

[From The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties and Investment Flows (Oxford: Oxford University Press, 2009)]

## **BITs, DTTs, and FDI flows: An Overview\***

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In the past two decades, foreign direct investment (FDI) has been spurred by the widespread liberalization of the FDI regulatory framework, combined with advances in information and communication technologies and competition among firms. Most countries have opened themselves to foreign investment, improved the operational conditions for foreign affiliates and strengthened standards of treatment and protection. In fact, virtually all countries now actively encourage FDI, as it can bring capital, technology, skills, employment, and market access. Investment promotion strategies include the establishment of Investment Promotion Agencies (IPAs), the offering of incentives, the preparation and dissemination of investment guides, and, notably, the conclusion of international investment agreements, especially bilateral investment treaties (BITs) and double taxation treaties (DTTs). For countries, the basic purposes of concluding BITs and DTTs are, respectively, to assure investors that investments will be legally protected under international law and to mitigate the possibility of double taxation of foreign entities and, in this manner, to help increase FDI inflows.

Whether BITs and DTTs do indeed affect the flow of FDI has been studied and debated for the past decade. This volume brings together published studies, updated articles and original pieces from that period dealing with that subject matter. Its focus is on BITs and DTTs because these (and especially the former) are the principal international investment agreements (IIAs), that is, instruments that, in a significant manner, address investment issues.<sup>1</sup> While the focus of this compendium is on the impact of BITs and DTTs on FDI flows, the chapters in the first section of this volume discuss the general nature of these agreements to facilitate the understanding of the subject matter; additional materials are listed in the bibliography. The present overview looks briefly at current FDI trends and their salient features, provides a general introduction to BITs and DTTs, and summarizes the findings of the studies contained in this compendium as to the impact of these agreements on FDI flows.

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<sup>1</sup> IIAs also include a number of bilateral free trade agreements with substantial investment chapters and regional and multilateral instruments on investment; studies of the effect of these agreements on FDI flows are not covered in this volume, although the number of countries covered by them rivals that of countries covered by BITs and DTTs. For a survey of studies of the impact of the NAFTA investment chapter, see José Alvarez, "The NAFTA's Investment Chapter and Mexico," in Rudolf Dolzer, Matthias Herdegen and Bernhard Vogel, eds. *Foreign Investment: Its Significance in Relation to the Fight Against Poverty, Economic Growth and Legal Culture* (Berlin: Konrad Adenauer Stiftung Foundation, 2006), p. 253.

## A. FDI trends and characteristics

The IMF and OECD define direct “foreign investment” as cross-border investment made by a resident entity in one economy (the “direct investor” or “multinational enterprise”) with the objective of establishing a lasting interest in an enterprise resident in an economy other than that of the direct investor (the “foreign affiliate”).<sup>2</sup> “Lasting interest” implies the existence of a long-term relationship between a direct investor and a foreign affiliate, and a significant degree of influence on the management of the latter. A minimum stake of 10% of the ordinary shares of an enterprise is generally regarded as being the minimum threshold for a foreign investment to be classified as a direct investment for statistical purposes.<sup>3</sup> FDI is typically measured in either *inflows* or *stocks*. “FDI inflows” refer to the capital provided by a foreign investor to a foreign affiliate (equity, loans, reinvestment earnings), while “FDI stocks” are the total value of foreign-owned assets at a given time.

Over the past twenty years, FDI inflows have expanded substantially, from approximately \$40 billion at the beginning of the 1980s, to \$200 billion in 1990, to some \$1.5 trillion in 2007 (Figure 1). Cross border mergers and acquisitions (M&As) are the principal drivers of this growth, as they are the main form of FDI in the developed world and an increasingly important one in emerging markets.<sup>4</sup> The value of the global inward FDI stock is expected to climb to about \$14 trillion by the end of 2007 (Figure 2). There are more than 80,000 multinational enterprises (MNEs) globally, with more than 800,000 foreign affiliates.<sup>5</sup> The developed countries attract the lion’s share of world FDI flows (nearly two-thirds in 2007<sup>6</sup>), with Asia being the most attractive region among emerging markets (Figure 3). Some two-thirds of world FDI inflows, and half of FDI inflows in developing countries, are in services.<sup>7</sup>

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<sup>2</sup> OECD, *Detailed Benchmark Definition of Foreign Direct Investment* (Paris: OECD, 1996), third edition, and International Monetary Fund, *Balance of Payments Manual* (Washington: IMF, 1993), fifth edition.

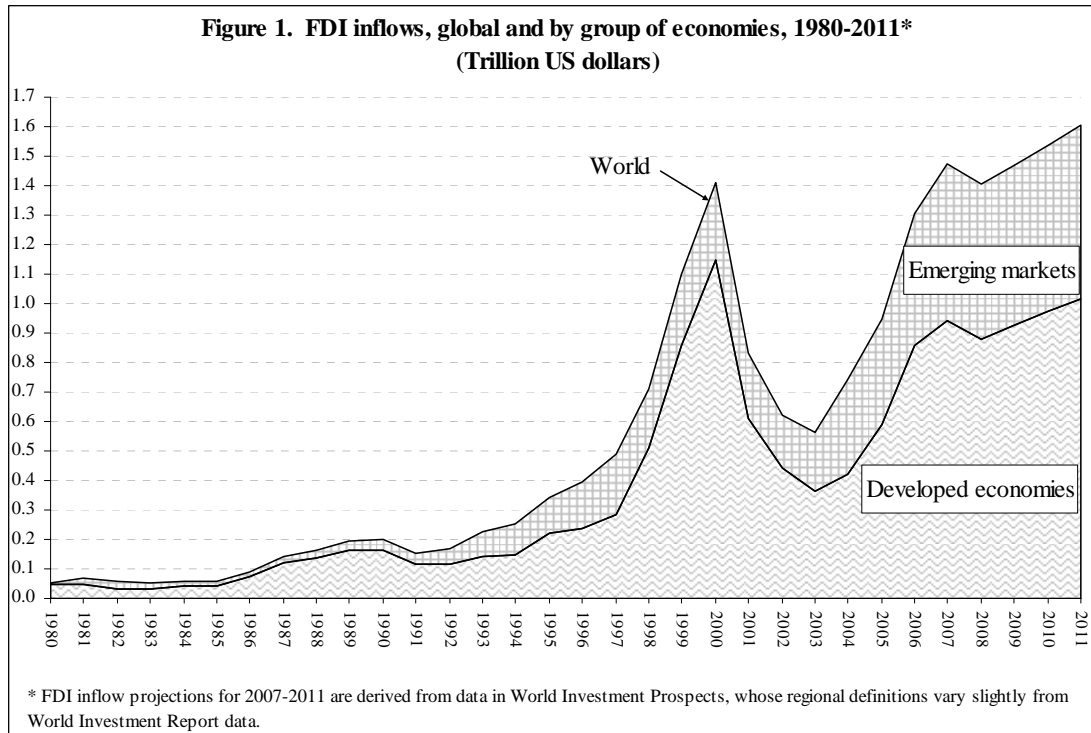
<sup>3</sup> It should be noted that the definition of “investment” in BITs is typically much broader and includes “everything of economic value, virtually without limitation,” in order to ensure flexibility in the BIT’s application. Calvin Hamilton and Paula Rochwerger, “Trade and investment: foreign direct investment through bilateral and multilateral treaties,” 18 N.Y. Int’l L. Rev. 1 (2005), p. 12.

<sup>4</sup> In this overview, *developed countries* are members of the OECD, excluding the Republic of Korea and Mexico. *Economies in transition* are the former Socialist countries, except if otherwise noted, and *developing countries* are all remaining countries. *Emerging markets* are economies in transition and developing countries combined. These categories vary slightly among different sources, so the data may reflect slight variations in country classifications. Similarly, the studies of the impact of BITs and DTTs included in this volume may employ slightly varied categorizations.

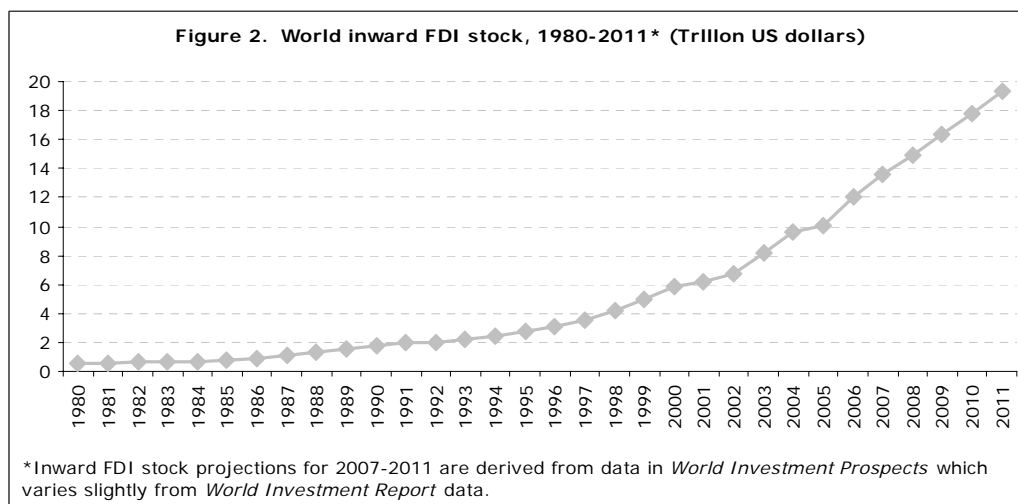
<sup>5</sup> UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development* (New York and Geneva: United Nations, 2007), p. 218.

<sup>6</sup> Laza Kekic and Karl P. Sauvart, eds., *World Investment Prospects to 2011: Foreign Direct Investment and the Challenge of Political Risk* (London: The Economist Intelligence Unit, 2007), p. 6 (table 1).

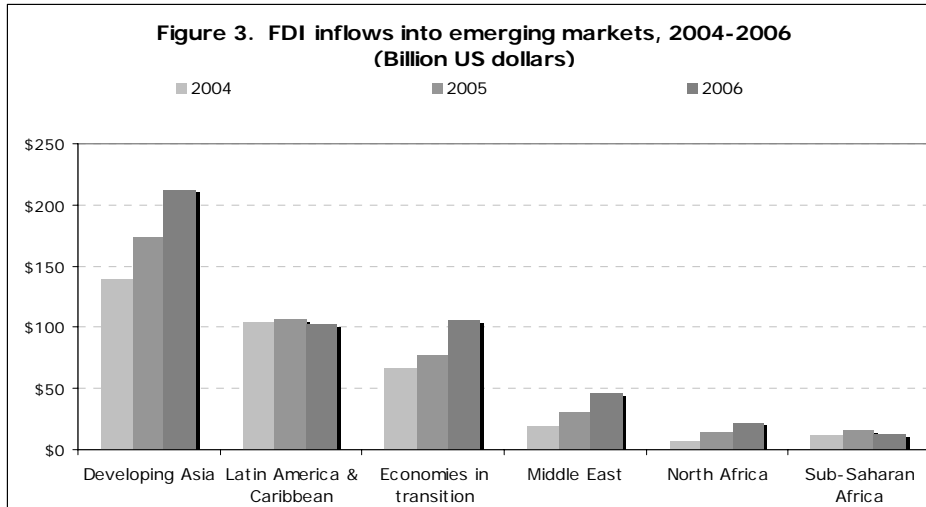
<sup>7</sup> As of 2005. UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development* (New York and Geneva: United Nations, 2007), p. xvi.



Source: UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development* (New York and Geneva: United Nations, 2007), p. 3, and Laza Kekic and Karl P. Sauvart, eds., *World Investment Prospects to 2011: Foreign Direct Investment and the Challenge of Political Risk* (London: The Economist Intelligence Unit, 2007).



