International investment agreements continue to increase in number…

International investment agreements (IIAs) have proliferated at the bilateral, regional and interregional levels over the past decade. By the end of 2005, the total number of IIAs exceeded 5,200. In addition, given the limited duration of IIAs and the evolution of international law on investment, several countries are renegotiating existing treaties.

… with some important normative developments

Several main trends can be discerned within these important normative developments:

- First, some BIT models have deviated from the traditional open-ended asset based definition of "investment", attempting to find ways to strike a balance between maintaining a comprehensive investment definition and excluding assets that are not intended by the parties to be covered investments.
- Second, revisions to the wording of various substantive treaty obligations are emerging that aim to elaborate upon the language and clarify the meaning of provisions dealing
  - with absolute standards of protection, in particular the meaning of the "fair and equitable treatment" standard and the concept of indirect expropriation.
- Third, a broader set of issues is addressed, including not only specific economic aspects, such as investment in financial services, but also issues where more room for host country regulation is sought, for example as regards the protection of health, safety, the environment and the promotion of internationally recognized labour rights.
- Fourth, the rise in investor–State disputes has resulted in a corresponding increase in interpretations of certain treaty provisions by arbitral tribunals. These interpretations are not always consistent with each other.
- Fifth, in light of the above, significant innovations regarding investor–State dispute settlement procedures are being made, in particular as far as greater and substantial transparency in arbitral proceedings (e.g. open hearings, publication of related legal documents) is concerned.

A new generation of IIAs is emerging…

International investment rules are increasingly being adopted as part of bilateral, regional, interregional and plurilateral agreements which address and seek to facilitate trade and investment transactions. These agreements cover a range of trade liberalization and promotion provisions, and also contain commitments to liberalize, protect and/or promote investment.

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1 The IIAs universe is composed of bilateral treaties for the promotion and protection of investment (or bilateral investment treaties), treaties for the avoidance of double taxation (or double taxation treaties), other bilateral and regional trade and investment agreements as well as various multilateral agreements that contain a commitment to liberalize, protect and/or promote investment.
flows between the parties. They also often address investment-related issues such as intellectual property rights, competition, services and the movement of labour. The proliferation of IIA agreements in recent years is one of the key developments in international economic relations which have arisen in response to the increasing global competition facing national economies as they seek resources and markets.

... with significant variations in their content

A number of patterns have emerged with regard to the investment provisions in "new generation" IIAs, albeit with many significant variations:

- Agreements geared at investment liberalization typically follow two main approaches: One is exemplified by NAFTA and provides for actual liberalization subject to a list of country exceptions (negative list approach); the other (exemplified by several European Union agreements with third countries) is to provide for the progressive abolition of restrictions on the entry, establishment and operation of investment.
- Agreements that provide for investment protection and liberalization (concluded by a small group of countries that includes, inter alia, Australia, Chile, Japan, Singapore, Mexico and the United States) follow the NAFTA model, but are more comprehensive (i.e. they cover more sectors), detailed (i.e. they provide greater sophistication) and, for the most part, more rigorous than prior NAFTA-style investment agreements.
- Other recent agreements have a narrower coverage of investment issues and only establishing a framework for cooperation on the promotion of investments (e.g. the free trade agreements signed between the countries of the European Free Trade Association and Central European countries).

As a result of these developments, foreign investors and countries are confronted with an ever more complex universe of investment rules...

As a result of these developments, foreign investors and countries have to operate within an increasingly complicated framework of multi-layered and multi-faceted investment rules, which may contain overlapping or even inconsistent provisions. New agreements are emerging rapidly, featuring a structure and approach to investment issues not found in earlier agreements. Even similar types of agreements may exhibit important differences.

... and need to cope with different kinds of interactions between IIA provisions

In general, IIA provisions may interact in any of at least five different ways:

- First, they may interact in such a way as to create and define a particular right or duty, an "explication" interaction. For example, the expropriation provision found in many IIAs requires payment of compensation for the expropriation of investment, but the nature of the assets protected by this provision typically can be identified only with reference to the definition of the term "investment". The greatest challenge to consistency presented by this interaction may arise from the agreement’s complexity. The larger the number of provisions involved in the interaction, the greater the likelihood that negotiators will not be able to anticipate all the consequences of the interaction.
• Second, separate IIA provisions may create or enforce the same right or duty, a “reinforcement” interaction. This occurs, for example, in services-related investment provisions in which parties reaffirm their commitments under the General Agreement on Trade in Services (GATS). Furthermore, the most-favoured nation clause (MFN clause) can have a reinforcement effect. Depending on how the MFN clause is drafted, the host country may be obliged under the IIA to honour, with respect to covered investments, commitments made with respect to foreign investment in any other agreements.

