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MUTATIONS OF NEO-LIBERALISM IN INTERNATIONAL INVESTMENT LAW

MUTHUCUMARASWAMY SORNARAJAH*

Over the past few decades, international investment law has been increasingly used as an instrument for neo-liberalist ideals. However, inspite of the repeated failures of neo-liberalism in international investment law, its adherents put forth new arguments and find new ways to augment these ideals, often cloaking old ideas in new forms in support of their ideals. In furtherance of this proposition, Part II of this article first discusses the four stages of international investment law, with particular focus on the third and fourth phases – neo-liberalism and normlessness. Part III of this article, after examining the arguments of recent investment law scholarship that absolute protection of foreign investments is a recent phenomenon, argues that such scholarship is a rehash of the ideals that had surfaced during the dominance of the neo-liberalism phase in international investment law. Part IV of this article illustrates and discusses how various states that are members of numerous investment treaties have reacted to the expansive interpretations of treaty provision by arbitrators. It also shows how states have reversed their earlier stances when their own interests were affected. As a counter to these neo-liberalist ideals, this article argues that international lawyers with a TWAIL perspective should confront and defeat these neo-liberal tenets in the interests of the third world. Further, the developing countries as a whole, should put forth a collective stand and be united in their opposition to investment treaties which would otherwise engender them to surrender their control over their natural resources.

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I. INTRODUCTION

A wounded beast struggling to survive, neo-liberalism¹ continues to take on new forms and guises in order to keep itself alive in international investment law. Its adherents are resorting to new arguments or rehashing old ones in the hope that the function of investment protection, unaffected by competing concerns of human rights, environmental protection and labour standards, can be preserved. The formulation of new principles in resistance to change that is brought about through the creation of possible new instrumental models, results in mutations in the legal reasoning, thrown up during the febrile decline of neo-liberalism. The formulation of these principles is being resisted within the discipline and has led to schisms amongst arbitrators as well as amongst academic commentators. The surprising mutations that have been advocated in order to keep neo-liberal visions alive despite the obvious global failure neo-liberalism has suffered as a result of the global economic crisis, is an indication of the vitality of neo-liberal instrumentalism in international investment law.

Over the last few decades, international law has become the instrument through which the tenets of neo-liberalism relating to foreign investment were thrust upon the world. The assumption upon which the law was constructed was that foreign investment was so essential to economic development that its flow should be facilitated through its absolute protection. This assumption, however, may be contested. History demonstrates that foreign investment was a means of exploitation of host economies. Though its enormous potential for increasing

¹ Neo-liberalism in this context refers to the revival of market fundamentalism in the post-Cold War era, which saw the market system of the United States triumphant over the communist system as a result of the dissolution of the Soviet Union. *See*, FRANCIS FUKUYAMA, *THE END OF HISTORY AND THE LAST MAN* (Penguin Books 1992). It was the prime model of the period of globalization and formed the dominant economic philosophy of the “roaring nineties”. *See* JOSEPH STIGLITZ, *FREE FALL: AMERICA, FREE MARKETS AND THE SINKING OF THE WORLD ECONOMY* (Allen Lane 2010).

economic development must be recognized, the harm that it could cause to the host economy if its effects (on the economy, social conditions or the environment, for example) remain unregulated has become the basis for the alternative argument that international law should not provide absolute guarantees for foreign investment. Through such absolute guarantees, the instrumentalism of free market fundamentalism fragments international law without paying heed to prescriptions of law relating to the environment, human rights or labour standards. These prescriptions may contain higher norms in the normative hierarchy than those dealing with investment protection. Instrumentalism becomes entrenched when those who resist neo-liberal prescriptions use the same techniques to argue for conflicting models. But, as a result of its early dominance in the field, neo-liberal principles will continue to show vitality, particularly because the dominant transnational class prefers to maintain such vitality by recasting the old structure in new forms.

The continuance of international institutions and hegemonic powers which support neo-liberal instrumentalism assures that in the absence of caution, there will be a revival of this hydra-headed apparition in the future.² Ideas have a cyclical pattern; if in decline at a stage of history, they lurk about until events become propitious for them to be revived. There will be a time when a revival of neo-liberalism will resurface but during the present time of its decline, posterity should have a record of the debates that took place within international investment law so that during a future revival of neo-liberalism, the manner in which it was dealt with in the past is known. It can then be confronted in a more assured fashion than it was in the present round of its triumph and retreat.³ It is necessary that lawyers belonging to TWAIL⁴ confront neo-liberal views so that the other side is heard.

² In the earlier periods, the law on foreign investment appeared in various guises. It took the form of international law on the basis that its rules are drawn from general principles of international law. See Lord Arnold McNair, *General Principles of Law Recognized by Civilized Nations* 33 BRIT. Y.B. INT'L L. 1 (1957). It took the form of transnational law on the basis that foreign investors did not have personality in international law. See PHILIP JESSUP, *TRANSNATIONAL LAW* (Yale Univ. Press 1956). Some would regard it as an aspect of *lex mercatoria*. When the law was constructed there was the same search for rationalization of a phenomenon that could not easily be fitted into the existing theories of international law. Mutations of theory had to take place in the making of the law.

³ On the retreat of neo-liberalism, see M. Sornarajah, *Towards Normlessness: The Ravage and Retreat of Neo-Liberalism in International Investment Law*, 2 Y.B. INT'L INVESTMENT L. 595 (2010).

⁴ TWAIL is a movement of Third World international lawyers whose main purpose is to articulate a different vision of international law that does not depend on the rules brought about by the powerful states in the past. It believes that much of Eurocentric international law was created without the consent of the peoples of Africa, Asia and Latin America at a time when they were in colonial subjugation. They argue for the revision of

The unfortunate fact is that the increasing publication of journal articles and books in the developed world by younger scholars eager to join the neo-liberal bandwagon has witnessed a profusion in the articulation of neo-liberal views. A search is assiduously being made for more reasoned means through which neo-liberal norms may be kept alive and as a result, mutations of the neo-liberal order are being preserved in new clothing. As in the past, we will soon be seeing a new crop of publicists reinforcing the mutations created by each other and foisting it upon the world as the wisdom of international law. However, the approaches that have been taken lack uniformity and convergence.

This lack of uniformity in development of the defence of neo-liberalism is in itself an indication of its decline, a relapse of the single hegemonic model that drove the law in the post-Cold War period. The hegemonic power itself seems to have retreated from the model: from its inception, the dominant trends in the international law of foreign investment have been shaped by the United States (“US”), but the US is retreating from adherence to the old law which stressed absolute standards of investment protection. The 2004 Model Investment Treaty of the US, in contrast to the earlier model, contains features that undermine the strong protection of foreign investment the US has insisted upon in the past.⁵

The retreat from neo-liberalism has led to the revival of an intense conflict of norms. In this context of norm-conflict, each interest group asserts the set of norms it prefers. The tried-and-true technique of reiterating law through repetition continues, although it is somewhat dented as a result of the challenge mounted not so much by developing country lawyers but by the powerful groups motivated to challenge the neo-liberal model in order to enhance environmental and human rights interests.⁶ But what is more insidious than repetition of the old norms is the

such law as well as for the creation of a more just law that takes into account the needs of the people of the Third World. They view existing international law as based on structural inequities and seek its reform. *See generally*, Makau Mutua, *What is TWAAIL?*, 94 AM. SOC’Y INT’L L. PROC. 31, 36 (2000); Antony Anghie, *The Evolution of International Law: Colonial and Postcolonial Realities*, 27(5) THIRD WORLD Q. 739-753 (2006) available at: <http://ptw.uchicago.edu/Anghie09.pdf>.

⁵ For a comparison of the 2004 model with the 1994 model, *see* Kenneth Vandevelde, *A Comparison of the 2004 and 1994 US Model BITs: Rebalancing Investor and Host Country Interests*, 1 Y.B. INT’L INVESTMENT L. 212 (2009).

⁶ The Secretary General of the United Nations appointed John Ruggie as Rapporteur on Human Rights and International Business. The Rapporteur has released several reports on various aspects of human rights and foreign investment. For a survey, *see* John Ruggie, *Business and Human Rights: The Evolving International Agenda*, 101(4) AM. J. INT’L L. 819 (2008). For the view that investment law must accommodate standards of sustainability, *see* SUSTAINABLE DEVELOPMENT AND WORLD INVESTMENT LAW (Marie-Claire Cordonier-Seger, et al. eds., Kluwer 2010).

appearance of old norms in new theoretical guises. Because of the manner in which they are dressed, these new explanations of the old norms are immediately attractive. It is necessary to ensure that these new techniques are understood to be a rehashing of old ideas in a manner that is acceptable in light of the tensions that have come about. These new guises are referred to as mutations not in a biological sense, but in the sense that they mimic the original structure though undergoing a change in form.

