LDCs), to address the deficiencies of first-generation IIAs and enhance overall policy coherence.

Comprehensive regime reform would benefit from intensified multilateral backstopping. UNCTAD, through its three pillars of work – research and policy analysis and advocacy, technical assistance and intergovernmental consensus-building – can play a key role, as the United Nations' focal point for international investment and development and the international forum for high-level and inclusive discussions on today's multilayered and multifaceted IIA regime.

INTRODUCTION

Growing concerns with the functioning of the IIA regime, together with the evolution of the global investment landscape and the sustainable development imperative, have in recent years triggered a move toward reforming international investment rule-making. As a result, the IIA regime has been going through a period of reflection, review and reform.

As evident from discussions at UNCTAD's World Investment Forums (WIF), from the heated public debate taking place in many countries and from various parliamentary hearing processes, including at the regional level, a shared view has emerged on the need for reform of the IIA regime to ensure that it works for all stakeholders. The question is not about whether to reform, but about the *what* and the *how* of such reform.

UNCTAD, as the United Nations' focal point for investment and development, has been setting and backstopping the agenda for sustainable development-oriented IIA reform at the global level through its three pillars of activities: offering analytical resources, such as the IIA and ISDS navigators (databases) and developing policy toolkits; facilitating a network and providing an international platform for consensus-building; and delivering technical assistance and advisory services.

Based on its stock of research and monitoring of investment policy developments, UNCTAD's *WIR15* responded to the reform challenge with a Road Map for IIA Reform. The Road Map was built upon UNCTAD's earlier work in this area, including UNCTAD's Investment Policy Framework for Sustainable Development (Investment Policy Framework) (*WIR12*) (figure 2), UNCTAD's reform paths for investment dispute settlement (*WIR13*) and its reform paths for IIA reform (*WIR14*), as well as on contributions by others.

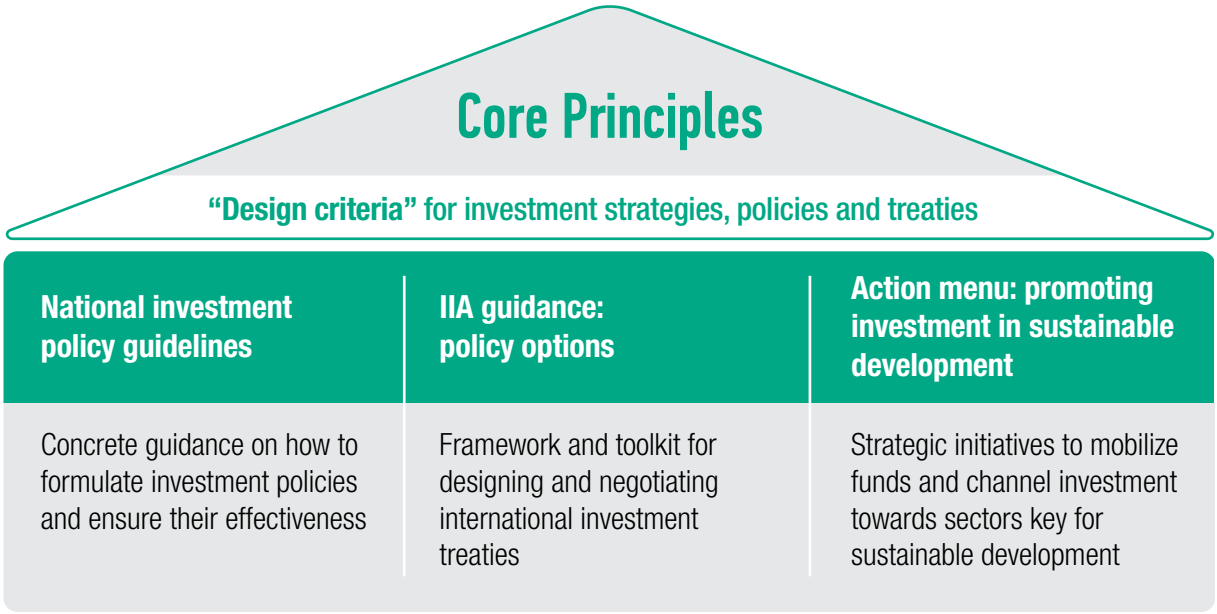
The Road Map addressed five main reform challenges (safeguarding the right to regulate for pursuing sustainable development objectives, reforming investment dispute settlement, promoting and facilitating investment, ensuring responsible investment, and enhancing systemic consistency). Among others, it offered policy options for key areas of IIA reform (i.e. substantive IIA clauses, investment dispute settlement and systemic issues).

WIR17 took stock of reform efforts in international investment policies, investment treaties and investment dispute settlement. It noted that the modernization of treaties was well underway, in particular through the inclusion of more sustainable development-oriented provisions in new treaties, with most of them following the options included in UNCTAD's policy tools.

However, while reform efforts were taking hold in new treaties, the large stock of old-generation treaties was lagging behind and becoming an increasing source of friction in the process of modernization of the investment regime. Consequently, the report called for Phase 2 of IIA Reform, tackling the stock of existing treaties. Building on the Road Map for IIA Reform from 2015, *WIR17* provided 10 concrete options for reform mechanisms.

The World Investment Report 2018 (*WIR18*) emphasized that alongside improving the approach to new treaties and modernizing existing treaties, countries needed to ensure coherence of their IIAs with each other, but also with national investment policies and

Figure 2. UNCTAD's Investment Policy Framework for Sustainable Development



Source: ©UNCTAD 2015.

with other bodies of international law (Phase 3 of IIA Reform). While reforming the IIA network through Phase 1 and 2 efforts, existing differences between treaties with different countries could become obstacles in the reform process. Also, many countries (especially developing ones) have national legal frameworks for investment that may contain provisions overlapping in scope with IIAs.

WIR18 concluded that strengthening cooperation between national and international investment policymakers, improving interaction and ensuring cross-fertilization between the national and international regimes (including by identifying lessons learned that can be transferred from one policy regime to the other) were crucial tasks for countries striving to create a mutually supporting, sustainable development-oriented investment policy regime. *WIR18* also offered policy guidance on avoiding conflict and maximizing synergies between IIAs and other bodies of international law affecting investment, notably through clearer treaty drafting, exceptions in IIAs and guidance on interpretation of IIA provisions.

The updated Reform Package (2018) presents a consolidated version of UNCTAD's research and policy guidance on IIA reform derived from these publications.

This report takes a holistic approach. It covers, in a single package, all the key aspects of IIA reform (i.e. substantive, procedural and systemic). It identifies reform areas and objectives and provides policy makers with flexible options to adapt and adopt. The options can be combined into individual countries' reform packages that respond to their specific needs and prerogatives.

UNCTAD's Reform Package stresses the importance of a collective approach to IIA reform. Given the large number of existing IIAs, the only way to make the IIA regime work for all is to collectively reform its components. In today's dynamic environment, where one change reverberates throughout the whole system, it is important to work toward a common vision.

By facilitating a network and providing a platform for a multi-stakeholder and inclusive global policy debate, UNCTAD helps build consensus on investment for sustainable development. Several high-level IIA Conferences, including those held at UNCTAD's WIFs, have reviewed and shaped UNCTAD's policy tools on IIA reform. They have also documented their worldwide use and implementation: over 150 countries have undertaken at least one UNCTAD action in their national or international investment policymaking in the pursuit of sustainable development-oriented IIAs.

Through its support to sustainable development-oriented IIA reform, UNCTAD responds to its mandates received from the United Nations Financing for Development Conference, enshrined in the Addis Ababa Action Agenda (July 2015) and to its institutional mandates, in particular from UNCTAD's Ministerial Conferences. As the United Nations' focal point for investment and development, UNCTAD brings coordination and coherence to reform efforts.

Ultimately, only a collective approach can ensure that reform does not lead to further fragmentation and incoherence, but is for the benefit of all. And only a collective approach will deliver an IIA regime in which stability, clarity and predictability help achieve the objectives of all stakeholders, namely effectively harnessing international investment relations for the pursuit of sustainable development for all.

I. IIA REFORM: RATIONALE AND STRATEGIC CONSIDERATIONS

A. IIAs in a changing context

International investment agreements (IIAs) – like most other treaties – are a product of the time when they are negotiated.

IIAs are concluded in a specific historic, economic and social context and respond to the then existing needs and challenges. As more than half a century has passed since the first bilateral investment treaty (BIT) was concluded, it is no surprise that IIAs have gone through a significant evolutionary process during this period. Today, they face a new context and new challenges. Four main phases can be identified (figure 3).

As recognized in UNCTAD's Investment Policy Framework, the reorientation in IIA rule-making responds to a new context for investment policymaking, nationally and internationally.

Figure 3. Evolution of the IIA regime

1950s–1964 Era of Infancy	1965–1989 Era of Dichotomy	1990–2007 Era of Proliferation	2008–today Era of Re-orientation
New IIAs: 37 **Total IIAs: 37** **New ISDS cases: 0** **Total ISDS cases: 0**	**New IIAs: 367** **Total IIAs: 404** **New ISDS cases: 1** **Total ISDS cases: 1**	**New IIAs: 2,663** **Total IIAs: 3,067** **New ISDS cases: 291** **Total ISDS cases: 292**	**New IIAs: 410** **Total IIAs: 3,271** **New ISDS cases: 316** **Total ISDS cases: 608**
• Emergence of IIAs (weak protection, no ISDS)	• Enhanced protection and ISDS in IIAs • Codes of conduct for investors	• Proliferation of IIAs • Liberalization components • Expansion of ISDS	• Shift from BITs to regional IIAs • Decline in annual IIAs • Exit and revision
GATT (1947) Draft Havana Charter (1948) Treaty establishing the European Economic Community (1957) New York Convention (1958) First BIT between Germany and Pakistan (1959) OECD Liberalization Codes (1961) UN Resolution on Permanent Sovereignty over Natural Resources (1962)	ICSID (1965) UNCITRAL (1966) First BIT with ISDS between Netherlands and Indonesia (1968) Draft UN Code of Conduct on TNCs (1973–1993) UN Declaration on the Establishment of a NIEO (1974) Draft UN Code of Conduct on Transfer of Technology (1974–1985) OECD Guidelines for MNEs (1976) MIGA Convention (1985)	World Bank Guidelines for treatment of FDI (1992) NAFTA (1992) APEC Investment Principles (1994) Energy Charter Treaty (1994) Draft OECD MAI (1995–1998) WTO (GATS, TRIMs, TRIPS) (1994) WTO Working Group on Trade and Investment (1996–2003)	EU Lisbon Treaty (2007) UN Guiding Principles on Business and Human Rights (2011) UNCTAD Investment Policy Framework (2012) UN Transparency Convention (2014)
Independence movements	**New International Economic Order (NIEO)**	**Economic liberalization and globalization**	**Development paradigm shift**

Underlying forces

Source: UNCTAD, *WIR15*.

Note: Years in parentheses relate to the adoption and/or signature of the instrument in question.

1. A new sustainable development paradigm

The conservation of natural resources, environmental protection and social well-being did not feature prominently on the international policy agenda some 50 years ago. Today, however, these objectives have become universally recognized guiding principles for all policymaking in developed and developing countries, including in investment policymaking (Hindelang et al., 2015). Accordingly, investment policies (and IIAs) can no longer be designed in isolation, but need to be harmonized with, and made conducive to, the broader goal of sustainable development. This is even more so, given the importance of international investment for achieving the Sustainable Development Goals (SDGs) as part of the post-2015 development agenda, and for living up to the commitments undertaken by countries at the third "Financing for Development" Conference in Addis Ababa.

As the global community's views on development have evolved, societies' expectations about the role of foreign investment have become more demanding. Today, it is no longer enough that investment creates jobs, contributes to economic growth or generates foreign exchange. Countries increasingly look for investment that is not harmful for the environment, which brings social benefits, promotes gender equality, and which helps them to move up the global value chain.

Moreover, concerns about the strength and conduct of individual foreign investors have brought foreign investment in general under closer domestic and international scrutiny. Investors are increasingly expected to do more than the minimum required by law. Increasingly, investment behaviour is assessed on whether it complies with international standards, such as the UN Guiding Principles on Business and Human Rights, the revised OECD Guidelines on Multinational Enterprises, and the FAO/World Bank/UNCTAD/IFID Principles on Responsible Agricultural Investment. In addition to standards developed by international organizations, investors are expected to develop their own corporate social responsibility (CSR) codes and to report on the actions they have taken in order to comply with them.

2. A new investor landscape

Developing countries and economies in transition nowadays attract more than half of global foreign direct investment (FDI) flows, and their importance as FDI recipients continues to increase. Emerging economies have not only become important hosts of FDI; they are increasingly large sources of investment themselves, with their share in world outflows exceeding one third. While these countries previously looked at IIAs mainly from a host-country perspective, they now also consider their interests as home countries to investment abroad.

3. The greater role of governments in the economy

Following the global financial crisis in 2008, governments have become less reticent about regulating and steering their economies. While private sector capital remains the chief engine of global economic growth and innovation, more and more governments are moving away from the deregulation approach to economic growth and development that has predominated since the 1990s. Industrial policies and industrial development strategies are proliferating in developing and developed countries alike (*WIR11*). These

strategies often contain elements of targeted investment promotion or restriction, increasing the importance of integrated and coherent development and investment policies.

Similarly, a stronger role for State regulation manifests itself with regard to sustainable development. As the goals and requirements of sustainable development have come to be widely accepted, new social and environmental regulations are being introduced and existing rules reinforced – all of which have implications for investment policy. The trend for policymakers to intervene more in the economy and to steer investment activity is visible in the overall increasing share of regulatory and restrictive policies in total investment policy measures over the last decade. This trend reflects, in part, a new realism about the economic and social costs of unregulated market forces but it has also given rise to concerns about investment protectionism.

B. Lessons learned from 60 years of IIA rule-making

IIA reform can build on lessons learned from 60 years of IIA rule-making.

Sixty years of IIA rule-making reveal a number of lessons on how IIAs work in practice and what can be learned for future IIA rule-making.

The expected key function of IIAs is to contribute to predictability, stability and transparency in investment relations, and to help to move investment disputes from the realm of State-to-State diplomatic action into the realm of law-based dispute settlement and adjudication. IIAs can help improve countries' regulatory and institutional frameworks, including by adding an international dimension to them and by promoting the rule of law and enhancing good governance. IIAs can reduce risks for foreign investors (i.e. act as an insurance policy) and, more generally, contribute to improving the investment climate. Through all of this, IIAs can help facilitate cross-border investment and become part of broader economic integration agendas, which, if managed properly, can help achieve sustainable development objectives. At the same time, experience has shown that IIAs "bite" (i.e. their protection provisions can and have been enforced by arbitral tribunals at sometimes huge costs to the State), and that – like any other international treaty – they limit the regulatory space of the contracting parties. As a result, concerns have been raised that these limits on regulatory space go too far, were not properly understood at the point of entry into IIAs or are inadequately balanced by safeguards for governments or by obligations on multinational enterprises (MNEs).

1. IIAs bite and may have unforeseen risks – take safeguards

IIAs are legally binding instruments and not "harmless" political declarations. As shown by the surge in ISDS cases during the last 15 years, they "bite". Broad and vague formulation of IIA provisions has allowed investors to challenge core domestic policy decisions, for instance in the area of environmental, energy and health policies. Whereas in the past, it was mostly developing countries that were exposed to investor claims, there are nowadays also more and more developed countries as defendants.

The language used in IIAs has generated unanticipated (and at times inconsistent) interpretations by arbitral tribunals, and has resulted in a lack of predictability as to what IIAs actually require from States. As a result, there is today a broadly shared view that

treaty provisions need to be clear and detailed, and drafted on the basis of a thorough legal analysis of their actual and potential implications.

Anticipating IIAs' effect on regulatory space is not straightforward. Although ISDS cases expose the constraints that IIAs can place on regulatory powers, there is no clear methodology for conducting regulatory impact assessments and for managing attendant risks. The IIA impact will depend on the actual drafting and design of the IIA and the capacity of national and subnational entities to effectively implement the treaty.

2. IIAs have limitations as an investment promotion and facilitation tool, but also underused potential

IIA rule-making needs to be informed by a proper cost-benefit analysis. However, determining the impact of IIAs on FDI flows is not a straightforward exercise. IIAs can help encourage cross-border investment flows by reducing political risks for foreign investors, liberalizing investment flows (depending upon the treaty's provisions) and, more generally, signalling a better investment climate to international investors, especially in countries with weak domestic investment frameworks and enforcement. However, IIAs are only one of many determinants of FDI decision-making, and their importance is contingent on other variables. IIAs cannot substitute for sound domestic policies and regulatory and institutional frameworks. IIAs alone cannot turn a weak domestic investment climate into a strong one, and, like other treaties, they cannot guarantee market outcomes in the form of inflows of foreign investment (UNCTAD, 2014a).

Yet, IIAs have underused potential as an instrument for sustainable development objectives. First, they can do more to promote and facilitate investment and channel it to sustainable development. Today, increasing the quantity of investment is not enough. What matters is its quality, i.e. the extent to which investment delivers concrete sustainable development benefits. In light of the financing gap for meeting the SDGs (developing countries face an annual gap of $2.5 trillion), investment needs to be channelled to specific SDG sectors (*WIR14*).

Second, IIAs can do more to enhance responsible investment. Although (foreign) investment can create positive conditions for improving peoples' lives, it can also carry the risk of negatively impacting on the environment, peoples' health and the enjoyment of their human rights. These effects can be aggravated due to domestic regulatory lacunae. It is important, therefore, that while IIAs continue to provide a firm basis for investment protection, they should also begin to address more directly investor responsibilities.

3. IIAs have wider implications for policy and systemic coherence and capacity-building

IIA negotiations are not only about investment policies per se, but also have implications for numerous other policy areas at all levels of policymaking within countries (national, subnational, municipal). Given their broad scope of application and the wide range of foreign investment operations, IIA disciplines interact with policies on trade, labour and social issues, taxation, intellectual property, land rights, sector-specific policies, national security issues, cultural policies, health and environmental protection, and many others. The far-reaching scope of these agreements and the obligations they create call for broad internal policy coordination – both at and within the national and subnational

levels – when developing a country's IIA negotiation strategy and in the negotiation process itself. Care needs to be taken to ensure coherence between IIA obligations and domestic policies, and to achieve consistency between IIAs and other international obligations of the IIA contracting parties.

Ensuring this degree of coordination can be a daunting challenge. The complexity of IIA negotiations and their likely impact on domestic policies calls for more capacity-building in developing countries, in particular least developed countries (LDCs). Without an in-depth knowledge of international investment law and pertinent arbitral decisions, countries risk concluding IIAs that do not properly reflect their interests and objectives. Moreover, without such coordination, countries risk entering into commitments that they cannot implement at either the national or subnational levels or that inadvertently (and unnecessarily) limit the pursuit of government policies. In addition, lack of capacity and negotiation skills also negatively affect countries' bargaining power.

C. Strategic considerations

When designing a future IIA regime that meets the challenges of the five priority areas for reform countries need to make a number of strategic choices, with a view to identifying reform areas, reform tools and best possible policy options for implementing reform.

These strategic choices include:

1. Whether or not to have IIAs

The first strategic choice is about whether "to have or not to have" an IIA. This requires a careful assessment of the pros and cons of such agreements (summarized in table 1). Countries may come to different conclusions, depending on their individual development strategies, their domestic investment policies, their role as a home or host country of investment, their prior experience with IIAs/ISDS and the way they conduct their international investment relations.

2. Whether to disengage from IIAs

Since most countries are – to varying degrees – already members of the global IIA regime, the question of having or not having IIAs is not only about concluding new treaties, but also about whether to maintain or terminate existing agreements. For some States, disengaging from existing IIAs may be appealing where IIA-related concerns feature particularly high in the domestic policy debate and where policymakers no longer consider IIAs to be an important element of their investment promotion strategies, both inward and outward.

Countries that consider this path need to keep in mind that treaty termination through denunciation is not permitted before the IIA has reached a certain "age", set by the duration provision of the treaty. In addition, denunciation does not immediately liberate contracting parties from their treaty obligations, since IIAs usually contain a "survival clause", protecting existing investment in the host country for a certain additional period, typically between 10 and 20 years. Finally, treaty denunciation that is undertaken without consulting the other contracting party risks negatively affecting foreign relations.

Table 1. Summary of arguments put forward in favour and against IIAs

Main arguments made in favour of IIAs	Main arguments made against IIAs
IIAs: • Contribute to a favourable investment climate. • Contribute to fostering and expanding economic and political cooperation between contracting parties. • Contribute to the stability and predictability of the policy framework, foster good governance and the rule of law. • Provide protection rights that are independent from host countries' domestic legislation (superiority of international law over national law). • Compared with customary international law, improve legal certainty as protection rights are specified by treaty. • Reduce political risks of investing abroad. • May facilitate the granting of investment guarantees by the home country. • Help to avoid politicization of investment disputes.	IIAs: • Do not guarantee additional investment inflows. • May negatively affect host countries' sovereign right to regulate in the public interest. • Expose host States to ISDS and associated financial risks. • Privilege foreign investors over domestic investors. • Only provide for investor rights, not obligations. • Reflect a negotiated outcome that is influenced by the bargaining power of the negotiating parties. • May result in overlapping and inconsistent IIA obligations of contracting parties. • Are difficult to amend in case of changing circumstances.

Source: UNCTAD, *WIR15*.

3. Whether to engage in IIA reform

The next strategic choice is whether or not to engage in IIA reform. Refraining from substantive changes to international investment policymaking sends an image of continuity and investor-friendliness. It may be particularly attractive for countries with a strong outward investment perspective and with no – or little – ISDS experiences. Not engaging in reform, however, comes with serious drawbacks in that it does not address any of the challenges arising from today's global IIA regime and keeps the country exposed to risks created by IIAs in their traditional form. Moreover, mounting pressure for reform from existing treaty partners and other constituencies in many countries will make it increasingly difficult to maintain the status quo.

4. How to reform IIAs

Should a country decide to embark on IIA reform, further strategic considerations come into play, relating to both substantive and procedural aspects. Pursuing IIA reform requires decisions on the sequencing of individual reform steps. Gradual, incremental reform steps may be easier to realize than a holistic approach. It may be advantageous to prioritize those areas for reform (e.g. certain IIA clauses or ISDS reform elements) where consensus among the respective actors is most likely to emerge.

The process of engaging in the above deliberations can be guided by a number of design criteria for investment policymaking. UNCTAD's Investment Policy Framework sets out 10 Core Principles for investment policymaking, which aim to guide policymaking at both the national and international levels (table 2). As such, the Framework's principles are also a useful guide for IIA reform.

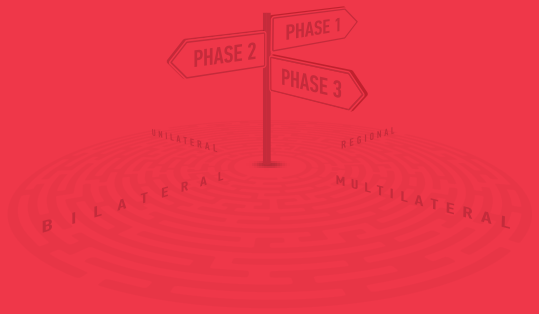
Overall, the response to these needs arising from new context, the lessons learned and the strategic considerations will depend on country-specific circumstances and preferences. Relevant factors include the kind of treaties that make up a country's IIA network, its individual experience with ISDS, the role it allocates to IIAs as part of its overall development strategy and the extent of IIA reform desired, including by its domestic stakeholders.

Table 2. Core Principles for investment policymaking

Area		Core Principles
Investment for sustainable development		• The **overarching objective** of investment policymaking is to promote investment for inclusive growth and sustainable development.
1	Policy coherence	• Investment policies should be grounded in a country's overall development strategy. All policies that impact on investment should be coherent and synergetic at both the national and international level.
2	Public governance and institutions	• Investment policies should be developed involving all stakeholders, and embedded in an institutional framework based on the rule of law that adheres to high standards of public governance and ensures predictable, efficient and transparent procedures for investors.
3	Dynamic policymaking	• Investment policies should be regularly reviewed for effectiveness and relevance and adapted to changing development dynamics.
4	Balanced rights and obligations	• Investment policies should be balanced in setting out rights and obligations of States and investors in the interest of development for all.
5	Right to regulate	• Each country has the sovereign right to establish entry and operational conditions for foreign investment, subject to international commitments, in the interest of the public good and to minimize potential negative effects.
6	Openness to investment	• In line with each country's development strategy, investment policy should establish open, stable and predictable entry conditions for investment.
7	Investment protection and treatment	• Investment policies should provide adequate protection to established investors. The treatment of established investors should be non-discriminatory in nature.
8	Investment promotion and facilitation	• Policies for investment promotion and facilitation should be aligned with sustainable development goals and designed to minimize the risk of harmful competition for investment.
9	Corporate governance and responsibility	• Investment policies should promote and facilitate the adoption of and compliance with best international practices of corporate social responsibility and good corporate governance.
10	International cooperation	• The international community should cooperate to address shared investment-for-development policy challenges, particularly in least developed countries. Collective efforts should also be made to avoid investment protectionism.

Source: UNCTAD, Investment Policy Framework for Sustainable Development 2015.

II. GENERAL GUIDELINES FOR IIA REFORM



A. Six Guidelines for IIA Reform

IIA reform should be guided by the goal of harnessing IIAs for sustainable development, focusing on key reform areas, and following a multilevel, systematic and inclusive approach.

Six Guidelines for IIA Reform guide any reform action, be it undertaken at the national, bilateral, regional or multilateral levels (table 3). Inspired by the UNCTAD Investment Policy Framework's Core Principles, the lessons learned from 60 years of IIA rule-making and the specific reform challenges of today, these six Guidelines aim at harnessing IIAs for sustainable development.

B. Five priority areas for reform

When placing the lessons learned from six decades of IIA rulemaking in this new context, five priority areas for reform emerge (figure 4).

1. Safeguarding the right to regulate

While IIAs contribute to a favourable investment climate, they inevitably place limits on contracting parties' sovereignty in domestic policymaking. Given the rising concerns that such limits go too far, especially if combined with effective enforcement, IIA reform needs

Table 3. Guidelines for IIA Reform

Description	
1. Harness IIAs for sustainable development	The ultimate objective of IIA reform is to ensure that the IIA regime is better geared towards sustainable development objectives while protecting and promoting investment.
2. Focus on critical reform areas	The key areas for reform are (i) safeguarding the right to regulate for public interest, (ii) reforming investment dispute settlement, (iii) strengthening the investment promotion and facilitation function of IIAs, (iv) ensuring investor responsibility, and (v) enhancing systemic coherence.
3. Act at all levels	The reform process should follow a multilevel approach and take place at the national, bilateral, regional, and multilateral levels, with appropriate and mutually supportive action at each level.
4. Sequence properly for concrete solutions	At each level, the reform process should follow a gradual, step-by-step approach, with appropriately sequenced and timed actions based on identifying the facts and problems, formulating a strategic plan, and working towards concrete outcomes that embody the reform effort.
5. Ensure an inclusive and transparent reform process	The reform process should be transparent and inclusive, allowing all stakeholders to voice their opinion and to propose contributions.
6. Strengthen the multilateral supportive structure	The reform process should be supported by universal and inclusive structures that help coordinate reform actions at different levels by offering backstopping, including through policy analysis, technical cooperation, and a platform for exchange of experiences and consensus-building.

Source: UNCTAD, *WIR15.*

to ensure that countries retain their right to regulate for pursuing public policy interests, including sustainable development objectives (e.g. for the protection of the environment, the furtherance of public health or other social objectives) (*WIR12*). Safeguarding the right to regulate may also be needed for implementing economic or financial policies (*WIR11*). At the same time, however, policymakers must be vigilant that providing the necessary policy space for governments to pursue bona fide public goods does not inadvertently provide legal cover for investment protectionism or unjustified discrimination.

2. Reforming investment dispute settlement

Originally modelled on the system of ad hoc confidential commercial arbitration between private parties, today, the ISDS system suffers from a legitimacy crisis. There are concerns that the current mechanism exposes host States to additional legal and financial risks, often unforeseen at the point of entering into the IIA and in circumstances beyond clear-cut infringements on private property, without necessarily bringing any benefits in terms of additional FDI flows; that it grants foreign investors more rights as regards dispute settlement than domestic investors; that it can create the risk of a "regulatory chill" on legitimate government policymaking; that it results in inconsistent arbitral awards; and that it is insufficient in terms of ensuring transparency, selecting independent arbitrators, and guaranteeing due process. IIA reform needs to address these concerns.

3. Promoting and facilitating investment

Promoting and facilitating investment is crucial for the post-2015 development agenda, with developing countries facing an annual SDG-financing gap of $2.5 trillion (*WIR14*). Thus far, however, the majority of existing IIAs does not include efficient investment promotion and facilitation provisions and reserve this issue for domestic policymaking. A third reform objective, therefore, is to expand the investment promotion and facilitation dimension of IIAs together with domestic policy tools and to target them towards foreign investment capable of promoting sustainable development.

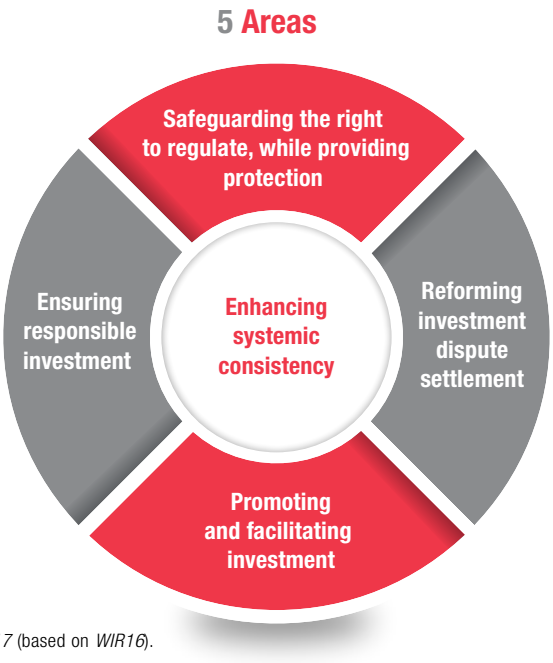
4. Ensuring responsible investment

Foreign investment can make positive contributions for development, but it can also negatively impact the environment, health, labour rights, human rights or other public interests (*WIR14*). Typically, IIAs set out few, if any, responsibilities on the part of investors in return for the protection that they receive. One objective of IIA reform therefore is ensuring responsible investor behaviour. This includes two dimensions: maximizing the positive contribution that investors can bring to societies ("doing good") and avoiding negative impacts ("doing no harm").

5. Enhancing systemic consistency

The atomised, multifaceted and multilayered nature of the IIA regime gives rise to gaps, overlaps and inconsistencies, between IIAs, between IIAs and other international law instruments affecting investment, but also between IIAs and domestic policies. IIA reform therefore should seek coherence in these various relationships. This is a reform objective that is relevant both in terms of content, the "what", but also in terms

Figure 4. UNCTAD's Road Map for IIA Reform: Five areas of reform



Source: UNCTAD, *WIR17* (based on *WIR16*).

of process, the "how" of IIA reform. Accordingly, it is here where the three phases of IIA reform interact, and at times overlap, most.

C. Four levels of reform actions

IIA reform actions should be synchronized at the national, bilateral, regional and multilateral levels. In the absence of a multilateral system, the best way to make the IIA regime work for sustainable development is to collectively reform the regime with a global support structure.

Actions for sustainable development-oriented IIA reform – including for Phases 2 and 3 of IIA Reform – can and should be undertaken at all levels: the national, bilateral, regional and multilateral levels (table 4). Certain reform actions are particularly useful at the national level (such as the development of a new model treaty), others at the bilateral (e.g. joint interpretation or amendment), regional (e.g. consolidation) or the multilateral level (e.g. referencing global standards).

At each level, the reform process would broadly follow a sequence of steps that include (i) taking stock and identifying the problems, (ii) developing a strategic approach and an action plan for reform, and (iii) implementing actions and achieving the desired outcomes.

The actions described below differ in their complexity, ease of implementation and impact. It is therefore important for each country to establish some sort of sequencing of reform actions, identifying actions for the near, medium and long-term future.

