INVESTMENT RULE MAKING AND GOOD GOVERNANCE IN INTERNATIONAL INVESTMENT ARBITRATION

Dr. Rosmy Joan[*]

ABSTRACT

This paper is about the role of the State in investment rule making, balancing the investor rights and the regulatory autonomy of the States, and thereby evolving good governance standards. This paper explores into how States could better define their treaty obligations, preserve more efficiently their sovereign prerogatives and ensure an appropriate level of accountability and responsibility of multinational companies. This paper argues that States shall be given an opportunity to resolve the issues at the domestic level to better reflect the values of good governance preceding the international investment arbitration. This paper also argues that States should be afforded with sufficient degree of regulatory flexibility to ensure good governance in pursuing policy objectives while they are expected to comply with good governance standards in their treatment of foreign investors. This paper views the model bilateral investment treaty as a powerful tool in the hands of the States to frame investment rules with clarity and certainty for good governance. This paper concludes that the Indian Model Bilateral Investment Treaty 2016 reflects the Indian style of investment rule making, for good governance balancing investor rights and the regulatory autonomy of the host State.

[*] Assistant Professor of Law, National Law University, Jodhpur (rosmyjoan@gmail.com)

1. INTRODUCTION

The question of how to balance the regulatory powers of the State with the rights of the individual in international investment dispute settlement is very pertinent for States to make good investment relations. There is still a long way to the development of a general theory, which reconciles the opposing positions of the State and the individual.[1] Host States are to be given space to pursue their sovereign policies, but they are expected to make good use of this space.[2] International investment treaties gradually come to be interpreted as requiring host States to maintain good governance standards in their dealings with foreign investors. Good governance implied firstly non-arbitrary and non-personalistic decisions by the State or consistent, predictable and stable policies. Good governance meant accountability of the State to the society. Lack of transparency, stability, predictability as well as the lack of effective remedies and enforcement mechanisms at a national level can now lead to a host State's liability in damages.[3]

Historically references to good governance, the rule of law and transformation of legal and bureaucratic culture in host States were sporadic and made predominantly in the context of justifications for the foreign investor's right to claim monetary damages directly against host States. Since its inception in early international investment treaties, the

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[1] Andreas Kulick, *Sneaking though the Back Door-Reflections on Public Interest in International Investment Arbitration*, 29 (3) ARBITRATION INT'L 435-51 (2013).
[2] Krista N. Schefer, *State Powers and Investor-State Dispute Settlement*, *in* THE ROLE OF THE STATE IN INVESTOR STATE ARBITRATION 19 (Shaheeza Lalani & Rodrigo Polanco Lazo eds., 2015).
[3] Mavluda Sattorova, *The Impact of Investment Treaty Law on Host States Behaviour Some Doctrinal, Empirical and Interdisciplinary Insights*, *in* THE ROLE OF THE STATE IN INVESTOR STATE ARBITRATION 162 (Shaheeza Lalani & Rodrigo Polanco Lazo eds., 2015).

private right to damages has been justified by reference to broader objectives of the international investment regime.[4]

A string of arbitral awards including *Metalclad*, *Tecmed*, and *Occidental* awards proclaimed that transparency, stability predictability, consistency ought to be construes as elements of Fair and Equitable Treatment (FET). A failure to create and maintain a transparent, stable and predictable regime was found to be a sufficient ground for claiming compensation against the host State. Beyond arbitral jurisprudence there are also treaties that contain a host State obligation to create and maintain in its territory a legal framework apt to guarantee to investors the continuity of legal treatment.[5] Such provisions advance a programme of good governance that no State in the world is capable of guaranteeing at all times.[6]

This paper examines the issues pertaining to governmental regulation and investor rights in ISDS and analyses the role of the State in investment rule making balancing the investor rights and the regulatory autonomy of the States for good governance.