Source: UNCTAD (<http://stats.unctad.org/fdi/>), and Kekic and Sauvart, *op. cit.*



Source: Kecic and Sauvant, *op. cit.*

Global FDI flows over the next few years will depend on the principal FDI determinants. The regulatory framework, on balance, will most likely remain favorable, with a further liberalization of FDI laws and regulations and the strengthening of the international investment law system; however, there are signs of a backlash against FDI that make the regulatory framework less welcoming in a number of countries.<sup>8</sup> Investment promotion, too, will continue, although countries may shift toward a more targeted approach. Finally, in light of the turmoil in financial markets and the effect this may have on the real economy, economic growth—the principal FDI determinant—may decrease substantially or even turn negative in key economies, negatively affecting FDI flows. Current estimates are that this combination of factors will mean that such flows will remain at a plateau of about \$1.4–\$1.6 trillion in the next few years, with the caveat that the current economic turmoil does not turn into a widespread recession.<sup>9</sup>

Twelve of the top 20 FDI recipients are developed countries, with the top 20 accounting for three-quarters of world FDI inflows. The United States is the leading recipient and will likely retain its dominant position in 2007–2011 (Table 1). However, FDI into the EU as a whole is significantly higher than inflows into the United States, and the EU will continue to outstrip the United States as a host region for such investment.<sup>10</sup> Among emerging markets, concentration also remains relatively high, with the top ten recipients accounting for 55% of all inflows to emerging markets in 2006. China was by far the main FDI host among emerging markets in 2006 (Figure 4), with almost 6% of the global total, and is expected to rank behind only the United States and the United Kingdom in 2007–2011.

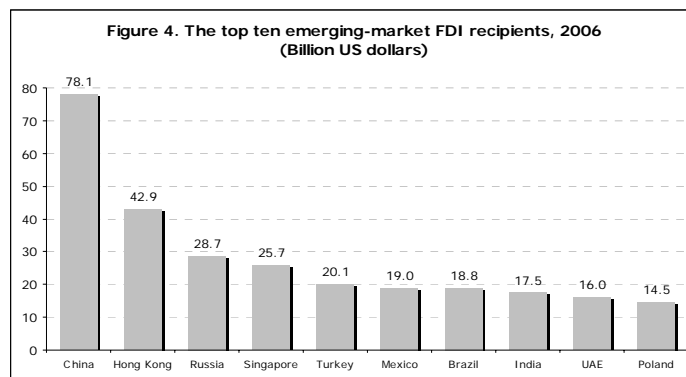
<sup>8</sup> Karl P. Sauvant, “Regulatory risk and the growth of FDI,” in Kecic and Sauvant, *op. cit.*, p. 71.

<sup>9</sup> Kecic and Sauvant, *op. cit.*, p. 6.

<sup>10</sup> These data include intra-EU flows—that is, FDI flows from one EU country to another. If intra-EU flows were excluded from the calculation, FDI inflows to the United States would exceed inflows to the EU.

Table 1. FDI inflows, 2007-2011 average (Billion US dollars and percent)			
Economy	Value	Rank	Share in world Total
US	251	1	17
UK	113	2	8
China	87	3	6
France	78	4	5
Belgium	72	5	5
Germany	66	6	4
Canada	63	7	4
Hong Kong, China	48	8	3
Spain	45	9	3
Italy	42	10	3
Netherlands	39	11	3
Australia	38	12	3
Russia	31	13	2
Brazil	28	14	2
Singapore	27	15	2
Sweden	26	16	2
Mexico	23	17	2
India	20	18	1
Ireland	20	19	1
Turkey	20	20	1

Source: Kecic and Sauvart, *op. cit.*, p. 9.

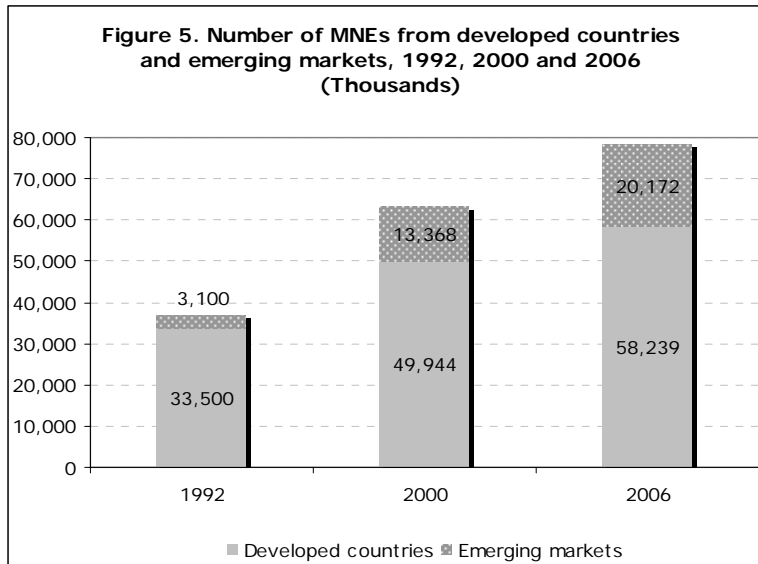


Source: Laza Kecic, “Global foreign direct investment to 2011,” in Kecic and Sauvart, *op. cit.*, p. 24.

While the vast majority of FDI flows emanate from developed countries, companies from emerging markets (mostly in Asia) are increasingly becoming important players in the world FDI market. An estimated 20,000 MNEs are now headquartered in emerging markets (Figure 5), and outward FDI flows from these economies rose to approximately \$210 billion in 2006, or 17% of the global total (Table 2). The stock of this investment amounts to an estimated \$1.8 trillion.<sup>11</sup> Until relatively recently, most FDI flows from emerging markets took the form of South-South investment. But MNEs from these economies have also in more recent years undertaken some large, high-profile acquisitions in developed countries that have attracted considerable attention. The rise of multinationals from the South—especially those of state-controlled entities (including sovereign wealth funds)—is feeding rising protectionist and nationalist sentiment in parts of the

<sup>11</sup> UNCTAD, *World Investment Report 2007*, *op. cit.*, p. 255. Note that this value is based on a different dataset from the values for FDI flows, and the classification of “emerging economies” may vary slightly.

developed world, which makes it all the more important to keep the development of emerging-market outward FDI in perspective. Despite the increase in these FDI flows in recent years (likely to be boosted further by investments by sovereign wealth funds), they are still dwarfed by investment originating in the developed world.



Source: UNCTAD, *World Investment Reports 1993, 2003, and 2007*. Annex tables.

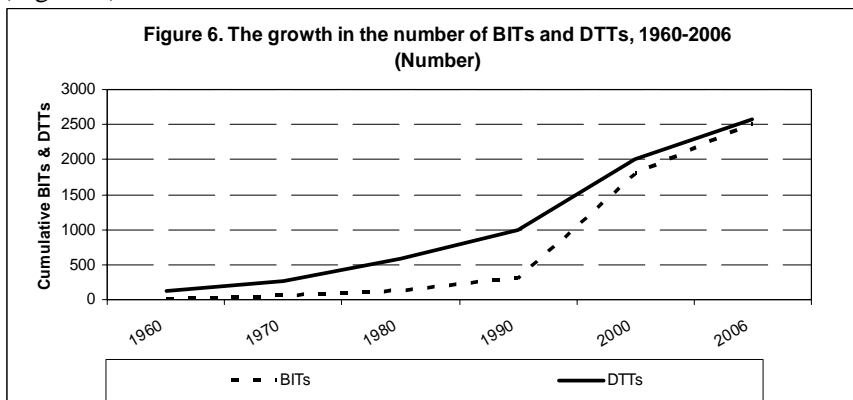
**Table 2. Global FDI outflows**  
(Billion US dollars and percent)

Country group	1999	2000	2001	2002	2003	2004	2005	2006
<b>Developed countries</b>	<b>1,004</b>	<b>1,104</b>	<b>687</b>	<b>477</b>	<b>505</b>	<b>723</b>	<b>731</b>	<b>1,051</b>
Share in total	93	87	89	88	93	88	82	83
<b>Emerging markets</b>	<b>73</b>	<b>163</b>	<b>81</b>	<b>64</b>	<b>41</b>	<b>94</b>	<b>160</b>	<b>210</b>
Share in total	7	13	11	12	8	12	18	17

Source: Kestic, "Global foreign direct investment to 2011," in Kestic and Sauvart, *op. cit.*, p. 28.

## B. International investment agreements

As countries increasingly opened their doors to FDI in the 1980s and 1990s, they simultaneously entered into numerous international investment agreements, leading especially to an explosion in the number of bilateral investment treaties (BITs) and bilateral double taxation treaties (DTTs) (Figure 6).

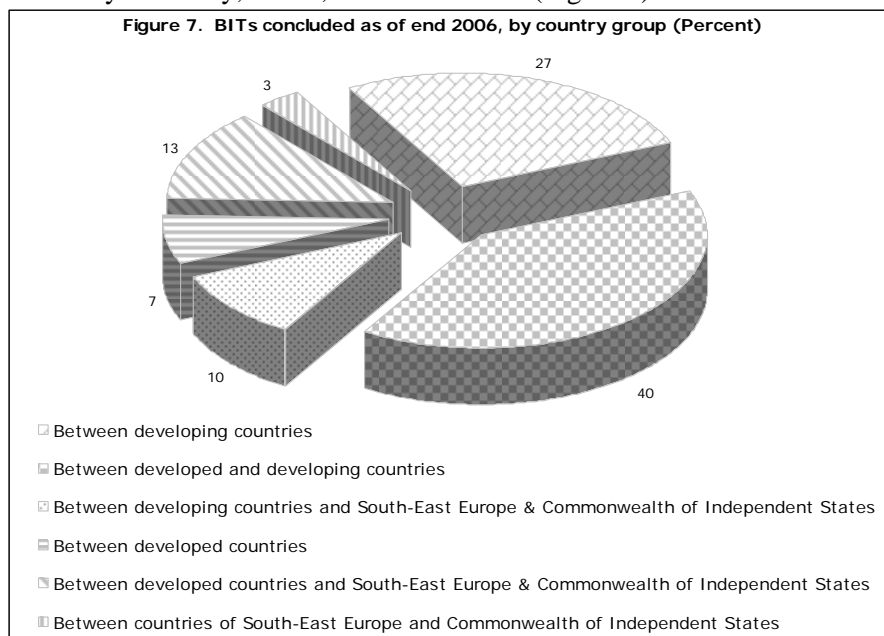


Source: UNCTAD (<http://www.unctad.org/iia>).

## 1. Bilateral investment treaties

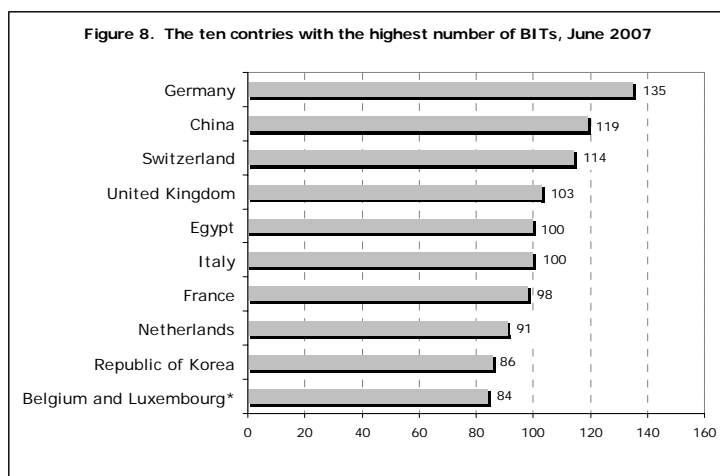
The FDI surge during the past few decades has been accompanied by a similar growth of international investment agreements. Pride of place among these agreements belongs to BITs—treaties that seek to protect and promote foreign investment. To put the evolution of BITs into a historic context, Kenneth Vandeveld (Chapter 1) traces the history of such agreements. He distinguishes three eras of BIT development (Colonial Era, Post-Colonial Era, Global Era), and describes how investment agreements have been shaped by the political, economic and legal contexts of each period. He also discusses broadly the evolution of the content of BITs as well as the legal enforceability of their substantive provisions, and articulates several current developments that may herald a fourth era in their development.