1. Actions at the national level

In its very nature, national-level reform action is unilateral. Accordingly, its potential to create actual change in terms of a new and more sustainable development-friendly IIA

Table 4. Road Map for IIA Reform

Level	Take stock/identify problem	Strategic approach/ action plan	Options for actions and outcomes

National	• National IIA review
	  • Treaty network and content profiles
	  • Impact and risk assessment
	  • Reform needs
		• National IIA action plan
		  • Design criteria and guidelines
		  • Reform areas and entry points
		  • Approaches for IIA reform
		  • Negotiating strategy
			• New model treaty
			• Unilateral termination
			• Implementation
			  • Domestic reform
			  • Increased awareness
			  • Improved institutions
			  • Capacity-building

Bilateral	• Joint IIA consultations to identify reform needs	• Plan for a joint course of action	• Joint interpretation • Renegotiation/amendment • Consensual termination

Regional	• Collective review
	  • Treaty network and content profiles (regional IIA and BIT network)
	  • Impact and risk assessment
	  • Reform needs
		• Collective IIA action plan
		  • Design criteria and guidelines
		  • Reform areas and entry points
		  • Approaches for IIA reform and for consolidating and streamlining the IIA network
			• Consolidation/rationalization of BIT networks
			• Common model
			• Joint interpretation
			• Renegotiation/amendment
			• Implementation/aid facility

Multilateral	• Global review of the IIA regime (e.g. *WIR15*)
	  • Stocktaking/lessons learned
	  • Identification of systemic risks and emerging issues
		• Multilateral consensus-building on key and emerging issues
		• Shared vision on systemic reform
			• Multilateral Action Plan
			  • Multilaterally agreed criteria and guidelines for systemic reform
			  • Developing instruments and/or institutions for facilitating reform at all levels
			• Multilateral backstopping
			  • Research and analysis
			  • Coordination, including "bridging" function with other bodies of law
			  • Technical assistance
			  • Platform/forum for consensus-building and exchange of best practices

Source: UNCTAD, *WIR15*.

regime is limited. However, national-level action is crucial for preparing proper IIA reform actions at the other (i.e. bilateral, regional and multilateral) levels, and it constitutes the very first step to harness the potential of IIAs for the sustainable development of a country.

National IIA reform needs to be accompanied by domestic reform efforts geared towards improving the regulatory framework for investment.

In other words, IIA reform needs to be accompanied by action regarding those issues that IIAs are supposed to address, by overcoming deficiencies and providing guarantees

and "insurance". This is important not only for avoiding the potential negative effects of IIA reform in terms of creating transaction costs, but also for further fine-tuning the role of IIAs in a country's development strategy. Indeed, one of the arguments for IIA reform is that the domestic regulatory regime of many countries has evolved to such a degree that classical "protection-focused" IIAs are no longer adequate instruments for harnessing investment for sustainable development.

All national-level reform actions would benefit from involving all stakeholders, including through interministerial consultations, parliamentary engagement and inputs from academia, civil society and business.

(i) IIA review

The first step for national-level IIA reform is an IIA review. Such a review takes stock of the country's network of IIAs, assesses the impact and risks flowing from these agreements and identifies concrete reform needs.

More specifically, this includes analysing a country's IIA profile, i.e. reviewing the country's existing IIAs in terms of partners, coverage, types and content. A subsequent impact and risk assessment looks at the IIAs' economic and policy impacts. This includes analysing their impact on investment flows and other economic indicators (e.g. trade flows, royalties and license payments flows, tax) and their interrelationship with other policies (e.g. overlaps, inconsistencies with national investment and other policies, with other international obligations). Such an assessment would also look at the problems the agreements have caused and the risks they give rise to, for example, through ISDS cases (whether withdrawn, settled or decided in favour of the State or the investor). Putting these findings into the context of the country's socioeconomic and political realities (as stipulated in its national development strategy and by today's SDG imperative) enables policymakers to draw lessons learned and to identify concrete reform needs. Although such a risk assessment can never be comprehensive, even if undertaken in a rudimentary manner or in a sector-specific manner, it can offer important insights.

(ii) National IIA action plan

The next step is the development of a national IIA action plan. Informed by a number of design criteria and guidelines (e.g. as outlined in UNCTAD's Investment Policy Framework) and the results of the national IIA review, the country can develop its strategic approach towards IIA reform. Regarding the extent of reform, the country decides whether to comprehensively address all five reform objectives or to single out one or two, such as safeguarding the right to regulate and improving investment dispute settlement. This choice informs the selection of reform areas and entry points to focus on and the policy options best suited for doing so. This last step benefits from comprehensive information about international and/or regional best practice (and state-of-the-art treaty practice). The policy options in UNCTAD's Investment Policy Framework as well as those in this reform package serve as examples.

Another key element of the national IIA action plan is the development of a negotiating strategy. Such a strategy sets out the concrete action steps for reforming the different IIA relationships the country maintains. This includes prioritizing certain relationships and setting timelines within which they will be addressed. IIA relationships to be prioritized include those IIAs that have reached the end of their initial duration, those with which

major problems have occurred and those that can be rationalized (in the context of regional endeavours).

Determining the best way of reforming these relationships is also important. The country needs to decide whether certain IIA relationships should be terminated, renegotiated or amended, all of this with concrete timelines, according to which the country approaches its IIA reform agenda with its preferred treaty partners. Finally, also joint interpretation or the negotiation of new IIAs are options to be considered.

(iii) New IIA model

In terms of concrete outcomes of national-level IIA reform, this includes first and foremost a new IIA model. The new model will be based on the respective strategic choices (e.g. the extent of reform), selection of reform objectives and areas, and respective policy options. A new model IIA can imply either partial amendments or a complete overhaul of the pre-existing model. By now, at least 50 countries and 4 regional integration organizations have embarked on developing a new model IIA. A new model can be accompanied by decisions on which of the new model's elements are priority objectives to be pursued and what fallback options exist if needed.

(iv) Treaty termination

Another set of concrete outcomes of national-level IIA reform action are unilateral actions, such as terminating or abandoning a treaty (see also below chapter IV.D., 10 options). Regarding the latter, rules for treaty termination are typically set out in the BIT itself. By the end of 2016, over 1,000 BITs had reached a stage where they could be unilaterally terminated by one contracting party immediately; many more are becoming available for such termination in the coming years. Countries wishing to terminate their IIAs need to have a clear understanding of the relevant treaty provisions (especially the survival clause) as well as the broader implications of such actions (UNCTAD, 2013c; *WIR11*; *WIR17*).

(v) Addressing bottlenecks for domestic IIA implementation and IIA reform

As a third element of the national IIA Action Plan, countries should identify their domestic IIA-implementation and IIA-reform bottlenecks. This could include at least four steps of government action. First, treaty implementation may require administrative actions to fully translate international obligations into national laws and administrative practices. Overall, IIA reform should go hand in hand with domestic regulatory adjustments to ensure coherence and create synergies (see also below chapter V, Phase 3 of IIA Reform). Second, the country may wish to create awareness at all levels of government concerning the countries' international IIA-related obligations (even in the absence of disputes). Information campaigns and active training of local officials directly dealing with foreign investors are examples in point. Third, there may be a need to build the necessary institutions to deal with IIA-related implementation issues. This step could range from establishing early-warning systems or ombuds-like institutional set-ups that are geared towards dispute prevention, to creating dedicated "defence" teams in the ministry charged with dispute settlement, and/or to follow through on the direct institutional commitments in IIAs, e.g. the establishment of joint committees. Finally, in all of this work, governments could identify their technical assistance and capacity-building needs

and take actions on their follow-up, through bilateral, regional or multilateral assistance programmes (such as UNCTAD's IIA work, its Investment Policy Reviews or e-governance programmes). The latter is particularly important for least developed countries and for other small and vulnerable economies.

2. Actions at the bilateral level

Bilateral reform action largely mirrors and builds on national-level actions. Bilateral action will usually create actual change in the legal instruments covering the pertinent bilateral relationship.

A joint IIA review aims at taking stock of the situation and at assessing the impact and the risks of the bilateral IIA relationship and at identifying reform needs. This time, the review is undertaken jointly, involving the respective actors from the two countries. Such a review can take the form of consultations, possibly making use of joint review committees and may be in the context of already existing joint economic committees or through a new, institutional set-up, whether ad hoc or permanent. Stakeholder involvement can help to inform the process.

Based on the review, the two countries would proceed to develop a plan for a joint course of action. Such a plan can include options such as the ones provided in the "10 Options for Phase 2 of IIA Reform", notably for instance joint interpretative statements (in the form of memoranda of understanding) on an existing treaty (UNCTAD, 2011c); amendments to or renegotiation of an existing treaty; or the consensual termination of the treaty either upon treaty expiration or if the treaty is superseded by a regional initiative to which both parties are members.

3. Actions at the regional level

Regional reform action follows similar steps as national and bilateral actions, but with additional layers of complexity and greater potential for change.

In terms of greater complexity, regional IIA rule-making implies overlaps and inconsistencies, particularly given the current practice in which new regional agreements do not provide for the phasing-out of older agreements covering the underlying respective bilateral relationships. At the same time, regional IIA reform provides an opportunity for more efficient and widespread reform as it involves more than two countries, and, if undertaken properly, would harmonize and consolidate existing investment rules. Moreover, regional endeavours may be subject to a different kind of dynamism than bilateral relationships in terms of setting a reform agenda and pursuing it. Regional integration organizations and their secretariats offer the platforms on which regional IIA reform could be pursued.

Again, the first step is an IIA review, this time undertaken collectively by the members of the regional organization/agreement and in a multi-dimensional manner. Similar to the above, such a review would look into the network and content profiles, assess impacts and risks and identify reform needs, including through stakeholder consultations. In doing so, a collective regional review would consider the different treaty layers and relationships that exist in a regional context. This would be, first and foremost, the regional agreement in question. Second, this would include the existing BITs among the partners to the regional undertaking (i.e. intraregional BITs with the other partners in the

regional undertaking). Third, this would include IIAs with third parties, be they between a single member of the regional undertaking and a third, external treaty partner, or between the regional undertaking as such and a third, external treaty partner. When identifying impact and risk, attention would need to be given to the multilayered character of this IIA network, including the overlaps, gaps and inconsistencies, and the attendant risks arising from it.

This special nature of the regional dimension would inform the collective IIA action plan. For example, when defining reform objectives, the fifth one – promoting systemic consistency – would deserve particular attention, not only in terms of substance of the rules, but also in terms of managing the relationship between them. Collective approaches regarding areas for IIA reform and for consolidation and streamlining of IIAs would be particularly important.

Collective approaches will translate into specific, time-bound actions and outcomes. In terms of actions, they range from further discussions and consultations to negotiations, amendments/renegotiations or interpretation of treaties. When it comes to addressing existing treaties, underlying BITs that have reached their expiration dates could be the first to be tackled; however, also other regional undertakings that have long not been updated or modernized are candidates for IIA reform, including, if possible, by consolidating underlying BITs with a regional IIA or managing the relationships of co-existing, overlapping IIAs (see below chapter IV.D., 10 options, Consolidating the IIA network and Managing relationships).

In terms of specific results, regional reform efforts could result in a new, common IIA model or a negotiating position for future treaties; a joint interpretation; a renegotiated/amended treaty; or the consolidation/streamlining of underlying BITs. Again, the renegotiated treaties can be the regional treaty at issue or a treaty between the region and third parties. A renegotiated regional treaty can also result in the termination of the underlying bilateral treaties. With this latter outcome, regional IIA reform action can directly support the broader IIA reform effort of streamlining and rationalizing the global IIA regime.

Similar to national-level reform action, regional IIA reform may require regulatory adjustments at the national level to ensure coherence and create synergies. This could be aided by creating new – or improving existing – regional facilities to provide coordination and technical cooperation. The latter could include legal aid and/or training for dispute management and/or prevention, help with translating regional obligations into national laws and administrative practices, follow-through on direct treaty commitments for regionally institutionalized investment promotion and facilitation, and, more broadly, assistance with the implementation of IIA reform at the regional and/or national level (e.g. assistance for conducting a national risk assessment or the implementation of identified reform action, such as the termination or renegotiation of an existing agreement). Regional technical assistance and capacity-building bodies could serve as counterparts to, and benefit from, international organizations providing such support.

4. Actions at the multilateral level

Reforming an IIA regime consisting of thousands of agreements is a global challenge that calls for common responses from all parties involved. Such a global, i.e. multilateral

reform effort, if successful, would be the most efficient way of addressing the sustainable development challenges, inconsistencies and overlaps that characterize the current IIA regime. At the same time, multilateral IIA reform is the most challenging reform option, particularly regarding how to pursue it.

Several types of multilateral IIA reform action, with increasing intensity and different character, can be identified. Multilateral guidance for the interpretation of IIA provisions, for example, could improve the transparency, predictability and stability of international investment law and help clarify the substance of key provisions, including their sustainable development dimension. Similarly, multilaterally agreed guidelines for investment policymaking could ensure a coherent, holistic and synergetic approach to IIA reform.

Some types of multilateral IIA reform action are being pursued already. Examples include the G20 Guiding Principles on Global Investment Policymaking, the Mauritius Convention, discussions on the establishment of a multilateral investment court or work to amend the ICSID Rules.

The 2018 edition of UNCTAD's Reform Package addresses multilateral IIA reform as part of "Phase 2 of IIA Reform". Chapter IV.D.7 sets out the pros and cons of multilateral engagement on IIA reform and takes stock of reform actions undertaken so far. Since this is a conclusion related to several reform-actions described in the chapter

IIA reform can take place at various levels of engagement – unilateral, bilateral, regional or multilateral – and countries can select processes and formats in line with their development strategies and needs as well as their strategic choices about the priority, intensity, depth and character of their engagement in IIA reform. Moreover, the various paths identified are not mutually exclusive. There is also room for cross-fertilization between different reform paths. However, ultimately, collective action is required to ensure that IIA reform is for the benefit of all.

D. Three phases of IIA Reform

UNCTAD's IIA reform is divided into three phases. Although the term "phase" suggests a temporal element in the sense of successive reform actions, UNCTAD's Phases of IIA Reform refer to different conceptual stages that are inter-related and that countries should consider at the same time when planning IIA reform.

In doing so, policy makers may wish to note that i) the implementation of the reform steps may well be gradual and staged over time; and ii) the substance of Phase 1 of IIA Reform, notably the policy options for the five priority areas of reform, is equally relevant for Phases 2 and 3. In other words, Phase 1 options inform policy makers' decisions on whether and how to modernize existing old-generation IIAs and whether and how to improve coherence, consistency and interaction between different levels and types of policymaking.

Phase 1 of IIA Reform involves making strategic choices on the extent and depth of the reform agenda, and choosing policy approaches for key areas, including substantive IIA clauses, investment dispute settlement and systemic issues. Implementation may involve, in particular, a country's reviewing its network of IIAs, preparing an action plan for the reform, revising its IIA model and starting to negotiate new, more sustainable development-friendly treaties.

Phase 2 of IIA Reform involves addressing the problems and risks posed by the large stock of existing, old-generation treaties. UNCTAD provides 10 concrete options that may be used at this phase of the reform.

Finally, Phase 3 of IIA Reform focuses on improving coherence, consistency and interaction between different levels and types of policymaking. This includes, in particular, the coherence of a country's IIA network, the IIA interaction with national investment laws as well as the interaction between IIAs and other bodies of international law affecting investment. The aim of this phase is to prevent conflict and maximize synergies.

The next chapter offers numerous policy options for the key IIA clauses. It discusses how the options contribute to reaching the five reform objectives and their respective pros and cons. The discussion is further supported by visuals, listing the particular reform options. It also offers selected treaty examples. Further drafting language can be found at the IIA Mapping Project on UNCTAD's Investment Policy Hub (http://investmentpolicyhub.unctad.org/IIA) and in the APEC-UNCTAD Handbook for IIA Negotiators (APEC and UNCTAD, 2012).

To a large extent, the reform options reflect the respective policy options for IIAs contained in UNCTAD's Investment Policy Framework for Sustainable Development. This Reform Package takes a different approach and includes only those options that contribute to IIA reform by addressing the above-mentioned five priority areas. It focuses on the most pressing issues (e.g. MFN, FET, indirect expropriation, investment dispute settlement) in more detail. Some of the options for individual IIA clauses are alternatives, others can be used together. All of this has to be seen in light of innovative, reform-oriented treaty drafting as showcased in recent IIAs (*WIR17* and *WIR18*).

III. PHASE 1 OF IIA REFORM: MOVING TO A NEW GENERATION OF IIAs

UNCTAD's REFORM PACKAGE
FOR THE
INTERNATIONAL INVESTMENT REGIME

A. Safeguarding the right to regulate

Options include clarifying or circumscribing provisions such as most-favoured-nation (MFN) treatment, fair and equitable treatment (FET) and indirect expropriation, as well as including exceptions, e.g. for public policies or national security, and other IIA provisions.

The right to regulate in the public interest is addressed in IIAs mainly through provisions related to the standard of treatment that the treaty affords to foreign investors. Among the provisions particularly implicated in delineating the balance between investment protection and the right to regulation in the public interest are MFN clauses, the FET standard, expropriation provisions and provisions on safeguards and exceptions, which may be either built into particular substantive standards of protection or drafted as generally applicable clauses. These issues are at the heart of the IIA reform debate and will be dealt with in detail in this section. Other IIA provisions (ranging from the preamble, to the scope and definition clauses, national treatment, the umbrella clause and provisions related to remedies and compensation) also have a bearing on the right to regulate; they are equally important for States to consider, but they figure less prominently in the reform discussion. They are therefore covered in a more abbreviated manner in the second part of this section. A number of other IIA provisions that can have an impact on the right to regulate (e.g. performance requirements or pre-establishment treatment) are not covered in this Reform Package.

1. Standards of treatment

(i) MFN

The MFN clause is a crucial provision for IIA reform. Failure to take appropriate action with respect to the MFN clause can undermine improved formulations of treaty provisions.

MFN clauses, routinely included in traditional IIAs, aim to prevent less favourable treatment of investors from the signatory State vis-à-vis comparable investors from any third country (i.e. nationality-based discrimination). The MFN principle thereby aims to ensure a level-playing field between investors of different foreign nationalities (UNCTAD, 2010b).

In actual ISDS practice, investors have relatively infrequently alleged that they have been discriminated against by virtue of the host States' more favourable application of domestic measures to investors of third states. Instead, investors have most often invoked the MFN clause to access more "investor-friendly" provisions in IIAs concluded by the host State with third countries.

In particular, investors have relied on the MFN clause to avoid dispute resolution requirements imposed by the applicable IIA (e.g. a set period of time for which they must pursue local remedies before turning to international arbitration). Several tribunals have deemed this circumvention possible in cases involving broadly drafted MFN clauses in which the claimant has been able to point to an IIA signed by the host State in which such pre-arbitration requirements were absent. In other cases, investors have invoked the MFN clause to benefit from higher protection standards than the ones found in the base treaty ("base treaty" is the treaty pursuant to which the claim is brought). For example, in situations in which an IIA with a third country has contained additional

investor protections or more favourable formulations, as compared to the base treaty, a number of tribunals have decided that it is possible for the investor to take advantage of these more favourable provisions to "replace" or "add to" the provisions in the base treaty.

Application of MFN clauses in this way can result in investors "cherry-picking" the most advantageous clauses from different treaties concluded by the host State, thereby potentially undermining individual treaty bargains and sidelining the base treaty. For example, treaty commitments may clash, or hard-won concessions in a negotiation (e.g. on flexibility in performance requirements) may be undone through the application of a broadly worded MFN clause, as interpreted by arbitral tribunals. This concern is particularly heightened given countries' current efforts to reform their IIA regimes, which implies a refinement and rebalancing of treaty standards. Clearly, States will need and want to be careful that the desired effects of newly crafted treaty provisions are not obviated by the application of a broadly worded MFN clause.

There are a number of options to address these challenges (figure 5).

A first option is to specify that the MFN clause does not allow for the importation of substantive or ISDS-related elements contained in older treaties. This option ensures that a country's IIA reform efforts are not compromised by provisions contained in its stock of older treaties.

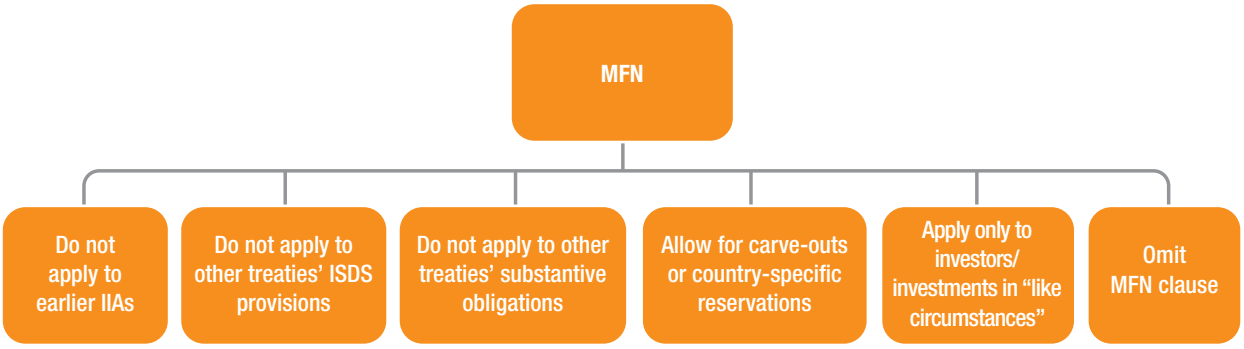
A second option is to specify that MFN treatment does not apply to ISDS provisions found in other IIAs, existing or future.

A third option is to specify that the MFN clause does not apply to substantive obligations undertaken in (existing or future) IIAs. Similarly, a treaty can clarify that substantive obligations in other IIAs do not in themselves constitute "treatment", absent measures adopted by a State pursuant to such obligations (e.g. Canada–EU CETA, 2016).

These three approaches support IIA reform and avoid the undoing of modernization efforts – however, they can raise concerns as to the diminution of the protective value of the agreement.

A fourth option is carving out from the MFN obligation certain sectors or industries or certain policy measures through a general carve-out (applicable to both parties) or through country-specific reservations. This option is particularly relevant for IIAs with a pre-establishment dimension.

Figure 5. Options for IIA reform: MFN



Source: UNCTAD, *WIR15.*

A fifth option, frequently undertaken in recent agreements, clarifies that the MFN obligation requires comparison of investors/investments that are "in like circumstances". Such a provision can go some way in safeguarding the right to regulate, but it can also raise questions about the specific criteria for comparison. Some recent treaties and models attempted to set out criteria for determining whether investors/investments are in "like circumstances" (Azerbaijan–Croatia BIT (2007)) (see also below national treatment).

A final option, followed by some countries, is to omit the MFN clause altogether. The Free Trade Agreement (FTA) between the EU and Singapore (2014), the FTA between India and Malaysia (2011), the ASEAN–Australia–New Zealand FTA (2009), the Japan–Singapore FTA (2002) and the SADC Model BIT (2012) are examples in point. Such an approach preserves a maximum of flexibility and can facilitate IIA reform. At the same time, omitting a standard that many consider to be one of the cornerstones of international economic law may raise concerns. In response, some have argued that in an IIA, the investment-enhancing effect of the MFN clause is less important as compared with other clauses and as compared with its presence in other international economic agreements (e.g. preferential trade agreements).

(ii) FET

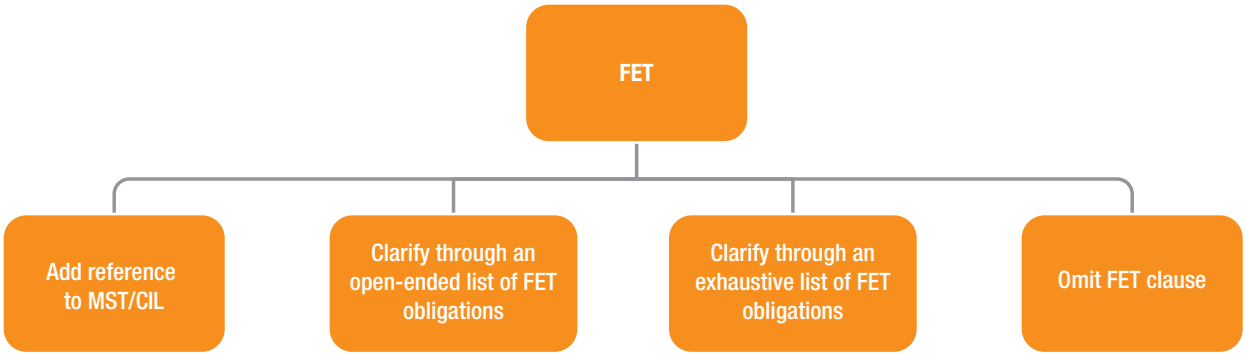
The FET standard is one of the IIA clauses that is at the core of today's debate on IIA reform. The standard is designed to protect foreign investors from government misconduct not captured by other standards of protection. It is also sometimes said that the FET standard may serve to foster good governance in host States. In actual practice, owing to its open-ended and largely undefined nature, the FET standard, especially as it has been drafted in traditional IIAs, has turned into an all-encompassing provision that investors have used to challenge any type of governmental conduct that they deem unfair. In fact, almost all ISDS cases to date have included an allegation of a FET breach.

There is a great deal of uncertainty concerning the precise meaning of the concept of FET, because the notions of "fairness" and "equity" do not connote a clear set of legal prescriptions and are open to subjective interpretations. Moreover, the relationship between FET and principles of customary international law, such as the international minimum standard of treatment, has raised significant issues of interpretation, especially where the IIA text contains no express link between FET and customary international law. As a result, the task of determining the meaning of the FET standard has been effectively left to ad hoc arbitral tribunals (UNCTAD, 2012a).

A particularly challenging issue that has arisen through arbitral practice relates to the use of the FET standard to protect investors' "legitimate expectations". Given the potentially far-reaching application of the concept of "legitimate expectations", there is a concern that the FET clause can restrict countries' ability to change investment-related policies or introduce new policies – including those for the public good – if they have a negative impact on individual foreign investors.

Traditional first-generation IIAs typically included an unqualified FET standard, which has given rise to some of the problems identified above. New-generation IIAs contain a number of more precise drafting options to choose from (figure 6).

Figure 6. Options for IIA reform: FET



Source: UNCTAD, *WIR15*.

A first option is to qualify the FET standard by reference to the minimum standard of treatment (MST) of aliens under customary international law (CIL). Depending on a particular tribunal's reading of MST/CIL, this approach may raise the threshold of State liability (e.g. the challenged conduct will need to be found to amount to egregious or outrageous mistreatment of foreign investors) and help to preserve States' ability to adapt their policies in light of changing objectives. However, the contours of MST/CIL are far from clear, and a reference to this concept could engender a new, significant uncertainty, for both States and investors. Moreover, in light of the arguments about the nature and development of CIL, not all countries may feel comfortable in referring to this concept.

A second option is to clarify the FET standard with an open-ended list of State obligations. The formulation may be "positive", specifying what the standard includes (e.g. the obligation not to deny justice in criminal, civil or administrative adjudicatory proceedings), or "negative", explaining what the standard does not include (e.g. establishing that the FET standard does not include a stabilization obligation that would prevent the host State from changing its legislation), or a combination thereof. This option has the advantage of clarifying the meaning of FET by indicating examples of what it covers and what it does not cover. One of its disadvantages is that the open-ended, indicative list of obligations, by its nature, leaves open the potential for expansion of the meaning of FET through subsequent arbitral interpretation.

A third option is to clarify or replace the general FET clause with an exhaustive, i.e. "closed" list of more specific obligations (e.g. a prohibition to deny justice or flagrantly violate due process, engage in manifestly abusive or arbitrary treatment). Although agreeing on such a list may be a challenging endeavour, its exhaustive nature would help minimize unanticipated and far-reaching interpretations by tribunals. As a further option, the contracting parties may wish to include a requirement for a periodic review of the list or the content of the FET obligation.

A final option that some countries have implemented in some of their IIAs is omitting the FET clause altogether (e.g. Bangladesh–Uzbekistan BIT (2000), Australia–Singapore FTA (2003)) or reducing it to a softer commitment; for example, by referring to FET in the preamble but not in the main treaty text (e.g. Turkey–United Arab Emirates BIT (2005) or Azerbaijan–Estonia BIT (2010)).[2] This approach reduces States' exposure to investor claims, but also reduces the protective value of the agreement.

(iii) Indirect expropriation

The expropriation provision is a key IIA element that mitigates an important risk faced by investors. Expropriation clauses do not take away States' right to expropriate property, but make the exercise of this right subject to certain conditions (UNCTAD, 2011a).[3] Expropriation provisions usually cover both "direct" and "indirect" forms of expropriation. "Indirect expropriation" covers acts, or series of acts, whose effects are "tantamount to" or "equivalent to" a direct, formal taking. These are acts that generally involve total or near-total deprivation of an investment or destruction of its value but without a formal transfer of title to the State or outright seizure.

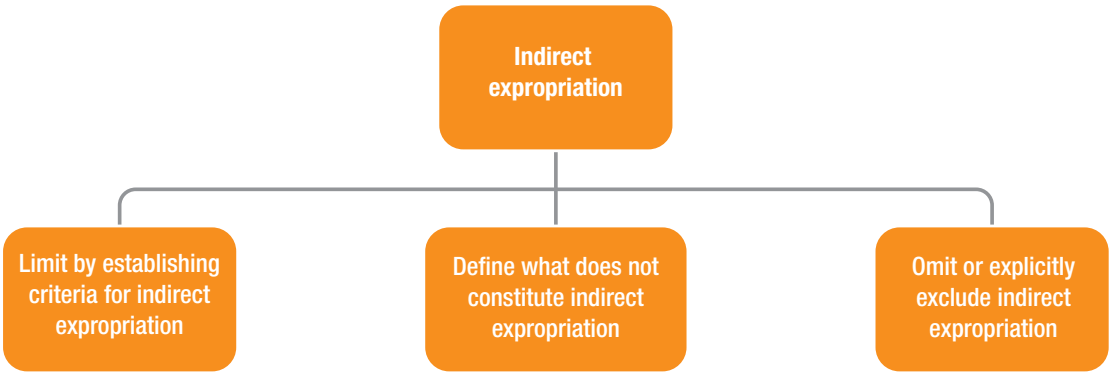
Investors have used provisions on indirect expropriation to challenge general non-discriminatory regulations that have had a negative effect on their investments (e.g. a ban or the imposition of restrictions on a certain economic activity on environmental or public health grounds). This raises the question of the proper borderline between expropriation (for which compensation must be paid) and legitimate public policymaking (for which no compensation is due).

Historically, IIAs have not contained any criteria for distinguishing between State action amounting to an indirect expropriation and State action of a general regulatory nature for which no compensation is due. More recent IIAs, however, typically set out a number of criteria and a few recent agreements go so far as to omit an explicit reference to indirect expropriation (e.g. Serbia–Morocco BIT (2013)). While the omission of a reference to indirect expropriation may serve to limit (or even eliminate) State exposure to liability for non-direct takings, it may also increase investors' perception of country risk and susceptibility to opportunistic regulatory behaviour.

There are a number of policy options in this regard (figure 7).

A first option is to limit the protection in case of indirect expropriation by establishing criteria that need to be met in order for an indirect expropriation to be found. This can include reference to (i) the economic impact of the government action; (ii) the extent of government interference with distinct, reasonable investment-backed expectations; or (iii) the character of the government action (e.g. whether it is discriminatory or disproportionate to the purpose of the measure under challenge). Another possible criterion is whether the measure(s) alleged to constitute an expropriation have produced a direct economic benefit for the State.

Figure 7. Options for IIA reform: Indirect expropriation



Source: UNCTAD, *WIR15.*

A second option is to define, in general terms, which measures do not constitute indirect expropriation. For example, it can be specified that "normal regulatory activities" (e.g. non-discriminatory, good faith regulations relating to public policy objectives) do not constitute indirect expropriation. Similarly, it can be clarified that a measure's adverse effect on the economic value of the investment is not enough to establish an indirect expropriation. A variant of this option is to clarify that certain specific measures (e.g. compulsory licensing in accordance with WTO rules) do not constitute indirect expropriation.

A third option is to omit a reference to indirect expropriation from the IIA or even explicitly exclude it from the treaty coverage. Depending upon drafting, the simple omission of a specific reference to "indirect" expropriation may not eliminate the possibility of liability for indirect expropriations: a bare reference to "expropriation" in an IIA may be interpreted as subsuming both direct and indirect expropriation in subsequent arbitral proceedings. In contrast, expressly excluding indirect expropriation from the coverage of an IIA may be perceived as considerably reducing the protective value of the IIA as it would leave investors unprotected from the types of indirect expropriation that are unrelated to States' regulatory conduct, such as "creeping" (through a series of damaging measures) or disguised (under a guise of lawful measures, e.g. tax enforcement) expropriation.

All of the above variations give guidance to arbitral tribunals that is presently lacking in most IIAs. None of these options exclude the risk of liability altogether (except perhaps for the express exclusion of protection for indirect expropriations), but rather allow for a better and clearer balancing of investor and State interests. In so doing, these options can help safeguard the right to regulate non-discriminatorily in the general public interest, while simultaneously providing greater legal certainty to investors with respect to the scope of IIA rights. Although explicit exclusion of protection for indirect expropriation is also an option that States can consider, such an option must be viewed as a rarity in contemporary State practice and may be perceived by investors as significantly lowering the protective value of the IIA. From the investors' perspective, such protection is particularly desirable in governance-weak economies where protection from measures of this nature under the domestic laws of the relevant host State may not be seen as reliable. In the absence of IIA protection for indirect expropriation, investors may seek investment insurance from private or public providers.