The neo-liberal episode illustrates the need for TWAAIL. During the highpoint of neo-liberalism, the period beginning with the collapse of the Soviet Union and ending with the global economic crisis, neo-liberalism was rampant due to the belief that it was the single system left standing after the Cold War contest between two distinct economic viewpoints. Its triumph saw the justification for the instrumental use of international law to create rules and institutions that thrust neo-liberal notions upon the global community. The World Trade Organization⁷ (“WTO”) was created with rules on services⁸ and intellectual property⁹. In the area of investment treaties, there was a proliferation of treaty-making leading to the creation of almost 3000 treaties.¹⁰ The resulting number of investment arbitrations enlivened a dormant field, with hundreds of cases involving multi-million claims against developing states¹¹ and big law firms and academic international lawyers alike benefitting from this trend. The “college of international lawyers” outdid each other in demonstrating fervour for the new basis upon which the law could be extended towards furthering neo-liberalism. Unfortunately, neither was there present a concern for poorer states affected or for the fact that the fundamental bases of their discipline was being distorted. It is a sad episode, which demonstrated that greed and not need created international law.¹² As Mahatma

⁷ Marrakesh Agreement Establishing the World Trade Organization, Apr. 15, 1994, 1867 U.N.T.S. 187, 33 I.L.M. 1125.

⁸ General Agreement on Trade in Services, Jan. 1, 1995, Marrakesh Agreement Establishing the World Trade Organization, Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, GATT Doc. MTN/FA, Annex 1B.

⁹ Agreement on Trade Related Aspects of Intellectual Property Rights, Jan. 1, 1995, Marrakesh Agreement Establishing the World Trade Organization, Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, GATT Doc. MTN/FA, Annex 1C.

¹⁰ According to the UNCTAD World Investment Report, the IIA universe at the end of 2009 consists of 2750 BITs and 295 other IIAs. *World Investment Report 2010: Investing in a Low-Carbon Economy* at 81, available at: www.unctad.org/en/docs/wir2010_en.pdf.

¹¹ *Investor-State Disputes Arising From Investment Treaties: A Review*, UNCTAD Series on International Investment Policies for Development (2005), at Box 1: Financial Implications of Investor-State Dispute Settlement, available at: http://www.unctad.org/en/docs/iteit20054_en.pdf.

¹² Muthucumaraswamy Sornarajah, *Law for Need or Law for Greed*, 6 INT'L ENVTL.

Gandhi said, the world has enough to meet man's need but never enough to meet man's greed – and we have witnessed law created to further man's greed being triumphant for a period of time. Although many developed country international lawyers stood firm in upholding the primary values of international law as a force for justice and as a bulwark against exploitation of the weak, it is necessary for a vigorous body of third world international lawyers to ensure that the interests of economic development of the poorer states of the world receive priority in the formulation of international norms. TWAIL performs this essential function. This will ensure that young international lawyers do not forget the basic ideals that fashion international law despite the fact that in its origin and in much of its life, international law as we know it today has been easily subsumed by factors such as power.

It is always necessary that each side in a debate be heard loudly and clearly. This is all the more important as economic studies now indicate that the premise upon which investment treaties proliferated is an uncertain one at best, with serious doubts cast upon the positive correlation between investment treaties and the flow of foreign investment into developing countries.¹³ With this in mind, the present article highlights the arguments currently being used to bolster the case for total investment protection to the detriment of the other considerations (apart from investment protection) that international law demands.

Part II of this article surveys the four stages of the development of international law and investment, while emphasizing the nature of the conflicts that took place at each stage, concentrates on the more recent third and fourth phases – neo-liberalism and normlessness or a return to the period of intense norm conflicts, respectively. Part III examines the argument set forth in recent academic works that universally binding principles of investment protection have emerged in

AGREEMENTS: POL., L. & ECON. 329 (2006).

¹³ There are several studies on the correlation between foreign investment flows and investment treaties. The evidence they present is not conclusive; see THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT: BILATERAL INVESTMENT TREATIES, DOUBLE TAXATION TREATIES, AND INVESTMENT FLOWS (Karl P. Sauvant & Lisa E. Sachs eds., Oxford Univ. Press 2009) for a collection of the principal studies on this subject and an overview. For example, Susan Rose-Ackerman & Jennifer L. Tobin, *Do BITs benefit developing countries?*, in THE FUTURE OF INVESTMENT ARBITRATION (Catherine A. Rogers & Roger P. Alford eds., Oxford Univ. Press 2009) (indicating their marginal utility depending on a variety of circumstances). Some, cautiously, find a positive correlation: see, Mary Hallward-Driemeier, *Do Bilateral Investment Treaties Attract Foreign Investment? Only a Bit and They Could Bite*, World Bank Pol'y Res. Working Paper No. 3121 (2003). There are an increasing number of such studies, but due to their conflicting nature, no definite conclusions can be drawn from them. Nevertheless, the studies subject the orthodox position that BITs promote investment flows to doubt.

various forms over the last few years. This article will argue, however, that the common theme amongst these efforts is the conservation of the principles of absolute protection of foreign investment articulated during the dominance of neo-liberalism. These writings take place towards the end of the third stage and the beginning of the fourth stage, as neo-liberalism begins to undergo stress and retreats. One form of the argument is that a multilateralization of the norms of investment protection has been brought about as a result of treaties, customs or a combination of the different sources of international law. It is an argument that was made soon after the failure of the effort to bring about a multilateral agreement on investment made by the Organization for Economic Co-operation and Development (“**OECD**”) (1995) and after the similar effort to create an instrument on investment under the WTO (2000).

There also continues an effort to portray the norms of investment protection through arbitration as constituting global administrative law. Notions of the rule of law and global governance are pressed into argument for multilateral norms of investment protection on the assumption that, the function of the rule of law is only the protection of the property of the rich and powerful. Another variant of the theme is that customary principles of international law have emerged as a result of recent practice. Though repeatedly refuted, it is an argument that has not disappeared. All this activity, notably, takes place in the narrow period between the third and fourth stages of the development of international law on foreign investment. While elaborating upon these new mutations, this article enumerates the author’s criticisms of the efforts being made to pour old wine into new jars.

The final Part of this article looks at recent treaty practice, concentrating upon how states have reacted to the expansive interpretations placed on treaty provisions in arbitral awards and the future influence these treaties may have on the law in light of their divergence from the stance of absolute investment protection. The varied formulations contained within treaties will inevitably undermine any multilateral code on investment protection. In the alternative, unlike older treaties, such a multilateral code can no longer be based on the aim of absolute investment protection since older treaties contain wide exceptions to responsibility for violation of the norms of investment protection. It is necessary to ensure that the trend towards “balanced” treaties favours the rights attached to the development of the poorer states. To the extent that the balance becomes tilted towards the recognition of social and developmental interests, treaties of protection will become less relevant as their role in the protection of foreign investment will diminish. This Part also deals with the schisms that have opened up within the ranks of arbitrators and examines how these schisms may be redirected towards shaping a result conducive to the creation of a law favouring economic development as understood by the lawyers of developing countries as well.

II. THE FOUR STAGES OF THE INTERNATIONAL LAW ON FOREIGN INVESTMENT

As already discussed above, four phases of the development of international investment law can be identified. The present phase of the law represents the fourth stage in the post-colonial phase of international investment law. As far as norm conflict is concerned, this phase is akin to the very first stage of the international law relating to foreign investment, involving a conflict between two normative prescriptions. In that early period, the contest was between the US and Latin America as investments in the rest of the world largely took place within the colonial context. The American view was that there was an international minimum standard which applied to foreign investment and that this standard mandated that disputes between foreign investors and host states in Latin America should be settled in accordance with an external standard by neutral tribunals sitting overseas.¹⁴ The central concept through which this prescription was advanced was the international minimum standard which had to be maintained by international law.¹⁵ This view was rejected by Latin American states, the recipients of American investments.¹⁶ They argued that a national treatment standard applied and that this standard of treatment permitted national courts to dispose of disputes between foreign investors and their host states according to national law. International law had no role to play or if it did, it merely referred the disputes to national law to be settled by national courts as the final arbiters. The standard was no different from that applied to local investors. The Latin American view was stated in the form of the Calvo Doctrine.¹⁷ This conflict in the first phase of international investment

¹⁴ For novel views on the evolution of American standards, see SANTIAGO MONTT, *STATE LIABILITY IN INVESTMENT TREATY ARBITRATION* (Hart Publishers 2009) (hereinafter MONTT).