2. THE BACKGROUND

All States seek to attract foreign direct investment for economic development. For this purpose, governments have liberalized their national regulatory frameworks for foreign investment and have also established investment promotion agencies to attract foreign direct investment actively. Corporations, which are simultaneously vital instruments for

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[4] Alan O. Sykes, *Public versus Private Enforcement of International Economic Law: Standing and Remedy*, 34(2) J. LEGAL STUDIES 631 (2005).
[5] Bilateral Investment Treaty, It.-Jordan, art. 2(4), July 21, 1996,
[6] El Paso Energy Int'l Co. v. Arg., ICSID Case No. ARB/03/15, Award, ¶ 342 (Oct. 31, 2011), IIC 519 (2011).

achieving national economic goals as well as actors seeking to maximize their own profits for their more restricted universes of shareholders, also appreciate that, in pursuit of resources and markets, they must operate globally. Fulfilling the capital needs for economic development through foreign investment enlarges the boundary of dispute settlement beyond the local limits of the State as the State deals not only with its institutions or nationals but also with the nationals of other States.[7] The past two decades witnessed a rapid development of the international investment treaty regime and its mechanism of dispute settlement. It is expected that the international investment treaty regime will continue to develop in the future with the rise in economic relationships between States. However the growing number of investor claims against sovereign states challenging a wide array of public policy decisions and regulatory measures[8] has evoked deep concerns about the potential costs associated with such treaties and calls for ISDS reform.[9]

Every legal arrangement, whether substantive or procedural, is always under some pressure for change to meet new situations of fact. For examining how far the existing pattern of factual relationships in the matter of foreign investment is regulated by accepted and acceptable rules of law, Lord Shawcross relies on the saying that "law is a reflection of fact—that it represents a fixed and predictable adjustment of the various

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[7] *See* E. I. Nwogugu, *Legal Problems of Foreign Investments*, 153 RECUEIL DES COURS 177 (1976-V).

[8] *See* Metalclad Corp. v. Mexico, ICSID Case No. ARB(AF)/97/1, Award, ¶¶ 92-93 (Aug. 30, 2000), IIC 161 (2000); Renco Group, Inc. v. Peru, ICSID Case No. UNCT/13/1; S.D. Myers, Inc. v. Can., UNCITRAL, Partial Award, ¶ 134 (Nov. 13, 2000), IIC 249 (2000); Saluka Inv. BV v. Czech, PCA, Partial Award, ¶ 290 (Mar. 17, 2006), ICGJ 368 (PCA 2006); CMS Gas Transmission Co. v. Arg., ICSID Case No. ARB/01/8, Award, ¶¶ 282- 284 (Apr. 25, 2005), IIC 65 (2005); Eureko B.V. v. Pol., UNCITRAL, Partial Award, ¶ 233 (Aug. 19, 2005), IIC 98 (2005).

[9] Lauge S. Poulsen & Emma Aisbett, *When the Claim Hits: Bilateral Investment Treaties and Bounded Rational Learning*, 65 (2) WORLD POL. 273-313, 274 (2013).

and sometimes conflicting interests which arise from any given relationship".[10] Lord Shawcross further observes that:

> *The impact of these facts upon the traditional rule is not, be it noted, the simple one that the old rule has gone: it is rather that States have felt obliged to review their relations with one another in this matter, sometimes on a bilateral, sometimes on a multilateral basis, for the purpose of adjusting the old law to the new factual situations.*[11]

Therefore the international investment law must accommodate and manage the convergence of different interests in the International Investment Agreements. Otherwise the respondent States who lost the claims will lose their faith in investment arbitration and this will result in backlash. The recent trends are showing that States like Brazil, India, South Africa, Bolivia, Ecuador, Venezuela and Indonesia are significantly changing their approach to investment rule making, with a lot of policy innovations.[12] It is in this context, this paper examines the investment rule making and good governance in international investment arbitration.