2. Safeguards

For the IIA elements below, the policy options are structured around a number of aspects, each requiring a choice between different options.

(i) Public policy exceptions

Investors may bring claims against public interest measures that have a negative effect on an investment's profitability. Whereas traditional IIAs typically do not contain express public policy exceptions, an increasing number of new treaties do include them. The formulation of such exceptions is often similar to the language found in the WTO's GATT Article XX and GATS Article XIV. These provisions aim at balancing investment protection with other public policy objectives and at reducing States' exposure to investor challenges of such measures. Public policy exceptions can also have an important signalling effect

towards the general public, indicating an agreement's compatibility with sustainable development and public policy considerations.

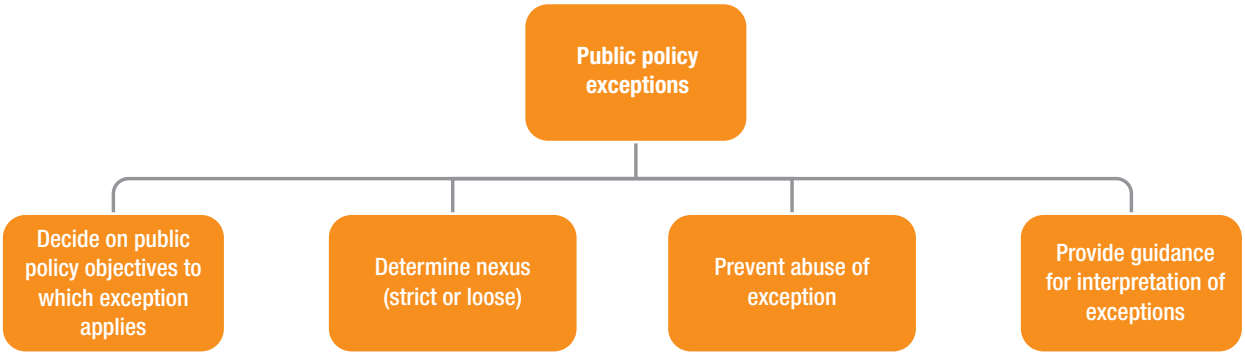
At the same time, the absence of express public policy exceptions does not mean that States cannot take public policy measures at all. Instead, such measures either may not be in conflict with IIA obligations in the first place or may be justified based on other principles of international law that inform the interpretation of IIA obligations. Nevertheless, including public policy exceptions expressly in an IIA increases legal certainty for host States: public policy exceptions explicitly allow for measures – which might otherwise be challengeable under the agreement – to be taken under specified circumstances. In so doing, they can have an important effect of increasing certainty and predictability about the scope of the IIA's obligations.

It should be noted that adding exceptions provisions raises questions about their relationship with some traditional investor protections, e.g. the provision on direct expropriation (if a direct expropriation corresponds to one of the objectives included in the exception clause, does this relieve the State of the duty to pay compensation?) or the FET standard (e.g. does the State's creation of protected legitimate expectations foreclose its later reliance on an exceptions clause?). Hence the relationship between an exceptions clause and each IIA obligation needs to be considered carefully. The Energy Charter Treaty's Article 24 on "Exceptions" for example, does not apply to the article on expropriation.

Assuming countries wish to include such exceptions into IIAs, they have a number of options at hand (figure 8), all with their pros and cons.

The first set of options relates to the type of situations that are covered. Countries can specifically list the public policy objectives to which they want the exception to apply (e.g. the protection of public health, public order and morals, the preservation of the environment). This list can be inspired from the relevant WTO (GATT and GATS) clauses but can also include other objectives, such as the provision of essential social services (e.g. health, education, water supply), the prevention of tax evasion, the protection of national treasures of artistic, historic or archaeological value (or "cultural heritage"), cultural or media diversity, or allow for the pursuit of broader objectives, such as the host countries' trade, financial and developmental needs. The exact content of such a list would depend on the negotiating partners' policy preferences.[4]

Figure 8. Options for IIA reform: Public policy exceptions



Source: UNCTAD, *WIR15*.

A second set of options relates to defining the required relationship (i.e. the "nexus") between a measure and the policy objective it pursues. This determines how easy or difficult it is for a State to use an exception. For example, the IIA can provide that the measure must be "necessary" to achieve the policy objective (strict test) or that it must simply be "related to" ("aimed at", "directed to" or "designed to achieve") the policy objective (less strict test): the stricter the relationship, the stronger the protective character of the agreement.

A third set of options aims at preventing potential abuse of exceptions. For example, an IIA can clarify that "exceptional" measures must be applied in a non-arbitrary manner and not be used as disguised investment protectionism. Again, these options can be inspired by the respective WTO (GATT and GATS) clauses.

A fourth option establishes guidance for tribunals in the interpretation of exceptions clauses. For example, IIAs can establish a mandatory mechanism whereby cases in which a respondent State invokes a public policy exception are referred to a joint committee of the contracting parties. The committee could guide the interpretation or, alternatively, issue a binding determination of whether or not a measure falls within the scope of the public policy exception. This allows States to retain a certain degree of control over the application of an exceptions clause.

(ii) National security exception

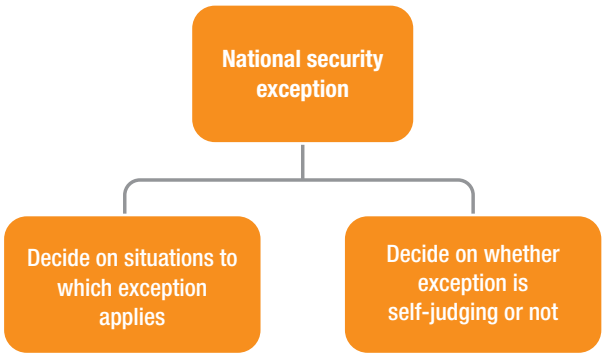
A number of policy developments raise concerns about the constraints that IIAs potentially impose on host States' measures that are designed to protect their national security interests.

In traditional IIAs, national security exceptions were included only sporadically. Their inclusion has been much more frequent in recent treaties (UNCTAD, 2009). At the domestic level, recent years have witnessed an expansion of the role of domestic screening and monitoring mechanisms for inward FDI (*WIR13*). In some cases, countries justify the imposition of investment restrictions or regulations on grounds of national security. Internationally, countries have invoked national security arguments in ISDS cases (e.g. in several cases brought against Argentina concerning measures taken to address the country's economic and financial crisis). National security issues figure prominently in a number of negotiations, particularly those in which pre-establishment commitments are under consideration (e.g. States may wish to retain their right to refuse the admission of foreign investors/investments where doing so would pose a risk to the State's security interests).

A national security exception enables a State to introduce emergency measures when its essential security interests are threatened or for the maintenance of international peace and security, even if these measures contradict substantive IIA obligations. Such measures may include the freezing of assets, other types of sanctions, or discriminatory treatment of investors of certain nationalities (or of foreign investors in general). In the pre-establishment context, such measures may include refusal of access to specific projects or transactions in industries considered as strategically important (such as manufacturing of arms, telecommunications, transportation, energy or water supply).

Assuming countries wish to include a national security exception into IIAs, they have a number of options at hand, all with their pros and cons (figure 9).

Figure 9. Options for IIA reform: National security exception



Source: UNCTAD, *WIR15*.

The first set of options relates to the types of situations that are covered and the degree of specificity that is applied to this policy choice. Countries can use a broadly formulated national security exception, e.g. for measures necessary for the protection of (or, with a looser nexus requirement, "directed to" or "designed to" protect) the State's "essential security interests". A related option is to define national security more specifically, e.g., as including measures taken to address a serious economic crisis situation or to maintain international peace and security.

Countries may take other steps to fine-tune, i.e. circumscribe, the coverage of treaty exceptions; for example, by including a reference to actions taken in pursuance of States' obligations under the UN Charter or by specifying that the exception covers only certain types of measures such as those relating to trafficking in arms or nuclear non-proliferation, applied in times of war or armed conflict, etc. Finally, a national security exception can also refer to "public order" or to the protection of "public security", with or without a clarification that this applies only to situations in which a genuine and sufficiently serious threat is posed to one of the fundamental interests of society.

Although national security exceptions are sometimes seen as reducing or limiting the protective strength of a treaty, clarifying and fine-tuning exceptions can help to increase predictability in the application of the clause and the circumscription of its application. A reference to the UN Charter can also help foster coherence between different bodies of law.

A second set of options relates to the standard of review that ISDS tribunals should apply to measures invoked for national security reasons. Here, the important parameter of a national security clause is whether it is formulated as "self-judging". If this is the case, the appropriateness of the measure in given circumstances is judged only by the invoking State itself (e.g. "measures which it considers to be in its essential security interests"). A "self-judging" exception gives host States a wide margin of discretion in its application and may trigger the perception that the treaty's protective value is somewhat reduced. It should be noted, however, that depending on the formulation chosen, a tribunal may still be able to review whether the exception is being relied upon in good faith and without manifest abuse.

In addition to these provisions, other IIA clauses have a bearing on safeguarding the right to regulate in the public interest. Although they figure less prominently in the reform

discussion, they are equally important for States to consider. These clauses include the preamble, provisions related to other substantive standards of treatment and provisions that delineate the scope and operative definitions of the treaty.

3. Other IIA provisions

(i) Preamble

The preamble is a clause with a cross-cutting impact. It plays a role in interpreting all other IIA obligations and can help address all of the five reform objectives identified. Thus, by identifying and clarifying the treaty objectives in the preamble, contracting parties provide important guidance for tribunals in investment disputes.

As regards the specification of treaty objectives, contracting parties can clarify that the IIA is not only about investment protection and promotion, but also is intended to serve other public policy interests, such as sustainable development, job creation, technology and know-how transfer. Another option is to state that the treaty is not intended to override national development objectives and that the parties preserve the right to regulate for legitimate policy objectives (e.g. public health, safety, environment, public morals, cultural diversity). The preamble can also clarify that the treaty is meant to be in line with the parties' other international obligations (e.g. treaties on human rights, environment, cultural heritage), and that the parties should not derogate from such obligations in order to promote and protect investment.

(ii) Scope of the treaty

Typically, IIAs are broadly formulated, covering all sectors of economic activities and all domestic measures that affect foreign investment. Nevertheless, countries may have an interest in carving out specific sectors or policy areas from the treaty scope (UNCTAD, 2010c).

Sensitive industries may include social sectors (e.g. education, health, the provision of water), cultural industries or defence. Exclusion can be full (from all treaty obligations) or partial (from some obligations only). As regards the carving out of policy areas, a potential candidate is taxation or issues related to the restructuring of sovereign debt (UNCTAD, 2011b). Again, this can be a full or partial exclusion. For example, taxation measures – while often excluded from the treaty scope – are sometimes kept subject to the expropriation and certain other IIA provisions (Japan–Mozambique BIT, 2013). Broad exclusions can help preserve the right to regulate, but they can also raise concerns that the treaty does not offer sufficient protections.

(iii) Definition of covered investment

A traditional, open-ended definition of investment grants protection to all types of assets. Although such an approach may be aimed at promoting an investment-attraction effect, it can also cover economic transactions not contemplated by the parties or expose States to unexpected liabilities – hence, the importance of clarifying the scope of covered investments (UNCTAD, 2010c).

One possibility is to require investments to fulfil specific characteristics. Treaty practice has converged on a number of such characteristics, notably, the commitment of capital,

the expectation of profit and the assumption of risk. Some IIAs include further criteria, e.g. "a certain duration" (Canada–EU CETA, 2016) or "establishing lasting economic relations" (Nigeria–Turkey BIT, 2011). A policy debate is under way as to whether an investment's positive contribution to (sustainable) development should constitute an additional criterion, and what indicators to use in this regard (Indian model BIT, 2015). Although some tribunals have looked at the investment's contribution to "economic development", such an additional criterion may be difficult to apply in practice and reduce predictability. The practice of some political risk insurers can, however, offer useful insights in this regard (OPIC, 2012).

IIAs could also compile an exhaustive list of covered investments or expressly exclude specific types of assets. Examples of assets that could be considered for exclusion are short-term, speculative or portfolio investments; sovereign debt obligations; claims to money arising from commercial contracts; or intellectual property rights that are not protected under the host State's law. There is also the possibility of adopting a narrow, enterprise-based definition of investment (e.g. Indian model BIT, 2015). A final option, complementary to any of the above, is to include a legality requirement; i.e. to specify that investment must be made in accordance with the laws and regulations of the host State.

(iv) Definition of covered investors

An IIA's definition of "investor" determines which investors are protected and able to bring claims against host States. More recently, increasing policy attention has been given to (indirect) ownership structures. In international investment policymaking, ownership chains have the potential to significantly expand the reach of IIAs (on UNCTAD's approach towards defining ownership and control see *WIR17*, chapter IV). About one third of ISDS claims in 2010–2015 were filed by claimant entities that are ultimately owned by a parent in a third country (not party to the treaty on which the claim is based). More than a quarter of these claimants do not have substantial operations in the treaty country (i.e. are "mailbox companies") – this share can increase up to 75 per cent considering claims based on treaties concluded by major ownership hub locations (*WIR16*).

IIAs increasingly circumscribe their coverage in response to three specific challenges: claims brought (i) by mailbox companies, ii) by entities controlled by a host State entity ("round-tripping"), (iii) by entities with ownership links to the investment that were purposely created in anticipation of a claim ("time-sensitive restructuring").

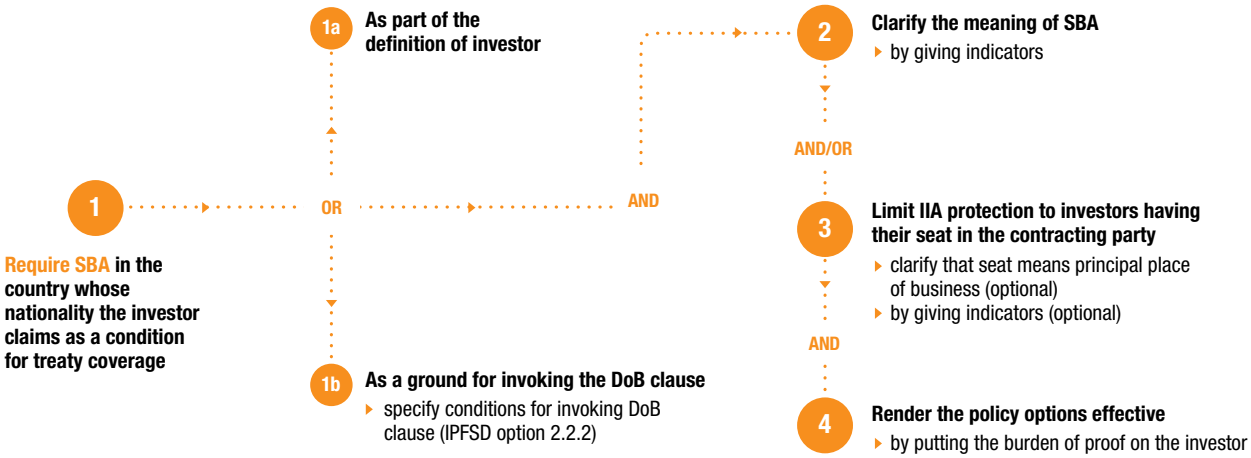
There are several policy options to focus or narrow the range of protected investors and exclude mailbox companies (figure 10). A first option is to include additional criteria in the definition of "investor". For instance, it could be clarified that the investor (legal entity) must not only be incorporated but also engaged in "substantial business activities" (SBA) in the home country. Additionally, IIAs can provide indicators for what might constitute SBA (*WIR16*).

A second option is to include a "denial of benefits" (DoB) clause to allow States to deny treaty benefits to mailbox companies (that are owned or effectively controlled by nationals of a third State or the host State) (figure 10). When designing a DoB clause, attention needs to be given to the time when the clause can be invoked. Several tribunals have held that the DoB clause may not be invoked against an investor after it initiates a formal arbitration claim, severely limiting the effective scope of these clauses.

To curb "round-tripping", IIAs can limit protection to investments and investors owned or *effectively* controlled by nationals of the home State contracting party, either through the definition of investment and investor clauses, or by way of reserving the right to deny benefits (figure 11). A second step, which brings additional predictability, is to clarify the meaning of effective control. When choosing indicators or criteria for effective control, policymakers need to strike a balance between objectivity and sensitivity to different circumstances (*WIR16*).

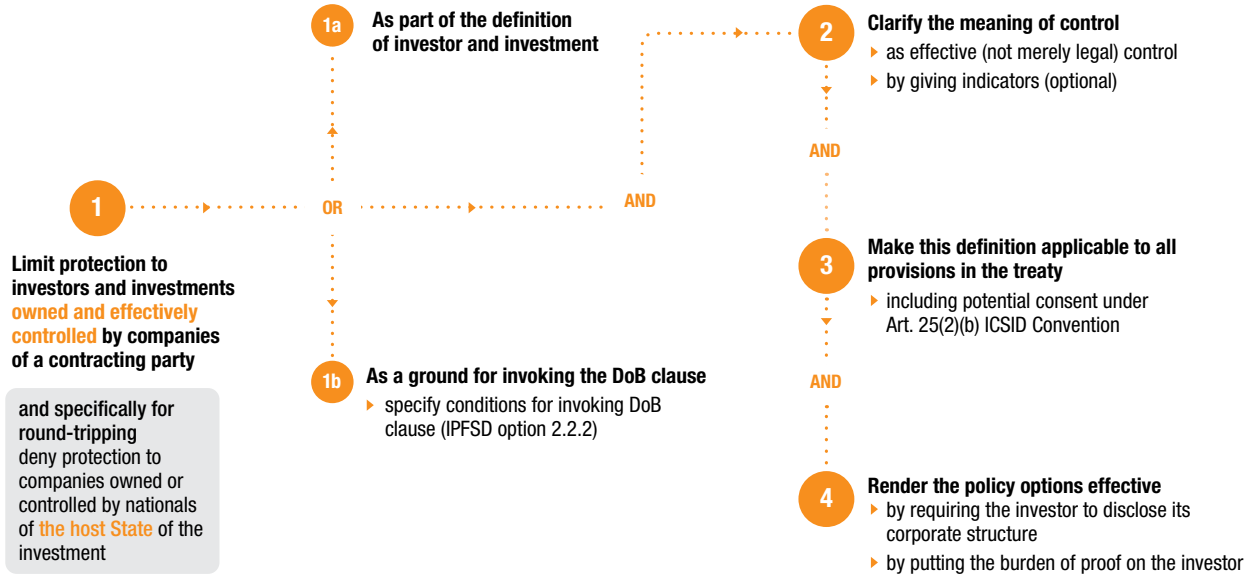
Finally, to counter "time-sensitive restructuring", IIAs can deny ISDS access to entities that have been restructured at a time when a dispute had already arisen or was foreseeable (figure 12). This policy option can be pursued through inclusion of a specific provision or through the DoB clause (then also specifying conditions for invoking the DoB clause, see above).

Figure 10. Mailbox companies: IIA options



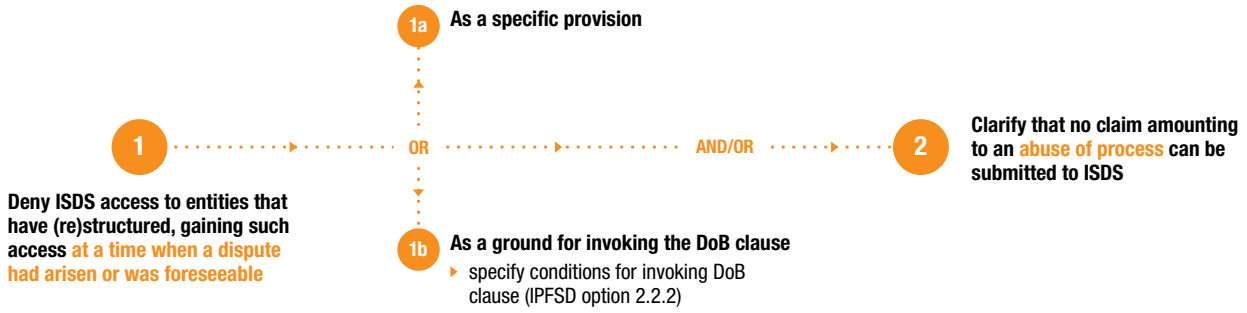
Source: UNCTAD, *WIR16.*

Figure 11. Indirect investments and round-tripping: IIA options



Source: UNCTAD, *WIR16.*

Figure 12. Time-sensitive restructuring: IIA options



Source: UNCTAD, *WIR16.*

(v) National treatment

The national treatment clause protects covered investors against nationality-based discrimination and guarantees them a level-playing field with comparable domestic investors. For a number of reasons, countries – in particular developing countries – may have an interest in limiting the scope of the national treatment principle. For example, States may wish to accord more favourable treatment to socially or economically disadvantaged minorities or ethnic groups.

A number of options exist to address these policy challenges. One option, included in a number of IIAs, is to clarify that the principle of non-discrimination applies only to investors "in like circumstances" and to establish criteria for making this assessment (e.g. COMESA Investment Agreement (2007, not in force), Indian model BIT (2015)).

A second option is to exclude sensitive policy areas (e.g. support programs for local start-ups or economic support for specific ethnic groups) from the national treatment obligation. A third option, rarely used, would be to make national treatment "subject to domestic laws and regulations". Finally, some IIAs omit the national treatment clause altogether (e.g. United Arab Emirates–Viet Nam BIT, 2003).

(vi) Umbrella clause

An "umbrella" clause, frequently included in traditional IIAs, requires a host State to respect any obligation that it has assumed with regard to a specific investment (e.g. obligations undertaken in an investment contract or concession agreement). The clause thus brings these contractual obligations under the "umbrella" of the IIA, meaning that their breach becomes a violation of the IIA.

Umbrella clauses have proven problematic in application, both with respect to the scope of the obligation undertaken and with respect to the potential for parallel dispute settlement proceedings (e.g. one proceeding to address the breach of contract claim and a parallel proceeding to address the alleged breach of the umbrella clause). Countries wishing to avoid the potentially far-reaching legal consequences of an umbrella clause can clarify and reduce its scope. For instance, States can clarify that the clause covers only "written obligations" and that the obligations must be "entered into" with respect to specific investments. They can also indicate that the umbrella clause applies only to conduct that constitutes an exercise of sovereign powers by a government, i.e. not an ordinary breach of contract by the State. Another option is to exclude the applicability

of the IIA dispute settlement mechanism to claims arising out of the umbrella clause. Finally, an increasing number of treaties omit the umbrella clause.

(vii) Remedies and compensation

Traditional IIAs do not specify the type of legal remedies a tribunal can order against a State. Furthermore, these IIAs contain no provisions as to the appropriate measure of compensation in the event of a breach of the treaty, with the notable exception of provisions on expropriation which have long included language regarding compensation. Several concerns have emerged in this connection. First, some arbitral tribunals have affirmed their power to grant any remedy they consider appropriate, including non-pecuniary remedies (e.g. an order to a State to revoke, amend or abstain from applying certain legislative, administrative or judicial acts). There are concerns that this type of remedy unduly interferes with States' sovereignty, especially if ordered by an ad hoc tribunal; others argue that there would be benefits in leaving the State the freedom to choose between pecuniary and non-pecuniary remedies. Second, some arbitral tribunals have granted monetary awards perceived as exorbitant in light of the State's public finances and compared with what the investor could conceivably obtain under the domestic rules.

There are several policy options – which can be used in a complementary manner – to deal with these concerns.

A first option is to set express limits on the remedial powers of tribunals. The growing trend has been to limit the available remedies to two forms: monetary damages and restitution of property, excluding the order to withdraw or amend a measure.

A second option concerns the standard of compensation for expropriation. The majority of IIAs set out a standard of prompt, adequate and effective compensation (the so-called "Hull formula"), rigidly connected to the investment's fair market value. This standard may result in high amounts of compensation, especially if the expropriated investment is valued using certain valuation methods such as the discounted cash flow analysis. Countries concerned about this possibility could consider terms such as "appropriate", "fair" or "equitable" compensation and "relax" the link between the standard of compensation and the market value of investment (SADC model BIT, 2012). Another approach would be to provide that – in case of lawful expropriation – arbitrators should rely on asset-based valuation methods (as opposed to methods based on future cash flows) and that, in any case, the award may not exceed the amount of capital invested plus interest at a commercially reasonable rate.

A third option is to include provisions that address the calculation of damages for treaty breaches that do not involve expropriation, with a view to limiting the extent of States' financial liabilities (BMWi, 2015).

(viii) Exceptions to free transfer of funds obligation

Most IIAs contain a clause granting investors the right to transfer funds, profits, capital and other payments freely and without delay. In times of economic or financial crises, this guarantee may be in conflict with the regulatory needs of host countries to impose capital controls or to put in place prudential measures aimed at ensuring the integrity and soundness of the financial system. Accordingly, the International Monetary Fund (IMF) has issued an official "institutional view" that encourages nations to regulate capital

flows under certain circumstances and has begun recommending such measures to member countries (IMF, 2012). The WTO similarly includes safeguards that allow nations to regulate the inflow and outflow of capital. Specifically, the GATS includes a "prudential carve-out" (Article 2, Annex on Financial Services) and a balance-of-payments exception (Article XII).

There are a number of options for addressing these challenges in IIAs. A first, increasingly used option is to include an exception for situations when a country experiences (or there is a threat of) serious balance-of-payments difficulties or other serious financial and economic crises (e.g. serious difficulties for macroeconomic management, in particular, monetary and exchange rate policies). A second option is to provide an exhaustive list of the types of funds that are freely transferable. A third, more general option is to make the free-transfer obligation subject to investors' compliance with certain key laws that aim at the protection of third parties (e.g. creditors) and prevention of illegal activities. The Austria–Nigeria BIT (2013) and Canada–Colombia FTA (2008) provide examples of this approach.

B. Reforming investment dispute settlement

Options include reforming the existing mechanism of ad hoc arbitration for ISDS while keeping its basic structure, and replacing existing ISDS arbitration systems.

Dispute settlement between investors and States through international arbitration is at the heart of the IIA reform debate. The increase in the number of ISDS cases in recent years (having reached at least 855 as of 31 December 2017), together with sometimes expansive, unexpected and inconsistent interpretations of IIA provisions by arbitral tribunals, has resulted in mounting criticism of the existing ISDS system (UNCTAD, 2015a, 2014b, 2014c, 2013a). This situation has triggered a worldwide debate about the pros and cons and about whether "to have or not to have" ISDS (table 5). Responding to these developments, a number of countries have been reassessing their positions on ISDS and have already adopted certain reform measures.

Two broad alternatives exist: to keep and reform ISDS, as some countries have done or to abandon and/or replace ISDS (table 6). Maintaining the status quo is hardly an option, given today's criticism of the existing system. Today, reforming dispute settlement is high on the agenda, with concrete steps undertaken, including at the multilateral level (box 1).

This section offers a number of concrete policy options in this regard. Countries can pick and choose, adapt and adopt the various options. They can use them in isolation or in combination, taking a hybrid approach. Whatever option countries prefer, they need to bear in mind three challenges: (i) what is needed is comprehensive reform, applying not only to ISDS but also to the substantive IIA provisions, since these are the root cause of many problems; (ii) reform steps ideally should not only apply to future treaties, but also address the stock of existing IIAs – the IIA "survival clause" poses challenges in this regard; and (iii) IIA reform is not enough – domestic capacity-building is needed for improving developing countries' administrative and judicial capacities, a prerequisite for some of the reform options suggested below.

Building on its past work on ISDS (e.g. the 2012 Investment Policy Framework (UNCTAD, 2015b), *WIR13* and the Pink Series Sequel on ISDS (UNCTAD, 2014b)), UNCTAD identifies

three sets of options for improving investment dispute settlement (table 6), along the two prongs of actions: reforming the existing ISDS system or replacing it. Some of these reform options can be combined and tailored to meet several reform objectives.

Table 5. Summary of arguments put forward in favour and against ISDS

Main arguments made in favour of ISDS	Main arguments made against ISDS
ISDS: • Provides an additional avenue of legal redress to covered foreign investors and enforces the substantive treaty obligations • Allows foreign investors to avoid national courts of the host State if they have little trust in their independence, efficiency or competence • Avoids recourse to diplomatic protection (investors do not need to convince their home State to bring claims or to exercise diplomatic protection) • Ensures adjudication of claims by a qualified and neutral tribunal • Removes any State immunity obstacles that may complicate domestic legal claims in some States. • May be faster than domestic court procedures in some countries • Allows recognition and enforcement of arbitral awards in many jurisdictions (under the ICSID Convention or the New York Convention)	ISDS: • Grants foreign investors greater rights than those of domestic investors, creating unequal competitive conditions • Exposes host States to legal and financial risks, without bringing any additional benefits, and can lead to "regulatory chill" • Lacks sufficient legitimacy (is modelled on private commercial arbitration, lacks transparency, raises concerns about arbitrators' independence and impartiality) • Fails to ensure consistency between decisions adopted by different tribunals on identical or similar issues • Does not allow for correcting erroneous decisions. • Creates incentives for "nationality planning" by investors from third countries (or from the host State itself) in order to gain access to ISDS • Is very expensive for users • Holds little additional value in the presence of well-established and well-functioning domestic legal systems

Source: UNCTAD, *WIR15*.

Table 6. Sets of options for reforming investment dispute settlement

Reforming existing investor-State arbitration		Replacing existing investor-State arbitration
Fixing existing ISDS mechanisms	Adding new elements to existing ISDS mechanisms	
1. **Improving the arbitral process**, e.g. by making it more transparent and streamlined, discouraging submission of unfounded claims, addressing ongoing concerns about arbitrator appointments and potential conflicts. 2. **Limiting investors' access**, e.g. by reducing the subject-matter scope, circumscribing the range of arbitrable claims, setting time limits, and preventing abuse by "mailbox" companies 3. **Using filters for channelling sensitive cases** to State-State dispute settlement 4. **Introducing local litigation requirements** as a precondition for ISDS	1. **Building in effective alternative dispute resolution** 2. **Introducing an appeals facility** (whether bilateral, regional or multilateral)	1. **Creating a standing international investment court** 2. **Replacing ISDS by State-State dispute settlement** 3. **Replacing ISDS by domestic dispute resolution**

Source: UNCTAD, *WIR15*.

Box 1. Reforming investment dispute settlement – recent developments

A multilateral mechanism for settling investment disputes

After first exploratory talks at the margins of the UNCTAD World Investment Forum (Nairobi, July 2016) and the OECD Investment Treaty Dialogue (Paris, October 2016), Canada and the European Commission co-hosted two days of exploratory discussions with third countries on the establishment of a multilateral investment court in Geneva (in December 2016). A "non-paper" outlined possible features of a future multilateral investment dispute mechanism and identified discussion points. Shortly after, the European Commission launched a public consultation on a multilateral reform of investment dispute settlement, which was open until mid-March 2017. In addition, a ministerial-level breakfast discussion on the multilateral investment court initiative was co-hosted by the European Trade Commissioner and the Minister of International Trade of Canada in January 2017 on the sidelines of the World Economic Forum in Davos, Switzerland.

On 13 September 2017, the European Commission released a proposal for a new multilateral investment court, including an impact assessment, with a view to opening negotiations for a Convention establishing such a court. On 20 March 2018, the EU Council adopted the negotiating directives authorising the Commission to negotiate, on behalf of the EU, a convention establishing a multilateral court for the settlement of investment disputes.

United Nations Commission on International Trade Law (UNCITRAL)

In early July 2016, UNCITRAL considered a report by the Geneva Center for International Dispute Settlement (CIDS), which suggested a road map for the possible reform of ISDS, including the potential of using the opt-in mechanism of the Mauritius Convention as a model for reform. The Commission requested that the UNCITRAL Secretariat review how the research project might be carried forward, if approved as a topic at the July 2017 Commission session. In that context, a number of consultations took place, e.g. through a questionnaire that was sent out to all governments as well as expert group meetings, such as a government expert meeting hosted by the Swiss Government in Geneva (in March 2017).

At its 50th session (3 to 21 July 2017), the UNCITRAL Commission decided to entrust its Working Group III with a broad mandate to work on the possible reform of ISDS. The first session of the Working Group III on this issue took place from 27 November to 1 December 2017, the second session from 23 to 27 April 2018.

Mauritius Convention on Transparency

As of July 2018, twenty-three States have signed and four have ratified the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration (Mauritius Convention). The Convention, which was opened for signature on 17 March 2015, entered into force on 18 October 2017. It enables States as well as regional economic integration organizations to make the UNCITRAL Transparency Rules applicable to ISDS proceedings brought under their IIAs concluded prior to 1 April 2014 and regardless of whether the arbitration was initiated under the UNCITRAL Arbitration Rules. The UNCITRAL Transparency Rules set out procedures for greater transparency in investor-State arbitrations conducted under the UNCITRAL Arbitration Rules and provide for a "Transparency Registry" as a central repository for the publication of information and documents in treaty-based ISDS cases. The Rules are already applicable to a number of IIAs concluded after 1 April 2014.

