

SCOPE AND EVOLUTION OF INTERNATIONAL INVESTMENT LAW

Introduction

International Investments are those investments that are made outside the domestic markets and offer portfolio diversification and opportunities for risk minimization. An investor can make international investments, thereby expanding his horizon of returns. In some cases, it can also help mitigate some systematic risks associated with a specific country's economy. International investing generally expands the eligible instruments for an investment portfolio beyond domestic investments.¹

International investment has become the single most important form of international economic transactions and the most potent vector of integration among economies. It has become more important than trade in delivering goods & services to foreign markets, and it interlocks national economies through increasingly integrated production networks and global value chains.

The presence of multinational enterprises across different international markets has led to a substantial share of international trade taking place within global value chains, thus tightly intertwining investment and trade. Emerging markets are increasingly participating in these developments as both major recipients of Foreign Direct Investment (FDI) and major outward investors.

All types of investments involve risk but international investment may present some special risks which include fluctuations in currency exchange rates, changes in market value (price risk), changes in foreign interest rates, significant political, economic and social events (geopolitical risk), lower liquidity, less access to important information and varying market operations and procedures.

Hence, despite the espousal of investing internationally by economists and advisors, most investors' portfolios are still dominated by domestic securities. This establishes the need for a robust legal regime for international investment to balance the legitimate economic and social concerns of the host countries and those of investors. Without such a legal framework, multinational corporations will lose profitable opportunities and poor countries will not

gain the contributions that foreign investment can make toward alleviating poverty.

International investment law is the field of international law that governs relationships between states and foreign investors. This paper examines the scope and evolution of the same.

Tracing the Evolution of International Investment Law

Unlike WTO law, the system of international investment law does not have any central treaty or institution. Despite the economic importance of international investment, there is no comprehensive set of rules governing this subject matter. International investment law consists of certain treaties and agreements.

The end of the Second World War, was marked by large-scale nationalisations. The need was felt for creating a broad organisational framework for the post-war economy. The first attempt was made to formulate international principles concerning FDI in the Havana Charter of 1948, which also established International Trade Organisation which dealt mainly with international trade.

The Havana Charter for an International Trade Organization, 1948 recognised the need and importance of international investments under Article 12, which states that international investment is of "*great value in promoting economic development and reconstruction and consequent social progress*". Article 12 called upon States to enter into bilateral and multilateral agreements relating to the opportunities and security for investment.²

Investment Treaties

International investment law largely comprises of more than 3,200 International Investment Agreements and Bilateral Investment Treaties and investment chapters in preferential trade agreements (collectively referred as Investment Treaties).

The world's first Bilateral Investment Treaty (BIT) was signed on November 25, 1959 between Pakistan and Germany. Since then, the number of such treaties has grown steadily. The most dramatic increase occurred during the 1990s, the decade

- ¹James Chen, International Investing Investopedia, available at <https://www.investopedia.com/terms/i/international-investing.asp> (Last visited on 24th April 2020)
- ²Havana Charter, World Trade Organization, available at https://www.wto.org/english/docs_e/legal_e/havana_e.pdf (Last visited on 24th April 2020)

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that marked the opening up of most economies by liberalisation and globalisation measures. By the end of 1999, BITs reached a total of 1,857.³ Currently, there are more than 2,500 BITs in force.

The investment treaties aim to attract foreign investment in order to promote economic development. This is done by providing foreign investors and their investments with certain protections, including some protections that go beyond those available to the domestic investors. These may include obligations on the home state to not expropriate property, not to discriminate against the investor, and to provide 'fair and equitable' treatment to the investor.

However, this aim of investment treaties to protect foreign investors and encourage FDI flow alone is no longer sufficient and needs expansion. In particular, investment treaties need to recognise, in addition, the need to promote sustainable development and FDI flows that support this objective. Further objectives include the protection of public welfare and human rights, including public health, labour standards, safety, and the environment. Especially more vulnerable economies may require dedicated international support through investment treaties.⁴

Domestic Investment Legislation

These investment treaties are supplemented by domestic investment legislation. Most countries have enacted laws governing foreign investments. Such laws typically include procedures for settling disputes - often designating a forum for dispute resolution.

The investment regime, increasingly provides the legal benchmark for national rule-making on investment. The international and national investment frameworks together regulate what international investors and governments can and cannot do. For instance, licenses, authorisations, permits and similar rights conferred pursuant to domestic laws.

For example, 'Natural persons' that are covered by the Energy Charter Treaty⁵ are defined by reference to each state's domestic laws determining citizenship or nationality but also extends coverage to permanent residents: 'Investor' means: "a) with respect to a Contracting Party: i) a natural person having the citizenship or nationality of or who is permanently residing in that Contracting Party in accordance with its applicable law."⁶

Free Trade Agreements

Apart from investment treaties, regional Free Trade Agreements (FTAs) also form the body of investment law. A free trade agreement or treaty is a multinational agreement according to international law to form a free-trade area between the cooperating states. In other words, it is a pact between two or more nations to reduce barriers to imports and exports among them. Under a free trade policy, goods and services can be bought and sold across international borders with little or no government tariffs, quotas, subsidies or prohibitions to inhibit their exchange. FTAs contain investment chapters.⁷

For example, the United States currently has a number of free trade agreements in place. These include multi-nation agreements such as the North American Free Trade Agreement (NAFTA), which covers the U.S., Canada and Mexico, and the Central American Free Trade Agreement (CAFTA), which includes most of the nations of Central America. The U.S. also has separate trade agreements with a number of nations from Australia to Peru.