¹⁵ The classic statement is in EDWIN BORCHARD, *THE DIPLOMATIC PROTECTION OF CITIZENS ABROAD OR THE LAW OF INTERNATIONAL CLAIMS* (Banks Law Pub. Co. 1916).

¹⁶ “Newly independent states, like the Latin American states had denied the existence of a rule mandating a minimum standard of treatment.” M. SORNARAJAH, *INTERNATIONAL LAW ON FOREIGN INVESTMENT* 123 (3d ed., Cambridge Univ. Press 2010) (hereinafter SORNARAJAH). See also, ANDREW PAUL NEWCOMBE & LLUÍS PARADELL, *LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT* 50 (Kluwer 2009) (hereinafter NEWCOMBE & PARADELL): “Throughout the 1960s and 1970s, Latin American states maintained their general opposition to the minimum standard of treatment and supported the NIEO *Declaration and the Charter of Economic Rights and Duties of States*. Latin American states remained uncomfortable with international investment arbitration, with no Latin American state becoming a party to the ICSID Convention in the 1960s or 1970s.”

¹⁷ DONALD SHEA, *THE CALVO CLAUSE: A PROBLEM OF INTER-AMERICAN AND INTERNATIONAL LAW AND DIPLOMACY* (Univ. of Minnesota Press 1955); Wenhua Shan, *Calvo doctrine, state sovereignty and the changing landscape of international investment law*, in *REDEFINING SOVEREIGNTY IN INTERNATIONAL ECONOMIC LAW* 248 (Wenhua Shan,

law became internationalized with the decolonization of African and Asian states. The latter states espoused the Latin American view whereas the former colonial powers of Europe adopted the American position. The cleavage of views existed between the capital exporting states of America and Europe and the capital importing states of Asia and Africa.¹⁸

It is during the second phase that the newly independent states of Asia and Africa joined with the Latin American states to espouse the New International Economic Order (NIEO), which, among other things, sought to universalize the Calvo Doctrine. The affirmation of the Calvo Doctrine was even stronger in the associated resolution containing the Charter of Economic Rights and Duties of States.¹⁹ The developing states also had, over the years, passed resolutions asserting the doctrine of permanent sovereignty over natural resources.²⁰ These developments were strongly resisted by the developed states, and so the compromise resolution accepting permanent sovereignty over natural resources contained the promise that contracts would be honoured and that disputes arising from the violation of contracts would be settled in accordance with international law. However, this compromise did not last long. The developing countries returned to assert the doctrine of permanent sovereignty over natural resources without any qualifications. They adopted the principle in their national constitutions and in their domestic legislation like the foreign investment codes and mining acts.

Developed states actively sought to reduce the changes being brought about and there were discussions about whether international norms could be created by

Penelope Simons & Dalvinder Singh eds., Hart 2008). For a revisionist view sanitizing the conflict, see MONTT, *supra* note 14, at 38–51.

¹⁸ The first two phases of the international law on foreign investment are described in SORNARAJAH, *supra* note 16.

¹⁹ These norms were advanced through General Assembly resolutions. The reaction was to treat these resolutions as not norm creating despite the fact that they were supported by a large majority of countries. The principal resolutions are the *Charter of economic rights and duties of states*, U.N. G.A. Res. 3281(xxix) of December 12, 1974, U.N. GAOR, 29th sess., Supp. No. 31 (1974) 50, UN Doc. A/9631, reproduced in 14 I.L.M. 251 (1975) (120 votes in favor; six against; ten abstentions); U.N. G.A. Res. 3201 (S-VI) of May 1, 1974 on the New International Economic Order, UN doc. A/res/S-6/3201, reproduced in 13 I.L.M. 715 (1974). The major countries that did not subscribe must be regarded as persistent objectors subscribing to the alternate system of investment protection. This supports the view regarding normlessness. In *Texaco Overseas Petroleum Co./California Asiatic Oil Co. v. the Government of the Libyan Arab Republic*, (1 I.L.M. 88 (1978)) the resolutions were regarded as *lex ferenda*.

²⁰ NICO SCHRIJVER, SOVEREIGNTY OVER NATURAL RESOURCES: BALANCING RIGHTS AND DUTIES (Cambridge Univ. Press 1997).

resolutions of the General Assembly.²¹ During this second phase, the law was kept in a fine balance, for much of the law that had been built up by the developed states also relied on weak sources of international law. They were contained in arbitral awards and in the writings of publicists which in terms of opposability would be weaker law creating sources than solemn resolutions of states made at the General Assembly indicating what their preferred norms of law are. The American assertion of norms had been resisted by Latin American practice. They were later adopted by the newly independent states of Africa and Asia. However, the decisions of arbitrators and writings of publicists were only subsidiary sources of international law at best. In the first two phases, contrary to the law as stated in standard textbooks in the developed world, there was no definite international law on the protection of foreign investment. Instead, a fine balance between the two contrasting sets of norms was retained.

The third phase related to the changes brought about by the preference for market-based solutions. The ascendancy of neo-liberalism in the 1990s²² ensured that the movement of the developing world towards sovereign control over foreign investment and the development of secure norms of investment protection through international law was halted on the ground that investment flows would be promoted through the existence of such norms. In this period, the fine balance that existed between the two sets of conflicting norms was heavily tilted towards the system favoured by the neo-liberal philosophy that came to dominate, at least for a short period, the economic thinking of many states of the world. The triumph of neo-liberalism can perhaps be dated to the dissolution of the Soviet Union, which signaled the end of communism and left democracy and its economic concomitant, the free market theory, as the prevailing philosophies at the end of the Cold War.

The end of neo-liberalism was perhaps the global economic crisis that began in 2008 as a result of the failure of policies based on neo-liberalism. The period between 1990 and 2008 is the third stage of the international law on foreign investment. Neo-liberalism was at its zenith in the first half of the period (1990-1998), when the WTO was formed and the Agreement on Trade-Related Investment Measures²³ was negotiated. With successive economic crises in Asia

²¹ See, for example, BLAINE SLOAN, UNITED NATIONS GENERAL ASSEMBLY RESOLUTIONS (Transnat'l Publishers 1991).

²² The reasons for the ascendancy are the fall of the Soviet Union, the removal of the competing ideology of communism, the decline of aid from developed states, the espousal of the doctrine by the "Washington Consensus" (an alleged conspiracy between the White House, the IMF and the World Bank) and the election of neo-liberals like Thatcher, Reagan and Kohl as leaders of the developed world.

²³ Agreement on Trade-Related Investment Measures, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1868 U.N.T.S. 186

(1998) and Latin America (2000-2002) however, the impetus behind neo-liberalism began to wane. After the 2008 crisis, regulatory control over the economy became the norm and neo-liberalism declined. In the field of international law on investment, this was witnessed by increasing calls for the recognition of the regulatory space of the host state and the resort to nationalization of banks in the developed world during the economic crisis.

During this third phase, international law became an instrument through which the dominant philosophy of neo-liberalism was expressed. In the political sphere, efforts such as the articulation of doctrines permitting forcible intervention to promote democracy were made to ensure the triumph of democracy. The dominance of the US as the single hegemonic power in a rapidly globalizing world ensured that it was able to push through norms based on its own political and economic system.²⁴ The role that a hegemonic power has in shaping international law through infusion of its preferred norms is evident in the international law on foreign investment as well as in other areas of international law.²⁵ It is during this period that one can find the best evidence for the view that a regime for international investment was emerging.²⁶

Trends within international law also favoured the change that was taking place. The fragmentation that took place later in the field has resulted in a plethora of works which have looked at the subject in isolation of the general principles of international law and without regard to the changes taking place in the climate in which international law had to operate. As a result of this fragmentation, the law came to be dominated by arbitrators and commentators who did not have firm grounding in public international law but were more inclined to see it as an extension of international commercial law. Consequently, contract based solutions dominated over concerns with the public interest of states.²⁷ The integrative approach developed did not distinguish between treaty rights and contract rights.²⁸

(hereinafter TRIMS Agreement).

²⁴ The promotion of norms-based democratic governance and market liberalization were clearly projects of the United States. See DEMOCRATIC GOVERNANCE IN INTERNATIONAL LAW (Brad Roth & Gregory Fox eds., Cambridge Univ. Press 2000).

²⁵ During this period, the United States was able to change international law on many fronts. The Bush doctrine on preventive force was announced. The document on intellectual property, the Trade Related Intellectual Property Rights (TRIPS) protected intellectual property of US multinational corporations. The setting up of the WTO was primarily an American project.

²⁶ Those who argue for the existence of an international regime largely focus on developments that took place during this period. See generally, JESWALD SALACUSE, THE LAW OF INVESTMENT TREATIES (Oxford Univ. Press 2010).