Source: UNCTAD.

1. Fixing the existing ISDS mechanisms

This set of reform options aims at reforming existing ISDS mechanisms *while keeping their basic structure*, namely that investors can bring claims against host States to ad hoc arbitral tribunals. Reform elements could be the inclusion in IIAs of new provisions designed to (i) improve the arbitral process; (ii) refine investors' access to investment arbitration; (iii) establish filters for channelling sensitive cases to State-State dispute settlement (SSDS); and (iv) introduce local litigation requirements. These reform options could be implemented by contracting States in existing and future individual IIAs and would not require coordinated actions by a large number of countries.

(i) Improving the arbitral process

This option focuses on reforming the way arbitration proceedings are conducted while preserving the main features of the ISDS system. The goals of such modifications are

to: (i) enhance the legitimacy of the ISDS system; (ii) enhance the contracting parties' control over the interpretation of their treaties; and/or to (iii) streamline the process and make it more efficient.

Specific reform steps may include the following:

- Providing for more transparency, for example, by granting public access to arbitration documents (including settlement agreements) and arbitral hearings and allowing the participation of interested non-disputing parties such as civil society organizations (UNCTAD, 2012b).
- Ensuring that persons adjudicating disputes possess the requisite skills and are fully independent, impartial, free from conflicts of interest and "affordable" to the parties, for example by creating rules on qualifications, conduct and/or remuneration of arbitrators (e.g. through a code of conduct).
- "Breaking the link" between the parties to the dispute and the arbitrators, for example, by establishing a roster of qualified arbitrators agreed upon by the contracting parties and determining by lot the arbitrators who sit on a specific case.
- Enhancing the contracting parties' role in interpreting the treaty, for example, by establishing mechanisms for the provision of binding joint party interpretations and facilitating interventions by the non-disputing contracting parties (UNCTAD, 2011c).
- Strengthening the contracting parties' control over adjudication of certain sensitive issues, for example, by requiring tribunals to refer certain matters (e.g. taxation, financial services (prudential carve-out), scheduled reservations) for joint determination in the first instance by the treaty parties, i.e. as a "filter" mechanism (NAFTA, 1992).
- Avoid wasting resources on full-length proceedings in case of manifestly unmeritorious claims, for example, by including a mechanism for early discharge of frivolous claims.
- Providing for a more equitable distribution of costs and discouraging submission of unfounded claims, through appropriate allocation of legal costs (fees paid by each party to arbitrators, lawyers, experts and other costs); for example, by expressly adopting the "loser pays" or the "cost follows the event" principles.
- Preventing investors from seeking relief for the same violation in multiple forums, for example, by including a "waiver" ("no-U-turn") clause (in contrast to the "fork-in-the-road" clause, often included in traditional BITs, "waiver" clauses do not discourage investors from first trying to obtain redress in the domestic courts of the host State).

(ii) Limiting investors' access to ISDS

This approach aims to narrow the range of situations in which foreign investors may resort to international arbitration, thereby reducing States' exposure to legal and financial risks posed by ISDS.

There are several possibilities to achieve this objective:

- Excluding certain types of claims from the scope of ISDS. This could apply, for instance, to certain sectors considered particularly sensitive (e.g. for claims relating to financial institutions and real estate), specific treaty provisions (e.g. pre-establishment obligations) or sensitive policy areas (e.g. measures adopted on national-security grounds). Exclusions can be party-specific or apply to all contracting States.

- Circumscribing admissible claims to treaty breaches only. This approach would exclude all non-treaty-based claims (e.g. alleged violations of domestic law, customary international law or investment contracts), but still provide investors with means to enforce the substantive protections found in the IIA. It can be combined with an applicable-law clause that allows application of the treaty and international law only (but not domestic law).
- Prohibiting recourse to ISDS after a certain time period has passed from the events giving rise to the claim ("limitations period"), e.g. three years. This introduces a time factor that fosters certainty and predictability with regard to the assumed treaty obligations. Without it, claims could be filed any time, exposing States to uncertainty. It may be useful to clarify whether the limitation period includes the time that the investor spends pursuing its claims in domestic courts.
- Preventing "abuse" of the treaty by denying ISDS access to investors who engage in "treaty shopping" or "nationality planning" through "mailbox" companies that channel investments but do not engage in any real business operations in the home State.
- Providing for State consent to international investment arbitration on a case-by-case basis.

(iii) Using filters for channelling sensitive cases to SSDS

This reform option provides for SSDS if a joint committee fails to resolve a case. While maintaining the overall structure of today's ISDS mechanism, this constitutes a *"renvoi"* of disputes on sensitive issues to SSDS; e.g. whether a measure is a "prudential" measure aimed at safeguarding the integrity and stability of the financial system or whether a taxation measure constitutes an expropriation. In this case, the ISDS proceeding is suspended until the State-State tribunal renders its decision. The latter is binding on the ISDS tribunal. This approach has been adopted in the BIT concluded between Canada and China in 2012 and in NAFTA (for investment disputes in financial services).

SSDS (be it in the form of arbitration, judicial or other procedures) may be better suited for sensitive issues of systemic importance, such as those relating to the integrity and stability of the financial system, the global system of international tax relations, or public health. For example, States are likely to use only those legal arguments with which they would feel comfortable in cases directed against them.

(iv) Introducing local litigation requirements as a precondition for ISDS (including exhaustion of local remedies)

This reform option aims to promote recourse by foreign investors to domestic courts while retaining the option for investor-State arbitration, as a remedy of last resort. In doing so, it would respond to some of the concerns arising from the steep rise in ISDS cases over the last decade. Domestic resolution of investment disputes is available in virtually every jurisdiction.

Two options could be considered to foster the use of domestic courts, without foreclosing investors' resort to ISDS:

- The IIA could require investors to exhaust local remedies before accessing international arbitration.

- The IIA could set out a "local litigation requirement", i.e. specify that the recourse to international investment arbitration becomes possible only after a certain period of time (e.g. 18 months) of litigating the dispute in domestic courts.

Requiring dispute resolution before the domestic courts of the host country puts foreign investors on an equal footing with domestic investors (as well as with foreign investors from States which do not have an IIA with the host country). It would also help establish a level-playing field among foreign investors, as the financial costs associated with international investment arbitration may preclude small and medium-sized enterprises from using it. In addition, national jurisdictions usually also include a right to appeal first-instance decisions and are well-suited to interpret and apply the domestic laws of the host State. Also, the argument has been made that reliance on ISDS is less important in countries with a sound legal systems, good governance and local courts' expertise. Finally, the argument is gaining ground that rather than focusing exclusively on ISDS, domestic reforms aimed at fostering sound and well-working legal and judicial institutions in host States are important. This may ultimately help remedy some of the host States' institutional deficiencies which IIAs and the ISDS mechanism were designed to address.

At the same time, however, there are concerns that some host States cannot guarantee an efficient and well-functioning domestic court system. Local courts may lack independence and be subject to political control and abuse by the State, including delaying tactics. Also, this approach would be particularly challenging in governance-weak countries, where local court decisions could be difficult to enforce. In other jurisdictions, owing to the high workload of local tribunals, the exhaustion of local remedies may span a long period of time and thereby reduce the value of the investment arbitration option. Furthermore, if the investor switches to ISDS after local litigation as an "appeal" to a domestic court ruling, this would potentially increase the legitimacy concerns with ISDS. Finally, local courts may not have the legal competence to apply international law – many jurisdictions do not allow for the direct applicability of IIAs, which would be a prerequisite for local enforcement of treaty obligations. In order for local enforcement to function therefore, such countries would have to transform the treaty into national law.

2. Adding new elements to the existing ISDS mechanisms

These policy options add new elements to complement the existing investor-State arbitration mechanism. They can be combined with the above-mentioned improvements of the mechanism.

(i) Appeals facility

This option would preserve the structure of the existing investment arbitration mechanism and add a new layer to it. An appeals facility could take two main forms: either a standing or an ad hoc body. It would have the competence to undertake a substantive review and correct the arbitral tribunals' first instance decisions.

An appellate mechanism would be given review jurisdiction that goes beyond the scope of review available under the existing annulment procedures under the ICSID Convention. The current ICSID annulment procedure, for example, does not entail a review of the merits and is limited to review on certain specified and limited grounds, e.g. irregular

constitution or corruption of the arbitral tribunal, serious departure from a fundamental rule of procedure, failure to state reasons for the award or a manifest excess of power. As a result, an ICSID annulment committee may find itself unable to annul or correct an award, even after having identified "manifest errors of law". An appeals facility could be given this broader power of review. In so doing, it could serve to enhance the predictability of treaty interpretation and improve consistency among arbitral awards. All this could significantly contribute to enhancing the political acceptability of ISDS and the IIA regime as a whole.

A joint committee established under a treaty could be tasked to hold consultations on the establishment of an appellate mechanism and identify specific issues for consideration, including the nature and composition of an appellate mechanism, and the applicable scope and standard of review (Canada–EU CETA (2016), United States model BITs (2004, 2012)).

Should countries decide to opt for establishing such an appeals mechanism, several sets of issues would need to be resolved:

First, issues regarding the establishment of such a body, notably whether it would have a bilateral, regional or multilateral nature. Although an appeals body may be easier to set up in a bilateral context, its expected function of fostering legal consistency and predictability would be more pronounced in a pluri- or multilateral context. In this connection, one would need to consider how the new mechanism could be reconciled with, and perhaps integrated into, the ICSID Convention (e.g. to replace the existing annulment procedure), the UNCITRAL Arbitration Rules, the rules of other arbitral forums used in ISDS and potentially other relevant international instruments such as the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Furthermore, developing an appeals facility capable of promoting interpretive harmonization and legal consistency would seem to require a mechanism under which it has the competence for reviewing all awards rendered under a particular treaty.

Second, issues regarding whether the appeals facility would be permanent (an appellate body) or ad hoc. Although ad hoc mechanisms would be easier to realize and involve lower costs, a permanent body may be more apt to ensure coherence in arbitral practice. An appellate body with permanent judges, appointed by States from a pool of eminent jurists, would allow the appeals facility to become an authority capable of delivering consistent – and balanced – opinions, which would rectify some of the legitimacy concerns about the current ISDS regime. Authoritative pronouncements by an appeals facility on issues of law would guide both the disputing parties (when assessing the merits of their respective cases) and arbitrators adjudicating disputes. At the same time, however, an appellate body with the authority to issue rulings with the force of precedents could place new limitations on the sovereignty of contracting parties through the establishment of an independent body of jurisprudence.

Third, issues regarding organization and institutional set-up of such a body. For example, who would elect the members of an appeals facility? How would they be elected? What would be the length of their tenure? What principles or code of conduct would govern their activities both with respect to their work within the facility and without it? What type of secretarial support would they receive? Who would finance it? Where would it be located?

Fourth, issues with regard to the added time and cost of the proceedings. The introduction of an appellate stage would add another layer of proceedings to the arbitration process, and care would need to be taken to put in place an efficient process, including timelines (e.g. as for the WTO Appellate Body).

Further, proceedings at an appellate stage would also involve additional costs for both investors and host States.

Fifth, issues related to the competence of such a body. These issues include the type of review available, the standard of review to be applied and the type of IIA decisions/awards which the body would be competent to address. For example, would the body be able to review only issues of law or also issues of fact? Would the body be able to remand an erroneous decision for reconsideration only by the tribunal that adopted it, or would it have the power to correct errors directly? Would the appellate facility have review power only over final awards or also over other decisions, e.g. on provisional measures and on jurisdictional issues?

(ii) Building in effective alternative dispute resolution

This approach to ISDS reform promotes the use of alternative dispute resolution (ADR) mechanisms as a step before the commencement of international investment arbitration (UNCTAD, 2010d; UNCTAD, 2010e). Although ADR cannot in itself solve key ISDS-related challenges, it can reduce the number of disputes which result in full-scale arbitration. This renders it a complementary, rather than a stand-alone, avenue for ISDS reform.

Whereas arbitration – like adjudication – follows an adversarial procedure leading to a binding decision by a third party, the outcome of ADR mechanisms ultimately requires acceptance by both parties. ADR has value because it can help resolve disputes at an early stage, thereby preventing them from severely and permanently damaging the relationship between the investor and host country. Because of its consensual nature, ADR may be particularly useful in cases of disputes where the parties consider it important to continue their investment cooperation beyond the present dispute. ADR also tends to be more informal and flexible than investor-State arbitration: its purpose is to find a solution that will be acceptable to both parties. If successful, therefore, ADR can help save time and money.

A limitation of ADR is that there is no guarantee that ADR procedures will lead to the resolution of a dispute; unsuccessful ADR can, therefore, increase the costs and time involved. That said, even if unsuccessful, ADR can serve to clarify the issues in dispute between the parties and help to streamline subsequent arbitral proceedings.

ADR may not always be feasible or acceptable to the host country, depending on the nature of the policy measure challenged by an investor, e.g. where the case relates to legislative measures. Moreover, given the consensual nature of ADR, a mediated outcome of the dispute that has not been endorsed by both parties cannot be enforced. Therefore, if one party does not respect the compromise solution proposed by ADR, binding arbitration may still become unavoidable.

The following policy options suggest actions at different levels of governance: the national and the international level (the IIA). Again, implementation of these options can be complementary.

At the *national level*, countries may want to consider ways in which to strengthen dispute prevention and management policies by:

- Emphasizing dispute prevention mechanisms through fostering information sharing between State agencies for the monitoring of sensitive sectors/industries for early warning signals of potential disputes.
- Establishing interinstitutional arrangements to address potential and emerging disputes more effectively.
- Empowering a particular agency to act as lead for the pursuit of amicable settlements (and potential subsequent arbitration).
- Creating investment ombuds offices or specific investment agencies to take the lead in resolving conflicts with investors early on.

At the *international level*, IIAs can include provisions on dispute prevention and management and integrate them into the IIA-based dispute settlement mechanism. Although a significant number of IIAs include the possibility of conciliation proceedings, policymakers may consider the need to strengthen existing mechanisms or add new ones (e.g. mediation). This can include:

- Adding an ADR provision.
- Strengthening the use of existing ADR as a dispute prevention mechanism by making it a compulsory step before the commencement of investment arbitration, e.g. through establishing "negotiation periods" (specified time periods during which consultations and negotiations must be pursued).
- Providing for institutional State-State mediation and conciliation efforts prior to investor-State dispute settlement.
- Formulating new provisions for ADR and dispute prevention and management, as e.g. set out by Brazil in its recently concluded cooperation and facilitation investment agreements (CFIA).

3. Replacing the existing ISDS system with other dispute resolution mechanisms

The options below would abolish the existing system of ad hoc investor-State arbitration and replace it with other mechanisms for settling investment disputes. Potential replacements include (i) the creation of a standing international investment court; (ii) SSDS; and/or (iii) reliance on domestic judicial systems of the host State.

The replacement options differ in the extent of change they bring. States can focus on one of the options or can pursue them in parallel or in combination. For example, option (iii) can be combined with option (ii) or option (i), which would preserve the possibility of some sort of international legal proceedings.

The option of replacing the ISDS has been recently pursued in the Australia–Japan Economic Partnership Agreement (EPA) (2014), the Australia–Malaysia FTA 2012, the Australia–New Zealand CEPA (2011), the Japan–Philippines EPA 2006, the Australia–United States FTA 2004, and the recently concluded CFIAs by Brazil (e.g. with Angola, Chile, Colombia, Malawi, Mexico, Mozambique in 2015). These treaties leave investment disputes subject to domestic courts but complement this process with the possibility of State-State proceedings under the treaty.

(i) Standing international investment court

This option retains investors' right to bring claims against host States but replaces the system of multiple ad hoc arbitral tribunals with a single institutional structure, a standing international investment court. Such a court would consist of judges appointed or elected by States on a permanent basis; it would be competent for all investment disputes arising from IIAs made subject to its jurisdiction and could also have an appeals chamber.

A standing investment court would be a public institution serving the interests of investors, States and other stakeholders and, more broadly, strengthening the legitimacy of the investor-State regime. A standing court could contribute to enhancing consistency and predictability in the interpretation of international treaties. It could also strengthen the perceived and actual independence and impartiality of adjudicators, by establishing them as judges with security of tenure and exclusivity of function who, unlike arbitrators in the present regime, would not be permitted to continue serving as counsel or expert witnesses. Moreover, a court could be competent for all investment disputes under an IIA, i.e. both investor-State and State-State proceedings. It has also been suggested that the competence of the court be broadened, depending upon the content of the IIAs made subject to its jurisdiction, in particular by giving legal standing or procedural rights to other stakeholders (Bernasconi, 2015).

Clearly, establishing such a court raises a number of important legal and political challenges, and, in its very nature, would constitute a long-term project. As countries move in this direction, they need to consider a number of key issues (see also above Appeals facility):

- Issues regarding the establishment of such a court, such as the need to build consensus among a critical mass of countries around a convention establishing such a court.
- Issues regarding organization and institutional set-up, such as the location, financing and staffing of the court.
- Issues around the participation of countries in the court, namely how to transition from a possible bilateral court established between key trading blocks, as recently proposed by the European Union (European Commission, 2015), to a more universal structure serving the needs of developing and least developed countries.
- Issues around the competence of the court, such as the type of IIAs and cases it is competent to address.

Multilateral consensus-building would help respond to the perception that such a court would work best in a plurilateral or multilateral context. It could help seek solutions for making a new court fit into the fragmented global IIA regime, which consists of thousands of mostly bilateral IIAs. Similarly, multilateral consensus-building would respond to the fact that a standing investment court may well start at a smaller scale, with an opt-in mechanism for those States wishing to join.

(ii) Replacing ISDS with SSDS

State-State arbitration is included in virtually all existing IIAs, and it is also the approach taken by the WTO for resolving international trade disputes.

Unlike the fostering of State-State dispute resolution as a complement to ISDS, this option presupposes that State-State proceedings would be the only way of settling investment disputes at the international level. The home State would have discretion on whether to bring a claim. States would need to decide on the court that should hear a case; options

Table 7. Summary of arguments put forward in favour and against State-State arbitration

Main arguments made in favour of State-State dispute settlement	Main arguments made against State-State dispute settlement
• Could avoid broader legitimacy concerns that have been raised in respect of ISDS • Could help to filter out frivolous claims • Only States can bring claims under international law as they are the principal subjects of the system • May help to avoid controversial legal issues related to challenges to public policies • States would not make certain types of legal arguments that could be used against them in the future • Does away with the privileges that ISDS bestows on foreign investors	• Could politicize investment disputes-commercial dispute would become a matter of State-State diplomatic confrontation • Investor interests could become a bargaining chip in international relationships • May be more cumbersome and lengthy for investors due to bureaucracy in either or both disputing States • May disadvantage SMEs vis-à-vis larger companies • Raises challenges for States in terms of costs of proceedings and legal remedies • Has implications for States in terms of administrative and institutional resources

Source: UNCTAD, *WIR15*.

include the International Court of Justice (ICJ), ad hoc tribunals or an international court as envisaged above.

State-State arbitration has a number of pros and cons (table 7).

Replacing ISDS with SSDS could be one way to reinstate countries' confidence in the IIA regime, address the legitimacy concerns raised with ISDS – by filtering out frivolous claims and avoiding controversial legal issues related to challenges to public policies; issues that could also be addressed by reforming the ISDS system (see above). More generally, this option would do away with the privileges that ISDS bestows on foreign investors; relying on SSDS would be in line with the principle that only States can bring claims under international law. Also, States may be less likely to make certain types of legal arguments that could be used against them in the future.

However, the argument is made that this option involves a number of challenges. The main challenge relates to a possible politicization of investment disputes, with all that this could entail (e.g. State discretion to pursue claims, elevating commercial disputes to the sphere of international relations, corporate lobbying). SSDS could also be more cumbersome and lengthy for investors because of bureaucracy in either or both of the disputing States. It could also place SMEs at a disadvantage vis-à-vis larger companies as regards having their case heard. There are also implications for States' administrative and institutional resources. Furthermore, there are questions about how rulings would be implemented, what kind of remedies would be appropriate, how these could be enforced, and who would bear the costs of the proceedings. One important implication to take into consideration is that SSDS could lead to the losing party being asked to bring a domestic measure into compliance with treaty obligations, not merely compensate for it (as is the case with ISDS), which implies a far greater intrusion into States' right to regulate.

There are also two other considerations to keep in mind. First, this option requires an identifiable home State, which in the case of complex multinational corporations, with affiliates in numerous countries and multiple ownerships, may be difficult to ascertain (*WIR16*). Second, host States may wish to avoid being confronted with diplomatic protection by investors' home States.

Given that there are so far only four known cases to date, it is difficult to draw lessons from State-State arbitration in IIAs.[5] Experience with SSDS in the WTO or in the context of regional agreements (including with respect to the remedies used, i.e. pecuniary vs. non-pecuniary) can help offer insights regarding the pros and cons of this option, but one needs to bear in mind the specific characteristics of investment disputes.

Overall, although the option of replacing ISDS with SSDS can help to address some of the concerns with regard to ISDS, it also raises a number of difficult challenges that would need to be addressed before taking this route.

(iii) Exclusive reliance on domestic dispute resolution

This option abolishes investors' right to bring claims against host States in international tribunals and limits their options for dispute resolution to domestic courts. Unlike the promotion of domestic resolution as a step preceding investor claims at the international level (e.g. exhaustion of local remedies, local litigation requirement), under this option, domestic judicial institutions would be the only and final mechanism for settling investor-State disputes. This option, it has been noted, has merits mainly in countries where reliance on ISDS is less important because of their sound legal systems, good governance and local courts' expertise.

As stated above, this option entails a number of pros and cons.

Arguments made in favour include that it treats foreign and domestic investors equally, and that it would help establish a level-playing field among foreign investors. It may also support fostering sound and well-working legal and judicial institutions in host States through domestic reform and could therefore help address some of the host-State institutional deficiencies which the IIA and the ISDS mechanism were designed to address. This would also respond to the increasing argument that rather than focusing exclusively on ISDS, domestic reforms aimed at fostering sound and well-working legal and judicial institutions in host States are important.

Arguments against this option rest on the concerns with regard to the independence, neutrality, efficiency and enforceability of local court rulings, especially in governance-weak countries. In addition, there are concerns that local courts may take a long time to settle a dispute (including because of delaying tactics). In the end, this could render the IIA non-enforceable. Moreover, local courts may not have the legal competence to apply international law, since many jurisdictions do not allow for the direct applicability of IIAs (see above).

ISDS offers benefits for foreign investors and potential advantages for home and host States compared to other means of dispute settlement, but in its present incarnation, the system suffers from significant drawbacks in its substance, procedure and functioning. There is thus a strong case for a systematic reform of investment dispute settlement. However, there are no quick and easy solutions. Reform options have their pros and cons and pose their own specific challenges.

Some of the reform options discussed in this section, such as clarifying the content of individual IIA provisions or limiting the access of investors to ISDS, are less difficult to implement than others. Some of the reform options can be undertaken through unilateral or bilateral actions, while others require regional, plurilateral or multilateral

efforts. Although multilateral options would go furthest in systemically addressing areas of needed reform, they would also face more difficulties in implementation and require agreement between larger numbers of States on a series of important questions.

In addition, in reforming investment dispute settlement, attention needs to be given not only to the thousands of individual investment treaties, but also to the existing multilateral ISDS-related instruments, such as the ICSID Convention and the widely used UNCITRAL Arbitration Rules. In this context, it has to be noted that terminating membership in one arbitral institution (e.g. ICSID), depending on the language used in the treaty, may have the effect that investors bring cases in other arbitration forums or under other arbitral rules (UNCTAD, 2010a). Hence, this option would not only fall short of preventing State liability, but, depending on the circumstances, could also entail exposing the State to less favourable procedures.

Finally, ISDS is an enforcement mechanism for the substantive provisions of IIAs. Hence, ISDS cannot be looked at in isolation, but only together with the substantive investment protection rules embodied in IIAs. Without a comprehensive package that addresses both the substantive content of IIAs and ISDS, any reform attempt risks achieving only piecemeal change and potentially creating new forms of fragmentation and uncertainty.

C. Promoting and facilitating investment

Options include adding inward and outward investment promotion provisions, as well as joint and regional investment promotion provisions. To these add several of the 10 action lines, covering more than 40 action items, set out in UNCTAD's Global Action Menu for Investment Facilitation.

States generally conclude IIAs with a view to attracting investment and benefitting from it. However, IIAs rarely include proactive investment promotion or facilitation provisions that effectively encourage outward or inward foreign investment. Instead, IIAs only indirectly promote investment – by protecting it. And IIAs lack the provisions to ensure a certain "quality" of the investment attracted (i.e. investment that delivers concrete and measureable sustainable development benefits to the host country). Given that fostering investment and ensuring its quality is crucial for bridging the financing gap for the SDGs (*WIR14*), this is an important element of IIA reform that has been taken on by UNCTAD (box 2).

To date, in the clear majority of existing IIAs, concrete investment facilitation provisions are either absent or weak (noting, however, that the precise extent of an IIA's facilitation dimension is hard to document because of the diversity of issues it comprises). Two types of clauses constitute an exception in this respect: Clauses facilitating the entry and sojourn of personnel and clauses furthering transparency.

These two types of clauses have commonly been included in IIAs since at least the 1980s and the 2000s, respectively.

More recently, a broader range of facilitation-related clauses (e.g. establishment of Joint Committees assuming facilitation-related tasks, or amicable dispute settlement mechanisms such as mediation) have made their way into modern investment treaty making – typically, however, without establishing legally binding, enforceable obligations (UNCTAD, 2017).

Box 2. UNCTAD's Global Action Menu for Investment Facilitation

Facilitating investment is critical for achieving the SDGs. According to UNCTAD's calculations (*WIR14*), developing countries face an annual SDG investment gap of $2.5 trillion. Despite the fundamental importance of investment facilitation for growth and development, to date national and international investment policies have paid relatively little attention to it.

To remedy this, in 2016 UNCTAD launched its Global Action Menu for Investment Facilitation, which is based on the organization's rich experiences with investment promotion and facilitation efforts worldwide over the past decades. It incorporates measures considered of key importance by investment promotion agencies (IPAs) and by the business community. It also builds on the 2012 and 2015 editions of UNCTAD's Investment Policy Framework for Sustainable Development, as well as UNCTAD's SDG Investment Action Plan (2014).

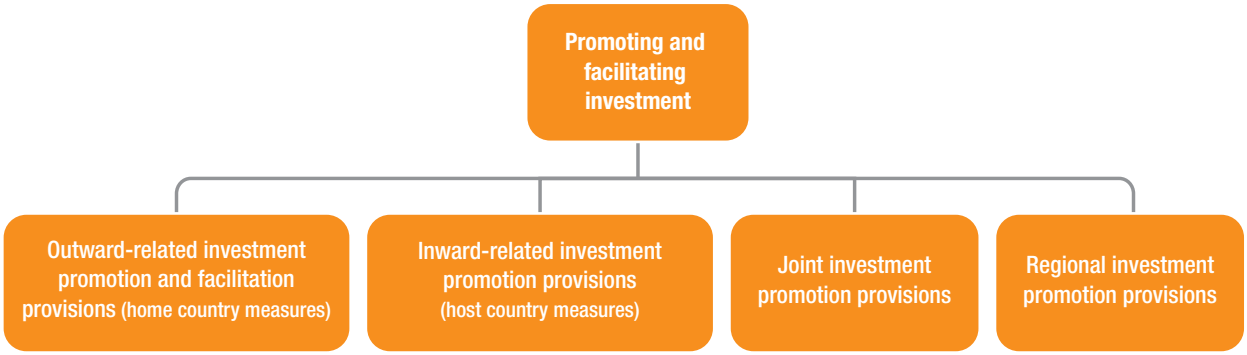
Following the endorsement of the Global Action Menu at the July 2016 World Investment Forum, during UNCTAD XIV, Ministers, heads of IPAs, senior investment treaty negotiators and others endorsed the initiative and requested that UNCTAD develop further policy advice and technical assistance tools, and continue building global consensus. The September 2016 update of the Global Action Menu incorporates the feedback and lessons learned from these multi-stakeholder consultations and intergovernmental processes.

In December 2016, UNCTAD's Trade and Development Board, the organization's governing body, continued the debate in a dedicated session also benefiting from a review of investment facilitation-related policies prepared by UNCTAD. At the session, regional groups and delegations affirmed their support for the Global Action Menu as an instrument for investment facilitation. Member States commended UNCTAD on the timeliness and quality of the updated version and endorsed the Global Action Menu as a "high-quality reference document for investment facilitation policies".

The Global Action Menu also formed the basis of the "Outlines for BRICS Investment Facilitation", charting good practices with a view to promoting investment, in particular intra-BRICS investment. The "Outlines" focus on three priority areas of investment facilitation: enhancing transparency, improving efficiency and promoting cooperation. They also incorporate a series of mutually supportive actions that BRICS countries can take, with a view to establishing a collaborative mechanism.

Source: UNCTAD.

Figure 13. Promoting and facilitating investment



Source: UNCTAD, *WIR15*.

This Reform Package offers a number of policy options for countries wishing to pursue this reform objective (figure 13). None of the options envisages a binding commitment for any of the contracting parties that would be enforceable through dispute settlement procedures. Most of the options require a certain financial and institutional capacity to implement them and therefore would need to be complemented with technical assistance (on a non-reciprocal basis) or special and differential treatment, particularly where the agreement involves structurally weak and vulnerable economies. Finally, there is some doubt about the value added of including such provisions in IIAs, given that actual investment promotion and facilitation measures are largely undertaken at the national level. At the same time, regional initiatives have set best practices in this regard.

1. Outward-related investment promotion and facilitation provisions (home-country measures)

Usually, IIAs regulate the behaviour of host countries. However, they can also include provisions directed at home countries. These options can, for example, emphasize the importance of specific home-country measures for promoting investment and/or stress home countries' endeavours to undertake such measures.

A first option is to refer to home-country promotion measures and encourage countries to proactively implement them. Such measures can include granting financial support; e.g. loans, grants (including R&D funding), providing investment guarantees (i.e. to protect investors against certain political risks in the host country) or holding equity participation in investment projects.

A second option is to refer to home-country technical assistance. Such assistance can aim at improving host countries' regulatory regimes and investment facilitation measures (e.g. help to simplify/streamline admission, registration or licensing procedures; to set up one-stop shops for registering an investment or a business; or to make available information on admission and establishment requirements, as well as on investment opportunities). Assistance can also aim at building institutional structures (e.g. judicial institutions, dispute prevention capacities, investment promotion agencies), at strengthening linkages between parties' research and academic centres or at facilitating feasibility studies for large investment projects.

A third option is to foster the sustainable development dimension of home-country investment promotion measures. Such provisions can state that the granting of outward incentives or investment insurance can be conditioned on the sustainable development impact or good governance record of the benefitting investment. The sustainable development impact can be specified, for example, by reference to specific sustainable development criteria (including for a specifically targeted region/community) or by reference to environmental and social standards (including (international) CSR standards). The United States' Overseas Private Investment Corporation (OPIC) uses about 30 development indicators to evaluate proposed projects. They include (i) job creation and human capacity-building (number of new jobs created, training and employee benefits); (ii) demonstration effects (e.g. technology and knowledge transfer, adoption of internationally recognized quality or performance standards); (iii) host-country impact (local procurement, and fiscal and foreign exchange impacts); (iv) environmental and community benefits (improvement of the environment and benefits to the local community); and (v) development reach (impact on basic infrastructure and/or its potential benefits to the poor and other underserved populations) (OPIC, 2012).

2. Inward-related investment promotion provisions (host-country measures)

An IIA can identify actions by host countries. Similar to the outward-related provisions, such clauses can stress the importance of these measures and/or aim to link them to specific sustainable development outcomes. An option is to condition host-country incentives on the sustainable development impact of the benefitting investment and that these incentives are in line with other policy areas such as industrial development strategies and regional economic cooperation. A variant is to condition the granting of investment incentives on the fulfilment of certain performance requirements, if this is permitted by the treaty.

Another variant is the establishment of an investment ombudsperson/facilitator in each contracting party. By monitoring and addressing investor concerns related to bureaucratic obstacles to doing business (e.g. business visas, obstacles to investment generally or to a specific investment project), an ombudsperson/facilitator can help ensure a business-friendly environment and, indirectly, affect a company's investment prospects and decisions. The ombudsperson/facilitator can be tasked with a number of activities, including addressing suggestions or complaints by investors and their home States; taking action to prevent, manage and resolve disputes; providing information on relevant legislative and regulatory issues; or promoting greater awareness and transparency.

