Withdrawing from Investment Treaties but Protecting Investment

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Abstract
A backlash against Investor State Dispute Settlement (ISDS), in which multinational corporations can sue governments, has led some states to unilaterally withdraw from some of the thousands of investment treaties that facilitate ISDS. But thanks to redundancies in the dense, decentralized network of investment treaties, states can reject some treaty commitments to ISDS and maintain most (if not all) international legal protections for foreign investors. In this article, we explain the source of redundancies, document the group of states that have taken advantage of unilateral withdrawal, and demonstrate that states can recalibrate their international legal commitments without eschewing contemporary international investment law.

Backlash and its limits
States know that tying their hands by signing international treaties can have drawbacks. If states only accept the commitments that they intend to keep, then abrogation should only occasionally happen, off the equilibrium path (e.g. Koremenos, 2005; Mitchell, 1994; Rosendorff and Milner, 2001. But see Helfer, 2005.) Yet since the late 2000s, a growing number of states has abrogated international investment treaties. Some states have unilaterally withdrawn from some investment treaties to protest Investor State Dispute Settlement (ISDS) provisions. ISDS allows foreign investors to sue states in international tribunals, should investors feel a state has violated its commitments to treat them fairly. Sometimes, foreign investors win big awards. ISDS thus triggers domestic frustration about the balance between foreign investors’ rights and national sovereignty (e.g. Poulsen, 2015; Wellhausen, 2015). The fact that states are taking the radical action of abrogating ISDS-enabling treaties has led many to worry about a backlash against the evolving international investment regime (e.g. Haftel and Thompson, 2013; Waibel et al., 2010).

We document limits to this backlash. Even states that have abrogated some investment treaties have not withdrawn from all international legal commitments to investor protection. In part that choice is due to the difficulty of exiting the dense, decentralized network of 3,000-odd investment treaties. At the same time, overlapping sources of access to ISDS allow states to use unilateral withdrawal to recalibrate rather than reject substantive or procedural international legal commitments. In this article, we explain the source of states’ redundant commitments to ISDS, survey the group of states that has unilaterally withdrawn from investment treaties, and show that their withdrawals have thus far resulted in little to no real reduction in foreign investors’ access to international legal protections.

Overlap and redundancy in investment treaties
States around the world have signed some 3,000 investment treaties in hopes of enhancing foreign investment (Elkins et al., 2006; Jandhyala et al., 2011). In exchange for that uncertain benefit, states constrain their policymaking so as to prioritize the property rights of foreign investors. Investment treaties expose states to litigation brought by foreign investors over property rights issues, via ISDS. If the international tribunal enabled by ISDS finds that a state has violated its legal commitments, it can require the state to compensate the foreign investor. Commitments to ISDS in investment treaties limit a state’s sovereignty and transfer rights to foreign investors, in exchange for the hope of more investment. Unsurprisingly, domestic audiences are sometimes frustrated with this tradeoff.

Most investment treaties are bilateral investment treaties (BITs), such that only investors originating from the two signatory states gain access to the treaty’s protections. Investor protections are also present in some multilateral treaties, such as NAFTA and now the Trans-Pacific Partnership (TPP). These treaties, too, provide protection to the subset of foreign investors from signatory states. One prominent multilateral investment treaty, the Energy Charter Treaty (ECT), protects only investors in energy industries from signatory states. While foreign investors’ precise legal protections in all these treaties have similarities, they are not identical (Allee and Peinhardt, 2010, 2014; Blake, 2013). As a result, a foreign investor’s nationality is an important determinant of the scope of protection available to it (Wellhausen, 2015).
In practice, however, many foreign investors enjoy multiple, overlapping channels of access to ISDS. First, many of today’s most prominent multinational corporations can claim protection under multiple treaties. Multinationals often invest in third countries via second-country subsidiaries. If those subsidiaries are located in countries with relevant investment treaties, then multinationals can usually access those treaties, too. Second, many foreign investors write treaty-like access to ISDS directly in their contracts. Third, many investment treaties grant access to multiple arbitration venues. Most commonly, investment treaties provide access to ISDS at the World Bank’s International Center for the Settlement of Investment Disputes (ICSID). Additionally, investment treaties regularly provide access to ISDS under the rules created by the United Nations Commission on International Trade Law (UNCITRAL), and those ad hoc tribunals can be constituted virtually anywhere. While there are procedural differences between ISDS at ICSID and under UNCITRAL rules, foreign investors can (attempt to) enforce the same substantive rights in either system. In sum, any given foreign investor may have access to multiple, overlapping procedural ISDS rights, not to mention overlapping substantive protections.