²⁷ The point is strongly made in GUS VAN HARTEN, INVESTMENT TREATY ARBITRATION AND PUBLIC LAW (Oxford Univ. Press 2007).

²⁸ Yuval Shany, *Contract Claims vs Treaty Claims: Mapping Conflicts between ICSID Decisions*

It also resulted in an emphasis on the analytical exposition of awards and the texts of treaties on which they are based. Again, technically competent commercial arbitrators are more prone to interpret the words of contracts and treaties that are relevant without regard the desirable outcomes in the law. Alternatively, the only preferable outcome arbitrators have in mind is ensuring that the contract is given effect, since international commerce cannot function unless parties respect the obligations they assumed. Arbitrators influenced by prevailing political tendencies tended to adhere to the views favourable to international business and failed to emphasize the strong public interest elements that exist in investment arbitration.

Yet these third phase developments did not go unchallenged. Within arbitration itself, schisms began to develop. The schisms that have arisen in the field of investment arbitration are best explained in the context of the attitudinal differences that have characterized developments in this area of the law, or as a struggle between two camps. There were those committed to neo-liberal views that required expansion of a system of foreign investment protection based on the values of promoting the free market ideals of sanctity of property, the importance of preserving commercial obligations and free flows of investment. These were promoted to the detriment of other values such as neutrality in arbitration, confining decisions to the consent of the parties, awareness of other values such as the protection of the environment and human rights and the primacy that must be attached to *jus cogens* principles of international law. The idea that investment protection had to operate within a system of international law containing hierarchies of interests and conflicting obligations did not come easily to arbitrators from a background in commercial arbitration, where contractual sanctity is prioritized. Contrastingly, it was also natural that another set of arbitrators prioritizing these values over the values of neo-liberalism should emerge. The fundamental fact that arbitrators brought different visions to their tasks resulted in wide divergences in the law stated in awards. It may also be argued that this divergence was complicated by the need for self-promotion by the arbitrator, since repeated appointments as an arbitrator become practically and realistically possible only if the arbitrator toes the lines drawn by appointing authorities of arbitral institutions or ties in with the goals of multinational corporations and their counsel.

The schisms that have occurred within the international law on foreign investment generally, and foreign investment arbitration in particular, are the result of ideological clashes that took place during years of the dominance of neo-liberalism during the third phase. These schisms are bound to increase in the

on *Multisourced Investment Claims*, 99 AM. J. INT'L L. 835 (2005); JAN OLE VOSS, THE IMPACT OF INVESTMENT TREATIES ON CONTRACTS BETWEEN HOST STATES AND FOREIGN INVESTORS (Martinus Nijhoff 2011).

present fourth phase. With increasing evidence of the failure of neo-liberalism finally manifesting in the global economic crisis in 2008, the schisms will become more pronounced as arbitrators begin to demonstrate a willingness to beat back the gains neo-liberalism made within the field. States too are beginning to assert themselves by pursuing vigorous defences to liability, as a result of which arbitrators have had to decide issues in a context outside the ambit of an inflexible and absolute law on investment protection.²⁹ At the same time, there was an increase in the questioning of the benefits of entering into investment treaties.³⁰ Some states withdrew from the system of treaty arbitration while others made treaties which whittled down the scope for investment protection by curtailing the interpretative extensions that neo-liberal arbitrators had made on the text of investment treaties and by providing for increasingly broad defences justifying state interference with foreign investment.³¹

The vestiges of the law created through neo-liberal thinking will remain until dismantled and the conflict will continue to affect the law for a longer period. The advances that were made during the ascendancy of the period of neo-liberal thinking, however, will be subjected to greater scrutiny. Although the principles upon which investment treaty arbitration rest may not disappear altogether, their force will be dented considerably. One may even argue that this may lead to a decrease in the confidence that foreign investors initially had in treaty based arbitration and that they may begin to look to contractual and other means for protecting their investments. The efforts to maintain the law created on the basis of neo-liberal principles, however, will remain.

²⁹ The Argentinian awards show the best evidence of this. The various aspects of the defence of necessity become prominent in these awards. But, jurisdictional defences like whether the investment was made in accordance with the foreign investment laws of the host state also became prominent. These issues are discussed in subsequent chapters. See Jurgen Kurtz, *Adjudging the exceptional at international investment law: security, public order and financial crisis*, 59 INT'L COMP. L. Q 325 (2010).

³⁰ Discussions broke out among economists and others as to whether it was provable that investment treaties led to greater investment flows. The doubters seem to have the stronger case leading to the question whether the developing states were surrendering their sovereignty without adequate reason. *Supra* note 13.

³¹ Ibironke T. Odumosu, *The Law and Politics of Engaging Resistance in Investment Dispute Settlement*, 26 PENN. STATE INT'L L. REV. 251 (2007).

III. KEEPING MORIBUND NEO-LIBERALISM ALIVE

The Retreat

As in the case of the “Village School Master”, who “though vanquished would argue still”,³² neo-liberal international lawyers continue to find ingenious ways of keeping alive an international law on foreign investment constructed entirely to promote the interests of multinational investment through the recognition of absolute principles of investment protection. The “rustics” are treated to long-winded books, which they cannot afford to buy and repetitious papers too long to read and contain the same message. Repetition is a technique of imperial law making which persists to this day.³³ Their arguments are ingenious, exploiting venerable doctrines like the rule of law and employing traditional rules like those on the formation of custom and arguments drawn from accepted disciplines like human rights and administrative law. All of this is despite the fact that a rapid succession of economic crises, beginning with the Asian economic crisis and culminating in the global economic crisis, has demonstrated the failure of the adoption of neo-liberal policies relating generally to market reform and specifically to international trade and investment.

For some of the developing countries that adopted neo-liberal policies, the consequences have been disastrous and have resulted in spectacularly failed economies. In the field of the law on foreign investment, the failure had left indelible results. In pursuance of the adoption of neo-liberal policies, Argentina had discarded the Calvo doctrine (despite espousing it for nearly a century) and had signed several investment treaties including one with the US. These policies led to an economic crisis and resulted in the need to take measures such as exchange controls and devaluation, which affected foreign investors. These measures also resulted in 46 claims for investment treaty violations, involving billions of dollars.

The only case resulting from the earlier Asian economic crisis did not meet the

³² Oliver Goldsmith, *The Village Schoolmaster*.

“... ”

In arguing too, the parson held his skill,
For e'en though vanquish'd he could argue still;
While words of learned length and thund'ring sound
Amazed the gazing rustics rang'd around;
And still they gaz'd and still the wonder grew,
That one small head could carry all he knew
...”

³³ LAUREN BENTON, *LAW AND COLONIAL CULTURES: LEGAL REGIMES IN WORLD HISTORY 1400–1900* (Cambridge Univ. Press 2001).

initial jurisdictional threshold because of the restrictive nature of the protection that the Asian treaties give to foreign investment. In *Gruslin v. Malaysia*,³⁴ exchange control measures taken by the Malaysian Government were challenged as violating the right to repatriation provided in the UK-Malaysia investment treaty. The tribunal upheld the argument that the treaty protected only “approved” investments. The limitation of granting treaty protection only to approved investments is common in Asian treaties.³⁵ The comparison demonstrates that going all the way with neo-liberalism in the area of foreign investment can have adverse consequences. It is a lesson that has been learnt by many developing countries the hard way.

We now find a retreat from neo-liberal stances of earlier years. Some Latin American states have withdrawn from the International Centre for the Settlement of Investment Disputes (“ICSID”) system, provoking a view that Latin America may return to the days of the Calvo doctrine. Asian states that have had harsh experiences with investment arbitration, like the Philippines, are reluctant to conclude treaties with investor-state arbitration clauses.³⁶ Some developed states are also content to leave investor-state dispute resolution out of their investment treaties.³⁷ The retreat is most evident in the treaty practice of the US. Its 2004 Model Investment Treaty contains many sovereignty-based control devices deviating from traditional and historical stances relating to absolute protection of investments. The Gillard government in Australia announced in April 2010 that it will not sign trade agreements providing for investor – state dispute resolution, thus ensuring that foreigners do not have greater rights of protection than Australian businesses.³⁸

In order to shore up the tenants that emerged during the heyday of neo-liberalism, neo-liberals principally seek to couch their arguments in terms of the rule of law, human rights law, the vision of a global administrative law to maintain

³⁴ ICSID Case No. ARB/99/3, Final Award (Nov. 27, 2000), 5 ICSID Reports 483 (2000).