3. THE INVESTMENT RULE MAKING AND GOOD GOVERNANCE

Investment protection treaties, with their investor State dispute settlement provision are or at least could be instruments to promote good governance. Indirectly they promote regulatory foreseeability by increasing the transparency of laws- in their existence, creation, and

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[10] *See* The Rt. Hon. Lord Shawcross QC, *The Problems of Foreign Investment in International Law*, 102 RECUEIL DES COURS 335 (1961).
[11] *Id*., at 340.
[12] *See generally* Cooperation and Facilitation Investment Agreements instead of ISDS in Brazil; Indian Model BIT 2016; South African Domestic Bill relying on Mediation instead of investment arbitration and so on.

application they ensure that governmental agents can be held accountable for violations of legal norms through the imposition of compensation where the investor can prove harmful effects stemming from the State's unlawful or unfair behaviour; and they may broaden participation in international governance by allowing natural and legal persons to bring an action directly against a government on the international level.[13]

Several States have criticized or expressed dissatisfaction with the current regime of the protection of foreign investment. They believe that investment treaties often require the surrender of important sovereign prerogatives and unacceptable limitations on regulatory powers.[14] From the host State's point of view, this is an encroachment on State sovereignty.[15] The host State mandate to compensate foreign investors while regulating for public interest would deter the States to act for public welfare in the future and they may give undue weightage to investor concerns over public interest.[16] For example in *Tecnicas Medioambientales Tecmed, S.A. v. United Mexican States* the tribunal found breach of Fair and Equitable Treatment for refusing the license renewal regarding the operation of a hazardous waste landfill.[17] Therefore

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[13] Schefer, *supra* note 2.

[14] MICHAEL WAIBEL ET AL. EDS., THE BACKLASH AGAINST INVESTMENT ARBITRATION (2010). *See* Part IV.

[15] Christopher Ryan, *Meeting Expectations: Assessing the Long-Term Legitimacy and Stability of International Investment Law*, 29 U. PA. J. INT'L L. 725, 729 (2008).

[16] Following the Fukushima disaster in Japan in 2011, the German government took the decision to phase out nuclear energy by 2022. Vattenfall, a Swedish company which had made substantial investments in the German nuclear sector, started legal proceedings against Germany, asking – according to media reports - for €4.7bn worth of compensation since they would be unable to capitalise on their investment. In 2011, tobacco company Philip Morris against Australia for introducing plain packaging laws on cigarette packets initiated investment treaty arbitration at the Permanent Court of Arbitration (PCA) in The Hague.

[17] Tecnicas Medioambientales Tecmed S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, ¶ 154 (May 29, 2003); Charles N. Brower & Stephan W. Schill,

the limitation of private arbitration to address public issues was identified.[18]

The real problem lies with the establishment of the limits within which the host State is entitled to exercise its inherent sovereign powers over foreign investors. These limits are set *inter alia* by international treaties binding the host State. It is certainly true that the overwhelming majority of these treaties are manifestly unbalanced. It is therefore important for the parties negotiating an investment treaty to define, as clearly as possible, the limits of their own benefit as well as for the benefit of the respective foreign investors.[19] They are essentially about the legal relationship between the host State and the foreign investor but as a rule impose obligations exclusively upon host States.[20] Not surprisingly in the arbitral proceedings that they generate, the host State is systematically the respondent in investment arbitration.[21] This is not inherent in these treaties; it is a deliberate choice of the contracting parties.[22] This part of the paper look into how States could better define their treaty obligations, preserve more efficiently their sovereign prerogatives and ensure an

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Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?, 9 CHI. J. INT'L L. 471, 474 (2009).

[18] Christopher Ryan, *Meeting Expectations: Assessing the Long-Term Legitimacy and Stability of International Investment Law,* 29 U. PA. J. INT'L L. 725, 740 (2008).

[19] Tarcisio Gazzini, *States and Foreign Investment A Law of the Treaties Perspective*, *in* THE ROLE OF THE STATE IN INVESTOR STATE ARBITRATION 29 (Shaheeza Lalani & Rodrigo P. Lazo eds., 2015).

[20] *Id.*, at 23.

[21] Mehmet Toral & Thomas Schultz, *The State A Perpetual Respondent In Investment Arbitration? Some Unorthodox Considerations, in* THE BACKLASH AGAINST INVESTMENT ARBITRATION 577 (Waibel et al. eds., 2010).