• Third, IIA provisions may create different rights or obligations applicable to the same subject matter, a “cumulation” interaction. One situation where the potential for inconsistency is clear in such an interaction may be found in agreements that have a chapter on investment and a separate chapter on trade in services. Investment chapters sometimes have provisions which follow a negative list approach, while services chapters sometimes have provisions on market access which adopt a positive list approach. Another example relates to agreements that have a chapter on trade in services generally and additional chapters on trade in certain service sectors, such as financial services. In addition, “cumulation” interaction may occur with respect to dispute resolution provisions. For instance, some IIAs include an investment chapter with an investor–State resolution mechanism that is cumulative to the more general dispute resolution mechanism in the agreement. The issue may arise as to whether disputes concerning other chapters of the agreement may be brought under the investor–State dispute resolution mechanism.

• Fourth, one provision may limit, diminish or extinguish the rights or duties created by another provision, a “contradiction” interaction. For instance, while a BIT may grant a right of establishment to foreign investors, a regional agreement to which a party to the bilateral agreement belongs may exclude such a right. Similarly, different treaties may contain different provisions and/or language concerning performance requirements and other substantive issues dealing with the treatment of foreign investment once admitted.

• Finally, one provision may increase the impact of a right or obligation created by another provision, an “amplification” interaction. For example, a host country that concludes an IIA with a chapter on trade in services may commit itself to granting market access to service providers in a particular sector of the economy. Once a service provider has established a commercial presence in the host country in accordance with the market access commitment, the commercial presence may also be considered an investment within the meaning of the investment chapter and, therefore, entitled to all of the protections afforded to investment generally.

… and interactions between IIA provisions and State contracts

There may also be interactions between the provisions of an IIA and the provisions of a contract between the host country and the foreign investor (i.e. a State contract), such as an investment authorization. In some cases, the interaction is a “reinforcement” interaction. This occurs, for example, where the IIA has a so-called "umbrella clause", which requires the host country to observe obligations into which it has entered with respect to an investment. Under this clause, a violation of the State contract also violates the IIA.
Provisions of IIAs may sometimes have “contradiction” interactions with provisions of State contracts. For example, IIA prohibitions on performance requirements may limit the host country’s ability to include certain requirements in a State contract. Similarly, IIA provisions on non-discrimination might limit the ability of the host country to guarantee preferential treatment to a particular investor in a State contract.

*These different kinds of interactions present new challenges for policymakers…*

The various interactions among an expansive patchwork of IIAs complicate the task for policymakers of gauging the full legal and policy implications of any such agreement and may increase the risk of investment disputes. Moreover, as global economic integration deepens, managing the impacts of integration on the domestic economy becomes more complex and the challenges involved in concluding IIAs correspondingly greater.

*… as IIA interactions may undermine policy coherence*

One of the main issues in this context relates to maintaining the consistency of a country’s economic development policy. Policy coherence, in general, requires that the provisions of a country’s IIAs be consistent with the country’s investment policy. In particular, IIAs should not be significantly over-inclusive (i.e. they go further than the underlying policy requires), or significantly under-inclusive (i.e. they do not go as far as the underlying policy requires). Policy coherence also requires that a country’s IIAs are consistent with one another. Not only should it be possible for a party to comply with all applicable IIA provisions, but also compliance with one IIA provision should not impair the pursuit of the policy underlying another IIA provision.

*There are several approaches to address the issue of policy coherence in IIAs…*

Because of the potential of IIA provisions to undermine policy coherence, some IIAs have adopted a number of solutions intended to maintain policy coherence in the face of overlapping IIA provisions.

The “definition” solution defines the terms of a provision in such a way as to eliminate any inconsistency with corresponding provisions in other IIAs. However, this solution implies that different IIAs use almost identical definitions for any given term, e.g. the definition of "investment". Such an outcome might be difficult to achieve. The same concern, albeit to a lesser extent, exists with regard to the “scope” solution, which limits the scope of a provision so as to avoid inconsistency with another corresponding provision, e.g. the geographical and temporal application of a treaty. The “hierarchy” solution specifies which provision shall prevail in case an inconsistency is spotted. This approach is reflected in the Vienna Convention on the Law of Treaties, which provides that the latter agreement prevails among the parties to both agreements. A systemic problem could therefore arise if a party to these contradictory agreements is not a party to the Vienna Convention. The “election” solution allows a specified actor to choose which provision shall prevail in the event of an inconsistency. This solution is very rare and comes close to a dispute set resolved by agreement of the parties. It leaves open the question of what would happen if the parties do not reach an agreement.
... and in respect of future treaty making

The existence of an increasingly complex framework of multi-layered and multi-faceted investment rules also has implications on the negotiations of future international investment rules:

- First, the complexity of negotiations increases as more and more countries issues are involved. This raises the questions of how broad the agenda of any particular set of negotiations should be, as well as how ambitious parties want to be with regard to the nature of commitments.

