The Evolving International Investment Regime: Expectations, Realities, Options
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*Edited by José E. Alvarez and Karl P. Sauvant with Kamil Gérard Ahmed and Gabriela P. Vizcaíno (New York: Oxford University Press, 2011).*

The transboundary flow of capital directed at establishing businesses is the engine of the world economy. Approximately 3000 bilateral and regional investment protection treaties worldwide govern this driver of economic globalization. As might be expected, the international investment regime now competes with the World Trade Organization for global praise and criticism. This volume looks at how these treaties and investor-state arbitrations that apply them accommodate the different expectations of various stockholders, including governments, foreign investors and civil society. The volume’s diverse authors focus especially on the views of developing countries and international civil society. They address the extent to which the regime is satisfying the expectations of those who originally drafted the treaties as well as the states now at the losing end of investor-state awards. They review critiques of the regime that help explain sovereign and political backlash, identify avenues for accommodating various interests, and make specific proposals to address concrete challenges. The volume should interest academics, practitioners, negotiators of international investment agreements, and others who want to know more about the rules that govern foreign direct investment, the activities of multinational enterprises, and those who seek to advance sustainable economic development through both.
THE EVOLVING INTERNATIONAL INVESTMENT REGIME: EXPECTATIONS, REALITIES, OPTIONS

Edited by
José E. Alvarez and Karl P. Sauvant with Kamil Gérard Ahmed and Gabriela P. Vizcaíno

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Foreword

Some might argue that the system for the protection of international investment has reached an impasse. Since the first modern investment treaty claim was referred to arbitration just over two decades ago, the ad hoc tribunals deciding these claims have produced at times conflicting decisions, sometimes with little regard for the regulatory interests of host states. The ensuing problems are not unique to the investment treaty regime; more broadly the proliferation of international dispute settlement mechanisms and the broadening of international law has increased the possibility that the same conduct of a state may be scrutinized in relation to different, sometimes disparate treaty regimes, applied by distinct dispute settlement fora, each operating in the absence of a binding system of precedents. But these more general characteristics of the international legal “system”—not themselves new—have risen to the surface in investment treaty arbitration, in part because of the increasing number of cases.

This book is a contribution to the debate on what can be done to address the deficiencies of the investment treaty regime. But in fresh contrast to a mass of literature on the so-called “crisis” of international investment law, it approaches the question by first considering the interests and expectations of the relevant stakeholders: capital-exporting and capital-importing states, investors, and host states. An examination of these interests and expectations provides the basis for constructive and realistic suggestions for reform, bearing in mind ever-present political concerns and realities.

Part I sets out the expectations of the most significant categories of stakeholders in the international investment regime, dealing primarily with developing states, and also with civil society, concentrating on nonbusiness groups aimed at social and developmental justice. Additionally, the question whether international investment agreements meet the concerns and expectations of these stakeholders is addressed. In this part, some of the common critiques of the investment treaty regime are examined anew: whether and to what extent there is a bias in favor of developed states; whether the emphasis on host state obligations could be recalibrated with a view to the imposition of responsibilities on investors and home states; and whether apparent inconsistencies in the case law can be explained by the specific facts and provisions at issue.

Part II is forward-looking as it sets out possible avenues for reform (including institutional options) and reflects on the way forward for law and policy with
emphasis on multilateralism, the responsibilities of investors, and the need for balancing of interests. Part III concludes with praise and pleas: the former for the flexibility so far demonstrated in the short life-span of investment treaty arbitration; the latter for the redress of imbalances, real or perceived. For those lawyers, arbitrators and diplomats who will have to confront those imbalances, this volume provides concrete and informed ideas, for which the editors and contributors are to be commended.

James Crawford
Lauterpacht Centre for International Law
University of Cambridge
April 2010
Preface

To make investments, business must have some conviction that governments will not unreasonably take property and that contracts will generally be enforced. In turn, governments expect taxes from business but also impose regulations and accountability standards to direct business activities toward the public interest. Regulations are viewed as particularly important when business activities might generate externalities, positive or negative; exploit monopolistic powers or otherwise imperfect markets; or affect income distribution in undesired ways. In domestic settings, countries and their firms have arrived at somewhat different balances between rights and controls over business and quite different views of administrative practices with regard to them. Once investors cross national borders, they operate under more than one regime, often under quite different concepts of rights and obligations. Moreover, when they do business in developing countries, investors from rich countries may face systems that not only differ from those of their home countries but which are evolving and not as clearly specified as what investors know from their experience. Understandably, such investors seek a degree of certainty about the security of their investments and contracts in environments that appear to be less secure than their home countries. And they prefer not to be caught up in conflicting demands between home and host governments.