From the state’s point of view, these overlapping commitments to ISDS mean that it has options to act on domestic dissatisfaction with ISDS without eschewing ISDS altogether. For example, a state can withdraw from a particular ISDS venue without limiting access to other venues. At most, a state’s withdrawal from any particular investment treaty will eliminate access to ISDS only for those foreign investors that have unique access through that treaty. By prioritizing piecemeal withdrawal from overlapping treaties, states can flexibly reconsider their body of ISDS commitments without needing to reject the institution wholesale.

In the last two decades, ISDS has faced a growing crisis of legitimacy. First, states can owe sizeable compensation to aggrieved foreign investors as a result of ISDS. Over 675 public investment arbitrations have been filed against over 120 states under ISDS through 2014. Foreign investors have won an award in 29 percent of concluded cases. Half of these awards are below US$20 million. Five proceedings have resulted in awards of US$1 billion or more—and investors have sought awards over US$1 billion at least 45 times (Wellhausen, 2016). Second, many see ISDS protections as problematic or unfair because they do not allow for reasonable state policies and regulations. Procedural commitments in ISDS may also be flawed: individual arbitrators may be biased, panel rulings can be inconsistent, and ISDS does not include an appeals process (e.g., Schultz and Dupont, 2015; Simmons, 2014; Van Harten, 2012). Third, and most importantly, states’ central motivation for signing investment treaties has been to enhance investment, accepting exposure to ISDS as a necessary tradeoff. However, a large literature has found that investment treaties at best sometimes increase certain kinds of investment (for a review, see Sauvant and Sachs, 2009). States and their publics are increasingly uncertain about what they are getting in exchange for ISDS exposure. In short, ISDS commitments may on balance generate significant liabilities while constraining government policy making (Poulsen, 2015). It is not surprising that more and more states are interested in recalibrating their commitments.

We take as given that this deep crisis of legitimacy generates incentives to withdraw from investment treaties. Still, backlash against ISDS has taken the form of recalibration rather than rejection. Even the most frustrated states continue to maintain a robust set of substantive and procedural international legal commitments to protect the property rights of foreign investors. States are not rejecting modern investment law wholesale. We survey below the states that have walked a middle path, thanks to redundancies in the decentralized network of investment treaties.

### Piecemeal withdrawal

Our brief case studies demonstrate that states have recalibrated their commitments to ISDS and international investment law without eschewing it altogether. As of 2016, seven states have withdrawn from some investment treaties, eliminating redundancies or abrogating treaties that apply only to small groups of investors (see Table 1). Sunset provisions in many of these treaties still bind states for years, and withdrawing states have so far respected these provisions and other investment treaties. Finally, we consider Argentina, a

<table>
<thead>
<tr>
<th>Country</th>
<th>Total Investment Treaties</th>
<th>Unilateral withdrawal from ICSID</th>
<th>Treaty (Partner Country)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bolivia</td>
<td>27</td>
<td>Yes</td>
<td>Yes (United States)</td>
</tr>
<tr>
<td>Venezuela</td>
<td>33</td>
<td>Yes</td>
<td>Yes (Netherlands)</td>
</tr>
<tr>
<td>Ecuador</td>
<td>26</td>
<td>Yes</td>
<td>Yes (Cuba, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, Dominican Republic, Uruguay, Finland)</td>
</tr>
<tr>
<td>South Africa</td>
<td>49</td>
<td>No</td>
<td>Yes (Belgium and Luxembourg, Spain, Germany, Switzerland, Netherlands)</td>
</tr>
<tr>
<td>Indonesia</td>
<td>70</td>
<td>No</td>
<td>Yes (China, Laos, Malaysia, Netherlands, Italy, France, Slovakia, Bulgaria, Egypt)</td>
</tr>
<tr>
<td>Italy</td>
<td>152</td>
<td>No</td>
<td>Yes, Energy Charter Treaty</td>
</tr>
<tr>
<td>Russia</td>
<td>79</td>
<td>No</td>
<td>Yes, Energy Charter Treaty</td>
</tr>
</tbody>
</table>

*Note: Data as of January, 2016. UNCTAD. UNCTAD lists some other Bolivian treaties that have been denounced but their status is difficult to confirm.*
state that for a time behaved as if it had withdrawn from ISDS altogether. Argentina’s return to compliance demonstrates that wholesale abrogation indeed carries costs that are too high to bear for a state interested in accessing international capital.

