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Political Risk and International Investment Law

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Keywords

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Abstract

International investment law provides a means for states to mitigate political risks that foreign investors face inside their borders. Its status quo includes thousands of international investment agreements (IIAs) and Investor–State Dispute Settlement (ISDS), a dispute resolution mechanism in which foreign, private investors sue host states in ad hoc international tribunals in pursuit of monetary compensation for property rights violations. In this review, we survey the vast contemporary literature on this regime to evidence the ways in which scholars have challenged the purported original goals of international investment law and its distributional consequences. In light of this literature's accomplishments, we highlight opportunities for a refocusing of international relations scholars' research agenda on dynamics of continuity and change in the regime. The status quo in international investment law is fragile, and, in our view, the regime is on the brink of a major shift toward prioritizing state sovereignty well above political risk mitigation.

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INTRODUCTION

International investment law provides a means of mitigating political risk to foreign investors - the nonmarket risk that a host state's political action unexpectedly violates a foreign investor's property rights. Inevitably, the introductions to most articles on contemporary international investment law and political risk follow a similar structure. First, the introduction takes time to explain the de facto treaty regime, in which some 3,000 international investment agreements (IIAs) provide decentralized legal protections to foreign investors originating from the signatory states of each specific IIA. Most commonly these are bilateral investment treaties (BITs), although it is now routine that trade agreements address investment protection as well. Next, the introduction explains the regime's dispute resolution mechanism, its most controversial component. Investor–State Dispute Settlement (ISDS) gives foreign investors standing to sue host states in international investment arbitration, in pursuit of monetary compensation for alleged property rights violations. Of a sample of 2,575 IIAs deemed particularly consequential by legal experts, 95% grant access to ISDS (UNCTAD 2020b). ISDS arbitrations are convened ad hoc, without systematic transparency, and without the approval of investors' home states. There is no system of precedent, as the set of protections afforded in ISDS-enabling IIAs varies, and even the definition and scope of core protections such as those against expropriation are not standardized (Alschner & Skougarevskiy 2016).[1] Nor is there a concept of double jeopardy or a substantive appeals system. Should the respondent host state lose in ISDS arbitration, it is not required to reverse the action ruled unlawful; instead, it owes monetary compensation to the foreign investor, typically on the order of tens of millions of dollars, and occasionally billions (Pelc & Urpelainen 2015, Wellhausen 2016). Such is the content of the introduction to an article on this topic, necessary to bring the reader up to speed on the basics of the remarkable status quo under examination.

The fundamental political tension motivating international law around foreign direct investment (FDI) is that while sovereign states hold the right to allow foreign capital to cross their borders, they also have the right to change their mind. In order for states to exercise the first right, IIAs and ISDS commitments have become de rigueur tools for sovereign states in assuring foreign investors that the second right is immaterial. The legally binding commitments in IIAs overwhelmingly prioritize political risk mitigation. For example, the US International Trade Administration's website answers the FAQ "Who benefits from these treaties?" as "any US company or national investing or planning to invest in that country can benefit from that Treaty."[2] In stark contrast, IIAs place few to no legal obligations on foreign investors to comply with or defer to host state development policy goals. Nor do host states have the reciprocal right to sue foreign investors under ISDS. Rather, signatory states' interests in economic development are relegated to preambles.[3] It is perhaps unsurprising that this imbalance between foreign investor rights and obligations is at the core of backlash against the status quo in international investment law. In recent years, more and more states in the Global South have come to reevaluate and even reject their IIA commitments. Even traditional capital-sending states in the Global North are joining in a variety of multilateral reform efforts (Roberts & St. John 2022).

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[1]Typical categories of actions covered in IIAs include direct expropriation, indirect expropriation, violations of fair and equitable treatment (FET), full protection and security, national treatment, and most-favored nation treatment (MFN) (Johns et al. 2020).

[2]2012 US Model Bilateral Investment Treaty, available at **https://ustr.gov/sites/default/files/BIT%20text%20for%20ACIEP%20Meeting.pdf**.

[3]The 2016 Morocco-Nigeria BIT moves closer to mutual obligations, but even its incremental adjustments are outliers. We thank Lauge Poulsen for discussion.

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It is not obvious why such a status quo emerged, why it has persisted, and how amenable it might be to fundamental reform. The vast scholarship on international investment law and political risk testifies to the myriad reasons for and consequences of this status quo. International political economists working in this area have leveraged their comparative advantage in analyzing distributional effects across "winners" and "losers" of international investment law. In fact, strange bedfellows among winners and losers call into question two stories of the regime's original goals: one, that it exists to promote FDI; two, that its purpose is to take the politics out of foreign investor-host state conflicts. Moreover, a growing body of scholarship challenges the presumption that the winners and losers of international investment law neatly cleave between the Global North and the Global South. Studies of what are now more than 1,000 publicly documented ISDS arbitrations reveal Global South states as sometime winners and Global North states as sometime losers.

Taking all these points into account, we see opportunities for scholars to use the observable implications of existing findings to speak to the longevity of the regime's status quo and what will come next. Litigation rather than FDI is booming, and more states in the Global North are experiencing the frustration of IIA- and ISDS-enabled constraints on sovereignty. We see evidence of a coming major shift in the accepted goals of the regime from protecting foreign investors against political risk to state sovereignty in determining the scope of legal obligations under international investment law. The actions of international organizations, individual states, and civil society actors engaged with reform efforts are generating a wealth of data that can be used by international relations scholars to effectively preregister hypotheses that advance explanations for the dynamics of change indicated by the literature.

In what follows, we first connect the regime's status quo to the body of literature that investigates patterns in international investment law across time.[4] We then review literature that has challenged beliefs about the regime's purported origins, as well as its consequences for the freedom of action of signatory states versus the interests and power of foreign investors as nonstate actors. Thanks to the success of scholarship produced so far, we support new research priorities focusing on the consequences of the shifting fault lines between winners and losers under the status quo.

THE STATUS QUO IN INTERNATIONAL INVESTMENT LAW

As Salacuse (2021, p. 182) puts it, "Granting a private party the right to bring an action against a sovereign state in an international tribunal regarding an investment dispute is a revolutionary innovation that now seems largely taken for granted. Yet its uniqueness and power should not be overlooked." Recognizing this uniqueness, we begin this review by describing the status quo of international investment law in light of literature exploring its patterns. In doing so, we draw on the extensive data collected by the United Nations Conference on Trade and Development (UNCTAD), which is the UN's permanent intergovernmental body tasked with supporting developing states in their access to the global economy.[5] We also connect these data to other sources that extend and sometimes challenge its records in theoretically relevant ways.

At the time of writing, UNCTAD counts 3,760 IIAs in the form of treaties, including BITs, multilateral investment treaties (for example, the Energy Charter Treaty), and trade treaties with investment clauses (for instance, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership). Of these treaties, 2,613 (70%) are in force and 427 (11%) were once in force but have

[4]This review prioritizes recent scholarship (2010–2021) that approaches issues from a political science perspective. A more extensive and interdisciplinary bibliography is available on the authors' websites.
[5]UNCTAD Investment Policy Hub: **https://investmentpolicy.unctad.org/**.