Governments have struggled to manage these problems associated with foreign direct investment. To the consternation of many foreign investors, a number of host countries long asserted their belief that investors must be subject to local laws, regulations, and other demands, and that disputes should be settled in local justice systems; they also insisted that investors’ home countries do not intervene on behalf of their nationals who had chosen to invest abroad.1 The policies did not reassure investors, who believed that they would not be treated fairly in local courts, at least in developing countries.

In response to problems, business abroad has urged home governments to help them defend their property rights, and governments have often obliged, in spite of the wishes of many host countries. The ways that home governments intervene have

1 Commonly called the Calvo Doctrine, after Argentinean Carlos Calvo, particularly noted for his Derecho Internacional Teórico y Práctico de Europa y América (Paris: A. D’Amyot, Durand et Pedone-Lauriel 1868).
changed. In the rather distant past, the United States and other rich countries would occasionally act militarily or insist on state-state arbitrations when their investors claimed mistreatment abroad. Later, the United States would threaten (and occasionally act) to cut off aid, vote against loans by multilateral financial institutions to offending countries, and cancel trade preferences under the Generalized System of Preference (GSP). Other home countries had similar ways to protect their investors. Such actions were, however, erratic, and constrained by broader foreign policy goals. By 1990, the United States, for example, had acted only twice under the Hickenlooper Amendment to cut off aid to a host country for taking property of U.S. investors. State Department arguments on broader foreign policy grounds—mainly that such actions would push the host toward the Communist camp—rather consistently trumped other departments' and congressional interest in protecting U.S. investors abroad.

Home countries have also attempted to regulate some of the activities of their firms abroad. The United States and other countries have, for example, attempted to keep foreign affiliates of their multinational enterprises from exporting to unfriendly countries and to discipline at home investors who engage in certain corrupt practices abroad. They have reached out extraterritorially to control restrictive business practices, and domestic groups have supported cases in the courts of home countries against investors when their affiliates abroad have allegedly violated human rights.²

Perhaps ideally, both home and host governments would accept restrictions on their behavior, and investors would be subject to globally-agreed rules that cover their property rights and their responsibilities. That such a rules-based multilateral regime does not exist is not for lack of efforts to build it. The International Trade Organization (ITO), proposed in the 1948 ITO Charter, would have covered foreign direct investment, along with antitrust and commodity agreements. Yet, the ITO Charter was never approved by the United States. Only the trade provisions survived, as the General Agreement on Tariffs and Trade (GATT) and eventually the World Trade Organization (WTO). Both the United Nations and the Organisation for Economic Co-operation and Development (OECD) attempted at various times to negotiate multilateral agreements on investment, and efforts were made to bring direct investment under the WTO. Yet, the efforts came to naught, with the exception of small steps at the WTO. There, only the Agreement on Trade-Related Investment Measures (TRIMs) and the General Agreement on Trade in Services (GATS) have been successfully negotiated. These impose restrictions on host country policies, but provide no protection of property, behavioral requirements for investors, or restrictions on home country actions.

Absent a true multilateral investment agreement, a complex network of arrangements and understandings has emerged. Providing at least partial reassurance to investors of the safety of their property, host countries have included clauses for

² Most prominent among these have been cases brought in the United States under the Alien Tort Claims Act.
international arbitration in some investment agreements, occasionally promised international arbitration in their own investment laws and, more significantly, signed a network of bilateral investment treaties and regional trade agreements with investment provisions. They call for similar mechanisms of dispute settlement, by international arbitration. The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention) and members’ commitments to the International Centre for Settlement of Investment Disputes (ICSID) increased investors’ hopes of collecting awards made to them by arbiters.