Bolivia

President Evo Morales is an outspoken opponent of investment treaties, and since 2009 the Bolivian constitution has included language threatening broad renegotiations of its investment treaties. Bolivia allowed its 1998 BIT with the US to expire in 2012 after the treaty surpassed its minimum existence of ten years, but Bolivia’s primary approach has been to renegotiate existing treaties.

In 2007 Bolivia became the first state to withdraw from the Washington Convention that underpins ICSID. This withdrawal allowed Morales to tout that he had rejected a major World Bank institution. However, Bolivia can still be sued: it has since faced at least four arbitrations facilitated by UNCITRAL rules.

Venezuela

In 2008, Venezuela withdrew unilaterally from the Netherlands–Venezuela BIT after several multinationals sued it via their Dutch corporate vehicles. The treaty became a ‘thorn in the side’ of President Hugo Chavez (Peterson, 2008). Nonetheless, the Dutch BIT will remain in force until 2023 under a sunset provision, and Venezuela has thus far continued to participate in arbitrations under it. Venezuela has also behaved as if withdrawing from one BIT carries limited costs. It has maintained its other BITs and has even signed new BITs with France, Indonesia, Belarus and Iran.3

In 2012, Chavez announced Venezuela’s withdrawal from ICSID, where it had faced 37 arbitrations. But of the 26 investment treaties in force in Venezuela, only those with Chile and Germany named ICSID as the sole arbitration venue (Ripinsky, 2012). Otherwise Chilean or German firms may still be able to access arbitration via subsidiaries in second countries that have treaties with Venezuela. Additionally, withdrawal had little to no impact on existing disputes: the 20 cases pending against Venezuela at ICSID at the time of withdrawal (ten of which were registered during 2011 alone) have proceeded as if the country were still an ICSID member.6

Ecuador

Ecuador exited ICSID, first partially with regard to oil and gas disputes and then fully as of 2010. It has denounced dozens of investment treaties and withdrawn from nine. Still, even Ecuador has been recalibrating and not foregoing its commitment to investment protection through international law.

A frustrated Ecuador asserted in 2007 that it would no longer allow oil and gas industry arbitration at ICSID (Peterson, 2009). Formally, Article 422 of Ecuador’s 2008 constitution forbids the country to enter into agreements under which Ecuador ‘would have to cede sovereign jurisdiction to international arbitral tribunals in contractual or commercial matters between the State and individuals or corporations’. Citing the constitution, President Rafael Correa terminated Ecuador’s investment treaties with Cuba, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, the Dominican Republic and Uruguay. Despite the broad constitutional language, the government used a cost-benefit logic to choose these BITs: it felt they failed to bring any noticeable benefits to the Ecuadorian economy and could only bring about costs via ISDS (Investment Treaty News, 2008). In contrast, Correa did not withdraw from the 1993 Ecuador-US BIT, despite having made public threats against it. Instead, Ecuador has used international courts to attempt to set aside awards won by US multinationals under the BIT; it has had mixed success.7 These set-aside attempts conflict with the spirit of the Washington Convention that set up ICSID, even if they can be read as consistent with the letter of the law. But it is notable that Correa’s strategy has been to operate in an international legal framework even when it comes to controversial investment disputes with the United States. Correa came close to changing his strategy of recalibrating international legal commitments when, in 2009, he denounced many of Ecuador’s remaining investment treaties.8 However, even in this moment of broad, anti-market rhetoric, Correa did not denounce the treaties with Bolivia, Peru or Spain. The National Assembly again acted on a cost-benefit logic; it rejected Correa’s request to withdraw from BITs with China, Chile, Venezuela, the Netherlands and Germany but approved withdrawal from the BIT with Finland. Correa was successful in leading Ecuador to fully withdraw from ICSID in 2010. Nonetheless, like Bolivia and Venezuela, Ecuador has since been sued repeatedly under UNCITRAL rules.9