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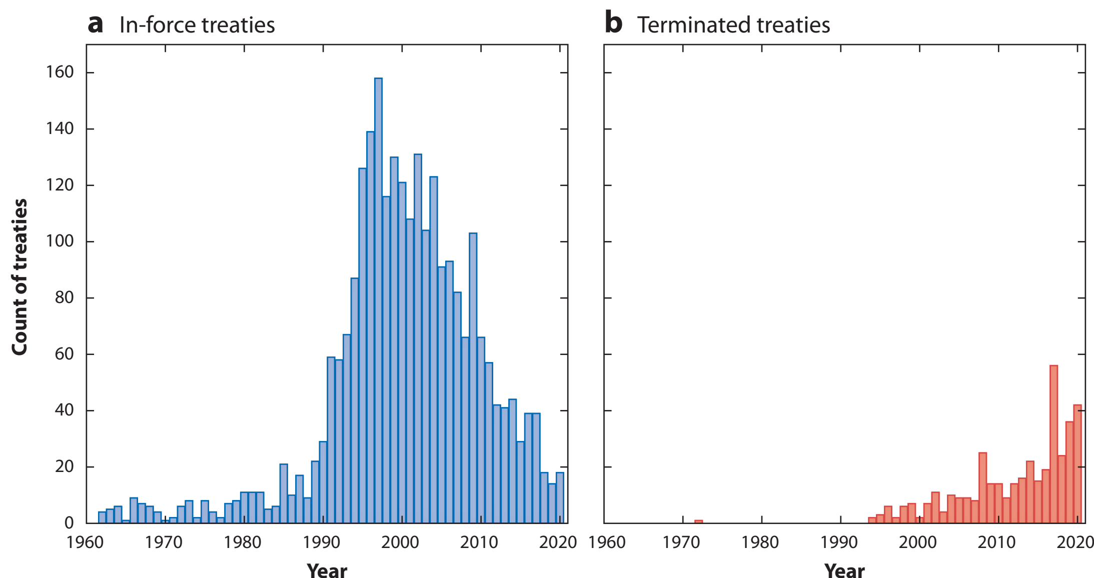

Figure 1

Count of (*a*) in-force and (*b*) terminated international investment agreements (IIAs) by year. The entry into force of new IIAs has been declining since the boom in the 1990s, while the number of terminated IIAs has been increasing. This figure does not include the termination of 277 intra–European Union IIAs in 2020 [see section titled Global North States as Winners But Also (Sometime) Losers]. Data are from the UNCTAD (United Nations Conference on Trade and Development) Investment Policy Hub.

since been terminated. Terminated treaties are typically renegotiated, although they can also result from the planned expiration of the treaty or, in some cases, unilateral withdrawal (Peinhardt & Wellhausen 2016). **Figure 1** shows that the number of new IIAs entering into force each year has been declining since the 1990s' boom, while annual terminations have been increasing. In 2017 alone, there were 56 terminations. This trend reveals that the regime's status quo is fragile, and that reform is gaining steam (Roberts & St John 2022). Still, fragility should not be overstated; already by 2013, some 1,300 IIAs had reached the end of their initial term and could be legally renegotiated or terminated by either party (UNCTAD 2013).

Although early IIAs from the 1960s and 1970s tended not to contain an ISDS clause (St John 2018, Hepburn et al. 2020, Poulsen 2020), researchers have documented ISDS access in 95% of a sample of 2,575 current IIAs deemed particularly consequential.[6] Foreign investors also gain access to ISDS via instruments other than state-to-state treaties. Access to ISDS and equivalent third-party, ad hoc investor–state arbitration is standard in concession agreements and other contracts in which the host state is the counterpart (Nottage & Thanitcul 2017).[7] Indeed, the first investor–state arbitration, brought by the Suez Canal Company against Egypt in 1864, was based on a contract between the parties (Yackee 2016). Berge & St John (2021) document ISDS provisions embedded in domestic investment laws in 74 states.

[6]These data are available thanks to a collaborative effort by UNCTAD and over 45 universities to map the content of UNCTAD's IIA database (Alschner & Skougarevskiy 2016, UNCTAD 2020b).
[7]See arbitration clauses documented via the important-yet-daunting effort to build a repository of petroleum and mining contracts (ResourceContracts.org).

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One consequence of this spaghetti bowl of ISDS-enabling instruments is that any count of ISDS arbitrations in the world is necessarily an estimate. Transparency requirements vary considerably across ISDS clauses within IIAs and the institutions that facilitate arbitrations (Hafner-Burton et al. 2016). Since its charter in 1965, the World Bank Group's International Center for the Settlement of Investment Disputes (ICSID) has become the focal point of ISDS arbitration (St John 2018). However, it is not a court: ICSID provides arbitration rules and services, such as meeting space, administrative support, and lists of vetted arbitrators. ICSID requires ISDS arbitrations that utilize its resources to be made public, but the extent of public information beyond basic identifiers for the counterparties and the ISDS-enabling instrument varies considerably. Through December 31, 2020, ICSID registered 803 cases (ICSID 2021).[8] The UN Commission on International Trade Law (UNCITRAL) is the second common source of ISDS arbitration rules and services. Given that it is not part of the World Bank and imposes fewer transparency requirements, scholars have expected weaker reputation effects for host state respondents sued under UNCITRAL's purview (Allee & Peinhardt 2011). Also through December 31, 2020, UNCTAD counts 1,104 ISDS arbitrations, including those involving ICSID resources but excluding those in which the enabling instrument is not a treaty.[9] Investment Arbitration Reporter (IA Reporter), a private service, counts 1,127 treaty-based ISDS arbitrations under the same definition used by UNCTAD. Further, thanks to investigative reporting, IA Reporter has uncovered 430 non-treaty-based ISDS arbitrations, filed under contractual clauses (80%), domestic laws (8%), or some combination (12%). While ISDS has become the public face of international investment law, its nonpublic components are a key source of backlash against it (Milner 2014). Nonetheless, UNCTAD's database has become the standard source in the scholarly literature and in the public eye, so we focus on its data.[10]

Figure 2 breaks up the UNCTAD on ISDS arbitration initiations (filings) by investor home and host state development levels. First, consider trends across all four quadrants. **Figure 2** reflects Yackee's (2010) finding that ISDS was for decades largely unknown to corporate lawyers. The use of ISDS arbitration began in earnest in the late 1990s. In fact, even those case counts do not reflect demand: Given as-yet limited ISDS capacity at law firms, practitioners could be selective as they culled through investors' pitches.[11]

Next, consider trends in each quadrant. Cases brought by investors from developed home states against developing host states have increased over time, adding up to 56% of cases (Pelc 2017, Bonnitcha & Williams 2020). Further, foreign investors from the Global South are increasingly using ISDS arbitration against other developing states (16.2% of cases). It is a fact that developing states have historically borne and continue to bear much of the burden of litigation (Sornarajah 2012). Still, increasing numbers of ISDS arbitrations against developed host states are spreading the burden of litigation. Litigation by investors from developed home states against other developed host states has gained traction, now accounting for 24.5% of cases. Last, while numbers are small, there are now consistently more than zero cases initiated by investors from developing home states in the Global South against developed host states. When traditional capital-sending home states are sued as host states, they confront the eyebrow-raising component of the regime long experienced by the Global South: the possibility of paying monetary compensation directly

[8]This includes some cases heard under UNCITRAL rules (the most common alternative), which can also use ICSID services.
[9]Other common service providers documented in the UNCTAD data include the International Chamber of Commerce and the Arab Investment Court (Link & Haftel 2019).
[10]Researchers will benefit from comprehensive ISDS data provided by the PITAD platform (Behn et al. 2019).
[11]Author's interview with practioner, September 2018.