[22] Tarcisio Gazzini, *States and Foreign Investment A Law of the Treaties Perspective*, *in* THE ROLE OF THE STATE IN INVESTOR STATE ARBITRATION 23 (Shaheeza Lalani & Rodrigo P. Lazo eds., 2015).

appropriate level of accountability and responsibility of multinational companies with specific reference to India.

In the Indian context, the Model BIT, 2016 contains expansive provisions to make the Investor State Dispute Settlement (ISDS) more transparent and accountable as good governance initiatives.[23] To ensure arbitrators are impartial and free of any conflict of interest, detailed disclosure norms and codes of conduct for arbitrators have been introduced. From an Indian perspective, investments treaties are not just instruments of investor protection, but also a valid tool promoting sustainable development goals, ensuring transparency in corporate dealings and preventing unethical business practices.[24] This part focuses on the Omission of Fair and Equitable Treatment, Investor-Home State Obligations and the Exhaustion of Local Remedies Requirement amongst many other good governance initiatives.

3.1 THE OMISSION OF FAIR AND EQUITABLE TREATMENT

The absence of a clear explanation of what is fair and what is equitable has led to a great variety of claims against host State regulations. It also raises fears that FET provision in IIAs threatens policy space and progress that has been made in promoting sustainable development. Such fears are intensified by the lack of legal certainty with respect to the application of fair and equitable treatment and the concrete scope of the standards sub

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[23] *See generally* UN World Summit for Sustainable Dev.: Plan of Implementation, World Summit for Sustainable Dev., UN Doc.A/CONF.199/L.1 (Johannesburg, South Africa 2002), Plan of Implementation of the World Summit on Sustainable Dev., UN Doc. A/CONF.199/20 (2002), ¶ 4; Principle 6, New Delhi Dec. on the Principles of Int'l Law Related to Sustainable Dev. (London: ILA, 2002); Monterrey Consensus of the Int'l Conf. on Financing for Dev., Report of the Int'l Conf. on Financing for Dev., UN Doc. A/CONF.198/11 (22 March 2002) Ch.1, Res. 1, annex (2002), ¶ 21.

[24] UNCTAD Expert Meeting on Taking Stock of IIA Reform, *Indian Model Bilateral Investment Treaty* (Geneva, Mar. 16, 2016).

elements such as fair procedure, non-discrimination, protection of investor's legitimate expectations, transparency and proportionality.[25]

There is also a possibility that any attempt to reform policies, which affect foreign investors interests could be argued as undermining the stability of law and business, leading to its being ruled incompatible with IIAs. Interpretations that overemphasize stability may be inconsistent with the promotion of sustainable development.[26] This sub part addresses in detail the issues raised by "regulatory State" and legitimate expectations.

3.1.1 Regulatory State

As States use specialized agencies to create and implement public policy, the number of government actors making and enforcing rules increases. The policy goals of one regulatory agency may conflict with those of another. This potential for disagreement is multiplied in a federal structure, in which different levels of government are also at work. A foreign investor may thus require administrative approval from a multitude of entities that do not have a mechanism to coordinate their decisions. Several investor State arbitral awards have suggested that such a duty of consistency may in fact be a component of the Fair and Equitable Treatment obligation, found in a vast majority of investment treaties. These awards have required consistency among different levels of government, different branches of government and different government

[25] Roland Klager, *Fair and Equitable Treatment and Sustainable Development*, in SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW 237 (Marie-Claire C. Segger et al. eds., 2011).
[26] Kate Miles, *National Treatment & Like Circumstances in Investment Law*, in SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW 261 (Marie-Claire C. Segger et al. eds., 2011).

ministries. This absolute duty of consistency would be difficult to implement and risks rewarding a foreign investor's lack of diligence.