By the end of 2006, 2,573 BITs had been signed,<sup>12</sup> most of them since 1990. In fact, from 1959 (when the first BIT was concluded between Germany and Pakistan) until the end of 1989, only 386 BITs had been signed; more than 2,000 BITs were entered into in the following 15 years. By the end of 2006, 177 countries had entered into one or more bilateral investment treaties. (UNCTAD has the best database of BITs, available on its website at <http://www.unctad.org/iaa>.) While BITs were originally signed overwhelmingly between developed and developing countries, developing countries now routinely sign investment treaties with other developing countries (and economies in transition). Indeed, 680 BITs had been signed between developing countries by the end of 2006, constituting 27% of the stock of BITs (Figure 7). The economies with the most BITs are led by Germany, China, and Switzerland (Figure 8).



Source: UNCTAD, *World Investment Report 2007*, *op. cit.*, p. 17.

<sup>12</sup> J. Zhan, J. Karl and J. Weber, “International investment rule-making at the beginning of the 21st century: stocktaking and options for the way forward,” in José Alvarez and Karl P. Sauvant, with Kamil Gérard Ahmed, eds., *The Future of International Investment Law and Policy* (forthcoming).



Source: [www.unctad.org/ia](http://www.unctad.org/ia).

In addition to the conclusion of new BITs, countries are increasingly renegotiating existing treaties; there have been 121 renegotiated treaties by June 2008.<sup>13</sup> Some countries are renegotiating treaties due to changed circumstances, such as to bring existing BITs in line with commitments under other investment agreements (for instance when the Central European countries acceded to the EU in 2004), or to add or update certain provisions, such as dispute settlement clauses. Although most BITs provide for tacit renewal upon their expiration, some countries are renegotiating expired BITs to amend host-country commitments or to clarify existing provisions. While many renegotiations are intended to strengthen investor protections, some renegotiated BITs narrow investor protections—at least in some respects.<sup>14</sup> An increasing number of BIT renegotiations is expected in the coming years, as many BITs with a duration of ten to thirty years were signed in the 1990s.

BITs only become legally binding instruments when they enter into force. Although the signing of a BIT may have some legal consequences for host countries under international law, this act does not “establish legally binding obligations of the latter vis-à-vis the foreign investors.”<sup>15</sup> Some BITs stipulate that the agreement enters into force upon the signature of both parties. Most BITs, however, require each party to complete the domestic requirements necessary for the BITs’ entry into force, for instance the ratification by a national parliament and the notification of ratification to the treaty partner. By the end of 2005, 76% of all BITs signed until that point had entered into force; this share partly reflects the time lag due to relatively complicated domestic

<sup>13</sup> UNCTAD Research Note, “Recent developments in international investment agreements,” UNCTAD/WEB/ITE/IIT/2005/1, available at: [http://www.unctad.org/sections/dite\\_dir/docs/webiteit20051\\_en.pdf](http://www.unctad.org/sections/dite_dir/docs/webiteit20051_en.pdf)

<sup>14</sup> Examples of the former are the extension of the prohibition of performance requirements and the strengthening of transparency provisions; examples of the latter are clarification concerning regulatory takings and fair and equitable treatment.

<sup>15</sup> “The entry into force of bilateral investment treaties,” *IIA Monitor*, No. 3 (2006), UNCTAD/WEB/ITE/IIA/2006/9, p. 4. (“Before a treaty enters into force, contracting parties have a general obligation to refrain from acts that would defeat the object and purpose of the agreement. *See* Article 18 of the Vienna Convention on the Law of Treaties.”) In addition to the international law obligation not to defeat the object and purpose of a treaty that a country has signed but not yet ratified, a country’s domestic law (or policy) may well be to give that obligation effect by providing an investor a right to challenge a law that an investor argues violates the “object and purpose” of a signed but unratified BIT.

ratification processes. The share of BITs in force increases with respect to earlier BITs; for instance, more than 90% of the BITs signed in the first half of the 1990s have entered into force.<sup>16</sup>

BITs are agreements between two sovereign states. From the point of view of the capital-importing country, their basic purpose is to help to attract FDI. From the point of view of the capital-exporting country, the basic purpose of BITs is to protect investors from political risks and instability and, more generally, safeguard the investments made by its nationals in the territory of the other state.<sup>17</sup> This is why, originally, they were concluded primarily between developed and developing countries, as the former were virtually the only sources of FDI, and the latter were seen as often having risky and volatile business environments. Some of the more recent BITs, especially those with the United States and Canada, go further than protecting investors' rights and require the liberalization of certain aspects of the FDI regime of a host country, for example by including provisions of national and most-favored-nation treatment at the establishment phase of an investment<sup>18</sup> or by prohibiting host country governments from imposing certain performance requirements on foreign investments.<sup>19</sup>

Peter Muchlinski (Chapter 2) provides an overview of the principal substantive and procedural provisions of BITs. The substantive rights typically include a guarantee of prompt, adequate, and effective compensation for expropriation, freedom from unreasonable or discriminatory measures, a promise of "fair and equitable treatment" for foreign investments, guaranteed national and most-favored-nation treatment for investments, and assured full protection and security of investments. Together, these provisions are meant to boost investor confidence and the transparency of the policy environment. As mentioned, a number of more recently concluded BITs have expanded these rights somewhat to cover a wider range of host country activities in detailed and complex ways. A number of these provisions limit the regulatory flexibility of host countries to pursue not only economic development policies but other public policies as well. However, recent BITs also place somewhat greater emphasis on certain public concerns, including health, the environment, national security, labor rights, and transparency in information exchange and rulemaking.

While BITs are largely similar in their substantive content and structure, recent innovations in their provisions have led to greater variation. In particular, three broad approaches seem to be emerging: the liberalization approach, used mostly by the United States, Canada, Japan and the Republic of Korea (and some other Western Hemisphere countries); the protection approach, mostly followed by European countries; and the more qualified protection approach, used mostly between developing countries. One notable difference is that the liberalization approach extends national treatment and most-favored-nation obligations to the pre-establishment phase of investment, while the two other approaches traditionally cover only the post-establishment phase. Additionally, the recent U.S. and Canadian model BITs clarify the meaning of, inter alia, the provisions on the minimum standard of treatment and regulatory takings, following lessons learned in recent NAFTA litigation, whereas the European BITs have not yet adopted these clarifications. BITs between developing countries are quite similar to the European BITs, but they

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<sup>16</sup> "The entry into force of bilateral investment treaties," *IIA Monitor*, No. 3 (2006), UNCTAD/WEB/ITE/IIA/2006/9.

<sup>17</sup> It should be noted that investments can also be protected through specific agreements between host country governments and foreign investors, or state contracts. These can be found especially in the natural resource sector.

<sup>18</sup> Most of these treaties have, however, reservations that restrict the applicability of such clauses.

<sup>19</sup> Tom Ginsburg, "International substitutes for domestic institutions: bilateral investment treaties and governance," 25 *Int'l Rev. of L. & Econ.* 107, at 108 (2005).

often put more emphasis on exceptions and include clauses requiring the contracting parties to choose between litigation in the host country or in an international tribunal in case of a dispute.<sup>20</sup>

The procedural rights, one of the novel and noteworthy features of modern BITs, afford investors an adjudicatory mechanism to enforce substantive rights.<sup>21</sup> Typically, investors can choose between arbitral panels at the World Bank's International Centre for Settlement of Investment Disputes (ICSID), arbitration at another designated forum<sup>22</sup> or ad hoc arbitration proceedings (especially UNCITRAL). This dispute settlement provision provides investors a remedy for unlawful or uncompensated actions by host states that affect their investments, usually without having to exhaust local remedies first before resorting to international arbitration. The designation of a third-party arbitration process frees investors from reliance on the political and judicial processes of host countries (which they often consider—rightly or wrongly—as being insufficient), and gives them direct access to protection under international law. If the proceeding is conducted under the ICSID Convention, the arbitration process is beneficial for the respondent state because it eliminates the possibility of diplomatic protection by the investor's home country. While the ICSID Convention (Article 36.1) provides that both host country governments of contracting states and investors of contracting states can initiate investment-dispute settlement proceedings, BITs limit such initiation to investors.<sup>23</sup>

There were only a handful of internationally arbitrated investor-state disputes in the 1980s and early 1990s; however, by the end of 2007, 290 known international treaty-based arbitration cases had been initiated, involving at least seventy-three countries—fifteen developed countries, forty-four developing countries, and fourteen economies in transition.<sup>24</sup> Over three-quarters of these cases had arisen since the beginning of 2002, and close to two-thirds of them were filed with ICSID (or the ICSID Additional Facility) (Figure 9).<sup>25</sup> Argentina has by far faced the highest share of claims filed at ICSID, most of which stem from its government's emergency measures during the 2001 financial crisis. At least forty-six cases had been brought against Argentina for violating investment treaty protections, with twenty arbitrations brought in 2003 alone. Almost all

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<sup>20</sup> UNCTAD, "South-south cooperation in international investment arrangements," UNCTAD/ITE/IIT/2005/3 (New York and Geneva: United Nations, 2005). Available at: [http://www.unctad.org/en/docs/iteiit20053ch2\\_en.pdf](http://www.unctad.org/en/docs/iteiit20053ch2_en.pdf)

<sup>21</sup> Most BITs have arbitration provisions, particularly the most recent ones; however, some do not, and some allow for very limited investor-state arbitration.

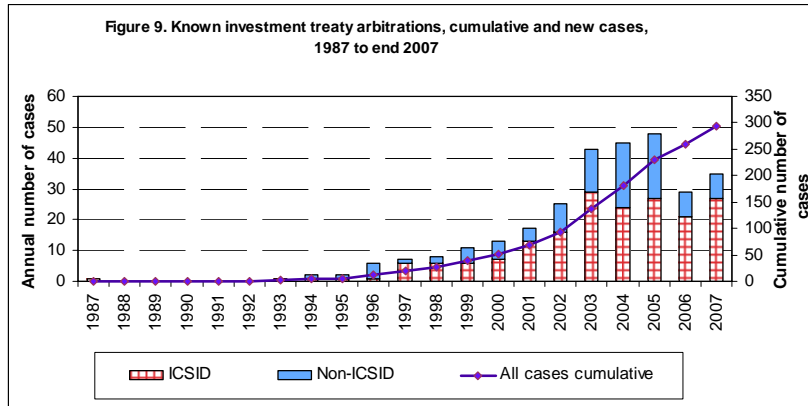
<sup>22</sup> Other institutions available for arbitration include the ICC Court of Arbitration in Paris, the Stockholm Chamber of Commerce Arbitration, the London Court of International Arbitration, and various regional arbitration centers.

<sup>23</sup> All treaty-based investment arbitration requires the consent of both parties. Host countries consent to treaty-based investment disputes in the dispute settlement clause of the BIT; since investors are not parties to BITs, BITs cannot constitute the investors' consent. An investor's consent is embodied in its claim, so no consent exists until the investor has filed a claim, at which point most BITs allow the host-country to file a counter-claim.