Although such an ombudsperson/facilitator would mainly act at the national level, it can be mandated to report to and cooperate with the institutional mechanisms set up under the IIA. Some recent agreements, such as the CFIAs signed by Brazil and Mozambique and by Angola and Brazil (2015), have such an ombudsperson/facilitator as one of their key features. The Foreign Investment Ombudsman in the Republic of Korea, which since 1999 has found solutions for grievances filed by foreign companies can also provide insights into the functioning of such a service.

3. Joint investment promotion provisions

An IIA may also establish mechanisms, institutions and/or processes by which both home and host countries cooperate on investment promotion.

A first option is to establish a joint council or committee on investment promotion. Such a body can be part of the overall institutional framework between the contracting parties or be a self-standing specific element; it can be permanent or ad hoc. Such a body could meet regularly to oversee the implementation of the agreement and its investment promotion effect; to assess investment relations and identify new investment opportunities; to organize joint seminars, conferences, workshops or fairs; to monitor the implementation of specifically listed investment promotion and facilitation measures (e.g. related to the granting of business visas); to address specific concerns of investors (e.g. based on a report by an ombudsperson); or to design, implement and monitor progress on a thematic work plan (e.g. on green investment, promotion of linkages, issues related to SMEs, global value chains (GVCs)).

A second option relates to linkages. For example, an IIA can seek to foster linkages and stimulate joint ventures, in particular with SMEs, by calling for the sharing of expertise on entrepreneurship and management, and by encouraging the publication of documents on SMEs and the exchange of information and know-how on topics such as taxes, finances and other conditions necessary for the setting up and expansion of SMEs.

A third option for joint investment promotion measures is to foster cooperation between national investment promotion agencies (IPAs). The IIA can provide a platform for IPAs to exchange experiences and best practices in investment promotion, to share information on concrete investment needs and opportunities (e.g. a pipeline of SDG-related investment projects), and to jointly present and prepare large investment projects identified as bilateral investment priorities. Again, all of this work can have a thematic focus. A related option is to expand such cooperation beyond IPAs and also include trade promotion organizations, including, for example, joint trade and investment promotion

missions. This would respond to the emergence of GVCs where ever intensifying trade and investment links call for closer coordination between domestic trade and investment promotion agencies.

Another option is cooperation and partnerships between outward investment agencies (OIAs) in home countries and IPAs in host countries, including for example, for the development and marketing of pipelines of bankable SDG investment projects (*WIR14*). Stimulating such OIA-IPA partnerships can bring information sharing, technical assistance and exchanges, the marketing, financing and facilitation of SDG investment projects as well as joint monitoring and impact assessment.

4. Regional investment promotion provisions

IIAs could also harness the potential of regional cooperation. Building on the promotion-related experiences of regional economic cooperation initiatives, a regional IIA could call for facilitating investment and for establishing joint investment promotion mechanisms and institutions for regional infrastructure projects (e.g. regional development corridors) and regional industrial zones. This can also take the form of regional SDG investment compacts (*WIR14*).

Regional investment promotion initiatives exist around the globe. The Association of Southeast Asian Nations (ASEAN) Investment Agreement (AIA) (2009) refers to the joint promotion of the region as an integrated investment area, offering special and differential treatment to new ASEAN members (technical assistance to strengthen their capacity for investment promotion) and tasking the AIA Council to provide policy guidance on investment promotion. Investment promotion is also included in the ASEAN–India Investment Agreement (2014) and the ASEAN–China Investment Agreement (2009). The Common Market for Eastern and Southern Africa (COMESA) Treaty (1993) establishes a centre for the promotion of industrial development that works closely and exchanges information with the investment promotion centres in the member States. The COMESA Investment Agreement (2007) obliges member States to strengthen the process of investment promotion, and the COMESA Coordinating Committee on Investment includes chief executives of IPAs. The Southern African Development Community (SADC) Investment Protocol (2006) sets out the activities of IPAs, e.g. to proactively identify business opportunities for investments, encourage the expansion of existing investments, develop a favourable investment image of their countries, make recommendations for improvements of their countries as investment destinations, keep track of all investors entering and leaving the country for the purpose of analysis in terms of investment performance, or to advise investors upon request on the availability, choice or sustainability of partners in joint venture projects. Finally, the Central American Common Market Agreement on Investment and Trade Services (2002) provides for the promotion of investments within the region. For example, parties are mandated to provide, upon request, available information on investment opportunities (e.g. information on prospective strategic alliances among investors, and information on investment opportunities in specific economic sectors of interest to the parties) and to exchange information concerning foreign investment trends and available investment opportunities.

D. Ensuring responsible investment

Options include "not lowering of standards" clauses and provisions on investor responsibilities, such as clauses on compliance with domestic laws and on CSR.

Ensuring responsible investment has several dimensions. First, this reform objective may refer to maximizing the positive contribution that investors can bring to societies and/or to avoiding investors' negative impacts (e.g. on the environment, human rights, public health). Second, this reform objective may relate to investors' obligation to do what is required by law and/or to investors' response to societies' expectations that businesses comply with voluntary standards, i.e. that they do more than what is required by the law. The relevance and suitability of the policy options below differ depending on which of these aspects is the prime objective (figure 14).

1. "Not lowering of standards" clause

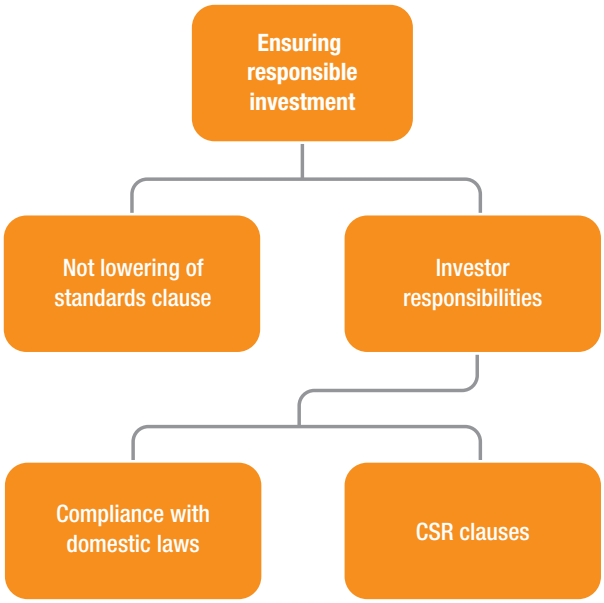
There is a concern that international competition for foreign investment may lead some countries to lower their environmental, human rights and other laws and regulations, and that this could result in a "race to the bottom" in terms of regulatory standards.

There are a number of options to address this concern.

A first option is to explicitly reaffirm parties' commitments under international agreements that they have concluded (e.g. in human rights, core labour rights or the environment). Doing so would not only help address concerns about a "race to the bottom", but also help foster overall coherence and synergy between different bodies of international law (systemic policy challenge).

A second option is to include a "not lowering of standards" clause in the IIA. The normative intensity of the clause may be increased by stating that each contracting Party

Figure 14. Ensuring responsible investment



Source: UNCTAD, *WIR15*.

"shall ensure" (instead of "shall strive to ensure") that it does not waive or derogate from environmental, labour or other laws (United States model BIT, 2012). This option has similar benefits as the explicit reaffirmation option, as it can (partly) respond to concerns regarding a potential race to the bottom and help manage the interaction between IIAs and national policies.

Both of these options move the IIA regime beyond its traditional role of focusing solely on investment protection and towards the goal of establishing and maintaining a regulatory framework that is conducive to sustainable development. By helping maintain – and build – a sound regulatory framework, these options can help promote responsible behaviour by investors and better manage the interaction between IIAs and domestic laws – and, possibly, help tip the balance in an ISDS case. However, there is a concern that such clauses, while constituting commitments of the contracting parties, are not enforceable in the traditional sense through ISDS and may have little concrete impact. Moreover, much of their impact depends on the quality of the host country's regulatory framework and its implementation.

A third option is to complement the above with a follow-up mechanism. This can include a mechanism for reporting on issues related to the implementation of the clause (including reporting on improvements of investment-related social, environmental or other laws and regulation).

2. Investor responsibilities

Most IIAs are asymmetrical in that they set out obligations only for States and not for investors. To correct this asymmetry, an IIA can also include provisions on investor responsibilities, as a few recent IIAs have done.

Although ensuring the responsible conduct of investors is a key objective of IIA reform, there are different views on the role of IIAs (in addition to, for example, national legal frameworks) in ensuring such conduct. Given the wide recognition of investors' responsibility to respect human rights and to conduct business in a responsible manner (e.g. as set out in the UN Guiding Principles on Business and Human Rights), the recognition of a need to rebalance IIAs, including as part of IIA reform, is gaining prominence.[6]

Noting the evolving views on the capacity of international law to impose obligations on private parties, there are two broad sets of options: raising the obligations to comply with domestic laws to the international level and designing CSR clauses.

(i) Compliance with domestic laws

Numerous IIAs include a requirement for investors to comply with laws of the host State when making an investment. This general obligation could be further specified in the IIA; for instance, by stipulating that the investment can be held legally responsible for damage caused to human health or the environment. The potential impact of this stipulation would be even more relevant if extended to damages arising in the post-operations stage of an investment; e.g. when foreign investors fail to ensure orderly divestment or environmental clean-up of their activities. This raises the issue under which conditions a parent company could be held responsible for damage caused by its foreign subsidiaries (*WIR13*).

More broadly, countries can strengthen their domestic regulatory frameworks by incorporating international principles and standards related to social, human rights, health, environmental and other risks associated with investment. Again, sharing of experiences and best practices, technical assistance and capacity-building can facilitate efforts in this regard (*WIR11*).

(ii) CSR clauses

The last decade has seen the development of CSR standards as a unique dimension of "soft law" that is rapidly evolving. CSR standards typically focus on the operations of MNEs and, as such, are increasingly significant for international investment.

The current landscape of CSR standards is multilayered, multifaceted and interconnected. The standards of the UN, the International Labour Organization (ILO) and the OECD serve to define and provide guidance on fundamental CSR issues. In addition, there are dozens of international multi-stakeholder initiatives, hundreds of industry association initiatives and thousands of individual company codes providing standards for the social and environmental practices of firms at home and abroad (*WIR11*).

In the past, the two universes of international rules affecting investment, CSR standards and IIAs, were largely disconnected. However, strengthening the responsibility dimension of IIAs calls for improving and strengthening the interaction between these two universes of international rules affecting investment.

There are a number of policy options to do so.

A first option is to encourage investors to comply with widely accepted international standards (e.g. the UN Guiding Principles on Business and Human Rights). This can be done either through a general reference, without listing the relevant CSR standards; by giving a list of the relevant standards; or by spelling out the content of relevant CSR standards. Each of these approaches has pros and cons. For example, building on the work done by CSR experts rather than reinventing the wheel saves time, costs and efforts and brings together two different bodies of law and policymaking, fostering coherence and improving systemic interaction. Referring to widely recognized and well-regarded instruments can add legitimacy and secure acceptance by different stakeholders.

A second, related option is to require tribunals to consider an investor's compliance with CSR standards, endorsed by the parties, when deciding an ISDS case. However, this raises the question of what legal consequences non-compliance would have. Furthermore, questions with regard to the cross-fertilization between different bodies of law; the need for arbitrators to familiarize themselves with the relevant, rapidly evolving normative standards; and the importance of managing interaction and coordination with CSR-related compliance processes and institutions arise.

A third option is to include a commitment by the parties to promote agreed best-practice international CSR standards. Parties can also commit to fostering compliance at the national level. Actions can include building local industries' capacity to take up CSR standards, by conditioning the granting of incentives on the observance of CSR standards, or introducing certain minimum standards (e.g. relating to anti-corruption, environmental, health and labour standards) into domestic laws.

A fourth option is to establish cooperation between the parties on CSR issues. Cooperation can involve the work of a special committee set up under the IIA and tasked to discuss CSR-related issues. Cooperation can also include promoting best-practice international CSR standards (e.g. by promoting the observance of applicable CSR standards and helping to implement them, including through specific industry support measures, market incentives and regulation), supporting the development of new voluntary standards (e.g. by cooperating on the above activities, and in the exploration and creation of new CSR standards) or other activities.

A fifth option that is worth considering, and that a number of countries are starting to pursue, is home-country efforts to regulate foreign investment for sustainable development. Whereas past CSR-related initiatives have largely taken a host-country perspective, an emerging policy development has home countries monitor or regulate the foreign activities of their companies, e.g. through export credit agencies and investment insurance (see above). Such an effort can address, among others, issues related to human rights, the environment or corruption.

All of the above options have their pros and cons. They can help support the spread of CSR standards, which are becoming an ever more important feature of the investment policy landscape. They can improve the interaction between different bodies of law and policy (see below), and help strengthen the "responsibility dimension" of IIAs. Although there are concerns that the "softer" approaches are unlikely to have a significant effect, they also carry certain advantages. For example, the softer the approach, the easier it will be to implement it and to make CSR part of the IIA. Moreover, soft approaches can have an important impact by "pushing the envelope" for conceptual debate and innovation in international investment policymaking. Referencing global (CSR) standards may in this aspect help to foster coherence and improve the interaction between IIAs and other areas of law and policymaking (*WIR17*) (see also below in chapter IIV.D., 10 options, Referencing global standards and in chapter V, Phase 3 of IIA Reform).

In addition to the reform-oriented elements presented above, some of the IIAs concluded in 2016 contain unique, innovative CSR features that have rarely been encountered in earlier IIAs. For instance, some recent IIAs contain provisions that fostering responsible investment by requiring investors to comply with environmental assessment screening procedures prior to establishment of the investment and to conduct social impact assessments of potential investments and to maintain an environmental management system and meet international certification standards, and investments in resource exploitation and high-risk industrial enterprises to maintain an ISO 14001 or equivalent standard (Morocco–Nigeria BIT). In a similar vein, some IIAs set out consequences for investors' failure to comply with investor obligations: e.g. subjecting them to civil actions before the courts of their home State in case of acts leading to significant damage, personal injuries or loss of life in the host State, and/or require investors to refrain from offering bribes to public officials and entitling States to deny substantive protection to investments established or operating by way of illicit means, corruption or other form of illegality (Morocco–Nigeria BIT and Brazil–Peru Economic and Trade Expansion Agreement) (*WIR17*).

E. Enhancing systemic consistency

In light of the atomized, multifaceted and multilayered nature of the IIA regime, a key reform challenge is to avoid further fragmentation of the system. This includes holistically addressing gaps, overlaps and inconsistencies across three dimensions of policymaking: between IIAs, between IIAs and other international law instruments and between IIAs and domestic policies.

The 2018 edition of UNCTAD's Reform Package presents Phase 3 of IIA Reform, which aims at enhancing investment policy coherence and synergies holistically across the above-mentioned three dimensions. For each dimension, policy interaction manifests itself in different ways, gives rise to different challenges and requires different solutions, in line with countries' specific national development priorities. Chapter V of this Reform Package takes stock of the status quo, outlines potential challenges and offers policy responses for improving investment policy coherence and synergies.

Questions of managing the relationship between treaties, or of consolidating them, are also addressed in Phase 2 of IIA Reform (see chapter IV of this Reform Package).

IV. PHASE 2 OF IIA REFORM: MODERNIZING THE EXISTING STOCK OF IIAs

A. Taking stock of reform

IIA reform has made significant progress in recent years. Sustainable development-oriented IIA reform has entered the mainstream of international investment policymaking and consolidated Phase 1 of IIA Reform.

Since 2012, over 150 countries have undertaken at least one action in the pursuit of sustainable development-oriented IIAs. For example, they have reviewed their treaty networks of revised treaty models. Most of today's new IIAs take into account the five priority areas for reform (see above chapter III) or include clauses that were set out in UNCTAD's Investment Policy Framework for Sustainable Development.

Evidence of IIA reform is particularly pronounced when treaties are compared over time. Table 8 shows the prevalence of modern treaty clauses in recent BITs, focusing on those that are particularly relevant for preserving the right to regulate while maintaining protection of foreign investors.

In fact, some provisions that were considered as "innovative" in IIAs concluded until 2010 now appear almost regularly. And almost all the recently concluded IIAs contain

Table 8. Reform-oriented elements in IIAs – comparison of "old" and "new" BITs

Treaty provisions Options for IIA Reform	**UNCTAD Policy Framework Option**	**Earlier BITs** (1959–2010) (2,432)	**Recent BITs** (2011–2016) (110)
Preamble Refer to the protection of health and safety, labour rights, environment or sustainable development	1.1.2	8%	56%
Definition of covered investment Expressly exclude portfolio investment, sovereign debt obligations or claims to money arising solely from commercial contracts	2.1.1	4%	39%
Definition of covered investor Include "denial of benefits" clause	2.2.2	5%	58%
Most-favoured-nation treatment Specify that such treatment is not applicable to other IIAs' ISDS provisions	4.2.2	2%	45%
Fair and equitable treatment Refer to minimum standard of treatment under customary international law	4.3.1	1%	29%
Indirect expropriation Clarify what does and does not constitute an indirect expropriation	4.5.1	5%	42%
Free transfer of funds Include exceptions for balance-of-payments difficulties and/or enforcement of national laws	4.7.2 4.7.3	18%	74%
Public policy exceptions Include general exceptions, e.g. for the protection of human, animal or plant life, or health; or the conservation of exhaustible natural resources	5.1.1	7%	43%

Source: UNCTAD, *WIR17*.

Note: The numbering refers to "Policy Options for IIAs: Part A. Post-Establishment", in the 2015 version of UNCTAD's Investment Policy Framework for Sustainable Development. Data derived from UNCTAD's IIA Mapping Project. The Mapping Project is an UNCTAD-led collaboration of more than 45 universities around the globe. Over 2,500 IIAs have been mapped to date, for over 100 features each. The Mapping Project's results are available at http://investmentpolicyhub.unctad.org/IIA/mappedContent#iiaInnerMenu. Although every effort has been made to ensure accuracy, UNCTAD assumes no responsibility for eventual errors or omissions in the mapping data.

at least one or two reform features (see also WIR18, table III.4). At the same time, some countries appear to be holding back from applying modern treaty drafting practices, and substantial differences in the IIAs concluded by a country at about the same time raise concerns about growing inconsistencies in and fragmentation of the IIA regime.

In addition to these innovative sustainable development-oriented elements, some new treaties also impose new, more far-reaching obligations on States. This includes broadening the scope of covered investments or introducing more far-reaching investor protections (e.g. expanding the list of prohibited performance requirements).

Reforming dispute settlement is high on the agenda, with concrete steps undertaken (e.g. reform-oriented clauses in new treaties, work on the establishment of an international investment court), including at the multilateral level.

Investment facilitation has also become an area of greater interest in investment treaty making. UNCTAD's Global Action Menu for Investment Facilitation was launched in *WIR16* to fill a systemic gap in national and international investment policymaking with a view to mobilizing investment for sustainable development and has obtained strong support from all investment and development stakeholders (see also above chapter III, box 2).

B. Three reasons for Phase 2 of IIA Reform

Despite significant progress in Phase 1 of IIA Reform, much remains to be done. First, comprehensive reform requires a two-pronged approach, i.e. not only concluding new treaties but also modernizing the existing ones (Phase 2). Second, reform needs to address the challenges of increasing fragmentation, both within the IIA regime as well as between the IIA regime and other areas of national and international policymaking (Phase 3).

Ultimately, only coordinated activity at all levels (national, bilateral and regional, as well as multilateral) will deliver an IIA regime in which stability, clarity and predictability serve the objective of all stakeholders: effectively harnessing international investment relations for the pursuit of sustainable development.

In terms of policy content, the five priority areas of reform identified in chapter III should serve as a basis for reform actions. When putting them into practice, countries would typically nuance, clarify or omit traditional treaty elements and add new sustainable development-oriented features. Sustainable development-oriented IIA reform may also include adding new treaty elements that can help make a country's investment climate more attractive, e.g. investment facilitation elements.

At the same time, it is becoming more common for new IIAs to not only contain reform-oriented elements, but to also impose new, more far-reaching obligations on States. This includes broadening the scope of covered investments or introducing more far-reaching investor protections (e.g. expanding the list of prohibited performance requirements).

1. Old treaties abound

Old-generation treaties abound: More than 2,500 IIAs (95 per cent of all treaties in force) were concluded before the year 2010. Meanwhile, some 700 treaties have not entered into force.

More than 2,500 treaties that are in force today were concluded before the year 2010 (95 per cent of all treaties in force) (figure 15). Most of these IIAs were negotiated in the 1990s: a time when the IIA universe was light on jurisprudence, but heavy on treaty making (about three new treaties per week). These older treaties typically contained similar, broadly worded definitions and substantive provisions, and few safeguards.

Today, many IIAs have been in force for longer than their initial periods of operation (most frequently set in the treaties at 10, 15 or 20 years). By the end of 2016, over 1,000 BITs had reached a stage where they could be unilaterally terminated by one contracting party immediately; many more are becoming available for such termination in the coming years. Moreover, the Vienna Convention on the Law of Treaties (VCLT) allows parties to terminate an agreement by mutual consent at any time.

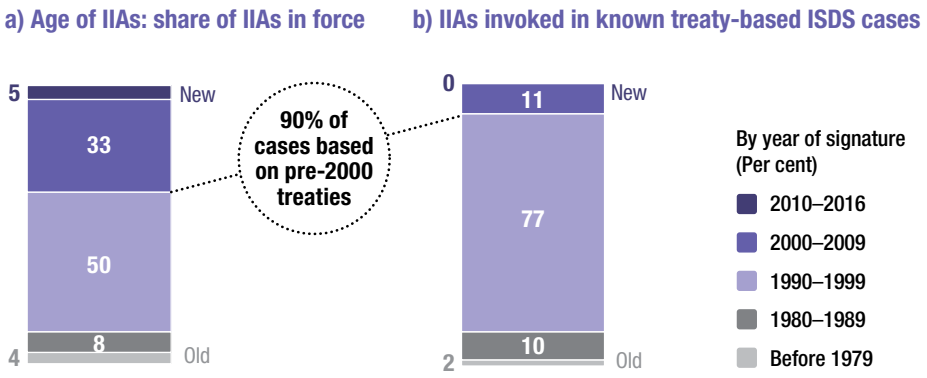
As agreements reach their expiry date, a treaty partner can opt for automatic prolongation of the treaty or notify its wish to terminate it. After reaching the end of the initial fixed term, many BITs can be unilaterally terminated at any time by giving notice ("anytime termination"), whereas some BITs – if not terminated at the end of the initial term – are extended for subsequent fixed terms and can be unilaterally terminated only at the end of the subsequent term ("end-of-term termination") (*WIR13*, box III.6).

Today's IIA universe is also characterized by a relatively large number of treaties that are not in force. By the end of 2016, there were 700 such treaties, about one fifth of all IIAs. Some are recently concluded treaties that are going through the process of domestic ratification (it takes 2.3 years on average for an IIA to proceed from signature to entry into force). However, the share of treaties dating from the 1990s and the 2000s that are not in force is quite significant, too (figure 16). This provides a window of opportunity for States to consider "abandoning" unratified treaties or renegotiating them in line with sustainable development priorities.

2. Old treaties "bite"

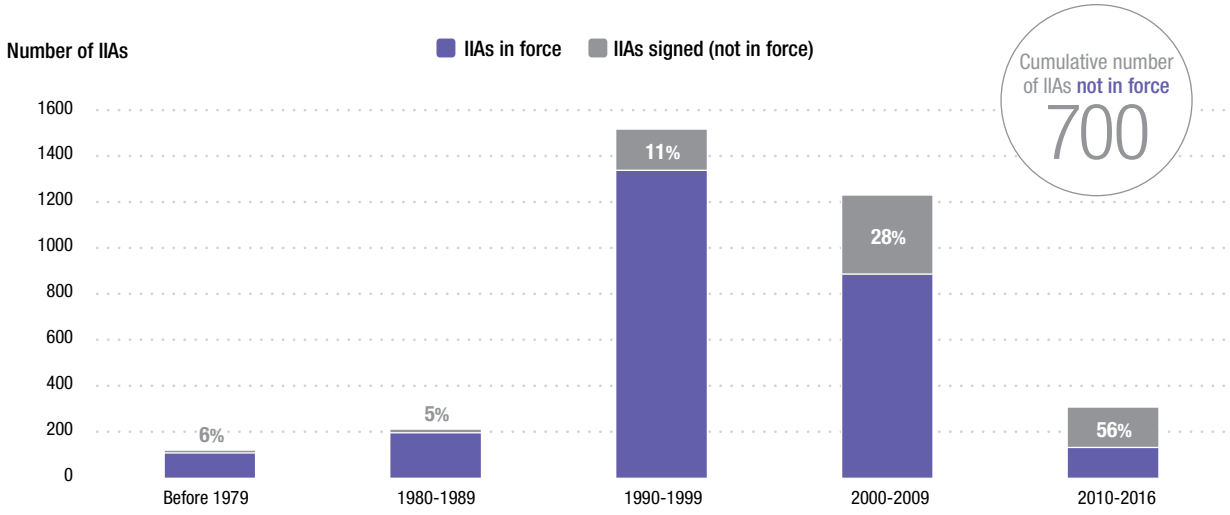
Old-generation treaties "bite": All of today's known ISDS cases are based on treaties that were concluded before the year 2010, most of which contain broad and vague formulations.

Figure 15. a) Age of IIAs: share of IIAs in force
b) IIAs invoked in known treaty-based ISDS cases



Source: UNCTAD, *WIR17* (based on IIA Navigator and ISDS Navigator).

Figure 16. Stock of IIAs and share not in force, by year of signature



Source: UNCTAD, *WIR17*.

Countries' experience with ISDS cases shows that "old treaties bite". At the end of 2016, virtually all of the known treaty-based ISDS cases had been filed pursuant to treaties concluded before 2010, which typically feature broad and vague formulations and include few exceptions or safeguards. Even though the stock of older treaties that are in force is larger than the number of more recent treaties and those treaties have been in existence for longer, the relative number of cases based on old treaties is still significantly higher (figure 15).

It is also noteworthy that about 20 per cent of all ISDS cases were brought under two plurilateral agreements from the early 1990s, the Energy Charter Treaty (ECT) and the North American Free Trade Agreement (NAFTA) (though the latter agreement contains several of today's IIA reform features).

In recent years, many countries (developing and increasingly developed countries alike) have experienced first-hand that IIAs are not "harmless" political declarations, but do "bite". Broad and vague formulations of IIA provisions have enabled investors to challenge core domestic policy decisions – for instance, in environmental, financial, energy and health policies. They have also generated unanticipated, and at times inconsistent, arbitral interpretations of core IIA obligations, resulting in a lack of predictability as to the kinds of State measures that might violate a specific IIA provision.

Treaty provisions need to be more clear and more detailed, drafted on the basis of thorough legal analysis of their actual and potential implications. As noted above, recent treaty drafting practice has started to take account of this view for new agreements, and the same lessons should be applied with respect to the stock of existing treaties during the next phase of IIA reform.

3. Old treaties perpetuate inconsistencies

Old-generation treaties perpetuate inconsistencies: Their continued existence creates overlaps and fragmentation in treaty relationships as well as interaction challenges within the IIA network, and between IIAs and other areas of international policymaking.

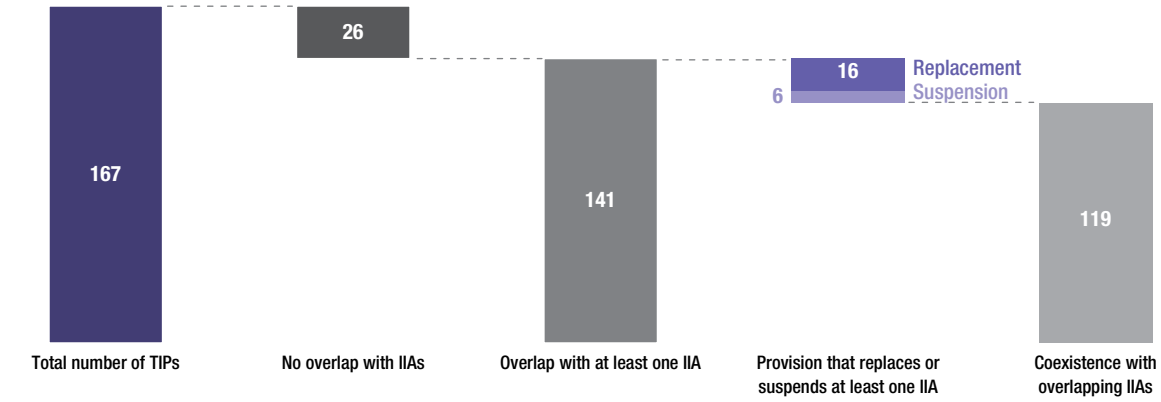
Today's IIA regime is characterized by gaps in treaty relationships (caused by a "patchy" treaty network), overlaps between treaties and divergence or inconsistencies in treaty clauses:

- The existing global treaty network only covers about one fifth of possible country relationships.
- Recent treaty making has resulted in increasing treaty overlaps. This is particularly pronounced in the context of megaregionals, but also in the case of FTAs. Among a sample of 167 TIPs (covering treaties with BITs-type substantive investment provisions and/or pre-establishment provisions), at least 119 overlap with earlier IIAs (concluded between all or some of the parties), which continue to exist in parallel to the new ones (figure 17). Over two-thirds of the sampled TIPs thus potentially exacerbate the IIA regime's fragmentation. Less than one-third either create new, previously uncovered treaty relationships or replace or suspend pre-existing, overlapping IIAs.
- Most new treaties display significant differences to earlier generation models (table 10). Sustainable development-oriented clauses that have become part of today's mainstream treaty practice (e.g. clarifications to treaty scope and substantive obligations as well as safeguards) are rarely found in old, first-generation IIAs. New, "reformed" IIAs with reformed treaty clauses thus often co-exist with old, "unreformed" IIAs containing unreformed treaty clauses.

To this must be added fragmentation (i.e. lack of coordination) with respect to current reform processes. Multiple, partially overlapping reform efforts are currently occurring – for example, in Africa (box 3) or with respect to initiatives to improve investment dispute settlement. In addition to managing relationships between treaties, there is therefore also a need to coordinate different reform processes. This task includes synchronizing reform efforts at different levels of policymaking (in the case of Africa, at the continental, regional and national levels) or combining them in multilateral contexts.

Finally, there is fragmentation of the international legal governance system for investment more broadly. IIAs interact with other areas of international law, such as environmental, labour, human rights, tax, and trade law. At times, ISDS cases have highlighted tensions between IIAs and these other areas of international law, as well as public policymaking in these areas. Policymakers need to consider these linkages and prevent international

Figure 17. Relationships between IIAs (Number of TIPs)



Source: UNCTAD, *WIR17*.

Box 3. Synchronizing regional IIA reform efforts in Africa

African countries are actively engaged in IIA reform at the regional level through parallel negotiations of, and amendments to, various "new generation" international investment instruments. These include, among others, the Pan-African Investment Code, Phase II of the Tripartite FTA between the Common Market for Eastern and Southern Africa (COMESA), the East African Community (EAC) and the Southern African Development Community (SADC), the Continental Free Trade Area, the COMESA Common Investment Area and the SADC Finance and Investment Protocol. This is in addition to IIA reform efforts at the national level under way in a number of African countries (e.g. Botswana, Egypt, Nigeria, South Africa).

These initiatives express the determination of African countries to embark on IIA reform in order to make the policy framework for investment in Africa more balanced and more oriented to sustainable development. However, they risk overlapping with one another, potentially diluting the impact of regional reform efforts and creating a more complex regime instead of harmonizing and consolidating it.

Another challenge relates to the existing intra-African BITs, of which 165 had been signed by the end of 2016 (of which only 38 are in force). The fate of these first-generation treaties remains uncertain. If the new regional IIAs under negotiation do not entail the replacement of older BITs, the result will be an undesirable multiplication of treaty layers. On the other hand, replacing existing BITs with new regional initiatives would contribute to the consolidation and harmonization of the international investment policy framework in Africa.

It is therefore crucial to synchronize reform efforts at different levels of policymaking (continental, regional and national). This requires coordination and cooperation among African countries in order to avoid overlap, policy inconsistencies and fragmentation.

Source: UNCTAD, *WIR17*.

investment law from evolving further into an even more isolated system with a narrow set of objectives (see also below chapter V, Phase 3 of IIA Reform). Many newer IIAs include reference to other international agreements and global standards, but within the overall network they remain rare.

C. Challenges and choices

Countries have numerous options for modernizing their stock of first-generation treaties and reducing fragmentation of the IIA regime. This chapter presents and analyses 10 options (i.e. mechanisms) and their pros and cons, for countries to adapt and adopt in line with their specific reform objectives. Determining which reform option is "right" for a country in a particular situation requires a careful and facts-based cost-benefit analysis, while addressing a number of broader challenges.