The International Law Commissions' Draft Articles on State Responsibility are widely recognized to codify customary international law on the subject.[27] These articles make clear that the State is treated as a unit for the purposes of international responsibility.[28] Most relevant for present purposes is the reference to State organs, such as government ministries, regulatory agencies and courts.[29] All of the acts taken by these entities in the scope of their duties are attributable to the State.[30] The State will thus be responsible for an entity's acts if the latter is empowered by the law of that State to exercise elements of the governmental authority and is acting in that capacity in the particular instance.[31] This is true even when the entity in question is not officially designated as an organ by municipal law.[32]

As States regulatory efforts have expanded in scope, there has been a corresponding tendency towards specialization and so fragmentation. States may choose to delegate authority for policy creation and enforcement to a variety of government actors. The resulting structure by which the State applies and extends rule making, monitoring and enforcement via bureaucratic organs has been dubbed the "regulatory State".[33]

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[27] Int'l Law Comm'n, Draft Articles on Responsibility of States for Internationally Wrongful Acts, Rep. on the Work of its Fifty-Third Session (2001).
[28] *Id.*, art.2, cmt. 6.
[29] *Id.*, art. 4(2).
[30] *Id.*, art. 4 (1).
[31] *Id.*, art. 5.
[32] *Id.*, art. 4, cmt. 11.
[33] David Levy-Faur, *The Odyssey of the Regulatory State, Episode One: The Rescue of the Welfare State* 14 (Jerusalem Papers in Regulation & Governance, Working Paper No. 39, 2011).

The regulatory State poses potentially significant difficulties for the traditional conceptions of attribution and international responsibility. This is due to the sheer number of government actors involved. States commonly delegate authority to ministries within the executive branch and regulatory agencies and this may result in differences of opinion or different policy goals. It may also be unknowing with the implicated government actors simply unaware of each other's decisions. In either case is State is responsible for all of these decisions under international law. Regardless of the actors involved, one common denominator is often a claim by the investor that it had received some form of official approval of its investment on which the investor was entitled to rely. Various tribunals found that consistency by the State in its relations with the investor is an important element of the fair and equitable standard.[34]

As part of its obligation to provide foreign investment fair and equitable treatment, a host State would be required to monitor decisions taken by all relevant government actors. It would then need to ensure that any inconsistent decisions are either avoided or remedied.[35]

Requiring States to ensure consistency would entail substantial effort and expense, assuming the goal is even attainable. If relevant laws and regulations are transparent and accessible as already required by the FET obligation, then international investment law should encourage due diligence. Foreign investors are in best position to know the details of their own investment plans. They should accordingly share responsibility with

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[34] *See generally* Metalclad Corp. v. United Mexican States, ICSID Case No. ARB(AF)/97/1, Award, ¶¶ 101, 107 (Aug. 30, 2000); Franck C. Arif v. Mold., ICSID Case No ARB/11/23, Award, ¶ 538 (Apr. 8, 2013); MTD Equity Sdn. Bhd. & MTD Chile S A v. Chile, ICSID Case No ARB/01/7, Award, ¶ 165 (May 5, 2004).

[35] Danielle Morris, *The Regulatory State and the Duty of Consistency*, *in* THE ROLE OF THE STATE IN INVESTOR STATE ARBITRATION 62 (Shaheeza Lalani & Rodrigo P. Lazo eds., 2015).

the host State for the regulatory compliance of that investment. An absolute duty of consistency on the other hand risks rewarding an investor's lack of diligence.[36]

3.1.2 Legitimate Expectations

Investor's legitimate expectations have played a significant role in the assessment of whether a State's conduct is fair and equitable.[37] A claim based on legitimate expectations is subject to a certain easy circularity of argument in that an investor can postulate an expectation to condemn the sovereign conduct without articulation of the origins and scope of expectations. This leads to the so-called moving target problem because one expectation can be expressed at different levels of generality.[38] A distinct and unique role of legitimate expectations remains unclear in different types of situations. This has led to a superfluous reliance on legitimate expectations as a basis for a breach of fair and equitable treatment in various situations.[39]

The fundamental element in the analysis of legitimate expectations is to determine which expectations are reasonable. The task is challenging because the boundary of reasonableness concept is malleable and elastic, as each side exerts some pull on one's sense of fairness.[40] The concept of reasonableness serves as the fundamental criterion for evaluating the validity of the public conception of justice and all political claims and