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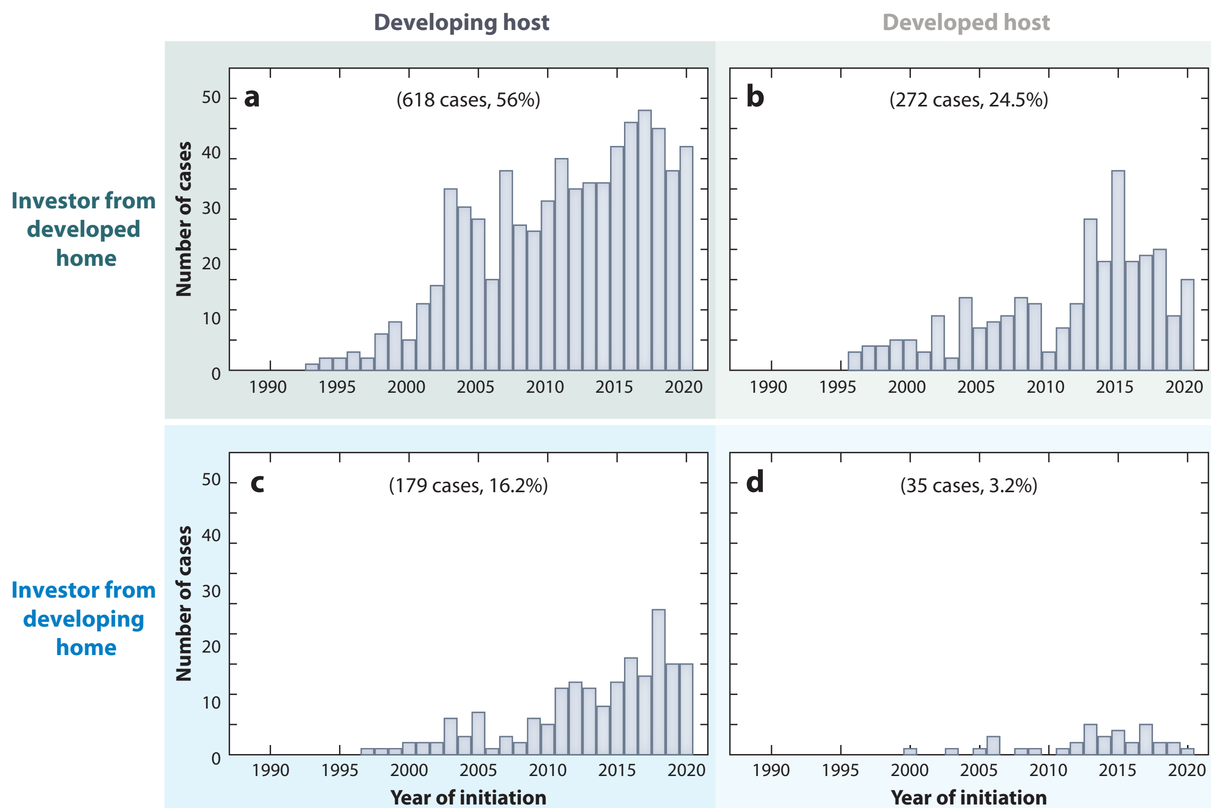

Figure 2

Treaty-based Investor–State Dispute Settlement cases per dyads of different levels of development. As expected, cases involving developed (Global North/OECD) home states and developing (Global South/non-OECD) host states dominate, but note the increase in cases in other quadrants. Data are from the UNCTAD (United Nations Conference on Trade and Development) Investment Policy Hub.

to foreign investors due to their political actions, even in a democratic setting (López-Rodríguez 2019).

Figure 3 summarizes data on the sample of 668 ISDS arbitrations with public outcome-year data.[12] UNCTAD codes four kinds of outcomes: investor wins, state wins, settlements, and other. Wins for the investor indicate a pro-investor tribunal ruling that awarded damages. State wins are pro-state rulings. As state wins are often the result of rulings on jurisdiction and not the content of claims, they cannot be interpreted as international legal approval for the disputed state action. Additionally, tribunals regularly require even winning respondent states to split litigation costs, so states often incur direct costs from litigation even as winners (Franck 2019). As for settlements, although their terms are rarely public, they are understood to require some concession from the respondent state. UNCTAD's "other" category includes discontinued cases, which are commonly understood as settlements as well. "Other" also includes cases in which the tribunal ruling does not award damages (2.4% of the sample).

[12]Nontransparency requires us to drop 82 arbitrations. We exclude the 354 cases that are pending at the end of the study period; these account for 32% of cases, consistent with the boom in recent years (**Figure 2**).

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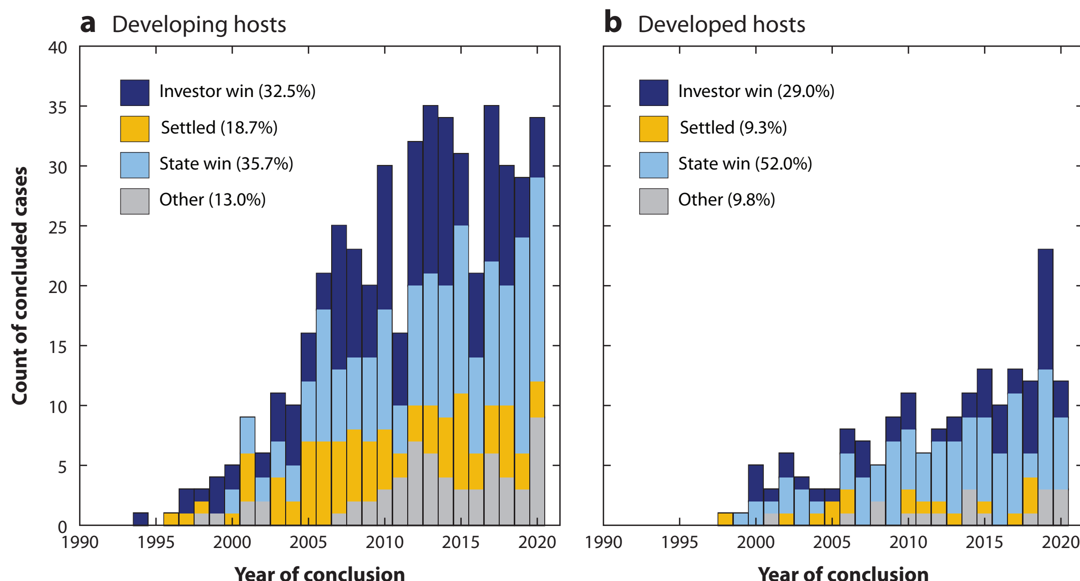

Figure 3

Known outcomes of concluded treaty-based Investor–State Dispute Settlement cases. (*a*) Developing host states have won 35.7% of cases (*light blue bars*), whereas (*b*) developed host states have won 52% (*light blue bars*).