There are at least 10 options available for countries that wish to change existing treaties to bring them into conformity with new policy objectives and priorities and to address the challenges arising from the fragmentation of the IIA regime (table 9). The mechanisms are not mutually exclusive and can be used in a complementary manner, especially by countries that have extensive IIA networks.

The 10 options differ in several aspects, as they encompass actions that are more technical (e.g. interpreting or amending treaty provisions) or rather political (e.g. engaging multilaterally), focus on procedure (e.g. amending or replacing treaties) or also on substance (e.g. referencing international standards), or imply continuous engagement with the IIA regime (e.g. amending, replacing, engaging multilaterally) or "exit" from it (e.g. termination without replacement, withdrawing from multilateral mechanisms). They represent modalities for introducing change to the IIA regime (the "how" of reform"), though they need to be seen and considered in combination with the treaty content design (the "what" of reform, or Phase 1 of IIA Reform, chapter III above).

Table 9. Overview of reform options: actions and outcomes

Action option	Outcome
1. Jointly interpreting treaty provisions	Clarifies the content of a treaty provision and narrows the scope of interpretive discretion of tribunals
2. Amending treaty provisions	Modifies an existing treaty's content by introducing new provisions or altering or removing existing ones
3. Replacing "outdated" treaties	Substitutes a new treaty for an "old" one
4. Consolidating the IIA network	Abrogates two or more old IIAs between parties and replaces them with a new, plurilateral IIA
5. Managing relationships between coexisting treaties	Establishes rules that determine which of the coexisting IIAs applies in a given situation
6. Referencing global standards	Fosters coherence and improves the interaction between IIAs and other areas of international law and policymaking
7. Engaging multilaterally	Establishes a common understanding or new rules among a multitude of countries, coupled with a mechanism that brings about change "in one go"
8. Abandoning unratified old treaties	Conveys a country's intent to not become a party to a concluded but as yet unratified treaty
9. Terminating existing old treaties	Releases the parties from their obligations under a treaty
10. Withdrawing from multilateral mechanisms	Similar in effect to termination, but leaves the treaty in force among the remaining parties who have not withdrawn

Source: UNCTAD.
Note: This classification is made for illustration purposes only. The table should not be seen as placing possible reform actions in any order of priority.

Determining whether a reform mechanism is "right" for a country in a particular situation requires a careful and facts-based cost-benefit analysis, while addressing a number of broader challenges. Strategic challenges include producing a holistic and "balanced" result, rather than "overshooting" on reform and depriving the IIA regime of its purpose of protecting and promoting investment. Systemic challenges arise from gaps, overlaps and fragmentation that create coherence and consistency problems. Coordination challenges require prioritizing reform actions, finding the right treaty partners to implement them and ensuring coherence between reform efforts at different levels of policymaking. Capacity challenges make it hard for smaller countries, particularly LDCs, to address the deficiencies of first-generation IIAs.

Choices must be made for identifying the best possible combination of the 10 policy options.[7] The chosen combination of options should ultimately reflect a country's international investment policy direction in line with its national development strategy. Moreover, when implementing IIA reform, policymakers have to consider the compound effect of options.

Some combinations of reform options may result in a treaty regime that is largely deprived of its traditional investment protection rationale or may result in a complete exit

from the IIA regime. Reform efforts, particularly comprehensive ones, should harness the benefits that can be obtained from the rule of law and respond to investors' expectations of predictability, stability and transparency in policymaking.

When choosing among reform mechanisms, policymakers should also consider the attendant challenges, both legal and practical. Among the legal challenges, three stand out as being particularly pronounced: the MFN clause, the survival clause and the management of transitions between old and new treaties. Each of these challenges may be particularly relevant for certain specific reform options:

- *MFN clauses* aim to prevent nationality-based discrimination.[8] Many tribunals have interpreted broadly worded MFN provisions as allowing the importation of more favourable provisions from IIAs signed by the host State with third countries. This has led to some controversy and subsequently more careful treaty drafting that limits the scope of application of the MFN provision. The inclusion of a broadly worded MFN clause in a new treaty can undermine reform efforts, as it allows investors to cherry-pick the most advantageous clauses from a host State's "unreformed" treaties with third countries. For existing IIAs, MFN-related challenges arise in particular for four reform options: joint interpretation, amendment, replacement and management of treaty relationships.
- *Survival clauses* included in most BITs are designed to extend treaty application for a further period after termination (some for 5 years, but most frequently for 10, 15 or even 20 years).[9] Depending on how they are formulated, survival clauses apply either only to unilateral termination or potentially also to joint treaty termination (including termination owing to replacement by a new treaty). Allowing an old-generation (unreformed) treaty to apply for a long time after termination would undermine reform efforts, particularly if doing so results in parallel application with a new treaty. Thus, survival clauses may need to be "neutralized" in old treaties that are being jointly terminated or replaced (including through consolidation). Challenges related to survival clauses are particularly pronounced with respect to reform options that terminate, replace or consolidate.
- *Transition clauses* delineate a treaty's scope of temporal application by clarifying in which situations, and for how long after a treaty's termination, an investor may invoke the old IIA to bring an ISDS case. If included in the new treaty, such clauses help ensure a smooth transition from the old to the new by limiting situations in which both treaties apply concurrently (or by clarifying that upon the new treaty's entry into force, the old treaty is phased out). Transition clauses effectively modify the operation of the survival clause in the "outgoing" treaty; they are particularly relevant for reform options that replace old treaties, including through consolidation.

In addition to legal challenges, policymakers also need to keep in mind and plan for the many practical and political challenges that might arise, as outlined in the following subsections.

D. Ten options for modernizing treaties

1. Jointly interpreting treaty provisions

IIAs with broadly worded provisions can give rise to unintended and contradictory interpretations in ISDS proceedings. Joint interpretations, aimed at clarifying the meaning

of treaty obligations, help reduce uncertainty and enhance predictability for investors, contracting parties and tribunals.

Clarifying IIA clauses can help reduce uncertainty arising from (broadly worded) provisions of first-generation BITs (UNCTAD, 2011c). Authoritative joint party interpretations therefore offer a degree of much-needed clarity for investors, host States and arbitrators alike. This reform tool is potentially the easiest in its practical application as it allows treaty parties to voice their positions on a specific IIA clause without undertaking a comparatively higher-cost and more time-consuming amendment or renegotiation of the treaty (interpretative statements do not require ratification) (table 10). By stating explicitly in the treaty that joint interpretation is binding on the tribunal, the parties can remove any doubt regarding its legal effect (*WIR13*). However, even in the absence of such a provision, the VCLT obliges arbitrators to take into account, together with the context, "[a]ny subsequent agreement between the parties regarding the interpretation of the treaty" (Article 31.3(a)).

Several countries have engaged in joint interpretations. In 2001, the NAFTA Free Trade Commission adopted "Notes of Interpretation of Certain chapter 11 Provisions", clarifying e.g. NAFTA Article 1105(1) on the minimum standard of treatment. In 2013, through a joint interpretative understanding, Colombia and Singapore clarified several provisions (such as FET and MFN) of their BIT (also signed in 2013). In January 2016, the parties to the TPP issued the "Drafters' Note of interpretation of 'Like Circumstances'", which is applicable to the treaty's NT and MFN provisions.

Two recent policy developments, different from but related to the traditional understanding of "joint interpretations", also merit consideration: In February 2016, India proposed a "Joint Interpretative Statement" to 25 countries with which it has IIAs whose initial period of validity had not expired. The statement sets out India's proposed interpretation of several provisions in those treaties, including the definitions of "investor" and "investment"; the MFN, NT, FET and expropriation clauses; and the ISDS provisions. In October 2016, the EU, its member States and Canada released a "Joint Interpretative Instrument" on the Comprehensive Economic and Trade Agreement (CETA). It sets out

Table 10. Reform action: Jointly interpreting treaty provisions

Clarifies the content of a treaty provision and narrows the scope of interpretive discretion of tribunals

Outcomes (pros)	Challenges (cons)
• Allows the parties to clarify one or several specific provisions without amending or renegotiating the treaty (no ratification required, less cost- and time-intensive) • Is particularly effective if the treaty expressly provides that joint interpretations by the parties (or their joint bodies) are binding on tribunals • Becomes relevant from the moment of adoption, including for pending disputes • Has authoritative power as it originates from the treaty parties	• Is limited in its effect as it cannot attach an entirely new meaning to the provision being interpreted • Can raise doubts about its true legal nature (may not always be easy to distinguish between a joint interpretation and an amendment) • Can leave tribunals with a margin of discretion • Might be difficult to establish as genuine if either party has consistently acted in a way that does not comport with the interpretation • May be difficult to negotiate in cases when a pending dispute involves the application of the provision concerned

Source: UNCTAD, *WIR17*.

the parties' agreement on a number of provisions that have been the subject of public debate and concern (such as the right to regulate and compensation).

Of note also is the frequent establishment in recent IIAs of joint bodies with a mandate to issue binding interpretations (e.g. Canada–EU CETA (2016); Morocco–Nigeria BIT (2016); Chile–Hong Kong, China BIT (2016)).

2. Amending treaty provisions

The expansively formulated obligations common to old IIAs may sometimes be difficult to "fix" through a joint interpretation. By amending treaty provisions, the parties can achieve a higher degree of change and thereby ensure that the amended treaty reflects their evolving policy preferences.

Typically, amendments are limited in number and do not affect the overall design and philosophy of a treaty (*WIR13*). Where treaty parties are concerned only with certain specific provisions (e.g. MFN, FET), discrete amendments might be preferred to the renegotiation of the whole treaty, an exercise that could be time-consuming and, depending on the other party (or parties), challenging (table 11).

Applicable amendment procedures depend on the treaty that is subject to change. For IIAs that do not regulate amendments, the general rules of the VCLT will usually apply. However, many newer IIAs include their own provisions on amendment. This is particularly important for pluri- or multilateral treaties, in which the large number of parties involved adds complexity to the process. IIA amendments are usually formalized through separate agreements (e.g. protocols or exchanges of letters or notes), which take effect following a procedure similar to the original treaty, i.e. after respective domestic ratification procedures are completed.

Comprehensive data on amendments are not yet available. Existing evidence suggests, however, that States have thus far used amendments rather sparingly (Gordon et al., 2015; Broude et al., 2016). Exceptions are the EU member States from Eastern Europe (Bulgaria, Croatia, the Czech Republic, Estonia, Latvia, Lithuania, Poland, Slovak Republic, Slovenia and Romania), which have made amendments by using protocols before and after accession to the EU. Of a sample of 84 IIAs concluded by these

Table 11. Reform action: Amending treaty provisions

Modifies an existing treaty's content by introducing new provisions or altering or removing existing ones

Outcomes (pros)	Challenges (cons)
• Constitutes a broader, more far-reaching tool than interpretation: can introduce new rules rather than merely clarify the meaning of existing ones • Selectively addresses the most important issues on which the parties' policy positions align • Can be easier to agree upon with the treaty partner and more efficient to negotiate compared with a renegotiation of the treaty as a whole	• Typically requires domestic ratification in order to take effect • Only applies prospectively, i.e. does not affect pending disputes • Does not lead to overall change in treaty design and philosophy • May lead to "horse trading" in which desired amendments are achieved only through a quid pro quo with parties demanding other amendments

Source: UNCTAD, *WIR17*.

countries that contain protocols, over 60 concern extra-EU BITs that were amended, among others, to bring their international obligations in line with their obligations under EU law. Some introduce exceptions to MFN clauses for regional economic integration organizations or include exceptions for national security reasons (e.g. Protocol (2007) to the Bulgaria–India BIT (1998) or the Protocol (2010) to the Czech Republic–Morocco BIT (2001)). Amendments have also been used by several EU member States to introduce balance-of-payments exceptions to provisions on the free transfer of funds (e.g. Protocol (2013) to the Kuwait–Lithuania BIT (2001), Protocol (2011) to the Bulgaria–Israel BIT (1993) or Protocol (2009) to the Czech Republic–Guatemala BIT (2003)). These latter amendments have also been made in reaction to the ruling of the European Court of Justice in 2009 that the transfer of funds provisions in certain EU member States' BITs with third countries breached EU law.[10]

Other countries have used amendments in a more sporadic manner to include adjustments to the ISDS mechanism (e.g. the Exchange of Notes (1997) to the Paraguay–United Kingdom BIT (1981), the Protocol (2000) to the Panama–United States BIT (1982), the Protocol (2003) to the Germany–Moldova BIT (1994)). More recent examples include the May 2016 amendments to the Singapore–Australia FTA (2003) agreed by the parties upon their third review of the treaty. The revised investment chapter includes numerous changes to definitions and substantive obligations, and adds exceptions to dispute settlement (including a carve-out from ISDS for tobacco control measures). These amendments are in the process of ratification.

Finally, in August 2016, members of the SADC amended Annex 1 of the SADC Finance and Investment Protocol. The amended version omits the FET provision and the ISDS mechanism, refines the definition of investment and investor, introduces exceptions to the expropriation provision and clarifies the NT provision and investor responsibilities as well as the right of host countries to regulate investment. These amendments are in the process of ratification.

3. Replacing "outdated" treaties

Treaty replacements offer an opportunity to undertake a comprehensive revision of the treaty instead of selectively amending individual clauses.

This reform action replaces "outdated" IIAs by substituting them with new ones. New IIAs can be concluded by the same treaty partners (e.g. when one BIT is replaced by a new BIT), or by a larger group of countries (e.g. when several BITs are replaced by a plurilateral treaty – see option 4). Approaching the treaty afresh enables the parties to achieve a higher degree of change (vis-à-vis selective amendments) and to be more rigorous and conceptual in designing an IIA that reflects their contemporary shared vision (table 12).

For replacement to be effective, countries need to be mindful of termination provisions in the earlier IIA, including how to ensure effective transition from the old to the new treaty regime (box 4) and how to deal with any survival clause (box 5).

To date, about 130 BITs have been replaced, mostly by other BITs or bilateral TIPs. Countries that have been active in this respect over the past 20 years include Germany, followed by China, Egypt, Romania and Morocco. Replacement treaties do not always incorporate elements of sustainable development-oriented reform. Current replacement

Table 12. Reform action: Replacing "outdated" treaties

Substitutes an old treaty with a new one	
Outcomes (pros)	**Challenges (cons)**
• Allows for a holistic approach to reform through a comprehensive revision of the treaty in line with the contracting parties' evolving policy objectives • Allows for the revision of the treaty's philosophy and overall design and the inclusion of new policy issues • Can be done at any time during the lifetime of the treaty	• Requires participation of a treaty partner or partners with similar views • Can be cost- and time-intensive, as it involves the negotiation of the treaty from scratch • Does not guarantee inclusion of reform-oriented elements (depends on the negotiated outcome) • Requires effective transition between the old and the new treaties

Source: UNCTAD, *WIR17*.

Box 4. Transition clauses

To ensure a smooth transition from the old to the new regime and prevent situations in which both apply concurrently, it is important to delineate clearly the respective treaties' scope of temporal application, e.g. by means of transition clauses. Such clauses clarify in which situations and for how long after an old IIA's termination an investor may invoke the old IIA to bring an ISDS case. Often such periods are limited to three years. Transition clauses typically modify the operation of survival clauses in the outgoing IIA (box III.5). They also ensure that investors do not fall between the cracks but remain protected throughout the transition from the old to the new IIA regime.

Anecdotal evidence suggests that only a minority of replacement IIAs contain transition clauses and that their prevalence is growing in recent regional and plurilateral IIAs. Treaty partners that are known to have used transition provisions at least once include Australia, Canada, Chile, the EU, the Republic of Korea, Mexico, Panama, Peru, Singapore and Viet Nam. Examples of transition clauses can be found in the Peru–Singapore FTA (2008) (Article 10.20), Australia–Chile FTA (2008) (Annex 10-E), Canada–EU CETA (2016) (Article 30.8) and other treaties.

Source: UNCTAD, *WIR17*.

Box 5. Survival clauses

Survival clauses, included in most BITs, are designed to extend a BIT's application for an additional period (some for 5 years, but most commonly for 10, 15 or 20 years) after treaty termination. Survival clauses apply to investments made prior to the date of termination but cover governmental measures adopted both before and after the date of termination (for the duration of the survival period). There are two main types of survival clauses: some are formulated to apply to unilateral treaty termination only (type 1); others do not make it clear whether they are limited to cases of unilateral termination or also apply to joint termination by the parties (type 2). Unilateral treaty terminations will invariably trigger the survival clause. In joint terminations, the situation is less clear: the survival clause may or may not be triggered, depending on its formulation (type 1 or 2) and whether it has been neutralized by the treaty parties at the time of termination.

To date, two known ISDS cases have been filed pursuant to BITs that had been jointly terminated (without replacement by a new treaty) by the contracting parties: *Marco Gavazzi and Stefano Gavazzi v. Romania* (ICSID Case No. ARB/12/25), filed in 2012 under the Italy–Romania BIT (1990), jointly terminated on 14 March 2010; and *Impresa Grassetto SpA, in liquidation v. Republic of Slovenia* (ICSID Case No. ARB/13/10), filed in 2013 under the Italy–Slovenia BIT (2000), jointly terminated on 10 June 2009. In both cases, the tribunals have issued their jurisdictional decisions, but their texts were not public at the time of writing. Available evidence suggests that both proceedings are going forward, i.e. that the tribunals dismissed any jurisdictional objections raised. It is unknown, however, whether the respondent States in these two cases raised an objection based on the purported inapplicability of the survival clause.

Given the lack of certainty on the matter, when jointly terminating an IIA countries are well advised to clarify their intention with regard to the survival clause, either by explicitly amending and/or suppressing it (neutralization), or explicitly confirming that they wish for the survival clause to apply. For instance, the survival clause was neutralized by the parties' express agreement in the context of the joint termination of the Argentina–Indonesia BIT (1995) as well as the joint termination of several BITs between the Czech Republic and several other EU member States.

Source: UNCTAD, *WIR17*.

examples include the ongoing renegotiation talks between Mexico and Switzerland on a treaty that will replace their BIT of 1995.

Of the 167 TIPs sampled, only 16 treaties – or 10 per cent – replaced at least one BIT they overlapped with. For example, Peru replaced three of its old BITs with subsequent FTAs that it concluded with the same partners, namely Chile (2006), Singapore (2008) and the Republic of Korea (2010). All three FTAs include an investment chapter, expressly provide for the termination of the prior BIT upon the FTA's entry into force and establish transition rules.

Alternatively, in rare instances some States suspend old BITs (or parts thereof) for the time that the new IIA is in force (e.g. Canada–Panama FTA (2010), Morocco–United States FTA (2004), European Free Trade Association (EFTA)–Republic of Korea Investment Agreement (2005)). This is not replacement per se, but rather a "conditional replacement", which leaves open the possibility that the old BIT may be revived if the new IIA is terminated.

4. Consolidating the IIA network

Abrogating multiple old BITs and replacing them with a new plurilateral IIA helps to modernize treaty content and reduce fragmentation of the IIA network at the same time.

Consolidation is a form of replacement (see option 3). It means abrogating several pre-existing treaties and replacing them with one single new, modern and sustainable development-oriented one. From an IIA reform perspective, this is an appealing option as it has the dual positive effect of modernizing treaty content and reducing fragmentation of the IIA network (i.e. establishing uniform treaty rules for more than two countries) (table 13).

For the EU, for example, whenever it signs an IIA with a third country, this new treaty replaces all BITs previously concluded with that country by individual EU member States. The Canada–EU CETA (2016), for example, is scheduled to replace eight prior BITs between Canada and EU member States (Article 30.8). Similar provisions are included in the EU's recently negotiated FTAs with Singapore (12 pre-existing BITs to be replaced) and Viet Nam (22 pre-existing BITs to be replaced).

Another example is the Mexico–Central America FTA concluded in 2011 (Costa Rica, El Salvador, Guatemala, Honduras, Mexico and Nicaragua), which replaced three earlier FTAs that were in place between Mexico and the other participating countries (i.e. Costa

Table 13. Reform action: Consolidating the IIA network

Abrogates two or more old BITs between parties and replaces them with a new, plurilateral IIA

Outcomes (pros)	Challenges (cons)
• Allows for a holistic approach to IIA modernization through a comprehensive revision of the treaty • Reduces fragmentation of the IIA network by decreasing the number of existing treaties • May be more cost-effective and time-efficient than pursuing multiple bilateral negotiations	• Requires the participation of numerous treaty partners • Does not guarantee inclusion of reform-oriented elements (depends on the negotiated outcome) • May be more difficult to achieve outcomes in plurilateral negotiations than in bilateral ones

Source: UNCTAD, *WIR17*.

Rica–Mexico FTA (1994), Mexico–Nicaragua FTA (1997) and El Salvador–Guatemala–Honduras–Mexico FTA (2000)).

However, most other plurilateral IIAs have missed the opportunity for consolidation and, instead, have led to parallel application of the new and old treaties. This adds complexity and inconsistency to an already highly complex system (*WIR14*). Some of these IIAs employ conflict clauses to manage overlapping treaty relationships (see option 5). Others adopt a default approach of parallelism but grant flexibility to the parties to decide between themselves. For example, in the TPP context, Australia separately agreed to terminate its BITs with Mexico, Peru and Viet Nam upon the entry into force of the TPP. Other TPP parties have thus far decided to keep their pre-existing IIAs in place (the number of IIAs with investment commitments between TPP parties that overlap with the TPP exceeds 20). In some ongoing plurilateral negotiations, the issue is still up for debate. For example, in Africa, the COMESA–EAC–SADC Tripartite FTA has the potential to replace more than 100 existing BITs between the participating States (see above box 3).

As with replacement generally, when opting for consolidation, countries need to be mindful of termination provisions in the outgoing IIAs and ensure an effective transition from the old to the new treaty regime (see option 3).

5. Managing relationships between coexisting treaties

Where countries opt for maintaining both old and new treaties in parallel, IIA reform objectives will be achieved only if – in the event of conflict or inconsistency – the new, more modern IIA prevails.

Instead of opting for replacement, some treaty parties decide that their old and new treaties should exist in parallel (table 14). This often appears to be the case when the new treaty is plurilateral (e.g. a regional FTA with an investment chapter), and the old, underlying treaties are bilateral. For instance, of the sample of 167 TIPs, more than two thirds (119) coexist with prior, overlapping IIAs. Generally, such parallelism adds complexity to the system and is not conducive to IIA reform. For the purpose of effective and comprehensive IIA reform, the better approach would be to avoid parallel application of coexisting IIAs between the same parties. However, States may have their reasons to opt for coexisting IIAs.

Table 14. Reform action: Managing relationships between coexisting treaties

Establishes rules that determine which of the coexisting IIAs applies in a given situation

Outcomes (pros)	Challenges (cons)
• Ensures that countries are not subject to simultaneously applicable obligations found in overlapping treaties • May aid reform efforts by ensuring that the more recent treaty prevails • While keeping the earlier treaty "alive" (i.e. creating parallelism), clarifies the new treaty's relationship with the earlier one	• Does not terminate the earlier treaty • Only mitigates the adverse consequences arising from coexistence; does not advance effective and comprehensive IIA reform • Impact dependent on the formulation used in the conflict clause

Source: UNCTAD, *WIR17*.

To mitigate potentially adverse consequences arising from this situation, States can include clauses that clarify the relationship between the coexisting IIAs.[11] For example, a conflict clause may specify which of the treaties prevails in case of conflict or inconsistency. Only about 35 treaties, or roughly one third of the 119 TIPs that overlap with coexisting IIAs, contain a clause explicitly allocating priority to either the existing or the new IIA.

Conflict clauses may be a useful tool for IIA reform if they prioritize new, more modern IIAs. For instance, of the 35 TIPs examined that contain conflict clauses, more than half (20) prioritize the newer IIA in cases of inconsistency. Examples include the Colombia–Republic of Korea FTA (2013) (Article 1.2(2)), the Mexico–Peru FTA (2011) (Article 1.3(2)) and the Panama–Taiwan Province of China FTA (2003) (Article 1.03(2)).

However, States often also opt to include clauses that give explicit priority to the earlier (often less reform-oriented) treaty (e.g. the Australia–Malaysia FTA (2012) (Article 21.2(2)) or the China–Japan–Republic of Korea Trilateral Investment Agreement (2012) (Article 25)).

In fact, 15 of the above-mentioned 35 TIPs give priority to the earlier treaty. States sometimes also include clauses that yield priority to the treaty that is more favourable to investors (e.g. side letters to the TPP signed by New Zealand with Australia, Brunei Darussalam, Chile, Malaysia, Singapore and Viet Nam) or that do not provide full clarity but leave open the question about the status of the pre-existing IIA (e.g. China–Republic of Korea FTA (2015) (Article 1.3)). These types of relationship clauses do little to promote IIA reform.

The challenge of managing relationships is also relevant for IIAs with distinct (but overlapping) coverage and for different chapters within an IIA. As rules on services and investment typically interact and overlap to some extent (e.g. Article I.2 of the General Agreement on Trade in Services, covering the so-called Mode 3 of services supply), it may be necessary to regulate this interaction. States have several options at hand. First, they may opt for overlapping coverage and use conflict clauses, providing that in case of inconsistency between the investment chapter and other chapters of an FTA, the other chapters prevail (e.g. Australia–United States FTA (2004) (Article 11.2)). Another option is to cover investment in services by both the services and investment chapters, but exclude certain investment protection obligations (typically NT and MFN) from the application to services investment (e.g. EFTA–Singapore FTA (2002) (Article 38(2) and (3)). States may also include a "Services-Investment" linkage clause in the services chapter that specifies which investment obligations apply mutatis mutandis to measures affecting the supply of services (e.g. India–Singapore Comprehensive Economic Cooperation Agreement (2005) (Article 7.24)). Or they may carefully delineate the scope of application, regulating the interaction in either the services or the investment chapter (e.g. excluding Mode 3 of services supply from the scope of the services chapter Article 10.1 TPP (2016)).

6. Referencing global standards

In their IIA reform efforts, countries can refer to multilaterally recognized standards and instruments. Such instruments reflect broad consensus on relevant issues and referencing them can help overcome the fragmentation between IIAs and other bodies of international law and policymaking.

IIAs are currently the most prominent tools that deal with foreign investment (at bilateral, regional, plurilateral and multilateral levels). However, international policymaking has also resulted in numerous other standards and instruments that may or may not be binding and – directly or indirectly – concern international investment (table 15 and table 16). In September 2015, for example, the global community adopted the 17 SDGs, and several of the 169 targets note the important role of investment for achieving these global objectives (e.g. Goal 7 target 7.a or Goal 10 target 10.b) or related to investment policy (e.g. Goal 1 target 1.b, Goal 17 targets 17.14, 17.15, 17.16). Similarly, in the 2015 Addis Ababa Action Agenda (AAAA), the outcome document of the Third UN Conference on Financing for Development (FfD), member States noted (in paragraph 91) that "[t]he goal of protecting and encouraging investment should not affect our ability to pursue public policy objectives. We will endeavour to craft trade and investment agreements with appropriate safeguards so as not to constrain domestic policies and regulation in the public interest."

Noteworthy is also UNCTAD's Investment Policy Framework for Sustainable Development, a non-binding framework that aims at making investment work for sustainable development and inclusive growth. Developed in 2012, and re-launched in updated form at the 2015 FfD Conference, the UNCTAD Policy Framework has since served as a point of reference for policymakers in more than 130 countries.

To this must be added numerous voluntary and regulatory initiatives to promote CSR standards and guidelines that foster sustainable development (e.g. ISO 26000 "Social responsibility", the UN Global Compact). Such instruments are a unique and rapidly evolving dimension of "soft law". They typically focus on the operations of MNEs and, as such, have increasingly shaped the global investment policy landscape over the last decades (*WIR13*).

Although some uncertainty remains about the role and weight that international arbitration tribunals would give to such instruments, policymakers have certain options for harnessing these global standards for IIA reform. For example, they can take the following actions:

- Introduce (e.g. by means of cross-referencing) global standards and instruments in their new IIAs, as a small, but growing number of agreements already do. Such clauses

Table 15. Reform action: Referencing global standards

Fosters coherence and improves the interaction between IIAs and other areas of law and policymaking

Outcomes (pros)	Challenges (cons)
• Can help shape the "spirit" (e.g. object and purpose) of the treaty and influence its interpretation by arbitral tribunals • Can inform the modernization of existing treaties and the creation of new ones • Can "reconnect" the different universes of international rules • Cost-effective and time-efficient (countries can make use of existing instruments that the parties have previously agreed to)	• Depending on the global standard at issue, can be seen as "overloading" the IIA regime with issues that are not central to IIAs' traditional objective of protecting foreign investment • Does not necessarily create "legal clarity" or restrict the interpretive discretion of arbitral tribunals • Does not give treaty parties control over future development of the respective instruments

Source: UNCTAD, *WIR17*.

Table 16. Selected examples of global standards with investment relevance

Common reference	Full title	Area of focus
UNFCCC	United Nations Framework Convention on Climate Change, 1771 UNTS 107 (opened for signature 4 June 1992, entered into force 21 March 1994), including the 1997 Kyoto Protocol (entered in force 16 February 2005) and 2016 Paris Agreement (entered in force 4 November 2016)	Climate change
SDGs	Transforming our world: the 2030 Agenda for Sustainable Development, GA Res 70/1, UN GAOR, 70th sess, UN Doc A/RES/70/1 (25 September 2015)	Sustainable development
FfD/AAAA	Addis Ababa Action Agenda of the Third International Conference on Financing for Development (Addis Ababa Action Agenda), GA Res 69/313, UN GAOR, 69th sess, 99th plen mtg, UN Doc A/RES/69/313 (27 July 2015)	Sustainable development
UNCTAD Policy Framework	Investment Policy Framework for Sustainable Development, UN Doc UNCTAD/DIAE/PCB/2015/5 (2015 rev.)	Sustainable development
UN Guiding Principles on Business and Human Rights	Report of the Special Representative of the Secretary General on the issue of human rights and transnational corporations and other business enterprises, John Ruggie, Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework, HRC, UN GAOR, 17th sess, UN Doc A/HRC/17/31, annex I (21 March 2011); see also HRC Res 17/4, UN GAOR, 17th sess, 33rd mtg, UN Doc A/HRC/RES/17/4 (6 July 2011)	Human rights
UN Anti-Corruption Convention	The United Nations Convention against Corruption, GA Res 58/4, UN GAOR, 58th sess, 51st plen mtg, UN Doc A/RES/58/4 (31 October 2003, entered into force 14 December 2005)	Anti-corruption
ILO Tripartite MNE Declaration	Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, adopted by the Governing Body of the International Labour Office at its 204th Session (November 1977), and amended at its 279th (November 2000), 295th (March 2006) and 329th (March 2017) Sessions	Labour rights
Universal Declaration of Human Rights	Universal Declaration of Human Rights, GA Res 217A (III), UN GAOR, 3rd sess, 183rd plen mtg, UN Doc A/810 (10 December 1948)	Human rights
UN Charter	Charter of the United Nations, 1 UNTS XVI (24 October 1945)	International peace, security and development

Source: UNCTAD, *WIR17*.

would – at a minimum – serve to flag the importance of sustainability in investor-State relations. They could also attune investors to their sustainable development-related responsibilities and operate as a source of interpretative guidance for ISDS tribunals.

- Adopt a joint statement, recalling their countries' commitments to certain enumerated global standards and instruments and noting that the investment (policy) relations among the participating countries are to be understood in light of these commitments. The effects would be similar to those of cross-referencing but would apply not only to new, but also to pre-existing treaties. The larger the group of participating countries (and, possibly, the longer the list of global standards), the stronger or the more far-reaching the effect would be.
- Incorporate, at a broader level, global sustainability issues into discussions on global economic governance and the international regulatory architecture for investment.

Overall, cross-referencing can play an important role in reducing fragmentation – and isolation – of different bodies of law and policymaking and can strengthen linkages

between IIAs and international sustainability standards. All of this would help shape global policy understanding, as it applies not only to future investment policymaking, but also to existing treaties.

For instance, several recent IIAs reference CSR standards in a general manner, typically referring to "internationally recognized standards" in areas such as labour, environment, human rights, anti-corruption and the like (e.g. Burkina Faso–Canada BIT (2015); Colombia–Panama FTA (2013)). Meanwhile, other recent IIAs are more specific, referring to global standards such as the SDGs (e.g. Morocco–Nigeria BIT (2016)); the UN Charter, Universal Declaration of Human Rights and/or ILO instruments (e.g. EFTA–Georgia FTA (2016); CETA (2016)); or the Organization for Economic Cooperation and Development (OECD) MNE Guidelines and OECD Principles of Corporate Governance (e.g. CETA (2016); Bosnia and Herzegovina–EFTA FTA (2013)).

A recent example of standard setting in a plurilateral context are the G20 Guiding Principles for Global Investment Policymaking, agreed on by the G20 in July 2016 during the group's Shanghai Ministerial Meeting and endorsed in September 2016 at the Hangzhou Summit (box 6). Being an example of standard setting themselves, the Guiding Principles also reference global standards, notably in Principle VIII which states that "investment policies should promote and facilitate the observance by investors of international best practices and applicable instruments of responsible business conduct and corporate governance".