A frustrated Correa urged the National Assembly in 2013 to withdraw from all of Ecuador’s investment treaties. A national commission was tasked with determining whether the remaining treaties violated Ecuador’s sovereignty, whether previous arbitration tribunals misinterpreted the treaties, and whether investment treaties are beneficial for the country. In late 2014, the commission recommended abrogating all remaining investment treaties. Nonetheless, as of 2016, Ecuador has not followed through. In fact, Ecuador used its treaty rights around ISDS to win a partial annulment of a large and controversial award to the oil and gas firm Occidental (Peterson, 2015b). It is notable that an anti-investment-treaty politician like Correa has found it useful to retain treaties over a year after an official, domestic commission gave him permission to withdraw wholesale.

South Africa

Post-apartheid South Africa quickly signed many investment treaties, but investors have used these to challenge Black Economic Empowerment (BEE) programs intended to address historical injustices (Poulsen, 2015). South Africa declared in 2010 that its 23 investment treaties ‘pose risks and limitations on the ability of the government to pursue its constitutional-based transformation agenda’ (Green, 2012). It unilaterally
withdrew from a BIT with Belgium and Luxembourgh as well as
BITs with Spain, Germany, Switzerland, and the Netherlands.
These partner states are economically consequential and
these withdrawals could have significant consequences for
the future of ISDS in South Africa.
Nonetheless, other indicators from South Africa lean more
toward recalibration than rejection of ISDS. South Africa has
made no indication that it will ignore sunset clauses, and it
remains a party to investment treaties with other EU mem-
bers. South Africa’s limited withdrawals may merely speed
up a process of renegotiation, as the EU itself is in the pro-
cess of consolidating its members’ many investment treaties
into one supranational commitment. South Africa now has a
new model investment treaty and, going forward, has pro-
muligated a policy of renegotiating treaties at time of
renewal (Carim, 2013). Consistent with this, the government
decided to renew the Singapore-South Africa BIT in 2015.

Indonesia
In response to contentious domestic politics around a min-
ing dispute, Indonesia somewhat ambiguously announced
in 2014 that it would either terminate or renegotiate its
investment treaties (Bland and Donnan, 2014; Ewing-Chow
and Losari, 2014). As of 2016, Indonesia has unilaterally ter-
minated nine BITs: with China, Laos, Malaysia, the Nether-
lands, Italy, France, Slovakia, Bulgaria and Egypt. It has
announced plans to withdraw from at least eleven more in
2016 to 2018.10 Argentina and Indonesia mutually agreed to rec
scind their BIT.
Indonesia has not abandoned international investment
law, however. It allowed controversial arbitrations to go for-
ward under exactly those treaties from which it is withdraw-
ing, and its recent interactions with Singapore provide
evidence that Indonesia wants to renegotiate and not only termi-
nate BITs (Lumbantobing, 2015; Today, 2015). As with
South Africa, Indonesia is signaling a commitment to update
treaties based on its new preferences.

Italy and Russia
Both Italy and Russia have rejected the Energy Charter
Treaty (ECT). Italy announced its withdrawal in 2015, after
it began to face arbitrations filed by investors in renewable
energy.11 Preexisting arbitrations continue, however, and
the EU remains a party to the ECT. Thus, Italy’s unilateral
withdrawal may have no impact. Additionally, Italy has
withdrawn from intra-EU BITs, but mutually and in concor-
dance with the European Commission’s desire to terminate
these treaties that the Commission sees as incompatible
with EU law.12
Controversial arbitrations under the ECT led to a new
record of US$50 billion in several awards against Russia.13
President Vladimir Putin, who had canceled ratification of
the ECT in 2009, announced in 2015 that Russia would not
pay. Nonetheless, Russia remains part of the ISDS system: it
has used rights available to it under international law to
attempt to get these awards set aside. In 2016, Russia won
in a domestic court in the Netherlands, which will make it
more difficult for investors to enforce the awards elsewhere.
Going forward, it is likely that Russia recalibrates around
rather than rejects international investment law, particularly
because its own multinationals use ISDS to file arbitrations
against other states. Indeed, more stakeholders in states that
have traditionally been recipients of international capital
may come to support ISDS, as those states grow their own
multinational corporations that invest abroad.