³⁵ See also *Yaung Chi Oo Ltd. v. Myanmar*, 8 ICSID Reports 463 (2003), another case in which an Asian treaty with restriction of protection to approved investment was considered.

³⁶ Thus, in the treaty with Japan, Philippines left out the investor-state arbitration provision. Philippines suffered adversely from *GPS v. Philippines* (ICSID Case No. ARB/02/06 (2006)) and *Fraport v. Philippines* (ICSID Case ARB/03/25). Local newspapers estimated the cost of the latter arbitration to be over \$45 million. It is still ongoing. There were two phases, an ICSID phase as well as an ICC phase.

³⁷ Developed states seldom conclude such treaties. In the US-Australia treaty, investor-state dispute settlement is not included. See, <http://www.dfat.gov.au/publications/trade/trading-our-way-to-more-jobs-and-prosperity.html>.

³⁸ *Id.*

global standards of governance and customary international law. With the failed attempt at the construction of a multilateral code on foreign investment with global applicability, the argument is now made through reinterpretation that neo-liberal tenets have now become universally applicable or that, in the alternative, avenues should be explored to make them universally applicable. The strategy that these techniques employ not only seeks to give legitimacy to the neo-liberal norms, it also seeks to make them applicable globally. An iniquitous regime of absolute protection of foreign investment becomes laundered through venerated doctrines like the rule of law so as to give them a new lease of life. Thereafter, it is foisted on the world as universally applicable norms. It is a good strategy, but unaccompanied by power which made such strategies succeed in earlier periods of foreign investment, it is bound to fail. Regimes can be created and sustained only in situations where there is a strong hegemonic leader desiring such a regime. The US, now being the largest importer of capital, does not have the power or the inclination to create and maintain such a regime. The different techniques of laundering the tenets of neo-liberalism are looked at in the following sections.

A. The Rule of Law Argument

The use of the doctrine of the rule of law is the most creative and perhaps the oldest of the justifications advanced for the absolute protection of foreign investment. As no one can quarrel with the rule of law, the disguising of the rules of investment protection in the garbs of the rule of law seeks to give it legitimacy by transference. It is a strategy that has been pursued at various stages in the history of the subject. The attempt has made a fresh appearance in recent times, demonstrating that whenever a system that promotes private power is under attack, a defence comes to be made through the use of lofty ideals. In the deepest days of colonialism, it was justified in noble terms as the duty to lead the savages of the world to a standard of civilization though in actual fact, the justification clothed the rapacious plunder of the developing world which in civilizational terms was arguably superior to the colonizers. The same civilizing mission is now used as a justification for the continued maintenance of neo-liberal norms.

The rule of law justification is an old one. The “rustics” were treated to this charade from old times when the Europeans, relatively new to the idea of civilization, sought to impose the “standard of civilization” on the rest of the world. The introduction of the idea of the rule of law into investment law was identified, in the initial phase, with the World Bank. It was reflected in the writings of the first two Secretaries-General of the ICSID.³⁹

³⁹ IBRAHIM SHIHATA, TOWARDS A GREATER DEPOLITICIZATION OF INVESTMENT DISPUTES: THE ROLES OF ICSID AND MIGA (Martinus Nijhoff 1993) (hereinafter SHIHATA).

The notion of the rule of law has a somewhat special status; initially for the common lawyer and later, for the rest of the world, due to the work of the International Commission of Jurists⁴⁰. Dicey, the foremost constitutional lawyer of his times, had popularized the phrase *the rule of law as a bulwark of liberty against the power of the state*, and prescribed it a meaning which had been generally accepted within the common law world. The Diceyan concept of the rule of law meant the equality of all before the law and the subjection of the State to the courts so that exercise of power could be reviewed. The Diceyan concept has animated the work of the International Commission of Jurists which, in struggling to establish the rights of people against dictatorships around the world, has used an elaborated notion of the Diceyan rule of law.

It is this principle of the rule of law as a bulwark against State power and its abuse against citizens that is used to serve the interests of the multinational corporations (“MNC”), themselves wielders and users of power both within their home and host communities. The abuse of this power within home communities takes place within developed states, which have democratic institutions and mechanisms capable of correcting such abuse. Such abuse within developing countries, however, cannot easily be rectified as it takes place either with the collaboration of local elites or in states that fear driving away desirable foreign investment by taking action against deleterious foreign investors. It also may well be the case that adequate institutional machinery does not exist to deal with abuses of MNCs even in the more sophisticated developing countries.⁴¹ The extent of human rights violations, pillage and murder that MNCs are responsible for is made evident by a long list of cases that have been brought in the US under the Alien Torts Act.⁴² The discussion of the foreign investment arbitration awards and the

⁴⁰ ICJ Declaration and Plan of Action on Upholding the Rule of Law and the Role of Judges and Lawyers in Times of Crisis, Adopted at the World Congress of the International Commission of Jurists in Geneva in December 2008, available at: http://www.icj.org/dwn/img_prd/GenevaDeclaration-ENG.pdf.

⁴¹ The sad incident of the escape of gas at the Union Carbide factory at Bhopal remains the classic example. The thousands of people affected by it remain largely uncompensated either through Indian law or through American law. See, <http://www.ndtv.com/article/india/bhopal-gas-tragedy-victims-still-await-justice-70213>. See also, Shruti Rajagopalan, *The Polluter Does Not Pay Model for Environmental Protection in India*, available at: http://www.emle.org/_data/Shruti_Rajagopalan_-_The_Polluter_Does_Not_Pay_Model_for_Environmental_Protection_in_India.pdf.

⁴² “In recent years, foreign citizens are increasingly targeting US companies in lawsuits which claim that the company acted in concert with foreign governments, or rogue elements within a foreign country, to commit torture, rape, murder, genocide or a host of other human rights violations. Several Fortune 500 companies have been placed in the crosshairs of these lawsuits, and a broad array of industries, including the chemical, pharmaceutical, financial services, energy and agriculture sectors, have been affected.”

concentration on this lucrative area of the law seeking to protect the assets of MNCs fails to mention the extent of abuse that is revealed by the expanding list of cases under the Alien Torts Act. Textbooks devote attention to foreign investment arbitration and the law under the subject without considering the impact of the case law involving the commission of international wrongs, under laws like the Alien Torts Act⁴³ or the work of the United Nations in considering the making of law to control human rights abuses by multinational corporations.⁴⁴

The rule of law argument in the context of the international law on investment does not even recognize the principle of equality, one of the basic tenets of the rule of law in that it privileges the foreign investor over local entrepreneurs and the interests of the local citizenry. It does not permit to the home state as much access to foreign arbitration as the foreign investor has so that it could institute arbitrations against abusive conduct of multinational corporations.

The system does not recognize equality between local entrepreneurs and foreign investors.⁴⁵ The protection of the foreign investor is held to a higher standard as constructed by the treatment standards and compensation mechanism provided for within a treaty. Quite apart from this, the fact that international investment law is designed to protect investment stability may work against the interests of the public of the host state when it comes to taking measures relating to the protection of the environment or human rights. International investment law may prevent regulatory measures being taken by the state as treaty provisions may prohibit such measures without full compensation. In any event, the ability to

Latham & Watkins LLP, *The Steady Rise of Alien Tort Claims Act Lawsuits and the Effect on US Companies*, September 7, 2010, available at: <http://www.lw.com/Resources.aspx?page=FirmPublicationDetail&publication=3703>.

⁴³ A spate of books has appeared on international investment law and arbitration, however none of them consider the human rights abuses of multinational corporations or their relevance to such arbitration in any great detail. Most are intent upon considering the construction of rules on investment protection by treaties or by arbitration awards giving the impression that the role of international law is devoted entirely to this end. *See generally*, leading textbooks on international investment, including CHRISTOPH SCHREUER & RUDOLPH DOLZER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* (Oxford Univ. Press 2008); STEPHAN W. SCHILL, *THE MULTILATERALIZATION OF INTERNATIONAL INVESTMENT LAW* (Cambridge Univ. Press 2009) available at: http://www.cambridge.org/gb/knowledge/isbn/item2428042/?site_locale=en_GB.

⁴⁴ A United Nations Rapporteur has been in existence to study the human rights violations of multinational corporations and device methods of dealing with them. The present Rapporteur, Professor John Ruggie had issued several reports, available online at: <http://www.business-humanrights.org/SpecialRepPortal/Home>.

⁴⁵ *See further*, DAVID SCHNEIDERMAN, *CONSTITUTIONALIZING ECONOMIC GLOBALIZATION* (Cambridge Univ. Press 2008).

so intervene may have to be tested out before a foreign arbitral tribunal. Thus the norms of international investment law as presently developed, and to the extent that they privilege foreign investors, violate the traditional understanding of the rule of law as inclusive of equality before the law.