Box 6. G20 Guiding Principles for Global Investment Policymaking

With the objective of (i) fostering an open, transparent and conducive global policy environment for investment, (ii) promoting coherence in national and international investment policymaking, and (iii) promoting inclusive economic growth and sustainable development, G20 members hereby propose the following non-binding principles to provide general guidance for investment policymaking.

I. Recognizing the critical role of investment as an engine of economic growth in the global economy, Governments should avoid protectionism in relation to cross-border investment.

II. Investment policies should establish open, non-discriminatory, transparent and predictable conditions for investment.

III. Investment policies should provide legal certainty and strong protection to investors and investments, tangible and intangible, including access to effective mechanisms for the prevention and settlement of disputes, as well as to enforcement procedures. Dispute settlement procedures should be fair, open and transparent, with appropriate safeguards to prevent abuse.

IV. Regulation relating to investment should be developed in a transparent manner with the opportunity for all stakeholders to participate, and embedded in an institutional framework based on the rule of law.

V. Investment policies and other policies that impact on investment should be coherent at both the national and international levels and aimed at fostering investment, consistent with the objectives of sustainable development and inclusive growth.

VI. Governments reaffirm the right to regulate investment for legitimate public policy purposes.

VII. Policies for investment promotion should, to maximize economic benefit, be effective and efficient, aimed at attracting and retaining investment, and matched by facilitation efforts that promote transparency and are conducive for investors to establish, conduct and expand their businesses.

VIII. Investment policies should promote and facilitate the observance by investors of international best practices and applicable instruments of responsible business conduct and corporate governance.

IX. The international community should continue to cooperate and engage in dialogue with a view to maintaining an open and conducive policy environment for investment, and to address shared investment policy challenges.

These principles interact with each other and should be considered together. They can serve as a reference for national and international investment policymaking, in accordance with respective international commitments, and taking into account national, and broader, sustainable development objectives and priorities.

Source: UNCTAD, *WIR17*.

7. Engaging multilaterally

Multilateral engagement is the most impactful but also most difficult avenue for IIA reform. When drawing inspiration from current or past multilateral processes, attention should be given to their differences in terms of intensity, depth and character of engagement.

If successful, a global multilateral reform effort would be the most efficient way to address the inconsistencies, overlaps and development challenges that characterize the thousands of treaties that make up today's IIA regime (table 17). That said, multilateral reform action is challenging – in particular, how to pursue it (*WIR15*, *WIR16*).

The recent past has seen a number of policy developments at the multilateral (or plurilateral) level that can inspire future multilateral IIA reform efforts. Inspiration can be found in both the way the "new rules" were developed and the processes or "tools" employed to extend the new rules to existing treaties. In this regard, multilateral rulemaking processes in areas others than IIAs (e.g. the OECD-based base erosion and profit shifting (BEPS) project) may also be instructive.

When considering to what extent lessons can be learned from these initiatives, attention needs to be given to the characteristics of various multilateral processes. Differences may exist regarding, inter alia, the scope and breadth of content covered, the number of countries involved (during rule creation and for later rule application), its legal nature (both of the actual rules and the mechanism used to foster broader application) and the extent to which such processes are institutionalized or hosted by an intergovernmental organization.

For example, the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration (the Mauritius Convention) fosters greater application of the UNCITRAL Transparency Rules to IIAs concluded prior to 1 April 2014. The Mauritius Convention effectively modifies a number of first-generation IIAs (of those countries that have ratified the Convention), which turns it into a collective IIA reform action.[12] Future IIA reform actions could draw upon (i) the process of multilateral negotiations that led to the UNCITRAL Rules and the Mauritius Convention and (ii) the Mauritius Convention's opt-in mechanism, which modifies certain aspects of pre-existing IIAs.

Table 17. Reform action: Engaging multilaterally

Establishes a common understanding or new rules between a multitude of countries, coupled with a mechanism that brings about change "in one go"

Outcomes (pros)	Challenges (cons)
• Among reform options, is best suited for dealing with policy issues of global relevance (e.g. sustainable development) or systemic issues (e.g. MFN clause) • If successful, is the most efficient type of reform action as it brings about change "in one go" for a multitude of countries or treaty relationships • Can help avoid further fragmentation arising from individual countries' piecemeal reform actions	• Is the most challenging reform path as consensus among many countries is hard to achieve • Can lead to a situation in which countries with small bargaining power or latecomers find themselves in the role of "rule-takers" • Is more likely to result – at least at the current stage – in non-binding instruments or instruments with a narrow substantive scope (e.g. individual aspects of ISDS); therefore has a limited overall impact on the IIA universe

Source: UNCTAD, *WIR17*.

Beyond the investment regime, the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (the BEPS Multilateral Instrument) fosters States' implementation of the tax treaty related measures of the Final BEPS Package, potentially amending over 3,000 bilateral tax treaties concluded thus far. The BEPS Multilateral Instrument deals with a number of issues of concern (e.g. hybrid mismatch arrangements, treaty abuse, streamlining dispute resolution) and creates change in a flexible, à la carte way. For example, the BEPS Multilateral Instrument will apply only to the tax treaties specifically designated by the parties to the Convention, and it uses opt-out mechanisms that allow parties to exclude or modify the legal effects of certain provisions. Choices between alternative provisions and opt-in mechanisms give the possibility of taking on additional commitments.[13] Future IIA reform actions could draw upon (i) the multilateral stakeholder process that led to the adoption of the Final BEPS Package; and (ii) the treaty's architecture, which is similar to (but more complex than) the Mauritius Convention, allowing for unilateral declarations, and selective reservations to or amendments of pre-existing tax treaties.

Current discussions on the establishment of a multilateral investment court and/or appellate mechanism could result in an instrument that ultimately changes ISDS provisions included in earlier treaties. The opt-in technique of the Mauritius Convention as a potential model for reform has also been explored in recent consultations that have examined the establishment of a permanent investment tribunal or an appellate mechanism (see above chapter III.B., Reforming investment dispute settlement). Another example for a multilateral reform action is the current ICSID Rules amendment process, drawing on input received from States, the private sector and the public, as well as the experience of the ICSID Secretariat.

Yet another example are the G20 Guiding Principles on Global Investment Policymaking, adopted with the backstopping of UNCTAD. Although non-binding, the principles are meant to serve as an important reference for negotiating IIAs and modernizing existing ones. They could effectively be the touchstone for global reform of the existing IIA regime and for the formulation of a new generation of IIAs, more appropriately aligned with 21st century concerns and priorities. Inspiration may be found in suggestions that (i) the principles may not only give guidance to treaty drafting but, by stating the G20 members' shared understanding of today's investment policymaking priorities, may also offer guidance for the interpretation of existing IIAs; and (ii) they may lay the basis for their broader application to countries other than members of the G20.

Finally, multi-stakeholder platforms and processes such as UNCTAD's WIFs, the international forum for high-level and inclusive discussions on today's existing multi-layered and multifaceted IIA regime, and the FfD, mandating UNCTAD to continue consultations with member States on IIAs, are useful as a platform for the expert research, analysis, backstopping and exchange on how to carry reform further.

8. Abandoning unratified old treaties

A relatively large number of BITs, many of them old, have not yet entered into force. A country can formally indicate its decision not to be bound by them as a means to help clean up its IIA network and promote the negotiation of new, more modern treaties.

Table 18. Reform action: Abandoning unratified old treaties

Conveys a country's intent not to become a party to a concluded but as yet unratified treaty

Outcomes (pros)	Challenges (cons)
• Can help clean up a country's IIA network • Is procedurally simple, requiring only a notice to the other parties • Can send a reform message to other treaty parties and the public	• Could be perceived as negatively affecting the country's investment climate • Could disturb relations with other treaty parties • May not affect existing cases arising from provisional application • May not affect future ISDS claims (during the survival clause period) if a country accepted provisional application pending ratification

Source: UNCTAD.

Under international law, countries are "obliged to refrain from acts which would defeat the object and purpose of a treaty" they have signed, even before the said treaty enters into force (VCLT Article 18). Formally "abandoning" a treaty ("abandonment" being used as a colloquial and legally neutral term) would make certain that a country has released itself from that obligation. This is usually a straightforward process because the treaty is not in force (table 18).

To date, few countries are known to have undertaken this reform action, though not all cases may have received public attention. Brazil abandoned 14 BITs signed in the 1990s after some of them were rejected by its Congress, as certain provisions were deemed unconstitutional. In 2008, Ecuador "denounced" two unratified BITs (with Honduras and Nicaragua). Most recently, in January 2017, the United States publicly stated its intention not to become a party to the TPP.[14]

However, in certain treaties, countries agree to "provisional application", which means that the treaty (or part of it) is applied after its signature but before its entry into force. Relinquishing a provisionally applied treaty is usually more complicated, as it comes close to terminating a treaty that has entered into force. Typically, the IIA will stipulate a process that a country must follow in order to terminate provisional application; this may also trigger the operation of a survival clause (see above box 5). Provisional application is more common in plurilateral IIAs (e.g. the Energy Charter Treaty (ECT) (1994); Canada–EU CETA (2016)) as ratification by multiple parties is likely to be a protracted process.

For example, in 2009, the Russian Federation issued a notice to terminate the provisional application of the ECT (the treaty contains a separate 20-year survival clause for signatories terminating provisional application).

9. Terminating existing old treaties

Terminating "outdated" BITs – whether unilaterally or jointly – is a straightforward (although not always instantaneous) way to release the parties from their obligations.

Terminating a treaty releases the parties from the obligation to further perform according to it (this differs from a treaty's termination due to its replacement by a new one, see options 3 and 4). A treaty can be terminated unilaterally (when the treaty permits) or by mutual consent (at any time). Rules for unilateral treaty termination are often set out in the BIT itself. Typically, BITs set out an initial period of operation of between 10 and 20

years, which must expire before a party may unilaterally terminate the treaty. Unilateral termination will trigger the survival clause (if existing in the treaty), which will prolong the treaty's operation for a set time after it has been terminated (table 19). For the sake of clarity, countries may consider neutralizing the survival clause when terminating a treaty jointly (see above box 5).

Of 212 BITs terminated as of March 2017, 19 treaties (9 per cent) were jointly terminated, without any replacement or consolidation; another 59 (28 per cent) were unilaterally terminated, while 134 (63 per cent) were replaced by a new treaty (figure 18). This suggests that countries are often receptive to termination, but generally when it is part of the process of concluding a new IIA. Noteworthy is also the process of termination of intra-EU BITs (*WIR17*).

Over the past decade, several countries have terminated their BITs (unilaterally or jointly); examples include the Plurinational State of Bolivia (10), Ecuador (10), and Indonesia (at least 20). The Argentina–Indonesia BIT (1995) provides an instance in which the parties have agreed to terminate the treaty while at the same time extinguishing the survival clause. South Africa has terminated 9 BITs, as part of the country's broader move to reshape its investment policy in accordance with its objectives of SD and inclusive economic growth; this also includes the adoption of the Promotion and Protection of Investment Act (*WIR16*), the formulation of a new Model BIT, and engagement at the

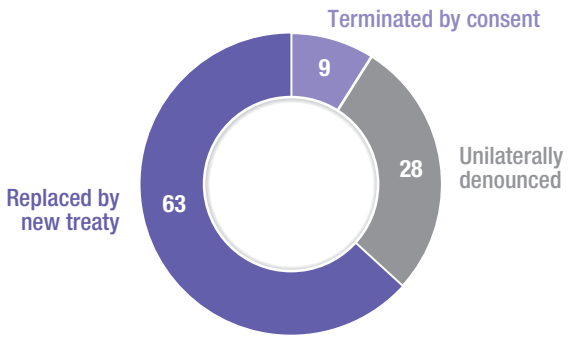
Table 19. Reform action: Terminating existing old treaties

Releases the parties from their obligations under the treaty

Outcomes (pros)	Challenges (cons)
• Can be unilateral or joint termination (without replacement by a new treaty)	• Could be perceived as worsening the investment climate in the terminating country or countries
• Sends a strong signal to reform-oriented domestic stakeholders and critics of the IIA regime	• Could result in investors of one party no longer being protected in the other party's territory
• Can promote sustainable development-oriented reform, if part of a coordinated, joint replacement strategy	• Might not be instantaneous if a survival clause is triggered (i.e. ISDS exposure remains for the duration of the survival clause period)

Source: UNCTAD, *WIR17*.

Figure 18. Terminated BITs, by type of termination as of March 2017
(Per cent)



Source: UNCTAD, IIA Navigator.
Note: Based on 212 terminated BITs (excluding expired BITs).

regional and continental levels, as well as in multilateral dialogues (*WIR17*). India revised its earlier Model BIT and adopted a new Model BIT at the end of 2015. Consequently, in 2016, India sent notices of termination to more than 50 treaty partners with whom the initial treaty term has expired with the intention to renegotiate a new treaty based on the revised Model BIT. India has already started to renegotiate with various countries. Recently, in May 2017, Ecuador's National Assembly approved the termination of 16 BITs and Ecuador's President signed the decrees formally terminating them.

10. Withdrawing from multilateral mechanisms

Unilateral withdrawal from an investment-related multilateral mechanism (e.g. the ICSID Convention) can help reduce a country's exposure to investor claims but may also create challenges for future multilateral cooperation on investment.

Unilateral withdrawal from an investment-related multilateral mechanism releases the withdrawing party from the instrument's obligations and – depending on the instrument at issue – can help minimize a country's exposure to investor claims (table 20). Unilateral withdrawal can also signal the country's apparent loss of faith in the system and a desire to exit from it (rather than reform it). It can show a preference for an alternative dispute settlement forum – for instance, a regional one (e.g. Union of South American Nations or UNASUR).

So far, two countries have withdrawn from the ECT, a treaty with over 50 signatories that has been used more frequently than any other IIA to bring ISDS cases. In 2009, the Russian Federation submitted its notice to terminate provisional application and declare its intention not to become party to the ECT. In 2014, Italy filed a notice of denunciation of the ECT, which took effect on 1 January 2016 (unlike the Russian Federation, Italy had ratified the ECT and was a fully fledged party to it). The ECT contains two separate 20-year survival clauses: for signatories that applied the treaty on a provisional basis and for fully fledged parties. The ICSID Convention has to date been terminated by three countries – the Plurinational State of Bolivia in 2007, Ecuador in 2009 and the Bolivarian Republic of Venezuela in 2012. All three had had multiple treaty-based investor claims filed against them at ICSID, with high financial stakes.

Table 20. Reform action: Withdrawing from multilateral mechanisms

Releases the withdrawing parties from the instrument's binding force	
Outcomes (pros)	**Challenges (cons)**
• Can help narrow a country's exposure to (future) investor claims (subject to the denounced treaty's survival clause and without prejudice to investor claims under other IIAs or before other international fora) • May reduce annual expenditures (e.g. if the treaty requires annual contributions) • Can be a second-best solution for countries that would prefer to reform the existing treaty, but cannot do so alone	• Could be perceived as negatively affecting the country's investment climate and/or could put the country into an "outsider" position • Deprives the country of further cooperation with other treaty partners and the opportunity to have a word in the evolution of the agreement • Applies prospectively only • Since most IIAs provide consent to multiple fora for ISDS, may not eliminate the risk of ISDS claims entirely • Could narrow protection for nationals investing abroad

Source: UNCTAD, *WIR17*.

V. PHASE 3 OF IIA REFORM: IMPROVING INVESTMENT POLICY COHERENCE AND SYNERGIES

UNCTAD's REFORM PACKAGE
FOR THE
INTERNATIONAL INVESTMENT REGIME

A. Improving investment policy coherence and synergies

Alongside improving the approach to new treaties and modernizing existing treaties, governments need to improve investment policy coherence and synergies. Striving for coherence does not always imply legal uniformity – inconsistencies and differences may be intended – but different policy areas and legal instruments should work in synergy.

Phase 3 of IIA Reform aims at enhancing investment policy coherence and synergies, a challenge that is also identified as the fifth priority area for IIA reform (see chapter II.B of this Reform Package). Phase 3 of IIA Reform addresses this policy challenge holistically across three dimensions:

- first, ensuring internal consistency within the country's IIA network;
- second, maximizing synergies between IIAs and the national legal framework for domestic and foreign investment;
- third, managing the interaction between IIAs and other bodies of international law that also touch upon investment.

For each dimension, policy interaction manifests itself in different ways, gives rise to different challenges and requires different solutions in line with countries' specific national development priorities. This chapter takes stock of the status quo, outlines potential challenges and offers policy responses.

Two issues merit particular consideration:

First, policy coherence does not necessarily require uniform legal language. Rather, mutually supportive policies allow countries the flexibility to decide, on a case-by-case basis and in line with their national development strategies (guided by the UNCTAD Investment Policy Framework's Core Principles), where on the scale between consistency and divergence individual policy interactions should be placed. Factors influencing this choice include strategic considerations, evolution over time and capacity.

Second, achieving a satisfactory level of investment policy coherence is not instantaneous. For example, a country's shift towards sustainable development-oriented investment policymaking will almost always produce a temporary phase of inconsistency. Such temporary inconsistency should not discourage investment policy reform. Instead, it should create momentum and foster more rapid and dynamic reform.

Working towards maximizing synergies from policy interactions in a regime consisting of thousands of investment treaties, national laws regulating domestic and foreign investment, and other bodies of international law affecting investment is a significant challenge for all countries, and for developing countries and LDCs in particular. This challenge calls for responses through a combination of individual, bilateral, regional and multilateral reform steps. Such steps should reflect on evidence-based policy analysis and, for many countries, may require backstopping through technical assistance and advisory services. UNCTAD can offer comprehensive support through its three pillars of (i) research and policy analysis, (ii) capacity-building and advisory services, and (iii) intergovernmental consensus-building.

B. Enhancing coherence within national IIA networks

At the country level, an incoherent IIA network (one that displays gaps, overlaps and inconsistencies, including with respect to sustainable development elements) can expose the host State to undesirable effects.

Among other things, it increases the country's vulnerability in ISDS because of "nationality planning" by investors and possibilities of MFN-based importation of treaty provisions from "old-generation" IIAs into modern treaties. Countries need to review their treaty networks, decide upon and implement actions required to improve coherence across their IIA networks. UNCTAD's 10 Reform Options (Phase 2) as well as its advisory activities can be helpful in this regard.

1. Coherence in a country's IIA network: Main divergences and influencing factors

The systemic complexity of countries' IIA networks manifests itself in lack of consistency, gaps in coverage and sometimes overlapping commitments of individual IIAs. The incoherence within the regime is becoming even more pronounced since sustainable development-oriented treaty drafting has been creating a new generation of investment treaties.

In terms of content, the main divergences between treaties relate to the following elements:

- the scope of the treaty (e.g. definitions of investment and investor, subject-matter exclusions from scope, expansion of certain obligations to the pre-establishment phase);
- the types and breadth of investment protections (e.g. FET, performance requirements, "umbrella" clause);
- the clarifications to key treaty obligations (e.g. refinements to FET, MFN or indirect expropriation clauses);
- the types and breadth of exceptions from treaty obligations (e.g. for public policy objectives, essential security, balance of payments problems);
- the approach to regulating investor responsibilities; and
- the way in which investment disputes are to be settled (whether ISDS is available, and if so, what are the conditions of access, relevant procedures etc.).

Additionally, differences arise among various types of IIAs, such as those focusing on investment protection (e.g. "typical" BITs), investment liberalization (e.g. "pre-2009" EU FTAs), investment facilitation (e.g. CFIAs), and investment cooperation (e.g. trade and investment framework agreements). And finally, there is the broader question about the extent to which sustainable development is embedded in investment treaty making.

Academic research has analysed countries' treaty network consistency, identifying front-runners (i.e. countries with a particularly high treaty network consistency) and laggards (i.e. countries with a particularly high level of treaty network inconsistency).[15] This research has revealed that some countries with higher GDP per capita exhibit more consistency across their IIAs.

Higher GDP per capita, potentially associated with greater economic and bargaining power, may be one, but not the only, reason for treaty network consistency. Other factors that may influence coherence within countries' IIA networks include:

- Model treaties (whether the country has developed a model treaty and if so, how determined it is to not deviate from it in the course of negotiations);
- Human capacity (the capacity and skills of IIA negotiators to negotiate and maintain a coherent IIA network over time);
- Conscious changes in national policy over time (whether the country has significantly changed its model treaty over time);
- Regionalism (whether countries party to a regional economic arrangement follow a common policy in IIA negotiations with third parties, see box 7);
- Policy position towards overlapping treaties (whether new regional/plurilateral agreements terminate or preserve pre-existing bilateral treaties among the contracting States);
- Public scrutiny of negotiating processes and outcomes (e.g. the scale and relevance of negative public perception and input from civil society when a country deviates from its announced IIA strategy or model in its treaties with third parties).

This suggests that advanced economies generally have the capacity to design IIA policy and develop a model treaty in accordance with their own national preferences and reflecting their investment policy priorities and objectives. Inconsistencies in treaty networks of those countries often result from the conscious changes in their approach to designing investment treaties over time. Smaller developing countries, on the other hand, often conclude IIAs that are based on other parties' treaty models, resulting in more intense undesired incoherence in terms of content, scope and approach to investment commitments.

Box 7. Efforts towards investment policy coherence in the EU

In the Lisbon Treaty (2007), European Union (EU) Member States transferred exclusive competence over FDI to the EU, as part of its common commercial policy. (As now confirmed by the European Court of Justice (ECJ), the EU has the exclusive competence to negotiate new IIAs with third States on behalf of its Member States, with the exception of portfolio investment and investor-to-State dispute resolution mechanism, which remain shared competencies.)

Investment treaties, negotiated by the EU Commission since that time, include numerous sustainable development features and reflect many of UNCTAD's reform-oriented policy options. The EU also offers examples of, and lessons for mechanisms aimed at ensuring policy coherence in a regional setting.

First, regarding overlap between a new EU-wide treaty and pre-existing BITs. When the EU concludes a new IIA with a third country or countries, this treaty also provides for the termination of pre-existing, overlapping BITs concluded by individual EU Member States with the respective third party (see e.g. CETA Art. 30.8). The aim is to progressively replace the EU Member States' old-generation BITs concluded with non-EU countries, which still account for a significant part of the BITs concluded worldwide.

Second, regarding EU Member States' new BITs. If an EU Member State wishes to negotiate a new BIT with a third State, it needs to obtain authorization from the EU Commission. This helps to ensure consistency with the EU's revised approach, as the EU may require the Member State to include or remove specific clauses or modify language in the negotiating draft, if deemed necessary.

Third, regarding intra-EU BITs, i.e. BITs concluded by EU Member States with third countries, which in turn have become EU Member States in the meantime. The European Commission has been requesting for some time that EU Member States terminate their intra-EU BITs (see WIR17, box III.6). In a recent ruling, the European Court of Justice found that ISDS clauses in intra-EU BITs were incompatible with EU law.[16]

Source: UNCTAD.

2. Challenges arising from incoherence between IIAs

Lack of intra-IIA coherence gives rise to a number of challenges (table 21). In particular, it increases States' exposure to and vulnerability in ISDS proceedings. This is due to two practices, both related to treaty shopping: first, corporate structuring of investment through a State that is perceived to have the most investor-friendly IIA with the host State ("nationality planning"); and second, "importation" of more investor-friendly provisions from other IIAs by invoking the MFN clause in the applicable IIA. Both of these practices have the potential to undermine sustainable development reform efforts in more modern treaties. This Reform Package offers specific policy options designed to eliminate or reduce the opportunities for both "nationality planning" and using the MFN clause in the way described (see above chapter III.A.).

Beyond treaty shopping, IIA incoherence can also create difficulties in managing treaty networks. Ensuring compliance with a patchy regime of different treaties may be particularly challenging for smaller States, for those States that experience resource constraints, and for those that have a particularly large set of incoherent treaties. Certain difficulties in "managing" treaty networks can also be experienced by investors, notably SMEs with resource limitations: they may find it difficult to determine which rights they have in a situation where there is more than one potentially applicable IIA.

Inconsistencies in a country's treaty network may also reduce the country's bargaining power in negotiations of new treaties. Having agreed to a certain (undesired) clause in one existing IIA, the country may find it difficult to argue against the inclusion of the same clause in future negotiations.

Lastly, intra-IIA incoherence may further reduce predictability in ISDS outcomes. To illustrate, if the same provision (e.g. definition of investment) is formulated somewhat differently in the country's different IIAs, an arbitral interpretation of this provision in one treaty will not be applicable to other treaties. Furthermore, empirical research demonstrates that arbitral tribunals may draw inferences from the inconsistencies of the host State's agreements with third States when interpreting the applicable IIA. For example, the fact that a modern FET clause in the State's recent treaty excludes "legitimate expectations" may be taken by the arbitral tribunal to suggest that the unqualified FET clause in the older IIA (applicable in the case) does cover legitimate expectations.[17]

Table 21. Lack of coherence between IIAs: Policy challenges

Increased exposure to ISDS risks	• "Nationality planning" by investors to obtain the coverage of the "most favourable" IIA • MFN-based "importation" of old-generation clauses from the host State's IIAs with third countries
Difficulties in managing IIA networks by States	• Challenges in ensuring State's compliance with patchy legal regime • Challenges in negotiating future IIAs
Lack of predictability	• Uncertainty and lack of predictability in ISDS outcomes, for States and investors alike, regarding the meaning of IIA provisions

Source: UNCTAD.

3. Policy options

Countries wishing to strengthen coherence of their IIA network can implement a number of actions/steps, including at the individual, bilateral, regional and multilateral levels.

As a starting point, countries' reform steps should be based on fact-based stocktaking of policy incoherence (including its intensity) and an assessment of whether such incoherence needs to be addressed. UNCTAD's policy research tools (e.g. IIA Mapping Project[18]) and its technical assistance and advisory activities (e.g. national IIA network reviews) can assist in conducting such stocktaking exercise.

Thereafter, countries need to decide how to remedy undesirable policy incoherence. This Reform Package can help identify priority areas for reform and identify key IIA clauses that need modernization (Phase 1, see above chapter III). Should change be needed for "old-generation" treaties, the 10 Options for modernizing treaties can help identify the best possible route to take (Phase 2, see above chapter IV.D.).

Beyond national and bilateral action, regional IIA reform, if undertaken properly (with the objective of consolidating investment policies by terminating pre-existing IIAs, and strengthening its sustainable development dimension) can help promote the harmonization of investment rules. The backstopping and support function of regional secretariats can make a positive contribution in this regard.

At the multilateral level, the sharing of experiences and best practices, in particular at UNCTAD's High-level IIA Conferences and biennial WIFs, has a useful role to play.

C. Maximizing synergies between the IIA regime and the national legal framework for investment

Countries' investment policy regimes typically have both a national and an international dimension. Although these dimensions often diverge intentionally, they nevertheless should interact in a way that maximizes synergies, including from a sustainable development perspective.

Shaping such interaction requires a solid understanding of the different objectives, functions and nature of the legal instruments involved. Strengthening cooperation between national and international investment policymakers, improving interaction and ensuring cross-fertilization between the two regimes (including by identifying lessons learned that can be transferred from one policy regime to the other) are crucial tasks for countries striving to create a mutually supporting, sustainable development- oriented investment policy regime.

1. Similarities and differences between IIAs and the national legal framework for investment

When assessing the best possible approaches to fostering synergies between national and international policy dimensions, it is important to recognize key structural and contextual differences. These relate to (i) the context and nature of the two policy regimes, (ii) their overall purpose and scope, (iii) their process of development and (iv) their evolution (table 22).

Table 22. IIAs and national legal and policy frameworks for investment: structural and contextual differences

Differences	IIAs	National legal framework
Context and nature	• Consist of BITs and TIPs, considered the primary international instruments governing foreign investment	• Consists of a broad system of investment-related laws, regulations and policies • May include a national investment law as an important element of the investment policy framework
Purpose and scope	• Offer (substantive and procedural) protections to foreign investors of a particular home country, which may go beyond what is available at the domestic level	• Covers foreign investors from any country; may also cover domestic investors • May offer protection, but can also include other elements, such as promotion, facilitation, admission, liberalization or regulation
Process of development	• Adopted as a result of a negotiation process at the international level, which typically involves bargaining power	• Adopted relatively autonomously by a country and dependent on internal political and legislative processes
SDG-oriented evolution over time	• Subject to global debate on sustainable development-oriented IIA reform • Exhibits reform approaches to IIAs by many States (based on UNCTAD Reform Package)	• Some elements (e.g. environmental laws) at the core of SDG-oriented policy reform • Other elements (e.g. national investment laws) less exposed to SDG discourse

Source: UNCTAD.

IIAs are considered the primary international instrument governing foreign investment, and they operate in a relatively well-defined universe. National legal frameworks for investment consist of a multitude of investment-related laws. Among them, national investment laws are an important element. They are complex and vary from country to country. Although they display significant divergences in their scope and content, some features are relatively consistent among them (box 8), and some contain provisions similar to those of IIAs (*WIR17*; UNCTAD, 2016; UNCTAD Investment Law Navigator).

Yet, to the extent that investment laws have typical IIA clauses, these clauses frequently lack the refinements and clarifications that are characteristic of modern IIA drafting. For example, in investment laws, none of the 17 clauses on indirect expropriation and only 2 of the 9 FET clauses are "refined" (figure 19). For IIAs, these kinds of refinements have become standard features of modern treaty drafting (*WIR17*). Regarding investment dispute settlement, whereas it is typically addressed in IIAs through ISDS, providing advance consent to international arbitration (95 per cent of IIAs), 66 of the 111 national investment laws (59 per cent) refer to international arbitration as a means for settling investor–State disputes; and of those, only 24 laws provide for advance consent to international arbitration (box 8).

Divergence between the two types of instruments is not necessarily undesirable. Importantly, the absence of some IIA-type protection clauses in national laws can be in line with what the national legal framework for investment aims to achieve (e.g. investment promotion or facilitation).

Box 8. A primer on national investment laws

For many developing and transition countries, the investment law is at the core of the domestic regulatory framework for foreign investment. UNCTAD's Investment Laws Navigator shows that at least 109 countries have such a law. Almost all of these are either a developing country (91) or an economy in transition (13), while in developed countries key FDI provisions can be found in various other laws. Of the investment laws, 64 per cent (71 laws) apply to both foreign and domestic investors, whereas the others target foreign investors only (40 laws). Countries in Asia are more likely to have foreign investment laws, whereas most countries in Africa have adopted investment laws that cover both foreign and domestic investors. Most all of the investment laws that are in force were adopted after 1989. Especially in the 1990s (after the end of the Cold War period), many countries (39) embraced new investment laws.

The main objective of investment laws is to promote (foreign) investment by regulating access to the domestic market; stipulating investor rights and guarantees; clarifying access to dispute settlement; setting up institutions, including investment promotion agencies and one-stop-shops; and providing incentives schemes. However, although most investment laws share the same objective and basic structure, they differ considerably in terms of content and quality of key FDI provisions (*WIR17*). Their specific content may also depend on their differing functions[19].

In addition, national investment laws operate within a complex web of domestic laws, regulations and policies that relate to investment (e.g. competition, labour, social, taxation, trade, finance, intellectual property, health, environmental, culture). Investment-related issues are typically also enshrined in countries' company laws, and – sometimes – in countries' constitutions. Accordingly, to the extent a country has an investment law, this law must be assessed in the context of the country's larger policy framework.

Source: UNCTAD Investment Laws Navigator.
Note: Data limited to laws that cover (or aim to cover) the basic legal framework for investment and include key FDI provisions (total is 111). Not included are laws that focus on only one specific element of this framework, such as incentives, access to land or national security.

Figure 19. Selected provisions in national investment laws

Source: UNCTAD.

Against this investment policy landscape, the issue that arises is how to best foster synergies between the national legal framework for investment and the IIA regime.

2. Challenges arising from the interaction between IIAs and the national legal framework for investment

Although national and international investment policymaking is structurally distinct in the ways outlined above, there are instances where the two dimensions interact. Such interaction gives rise to at least three specific challenges:

- Policymakers in charge of national and international investment policies might be operating in silos and create outcomes that are not mutually supportive or, worse, conflicting.
- Incoherence (e.g. between a clearly defined FET clause in one or several IIAs and a broad FET clause in an investment law) may have the effect of rendering IIA reform ineffective. Similarly, broadly drafted provisions in "old" IIAs risk cancelling out reform efforts in new, more modern investment laws.
- Incoherence between investment laws and IIAs may also create ISDS-related risks when national laws include advance consent to international arbitration as the means for the settlement of investor–State disputes, which could result in parallel proceedings (box 9).