Noncompliance v. Withdrawal
Russia’s action raises the question, why withdraw when you
could not comply? Starting in the mid-2000s, Argentina sys-
tematically refused to pay multiple arbitral awards.14 Argen-
tina’s noncompliance looked like an outright rejection of
ISDS, and it triggered the World Bank to threaten to stop
loans.15 In 2013, Argentina paid its five outstanding ICSID
awards (over US$450 million) to British, American and
French firms.16 Days later, it secured a three-year, US$3 bil-
lion loan from the World Bank. The timeline suggests that
Argentina’s broad noncompliance, outside the rule of law,
had proved too costly.
If in the future another state refuses to pay awards, we
would expect it to learn from Argentina: the state would be
well served to limit its noncompliance and (try to) justify it
as mere recalibration. It is notable, however, that the several
other states surveyed here have not used absolute refusal
to pay awards to express their objections to ISDS. Through
piecemeal withdrawal, states can push back against ISDS
without needing to take the drastic step of rejecting mod-
ern international investment law altogether.

Conclusions
Frustration over ISDS has thus far led a small handful of
states to reject some of their treaty commitments to invest-
ment protection.17 Even so, states that withdraw from
decentralized, overlapping treaties can push back against
ISDS while retaining credible legal commitments.
One takeaway is that even highly frustrated states are not
attempting to totally withdraw from modern international
investment law. It is possible that the complex system of
global rules toward foreign investment is biased toward
multinational corporations. Yet it seems that even states
that perceive such bias also see too many potential gains
from international capital to justify total withdrawal. Whether
states’ desire for international capital will someday
diminish is an open question. Regardless, the system is such
that states can push back without immediately resorting to
a wholesale rejection of modern institutions.

Notes
The authors benefited from feedback from participants at the 2015
Texas Triangle Conference at Texas A&M University, as well as from
Todd Allee, Yoram Haftel, Lauge Poulsen, Zoe Williams, and our anon-
ymous reviewers.
1. Most investment treaties were signed after 1990 and offer innovative protections and real possibilities of enforcement.

2. Many BITs provide most favored nation (MFN) protection, such that investors covered by a BIT receive the strongest protections offered to other firms covered by BITs.

3. Similarly, states are more likely to abrogate military alliances when a member experiences a change that affects the alliance’s value (Leeds and Savun 2007).

4. Using a sample of 1,896 treaties in force as of 2014, Gordon and Pohl (2015) find that even if one party to the treaty immediately denounced it, 90 percent would still bind treaty partners 10 years later, 50 per cent would affect partners 15 years later, and 25 per cent would still have some effect 20 years later (20–21).

5. Venezuela may be noncompliant with an award under another BIT. In 2014, a Canadian investor both won a US$713 million award and filed separately in US courts for its enforcement. The investor nevertheless remains in Venezuela. To date, Venezuela is not publicly contemplating withdrawing from the Canada-Venezuela BIT. Gold Reserve Inc. v. Bolivarian Republic of Venezuela (ICSID ARB(AF)/09/1). There are no public complaints of nonpayment from the investors who have won two other (admittedly smaller) awards against Venezuela (ICSID ARB/96/3 and ICSID ARB/00/5).

6. Venezuela has made some moves to replace ICSID with a regional institution that nevertheless facilitates ISDS.

7. Cases include LCIA UN3467, PCA 34877, and ICSID ARB/06/11.

8. This included investment treaties with the US, UK, Netherlands, Germany, France, Canada, Switzerland, Finland, Sweden, China, Argentina, Chile, and Venezuela.

9. Like Venezuela, Ecuador has also proposed the creation of an alternative to ICSID.

10. These are: Spain, Cambodia, India, Romania, Turkey, Vietnam, Hungary, Singapore, Pakistan, Switzerland, and Kyrgyzstan. As reported by Peterson (2015c).

11. Italy claims it wants to economize by avoiding paying dues to the ECT governing body (Hepburn and Peterson, 2015).

12. There is some evidence that Croatia does not mutually recognize the termination of their BIT with Italy. The Czech Republic has also been terminating intra-EU BITs.

13. PCA AA226, AA227, and AA228.

14. Argentina has 54 investment treaties in effect. It has been sued over 50 times, more than any other state.

15. Argentina also faced bilateral punishments, particularly from the US and Spain.

16. Argentina made the payments in sovereign bonds, and claimants quickly sold them onward.

17. Some states, like India, are writing new model investment treaties and recalibrating without employing unilateral withdrawal.

References


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