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**Research Report**

## Different investment treaties, different effects

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## Columbia FDI Perspectives

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### **Different investment treaties, different effects**

by

Clint Peinhardt and Todd Allee\*

The proliferation of investment treaties is perhaps exceeded only by academic studies of those treaties. Legal scholarship has long been attentive to the evolution in international investment agreement (IIA) content -- but until recently, quantitative assessments of IIAs have tended to treat them as interchangeable: the only measure of investor protections encoded in IIAs is whether a treaty had been signed and/or entered into force. Thankfully, the United Nations Conference on Trade and Development has been at the forefront of capturing not just IIAs' proliferation but also the evolution in their content. Its work shows that treaties apply for differing durations, have conflicting procedures for termination and include varying definitions of even basic terms, such as "investors" and "investment." Other quantitative studies have begun to measure these variations, focusing initially on differences in dispute resolution.<sup>1</sup> Some IIAs demand that investors choose between domestic and international dispute resolution; some provide explicit consent of both parties to international arbitration; and some designate a particular forum for arbitration, whereas others specify multiple options. Of course, IIAs vary across many dimensions, but our initial examination of dispute resolution provisions alone demonstrates the importance of examining IIA content.

Importantly, the variations across IIAs are systematically related to characteristics of the governments negotiating them. Even powerful countries' model investment treaties are rarely enacted in full, and treaties enact language that reflects carefully balanced bargaining positions.

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<sup>1</sup> Jason Webb Yackee, "Bilateral investment treaties, credible commitment, and the rule of (international) law: Do BITs promote foreign direct investment?," *Law & Society Review*, vol. 42 (December 2008), pp. 805-32.

For example, treaties between countries with great power disparities provide stronger international arbitration provisions; treaties between relative equals tend to be less stringent.<sup>2</sup>

Most published quantitative studies find a correlation between IIAs and foreign direct investment (FDI) -- but, increasingly, this relationship appears more complex than the simple “IIAs increase FDI” story. The earliest studies found little evidence of this story, but in recent years a number of studies have found correlations between the number of IIAs a country signs and its inward FDI. Other research finds that IIAs and FDI between signatories move together as well. Both approaches have elicited criticism on methodological grounds, since previous FDI can influence which countries get IIAs.<sup>3</sup> Also, the FDI effects of IIAs depend on compliance: states that sign IIAs but appear more often (or lose) in international arbitration will not gain new FDI, and in fact may jeopardize the investment stocks they already possess.<sup>4</sup>

New research on IIAs simultaneously examines how the characteristics of their individual state parties, the relationship between those parties, and treaty content affect investment. IIAs do appear to have differing effects on FDI due to their varying levels of investor protection.<sup>5</sup> After taking into account which states sign stronger treaties, the specific language in dispute resolution clauses can impact FDI; for example, treaties that omit any reference to local dispute resolution options appear more likely to increase FDI between the signatories.

For policymakers, this implies that not all countries are likely to gain FDI as a result of IIAs. Only countries on the cusp of establishing good investment climates may benefit, for example by signing more comprehensive investment treaties than their peers. Countries already unattractive to foreign investors are unlikely to become more so as a result of a typical IIA. Likewise, those already viewed as safe investment hosts may only stand to lose ground if they sign weak treaties. Overall, the actual investment effects of investment treaties depend greatly on context. Lastly, our findings do not imply that investors pay great attention to all treaties; instead, where BITs contribute especially critical information, such as in newly independent countries, treaties that commit states more credibly to investor protections can attract FDI.<sup>6</sup>

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<sup>2</sup> See, Todd Allee and Clint Peinhardt, “Delegating differences: Bilateral investment treaties and bargaining over dispute resolution provisions,” *International Studies Quarterly*, vol. 54 (March 2010), pp. 1-26.

<sup>3</sup> See, e.g., Emma Aisbett, “Bilateral investment treaties and foreign direct investment: Correlation versus causation,” in Karl P. Sauvant and Lisa Sachs, eds., *The Effect of Treaties on Foreign Direct Investment* (New York: OUP, 2009), pp. 395-437.

<sup>4</sup> Todd Allee and Clint Peinhardt, “Contingent credibility: The impact of investment treaty violations on foreign direct investment,” *International Organization*, vol. 63 (July 2011), pp. 401-432.

<sup>5</sup> Clint Peinhardt and Todd Allee, “Devil in the details? The investment effects of dispute settlement variation in BITs,” in Karl P. Sauvant, ed., *Yearbook on International Investment Law and Policy 2010-2011* (New York: OUP, forthcoming).

<sup>6</sup> Axel Berger, Matthias Busse, Peter Nunnenkamp, and Martin Roy. 2011. “More stringent BITs, less ambiguous effects on FDI? Not a bit!” *Economics Letters*, vol. 112 (September 2011), pp. 270-72.

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