Comparing the left and right panels of **Figure 3**, we see again that developing host states have borne the brunt of litigation. Through December 31, 2020, claimant investors have won or developing respondent states have settled 51.2% of cases. Nevertheless, the right panel documents that developed respondent states have consistently lost or settled cases since the 2000s, adding up to 38.3% of the cases they have faced. That developed respondent states are not only being sued (**Figure 2**) but also incurring direct costs from arbitration is consistent with the spread of ISDS backlash beyond developing states.

Consider also the kinds of foreign, private investors filing ISDS arbitration. Note that observed claimants are the result of a long selection process. The foreign investor must have a conflict salient enough to be raised with the host state, be unsuccessful in resolving it outside ISDS, have access to ISDS arbitration via an IIA or other means, choose to incur the costs of filing for arbitration, and participate in the process in such a manner that it is or becomes public knowledge. Additionally, the requirements to qualify as a foreign investor for ISDS purposes vary across IIAs and are often legally contested (Betz et al. 2020, Thrall 2021b). Tracing the full selection process leading to observed claimants remains an open task (Wellhausen 2019). Regardless, observed claimants are responsible for the public face of ISDS and implicated in calls for reform. **Figure 4** highlights theoretically and politically relevant categories of claimants: Fortune Global 500 firms, corporate investors, and foreign individuals. The "superstar multinationals" of the world in the Fortune Global 500 list have initiated 91 ISDS arbitrations (8.2%); examples include Chevron, Samsung, and Telefonica. The fact that the largest, most productive multinational corporations (MNCs) are a small proportion of observed claimants suggests that the realized costs of ISDS proceedings may not meaningfully correlate with a host state's ability to attract and retain growth-enhancing FDI made possible by those MNCs (Franck 2011). Still, Fortune Global 500 firms have signaled that they value access to ISDS; for example, an ExxonMobil spokesperson celebrated the Trump

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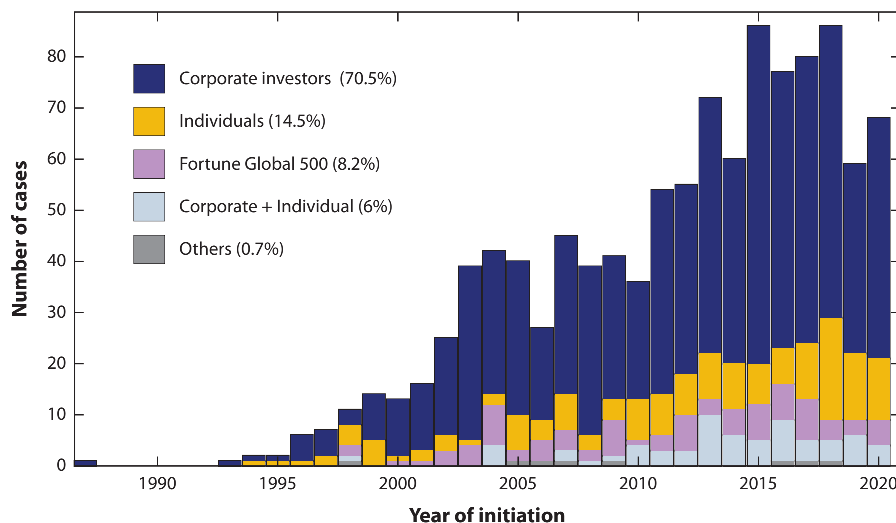

Figure 4

Breakdown of (known) types of claimant investors. Corporate investors that do not belong to the Fortune Global 500 list dominate claims (70.5%, *dark blue bars*). The share of arbitrations initiated by or involving individual named investors (20.5%, *yellow* plus *light blue bars*) has increased over time.

administration's decision to revise but not abandon the North American Free Trade Agreement's ISDS provisions in the renegotiated United States–Mexico–Canada Agreement (Carter 2021).

70.5% of cases have been initiated by either the headquarters or foreign subsidiaries of corporate investors that are not among the 500 largest global firms in the world. Our coding of "corporate investor" is, however, broad in its scope. The category includes large, productive corporations that are usually associated with the benefits that host states hope to attain with FDI. One example is Westmoreland Mining LLC, an American mining firm with about 3,000 employees and over $1 billion in annual sales, which filed against Canada in 2018 and again in 2019. The category also includes smaller firms such as Dan Cake S.A., a Portuguese manufacturer of baking goods with about 500 employees and $60 million in annual sales that sued Hungary in 2012. In fact, this category includes many very small firms on which public information is scarce, and which are unlikely to be meaningful sources of development-enhancing FDI. Additionally, the thousands of IIAs combine with the intricacies of modern corporate ownership to provide investors with overlapping opportunities to access ISDS or even forum shop between ISDS clauses.[13] Thus, even corporate investors understood as large may have little to no development-enhancing FDI in the host state.

Also important for the public face of ISDS arbitration is the category of individual claimants. In 14.5% of known cases, the claimant investor is a foreign individual rather than a corporation. Individual investors are also named claimants in another 6% of cases filed by a combination of individual(s) and corporate investor(s). Individual claimants include people who play at best a minor role in the host state economy but, because of the status quo in international investment law, have standing to sue the host state (Baumgartner 2016). Among individual claimants is, for instance, Omar Bin Sulaiman, the Saudi businessman with substantial investments in the Middle

[13] Philip Morris filed for ISDS arbitration against Uruguay via its Swiss entity and against Australia via its Hong Kong entity (Moehlecke 2020).

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East. Another example is Sergei Pugachev, once a member of Vladimir Putin's inner circle, who has filed multiple claims of unlawful expropriation of his investments in Russia under the status of a French foreign investor, thanks to his status as a dual national of Russia and France. Adding to the controversy over who files for ISDS is the rise of third-party funding of ISDS arbitrations, in which investors fund the claimant in return for a portion of any resulting award (Kalyanpur & Newman 2021, Williams & Dafe 2020). Unsurprisingly, this industry aims to keep its funding targets as confidential as possible. In summary, the variety of foreign (or "foreign") investor claimants documented in **Figure 4** suggests that many ISDS users are difficult to reconcile with the logic that IIAs and ISDS clauses are a means of mitigating political risk that would otherwise deter development-enhancing FDI.

CHALLENGING THE ORIGIN STORIES OF THE GOALS OF INTERNATIONAL INVESTMENT AGREEMENT AND INVESTOR–STATE DISPUTE SETTLEMENTS

Are the thousands of IIAs and the growing wave of ISDS arbitrations consistent with the objectives of international investment law? If not, how did this status quo come about, and what has it achieved? Two common origin stories posit two goals of the contemporary international investment legal regime. First and most prominent is the explanation that states sign IIAs and commit to ISDS as credible commitment devices to mitigate political risk and thereby promote FDI. Second is the notion that the legalization of investor–state conflicts is an effective means of depoliticization and obviates the need for diplomatic involvement. Scholars have found little to no evidence that the status quo accomplishes either of these goals. The mismatch between the two common origin stories we cover next and their observed outcomes has motivated scholars to theorize around other reasons why host states commit to the regime.

