Igor Mojanoski[*]

BILATERAL INVESTMENT TREATIES AS A MEANS FOR ADVANCEMENT OF FOREIGN DIRECT INVESTMENT

Abstract……………………………………………….....1
I. *Introduction*………………………………….……………1
II. *The origin of the concept*……….………….……..2
III. *The content of BITs*……………….…………….…..5
IV. *3 categories of provisions*..…………….……..5
V.*The changing character of BITs*………………5
VI. *Features of BITs*……………………………6
VII. *Reasons for making bilateral investment treaties*………………………………………………10
VIII. *Conclusion*…………………………………...15

-abstract-

The aim of the analysis of BITs as a method for advancement of foreign direct investment is to cover several important topics. Those are: defining the term and the concept, determining its historic development, explaining its basic characteristics, analyzing their features and the reasons for concluding them. BITs serve a purpose of advancing the economic linkages of the signatory parties, with an ultimate objective of development or economic advancement. From the eighteenth century onward the forerunners of the modern BITs were the historic so-called Friendship, Commerce and Navigation (FCN) agreements that were concluded by the major colonial powers as well as the USA. The key difference between the FCN treaties and modern BITs is that the FCN instruments were designed at a time when international commerce largely consisted of trading in goods by merchants. Irrespective of the number of BITs concluded, their basic characteristics are more or less the same - they are designed to cover the following five substantive areas: (i) definition of investment and investor; (ii) admission of foreign investors; (iii) fair and equitable treatment of investors; (iv) compensation in the event of expropriation; and (v) methods of settling disputes. Formally, BITs regulate FDI-related issues such as admission, treatment, expropriation, and the settlement of disputes at the bilateral level. Several important features are relevant for BITs: are concluded between capital-exporting states and capital importing states, are differentiated phases of pro-investor attitude and phases of state-centred thinking, cover mechanism to expand international standards and to codify lex specialis, arises the question whether exhaustion of local remedies is required. One important reason to conclude BITs being analyzed is certainly the fact that they have instilled a sense of security in foreign investors. Finally, the reasons for concluding BITs are being presented.

Keywords: *Friendship, Commerce and Navigation (FCN) agreements, Bilateral Investment Treaties (BITs), investment, investor, dispute settlement.*

I. INTRODUCTION

When defining the bilateral investment treaties (BITs) we can say that they have been in existence for centuries although they initially contained substantially less in the way of formal rules than those in existence today.“The reduction in trade barriers over the second half of the last Century went hand in hand with increasing regulation of international trade flows, via the creation of supranational institutions – preferential trade agreements at the

[*] Igor Mojanoski, PhD Student in Business Law, Ss. Cyril and Methodius University in Skopje, Faculty of Law Iustinianus Primus, e-mail: igormojanoski@gmail.com

regional level, and the World Trade Organization at the multilateral level." (Desbordes & Vicard, 2009)
As treaties, Collins defines that "BITs are legally binding agreements between two sovereign nations which comprise various protections for international investment for the stated purpose of advancing the economic linkages of the signatory parties, with an ultimate objective of development or economic advancement. This goal tends to be found in the preamble of the average instrument. For instance, the Germany–Hong Kong BIT of 1996 states in its preamble:

> Desiring to create favourable conditions for
> greater investment by investors of one
> Contracting Party in the area of the other;
> Recognising that the encouragement and
> reciprocal protection of such investments will
> be conducive to the stimulation of individual
> business initiative and will increase
> prosperity in both areas;[*]" (Collins, 2017, pp. 81-82)

"BITs typically include general levels of protection for investments. These norms are claimed to be drawn from customary international law, though there is some dispute as to precisely what minimum level of protection is required." (Schneiderman, 2008, p. 33)
Regarding the benefits from the treaties, it is the national investors of one party investing in the territory of the other party who gain the direct benefits contained in the treaty, although in theory a claim against the other party under international law for failure to uphold the treaty's obligations could be brought by a state party itself. As with all treaties, BITs are concluded between the executive branches of the state's government. In many instances they must be ratified through internal legislative procedures. (Collins, 2017, p. 82)

II. THE ORIGIN OF THE CONCEPT

1. The forerunners - Treaties of friendship, commerce and navigation

From the eighteenth century onward the forerunners of the modern BITs were the historic so-called Friendship, Commerce and Navigation (FCN) agreements that were concluded by the major colonial powers as well as the USA. The most active user of these treaties was perhaps the USA, establishing a large number during the nineteenth century. As noted earlier, these treaties were not confined to commerce; they extended to military matters involving matters such as access to ports and navigation through internal waters. The historic parallels are compelling although they are quite removed from what we now understand modern BITs to be. (Collins, 2017, pp. 80-81)
The key difference between the FCN treaties and modern BITs is that the FCN instruments were designed at a time when international commerce largely consisted of trading in goods by merchants. Granting a minimum level of protection that was embodied in customary international law, FCNs were intended to ensure that travellers were not subjected to weak or unfair laws that existed in host states.[1] They did not involve direct investment by

[*] 19 Feb 1998 (entry into force).
[1] M. Sornarajah, *The International Law on Foreign Investment* (Cambridge University Press, 2010).