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[36] *Id.*, at 67.
[37] Electrabel S.A. v. Hung., ICSID Case No. ARB/07/19, Decision on Jurisdiction, Applicable Law and Liability, ¶ 7.75 (Nov. 30, 2012).
[38] Franck Arif v. Mold., ICSID Case No ARB/11/23, Award, ¶¶ 533-35 (Apr. 8, 2013).
[39] Michele Potesta, *Legitimate Expectations in Investment Treaty Law: Understanding the Roots and Limits of a Controversial Concept*, 28 (1) ICSID REVIEW-FOREIGN INVESTMENT L.J. 88-122 (2013).
[40] Abdi v. Secy. of State, Home Dept. [2005] EWCA (Civ) 1363, ¶ 66 (Nov. 22, 2005).

decisions. Under Rawlsian theory reasonable citizens have to recognize the right of others to develop, pursue and realize their own visions of the good life.[41] Such recognition is necessary to establish and preserve a well-ordered liberal democracy. Transposing that framework to the context of an investment treaty, investors as rational and reasonable agents have to recognize that in some circumstances, especially in time of crisis, States may have to take draconian measures to protect public interests.[42] It is argued that despite numerous approaches for defining the boundaries of expectations, no coherent rules have been developed to apply those approaches in a principled and systematic manner.[43]

Reasonableness of expectations must take into account the underlying presumption that, absent an assurance to the contrary, a State cannot be expected to freeze its laws and regulations especially measures in response to unpredictable circumstances.[44] Some tribunals went further in recognizing that a State owes a duty to its people to be able to respond to the emerging needs and ensure maximum effective use of its economic resources.[45] It would be unconscionable for a State not to be able to respond to changing needs and circumstances.[46] Expansive recognition of legitimate expectations will create excessive burden on States.[47]

FET is omitted in the Model BIT 2016; however, the duty to afford due process and the protection is granted against manifestly abusive

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[41] Shaun P. Young, *Rawlsian Reasonableness: A Problematic Presumption?*, 39(1) CANADIAN J. POL. SCI. 159-180 (2006).
[42] El Paso v. Arg., Award, ¶ 363.
[43] Teerawat Wongkaew, *The Transplantation of Legitimate Expectations in Investment Treaty Arbitration A Critique*, *in* THE ROLE OF THE STATE IN INVESTOR STATE ARBITRATION 98 (Shaheeza Lalani & Rodrigo Polanco Lazo eds., 2015).
[44] Micula v. Romania, Awrad ¶ 673; Suez v. Argentina, Decision on Liability ¶ 236.
[45] Total v. Argentina, Decision on Liability ¶ 115; El Paso v. Argentina, Award ¶ 369.
[46] Continental Casualty v. Argentina, Award ¶ 258.
[47] EDF v. Romania, Award ¶ 217.

treatment or targeted discrimination on manifestly unjust grounds or denial of justice in any judicial or administrative proceedings.[48] Further the definition of government is very narrow and refers only the actions of central government.[49]

3.2 INVESTOR AND HOME STATE OBLIGATIONS

The purpose of IIAs is not only to protect investments, but also to promote the economic development of the host States, and for that reason there must be some regulation or control regarding investor's wrongful acts that are detrimental to the host State's economy.[50]

The International Institute for Sustainable Development (IISD) has elaborated a model IIA that provides for investor's responsibility[51] and includes provisions on corporate governance,[52] corporate social responsibility,[53] and investor's liability for civil wrongs[54] as well as