It is in the light of these developments that the idea that the protection of the property of MNCs is somehow linked to the rule of law sounds hollow and unacceptable. Not only is it a perversion of the concept of the rule of law but it subverts an idea that was intended to protect the powerless mass of humanity against tyrants and dictator sand channels it to aid entities that traditionally have kept alive such rulers in their own search for profits, often at the cost of human suffering.

It is interesting to trace the manner of this development and its present mutation. An early statement of the rule of law argument appears in the writings of Aaron Broches, the first Secretary General of ICSID, who is credited with the origins of the ICSID Convention.⁴⁶ It was continued in the writings of Ibrahim Shihata, the second Secretary General, which showed the commitment of the World Bank to creating the linkage between the rule of law and foreign investment protection.⁴⁷ The World Bank has consistently acted on the basis of the classical belief that sound institutional protection of property and contract are the fundamentals upon which economic development could be built. However, realizing that it was too difficult to link the rule of law with foreign investment protection, the World Bank soon changed a vowel and spoke in terms of the “role of law” in foreign investment in presenting its programme of law reform, particularly in commercial law, as the basis for economic development. This modesty was not retained in the age when neo-liberalism saw its absolute triumph. The early formulations merely made the link by indicating that the state, which maintained the rule of law would attract more foreign investment because of the stability it provided. This was a truism. Of course, with the spectacular success of China, a country that can hardly be associated with the rule of law in any traditional sense, the myth that a state needed a strong rule of law for economic progress has become dented. A distinction began to be drawn between rule of law ‘light’ and rule of law ‘strong’.⁴⁸

The rule of law took a new turn when it was directly incorporated into the agenda of foreign investment with the stated view that the idea of the rule of law

⁴⁶ As cited in Margrete Stevens, *The ICSID Convention and the Origins of Investment Treaty Arbitration*, in ALBERT VAN DEN BERG, 50 YEARS OF THE NEW YORK CONVENTION (Kluwer 2008).

⁴⁷ SHIHATA, *supra*, note 39.

⁴⁸ RANDAL PEERENBOHM, CHINA'S LONG MARCH TOWARD THE RULE OF LAW (Cambridge Univ. Press 2003).

itself contained the protection of foreign investment as one of its aims.⁴⁹ This notion came in different guises. One was that the rule of law required the protection of the right to property. This view took the Lockean thesis that the protection of the right to property was the most important function of organized society and supported the protection of the assets of the foreign investor as an important function of both domestic and international law. Put in this way, it was easy to incorporate the right to property within the rule of law. Another method was to argue that the rule of law contained basic standards of governance and that since it was important for them to be recognized globally, the function of international law was to ensure that these standards, which importantly contained rules as to the treatment of the foreign investor, should be maintained. These arguments are reminiscent of the standard of civilization that existed during colonial times. The argument then was that the burden rested on the “civilized” states of Europe to ensure that those in other parts of the world, particularly Asia and Africa, should be led to the same standard of civilization that the Europeans enjoyed. As has been well documented, this seemingly altruistic justification cloaked centuries of plunder of the peoples of African and Asia. The question that must now be asked is whether the new altruism purveyed through the rule of law and standards of governance seeks to be a cloak for another bout of multinational plunder of the less powerful parts of the world.

B. Global Administrative Law

All the new arguments coalesce in the attempt to argue that foreign investment arbitration is a facet of global administrative law and that foreign investment arbitration seeks to be a part of global governance.⁵⁰ It is a sophisticated argument that sees in the explosion of investment treaties as well as in the number of arbitral awards interpreting their provisions, a genesis of a global multilateral system of foreign investment protection.

The argument states that the current regime institutes what is in effect the review of the measures taken by a state against the foreign investor, much in the mould of an administrative tribunal in domestic law. The difference is that the venue is shifted to an external location in order to facilitate neutrality. Rules that have been developed for such review are similar to domestic administrative law. Heavy reliance is placed on the existence of the fair and equitable standard on which arbitrators have read into the rule that, where legitimate expectations of the

⁴⁹ Susan Franck, *Foreign Direct Investment, Investment Treaty Arbitration, and the Rule of Law*, 19 PAC. MCGEORGE GLOBAL BUS. & DEV. L.J. 337 (2007).

⁵⁰ Benedict Kingsbury & Stephan W. Schill, *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law*, NYU School of Law, Public Law Research Paper No. 09-46 (September 2, 2009), available at: <http://ssrn.com/abstract=1466980>.

foreign investor are violated by the state, liability for such violations should arise. The linkage between domestic administrative law and the development of the fair and equitable standard to include the protection of legitimate expectations enables the drawing of the conclusion that investment arbitration is a species of global administrative law.

The development of the link between the fair and equitable standard and legitimate expectations in itself is interesting. The genesis of the idea may be found in a speech that Professor Orrego-Vicuna gave at the annual meeting of the American Society of International Law in 2004.⁵¹ In it, he drew the connection between some English cases in which the courts used the concept of legitimate expectations and provided relief on the basis of the violation of these expectations. English courts, however, have seldom held that there is a substantive principle of administrative law that states that damages must result when a state or an administrative agency goes back on a commitment made to the citizen. Instead, the remedy provided is only that there must be due process remedies available to a citizen whose expectations are interfered with.⁵² The case in English law where legitimate expectations were held to create a substantive principle has since been distinguished by subsequent cases. In *R v. North and East Devon Health Authority, ex parte Coughlan*,⁵³ it was held that a health authority must honour a commitment given to a paraplegic who was promised that she would not be shifted from a care home close to her parent's home.

Later cases have regarded *Coughlan* to be a singular instance and have not followed the decision. The courts have explained the refusal to follow *Coughlan* in the following terms:

*“Here lies the importance of that fact that in the Coughlan case that few individuals were affected by the promise in question. The case’s facts may be discrete and limited having no implications for an innumerate class of persons. There may be no wide-ranging issues of general policy or none with multi-layered effects, upon whose merits the court is asked to embark.”*⁵⁴

⁵¹ Francisco Orrego-Vicuna, *Foreign Investment Law: How Customary is Custom?*, 99 AM. SOC'Y INT'L L. PROC. 97 (2005) (“Fair and equitable treatment is not really different from the legitimate expectations doctrine as developed, for example by the English court and also recently by the World Bank Administrative Tribunal”).

⁵² See further, PAUL CRAIG, *ADMINISTRATIVE LAW* 639-656 (5th ed., 2005). Professor Craig's writings pressed the idea of substantive relief.

⁵³ [2001] Q.B. 213 (hereinafter *Coughlan*).

⁵⁴ *Begum v. The Returning Officer of the London Borough of Tower Hamlets*, [2006] E.W.C.A. civ 733 (¶ 68, citing with approval earlier cases, distinguishing *Coughlan*).

Investment cases are also quite different from the *Coughlan* type situation. Because of the public interest implications of the decisions the state has to make in them, the tribunals that decide such cases will have to take decisions that implicate concerns that transcend the immediate interests of the foreign investor and his operations within the state. The investment arbitrations that have used the notion of legitimate expectations have made decisions that implicate public interests. They have applied a notion, purportedly derived from national legal systems, but which provides remedies that are based on the violation of substantive standards. National systems do not go that far simply because of the fact that administration will become impossible if administrative policies relating to taxation, environmental regulation, labour issues and a host of other matters have to be changed in order to meet new and unexpected circumstances which arise. It cannot be expected that a state should be constrained by solicitude to prior commitments to the foreign investor when such circumstances arise.

The European Court of Justice also generally avoids imposing substantive obligations on the basis of legitimate expectations. It instead seeks to balance overriding public interests with the expectations of individuals.⁵⁵ In contrast, the breadth of the rule that has been stated by investment arbitral tribunals is so staggering that states could not have expected that the provision on fair and equitable standard could be used in such an expansive manner. They could not have expected an interpretation linking this standard with the notion of legitimate expectations. The suspicion also arises that the investment tribunals have been loaded with arbitrators inclined to entrench the notion of legitimate expectations in international investment law. The repeated appointment of such persons to investment tribunals causes concerns and leads to the inference that arbitrators partial to the acceptance of neo-liberal tenets find appointments so that new emergent mutations maybe confirmed and neo-liberalism continues to thrive.