<sup>24</sup> UNCTAD, *IIA Monitor*, No. 1 (2008). There are also higher estimates. See the "Investment Treaty News: Year in Review 2006," [http://www.iisd.org/pdf/2007/itn\\_year\\_review\\_2006.pdf](http://www.iisd.org/pdf/2007/itn_year_review_2006.pdf). For a discussion of the reasons for this rise in investment disputes, see Jeswald W Salacuse, "Explanations for the increased recourse to treaty-based investment dispute settlement: resolving the struggle of life against form?", in Karl P. Sauvant with Michael Chiswick-Patterson (eds.), *Appeals Mechanism in International Investment Disputes* (New York: Oxford University Press, 2008).

<sup>25</sup> The total number of investor-state arbitration proceedings is not known because ICSID is the only institution that publicly provides a list of cases. UNCTAD, "Investor-state disputes and policy implications," TD/B/COM.2/62 (Jan. 17, 2005), available at [http://www.unctad.org/en/docs/c2d62\\_en.pdf](http://www.unctad.org/en/docs/c2d62_en.pdf). It appears that, in 2006, there were more non-ICSID cases than ICSID cases. See the "Investment Treaty News: Year in Review 2006," [http://www.iisd.org/pdf/2007/itn\\_year\\_review\\_2006.pdf](http://www.iisd.org/pdf/2007/itn_year_review_2006.pdf).

treaty-based investment disputes are disputes brought by investors against host countries; the only known exception is a 2003 dispute between Chile and Peru, brought by Peru against Chile after a Chilean firm filed an investor-state claim against Peru.<sup>26</sup> These proceedings have alleged treaty violations in response to a range of state measures, including, for instance, emergency laws enacted during a financial crisis and the re-zoning of land for specific uses, and in a broad range of sectors such as construction, water and sewage services, telecommunications, financial services, mining, gas and oil production.<sup>27</sup>



Source: UNCTAD, *IIA Monitor*, No. 1 (2008).

Because of the confidentiality of proceedings, it is difficult empirically to evaluate data about parties to investment arbitrations, judgments and awards (if any).<sup>28</sup> However, while imprecise and potentially subject to statistical biases, some trends can be inferred from data relating to known arbitrations. A study of 102 known investment treaty arbitration awards, deriving from eighty-two individual cases, showed that the tribunals resolved the treaty claims, and assessed whether damages were to be awarded, in fifty-two cases. In the majority of these (31 cases), the investor claimants were awarded nothing, while in twenty-one cases, the country respondent was ordered to pay damages to the investors.<sup>29</sup> Furthermore, in the cases in which the investors did win, the awards were generally not large: only eight of the twenty-one cases that resulted in awards for the investors awarded them more than \$5 million.<sup>30</sup> There were four cases in which the award exceeded \$10 million; the largest was a 2003 award to a Dutch-based firm in a dispute with the Czech Republic, in which the latter was ordered to pay some \$270 million plus substantial interest for violating the terms of an investment treaty with The Netherlands.<sup>31</sup> In 2006 and 2007,

<sup>26</sup> Lucchetti S.A. and Lucchetti Peru S.A. v. Republic of Peru, ICSID Case No. ARB/03/4. There were a few other ICSID cases brought by states against investors; however in those cases, the basis of jurisdiction was not a treaty but a contract between the investor and the state concerned: *Tanz. Elec. Supply Co. Ltd. v. Indep. Power Tanz. Ltd.*, ICSID Case No. ARB/98/8 and *Gabon v. Société Serte*, ICSID Case No. ARB/79/1, *Government of the Province of East Kalimantan v. PT Kaltim Prima Coal and others* (Case No. ARB/07/3).

<sup>27</sup> UNCTAD, "Investor-state disputes and policy implications," TD/B/COM.2/62 (Jan. 17, 2005), available at [http://www.unctad.org/en/docs/c2d62\\_en.pdf](http://www.unctad.org/en/docs/c2d62_en.pdf). A recent empirical study found that energy is the most heavily arbitrated sector, followed by the financial sector, food and beverage sector, transportation, and real estate transactions. Susan Franck, "Empirically evaluating claims about investment treaty arbitration," 86 *NC L Rev.* 1, at 38 (2007)

<sup>28</sup> However, numerous awards and other decisions are available through a variety of sources.

<sup>29</sup> Franck, *supra* note 27, at 52.

<sup>30</sup> The investor claims are often very high. So in cases in which there have been awards, the awards have often been substantially lower than the initial claims. Franck, *supra* note 27, at 54.

<sup>31</sup> *CME Czech Republic B.V. v. Czech Republic*, UNCITRAL, Final Award (Mar. 14, 2003), at

however, several awards in excess of \$10 million indicate that the size of the awards may be increasing.<sup>32</sup>

It is unclear whether the rise in arbitrations will have an effect on the location of FDI or on countries' perceived value of BITs—and, if there is an effect, what it will be. It is possible that this development may increase investors' awareness of the protections and procedural rights that BITs afford investors and hence may cause more investors to consider the existence of investment treaties and the availability of arbitration when deciding on locations for FDI.<sup>33</sup> On the other hand, the risk of investor success in these disputes, the financial burden of arbitration proceedings, and the sovereignty costs<sup>34</sup> associated with the implementation of these treaties may lead some countries to conclude that the costs of BITs (and IIAs in general) outweigh their benefits. Ecuador's announcement in February 2008 that it plans to withdraw from nine of its bilateral investment treaties and Bolivia's withdrawal from the ICSID Convention in May 2007 may reflect a growing skepticism toward investment treaties and the international arbitration of investment disputes.<sup>35</sup> As countries and investors adjust to the new provisions and scope of recent IIAs, as new patterns emerge in investment arbitration as regards, for example, the risk of being sued or the size of awards, and as the size of the international treaty network grows, the effect of these treaties on FDI flows may evolve as well.

Although both developing and developed countries have been concluding BITs at a rapid pace over the past few decades—as capital exporters seek to benefit from investor protections and capital importers hope to benefit through increased FDI flows—several scholars have been critical about BITs and their impact on developing countries. There is first of all the question

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[http://ita.law.uvic.ca/documents/CME-2003-Final\\_001.pdf](http://ita.law.uvic.ca/documents/CME-2003-Final_001.pdf) (awarding CME \$269,814,000 in damages for breach of an investment treaty).

<sup>32</sup> Note, however, that this trend has been dominated by the recent cases involving Argentina. It is also important to note that, in an unknown number of cases, investor claims are settled before the arbitration process is set in motion; the data on known awards do not account for such settlements between parties. In some cases, investors may be using the threat of procedural rights of BITs to compel host country compensation or the recall of certain host country measures that adversely affected an investment. Furthermore, the possible “regulatory chill” resulting from the risk of treaty arbitration is impossible to measure. Therefore, the impact of BITs on the balance of power between investors and host countries is not measurable only from the awards effectively pronounced.

<sup>33</sup> See Susan Franck, “Foreign direct investment, international treaty arbitration, and the rule of law,” 19 *Pac. McGeorge Global Bus. & Dev. L.J.* 337 (2007).

<sup>34</sup> See especially Santiago Montt, “The BIT generation's emergence as a collective action problem: prisoner's dilemma or network effects?” *Latin American and Caribbean Law and Economics Association Annual Papers*, paper 043007'3, University of California, Berkeley, 2007. It should be noted in this context that all BIT guarantees can also be implemented unilaterally through domestic legislation, though domestic legislation cannot “internationalize” the commitment to certain forms of guaranteed investor treatment, which is a particularly valuable aspect of BITs in certain countries from the perspective of investors.

<sup>35</sup> Moreover, on December 4, 2007, Ecuador notified ICSID that it would not consent to ICSID arbitration of disputes pertaining to investments in natural resources, such as oil, gas, and minerals. Pursuant to Article 25(4) of the ICSID Convention, a Contracting State may notify the Centre of the class or classes of disputes which the State would or would not consider submitting to the jurisdiction of the Centre. Such notification may be made at the time of ratification, acceptance or approval of the Convention or at any time thereafter. “Ecuador's Notification under Article 25(4) of the ICSID Convention,” ICSID news release, December 5, 2007. There were also reports as of April 2008 that the Committee on Territorial Sovereignty of the Constituent Assembly of Ecuador has recommended to the floor a provision forbidding the government from submitting controversies to international arbitration. “Mesa de soberanía elimina el arbitraje internacional para el país,” *Diario Hoy* (April 15, 2008). Venezuela and Nicaragua have also suggested that they may withdraw from the ICSID Convention.

whether, from a host country point of view, these treaties achieve their most basic objective—namely, to attract more FDI—precisely the focus of this volume. But there are broader considerations as well. Andrew Guzman (Chapter 3) argued that, whereas developing countries might have been better off negotiating a multilateral investment agreement as a group, individual developing countries defected in a prisoners’ dilemma situation as each tried to attract the largest possible share of foreign investment by concluding bilateral treaties with developed countries.<sup>36</sup> He suggested that, by not taking collective action with other developing countries, countries have ratcheted up the investor protections that each country has committed to in bilateral agreements rather than working toward a multilateral agreement that could have made them all better off.<sup>37</sup>

Others are critical of BITs because they find that, by agreeing to international enforcement mechanisms and institutions, developing countries have neglected domestic legal institutions and mechanisms, such that “under some circumstances BITs may lead to lower institutional quality in subsequent years.”<sup>38</sup> Finally, a number of authors have cautioned against the increased restrictions on developing countries’ regulatory flexibility imposed by BITs, even if new policies would be consistent with the country’s development objectives, or the furtherance of human rights goals, or would be necessary or desirable in response to a specific situation at a given time.<sup>39</sup> Whether countries are responding to economic crises (such as in Argentina following the 2001 financial crisis) or trying to protect nascent local industries, some BITs prohibit the country from imposing measures that could adversely affect foreign investors.<sup>40</sup>

While BITs are by far the most common agreements on foreign investment, beginning in the 1990s, investment issues have also been addressed increasingly and in a substantial manner in bilateral and regional free trade agreements, which, in the process, have become free trade and investment agreements (FTIAs).<sup>41</sup> Typical investment provisions of FTIAs include most-favored-nation and national treatment. In addition to provisions that specifically address investment protection, they often also include liberalization clauses. In that manner, they might directly

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<sup>36</sup> Some of this reasoning seems to assume that, at any given time, there is a fixed pool of FDI for which countries compete. It is unclear to what extent this is accurate; the rise of FDI flows during the past decade indicates that this is not the case.

<sup>37</sup> One could add, however, that, in the absence of BITs, host countries may be tempted to provide even more specific guarantees to foreign investors (especially efficiency-seeking foreign investors) which could lead to more “beggar-thy-neighbor” policies. Therefore, while BITs may leave developing countries worse off than a multilateral investment agreement would, they may do so less than to let investors “host-country shop” for special privileges.

<sup>38</sup> Ginsburg, *op. cit.*, p. 122.

<sup>39</sup> See e.g., Luke Eric Peterson and Kevin R. Gray, “International human rights in bilateral investment treaties and in investment treaty arbitration,” International Institute for Sustainable Development (2003), p. 5. Peterson argued, for example, that “host states may wish to regulate the economy, including foreign investors embedded therein, in a manner which seeks to *promote or protect* certain human rights interests.... Where bilateral investment treaties are in place, foreign investors will often enjoy the ability to challenge these human-rights inspired measures through international arbitration.” See also, Ursula Kriebaum, “Privatizing human rights—the interface between international investment protection and human rights,” *Transnational Dispute Management* (2006), p. 14: “[An] investor may use BIT provisions to challenge human rights-inspired regulations that interfere with its investment.”