International Investment Law as a Vehicle to Attract Foreign Direct Investment

For good reason, the most ink has been spilled in interrogating what has been the crucial selling point of IIAs and ISDS for capital-seeking states: that making these hands-tying, credible treaty commitments will increase inflows of FDI (Kerner 2009, Poulsen 2015). Left out of the previous sentence is the linked expectation that the FDI attracted by IIAs will promote economic development consistent with the host state's priorities; the broader literature on the political economy of FDI (reviewed by Pandya 2016) shows that this outcome is far from obvious. Regardless, scholars searching for a causal link from IIAs to FDI are already stuck on the first point. Some studies extract evidence of conditional effects, for example, that IIAs only increase fixed capital FDI (Kerner & Lawrence 2014, Colen et al. 2016), that the effects are dependent on IIA ratification (Haftel 2010), or that effects exist only among foreign investors with certain kinds of nonmarket risk management strategies (Albino-Pimentel et al. 2018). Yet, in a meta-analysis of 2,017 estimates drawn from 74 studies, Brada et al. (2021, p. 58) find that the effect of IIAs on FDI "is so small as to be considered as negligible or zero."

Many scholars have for good reason also explored whether states' ex ante commitments to ISDS in particular have a convincing link to FDI, given its design. ISDS has the potential to facilitate efficient breach, whereby a host state takes adverse action, the tribunal assigns the appropriate value of compensation due to the foreign investor, and the foreign investor is made whole despite the realization of political risk (Pelc & Urpelainen 2015). Around 31% of ISDS investor-claimants retain investment in the respondent host state or return after exiting it, especially in the context of lower-stakes disputes (Wellhausen 2019). Whether one interprets this

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percentage as high or low, it suggests that ISDS has the capacity to resolve time-inconsistency problems between host states and foreign investors.

Be that as it may, scholars have theorized that states face meaningful indirect costs from market actors other than the claimant as a consequence of being sued, resulting in poorer investment climate measures and significant declines in FDI (Allee & Peinhardt 2010).[14] A robust body of scholarship points to heterogeneity in these market-generated indirect costs: by investor home state (Wellhausen 2015b, Aisbett et al. 2018), industry (Shim et al. 2021), the claimant's level of integration into the host state economy (Johns & Wellhausen 2016, Betz & Pond 2019, Cutler & Lark 2022), market dominance (Kim et al. 2019), and the content of legal claims (Wellhausen 2019, Kerner & Pelc 2022). That investor heterogeneity conditions the effects of political risk and its realization on subsequent investment choices parallels scholarship outside the specific context of ISDS (Frieden 1994, Johns & Wellhausen 2021, Thrall 2021a). Regardless, from the point of view of a state that intended its credible commitments to IIAs and ISDS to increase inward FDI, the outcomes have been disappointing: Not only have hands-tying devices failed to generate significant increases in FDI but they also led to considerable declines in FDI "when the claims hit" (Poulsen & Aisbett 2013).

Legalization as a Substitute for Politics

The second common, albeit less discussed, origin story of contemporary international investment law speaks to both its purpose and the timing of World Bank's 1965 charter of ICSID and launch of ISDS services (St John 2018). In this narrative, the investment treaty regime was designed to depoliticize investment disputes, specifically by blocking home states from using diplomatic leverage and even force in promoting their investors' interests abroad (on occurrences of gunboat diplomacy from the 1940s to the 1980s, see Mandel 1986). ICSID's timing is linked to the wave of decolonization around the 1960s, during which newly sovereign states protested that FDI was "antithetical to development" because it would serve as "a tool for continued control by external powers" (St John 2018, p. 63). Justifying political risk mitigation institutions as a means of promoting FDI was a nonstarter. Rather, proponents of international investment law had to establish that FDI would mitigate the imperialism associated with it. This required designing institutions such that "home country diplomatic interventions—or the leveraging of state power and apparatus to advance the interests of private investors—would no longer be necessary" (Gertz et al. 2018, pp. 239–40).

However, a robust body of scholarship establishes that IIAs and ISDS do not fulfill the goals of this origin story either. In terms of institutional design, ISDS procedures provide many entry points for politics. First, consider disconnects between the professional incentives of arbitrators and apolitical goals (Tucker 2018, Poulsen 2022). In constituting ad hoc tribunals, the counterparties nominate the three arbitrators: one chosen by each side, and one agreed upon by both sides. One of ICSID's services is to maintain lists of vetted arbitrators, from which arbitrators (in whatever venue) are typically chosen. There is growing recognition of biases generated by underrepresentation of arbitrators originating from the Global South on these lists (Puig & Strezhnev 2017). The experiences of arbitrators on these lists also make them attractive as sources of legal representation (Tucker 2018). Double hatting occurs when the same individual is chosen as an arbitrator in one case and legal counsel in another, generating imbalances in power and

[14]But see Wellhausen (2015a) for evidence that benefits in sovereign debt markets correlate with ISDS filings triggered by revenue-raising state actions.

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conflicts of interest (Langford et al. 2017). Moreover, individuals on these lists command high prices, which add to the direct costs to respondent host states of securing experienced legal professionals (Tucker 2018, Franck 2019).

Standard operating procedures in the law generate further entry points for politics. ISDS is designed such that the claimant need only prove a main legal violation to secure full compensation. This means that judicial economy (arbitrators' incentives to consider only the minimum number of claims necessary to render a judgment) and moving bars (changes in trends in rulings on the interpretation and scope of legal protections) are not exogenous to politics (Johns et al. 2020). This design has important yet difficult-to-measure distributional effects, as it is impossible to use observed rulings to either substantiate or deny the extent of normatively concerning "frivolous litigation" (Pelc 2017). Moreover, even though dozens of countries have created model IIA templates to establish efficiency in treaty negotiations, varying investor protections weaken the possibility of even informal precedence on those claims that receive rulings. Variation in treaty content highlights the importance of state bargaining power in negotiating the protections afforded by any given treaty (Alschner 2014, Manger & Peinhardt 2017, Berge 2020), and states continue to leverage political power outside of international investment law. Studies focused on the US demonstrate that politics drives US choices over negotiating IIAs; it has not gone unnoticed that the US has never lost at ISDS arbitration (Chilton 2016).[15] Further, US diplomats advocate for aggrieved investors whether ISDS access is available or not (Gertz 2018, Gertz et al. 2018). Dozens of state-owned agencies provide political risk insurance to their own investors abroad, on top of signing IIAs securing them access to ISDS (Wellhausen 2015b, Arel-Bundock et al. 2020). The Multilateral Investment Guarantee Agency is the key multilateral provider of political risk insurance. Yet it, like ICSID, is part of the World Bank Group, so its portfolio is inextricably linked to the preferences of its nation-state shareholders (Malik & Stone 2018). Further, the rise of MNCs from the Global South has brought to the fore the question of the intended status of state-owned enterprises (SOEs) under IIAs and ISDS. SOEs have long been core participants in international commercial arbitration, both as claimants and respondents (Hale 2015). However, more and more SOEs are filing for ISDS arbitration as foreign investors, which incorporates home state politics into the regime (Allee & Peinhardt 2014, Polanco 2019). Further, SOEs are facing litigation as representatives of host states, accused of taking actions that qualify as treaty violations. Arguably, this reintroduces the host state concern that international investment law can be "a tool for continued control by external powers" (St John 2018, p. 63).