Further, a network of bilateral treaties has been concluded for the prevention of double taxation. At the same time, less formal bilateral agreements between treasuries have added to efforts to reduce conflicting demands for tax revenue from international investors. Along with these governmental arrangements, nongovernmental organizations (NGOs) have created voluntary standards of behavior for investors.³

Yet, few parties are very happy with the patchwork system that has been built out of these various arrangements. Whatever the facts, developing host countries believe that decisions of arbiters are biased against them and that arbiters refuse to take adequate account of the need to modify bad agreements, to allow adjustments to arrangements when countries face crises, to make changes to share windfalls, or to take into account social goals. They have resented the extraterritorial application of home country laws, continuing home country “diplomatic” support for investors, and the lack of mandatory rules on the behavior of investors. They have also not always agreed with the priorities of NGOs when they push behavioral standards. On the NGOs’ side, some organizations believe that arbiters are insensitive to social and environmental needs when they rule on disputes between investors and their host countries. Both host governments and investors find the arbitration system slow, costly, and unpredictable. Even the United States, which has viewed itself principally as a home country of foreign direct investment and as having a good domestic judicial system, has been somewhat taken aback by the fact that investors have brought cases against it under the North American Free Trade Agreement (NAFTA).⁴

Observers differ somewhat on how to build a better system—or even whether substantial change is needed. Some of the authors in this volume believe it is time to try again for a global agreement on investment. Maybe an agreement is now possible, given that the divide between host and home countries and their corresponding perception of self-interest has become fuzzier. Brazil, India, and China, for example, are now homes as well as hosts to foreign investors. Mexican and Brazilian investors have seen their projects nationalized in other Latin American countries. And since the United States has had cases brought against it by investors, it might have more sympathy with host countries’ arguments about interference in their domestic

³ These are illustrated by the Extractive Industries Transparency Initiative and the Equator Principles.
⁴ To date, the United States has not lost a case, but its politicians have reacted to the possibility that local or national courts might be overruled by an international tribunal.
affairs. In fact, the United States' recent model bilateral investment treaty shows more concern for host country views than did its earlier treaties.

Others, however, believe that the world has not changed that much and that old barriers to global agreement persist. Not only have the host—and home—camps not come together, as illustrated by the failed attempts to introduce more investment rules in the WTO, but multinational enterprises have not yet seen fit to support a global agreement. Without their support, a comprehensive agreement is unlikely. Moreover, the search for broadly accepted principles that could govern such an agreement has hardly been successful. For example, the most favored nation (MFN) principle for access to host country markets is unlikely to be accepted for investment, as it has been for trade. Even the United States differentiates its investment policies by country of origin. Similarly, there are few viable proposals for "escape clause" provisions that are comparable to dumping rules and surge rules in the WTO, which were essential to its political acceptance by member countries. As a result, I remain pessimistic about a comprehensive global approach and thus lean toward trying to improve the current system.

The diverse authors of the chapters of this book bring some order to the criticisms of the current patchwork system and to the proposals for improving it. Although lawyers have tended to dominate discussion of the investment regime, not all of the authors in this volume are lawyers. Whatever discipline they come from, they have made their arguments accessible to a broad range of readers—corporate managers, government policymakers, economists, and others concerned with the implications of foreign investment, and the regime in which it operates, for both economic and social development. The authors delve more deeply into the concerns of these parties than has been typical of the rhetoric that has surrounded the debates. Fittingly, they start from different points of view, covering the concerns of investors, host countries, home countries, and civil society. In spite of the authors' different starting points, some themes run through a number of the chapters.

An investment regime that would be considered legitimate by the principal parties ought to eliminate the role of power in the protection of investors, but nothing in the current regime explicitly restrains home countries from using their aid, market access (under GSP, for example), or their votes in multilateral financial institutions on behalf of threatened investors. Yet, I believe that the existing regime does somewhat reduce such interventions by home governments. Home governments intervene largely because their investors use political access to demand help. Increasingly, however, home governments are able to deflect the demands of their investors, or at least to respond in lukewarm ways, because they can legitimately tell investors in

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5 The highly publicized (in 2006) proposed acquisition by Dubai World Ports of port facilities in the United States already in the hands of a British investor illustrates the sensitivity even in a rich country to the origin of foreign direct investment.
to provide them protection already, through investment treaties. That is progress.

To be completely accepted by developing countries, however, an investment regime should also impose behavioral rules on foreign investors. So far, rules have been compulsory only for those that home countries favor, such as restrictions on bribery; they have been voluntary for those sponsored by NGOs. Although some NGOs have supported behavioral rules in bilateral investment treaties, it is not so clear that their preferences match completely the preferences of developing host countries. NGOs' interests in human rights and investment have resulted in attempts to use courts in investors' home countries to counter violations abroad, but the cases have produced a mixed record that is not entirely satisfactory to the NGOs.