<sup>40</sup> J.F. Perez-Lopez and M.F. Travieso-Diaz, “The contribution of BITs to Cuba’s foreign investment program,” 32 *Law & Pol’y Int’l Bus.* 529 (2001).

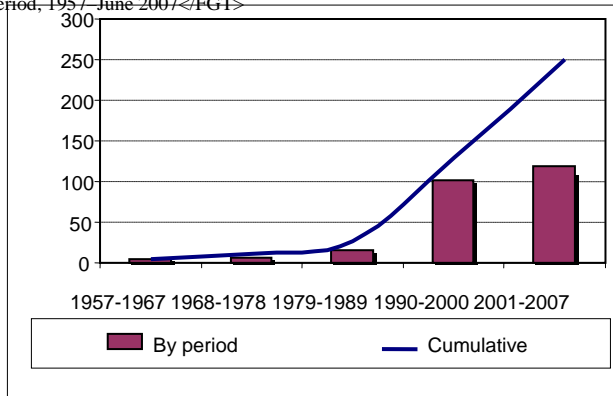
<sup>41</sup> This represents a return to earlier patterns (e.g. the U.S. Friendship, Commerce and Navigation treaties) in which treaties addressed investment issues in the context of a range of issues. This approach allows trade-offs across issue areas (e.g. market access for increased investor protection). FTIAs also increasingly address host country responsibilities with respect to labor rights and environmental protection, topics ordinarily not addressed in BITs and never in DTTs.

influence FDI flows by liberalizing investment conditions (by, most notably, opening sectors for investment). They might also indirectly influence FDI flows by enlarging the market, changing trade flows, setting and harmonizing standards, and improving a host country's economic growth potential and overall investment climate.

While the overall number of FTIAs and other treaties with investment provisions is still small (fewer than 10% of the number of BITs) their number is growing rapidly and, to the extent that they are regional, they cover more countries than there are agreements. As of June 2007, 251 FTIAs had been signed—nearly twice as many as five years earlier (Figure 10).<sup>42</sup> These agreements are increasingly signed among developing countries; at the end of 2006, there were more than ninety IIAs other than BITs and DTTs concluded among developing countries.<sup>43</sup> In contrast, the rise in the number of new BITs has slowed down in recent years, partly because most countries have already concluded BITs with their most important investment partners, partly because investment protection is increasingly included in free trade agreements and other IIAs, and partly, perhaps, because arbitral awards in favor of investors may make some countries more wary about concluding additional BITs.

Finally, there are also a number of inter-regional and multilateral investment agreements, most prominent among them the Energy Charter Treaty,<sup>44</sup> the General Agreement on Trade in Services, and the Trade-related Investment Measures Agreement. While they are meant to establish a more welcoming enabling framework for FDI, their effect on FDI flows is difficult to ascertain.

<FGN>Figure 10.</FGN> <FGT>Number of other agreements\* concluded, by period, 1957–June 2007</FGT>



<FGS>Source: UNCTAD ([www.unctad.org/ia](http://www.unctad.org/ia)).</FGS>  
 <FGC>\* International agreements, other than BITs and DTTs, that contain investment provisions.</FGC>

## 2. Double taxation treaties

The surge of FDI flows has also been accompanied by a surge of double taxation treaties. They serve a different but complementary purpose to BITs. While the primary purpose of BITs is to protect foreign investments, one of the main purposes of DTTs is to deal with issues arising out of the allocation of the revenues generated by these investments between host and home countries—for instance, how to allocate tax revenue from taxes imposed on income earned by multiple

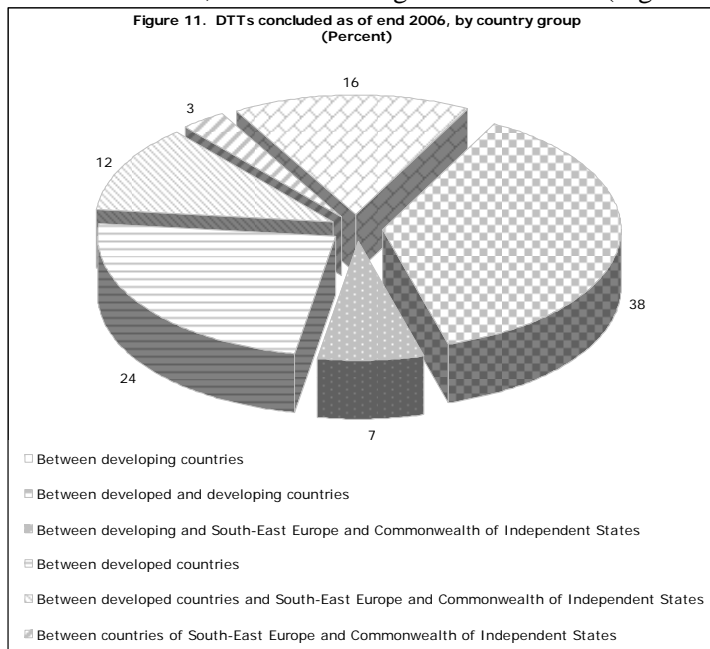
<sup>42</sup> UNCTAD Research Note, “Recent developments in international investment agreements,” UNCTAD/WEB/ITE/IIT/IIA/2007/6, available at: [http://www.unctad.org/en/docs/webiteia20076\\_en.pdf](http://www.unctad.org/en/docs/webiteia20076_en.pdf)

<sup>43</sup> UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development* (New York and Geneva: United Nations, 2007), p. 17.

<sup>44</sup> See e.g., Wälde, Thomas W. (ed.). *The Energy Charter Treaty: An East-West Gateway for Investment and Trade* (London, The Hague, Boston: Kluwer Law International Ltd., 1996).

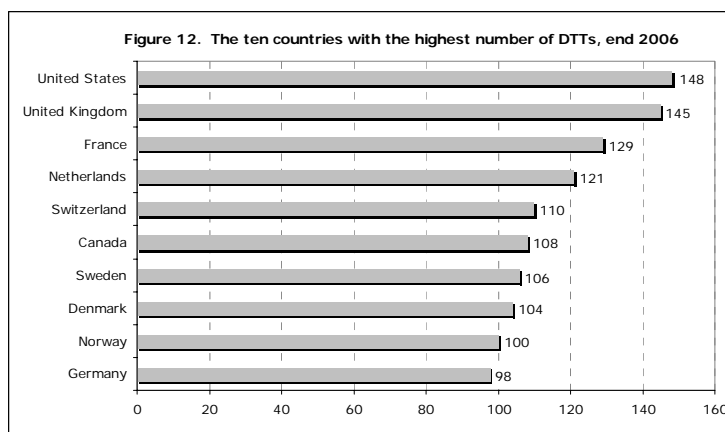
entities of a MNE system. The preferential tax and related arrangements in DTTs reduce the administrative complexity of foreign investments and facilitate the flow of goods and services between the treaty partners. As is the case with BITs, the propensity of countries to enter into DTTs reflects the growing role of FDI in the world economy and countries' efforts to attract MNEs to their own territories and facilitate their operations.

The steady rise of DTTs (Figure 6) began nearly four decades ago (while the sharp rise in BITs began in the early 1990s). By the end of 2006, 2,651 DTTs had been signed.<sup>45</sup> Unlike BITs, which were initially concluded largely between developing and developed countries, DTTs were initially signed primarily between developed countries, as these were traditionally the main capital exporting and capital importing countries and thus faced the greatest double taxation challenges. Starting in the late 1960s, as emerging markets increasingly became host countries for FDI, and gradually also became home countries, the number of those countries that signed DTTs with both developed countries and other developing countries also began to rise rapidly (Figure 11). Developed countries still top the list of the countries with the largest number of DTTs, led by the United States, the United Kingdom and France (Figure 12).



Source: UNCTAD, *World Investment Report 2007*, *op. cit.*, p. 18.

<sup>45</sup> Zhan, Karl and Weber, *op. cit.*



Source: [www.unctad.org/iia](http://www.unctad.org/iia).

Most double taxation treaties are based on one of two international models, which in turn are based on models developed by the League of Nations. Developed countries coordinate their efforts on international tax matters in the Fiscal Committee of the OECD. In 1963, these countries issued a draft model DTT,<sup>46</sup> which is updated periodically and has become the model for most DTTs concluded since its conception. In addition, a Committee of Experts on International Cooperation in Tax Matters, convened by the Secretary-General of the United Nations, issued a “Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries,” as well as the “United Nations Model Double Taxation Convention between Developed and Developing Countries” in 1979, which are also updated periodically.<sup>47</sup> The UN model was drafted specifically because of concerns that the OECD model was not appropriate for tax treaties between developed and developing countries, which involve non-reciprocal cross border activity. Nevertheless, the OECD and UN models share many common features. Most DTTs are based on one of these two models, with exceptions and variations depending on the specific relationship between the two contracting states. One other model DTT is that of the United States, first published in 1977, which incorporates much of the OECD model but also includes provisions to reflect the specific policies of the United States.<sup>48</sup>

Reuven Avi-Yonah (Chapter 4) provides an overview of the reasons for the rise of DTTs and their salient features. The need to address the issue of revenue allocation between host and home countries arose as increased international investment created a potential conflict of tax jurisdictions, that is, two or more jurisdictions had the right to levy tax on a single event or a single taxpayer (e.g., a company operating in several countries). Double taxation can also occur in other situations, for instance if jurisdictions have different tax definitions, residency requirements or income classifications. When the national tax laws of the two countries differ significantly, the jurisdictional conflict can also lead to improper conduct by taxpayers. Jurisdictional conflicts can

<sup>46</sup> The “OECD Model Convention on Income and on Capital” (MTC) is available at:

[http://www.oecd.org/document/17/0,3343,en\\_2649\\_33747\\_35035793\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/17/0,3343,en_2649_33747_35035793_1_1_1_1,00.html)

The electronic version of the MTC is based on the text as it was updated in January, 2003, but includes the 1963 and 1977 texts.

<sup>47</sup> The “Manual for the Negotiation of Bilateral Tax Treaties between Developed and Developing Countries” is available at: <http://unpan1.un.org/intradoc/groups/public/documents/un/unpan008579.pdf>; the “United Nations Model Double Taxation Convention between Developed and Developing Countries” is available at: <http://unpan1.un.org/intradoc/groups/public/documents/UN/UNPAN002084.pdf>.

<sup>48</sup> “U.S. Model Income Tax Convention of Sept. 20, 1996,” available at: <http://www.treas.gov/offices/tax-policy/library/model1996.pdf>.

be relieved unilaterally (under national tax laws) or at times multilaterally<sup>49</sup>; on the other hand, DTTs provide the most important and most common international measures to relieve double taxation problems.

