

Towards a Repository of Policy Options for IIA Reform

Research Project Rethinking the International Investment Law Regime¹ⁱ

Mr. Simon Lester,
Trade Policy Analyst,
Cato's Herbert A. Stiefel Center for Trade Policy

Investor-state dispute settlement and the international investment regime are at something of a cross-roads. Major governments such as South Africa and Indonesia are re-thinking their involvement in the system. Australia mostly pulled out for a while, and is now somewhat back in. In the EU, a major public consultation on these issues is taking place, although it is not clear whether any significant changes, beyond those the EU has already adopted in its negotiations with Canada, will be possible.

These developments provide an opportunity to look critically at the fundamental basis of the investment regime. I focus on two points: What is the problem the investment regime seeks to address? How is that problem best dealt with?

Is there a problem with bad treatment of foreign investment?

The assumption underlying the investment regime is that foreign investors receive "bad" treatment of some sort. This treatment may be worse than what domestic investors receive, or it may just be bad in a more objective, rather than comparative, sense. Obligations designed to address this bad treatment include national treatment/MFN treatment obligations; a minimum standard of treatment obligation; and rules on expropriation.

But is there really a problem with bad treatment of foreign investment? This question has not been well studied. There is some research on the number of expropriations, which shows a precipitous decline. The data show that what was a big problem in the 1950s, 1960s and 1970s is a fairly small issue today.

In terms of other forms of bad treatment, this has never been quantified. Supporters of the investment regime have not pointed to any comparative studies that examine how governments around the world treat foreign investors in terms of due process or transparency issues. There may be a problem of some sort, but we really do not know much about it. As a comparison, in the trade world, the thousands of tariffs governments impose are easy to see; and the TBT Committee of the WTO receives notifications of, and discusses, technical regulations. Here, by contrast, the alleged problem is anecdotal. And furthermore, it is not place in its proper framework of treatment of investment generally.

In addition, beyond the absence of proof of bad treatment, any cursory examination of the treatment of foreign investors would show that treatment is often too good, in the sense that foreign investors are showered with subsidies by host states for investment. Thus, it may be more fruitful, when thinking about problems related to foreign investment, to take on the problem of treatment that is biased towards foreign investors.

¹ The opinions expressed in this paper are those of the author and do not necessarily reflect the views of the UNCTAD Secretariat or its Member States.

If there is a problem, what should we do about it?

For the sake of argument, let's assume there is a problem with bad treatment of foreign investors. How would we best address it?

Clearly, national treatment and MFN obligations can be useful here. Non-discrimination is a long-standing and widely accepted part of the international economic law regime. If these obligations can be used to discourage discrimination against foreign investors, that would be of great benefit.

By contrast, the obligations related to the minimum standard of treatment and expropriation are problematic as they exist now, for a number of reasons, including the following.

First, they only provide protections to foreign investors, not domestic investors. That seems like a strange result. If foreign investors receive compensation for expropriation, why shouldn't domestic investors receive it as well? **A better solution might be a treaty that requires governments to incorporate expropriation (and minimum standard of treatment) obligations into domestic law.**

Second, they are not well defined. Tribunals have offered varying interpretations of these provisions, and governments cannot agree on their scope. This makes enforcement uneven and unpredictable. Recent attempts at clarification do not provide much additional certainty.

Conclusions

- **Critics of the investment regime should make their arguments carefully.** Some attacks on the regime seemed to be rooted in a nationalist vision of the world, or in anti-corporate ranting. Such approaches are not very effective.
- **Instead, what is needed now is a thoughtful consideration of what problems exist in the world of foreign investment as it stands today, and how they might be addressed through international rules.** At first glance, the current system does not seem well-calibrated for this task.
- As part of this examination, it is **important to take into account the broader international system**, including trade, intellectual property, environmental, and human rights issues. How do these various issues fit together? The fragmentation of international law has become a real problem in recent years.
- All of those involved in this area have a strong incentive to engage in this process in good faith. **For the system to work, the investment regime cannot just be about opportunities for big corporations to sue, or threaten to sue, governments. It has to be based on a balanced framework that pursues clear and sensible policies.**

ⁱ For more information about the work of the CATO institute see

<http://www.cato.org/publications/policy-analysis/liberalization-or-litigation-time-rethink-international-investment>

<http://www.cato.org/publications/commentary/does-us-eu-foreign-investment-need-protection>

<http://www.cato.org/publications/commentary/improving-investment-treaties-through-general-exceptions-provisions>

http://object.cato.org/sites/cato.org/files/articles/tie_w13_lester.pdf

<http://www.cato.org/publications/free-trade-bulletin/compromise-advance-trade-agenda-purge-negotiations-investor-state>

<http://www.cato.org/events/investor-state-dispute-settlement-mechanism-examination-benefits-costs>