The authors of chapters in this volume disagree somewhat on how inconsistent decisions under the arbitral regime are. I look not only at the frequently cited cases—for example, involving Argentina and the Czech Republic—of alleged inconsistencies, but also at the calculations of awards, where I see largely chaos. Although arbitration is not supposed to be based on precedents, the fact is that decisions increasingly draw on precedents. This reflects, I believe, the search for common law, in the absence of a rich body of legislation to guide arbitrators. It ought to lead toward consistency. But until there is an appeals process to resolve conflicting decisions and to force fuller statements of panels' reasoning, the development of that law is slower than it need be. I recognize the problems of building common law in a world in which different treaties have different provisions; however, the existence of an appellate body would itself likely lead toward more common language, as parties to agreements support provisions with meanings that have been clarified. An appeals process could also increase the perception of legitimacy on the part of the developing countries, if it explicitly calls for representation of both host and home countries.

In the end, the backlash from developing countries is itself sufficient justification to reexamine the system. Perceptions matter. I personally do not believe that a system that supports rigidly the freezing of terms of investment agreements for twenty-five or more years has a chance of being universally accepted by developing countries. Especially in the poorest of them, agreements are often negotiated by officials without the skills required to protect national interests. Corruption often underlies terms, corruption that is difficult to prove or which subsequent officials are reluctant to bring up. Agreements have often assigned risks to host countries that they are unable to bear, in a financial crisis for example. No government can

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6 Noel Maurer at Harvard Business School is documenting the link between the desire of U.S. officials to avoid the foreign policy costs and their support of international dispute settlement.


8 Although the distinction may be declining, as developing countries build their own multinational enterprises, the perception of host and home is still very important in how countries see their interests.
resist the political pressures to change long-term deals in the face of what appear to
the public to be obscene profits from the country’s natural resources or from low-
risk public utilities. An investment regime must recognize that an agreement
negotiated for this long a period is unlikely to last in the face of new governments,
increased skills, changed prices for raw materials, or financial crises. Any revised
regime should ensure that investors are treated reasonably, but it must also recog-
nize that bonanzas from bad agreements or changed circumstances impose unac-
ceptable political and economic costs on host countries.

In the best of all worlds, investors would not need international protection of their
property rights or rules covering their behavior within host countries. Domestic
justice systems would protect their property rights, although perhaps with different
balances in different countries. Investor behavior would be responsive to adequate
and reasonable domestic regulation. A multilateral agreement would have to deal
only with government commitments and issues that truly spill over borders. It
might, for example, parallel trade agreements in assuring a certain degree of market
access. It might restrict home government support of investors abroad. And it would
deal with special problems that arise because of multinationality, such as those
involving reporting and taxation. But this is not the best of all worlds, and some sort
of more comprehensive international regime will be needed for a long time. The one
that we now have has arisen haphazardly and can surely be improved. In fact, the
current backlash by some host countries and the costs, delays, and unpredictability
demand change. The authors of chapters in this book not only explore in more
depth problems with the existing system, but they also make various proposals for
improvement.

Louis T. Wells
Herbert F. Johnson Professor of International Management
Harvard Business School
Acknowledgments

The Vale Columbia Center on Sustainable International Investment held the Second Columbia International Investment Conference entitled, “What’s New in International Investment Law and Policy?,” on October 30–31, 2007, at Columbia University. We would like to acknowledge and thank the sponsors of that event, Mark and Gail Appel, without whom the Conference would not have happened. We would also like to thank the co-organizers of the event: the Vale Columbia Center on Sustainable International Investment (a joint center of Columbia Law School and the Earth Institute at Columbia University); the Center on Global Legal Problems, Columbia Law School; the Integration and Trade Sector, Inter-American Development Bank; and the American Society of International Law.

The core of this publication consists of original contributions prepared and presented at the Conference and subsequently finalized in light of the discussions at that event. Special recognition is due to the distinguished authors of this volume and the rapporteur of the Conference for their contribution to the international debate on some of the challenges that the international investment law and policy regime is facing and, more importantly, different ways to address these challenges. They benefited from the feedback they received from the Conference’s lively participants and the active discussions chaired by Katharina Pistor and Merit E. Janow.

Michael O’Sullivan led the organization of the Conference and energetically dealt with logistical issues relating to the early stages of preparing this volume, working in particular with Maria Estenssoro and Chrysilla Bautista and supported by Jan Peter Sasse, Edward Platt, and Carlos Mauricio Mirandola. Lisa Sachs, too, helped make this publication possible.

To all of them: thank you very much!