There are other problems that arise when principles that apply within domestic law are elevated to the global level where exact parallels do not exist. It is evident that global administrative law seeks to achieve something more than what is known to common lawyers. Common lawyers view domestic administrative law as involving the protection of the rights of the common man against the might of the state so that, a part of it is devoted to ensuring that interferences with the facilities that the state provides are not withdrawn from any particular individual without observing the principles of natural justice and another part requires that there should be reasonableness in the exercise of delegated discretionary powers by administrative officials. In the case of foreign investment protection, if administrative law principles can in fact be employed, the results that are envisaged are the protection of large MNCs (in themselves significant bases of economic

⁵⁵ PAUL CRAIG, *EUROPEAN UNION ADMINISTRATIVE LAW* (Oxford Univ. Press 2006).

power) from a developing state that is seeking, as a result of changes that necessitate regulatory intervention, to regulate its economy for the benefit of its people. The interests that stand in opposition are the interests of the MNCs and the interests of the people of the State for whose benefit the State seeks to act. It is not an issue that domestic administrative law is devised to decide. It is difficult to justify the basis on which such a conflict of interests can be decided by an arbitral tribunal that cannot take into consideration the local issues that are relevant. It is obvious that local courts are more competent to deal with such issues.

It is interesting that developed states such as Canada and the US, put an end to the possibility of the fair and equitable standard being developed through the notion of legitimate expectations as a basis for review of their administrative measures. This was done when the three North American Free Trade Agreement (“NAFTA”) partners, US, Canada and Mexico sought an interpretive statement from the NAFTA Commission which confirmed the belief of these states that, the fair and equitable statement meant no more than the international minimum standard in customary international law. In their model treaties, these countries describe the fair and equitable standard as indistinct from the international minimum standard of customary international law. That practice has been followed by other states as well. Some states leave out the fair and equitable standard from their newer treaties.⁵⁶ Thus, states have evinced a desire to put an end to the arbitral adventurism that has led to the possibility of arguments relating to global administrative law.

C. Customary International Law

It is often argued that the accumulation of some 2700 investment treaties constitutes customary international law.⁵⁷ Despite the number of times that this argument has been repeated in the hope that repetitions of the mantra can lead to the salvation of the belief,⁵⁸ there is little substance in stating that the existence of a large number of bilateral treaties gives rise to customary international law. It is not the number of the treaties but rather the uniformity of the substance that is

⁵⁶ NEWCOMBE & PARADELL, *supra* note 16, at 261, *citing* L. TUDOR, *THE FAIR AND EQUITABLE TREATMENT STANDARD IN THE INTERNATIONAL LAW OF FOREIGN INVESTMENT* (Oxford Univ. Press 2008): “Finally, in some IIAs, there is no provision for fair and equitable treatment. For example, the India-Singapore Comprehensive Economic Cooperation Agreement (2005) has no fair and equitable treatment clause. A study on fair and equitable treatment clauses found that of 365 BITs surveyed, nineteen did not provide for fair and equitable treatment”.

⁵⁷ ANDREAS F. LOWENFIELD, *INTERNATIONAL ECONOMIC LAW* 584 (2d ed., Oxford Univ. Press 2008).

⁵⁸ *See, for example*, Stephen Schwebel, *The Influence of Bilateral Investment Treaties on Customary International Law*, 98 AM. SOC'Y INT'L L. PROC. 27(2004).

relevant. It may be that almost all treaties accept the Hull formula that “prompt, adequate and effective” compensation must be paid upon expropriation. Does this mean that the Hull formula has become customary international law and displaced the competing “appropriate” standard of compensation? The answer cannot be a positive one because the treaties do not protect all types of investments for any rule to be stated as to the standard of compensation.

Many treaties protect only investments approved by the host states leaving non-approved investments, outside treaty protection. Others protect investments made in accordance with the laws and regulations of the host state, again, leaving investments made outside the laws and regulations without protections.⁵⁹ This indicates that the treaties largely protect only investments that qualify for protection and the investments so qualified cannot be uniform as the laws and regulations of states differ. It therefore cannot be stated that investment treaties give rise to a uniform rule that in the event of compensation there must be payment of prompt adequate and effective compensation. The same logic applies to the statement of treaty standards. The various nuances in existing treaties make the extraction of a uniform rule difficult. The view that these treaties contribute to the formation of customary international law is only possible if one makes a superficial survey that concentrates on the similarities apparent in the outer shell of these treaties. It is not possible to say that there is sufficient uniformity even in the treaties of a single state as the treaties reflect the different negotiating powers of the parties, the different attitudes to such treaties that prevailed at the time of negotiations and the different philosophical and political views that parties themselves had at the time of negotiating their own treaties. The practice of a single state would vary depending on the stage at which the treaty was negotiated. Thus, the older Chinese treaties do not permit arbitration of disputes except in the case of the quantum of compensation. The post-2008 treaties do not contain this limitation. The change is attributed to the fact that China is now an exporter of capital⁶⁰ and is keen to protect its capital outflows.

D. The Constant Jurisprudence

The second idea is one of the multilateralisation of foreign investment law, not only as a result of the presence of bilateral and investment treaties containing similar standards, but also because of the growing similarity in interpretations of

⁵⁹ This limitation can be found in the treaties made by the Southeast Asian states such as Singapore and Malaysia. *See* SORNARAJAH, *supra* note 16, at 194.

⁶⁰ In the year 2009, China (including Hong Kong) accounted for 120.5 billion \$ in terms of outward FDI. The 2010 estimates are 144.1 billion \$. UNCTAD, Global Investment Trends Monitor, Issue No. 6, (Apr. 27, 2011), *available at*: http://www.unctad.org/en/docs/webdiaicia20114_en.pdf.

these standards by arbitral tribunals.⁶¹ This thesis too is not supportable as there is a continuing schism among arbitral awards, which have interpreted the same or similar provisions of treaties in a multitude of ways. As long as these schisms remain – and the signs are that the divisions between arbitrators are endemic – the possibility of uniform interpretations of the provisions of the treaties is remote. Having dealt with these various canards which lay the grounds for the mutations of neo-liberalism, it is possible now to deal with an idea that seeks to encapsulate the notions contained in neo-liberalism that, strict foreign investment laws lead to better standards of global governance which will bring about economic development through foreign investment-an old idea in new garbs.

IV. REACTIONS OF STATES TO ARBITRAL EXPANSIONISM

Neither arbitrators nor arbitral awards can create international law that goes against the practice of states. Arbitral awards are, at best, subsidiary sources of international law. Notwithstanding claims with respect to a jurisprudential constant, the schisms that have developed within arbitral awards belie the possibility of the extraction of any definite rules from the expansionist awards of recent times. States, however, have reacted to the possibility of such expansionism inherent in the adoption of neo-liberal stances.

First, there is complete withdrawal from the treaty system itself. Though this stance has not been concretely taken by any state, it is being considered by several countries. The recent situation in Europe where the European Commission has frozen the making of any new investment treaties by individual member states and taken the view that there must be a common policy followed by the European Union on issues of foreign investment signals the end of treaties that had been negotiated by the different European states.⁶² Some of them, particularly those, which had suffered adverse consequences of investment arbitration,⁶³ had earlier announced reconsideration of their policies relating to the usefulness of investment treaties. In this context, the text of the common European treaty is a

⁶¹ See Stephan W. Schill, *The Multilateralization of International Investment Law - Emergence of a Multilateral System of Investment Protection on Bilateral Grounds*, 2(1) TRADE L. & DEV. 59.

⁶² Article 207 of the Treaty of Lisbon mentions foreign direct investment as one of the many constituents of the EU's common commercial policy. Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community, CIG 14/07 (Jan. 1, 2009), available at: <http://www.consilium.europa.eu/uedocs/cmsUpload/cg00014.en07.pdf>.

⁶³ The Czech Republic has faced several arbitrations. One situation, concerning the investments of Lauder, resulted in two diametrically opposite awards on the same facts. It also illustrated the multiplicity of claims that could arise from the same issues. *CME v. The Czech Republic*, UNCITRAL Award (Sept. 3, 2003); *Lauder v. the Czech Republic*, UNCITRAL Award (March 14, 2003).

much awaited event.⁶⁴ A glaring example of withdrawal from the treaty system is that of Brazil, which saw spectacular development without any bilateral investment treaties.

Other states have reconsidered their positions on investment arbitration. Australia announced that its future treaties will not include investor-state arbitration.⁶⁵ The reasons given in its report are that such arbitration places the foreign investor in a position of superiority over the local investor. The report also queries the legitimacy and utility of treaty based investment arbitration in the context of the schisms, which have developed within it, in recent times. For different reasons, Bolivia and Ecuador have withdrawn from ICSID arbitration. Venezuela has withdrawn from submitting petroleum disputes to ICSID arbitration. These withdrawals may spark off a trend, at least within Latin America, signaling a return to the Calvo doctrine. Argentina, almost certainly, will return to the Calvo doctrine, once it finishes the round of arbitrations it is currently saddled with.