In order to help eliminate double taxation and to relieve jurisdictional conflicts, double taxation treaties standardize tax definitions in the countries party to a treaty, and they detail specific allocation rules for different categories of income, reducing uncertainty about the tax environment in both countries. DTTs also can limit transfer pricing, help to combat tax evasion (notably through the exchange of information), reduce the risk of treaty shopping<sup>50</sup>, provide non-discrimination rules, and outline ways in which tax disputes can be resolved by prescribing specific conflict resolution mechanisms and arbitration procedures.<sup>51</sup> Furthermore, while unilateral measures can often eliminate double taxation on their own, thus obviating the need for DTTs to prevent double taxation, the treaties can still be useful in “borderline” situations, such as cases in which the source of income is disputed.<sup>52</sup> Importantly, DTTs provide greater legal certainty to foreign investors with respect to the tax treatment of their cross-border activities in both the host and the home country.<sup>53</sup> In the absence of DTTs, there could be more source taxation and less residence taxation, and there would be more administrative complexity, especially where investment flows are reciprocal. While the stated purpose of DTTs is to address these tax issues—the very limited preambles of most DTTs do not mention FDI—most countries (including the United States), as well as much literature and commentaries, have claimed that, by eliminating excessive taxation, tax treaties can help increase trade and investment between the two treaty signatories.<sup>54</sup>

Capital-exporting countries, foreign investors and capital-importing countries stand to gain from DTTs. For capital-exporting countries, tax treaties facilitate the foreign expansion of their own companies by relieving potential double taxation problems in foreign territories without risking improper tax evasion or fraud. Foreign investors benefit from taxation treaties because, even in cases in which there is no double taxation, tax treaties generally include greater and more comprehensive tax protections for investors than are available under the domestic tax rules of either host or home countries, which moreover can change at any time.<sup>55</sup> Furthermore, DTTs determine the maximum rates of taxation (particularly the withholding tax rates) that can be imposed by a host country, and a number of countries give preferential rates to firms in countries with whom they have DTTs. Capital-importing countries benefit because the extra tax protection afforded to foreign investors can be an added incentive for foreign investment in their territories, if other locational determinants for FDI are satisfactory. Furthermore, when DTTs contain tax-sparing provisions (whereby residence countries would grant double tax relief for the tax that would have been due in the host country were it not for a tax incentive offered to the investor), these can make some of the incentives offered by host countries more effective. And many DTTs

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<sup>49</sup> The various attempts at multilateral agreements thus far have had little success. Those that have been somewhat successful have been supplemented by bilateral treaties among the parties to the multilateral agreement. Karl P. Sauvant and Jorg Weber, eds., *International Investment Agreements: Key Issues* (New York and Geneva: United Nations, 2004), volume II, p.204.

Available at: [http://www.unctad.org/en/docs/iteiit200410v2\\_en.pdf](http://www.unctad.org/en/docs/iteiit200410v2_en.pdf).

<sup>50</sup> Treaty shopping is the routing of an investment and the associated income through a particular country in order to take advantage of treaty benefits intended for the residents of that country and its treaty partners.

<sup>51</sup> Sauvant and Weber, *op. cit.*, p. 203.

<sup>52</sup> Tsilly Dagan, “The tax treaties myth,” 32 *Journal of International Law and Politics* 939, at 979. (2000).

<sup>53</sup> Sauvant and Weber, *op. cit.*, p. 204.

<sup>54</sup> Allison Christians, “Tax treaties for investment and aid to Sub-Saharan Africa,” 71 *Brook. L. Rev.* 639 (2005), p. 658.

<sup>55</sup> Sauvant and Weber, *op. cit.*, p. 204.

include an exchange-of-information provision that allows the developing country to obtain information exchanged from capital-exporting countries, which can help developing countries tax capital invested by their rich residents overseas.

While DTTs may help developing countries attract more foreign investment, they also, *prima facie*, reduce the tax revenue of these countries. DTTs typically reduce source-based taxation (of the host country), thereby shifting tax revenues from the source country to the residence country, and most developing countries are net capital importers. As one author notes, though “the contraction of taxing jurisdiction is technically reciprocal in the treaty document, the one-sided flow of capital toward LDC [less-developed country] as source-country ensures that only that country experiences a true contraction of its taxing jurisdiction.”<sup>56</sup> The reduced tax revenues of developing countries can only pay off if DTTs do in fact lead to higher economic growth, for which more FDI flows may be integral.<sup>57</sup> Solely from a FDI attraction perspective, it appears that developing countries may therefore need to decide whether it is better for them to preserve their tax jurisdiction over foreign investors in order to maximize their tax revenue, or to agree to relieve source-country taxation in order hopefully to attract more FDI. In a recent article, Tsilly Dagan illustrated the conundrum and presented a game theory rationale that explains why many developing countries have opted for the latter.<sup>58</sup>

### C. The determinants of FDI flows

The issue examined in this volume is to what extent the expansion of the BIT and DTT networks has directly led to the rapid growth of FDI flows that occurred during the past decade or so. The principal difficulty for assessing the impact is that the existence of an investment or double taxation treaty is but one determinant that may affect decisions to invest abroad. Three sets of FDI determinants can be distinguished: the regulatory framework; investment promotion; and economic factors.

*The regulatory framework.* The number of BITs and DTTs concluded over the past couple of decades, and their pro-investor content, is reflective of the general movement of countries toward efforts to attract FDI by liberalizing their FDI regimes and creating national regulatory frameworks that are favorable for foreign investors. The regulatory framework of a host country is a key determinant for the location of foreign investment in so far as foreign investors simply cannot enter into, and operate in, a country if national laws prohibit or impede foreign investment. For over two decades, virtually all countries have been improving their investment climate by adopting national laws and regulations, including those that open more sectors to foreign investment, that facilitate inward FDI. Between 1991 and 2006, out of 2,533 national legal and regulatory changes relevant to foreign investment, 91% were in the direction of making the host country environment more favorable for FDI (Table 3). However, one should also note that, while the share of regulatory changes that are favorable to FDI remains high, the number of favorable changes has decreased significantly since 2004; in fact, the number of regulatory changes that are less favorable to FDI tripled between 2002 and 2006, perhaps signaling an increased skepticism in some countries of the benefits of FDI and a new tendency toward FDI protectionism.

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<sup>56</sup> Christians, *op. cit.*, p. 658.

<sup>57</sup> One should note in this context that, while FDI inflows contribute to economic growth, economic growth alone does not necessarily guarantee human development, the ultimate goal of countries.

<sup>58</sup> Dagan, *op. cit.*

Table 3. National regulatory changes, 1991-2006

Year	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	Total
Number of countries that introduced changes	35	43	56	49	63	66	76	60	65	70	71	72	82	103	93	93	
Number of regulatory changes	82	77	100	110	112	114	150	145	139	150	207	246	242	270	205	184	2,533
More favorable to FDI	80	77	99	108	106	98	134	136	130	147	193	234	218	234	164	147	2,305
Less favorable to FDI	2	0	1	2	6	16	16	9	9	3	14	12	24	36	41	37	228

Source: UNCTAD, *World Investment Report 1996: Investment, Trade and International Policy Arrangements* (New York and Geneva: UN, 1996), p. 132; UNCTAD, *World Investment Report 2007*, p. 14.

International investment agreements are part of the regulatory framework of a host country and can affect aspects of it directly. Most importantly, BITs establish certain standards of treatment that become parameters for national regulations in the investment area, and DTTs establish or clarify tax treatment for foreign investors. Investment agreements may also provide for the opening of certain sectors of the host country economy. Finally, if a country has concluded a BIT with the home country of an investor that grants investors from that home country certain enforceable rights, the investor typically has access to international arbitration.<sup>59</sup>

*Investment promotion.* In addition to liberalizing national policies concerning foreign investment, many countries facilitate foreign investment pro-actively. For this purpose, virtually every country has established an investment promotion agency to attract FDI and ease its operation. Among other things, these agencies offer incentives and various investment services, upgrade amenities for foreign investors, issue investors' guides, generally seek to improve the ease of doing business in its country, and may engage in policy advocacy.

*Economic factors.* While a country's regulatory framework must be enabling, and investment promotions can help, the locational decisions of MNEs ultimately depend on economic factors in prospective host countries. The economic determinants of FDI can be divided into three categories. *Locational resources and assets* include the quality of labor; the nature of the physical and institutional infrastructure; the availability of natural resources; and the technology system and the domestic enterprise base. *Market variables* include economic growth and per capita income, the size of the host country market for goods and services, access to regional and global markets, country-specific consumer preferences, and the structure of the host country market. *Efficiency* considerations include the cost of resources and other inputs such as transport and communication costs and membership in a regional integration agreement. It is on the basis of these economic factors that the business case for an investment is made. Moreover, these economic variables also have to be seen in the broader framework of a number of macro factors, such as the performance of the world economy, and a number of social and political factors, including the policy approach to private business in general.

It is clear, then, that no individual factor, such as an investment treaty, could move FDI flows by itself, and it is equally clear that it is very difficult to isolate the importance of any particular factor. To put it differently: if BITs and DTTs affect FDI flows, they do so in the context of a host of other determinants, with a number of them considerably more important than individual aspects of the regulatory framework. In general, the regulatory framework of a host country is at best enabling; once it is permissive, the economic determinants become key, especially market

<sup>59</sup> Some investment insurance programs require (technical) investment agreements between home and host countries in order for investors to obtain political risk insurance; such insurance programs normally require that the host country consents to arbitration in case of investor disputes. World Bank, *World Development Report 2005: A Better Investment Climate for Everyone* (Washington: World Bank, 2005), at 177. Available at: [http://siteresources.worldbank.org/INTWDR2005/Resources/complete\\_report.pdf](http://siteresources.worldbank.org/INTWDR2005/Resources/complete_report.pdf); see also Jason Yackee, "Conceptual difficulties in the empirical study of bilateral investment treaties," University of Wisconsin Law School Legal Studies Research Paper Series, Paper No. 1053 (October 2007), p. 48. Available at: <http://ssrn.com/abstract=1015088>

size and growth, skills, resources, and costs. While the economic determinants are not everything, everything is nothing when it comes to attracting FDI.

In this context, then, BITs and DTTs can help improve the regulatory framework by complementing host-country policies related to FDI, guaranteeing certain investor rights, making the legal and tax frameworks more transparent and stable for investors, and mitigating the potential impacts of political or economic instability by establishing certain enforcement procedures. If BITs and DTTs help improve the regulatory determinants for FDI, they then allow the key economic determinants—if present—to prevail. Despite difficulties with respect to identifying the specific impact of treaties on investment flows (given the wide range of other variables that need to be considered), as well as cause and effect relationships between the existence of BITs and DTTs and FDI flows, a number of scholars have attempted to assess the impact of such agreements on FDI flows. The following sections highlight the findings of the principal studies undertaken during the ten-year period from 1998 to 2007 and reproduced in this volume.

#### **D. BITs and FDI flows**

Given the principal purpose of BITs—to protect investment and hence encourage investment flows—it is only natural that the question has been raised whether they do, in fact, lead to higher investment flows. Jeswald Salacuse and Nicholas Sullivan (Chapter 5) and Tim Buthe and Helen Milner (Chapter 6) both determined that concluding BITs does have a positive effect on FDI inflows and that the effect is larger when developing countries conclude these agreements with economically more important countries. Analyzing the impact of BITs with OECD countries on aggregate FDI inflows to 100 developing countries, Salacuse and Sullivan found that, when developing countries concluded BITs with OECD countries, FDI inflows were likely to increase. Furthermore, they determined that a U.S. BIT was likely to have more of an impact than other OECD BITs in promoting overall FDI, and that a U.S. BIT was likely to promote U.S. FDI as well. Similarly, Eric Neumayer and Laura Spess (Chapter 7), looking at 119 developing countries between 1970 and 2001, found that developing countries that signed more BITs with developed countries that were major source countries of FDI received a higher share of FDI flowing to developing countries.

Most authors agree that the strength of the impact of BITs on FDI inflows depends on several political, regulatory and economic factors, both within the host country and globally. For instance, Neumayer and Spess found that countries with faster-growing economies and larger populations receive more FDI. Moreover, they suggested that BITs may in fact function as substitutes for poor host country institutional quality. Precisely because political risk and volatility are constraints on FDI inflows, Neumayer and Spess suggested that countries “with particularly poor domestic institutional quality possibly stand the most to gain from BITs,” and that the positive effect of BITs on FDI decreases as governments become more stable. In fact, it is possible that merely signing a BIT, before implementation actually occurs, has a positive signaling effect, as Peter Egger and Michael Pfaffermayr’s analysis of outward FDI stock from OECD countries (Chapter 8) suggested, though they did find that BITs that have entered into force have a stronger positive effect on outward FDI stock than those that have merely been signed. Buthe and Milner developed a theoretical argument that explains an increase in overall inward FDI flows as a function of the success of BITs as a political commitment by developing countries to economically liberal policies, which foreign direct investors generally seek, at least in developing countries. Investors consider these commitments to be more credible because BITs signal such commitments and governments’ compliance with them and, in addition, make breaking such commitments more costly.