José E. Alvarez
Hamilton Fish Professor of International Law and Diplomacy
Columbia Law School

Karl P. Sauvant
Executive Director
Vale Columbia Center on Sustainable International Investment

Kamil Gérard Ahmed
Columbia Law School/Akin Gump Strauss Hauer & Feld LLP

Gabriela P. Vizcaíno
Columbia Law School/Universidad de Buenos Aires
Editors and Contributors

Kamil Gérard Ahmed is an associate in the corporate practice group of Akin Gump Hauer Strauss and Feld LLP in New York. He practices in the areas of private and public mergers and acquisitions, cross-border transactions, restructurings, financings and securities transactions. Mr. Ahmed has represented North American, European and Middle Eastern companies, underwriters, issuers and government entities in a number of industries, including financial services, oil and gas and nuclear energy. He graduated from the LL.M. program at Columbia Law School with highest academic honors, where he focused on the law and economics of foreign direct investment and international financial systems. Prior to that, he worked at a leading Canadian law firm and graduated from the joint JD/MBA program at the University of Toronto where he was on the Dean’s List. Mr. Ahmed has published a number of scholarly articles. He is admitted to the bars of New York and Ontario and is from Montreal, Québec, Canada.

Stanimir A. Alexandrov is a partner with the Washington, DC, office of Sidley Austin LLP and co-chairs Sidley’s international arbitration practice. He practices in the areas of international dispute resolution, including investor-state arbitration and international commercial arbitration, and resolution of trade disputes before the WTO. He has advised and represented private parties and governments in arbitration before ICSID, as well as in ICC, UNCITRAL, and AAA international arbitration. Mr. Alexandrov has been appointed to the ICSID’s Panel of Arbitrators and the Panel of Conciliators and has served as an arbitrator in a number of investor-state disputes. He has appeared as an expert witness in international arbitration on matters of interpretation of investment treaties. Mr. Alexandrov is a professorial lecturer at the George Washington University Law School in Washington, DC. Prior to entering private practice, Mr. Alexandrov was Vice Minister of Foreign Affairs of Bulgaria, and a negotiator of trade and investment agreements.

José E. Alvarez is the Herbert and Rose Rubin Professor of International Law at New York University School of Law. He is past president of the American Society of International Law. Mr. Alvarez is a graduate of Magdalen College, Oxford University, and Harvard Law School. Formerly an attorney-adviser at the U.S. Department of State, he has also held appointments at Columbia Law School, the University of Michigan Law School, and George Washington University Law School. Mr. Alvarez also has been an International Affairs Fellow at the Council on Foreign Relations,
where he is a member, and has served on the Board of Editors of the *American Journal of International Law* and the *Journal of International Criminal Justice*. His principal areas of publishing and teaching are international law, especially international organizations; international tribunals; war crimes; international legal theory; and foreign investment. His lectures at The Hague Academy of International Law in August 2009, entitled "A New Public International Law Regime for Foreign Direct Investment," are expected to be published in 2010.

**Andrea K. Bjorklund** is Professor of Law at the University of California, Davis, School of Law. She teaches courses in international arbitration and litigation, international trade, international investment, international business associations, conflict of laws, and contracts. She is co-rapporteur of the International Law Association's Study Group on the Role of Soft-Law Instruments in International Investment Law and adviser to the American Law Institute's Project on a Restatement of the U.S. Law on International Commercial Arbitration. She has written extensively on investor-state arbitration issues, and has published chapters in several books, such as the *Oxford Handbook of International Investment Law*, as well as pieces in several journals. She is also co-author of *Investment Disputes Under NAFTA: An Annotated Guide to NAFTA Chapter 11* (Kluwer 2006; updated 2008, 2009). Prior to entering the academy, Ms. Bjorklund worked on the NAFTA arbitration team in the U.S. Department of State’s Office of the Legal Adviser, and also worked for Commissioner Thelma J. Askey on the U.S. International Trade Commission and in private practice at Miller & Chevalier in Washington, DC. A graduate of Yale Law School, she clerked for Judge Sam J. Ervin, III, on the U.S. Court of Appeals for the Fourth Circuit.

**John Cobau** is Chief Counsel for International Commerce at the U.S. Department of Commerce, serving as the lead attorney for the International Trade Administration. Since coming to the Department of Commerce in 1997, Mr. Cobau has been personally involved in the negotiation and implementation of many international agreements, including free trade agreements, textile agreements, and multilateral trade agreements. He was actively involved in the enactment and implementation of the Foreign Investment and National Security Act of 2007. He spent 2007 as Director for International Trade and Investment at the National Security Council. Before coming to the Department of Commerce, Mr. Cobau practiced trade law with a private firm in Washington, DC, for four years. He is a graduate of Princeton University and the University of Michigan Law School.