- Second, the negotiation of IIAs includes interrelated, difficult policy issues that at least in principle touch upon a whole range of domestic concerns, comprising, increasingly, social and environmental matters. Indeed, such agreements reflect the growing internationalization of the domestic policy agenda. Failure to take related issues of national policy properly into consideration may have serious development implications for the host countries. Therefore, IIAs should reflect a certain balance between rights and responsibilities – either by including them within the same instrument or by establishing bridges with other binding and non-binding international instruments.

- Third, although IIAs by definition contain obligations that, by their very nature, limit to some extent the autonomy of participating parties, the need for a certain degree of flexibility to allow countries to pursue their development objectives in the light of their specific needs and circumstances should be addressed. The more investment agreements go beyond promotion and protection issues and in particular attempt to include commitments to liberalize, the more complicated their negotiation becomes. Where liberalization is sought, progressive liberalization of investment regulations may be more acceptable than upfront and all-embracing commitments to liberalize.

- Fourth, transparency in the conduct of investment negotiations plays a key role in securing the necessary support and legitimacy for international investment agreements. The awareness, understanding and input of all development stakeholders are important.

Developing countries are confronted with particular challenges ...

While the above issues are important to all countries at any level of development, developed, developing and transitional alike, they are particularly pertinent for developing countries that have a smaller capacity to deal with them. Developing countries are faced with several challenges in this regard:

- First, developing countries need to ascertain how best to integrate IIAs into their economic development policy. These agreements are intended to promote economic development by providing a stable, predictable and transparent environment for foreign investment. However, all international agreements circumscribe the discretion of the parties. Developing countries need to retain sufficient policy space to promote economic development, without undermining the effectiveness of the IIA.

- Second, developing countries need to establish and maintain policy coherence in the face of a large number of interacting IIAs. As an initial matter, this entails creating a coherent national development approach that integrates investment, trade, competition, technology and industrial policies. As new IIAs are negotiated, each should be
reviewed carefully to ensure that it is consistent with and, in fact, promotes the country’s economic development. Establishing and maintaining policy coherence has become more challenging for developing countries in recent years because of at least two factors. One factor is that many developing countries are now both capital-importing and capital-exporting economies. Thus, an IIA may have implications for a developing country as both a host and a home country. The other factor is the sheer number and complexity of the agreements.

- Third, as domestic capacities in developing countries increase, a more sophisticated approach aiming at technological and scientific collaboration between foreign and domestic firms is required. This includes the crucial question of how to balance national and international R&D policies. IIAs usually address numerous issues that are relevant in this respect, such as the entry and establishment of R&D-related FDI, performance requirements, incentives and the movement of key personnel. Developing countries need to examine as to what extent these provisions can actually contribute to enhancing their R&D potential, and how IIAs interact with international agreements on intellectual property rights.

- Fourth, developing countries need to ensure that they have sufficient capacity to analyse the scope of obligations into which they are entering when they conclude an IIA. They also need to improve their capacities to understand the economic and social implications of the commitments contained in IIAs.

- Fifth, developing countries need to implement the treaty commitments they have assumed. Implementation entails completing the ratification process, bringing national laws and practices into conformity with treaty commitments, informing and training local authorities that actually have to apply the IIA, managing the disputes that arise under IIAs, and re-evaluating national investment policies in the light of national development strategies and past experience.

- Finally, finding a development-oriented balance in future IIAs that adequately addresses the issue of policy coherence is a major challenge. In the pursuit of the development dimension of IIAs, more attention also needs to be paid to commitments by home countries and to the contributions that TNCs can make to advance the development impact of their investment in developing countries.

... which underlines the importance of policy research and analysis, capacity building and technical assistance

As already noted, the burden of addressing these challenges is likely to weigh disproportionately on developing countries, especially the least developed ones, because they often lack the human and financial resources needed to implement agreements. This underlines the importance of policy research and analysis, as well as capacity-building technical cooperation to help developing countries to assess better various policy options before entering into new agreements and to implement the commitments made. International organizations can play a role in this regard.