Several analysts have also found that the sheer number of BITs signed by a country influences FDI inflows. Neumayer and Spess found that countries with a higher cumulative number of BITs receive more FDI inflows. Robert Grosse and Len Trevino (Chapter 9) and Kevin Gallagher and Melissa Birch (Chapter 10) also found a strong positive relationship between the total numbers of BITs concluded by a country and FDI inflows to that country in studies that focused on Central and Eastern Europe and Latin America, respectively.<sup>60</sup> Susan Rose-Ackerman (Chapter 11) took a global view, finding that, as the total worldwide coverage of BITs goes up, overall FDI flows to developing countries may increase, though the marginal benefit to any one country of signing BITs will decrease. Unlike Neumayer and Spess, Rose-Ackerman found that “the marginal impact of BITs is greater in countries that already have relatively effective legal regimes and favorable economic environments.”

Not all empirical studies shed such a favorable light on BITs’ impact on FDI inflows. Several scholars determined that BIT protections cannot substitute or compensate for the economic and regulatory risks of a host country; to the extent that such treaties affect FDI flows, they do so as one of a host of other regulatory and economic determinants that impact FDI. A 1998 UNCTAD study (Chapter 12), one of the first to evaluate the impact of BITs on FDI flows, concluded that, on balance, BITs did not play a primary role in increasing FDI, and that a larger number of BITs ratified by a host country would not necessarily lead to higher FDI inflows. In another early study, Mary Hallward-Driemeier (Chapter 13) analyzed the bilateral flow of FDI from 20 OECD countries to 31 developing countries from 1980 to 2000 and noted that BITs had an insignificant effect on FDI flows. However, she also found that, rather than encouraging more FDI flows in riskier environments, BITs only have a positive effect on FDI flows in countries with an already stable business environment and reasonably strong domestic institutions. If a country signs a BIT while undertaking domestic regulatory reforms that facilitate FDI, it would be the institutional reforms and liberalization that may affect investors’ locational decisions rather than simply the BIT itself. Hallward-Dreimer’s results suggested that the size of a host country’s market is a more conclusive determinant of FDI flows than the conclusion of a BIT. Jason Yackee (Chapter 14) also found little evidence that BITs have any effect on FDI flows.<sup>61</sup> Emma Aisbett’s study (Chapter 15) demonstrated the importance of accounting for the endogeneity of BIT adoption when assessing the impact on FDI flows. She suggested that the relevance of BITs may vary by sector or that there may be reverse causality, where a higher growth rate of FDI leads to an

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<sup>60</sup> In a 2008 study, Len Trevino, Douglas Thomas and John Cullen also find BITs to be “significant indicators of inward FDI in Latin America.” They argue that institutionalization is a process that can legitimize a host FDI market for foreign investors through three (cognitive, normative and regulative) pillars. They found that while BITs work through the regulative framework, the “signals BITs send through the cognitive and normative pillars are more dominant than those sent through the regulative pillar,” and that in general, “institutional processes that legitimize [a host country FDI market] through the cognitive and normative pillars... are better indicators of inward FDI than those that legitimize primarily through the regulative pillar [such as trade or tax reform].” Trevino, Len J., Thomas, Douglas E., and Cullen, J., “The three pillars of institutional theory and FDI in Latin America: An Institutionalization Process,” 17 *International Business Review* 118 (2008).

<sup>61</sup> In a recent paper, Peter Buckley et al. tested the effect of various supranational institutional factors, including BITs, on the decision-making of Chinese MNEs from 1991 to 2003, and found no significant relationship between Chinese outward FDI patterns and the conclusion of a BIT with China; they also did not find a signaling effect of the total number of BITs concluded by a country. (It should be noted in this context that the protection offered by Chinese BITs is not as strong as that of treaties of other countries.) See Peter Buckley et al., “Explaining China’s outward FDI: an institutional perspective,” in Karl P. Sauvant, with Kristin Mendoza and Irmak Ince (eds.), *The Rise of Transnational Corporations from Emerging Markets: Threat or Opportunity?* (Cheltenham: Edward Elgar, 2008).

increased probability of a BIT being negotiated. Deborah Swenson (Chapter 16) also found that countries were more likely to sign BITs if they already had high levels of FDI, suggesting that “the interest of existing foreign investors drove the signing of BITs, at least in part”; but she maintained that signing these BITs may have helped these countries retain existing levels of FDI. She also emphasized the importance of controlling for timing, intrinsic country attractiveness and investor identity in analyses of BIT effectiveness. She found that, controlling for these variables, data from the late 1990s suggest that BIT signing did help developing countries attract more FDI.

Taken together, these analyses suggest that it is difficult to establish firmly the effect of BITs on FDI flows. Intuitively, one would expect that such treaties, by providing a sort of good housekeeping seal of approval, have a positive effect on FDI flows as they signal that a country is interested in attracting such investment and that it provides certain guarantees under international law to protect it (thereby reducing the risk premium of an investment); and this signal is not only sent to a particular treaty partner but to the international investment community as a whole. The incidence of treaty shopping—whereby a firm invests in another country not from its home country but via a country that has a BIT with the prospective host country—also suggests that at least some firms deliberately seek the protection of a treaty. The rise in international arbitral cases shows, furthermore, that investors pursue their rights if they feel aggrieved. Moreover, if BITs not only protect investments but also liberalize entry and operations, one would expect a rise of inflows, assuming attractive investment opportunities.

So why the different findings in the chapters included in this volume (methodological issues aside)? To begin with, most of the bilateral FDI stock and flow data are poor. Where they exist, moreover, the nature of FDI may play a role: the effect of BITs on investors’ locational decisions is likely weaker for natural resource and market-seeking investors for whom the economic determinants of FDI are clear, whereas such treaties might more likely influence the decision-making of efficiency-seeking investors for whom several investment locations may be otherwise equally attractive. But FDI data mostly do not allow one to distinguish clearly between these various types of FDI. Difficulties exist also in disentangling the causal effects from BITs on FDI flows from the causal effects of a simultaneous and autonomous liberalization of the national FDI regulatory framework—a trend, as shown, that is strong and pervasive. The level of development of the BITs partners—for instance whether BITs are signed between developed and developing countries or between developing countries, or whether the developing country is more or less developed—may also play a role. More generally, BITs may be relatively more influential in certain countries or contexts than in others, depending on the type of investments common to a country or the mix of other—more crucial—FDI determinants. The magnitude of the correlation between BITs and FDI, then, may vary for various countries and regions for reasons that are not captured or explored in the studies. Furthermore, the effect of BITs may change over time, for instance as the worldwide coverage of BITs continues to grow and as more or less all important countries conclude BITs with each other, the ability of these treaties to influence locational choices may even out.

The diverse findings in the literature may also reflect variations in the provisions of BITs. For example, most regression analyses look at whether or not BITs were in place, without factoring in the varying degrees of investor protections and benefits in these treaties<sup>62</sup>, for example, as regards the breadth of arbitration rights or the primacy of BIT rights over national law. Another variation that could account for disparities in the studies is that BITs that include *liberalizing* provisions in addition to investor protection provisions (especially BITs with the United States, Canada, and

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<sup>62</sup> Franck, *supra* note 33; Deborah L. Swenson, “Why do developing countries sign BITs?,” 12 U.C. Davis J. Int’l L. & Pol’y 131, at 153 (2005).

Japan) can influence FDI flows by opening sectors previously closed to foreign investment; assuming the economic determinants are right, it would not be surprising for “liberalizing” BITs to lead to more FDI. This could perhaps explain the different findings for countries that have concluded BITs with the United States as opposed to other OECD countries.

The specific BIT effect can be further complicated if a BIT country enters, more or less simultaneously, bilateral or regional free trade and investment agreements: these latter agreements could have a similar “opening” effect for FDI and/or they could lead (via trade liberalization) to a larger market,<sup>63</sup> with both effects potentially leading to an increase in FDI flows. Moreover, when the effect on FDI flows of BIT countries is compared with that of non-BIT countries, the comparison is complicated if the latter are covered by bilateral, regional or multilateral agreements with substantial investment provisions, blurring the distinction between these two groups of countries.<sup>64</sup> Put simply, countries have multiple tools for protecting foreign investments and the interests of foreign investors in addition to BITs, so a more comprehensive study would need to account for alternative investment promotion and protection measures in addition to BITs.<sup>65</sup>

Crucial, however, is the importance of the economic factors—and BITs do not directly influence them. Unless, as pointed out earlier, they are favorable, FDI typically does not take place; and when they are favorable, and especially when they are strongly favorable, FDI can also take place in the absence of BITs. Since the economic factors trump virtually all other factors (assuming FDI is permitted), any study that seeks to isolate the specific BITs effect on FDI flows needs to include economic variables fully in its calculation.

Considering the complex relationship between investment treaties and the various variables of the three sets of FDI determinants, it is not surprising that it is difficult to establish firmly the effect of BITs on FDI flows. It fits into this picture that, in a June 2007 survey of 602 senior executives of MNEs around the world, roughly one-fifth of the recipients indicated that the existence of international investment agreements influenced their locational decisions “to a very great extent”<sup>66</sup> while an equal share said that such agreements influenced their decisions “not at all.” At the same time, roughly half of the respondents indicated that IIAs influenced locational decisions “to a limited extent,” suggesting that other factors needed to be present (Figure 13). A World Bank report also noted that there is evidence that many investors may not be aware of existing BITs when they make locational decisions, and may in fact “remain oblivious until some issue arises when its provisions may be relevant.”<sup>67</sup>

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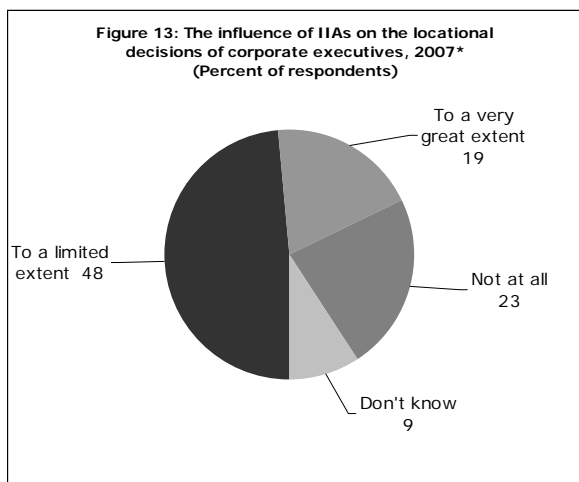
<sup>63</sup> For example, a World Bank study found that regional agreements that create larger markets positively affect FDI inflows when other institutional variables affecting the investment climate are satisfactory (though agreements that do not result in larger markets do not positively affect FDI flows). Richard Newfarmer, “Beyond merchandise trade: services, investment, intellectual property, and labor mobility,” in *Global Economic Prospects 97*, at 109 (2005), available at <http://siteresources.worldbank.org/INTGEP2005/Resources/gep2005.pdf>

<sup>64</sup> For example, many developing countries are covered by the GATS—and FDI in services to developing countries accounts for more than half of all FDI flows to these countries.

<sup>65</sup> Swenson, *op. cit.*, p. 153.

<sup>66</sup> One could question, however, whether some of the senior executives who answered that IIAs influenced their locational decision making “to a great extent” may have strategically over-stated the importance of IIAs in their decision making in order to encourage the granting of such further protections IIAs may offer them.