**James Crawford** is the Whewell Professor of International Law at the University of Cambridge and a Fellow of Jesus College, Cambridge. He is a Senior Council (NSW) and a member of the English bar, practicing from Matrix Chambers. He was the first Australian member of the United Nations International Law Commission (ILC) and was responsible for the ILC’s work on the International Criminal Court during 1994 and for the second reading of the ILC Articles on State Responsibility in 2001. In addition to scholarly work on statehood, collective rights, investment law, and international responsibility, he has appeared frequently before the International Court of Justice and other international tribunals, and is engaged as expert, counsel, and arbitrator in international arbitration.
John H. Dunning was engaged with researching the economics of FDI and multinational enterprises since the 1950s. He authored, co-authored or edited forty-four books on this subject as well as on industrial and regional economics. He was Emeritus Professor of International Business at the University of Reading and State of New Jersey Professor of International Business at Rutgers University. In addition, he was Visiting Professor at several universities in North America, Europe, and Asia. He had honorary doctorates from six leading European and Asian universities, and was an honorary Professor of International Business at the University of International Business and Economics at Beijing. In 2002, he received the Distinguished Scholar in International Management award at the Academy of Management and, in 2004, he was honored with a lifetime award for his contribution to international business studies by the European International Business Academy. In 2008 he received the honor of Officer of the British Empire from Queen Elizabeth II.

Roberto Echandi is Director of the Program on International Investment and member of the faculty at the World Trade Institute, University of Bern, and member of the faculty at the Master’s Program on International Economic Law and Policy at the University of Barcelona. He has been Ambassador of Costa Rica to the Kingdom of Belgium, Grand Duchy of Luxembourg, and the European Union, and Chief Negotiator for Costa Rica for the Association Agreement between Central America and the European Union. He received his LL.M. and undertook his doctoral studies in International Trade Law from the University of Michigan School of Law. He also holds his M.Phil. in Latin American studies from the University of Oxford and an LL.B. from the University of Costa Rica. He has also served as Adjunct Professor of Law at Georgetown University Law Center, Director-General for International Trade at the Ministry of Foreign Trade of Costa Rica, Special Adjunct Ambassador for U.S. Trade Affairs, and legal adviser to the Appellate Body Secretariat of the WTO. Mr. Echandi has published several books and articles examining investment issues, dispute settlement, trade in services, and the evolution of regional economic integration in the Americas.

Susan D. Franck is Associate Professor at Washington & Lee University School of Law where her teaching and scholarship relates to international economic law and dispute resolution. Ms. Franck has been an Assistant Professor at the University of Nebraska Law College, a Visiting Professor at the Vanderbilt University School of Law and a Visiting Associate Professor at the University of Minnesota Law School. Before returning to the academy, Ms. Franck practiced in the area of international economic dispute resolution on both sides of the Atlantic at Wilmer, Cutler & Pickering and Allen & Overy. She received her B.A., summa cum laude, in Psychology and Political Science from Macalester College in 1993 and her J.D., magna cum laude, from the University of Minnesota in 1998. Thereafter, Ms. Franck received a U.S.-U.K. Fulbright Grant to study international dispute resolution at the University of London where she received an LL.M. with merit. She has published articles in journals such as the American Journal of International Law, Fordham Law Review, Harvard Journal of International Law, Minnesota Law Review, and North Carolina Law Review.
Rainer Geiger is a senior adviser to OECD and the Arab Centre for the Development of the Rule of Law and Integrity. He is a graduate of the University of Heidelberg in Germany and Columbia Law School, holding both a Ph.D. and an advanced law degree. He began his professional career in the Ministries of Economics and Economic Cooperation in Germany and served as Secretary of the Finance Commission of the Conference on International Economic Co-operation in Paris. In 1977, he joined the OECD, holding different positions in the areas of investment, competition, and governance and served until 2008 as Deputy Director for Financial and Enterprise Affairs. From 1995 to 2005, Mr. Geiger was chairperson of the Executive Board of the Centre for Private Sector Development in Istanbul, Turkey, and until 2008 Co-chair of the Investment Compact for South East Europe. Since 1987, Mr. Geiger has been teaching a doctorate program in international economic law at the University of Paris I, Panthéon-Sorbonne. Mr. Geiger has published numerous articles in the field of investment, development, competition, and corporate governance.