WhyElse Might International Investment Agreements and Investor–State Dispute Settlement Exist?

If IIAs and ISDS have not decisively increased FDI by performing a credible commitment function and/or depoliticizing investor–state disputes, why do they exist? The most influential explanations focus on diffusion mechanisms (Jandhyala et al. 2011). Diffusion motivated by the competition for capital is consistent with empirical evidence that IIAs proliferate in clusters, as states feel pressure to keep up with their competitors' efforts to mitigate political risks (Elkins et al. 2006). Another argument is that diffusion is facilitated by boundedly rational states ignoring "low-probability, high-impact risks" such as an ISDS claim, especially in the 1990s and 2000s (Poulsen 2015). In addition to diffusion mechanisms, there are numerous direct explanations for state choices. Substituting domestic law with international investment law is attractive for host states with low-credibility

[15] At the time of writing, the Office of Trade Agreements Negotiations and Compliance of the Department of Commerce has a dedicated phone line for US investors to inquire about using ISDS.

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domestic judicial institutions (Malesky & Milner 2021). It can also prove particularly useful for states in poor economic circumstances (Betz & Kerner 2016). State choices over IIAs and ISDS are also a product of domestic political institutions (Blake 2013, Haftel & Thompson 2013) as well as concerns over regime stability (Arias et al. 2018, Billing & Lugg 2019). These multiple efforts to explain the emergence of international investment law are paralleled by explanations rooted in its distributional consequences, to which we now turn.

INVESTOR–STATE DISPUTE SETTLEMENT'S WINNERS AND LOSERS

A large literature takes the political economy approach of examining distributional effects to understand persistence in IIAs and ISDS. We review this literature with special attention to the fault lines dividing winners and losers. Further, evidence of shifts in fault lines speaks to the increasing fragility of the status quo.

Global South Developing Host States as Losers

Reasons to characterize developing host states as the central losers of the status quo abound, with many already obvious in the failure of investment promotion or depoliticization origin stories. Here we organize additional scholarship that characterizes these countries as losers, focusing on the costs they have long sustained in ISDS arbitrations.

A straightforward cost of ISDS to respondent states is that of litigation itself. While host states do not have to pay compensation when they prevail in a case, significant costs related to counsel and tribunal fees still apply. Franck (2019) calculates the average litigation cost for respondent host states as nearly $5 million. Although rulings sometimes require the investor to pay some or all of the respondent state's litigation costs, the onus is on the host state to enforce this—a difficult endeavor worthy of scholarly attention (Van Harten & Loughlin 2006, Puig 2014).[16] When host states do lose, the amount of compensation owed to the claimant can be substantial. Nontransparency makes it difficult to pin down these values. Nonetheless, out of the 203 tribunal awards recorded by UNCTAD, 44% report compensation awards from $10 million to $100 million. About a dozen awards have reached $1 billion or more, all of which have been filed against developing respondent states. Bonnitcha et al. (2017, p. 199) argue that compensation has become progressively detached from the fair market value of an expropriated asset, as awards increasingly reflect potential losses stemming from regulations that are not necessarily attached to objective valuations.

Another much scrutinized costly aspect of ISDS is its ability to constrain sovereign governments in their regulatory powers (Tienhaara 2006). The infamous chilling effect is "delaying, compromising, or abandoning the formulation or implementation of bona fide regulatory measures in the interest of the public good as a result of a real or perceived threat of investor-state arbitration" (Schram et al. 2018, p. 195). This has long generated concerns. For example, the demise of the Multilateral Agreement Initiative proposed by the OECD in 1995, which was the most recent effort to develop a centralized, multilateral standard for investment protection, is partially attributed to its potential chilling impact on environmental regulation (Baughen 2001). Scholars have discussed various mechanisms and collected different kinds of evidence pertaining to the chilling effect in environmental (Van Harten & Scott 2016), public health (Sell & Williams 2020), and labor (Ye 2020) policies. Others have considered the effects of ISDS on the regulation

[16]Further research can also benefit from broader treatments of enforcement in international law (e.g., Magesan 2013, Johns & Pelc 2018).

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of market competition (Manger 2008), in response to economic crises (Bellak & Leibrecht 2021), and in sovereign debt renegotiation (Gallagher 2012). We also have evidence that the actual chilling effect may be more limited than many have worried. Moehlecke (2020) shows that arbitrations against one host state do discourage third states from enacting the disputed regulation but that such an effect is specific to the targeted policy and not long-lasting—although it is longer lasting precisely for developing states.[17]

Some have explored the proposition that restrictions on sovereign regulatory autonomy generated by ISDS might nonetheless benefit developing states by fostering good governance (Bonnitcha et al. 2017, Sattorova 2018). For instance, foreign media organizations have successfully invoked ISDS against authoritarian host states that violated principles of press freedom [such as in *Al Jazeera v. Egypt* (King 2020)], and tribunals have established that cultural heritage is a legitimate reason for host countries to take measures that could otherwise be claimed as violation of obligations to foreign investors [as in *Parkerings v. Lithuania* (Francioni 2012, p. 728)]. However, this and other evidence remains anecdotal, and a link between ISDS and good governance has not found systematic support in the literature. (Moehlecke et al. 2021 provide evidence that developing host states are systematically more likely to overturn regulations disputed by powerful incumbent foreign investors, regardless of whether those policies are the result of democratic processes. Importantly, investment treaties are signed by sovereign states, and whether the promotion of liberal or democratic principles would constitute a win depends fundamentally on the host state's political regime.

The field of international political economy has long acknowledged that FDI imposes tough trade-offs for host developing countries because of its "distributive and sovereignty costs" (Pandya 2016, p. 466). However, the dilemma concerning ISDS is not as complex. Presumed benefits remain largely unfulfilled, while the monetary and sovereignty costs keep growing. Nonetheless, and perhaps contrary to Strange's (1996) concerns about the "retreat of the state," developing countries are pushing to reshape their ways of protecting foreign investors in pursuit of preserving more space for their sovereign powers. With that notion in mind, we now turn to discuss the conditions under which developing states are deriving wins despite the adverse status quo.