[48] *See* Article 3.
[49] "In some respects, the actions of state governments are covered by the BIT, but not those of local governments".
[50] For example the preamble of the agreement among the Government of Japan, the Government of the Republic of Korea and the Government of the People's Republic of China for the promotion, facilitation and protection of investment signed in 2012 stipulates that, "recognizing that the reciprocal promotion, facilitation and protection of such investment and the progressive liberalization of investment will be conducive to stimulating business initiative of the investors and increase prosperity among the contracting parties".
[51] The International Institute for Sustainable Development (IISD), Model International Agreement on Investment for Sustainable Development (2005).
[52] Art.15, Model International Agreement on Investment for Sustainable Development (2005).
[53] Art.16, Model International Agreement on Investment for Sustainable Development (2005).
[54] Art.17, Model International Agreement on Investment for Sustainable Development (2005).

mandatory provisions for the protection of minimum environmental and labour standards.[55]

The Model BIT indicates a change in course on the part of the Government following the IISD Model. After delineating India's duty to protect investors and their investments, India's model text also places responsibilities on both investors and their home states to ensure responsible corporate conduct and inclusive and sustainable growth in its territory.[56] Once admitted within the jurisdiction of the host state, foreign investors must respect its sovereignty and comply with its laws and regulations.[57] The Model BIT requires foreign investors to contribute to the development of the host country and to operate by recognizing the rights, traditions and customs of local communities in order to obtain treaty benefits. Investors are also required to make long-term commitments, hire local employees, avoid corruption, be transparent about financial transactions and governance mechanisms, and comply with host country taxation policies. Signatory home States are required to act against investors found to be violating Indian laws.[58] Host countries could initiate counterclaims in international arbitration for any violations of obligations on foreign investors. This is a mechanism to ensure good governance using IIAs.[59] The lack of obligations on investors, and in particular the absence of any requirement that investors themselves behave transparently

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[55] Art.22, Model International Agreement on Investment for Sustainable Development (2005).
[56] Kavaljit Singh, *Decoding India's New Model BIT,* MADHYAM (2015).
[57] The preamble of BIT between Switzerland and Nigeria for instance reiterates the duty of the investor to respect the sovereignty of the host country and observe its laws.
[58] Premila N. Satyanand, *Once BITten, Forever Shy: Explaining India's Rethink of Its Bilateral Investment Treaty Provisions*, 16 (1) AIB INSIGHTS 17 (2015).
[59] Anna Joubin-Bret et al., *International Investment Law and Development*, *in* SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW 24-25 (Marie-Claire C. Segger et al. eds., 2011).

and eschew corruption, presents a serious flaw, as a result of which IIAs might contribute to entrenching bad governance.[60] Thus investor responsibilities in addition to investor rights are also finding a place in recalibrating the asymmetry between investment regulation and investment protection within the good governance framework.[61]

3.3 EXHAUSTION OF LOCAL REMEDIES REQUIREMENT

Modern investment treaties habitually grant investors the right to bring a claim against the host State directly before an international arbitral tribunal. Allowing foreign investors to resort to international treaties and arbitration and thereby avoid domestic law and institutions international investment law does not ameliorate but in fact entrenches weakness of domestic legal orders.[62] By allowing foreign investors to exit domestic legal orders IIL creates the problems of reverse discrimination against domestic investors as well as regulatory chill.[63] The regulatory chill impact of IIAs on host governments may work against governance improvements. The investor rights enshrined in BITs and enforced through private arbitration represent a significant shift in power from states to private investors.[64]

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[60] Stephen Gelb, *States and the Investor State Arbitration Regime*, *in* THE ROLE OF THE STATE IN INVESTOR STATE ARBITRATION 127 (Shaheeza Lalani & Rodrigo Polanco Lazo eds., 2015).
[61] *See* Celine Tan, *Reviving the Emperor's Old Clothes: The Good Governance Agenda, Development and International Investment Law*, *in* INTERNATIONAL INVESTMENT LAW AND DEVELOPMENT BRIDGING THE GAP 147, 175 (Stephan W Schill et al., eds., 2015).
[62] *Id.*
[63] UNCTAD Series on Issues in International Investment Agreements II: Fair and Equitable Treatment: A Sequel (United Nations, Geneva, 2012) 12.
[64] Gus van Harten, *Private Authority and Transnational Governance: The Contours of the International System of Investor Protection*, 12(4) REV. INT'L POL. ECON. 600-23 (2005).