Joachim Karl is Chief of the Policy Research Section in the Division on Investment and Enterprise of UNCTAD. Before joining the United Nations in November 2005, he worked for seven years on international investment matters at the OECD and the Energy Charter Secretariat in Brussels. He started his professional career in the German Ministry of Economics in 1987, where he dealt with regional state aids, European Law issues, and the negotiation of international investment agreements. Mr. Karl holds a Ph.D. in international law from the University of Konstanz in Germany, and a Master of Public Administration degree from Harvard’s John F. Kennedy School of Government. He has written numerous articles on European law and international investment issues and was a lecturer at the German Federal Academy of Public Administration.

Sarianna M. Lundan holds the Chair in International Management and Governance at the University of Bremen in Germany. She is also an Associate Research Fellow at ETLA, the Research Institute of the Finnish Economy in Helsinki. She has published widely in journals and books, and has co-authored with John H. Dunning the second edition of Multinational Enterprises and the Global Economy, which has become an influential reference work in the field of international business. She has contributed to several research projects funded by UNCTAD and the Commonwealth Secretariat on the preconditions and impact of foreign investment, particularly in connection with the environmental and social impact of multinational enterprises. In 2009 she was elected Fellow of the European International Business Academy.

Howard Mann has been active in the field of international investment law since the mid-1990s. He is the Senior International Law Adviser at the International Institute for Sustainable Development (IISD) and was the founder of IISD’s Investment and Sustainable Development program. He has published numerous articles on issues related to investment law and sustainable development, and was lead author of IISD’s 2005 Model International Agreement on Investment for Sustainable Development, the leading comprehensive alternative model agreement in the field. As international lawyer for the Government of Canada he worked on
various international negotiations, including climate change and the NAFTA environmental negotiations. He received his law degree from McGill University and holds an LL.M. and Ph.D. from the London School of Economics. He has taught at the University of Ottawa Law School and lectures at conferences across the globe on investment law and sustainable development issues.

Petros C. Mavroidis is Edwin B. Parker Professor of Foreign & Comparative Law at Columbia Law School and Professor of European Union and WTO Law at the University of Neuchâtel. He also serves as chief co-rapporteur at the American Law Institute for the project “Principles of International Trade Law: The WTO.” He has recently published Trade in Goods (Oxford University Press, 2007) and The Law and Economics of Contingent Protection (with Patrick Messerlin and Jasper Wauters, Edward Elgar, 2007). Professor Mavroidis previously served as chair for Competition Law at European University Institute, Florence, and as a member of the Legal Affairs Division at the WTO. He is a graduate of the University of Heidelberg, Germany, and holds an LL.M. from the University of California at Berkeley, an LL.M. from the Institut d’Etudes Européennes, U.L.B., Belgium, and an LL.B. from the University of Thessaloniki, Faculty of Law and Economic Science.

Peter T. Muchlinski is Professor in International Commercial Law at the School of Oriental and African Studies (SOAS), University of London. He is the author of Multinational Enterprises and the Law (2nd ed., Oxford University Press 2007) and is co-editor (with Federico Ortino and Christoph Schreuer) of the Oxford Handbook of International Investment Law (Oxford University Press 2008). He acts as an adviser to the United Nations Conference on Trade and Development (UNCTAD) on investment law issues. Until its dissolution in 2008, he was co-rapporteur to the International Law Association Committee on the International Law on Foreign Investment. He is currently a member of the ILA Committee on Non-State Actors in International Law.

Jeffrey D. Sachs is Director of the Earth Institute, Quetelet Professor of Sustainable Development, and Professor of Health Policy and Management at Columbia University. He is also the Special Adviser to United Nations Secretary-General Ban Ki-Moon on the Millennium Development Goals, and the president and co-founder of Millennium Promise, a nonprofit organization aimed at ending extreme global poverty. Mr. Sachs is internationally renowned for his work as an economic adviser to various governments and for his work with international agencies on problems of poverty reduction, debt cancellation, and disease control. He was named one of the one hundred most influential people in the world by Time Magazine in 2004 and 2005; and is the author of the New York Times bestsellers The End of Poverty (Penguin 2005) and Common Wealth (Penguin 2008). He is the recipient of several awards and honors, including the Sargent Shriver Award for Equal Justice and the Centennial Medal from the Graduate School of Arts and Sciences at Harvard University. Mr. Sachs holds honorary degrees from universities around the world.