<sup>67</sup> World Bank (2005) *World Development Report 2005*, *op. cit.*, p. 177.



\* The question in the EIU survey was: “To what extent does the existence of an international investment agreement (for example, a bilateral investment treaty) influence your company’s decision on which markets to invest in?”

Source: Matthew Shrinkman, “The investors’ view: economic opportunities versus political risks in 2007-11,” in Kekic and Sauvart, *op. cit.*, p. 96.

## E. DTTs and FDI flows

There are considerably fewer studies of the impact of DTTs on FDI flows than there are of the effect of BITs. On the one hand, this may not be surprising since one of the declared principal objectives of BITs is to promote FDI flows, and this objective invites a test whether it is indeed achieved; in addition, BITs are politically more sensitive because they directly influence the regulatory space of host countries across a range of important policy areas. On the other hand, DTTs (highly technical treaties) should be important for the locational decision of firms as they can directly affect the “bottom line” of a company’s performance. Moreover, the incidence of DTT treaty shopping suggests that they influence the routing of investment flows. A well-known example is the fact that a good part of FDI into India is routed through Mauritius, as the latter has a more favorable DTT with India than those concluded between India and the original residence countries of investors.<sup>68</sup>

In any event, most of the difficulties that afflict the analysis of the impact of BITs on FDI flows also are relevant to the impact of DTTs on FDI flows and hence need not be rehearsed. Indeed, most empirical studies have generally found that DTTs entered into since the early 1980s have not had a demonstrable impact on investment flows. The analysis by Bruce Blonigen and Ronald Davies (Chapter 17) of the impact of bilateral tax treaties on FDI activity in OECD countries from 1982 to 1992 found that DTTs are associated with larger FDI stocks and flows. However, when older DTTs concluded many years before the period of their study are distinguished from newer DTTs entered into during their observed time period, they found that the newer treaties had no positive effect on FDI activity. In a subsequent study, Blonigen and Davies (Chapter 18)

<sup>68</sup> In *Union of India and Anr vs. Azadi Bachao Andolan and Anr* (Oct. 7, 2003), the Supreme Court of India held that tax treaty shopping was valid under the Indo-Mauritius tax treaty. In part of its decision, the Supreme Court emphasized that tax treaty shopping could positively attract more FDI to India (“In recent years, India has been the beneficiary of significant funds through the ‘Mauritius conduit.’”) Eduardo Baistrocchi, “The structure of the asymmetric tax treaty network: theory and implications,” Bepress Legal Series, Working Paper 1991 (2007).

investigated U.S. FDI flows from 1980 to 1999 and found that DTTs concluded by the United States during this period had no significant effect on inward and outbound FDI.<sup>69</sup> In fact, Blonigen and Davies concluded that recent DTTs have had negative effects on OECD outbound FDI flows, which they suggested could be a consequence of the elimination of tax avoidance opportunities in DTTs. Peter Egger et al. (Chapter 19) also found a negative effect of newly implemented DTTs on outward FDI stock from OECD countries when analyzing FDI data two years prior and two years after DTT conclusions from 1985 to 2000.

A couple of the studies focus on the relative importance of tax treaties to the locational decision-making of MNEs. Henry Louie and Donald Rousslang (Chapter 20) investigated how both the quality of host-country governance and having a bilateral income tax treaty with the United States affect the rates of return that U.S. companies expect from their foreign investment. They found that poor governance causes U.S. companies to require significantly higher rates of return, thereby discouraging inward FDI, and that, after accounting for the quality of host-country governance, a tax treaty does not have an effect on the required rates of return. Similarly, Allison Christians (Chapter 21) used a case study of a hypothetical tax treaty between Ghana and the United States to demonstrate that a typical tax treaty with a low-income developing country does “not provide major tax benefits to the private sector [so] even if concluded, these treaties would not have a significant impact on cross-border investment and trade.”

Some of the studies in this volume arrive at more guarded conclusions about the impact of DTTs on FDI flows. Daniel Millimet and Abdullah Kumas (Chapter 22) determined that assumptions in previous studies concerning the timing of the effect of tax treaties are important, finding that allowing for anticipatory and lagged effects of treaty formation indicates a more substantial, positive effect on FDI activity. Eric Neumayer (Chapter 23) found that developing countries that have signed more DTTs with major capital exporting developed countries are, in fact, likely to have received more FDI in return. However, his results showed that DTTs are only effective in middle-income developing countries, not in low-income developing countries, a qualification supported by Christians’ study.

Apart from the difficulties already reviewed in the context of BITs, there are several possible specific explanations for why double taxation treaties may not lead to higher FDI flows. For instance, as with many provisions in BITs, several of the tax alleviation provisions in tax treaties that are expected to encourage FDI flows can also be implemented unilaterally through the domestic policies of host governments,<sup>70</sup> so countries with DTTs may not provide a significantly different tax framework than countries without such treaties. Another possibility is that, while DTTs largely address the problem of double taxation, they also reduce opportunities for tax evasion by foreign investors, which may even act as a disincentive for FDI. Another rationale advanced by some of the literature is that DTTs limit the tax revenue of host countries, thereby reducing the governmental resources to construct the infrastructure necessary to attract and support FDI in the first place.<sup>71</sup> More broadly, the existence and widespread use of tax havens, the

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<sup>69</sup> The aforementioned paper by Buckley et al. on factors affecting the decision-making of Chinese MNEs from 1991 to 2003 similarly found no significant relationship between Chinese outward FDI patterns and the conclusion of a DTT with China; they also did not find a signaling effect of the total number of DTTs concluded by a country. Buckley et al., “Explaining China’s outward FDI: an institutional perspective,” in Sauvant, with Mendoza and Ince (eds.), *op. cit.*

<sup>70</sup> For instance, most countries implement the foreign tax credit or exemption of foreign source income unilaterally. For a discussion of unilateral policies to relieve double taxation and how they compare to tax treaty provisions see Dagan, *op. cit.*

<sup>71</sup> See, e.g., Buckley et al., “Explaining China’s outward FDI: an institutional perspective,” in Sauvant, with Mendoza and Ince (eds.), *op. cit.*

possibility of allocating various charges across the affiliates of a corporate system and the use of transfer pricing may provide alternatives to DTTs for firms seeking to minimize their tax burden.

#### **F. BITs, DTTs and FDI flows**

A potential omitted variable in all of the above studies, including the studies of the effect of BITs on FDI, is that each study focuses either on BITs or on DTTs but not on both, and none of the studies include a variable for the presence of the other type of treaty. Tom Coupé, Irina Orlova, and Alexandre Skiba's study (Chapter 24) showed that the correlation between the two types of treaties is statistically significant. They estimated the effect of both BITs and DTTs on FDI flows from seventeen OECD countries into nine economies in transition, focusing on such economies to increase the homogeneity of their sample and because available data provide them with a good proxy for a wide range of home policies that may influence their results. Their results showed that transition economies that have BITs with developed countries receive more FDI inflows from those countries, but that tax treaties do not have a significant effect on FDI inflows. Their results also suggested that BITs are substitutes for institutional quality as the net effect of a BIT is smaller (but still positive) if the quality of a host country's institutions is higher.

#### **Conclusions**

One uncontroversial truth is that virtually all countries value FDI as a means to advance their economic development. Therefore, not surprisingly, they compete with each other to attract investment. This competition for FDI has spawned literally thousands of international investment agreements intended to protect—and hence attract—investors, and, more generally, create a favorable investment climate. BITs and DTTs are a central part of this process as they are seen to enhance the locational advantages of countries by enshrining certain approaches to the treatment of foreign investors in international treaties, thereby improving the regulatory environment for investment. Even in the absence of conclusive evidence as to the effect of BITs and DTTs on FDI flows, countries continue to conclude these agreements, and the number of such treaties continues to grow. Governments could be signing these treaties because, as more countries conclude more and more of these agreements, they could be afraid that investors may avoid investing in countries that have *not* signed such treaties—so countries (especially developing countries) may feel they need to sign these agreements to stay competitive, or at least “to appear enlightened or receptive to modern international law trends.”<sup>72</sup> UNCTAD has suggested that, in some cases, foreign investors with existing investments have encouraged their home country governments—or the host country governments—to conclude BITs to protect existing investments; this means that studies that find that BITs did not stimulate FDI flows might overlook that BITs positively affect FDI flows by helping host countries to retain existing levels of FDI.<sup>73</sup>

It is also possible that governments, even if they are not entirely sure whether BITs and DTTs lead to higher FDI flows, think that these treaties do not hurt such flows and, in any event, can serve other purposes—although there are trade-offs in terms of accepting international disciplines, with the corresponding reduction of national policy space. For example, some governments may want to use the commitments they have entered into in these treaties to advance domestic policy reforms. Conversely, governments could also be signing these agreements to signal to investors that they are prepared to bind their improved national policy frameworks and the regulatory changes that favor FDI in international agreements that cannot be changed unilaterally. This may be particularly important for countries that are politically or economically

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<sup>72</sup> Ginsburg, *op. cit.*, p. 117.

<sup>73</sup> UNCTAD, *Bilateral Investment Treaties in the Mid-1990s* (New York: United Nations, 1998), p. 142.

instable, or countries with high levels of corruption, as “investors may be especially concerned about the permanence or strength of domestic reforms implemented in [such] countries.”<sup>74</sup> In that case, BITs and DTTs “may be the result of policy changes rather than the embodiment of them,” which is supported by the fact that, simultaneously with the adoption of these bilateral treaties, countries “were also adopting internal regulatory changes that made foreign investment more liberal.”<sup>75</sup>

Finally, governments that would want to strengthen the positive effects of especially BITs on FDI flows could go beyond relying on the indirect effects that are thought to be associated with better protection. They could do this by stipulating in BITs various measures that home countries could take to increase FDI flows to developing countries. Such measures could include, for example, various fiscal and financial incentives that home countries could grant to their firms if they invest in developing countries (and especially the least developed among them); technical assistance to build investment promotion capacities; information about investment opportunities; and improved market access. Such commitments, in fact, could also extend to efforts to enhance the benefits of FDI to host countries and their economic growth and development, for example, through the promotion of technology transfer and the creation of more linkages between foreign affiliates and domestic firms.<sup>76</sup> The negotiation of new BITs and the renegotiation of BITs underway may offer opportunities to do so.

Aside from the specific motivation for or impact of these investment agreements, there is another effect of the proliferation of BITs: they strengthen the rule of law in the sphere of international investment and hence contribute to the emergence of international investment law. This is not to suggest that the network of BITs constitutes, in and of itself, a coherent international investment law system. But the fact that the great majority of countries subscribe to a range of standards that are similar in nature and that these standards are being clarified and refined through practice, may indicate that a number of the building blocks for such a system are being put in place. As international investment rule-making involves the great majority of countries,<sup>77</sup> is a dynamic process and proceeds at a rapid pace, all countries have the opportunity to participate actively in designing the international investment law system and to seek to influence it in a manner that ensures that their interests are taken into account.

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<sup>74</sup> Swenson, *op. cit.*, p. 133.

<sup>75</sup> Ginsburg, *op. cit.*, p. 117.

<sup>76</sup> See UNCTAD, *Investment Promotion Provisions in International Investment Agreements* (Geneva: United Nations, forthcoming).

<sup>77</sup> Important in this context is that, in contrast to earlier periods, emerging markets participate actively in this process. By the end of 2006, developing countries alone were signatories to 77% of all BITs, 61% of all DTTs, and 81% of all other international investment agreements, and a number of these involve only developing countries. See UNCTAD, *World Investment Report 2007: Transnational Corporations, Extractive Industries and Development* (New York and Geneva: United Nations, 2007), p. 17.