Requiring governments to compensate foreign investors for their losses, while not extending equivalent protection to other private actors is likely to lead decision makers to over value the interests of foreign investors.[65] There is a little doubt that over valuing foreign investors' interests is unlikely to benefit host communities through a spill over of good governance practices into the domestic sphere.[66] Instead the disadvantaging of domestic investors may lead to the internal political opposition and backlash against investment treaty law.[67] The Indian Model BIT balances the interests of States and investors by keeping the requirement of exhaustion of local remedies only for a period of five years.

4. CONCLUSION

It is important to stress that the flexibility of the current legal framework in the field of foreign investment, which is essentially constituted of BITs and other treaties with a normally limited number of parties, permit States to tailor their commitments in accordance with their specific and changing needs.[68] This flexibility in governmental action vis-à-vis the private sector is justified under the good governance framework,

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[65] Jonathan Bonnitcha, *Outline of a Normative Framework for Evaluating Interpretations of Investment Treaty Protections*, *in* EVOLUTION IN INVESTMENT TREATY LAW AND ARBITRATION 128 (Chester Brown & Kate Miles eds., 2011).

[66] Tom Ginsburg, *International Substitutes for Domestic Institutions: Bilateral Investment Treaties and Governance*, 25 INT'L REV. L. ECON. 21 (2005).

[67] MICHAEL WAIBEL ET AL. EDS., THE BACKLASH AGAINST INVESTMENT ARBITRATION (2010).

[68] Kevin C Kennedy, *A WTO Agreement on Investments: A Solution in Search of a Problem*, 24 UNIV. OF PENNSYLVANIA J. INT'L ECON. L. 83 (2003).

and it will be the base for economic growth and social development through foreign investments.[69]

Having a strong and predictable ISDS management framework brings sustainability in providing a more effective response to investment disputes,[70] and may even serve as a deterrent to claims as investors assess the option of international investment arbitration.[71] If States are expected to comply with good governance standards in their treatment of foreign investors, they should be afforded the corresponding degree of regulatory flexibility to ensure good governance in pursuing other policy objectives.

Uniform rules of investment protection saves transaction costs in the drafting of BITs,[72] stabilizes the economy, reduces international conflicts and provides legal security to investors as well. The use of model treaties did not only serve the purpose of facilitating the negotiations about the content of a BIT and thus of reducing the drafting and negotiation costs. It also aimed at ensuring a certain level of uniformity with respect to the standards governing the investment relations between the home State and varying host States and to make more credible commitments with respect to foreign investors.[73] The current reforms in BIT including on most disputed provisions in International Investment Arbitrations would create more stable investment regime and minimize misuse of ISDS

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[69] Susan D. Franck, *Foreign Direct Investment, Investment Treaty Arbitration, and the Rule of Law*, 19 GLOBAL BUSINESS & DEV. L. J. 337, 341 (2007).
[70] World Bank, *Initiatives in Legal and Judicial Reform* (World Bank 2004) 2.
[71] Kathryn Gordon & Joachim Pohl, *Investment Treaties Over Time: Treaty Practice and Interpretation in a Changing World* (OECD Working Papers on International Investment, 2015/02, 2015) *available at* http://dx.doi.org/10.1787/5js7rhd8sq7h-en
[72] Kevin C Kennedy, *A WTO Agreement on Investment: A Solution in Search of a Problem?* 24 U. PA. J. INT'L ECON. L. 77, 79–80 (2003).
[73] STEPHAN W. SCHILL, THE MULTILATERALIZATION OF INTERNATIONAL INVESTMENT LAW 91 (2009).

mechanism.[74] Now as investment law is in the process of rebalancing the interests of States and investors, we need to remain committed to pursuing a goal of improving States as regulators of individual's lives, not just to state powers for the sake of preserving sovereignty.[75]

[74] UNCTAD Expert Meeting on Taking Stock of IIA Reform, *Indian Model Bilateral Investment Treaty* (Geneva, 16 March 2016).
[75] Schefer, *supra* note 2, at 21.