Karl P. Sauvant is the Founding Executive Director of the Vale Columbia Center on Sustainable International Investment, Senior Research Scholar and Lecturer in Law at Columbia Law School, co-director of the Millennium Cities Initiative,
Chatham House Foundation Fellow, and Member of the International Advisory Council at the International Center for Corporate Accountability, Baruch College, CUNY. He also serves as Guest Professor at Nankai University, China. He previously served as Director of UNCTAD’s Investment Division. He is the author of, or responsible for, a substantial number of publications. In 2006, he was elected an Honorary Fellow of the European International Business Academy. He completed a Ph.D. at the University of Pennsylvania.

**Brigitte Stern** is Professor at the University of Paris I, Panthéon-Sorbonne, and at the Graduate Institute of International Studies, Geneva. She is also a member of the United Nations Administrative Tribunal. Ms. Stern has served as a consultant and expert for international organizations. She is active in international litigation, acting as Counsel before the International Court of Justice and in international arbitration, acting as Counsel and as Arbitrator (Sole Arbitrator, Member or President) in numerous ICSID, ICC, NAFTA, Energy Charter, and UNCITRAL arbitrations.

**Gabriela P. Vizcaíno** is an associate at Mitraní, Caballero, Rosso Alba, Francia, Ojam & Ruiz Moreno Abogados in Buenos Aires, Argentina, and currently participating in Sullivan & Cromwell LLP visiting lawyers program in New York. She practices in the areas of international commercial transactions, mergers and acquisitions, investment projects, corporate finance transactions, and dispute resolution-related matters. Ms. Vizcaíno obtained her LL.M degree from Columbia University and her Argentine law degree from the University of Buenos Aires, where she regularly teaches courses on corporations, arbitration, and international trade. In addition, she contributed to several international publications, including the Spanish language edition of the *Schlechtriem & Schwenzer Commentary on the U.N. Convention on the International Sale of Goods* (edited by Ingeborg Schwenzer and Edgardo Munoz, Thomson & Aranzadi), expected to be Published in 2011.

**Jörg Weber** is Officer-in-Charge of the Policies and Capacity Building Branch and Chief of the International Arrangements Section in UNCTAD, responsible for implementing the work of the Organization on international investment agreements. He has been with this program since its inception in 1998. Prior to this, Mr. Weber has been a team member of the prestigious annual United Nations publication, the *World Investment Report*, since it was first published in 1991. Mr. Weber joined the United Nations in 1990, working on foreign direct investment and multinational enterprises issues. Since 1998, he has focused on matters related to international investment agreements. Mr. Weber received his Ph.D. from the Free University of Berlin.

**Louis T. Wells** is the Herbert F. Johnson Professor of International Management at the Harvard Business School. He has served as consultant to governments of a number of developing countries, as well as to international organizations and private firms. His principal consulting activities have been concerned with foreign investment policy and with negotiations between foreign investors and host governments. His research interests include multinational enterprises; international business-government relations; foreign investment in developing countries; and foreign investment by firms from developing countries. He was the Coordinator for

James Zhan is Director of UNCTAD’s Investment and Enterprise Division. He has a Ph.D. in economics and was a research fellow at Oxford University. He is the author of a number of books and articles on economic and legal issues. Currently, he leads a number of UNCTAD publication series: World Investment Report; International Investment Policy Series; National Investment Policy Reviews; and Investment Advisory Series. He was the team leader of the series on Global Prospects for Investment and Strategies of Transnational Corporations and UNCTAD’s Transfer of Technology Series. He is Visiting Professor at Nankai University and Senior Adviser to the China International Investment Promotion Council.

Nassib G. Ziadé has been the Deputy Secretary-General of the International Centre for Settlement of Investment Disputes (ICSID) since 2007. He also served between April 2008 and June 2009 as the Acting Secretary-General of ICSID. He is a Visiting Professor at the University of Miami School of Law, where he teaches investment arbitration. A dual Lebanese and Chilean national, Mr. Ziadé has extensive experience in the administration of international legal proceedings and in the management and development of international tribunals. From 1997 to 2007, he served as the Executive Secretary of the World Bank Administrative Tribunal. He is a member of the Court of the London Court of International Arbitration (LCIA), a member of the Permanent Court of Arbitration and a Council member of the International Federation of Commercial Arbitration Institutions (IFCAI). Mr. Ziadé has published extensively in the field of international law, and is a frequent speaker at conferences on a range of legal topics. He is a Patron of the American Society of International Law and a member of its Executive Council. He is the Editor-in-Chief of the ICSID Review—Foreign Investment Law Journal, a member of the Editorial Advisory Committee of International Legal Materials, and a member of the Editorial Committee of the Journal of Arab Arbitration.