Global South Developing Host States as (Sometime) Winners

It is unsurprising that capital-seeking states sued in ISDS are fighting the status quo (Simmons 2014). Notably, unilateral efforts by developing states are driving the trend in the termination of IIAs documented in **Figure 1** (Calvert 2018, Meyer & Park 2018). Ecuador, Bolivia, and Venezuela have made waves by going so far as to unilaterally withdraw from IIAs as well as ICSID; Indonesia, India, and South Africa have been trailblazers in rethinking their full set of IIA commitments (Peinhardt & Wellhausen 2016). More and more developing states are taking advantage of the scheduled expiration of treaties to renegotiate terms that better reflect their interests in preserving "state regulatory space" over the property rights of foreign investors (Haftel & Thompson 2018, Thompson et al. 2019). Notably, there is significant variation in developing countries' approaches to termination and renegotiation as a function of their treaty partners' bargaining power (Huikuri 2020). However, the success of developing states' efforts to redefine their participation in the status quo is limited by the regime's decentralization (Gordon & Pohl 2015). The density and complexity of cross-cutting bilateral and multilateral IIAs makes possible double jeopardy in which

[17]In contrast, Berge & Berger (2021) find that ISDS has a greater chilling effect on environmental regulations in more developed host states with greater bureaucratic capacity.

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host states respond to claims that were initiated under different legal instruments but pertain to the same underlying issue. Further, the same foreign investor often has legal standing in more than one home state, meaning that a given withdrawal does not obviously protect a host state from litigation by a given investor (Alschner 2014, Peinhardt & Allee 2016). Additionally, many treaties contain sunset clauses that extend their protections for even a decade after termination (Meyer & Park 2018).[18]

Regardless, these unilateral efforts by developing states have given rise to serious multilateral reform efforts, which can be considered a victory for developing host states (Schill 2017, Roberts & St John 2022). Numerous ideas are on the table, such as giving legal voice to civil society actors, switching to state-to-state arbitration, reconciling overlapping IIAs, extending ISDS to domestic firms, integrating investment and trade law, harmonizing escape clauses, and more (Puig & Shaffer 2018, Polonskaya 2020). Particularly relevant are calls for host states to have the reciprocal right to sue foreign investors, so that IIAs also address investor misconduct in host states (Marcoux 2020, Ho & Sattorova 2021). Among the efforts considered most promising are policy changes by ICSID and other ISDS service providers, as well as working groups at UNCITRAL,which received its mandate in 2017 despite US opposition (Roberts 2018).[19] UNCTAD reform efforts have already resulted in practical guides to "expedite the modernization of the existing stock of old-generation investment treaties" with a focus on sustainable development goals (UNCTAD 2020a, p. 2). However, UNCTAD's position of "gradual innovation" does not obviously suggest that its reforms would turn developing state losers to winners.

Given limitations surrounding multilateral reform efforts, it is valuable to consider outcomes in developing states that have long found alternatives to the status quo of international investment law. Brazil is one of the few developing states that has never ratified an IIA with an ISDS clause even though it signed over a dozen in the 1990s, a choice attributed to the combination of an unresolved executive and concentrated legislative opposition (Campello & Lemos 2015). Although the counterfactual is unknowable, this has not harmed Brazil's ability to attract FDI; in 2020, Brazil was the sixth largest FDI recipient in the world (UNCTAD 2021). Recently, Brazil has been negotiating agreements on cooperation and facilitation of investments (ACFIs), partially motivated by the interests of Brazilian MNCs to secure protection for their investments abroad. The principle in ACFIs is to prevent litigation through institutions such as mediation in a joint committee with an ombudsperson (Monebhurrun 2016). Crucially, ACFIs stipulate that if and when litigation occurs, it must be addressed through state-to-state arbitration. Key elements of the Brazilian model have already been incorporated in the Mercosur Protocol, a notable regional investment treaty signed in 2017.

The rise of MNCs from the Global South means that more developing states have serious interests in the principle of investment protection, not only as host states but also as home states, giving them more opportunities to benefit from the status quo. South–South IIAs are facilitating an increasing number of ISDS arbitrations (**Figure 2**; Morosini & Ratton Sanchez Badin 2018). The dual interests of new home states like Brazil and Russia (a claimant home state for 25 known ISDS arbitrations at the time of writing) suggest meaningful differences from those of smaller developing states as they look to the future of international investment law (Manger 2009, Alschner & Skougarevskiy 2016, Haftel et al. 2022). In this context, China's choices over IIAs and ISDS are

[18]Notably, Venezuela has taken actions consistent with its sunset clause–based commitments to ICSID despite its dramatic withdrawal.

[19]There are less well-developed efforts at the OECD and World Trade Organization. EU efforts are discussed in the context of Global North developed states in the next section.

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also quite salient (De Stefano 2021, Shan et al. 2020). Consistent with its Going Global Strategy from the late 1990s, which sought to promote Chinese FDI across the world, China's many IIAs share the Global North focus on protecting its nationals' investments abroad (Chaisse 2019). Chinese IIAs also are explicit in specifying protection for its SOEs as foreign investors. China's formal involvement with the regime has been relatively modest so far; only eight cases have been initiated by Chinese investors abroad and eight cases filed against China (Invest. Arbitr. Report. 2021).[20] Of course, a low number of observed ISDS arbitrations does not mean that the regime has been unimportant to China in deterring or resolving disputes outside of litigation. Moreover, China will likely be in the spotlight if and when reform efforts increase foreign investors' obligations under the regime, especially those concerning human rights and sustainable development.

Global North States as Winners But Also (Sometime) Losers

Contrary to the most dire expectations about fundamental power imbalances in IIAs and ISDS, a number of traditional capital-sending, developed states have become increasingly proreform as they experience the costs borne by host states. Efforts by civil society have raised popular awareness in developed states of the eyebrow-raising status quo, thereby aiding cooperation and coalition building in growing reform efforts (Hahm et al. 2019, Marceddu & Ortolani 2020). Indeed, scandalous lawsuits brought against developing host states have made the nonspecialized news in developed states (Provost & Kennard 2015, Hamby 2016). Further, survey experiments fielded in developed states provide evidence that ISDS erodes public support for status quo trade and investment agreements—even to the extent of sparking popular protest (Hahm et al. 2019, Spilker et al. 2020).

But adverse public opinion is not solely responsible for developed states' pushback against the status quo. As foreign investors have the unique standing to file for ISDS arbitration without home state approval, it is wrong to presume that home state priorities in foreign affairs would coincide with a given investor's decision to use treaty-based ISDS mechanisms. Although the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention) applies once an award is issued, enforcing it against a recalcitrant respondent state regularly requires a circuitous path through domestic courts and/or active efforts to chase down and seize state assets. These realities generate demands for home states to engage in commercial diplomacy on behalf of their nationals, again in ways that may not match foreign policy priorities. What is more, foreign investors' standing to sue without home state involvement generate costs for developed states as hosts, especially when claimants are not associated with growth-enhancing FDI (see **Figure 4**).

In thinking about developed home states' dilemmas in balancing their investors' interests with their own, the European Union's evolving situation is instructive. The Lisbon Treaty included FDI policy in the EU Common Commercial Policy, which inaugurated a thorny debate about the status quo of international investment law in the bloc (Shan & Zhang 2010). Specifically, it was for many years unclear whether intra-EU BITs were compatible with EU law and whether they should be terminated (Basedow 2020). In 2020, two years after the EU Court of Justice ruled that intra-EU BITs conflicted with EU law (*Slovak Republic v. Achmea B.V.* 2018), the Agreement for the Termination of Bilateral Investment Treaties between the Member-States of the European Union entered into force, which terminated 277 intra-EU BITs including their sunset clauses. However,

[20]For comparison, US investors abroad have initiated 194 arbitrations, and the United States has been the respondent in 20 cases (due especially to ISDS provisions under NAFTA).