At present, the United States has free trade agreements in force with 20 countries. These agreements mean that about half of all goods entering the U.S. come in free of tariffs, according to government figures.⁸

- ³Bilateral Investment Treaties 1959-1999, United Nations Conference on Trade and Development, available at <https://unctad.org/en/Docs/poiteiid2.en.pdf> (Last visited on 24th April 2020)
- ⁴Karl P. Sauvant, The evolving international investment law and policy regime: Ways forward, International Centre for Trade and Sustainable Development, available at <https://www.ictsd.org/bridges-news/bridges-africa/news/the-evolving-international-investment-law-and-policy-regime-ways> (Last visited on 24th April 2020)
- ⁵Infra note 6, at 7
- ⁶Catherine Yannaca, International Investment Law: Understanding Concepts and Tracking Innovations, Organisation for Economic Co-operation and Development, available at <https://www.oecd.org/investment/internationalinvestmentagreements/40471468.pdf> (Last visited on 24th April 2020)
- ⁷Free Trade Agreement, Investopedia, available at <https://www.investopedia.com/terms/f/free-trade.asp> (Last visited on 24th April 2020)
- ⁸Free Trade Agreements, Office of the United States Trade Representative, available at <https://ustr.gov/trade-agreements/free-trade-agreements> (Last visited on 24th April 2020)

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The European Union is another notable example of free trade. The member nations form an essentially borderless single entity for the purposes of trade and the adoption of the euro by most of those nations smooths the way further.

The Energy Charter Treaty

There is also one relevant subject specific investment agreement, the Energy Charter Treaty. The Energy Charter Treaty is an international investment agreement that establishes a multilateral framework for cross-border cooperation in the energy industry.

The Energy Charter Treaty was signed in December 1994 and entered into legal force in April 1998. Currently there are 53 Signatories and Contracting Parties to the Treaty, although neither Canada nor the United States is a party.⁹

The Treaty's provisions focus on the following broad areas:

- the protection of foreign investments, based on the extension of national treatment, or most-favoured nation treatment (whichever is more favourable) and protection against key non-commercial risks;
- the resolution of disputes between participating states, and - in the case of investments - between investors and host states;

The treaty is responsible for the protection of foreign direct investment. Its provisions protect investors and their investments from political risks involved in investing into a foreign country such as discrimination, expropriation, nationalisation, breach of contract, damages due to war, etc. The treaty is legally binding in nature.

Investor-State Dispute Settlement

Investment treaties frequently permit foreign investors to directly bring legal challenges against the government of the state in which their investment is held, through a process known as 'investor-state dispute settlement' (ISDS).

The obligations of governments under international investment law vary depending on the provisions of the relevant treaty. However, certain concepts are common to the majority of investment treaties. Investment tribunals are not bound to follow decisions of prior tribunals, but in practice, tribunals very often rely on the decisions of earlier tribunals, including decisions made in relation to other investment treaties.

A common element of investment treaties is the ability of an investor to invoke the compulsory dispute settlement provisions of the treaty and to initiate arbitral proceedings against a host state with the possibility of claiming damages for breach of one or more of the disciplines of the treaty. A state's consent to arbitration is established by its ratification of the investment treaty. It is not necessary for a state to establish consent on an individual basis for each dispute.

Common forums for such arbitrations include the International Centre for the Settlement of Investment Disputes (ICSID) and the Arbitration Institute of the Stockholm Chamber of Commerce. The applicable law for such disputes comprises the international investment agreements, the domestic laws of the state, and relevant rules of general public international law.

ISDS was originally envisaged as a way to protect investors from arbitrary state abuse. This had the ultimate goal of promoting foreign investment between state parties. Nowadays, there are concerns that ISDS has the potential to disturb social and environmental regulation by allowing corporations to sue governments when such regulation negatively impacts their investments.¹⁰

In recent years, some states have responded to concerns about the fairness of compulsory arbitration by refusing to participate in the arbitration. Other states have terminated their consent to dispute settlement in certain arbitration forums. In January 2012, Venezuela denounced ICSID, becoming the third country, after Bolivia and Ecuador, to do so.¹¹

• ⁹The Energy Charter Treaty, International Energy Charter, available at <https://www.energycharter.org/process/energy-charter-treaty-1994/energy-charter-treaty/> (Last visited on 24th April 2020)

• ¹⁰Investor state dispute settlement (ISDS), Business & Human Rights Resource Centre, available at <https://www.business-humanrights.org/en/investor-state-dispute-settlement-isds> (Last visited on 24th April 2020)

• ¹¹Elizabeth Whitsitt and Nigel Bankes, The Evolution of International Investment Law and its Application to the Energy Sector, Alberta Law Review, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2778912 (Last visited on 24th April 2020)

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The investment law framework needs to provide clear rules and a suitable mechanism for resolving disputes between these the two actors. Governments can develop national investor-state conflict management mechanisms which would allow governments and investors to address their grievances at the domestic level before they escalate into full-blown legal disputes and move the international tribunals. Another major reform that can be looked into involves the establishment of appeals mechanism.

Moreover, the international investment law should provide international support to help all economies become more attractive for international investors and help to establish a level playing field by providing administrative and legal assistance.

Special focus should be on assisting developing countries during negotiation of which bilateral investment treaties and investment agreements.

An improved investment regime, providing the enabling framework for increased flows of sustainable FDI is imperative. Recognizing how immensely FDI can contribute to economic development, all governments want to attract it. Indeed, this has led to fierce competition in all countries for attracting foreign capital. Countries, especially developing nations, seek such investment with liberal policy frameworks and are paying more attention to measures that actively facilitate it. Entire world economy is reaping benefits of international investments which have globally led to creation of a new world economic order.



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