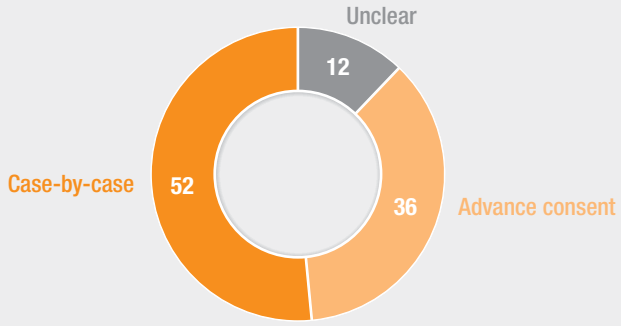
Box 9. ISDS: facts, figures and risks

Although treaty-based ISDS has come to the forefront of today's international investment policy debate, the inclusion of ISDS in national investment laws and the resulting ISDS cases have thus far triggered less controversy. In fact, the number of ISDS cases brought on the basis of national investment laws is relatively low.

By the numbers: ISDS clauses in different legal instruments

- ISDS is typical for IIAs: 95 per cent have ISDS clauses
- ISDS is less common but still present in national investment laws: 59 per cent have ISDS clauses (only 24 out of 66 laws provide advance consent; see above)
  - Laws in Africa are most likely to include ISDS: 77 per cent
  - Laws in transition economies are also likely to include ISDS: 70 per cent
- When including ISDS, national investment laws take a more cautious approach, often using so-called case-by-case consent. Such clauses offer the possibility of ISDS but require an additional act of consent by the host State government before an ISDS arbitration can go forward.
  - National investment laws that allow for ISDS on a case-by-case basis: 52 per cent
  - BITs that provide for case-by-case consent: 4 (total), most of which were concluded in the 1970s (Sweden–Yugoslavia BIT (1978), Sweden–Malaysia BIT (1979), Egypt–Sweden BIT (1978) and Sri Lanka–Switzerland BIT (1981); see also the Pan African Investment Code (2015)).

Box figure 9.1. Types of consent to international arbitration in national investment laws (Per cent, total = 66)



Source: UNCTAD, Investment Laws Navigator.

By the numbers: ICSID-registered cases based on different legal instruments[a]

- ICSID cases brought based on national investment laws only: 26 cases

/...

Box 9. ISDS: facts, figures and risks (Continued)

- ICSID cases brought based on both national investment laws and IIAs: 35 cases
  - Total: 61 cases brought on the basis of an investment law
- Certain States have been subjected to higher numbers of ICSID cases based on their national laws.

Box table 9.1. ICSID-registered cases based on national laws

Country	Based on national law	Total IIA-based ICSID cases
Venezuela (Bolivarian Republic of)	12	39
Uzbekistan	6	6
Guinea	5	0
Kazakhstan	5	11
Albania	4	6
Egypt	3	28
El Salvador	3	3
Kyrgyzstan	3	3
Congo, Dem. Rep. of	2	4
Tunisia	2	1

Source: UNCTAD.

Other states that have been subjected to at least one ICSID case based on a national investment law include Cameroon, Côte d'Ivoire, Gabon, Georgia, Jordan, Madagascar, Mauritania, Montenegro, Mozambique, Niger, Nigeria, Papua New Guinea, Senegal, South Sudan, Tanzania, Timor-Leste and Yemen.

Possible risks of advance ISDS consent in both IIAs and national investment laws

Advance ISDS consent in both IIAs and national investment laws can increase countries' exposure to ISDS, prolong proceedings and impose higher costs on the defending States, with the potential for contradictory awards.

- Increased exposure: e.g. in *Caratube v. Kazakhstan*, after the original IIA claim had been dismissed on jurisdictional grounds, the investor renewed its claim based on the same IIA and, in addition, brought a claim based on the national investment law; the investor was ultimately awarded $39 million in damages[b]
- Prolonged proceedings: e.g. in *Champion Holding Company et al. v. Egypt*, investors brought a subsequent claim based on both the national law and the IIA after treaty-based claims were dismissed (case still pending)[c]
- Higher costs: e.g. in *Pac Rim Cayman v. El Salvador*, an arbitral tribunal dismissed the treaty-based claim in the jurisdictional phase but allowed the national law-based claim to go forward; proceedings drew out for an additional four years and generated significant legal and arbitration costs[d]

Source: UNCTAD.

[a] Based on 640 cases registered under ICSID Arbitration or Additional Facility Rules as of January 2018, pending or concluded.

[b] *Caratube International Oil Company LLP and Devincci Salah Hourani v. Republic of Kazakhstan* (ICSID Case No. ARB/13/13).

[c] *Champion Holding Company et al. v. Arab Republic of Egypt* (ICSID Case No. ARB/16/2).

[d] *Pac Rim Cayman Ltd v. Republic of El Salvador* (ICSID Case No. ARB/09/12); see also *ABCI Investments N.V. v. Republic of Tunisia* (ICSID Case No. ARB/04/12).

3. Policy options

Maximizing sustainable development benefits requires maximizing synergies between IIAs and the national legal framework for investment. There are several entry points for countries to address the challenges (table 23).

(i) Strengthening cooperation between policymakers

There is a risk that investment policymaking occurs in silos, and that instruments are formulated in a vacuum, without sufficient coordination between the authorities in charge

Table 23. IIAs and the national legal framework for investment: entry points for maximizing synergies

Strengthening cooperation between policymakers	• Improve coordination between institutions charged with national and international investment policymaking • Encourage consultation between the various stakeholders in the investment regime
Improving interaction between the two regimes	• Establish clear principles for inter-operation of the different elements of the regimes • Condition IIA protections on investors' compliance with domestic law, provided that such laws are in line with international commitments • Use divergence to pursue strategic policy objectives
Ensuring cross-fertilization between the two regimes	• Determine where the national legal framework for investment can benefit from elements found in modern IIAs • Determine where IIA negotiators can consider features common to national investment policymaking

Source: UNCTAD.

of IIAs and those in charge of domestic investment rules. Lack of interaction may also occur between ministries in charge of investment and those in charge of related policies (see discussion below). These challenges occur in all countries but can be particularly pronounced in small, developing countries that have insufficient human resources and institutional or administrative capacities. Strengthening cooperation between the authorities in charge of the various dimensions of a country's investment policy framework is crucial for ensuring a coherent approach that reflects the country's overall strategy on investment for development. One option for doing so is the establishment of special agencies or interministerial task forces with a specific mandate to coordinate investment policy-related work (including the negotiation of IIAs) of different ministries and other government units. In addition, stakeholder consultations can help maximize synergies.

(ii) Improving interaction between regimes

Well-managed legal interaction between different investment policy instruments, based on a clear understanding of the different functions and objectives of the two regimes and the way they relate to each other, can help minimize challenges arising from diverging or conflicting clauses. Both IIAs and national investment laws sometimes contain elements that address the interaction between the two bodies of law:

- Establishing the precedence of one regime over the other in the event of conflict. Technical provisions, such as "relationship management" clauses, can help guide the legal interaction between intersecting and overlapping instruments, and establish clear precedence. More than 30 per cent of national investment laws (34) contain such "relationship management" clauses. Of these 34 laws, 16 explicitly acknowledge that the IIA takes precedence over national laws. Others include more vague formulations, such as providing that rights guaranteed under the investment law are "without prejudice to" rights derived from international instruments. Clear drafting can help

provide legal guidance to government actors, investors and tribunals (in the event of dispute) on how these regimes should interact.[20]

- Conditioning IIA protections on investor compliance with domestic law. To benefit from the protection of the agreement, more than 60 per cent of IIAs require that an investment must be made in accordance with domestic law. This can include safeguards and requirements related to corporate disclosure and to social, environmental or public health protections. This approach can help improve coherence between the two regimes with respect to certain, albeit limited, aspects and can also promote responsible investor behaviour. This is particularly so if compliance with domestic laws is also extended post-entry (e.g. to the operations or post-operations stage; UNCTAD, 2015b, option 7.1.1), provided that such laws are in line with international commitments.
- Using divergence to pursue strategic policy objectives. Although the management of policy interaction would typically strive for consistency, conscious and temporary divergence between the national and international investment policy regimes can also foster the achievement of strategic goals. For example, the international regime could drive change at the national level, as sometimes seen in the context of pre-establishment agreements (*WIR04*).[21] At the same time, changes in countries' domestic policy priorities (and subsequently national laws and policies) can also spur change in a country's approach to international investment policymaking.

(iii) Ensuring cross-fertilization between the two regimes

Cross-fertilization between domestic investment rules and IIAs can ensure that lessons learned in one realm of policymaking benefit the other. Facilitating cross-fertilization not only requires intensified cooperation between policymakers (as noted above), but also the careful identification of potentially transferable lessons learned. It is important to note that lessons learned cannot be transferred mechanically. Instead, careful attention must be given to the key structural and contextual differences between the different regimes.

For example, the fact that a country has a widely liberalized investment regime at the domestic level does not automatically translate into the need to inscribe this level of openness into IIAs. Instead, countries may wish to preserve regulatory space as regards the entry conditions for foreign investment. Similarly, the fact that a country has started to carefully circumscribe key protection clauses, e.g. FET, in IIAs does not mean that such a clause should automatically be "exported" into national laws. Instead, countries may wish to refrain from having FET clauses in national investment laws at all.

Considering these dynamics is of particular importance in light of today's imperative of sustainable development-oriented IIA reform. There is a concern that, under certain conditions (where a national investment law includes advanced consent to international arbitration as a means for the settlement of investor–State disputes as well as traditional investment protection clauses), unreformed national investment laws may render sustainable development-oriented IIA reform more challenging. Similarly, unreformed IIAs can dilute the relevance of and even cancel out more modern investment-related laws that contain sustainable development features.

IIA policymakers may wish to consider reflecting the following national law approaches in investment treaties:

- Investment facilitation: Investment laws generally include a range of investment facilitation provisions (UNCTAD, 2016). In addition to the provisions found in some IIAs (e.g. clauses on transparency and on entry and sojourn of foreign personnel), many investment laws also contain references to the facilitation services of investment promotion agencies and one-stop shops.
- Investor obligations: About two-thirds of investment laws make explicit reference to investor obligations. Beyond the commonly stated obligation to comply with host-country laws, investment laws often also include one or more specific requirements, such as corporate disclosure, respect for labour rights and standards (e.g. those pertaining to social security, minimum wages and trade union rights) and respect for environmental and public health legislation. In addition, some laws specify that investors must honour fiscal obligations or refer to obligations regarding hiring, training and skill transfer for local staff.
- Settlement of investment disputes: More than half of the investment laws analysed here include provisions for international arbitration for the settlement of investment disputes, frequently on a case-by-case consent basis (box 9). Many laws also include clauses on recourse to local courts and alternative dispute resolution (64 and 21 laws, respectively). For current reform efforts to improve international investment dispute settlement, policymakers may wish to consider whether lessons can be learned from the national level.

National investment policymakers may wish to consider reflecting the following IIA approaches in domestic law:

- Refinements: To the extent that national investment laws have typical IIA clauses (e.g. on FET, expropriation or transfer of funds), these clauses frequently do not have the refinements and clarifications that are typical of modern IIA drafting (for IIAs, see *WIR16*, *WIR17*).
- Sustainable development orientation: Only a small number of national investment laws refer – in their preamble or another dedicated clause on the objectives of the law – to sustainable development (or environmental or human health protection). It should be noted, however, that sustainable development-related concepts may be found in other national laws and policies. For IIAs, in turn, a focus on sustainable development-oriented reform has become standard (*WIR16, WIR17*).

In maximizing synergies between the international and national investment policy dimensions, it is important to remain flexible. Divergences between IIAs and national investment laws are often desirable and, in fact, may be intentional. While recognizing the need for different approaches to the legal framework for investment at the national and international levels, policymakers should strive for a more synergetic approach to the formulation of IIAs and the national legal framework for investment in order to produce an investment regime that is in line with a country's broader national development strategy and with sustainable development imperatives.

D. Managing the interaction between IIAs and other bodies of international law affecting investment

The fragmentation of international law has led to different systems that each pursue their own objectives, with each system often being developed and decided on in isolation. In line with today's SDG imperative, IIA reform should take into account the interaction

between IIAs and other bodies of international law affecting investment. IIA reform can help avoid conflict and maximize synergies, notably through clearer treaty drafting, exceptions in IIAs and guidance on interpretation of IIA provisions.

1. Examples of interaction between IIAs and other bodies of international law affecting investment

The investment policy regime does not exist in a vacuum; it interacts with other areas of economic law and policy (e.g. competition, finance, intellectual property, development, [22] taxation and trade), as well as with areas of law and policy that are typically considered "non-economic" (e.g. culture, environment, health, labour, social or gender-related issues; land rights; national security issues).[23]

Different areas of international law diverge from each other in important ways. For example:

- Type of regime: Some international regimes, such as IIAs and double taxation treaties (DTTs), comprise mostly bilateral agreements, while others, such as human rights, trade and environment, are largely multilateral. Also, some areas of law are governed by enforceable legal instruments while others promulgate "soft law" norms, such as guidelines.
- Type of dispute settlement: At the international level, the IIA and trade regimes stand out as two regimes containing litigation-type dispute settlement, as opposed to dispute prevention or other types of mechanisms (multilateral environmental agreements, DTTs' mutual agreement procedures, etc.). Both IIAs and some international human rights conventions allow private parties (companies and individuals), as opposed to States, to bring direct international claims.[24]
- Type of protection and content: Some regimes govern the relationships between States and private parties (IIAs, human rights), while others seek to regulate or shape States' policies with a view to achieving certain global objectives, such as environmental protection, financial stability or preservation of cultural heritage.

These differences result in a multitude of types of interrelationships between these legal regimes, as well as interactions in policy practices. Moreover, by its very nature, economic activity (such as investment or trade) will affect both the environment and the social conditions for the public and workers.

2. Challenges resulting from the interaction between IIAs and other bodies of international law affecting investment

The various ways in which the IIA regime interacts with other bodies of international law give rise to several distinct, but often interrelated, challenges (table 24). These challenges can be placed in three broad categories: reduction of regulatory space, administrative complexity and uncertainty about dispute settlement.

The reduction of regulatory space manifests itself in several interrelated ways. Most prominent in the public debate is the risk that IIAs can constrain policymakers in the pursuit of important public policy objectives in a manner that was not anticipated. Such constraints could have a chilling effect on future, non-investment related national or international law-making (van Harten et al.; Bonnitcha et al.). For example, in the wake

Table 24. IIAs and other bodies of international law and policies: policy challenges

Reduction of regulatory space	• Unexpected chilling effect on future, non-investment-related law-making • Exposure to ISDS
Administrative complexity (for States and investors)	• For States: difficulty in managing distinct but overlapping policy areas and international obligations • For investors: investment decisions taken in light of fragmented web of international (and national) laws
Dispute settlement	• Risk of isolated treaty interpretation • Litigation of one issue in multiple fora • In case of ISDS competence, uncertainty about interpretation

Source: UNCTAD.

of the (ultimately unsuccessful) tobacco-related disputes brought against Australia and Uruguay, several developing countries claimed an inability to enact strong tobacco control laws given the threats that multinational tobacco companies might bring international investment claims.

Second, there are administrative difficulties inherent in managing an international legal regime consisting of many different policy areas layered on top of an already intricate domestic policy framework. For States in which different ministries negotiate and implement international agreements across subject matters, these issue areas can and do conflict. Small and resource-constrained countries may find this situation particularly difficult to navigate. These challenges also result in more uncertainty for States that are trying to determine which measures could constitute an IIA violation. Administrative complexity also arises for investors, for example, in the determination of which operational rules apply and/or prevail for their investment at any given point in time or place.

Third, dispute settlement poses three distinct challenges: the risk of isolated treaty interpretation, litigation in multiple fora and uncertainty about ISDS tribunals' approach to another body of law.

The risk of isolated treaty interpretation arises from the special nature of international law. Treaties can be interpreted in a fragmented way (International Law Commission Study Group). Legal scholars have analysed the intensity with which international legal regimes engage and reference other areas of law. Interestingly, ISDS tribunals interact more with other bodies of law, than, for example, dispute settlement processes under the WTO (Charlotin). Moreover, in ISDS there is convergence around certain public international law norms, as interpreted by the ICJ. This is reflected in the frequency with which ICJ jurisprudence is cited in ISDS. For example, ISDS tribunals have cited as many as 184 ICJ decisions in numerous awards, decisions or orders.[25]

Litigation in multiple fora could also arise. Bringing the same facts, claims or arguments before multiple fora (e.g. ISDS and WTO dispute settlement; ISDS and European Court of Justice) risks conflicting or confusing judgments. Thus far, litigation has been

brought in multiple fora in both the economic realm (e.g. investment and trade) and the non-economic realm (e.g. investment and human rights).

Uncertainty about ISDS tribunals' approach to another body of international law, particularly in light of the multitude of scenarios which may require arbitrators to consider such rules. Such scenarios include the State alleging that a measure is either permitted or required by another norm of international law; the claimant arguing that the State's violation of a non-investment rule entails a breach of the IIA; and the State arguing that the claimant has breached an obligation and therefore may not make a claim under the IIA. For example:

- In *S.D. Myers v. Canada,*[26] to justify the imposition of an export ban for a certain chemical, Canada referred to its international obligations under the Basel Convention and the Transboundary Agreement between Canada and the United States.[27] The tribunal examined the environmental instruments invoked; it concluded that the true reason for the export ban was protectionist rather than environmental.
- In *UPS v. Canada,*[28] the claimant asserted that certain provisions of NAFTA's Chapter 15 (addressing competition policy, monopolies and State enterprises) could be used as a basis for claiming damages in ISDS. The tribunal held that its jurisdiction was limited to failures to abide by the terms of the investment chapter (Chapter 11) but nevertheless found that conduct in violation of a party's obligation under NAFTA as a whole (including Chapter 15) could also constitute a violation of Chapter 11.[29]
- In *Urbaser v. Argentina,*[30] Argentina lodged a counterclaim, invoking several international instruments[31] and alleging that the investor's failure to invest in service expansion compromised the human right to water. Pointing to developments in CSR and the United Nations Guiding Principles on Business and Human Rights, the tribunal stated that it could no longer be said "that companies operating internationally are immune from becoming subjects of international law".

Also of relevance is a recent judgment by the European Court of Justice, which held that the arbitration provisions of the Netherlands–Slovakia BIT were incompatible with EU law.[32] This judgment could call into question any awards rendered under that BIT and other intra-EU BITs.

3. Policy options

In order to foster sustainable development-oriented policy coherence, IIA reform must take into account the interaction between IIAs and other bodies of international law. Addressing this relationship in IIA reform can help avoid conflicts and provide arbitral tribunals with guidance on how to interpret such interaction.

One way of managing some of the above-mentioned risks is through clearer drafting in IIAs.[33]

- Including exceptions for other areas of policymaking. A first option is clearer and more sustainable development-oriented exceptions clauses or carve-outs for other areas of policymaking (e.g. temporary safeguards in the event of serious balance-of-payments difficulties; clauses for prudential measures; environmental, cultural or national security exceptions).[34]
- Cross-referencing. A second option is to manage the interaction of policy regimes, as some treaties have begun to do. For example, some of the more than 300 BITs

that include balance-of-payments exceptions specify that the exceptional measures to derogate from the free transfer provision must be consistent with the Articles of Agreement of the IMF (e.g. Cambodia–Japan BIT, Article 19 (2007); Colombia–Turkey, Article 9 (2015); Japan–Kenya, Article 17 (2016)). Interestingly, the WTO GATS specifies that, in consultations related to restrictions to safeguard the balance of payments, all findings of statistical and other facts presented by the Fund shall be accepted, and conclusions shall be based on the assessment by the Fund.

- Guiding interpretation. A third option is clauses that can guide ISDS tribunals in their interpretation of key treaty terms (in terms of both jurisdictional and merits questions). References to other bodies of law or the SDGs in IIAs, e.g. through preamble language, can also guide tribunals that are grappling with overlapping legal regimes in the resolution of a dispute.

E. Dynamics of policymaking: flexibility and policy space

Striving for coherence does not necessarily imply legal uniformity – inconsistencies and divergence may be intended – but different policy areas and legal instruments should work in synergy.

A country's strategic considerations may result in policy divergences that are intentional. For example, as mentioned above, a country may wish to conclude IIAs that give greater (pre-)establishment rights than its national legal framework for investment. This greater level of openness in IIAs can be used – intentionally – to drive change at the national level (e.g. IIA-induced liberalization; *WIR04*). Similarly, a country may choose to stop short of enshrining the country's actual level of openness, as set out in the national legal framework for investment, in IIAs. In that case, the differences can also be intentional, with the goal of giving the country policy space to explore opening new sectors to foreign investment and, if need be, reintroducing limitations on investment in those sectors in the future (*WIR15*; UNCTAD, 2015b).

Similarly, country policies may evolve. Indeed, policy shifts are a regular feature at both the national and international levels of policymaking. For example, new factors may emerge on the domestic policy scene, including a new government in power, economic or financial crises, social pressures or environmental degradation. Similarly, a country's shift towards sustainable development-oriented investment policymaking will almost always produce a temporary phase of inconsistency. Such temporary inconsistency should not discourage investment policy reform. Instead, it should create momentum and foster more rapid and dynamic reform. At the same time, countries must embrace flexibility in adjustment periods and time lags, which are nearly always present in governmental shifts or promulgation of new policies.

Lastly, policy divergence may result from differential levels of development, which translates into different policy needs and objectives, as well as different capacity to implement policies. Policy interaction should be tailored to the particular conditions prevailing in a country and to the realities of the economic asymmetries between countries. Finding the proper balance between flexibility and consistency, i.e. a coherent balance that leaves sufficient space for individual countries to pursue their needs, is crucial for countries in the pursuit of their national policy strategy on investment for sustainable development.

The need for flexibility in the pursuit of policy coherence and in the management of policy interaction also flows from UNCTAD's Core Principles for Investment Policymaking, as set out in UNCTAD's Investment Policy Framework for Sustainable Development. Principles such as policy coherence (noting that investment policy should be integrated in an overarching development strategy) and dynamic policymaking (recognizing that national and international investment policies need flexibility to adapt to changing circumstances) are key ideas to embrace when embarking on Phase 3 reform actions.

In sum, in considering next steps for investment policy reform, countries should be guided by the objectives of fostering coherence, maximizing synergies and improving interaction between various instruments that govern investment. However, investment policy consistency should not be pursued for its own sake, but rather in a way that is coherent and mutually supportive for investment as a driver of sustainable development.

VI. CONCLUSIONS

This Reform Package presents a holistic and multi-level blueprint for reforming the IIA regime with a view to harnessing investment for sustainable development. Reorienting international investment policy making towards sustainable development is essential for mobilizing much needed foreign investment and channeling it towards concrete SDG outcomes.

This Reform Package takes stock of the ongoing debate, the arguments, the history and the lessons learned of IIA reform. It identifies reform areas and objectives and provides policy makers with flexible options to adapt and adopt. The options can be combined into individual countries' reform packages that respond to their specific needs and prerogatives.

The UNCTAD Reform Package does so by covering IIA reform comprehensively:

- It provides options for treaty clauses for the five priority areas with a view to sustainable development-oriented treaty making (safeguarding the right to regulate for pursuing sustainable development objectives, while providing protection; reforming investment dispute settlement; promoting and facilitating investment; ensuring responsible investment; and enhancing systemic consistency of the IIA regime) (Phase 1 of IIA Reform);
- It identifies and discusses 10 reform mechanisms that countries may use to modernize existing old-generation treaties (Phase 2 of IIA Reform); and
- It gives policy guidance for ensuring coherence and maximizing synergies within countries' IIA networks, and between IIAs and national investment policies and IIAs and other bodies of international law affecting investment (Phase 3 of IIA Reform).

IIA reform is well underway across all regions, and many countries and regional groupings are in the process of reviewing, reforming and revising their IIAs, often on the basis of UNCTAD's Investment Policy Framework and its earlier guidance on reform of the IIA regime.

However, a lot remains to be done, and when pursuing the reform options presented in this Reform Package, policymakers may face a number of challenges. These include strategic and systemic challenges, as well as challenges relating to coordination and capacity.

At the strategic level, countries need to determine the right extent of reform on the basis of a comprehensive and facts-based cost-benefit analysis in light of their offensive and defensive interests. Importantly, this means ensuring that reform produces holistic results (covering all five areas of reform and all levels of policymaking), but without depriving the IIA regime of its fundamental purpose of protecting and promoting investment. When examining different reform options, policymakers need to consider the need for balance between preserving those elements of the current investment policy regime that work well and improving those parts on which action is required to make it work better for sustainable development. Similarly, policymakers need to avoid unintended consequences of reform. Ultimately, the regime must be reoriented so that it becomes balanced, predictable and conducive to sustainable development.

At the systemic level, policymakers need to address the challenges that arise from gaps, overlaps and fragmentation and that create coherence and consistency problems.

This includes challenges arising from the survival, transition and MFN clauses, as well as the ones being addressed through Phase 3 of IIA Reform.

A third set of challenges relates to coordination. These challenges include finding treaty partners with similar reform objectives and prioritizing individual reform actions and options, considering their importance and feasibility, as well as their suitability in light of long and short-term IIA reform objectives and overall development strategies. Coordination also benefits from communicating reform to affected stakeholders – within and outside the country. Treaty partners, the international community and foreign investors (both established and prospective) need to receive a clear message that a country's reform endeavours will not result in a less attractive business environment or encourage protectionism. Coordination challenges also include ensuring coherence between reform efforts at different levels of policymaking (national, bilateral and regional, as well as multilateral).

A final set of challenges relates to capacity. Successful reform requires strong internal structures for preparing and carrying out actions, with solid processes and decisionmaking and implementation capacities (e.g. sustained internal coordination among State organs, awareness raising and capacity-building). This is particularly difficult for developing countries and LDCs, which may face challenges in terms of negotiating and implementing capacities. It is therefore very important for these countries to benefit from opportunities to build the technical capacity of IIA negotiators, as well as to ensure the preservation of institutional knowledge of IIA issues and continuity in the staff engaged in IIA reform. To these technical challenges adds the challenge of capacity in terms of bargaining power. The latter makes it more difficult for developing countries and LDCs to be effective in negotiating and altering their existing IIA networks and addressing the drawbacks of existing first-generation IIAs.

All these challenges call for a coordinated approach to IIA reform, supported by multilateral backstopping. UNCTAD, through its three pillars of work – research and policy analysis, technical assistance and intergovernmental consensus building – can play a key role in this regard. In particular, UNCTAD's role as the United Nations' focal point for international investment and the international forum for high-level and inclusive discussions on today's multilayered and multifaceted IIA regime, as reconfirmed in its mandates from the Nairobi Maafikiano and the Addis Ababa Action Agenda, can help bring coordination and coherence to reform efforts. Ultimately, the higher the degree of coordination at the various levels of policymaking, the higher the chances of creating a less fragmented and more balanced, stable and predictable IIA regime that effectively pursues sustainable development objectives.

NOTES

1 European Commission, 2015, pp. 11–12.

2 Some countries also include a list without explicitly including a provision entitled "FET"; the SADC model BIT and the Indian model BIT are examples.

3 To this purpose, IIAs usually stipulate the requirements for a lawful expropriation, i.e. for a public purpose, non-discriminatory, in accordance with due process of law and against compensation.

4 Another option is to include a broadly formulated exception for domestic regulatory measures aimed at pursuing legitimate public policy objectives.

5 *Mexico v. United States* (2000), *Peru v. Chile* (2003), *Italy v. Cuba*, ad hob arbitration (2003), *Ecuador v. United States*, Permanent Court of Arbitration (2001).

6 In June 2014, the UN Human Rights Council passed a resolution, by majority, that decided to establish an open-ended working group on a legally binding instrument on transnational corporations and other business enterprises with respect to human rights.

7 For example, treaty termination is frequently combined with replacement or consolidation.

8 MFN clauses typically prohibit less favourable treatment of investors from a signatory State when compared with treatment of "like" investors from any third country.

9 Typically, such clauses cover governmental measures adopted both before and after the date of termination (for the duration of the survival period), but apply only to investments made before the treaty's termination.

10 See European Court of Justice (ECJ), *Commission v. Austria*,C-205/06, Judgement (3 March 2009); ECJ, *Commission v Sweden*, C-249/06, Judgement (3 March 2009); ECJ, *Commission v Finland*, C-118/07, Judgement (19 November 2009).

11 If the new overlapping treaty does not include a relationship clause of any kind, the relationship between the co-existing treaties will be guided by the VCLT, notably its Articles 30 and 59 (as applicable).

12 For the status of the Convention, see the UNCITRAL website at www.uncitral.org/uncitral/en/uncitral_texts/arbitration/2014Transparency_Convention_status.html.

13 Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (adopted 24 November 2016).

14 United States, The White House, "Presidential Memorandum Regarding Withdrawal of the United States from the Trans-Pacific Partnership Negotiations and Agreement", 23 January 2017.

15 W. Alschner and D. Skougarevskiy, "Mapping the Universe of International Investment Agreements", Journal of International Economic Law, 2016, pp. 561–588.

16 ECJ, *Slovak Republic v. Achmea B.V.* (Case C-284/16), Judgment, 6 March 2018.

17 See, e.g., A.D. Mitchell, "Someone Else's Deal: Interpreting International Investment Agreements in the Light of Third-Party Agreements", *European Journal of International Law*, Vol. 28, Issue 3, 3 November 2017 (finding that a significant number of tribunals have interpreted the applicable IIA with reference to a party's IIAs with a third State, its model BIT and/or IIAs concluded between other States parties).

18 See http://investmentpolicyhub.unctad.org/IIA/mappedcontent.

19 J. Bonnitcha, "Investment Laws of ASEAN Countries: A comparative review", International Institute for Sustainable Development (December 2017), https://www.iisd.org/sites/default/files/publications/investment-laws-asean-countries.pdf.

20 Although the Vienna Convention on the Law of Treaties provides that a State may not invoke its national law as a justification for its failure to perform an international treaty (Art. 27), the legal status of a specific treaty (IIA) within the national legal regime may depend on whether that regime is monist or dualist.

[21] In such circumstances, a country's IIA negotiators would intentionally agree to internationally committing the country to a degree of openness that is more far-reaching than what is prescribed in terms of entry and establishment at the national level. At times combined with a phase-in schedule, such (temporary) divergence could translate into national-level policy action (e.g. domestic reforms such as liberalization; see WIR04, "IIA-driven policy interaction").

[22] Some FTAs include chapters on development, which could provide a means for State parties to assist other members with respect to the implementation of their treaty commitments, including commitments under investment chapters.

[23] The distinction between economic and non-economic areas of policymaking may be blurring. Many recent environmental treaties may also be considered economic in nature, e.g. the United Nations Framework Convention on Climate Change (UNFCCC).

[24] Nonetheless, in contrast to human rights treaties, IIAs do not require claimants to exhaust local remedies before submitting claims to an international tribunal.

[25] A few ICJ or PCIJ cases are cited with regularity in ISDS decisions, e.g. *Case concerning Elettronica Sicula S.p.A. (ELSI)* (United States/Italy), Judgment (20 July 1989); *Case concerning the Barcelona Traction, Light and Power Company, Ltd.* (Belgium/Spain), Judgment (5 February 1970), and *Case concerning the Factory at Chorzów* (Claim for Indemnity) (Merits) (Germany/Poland), Judgment (13 September 1928).

[26] UNCITRAL, Partial Award, 13 November 2000.

[27] Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal, signed on 22 March 1989. The Basel Convention is a multilateral environmental agreement, to which Canada is a party, but the United States, the home country of the investor, is not.

[28] ICSID Case No. ARB/02/1, Award on Jurisdiction, 22 November 2002, Award, 24 May 2007.

[29] Interestingly, in *Al Tamimi v Oman*, the State successfully defended against the investor claims, in part, on the basis of non-investment chapters and provisions of the Oman-United States FTA (2006) related to environmental protection. *Adel A Hamadi Al Tamimi v Sultanate of Oman* (ICSID Case No. ARB/11/33) Award, 3 November 2015.

[30] ICSID Case No. ARB/07/26, Award, 8 December 2016.

[31] Argentina invoked the Universal Declaration of Human Rights of 1948; the International Covenant on Economic, Social and Cultural Rights of 1966; the ILO Tripartite Declaration of Principles concerning Multinational Enterprises (as amended in 2006); and UN General Assembly Resolution 64/292 of 2010.

[32] ECJ, *Slovak Republic v Achmea B.V.* (Case C-284/16), Judgment, 6 March 2018.

[33] To this is added refining IIA clauses that deal with substantive and procedural protections, as suggested in the UNCTAD Investment Policy Framework for Sustainable Development and the UNCTAD Reform Package for the International Investment Regime, and as implemented in recent treaties.

[34] This should be done with caution, however, as there is a risk that such clauses could be interpreted narrowly, thus circumscribing the State's regulatory space in a way that was not intended. See *Bear Creek Mining v Peru* (ICSID Case No. ARB/14/2), Award, 30 November 2017, paragraph 473.

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