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Austria, Finland, Ireland, and Sweden did not agree to terminate their intra-EU BITs.[21] At the time of writing, the status quo is that most EU investors do not have IIA protections in other EU states, while foreign investors from outside the European Union remain covered by their IIAs with specific member states. Additionally, the European Union has refrained from making a clear decision on the rights of individual member states to maintain BITs with non-EU states or their rights to negotiate further IIAs. The European Union's preferred resolution is via the creation of a multilateral, permanent investment court as a replacement for ISDS and decentralized IIAs, and it is taking active measures to lay the groundwork for such a court. However, the principle of a permanent court is highly contentious even among proreform states, both within the European Union and on the international stage (Roberts 2018).

The Energy Charter Treaty (ECT) also illustrates shifting fault lines between winners and losers under the status quo. The ECT, devised in the 1990s to govern international flows of investment and technology in Europe, is unique as an industry-specific treaty that contains an ISDS clause. It has come under fire for at least four reasons. First, the ECT has produced 135 ISDS filings, representing 12% of cases. For comparison, the next most common treaty has produced only 72 cases (6.5%, NAFTA). Second, consistent with ISDS in general, developing states have borne considerable costs from the ECT. Most prominent have been high-profile ISDS filings against Russia; the ECT in 2005 produced the largest award to date, $40 billion to be paid by Russia to Hulley Enterprises. Russia's exposure to ISDS under the ECT hinged on legal interpretations by (ad hoc) tribunals that Russia's provisional application of the ECT was sufficient to provide jurisdiction. Russia's basic position is that, as it signed the ECT in 1994 but never ratified it, it has not agreed to ISDS (Voon & Mitchell 2017). Understandably from its point of view, Russia is not complying with ECT rulings. Third, developed states have found themselves bearing huge costs as respondents in ECT-based ISDS. Around half of ECT cases have been filed against three states: the Czech Republic, which is traditionally a host state, and Italy and Spain, more commonly home states. During the European financial and debt crisis, these three states (like many others) followed austerity measures and were forced to make difficult decisions over fiscal policy. Each of these three governments made the decision to roll back incentives intended to attract FDI in renewable energy projects (López-Rodríguez 2019). The choice made by Spain and Italy to renege on commitments to foreign investors in times of crisis is exactly the kind of choice that has triggered waves of litigation against traditional host states (including the Czech Republic) (Haftel & Levi 2020). Italy withdrew from the ECT in 2016 in protest, although it remains constrained by the ECT's sunset clause, just as has been the case for developing states withdrawing from individual IIAs. A fourth issue has arisen since 2017, when the ECT initiated a process of modernization to better align with the Paris Agreement. Suffice it to say, designing a climate-friendly energy treaty that prioritizes foreign investors' property rights is perhaps a step too far (Cima 2021).

By late 2021, COVID-19 (coronavirus disease 2019) emergency measures have underpinned investor claims in a few (public) ISDS filings. Many observers expect a worldwide deluge of cases due to the emergency policies enacted by all states.[22] From the point of view of the host state, prioritizing foreign investor property rights over nation-state sovereignty in the context of a pandemic borders on the absurd. Yet weak (or nonexistent) escape clauses for host states in most IIAs, as well as ad hoc arbitration without a substantive appeals system, mean that host states could very

[21]Investors from these four home states have used their intra-EU BITS to file numerous ISDS arbitrations against other EU states; only Austria has been sued once under an intra-EU BIT.

[22]Already in May 2020, a group of public intellectuals in law and economic development called for a moratorium on ISDS arbitrations pertaining to measures taken to address the pandemic (CCSI 2020).

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well lose at arbitration. Developing states have long experienced the incongruity of compensating foreign actors for policy actions undertaken in the national interest, irrespective of domestic support. If and when COVID-19 measures trigger ISDS filings against developed states, they too will face the prospect of compensating foreigners for emergency policies. Despite the pandemic's universality, we expect its fallout in developed states as FDI hosts to pose the biggest challenge to the already-fragile status quo in international investment law.

CONCLUSIONS

For a proponent of the status quo in international investment law, the body of scholarship reviewed here is disappointing. Hands-tying commitments to protect foreign investors' property rights were meant to allow developing states with scarce capital and weak rule of law to mitigate political risk in the absence of otherwise credible investor protections. But IIAs do not trigger floods of desirable FDI, nor has legalization kept home state interests out of investor–host state conflicts. At the same time, ISDS has exposed developing host states to hundreds of foreign investor claims, many conflicting with state regulatory priorities, sparking domestic protest, and effectively taking funds from taxpayer pockets to compensate foreign firms.

Even as developing states continue to accrue costs, more and more developed states are also joining the ranks of losers as respondent host states sued by foreign investors. In fact, the evolution of the landscape of FDI suggests that developed states and their foreign investors might consider IIAs and ISDS as less valuable forms of political risk mitigation, undermining their interests in the regime even when they are winners (Kim & Osgood 2019, Wellhausen 2022). Contemporary FDI is a product of complex developments such as the fragmentation of production across global value chains (Kim & Rosendorff 2021), the swell of intrafirm trade/FDI, and the associated complications of transfer pricing (Malesky 2015), layered and often opaque firm ownership structures (Thrall 2021b), foreign investment from SOEs and sovereign wealth funds, and the rise of MNCs from the Global South. Taken together, these developments expand the domain of political risk and challenge long-standing assumptions about the identities and interests of foreign investors, home states, and host states. At minimum, the status quo in international investment law makes less sense as these concepts become more mutable.

In our view, mounting losses for traditional capital-sending states in the Global North would be the proximate cause of a major shift in the legal balance between mitigating political risks for foreign investors and protecting state sovereignty. In the United States, consensus around the idea that ISDS is too costly has even crossed partisan lines; both Robert Lighthizer (President Trump's Trade Representative) and President Biden share a negative view toward the institution (Trader & Stimson 2018, Stimson 2020). Now it is likely that IIAs and ISDS will be invoked in ad hoc adjudication of the legitimacy of pandemic emergency measures—from the point of view of foreign investors' property rights. All of this is happening against the backdrop of the broader backlash in developed states against economic globalization, which may even erode the long-standing consensus that FDI is something to be promoted (Walter 2021). It appears increasingly unrealistic that a sufficiently powerful coalition of winners will long protect the status quo in treaty-based international investment law. At the time of writing, active reform efforts at UNCITRAL, ICSID, UNCTAD, and the European Union, among ECT signatories, and at other international organizations exist alongside states' unilateral treaty withdrawals and bilateral treaty renegotiations. International relations scholarship already offers many rich insights on the sources of fragility in contemporary international investment law. Now, we are well positioned to apply the foundational concepts of power and sovereignty to understand dynamics of continuity and change in the regime.

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