The trend towards what are described as “balanced treaties”, however, is more spectacular. This has been the major reaction by states not only to the expansionist views taken by the arbitrators in interpreting investment treaties but also to campaigns by non-governmental organizations (“NGO”) and other groups to demonstrate that investment treaties prevent host states from regulating foreign investment in the public interests. Alongside concerns for the environment and human rights were concerns that states would not be able to deal with economic crises and other situations of emergency that could arise without fearing a spate of arbitrations. The Argentine experience had indicated this. In response to these developments, states began to draft what have come to be known as balanced treaties. It is best to describe them first before drawing conclusions about this new phenomenon.

“Balanced” treaties accommodate the home state’s interests in conserving regulatory space by introducing provisions that avoid liability for treaty violation by identifying circumstances in which a state may regulate foreign investment. First, these treaties prevent expansionist interpretations by arbitrators by ensuring that the clauses in the treaties that have been subjected to such interpretations are either removed or restrictively defined. Thus, the fair and equitable standard is left out of some recent treaties or in the practice of some states. In the alternative, it is

⁶⁴ For the recent text of a communiqué announcing the consideration of a European treaty, *see* <http://ita.law.uvic.ca/documents/ECTradeandInvestmentCommunication.pdf>.

⁶⁵ Report by the Australian Government Productivity Commission on Bilateral and Regional Trade Agreements, *available at*: <http://www.pc.gov.au/projects/study/trade-agreements>.

defined by stating that it is no different from the international minimum standard in customary international law. Expansionary trends in the interpretation of the provision on expropriation,⁶⁶ have been stopped through the inclusion of the provision that regulatory expropriations do not give rise to a duty to compensate. This limitation knocks the wind out of the provision on expropriation. The limitation is to be found in some important model treaties, including those of the US (2004)⁶⁷ and Canada (2004)⁶⁸.

Secondly, the list of exceptions or preclusion of liability continues to grow. The most important of them is the oft-used national security exception, usually drafted in subjective terms. A state merely has to invoke the exception and provide that its measures are taken to protect national security and the arbitral tribunal would lose jurisdiction over the matter. Some argue that the arbitral tribunal must be convinced that there should be objective circumstances for the subjective invocation of the preclusion, but that is mere theory, for it is unlikely that the tribunal would question the determination of the state if there is prima facie evidence of a national security situation. The US and Canadian model treaties provide for subjective determinations of national security.

The list of such preclusionary factors will become longer as claims to other circumstances necessitating regulation are added. Following formulations in the

⁶⁶ These trends were greatly assisted by the presence of anything “tantamount to a taking” amounting to expropriation under the treaty provision. In *Myers v. Canada*, a ministerial statement contemplating the ban of a chemical was alleged to be an expropriation as its effect was to depreciate the value of the shares of the only company manufacturing the chemical. Canada settled the dispute by paying compensation. On similar facts in *Methanex v. USA*, the United States successfully pleaded that since the purpose of the ban was the protection of the public from the use of the poisonous chemical, the expropriation was regulatory and hence was not compensable. *S.D. Myers, Inc. v. Canada*, Partial NAFTA Award under the UNCITRAL Arbitration Rules, 40 I.L.M. 1408 (Nov. 12, 2000) available at: [http://italaw.com/documents/PartialAward_Myers_000](http://italaw.com/documents/PartialAward_Myers_000;); *Methanex Corporation v. United States of America*, Final Award, Ad Hoc – UNCITRAL Arbitration Rules (Aug. 3, 2005) available at: <http://italaw.com/documents/MethanexFinalAward.pdf>.

⁶⁷ Clause 4(b), Annex B (Expropriation) of the U.S. 2004 Model BIT: “Treaty Between the Government of the United States of America and the Government Of [Country] Concerning The Encouragement and Reciprocal Protection of Investment”.. Available at: <http://www.state.gov/documents/organization/117601.pdf>.

⁶⁸ Article 10 of Canada’s 2004 Model BIT: “Agreement Between Canada and _____ For The Promotion And Protection Of Investments”. Available at: <http://www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/2004-FIPA-model-en.pdf>.

General Agreement on Tariffs and Trade⁶⁹, investment treaties now often preclude measures taken to protect health, morals and welfare of the public, from creating liability for the violation of existing treaty obligations. Likewise, the trend is towards ensuring that measures protecting labour standards, the environment and human rights are not considered to create liability in the event of inconsistency with respect to any treaty obligation. Since the range of what is included in some of these areas is potentially wide, the extent of the preclusion that is created is such as to undermine their principal purpose of protection of foreign investment.

In addition, there is now a move to ensure that the treaties do not hinder the aim of sustainable development. Again, the range of matters that could be brought within the concept of sustainable development is broad. An insistence that investment treaties should not violate the aims of sustainable development will ensure that the balance in the investment treaty is very much tilted in favour of the public interests of the host state. Investment protection becomes otiose as a result, its objective whittled down by the broad preclusionary circumstances that have come to be recognized in more recent treaties.

Thus recent practice of states, moreover the developed states, indicates that they are moving away from the neo-liberal conception that investment flows are promoted by secure investment treaties which emphasize the protection of foreign investment.

V. CONCLUSIONS

The lessons to be derived from this episode for international lawyers of the developing world are clear. International law in this area, as in many areas, has undergone, and continues to undergo, cyclical change. In the first period of the formation of international investment law, the contest between the international minimum standard formulated by the US and the Calvo doctrine resulted in both a stalemate and balance as neither set of norms was able to dominate. The balance was somewhat tilted during the period after decolonization with the numerical strength of the Third World used to push through normative packages containing the New International Economic Order. During this phase too, the balance continued to be retained although the norms of developing states gathered considerable support. In the third phase of neo-liberalism, there was a movement away from the norms previously articulated by developing states. Though not complete, the period saw an ascendancy of the norms of neo-liberalism through a proliferation of investment treaties. Arbitral tribunals took the neo-liberal tenets in

⁶⁹ Article XX, General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A.

the treaties further than was intended by states establishing investment protection. Schisms appeared within the arbitral community as a result, and states have reacted by introducing defences into investment treaties. With a succession of economic crises, neo-liberalism, which accelerated the trend towards absolute investment protection, was dented. The global economic crisis in 2008 considerably eroded the reliance states placed on neo-liberal theories. States assumed a greater regulatory role, which meant that they could not adhere to the expansive standards of protection of foreign investment embraced in the past. Developed countries were at the forefront of these changes and NGOs clamoured for the restriction of a system that ignored environmental and human rights issues. The locus of power in matters relating to foreign investment shifted to newly industrializing countries like China and India. In the context of these changes, it became necessary for developed states to change their stances on investment protection. They began moving towards a position that gave rise to the view that what was desired was a balance between protection of foreign investment and the regulatory concerns of states. The pursuit of such a balance could prove to be a chimera. It will not satisfy foreign investors, and states will want to decide for themselves what the regulatory concerns that justify their action are.

It is in this period of change that developing country international lawyers should assess their own future roles in this area. It is clear that China and India will have a greater role to play but equally, it may well be that in their rush to prosperity and great power status, they may act as all powerful states had done in the past. China's newer treaties indicate its desire to protect its outgoing investments through newer types of treaties that enlarge the scope of dispute resolution well beyond what the older treaties permitted. While the older treaties confined arbitration by foreign tribunals to disputes involving compensation for expropriation, the newer treaties do not contain such a restriction. This announces China's interest in joining the capitalist nations that rely upon investment foreign arbitration. India's practice is more recent but it too will make more treaties. The indications are that China and India will join the developed states and participate in their model of investment protection. If this pattern develops, China and India would effectively abandon their earlier positions as champions of developing countries and follow the pattern set by developed states. These countries' search for energy sources may make them do exactly what the European powers did in the extraction sectors. They may thus seek absolute protection for their investments, although it is to be hoped that such a scenario does not eventuate and that the two states remain steadfast in their commitment to their earlier policies championing the Third World interest in development.

The developing countries left behind must take a firm stand in opposition to the systems of absolute protection that has been built up. They must ensure that their ability to control their natural resources is not surrendered through the

making of inflexible treaties that confer absolute protection upon foreign investment. The problem will in all likelihood not lie in the treaties that contain transparent interests and are subject to the scrutiny of many interested parties (local as well as foreign), such as NGOs. Developing countries should not get “picked off” individually but must remain united in presenting desirable norms such as the permanent sovereignty over natural resources, the ability to change arrangements when fluctuations in surrounding circumstances of a foreign investment occur, or the ability to change taxation regimes so that the full benefits of the foreign investment as it unfolds may be captured for the benefit of their citizens.