multinational corporations or instances where consortiums set up permanent operations in host countries. The protection that should be accorded to individual foreigners was emphasized by FCN treaties at a very general level, as trading was largely done by individuals establishing themselves overseas for the purposes of trade – effectively the point at which trade becomes investment. (Collins, 2017, pp. 80-81)

Later bilateral investment treaties which dealt with the more specific needs of foreign investors were formulated by using the experience of the FCN treaties. (Sornarajah, 2010, pp. 180-181)

The FCN treaties were concluded with smaller, less powerful states, which could be tied to the larger power in the context of the bipolar world that existed at the time the treaties were signed were measures for spreading the influence of the major powers. "Following the changes in the economic and power balances and in the internal structure of the states, FCN treaties came to be used in ways quite unintended by the powerful state which secured the treaty. Thus, the FCN treaty between Japan and the United States, which permits access to and establishment in the Japanese market, has come to be used by Japan for making claims of access to US markets at a time when there was a dramatic change in the economic balance between the two states.[2] Not only is access claimed on the basis of the treaty, but claims are also made as to exemptions from domestic laws such as those on nondiscrimination in employment." (Sornarajah, 2010, p. 181)

"Nicaragua has used the dispute-settlement provisions of its FCN treaty with the United States to establish jurisdiction in its claims against the United States regarding the military intervention of the United States in Nicaragua's internal affairs.[3] Similar use of an FCN treaty was made by Iran in the Oil Platforms Case. The fact that worms may turn and the treaty may be used against the more powerful party will lead to a rethinking of the usefulness of these broadly framed treaties." (Sornarajah, 2010, pp. 181-182)

---

[2] The arguments based on the treaty bestowing powers on a company to use its own employment practices were used by the
defendant Japanese company in Sumitomo Shoji America Inc. v. Avagliano, 457 US 176 (1982). The Supreme Court
sidestepped the argument by holding that the Japanese company was a US corporate national as it had incorporated in the
United States, and that it could not therefore claim the treaty rights. This would mean that a Japanese employer, choosing not
to incorporate in the United States, could violate US laws against discrimination with impunity. The result was never thought
of at the time of the treaty simply because the economic dominance of Japan was not contemplated at the time. In a later case,
Fortino v. Quasar Co., 950 F 2d 389 (1991), the right of a Japanese subsidiary to employ Japanese personnel in preference to
Americans was recognised on the basis of the provisions of the FCN treaty. The decision has been criticised: S. Mozarsky,
'Defining Discrimination on the Basis of National Origin under Article VII(1) of the Friendship Treaty Between United States
and Japan' (1992) 15 Fordham ILJ 1099.

[3] Nicaragua Case [1984] ICJ Reports 352.

2.The beginnings of the modern era of BITs

The driving question to address is when the features elaborated by the idea to provide a particular level of international protection for foreign investments become binding in nature. The first bilateral investment agreement (BIT) between Germany and Pakistan concluded in 1959 is considered as a starting point for the 'era of modern investment treaties'. An exclusive emphasis on the protection of foreign investment and a "re-assessment"[4] of already existent substantive guarantees is what this treaty is best described with. The Germany-Pakistan BIT did not contain an investor-state dispute resolution clause and referred to state-to-state dispute settlement.[5] (Kozyakova, 2021, pp. 19-20)

"Other European powers followed Germany's lead, engaging in a programme of BITs throughout the remainder of the twentieth century. The USA, by contrast, was a latecomer to the world of BITs, preferring instead to concentrate on regional trade arrangements with investment chapters, most notably NAFTA." (Collins, 2017, p. 81)

The BIT between Italy and Chad entered into in 1969 was the first agreement to mark "the true beginning of the modern BIT practice"[6]. According to Professor Andrew Newcombe and Dr Lluis Paradell, this represents the starting point "because it combines substantive investment promotion and protection obligations with binding investor-state arbitration to address alleged breaches of those obligations."[7] However, the present author's examination of other agreements from this period has found that the 1968 BIT between the Netherlands and Indonesia also contained an acceptance of ISCID jurisdiction and, thus, a binding investor-state arbitration clause.[8] (Kozyakova, 2021, pp. 19-20)

"Especially in the 1990s, this process of the proliferation of international investment agreements accelerated dramatically, leading to a dense network of over 2,600 BITs concluded by the end of 2007.[9]" (Klager, 2011, pp. 25-26)

Starting in the 1980s, this fundamental change in mind of developing countries, is mainly due to the victory of market ideology facilitated by the collapse of the Soviet bloc and the debt crisis of the 1980s which reduced the availability of private lending as the main alternative source of capital.[10] (Klager, 2011, pp. 25-26)

The emergence of developing countries acting as capital-exporters, concluding themselves BITs with other developing countries was another factor contributing to this trend.[11] Developed countries increasingly recognised their position of being not only capital-exporters but also capital-importers. More recent tendencies are indicating the growing reluctance of developed countries towards further investment liberalisation[12] and all contribute to an increasingly fragmented political process, in which the different ideological positions become

[4] Kishoiyian (1993), p. 331.
[5] See Article 11, Treaty for the Promotion of Investments between Germany and Pakistan, 25 November 1959, 457 U.N.T.S. 24.
[6] Newcombe and Paradell (2009), p. 45.
[7] Newcombe and Paradell (2009), p. 45.
[8] See Article 11, Agreement on Economic Cooperation between the Netherlands and Indonesia, 7 July 1968, http://investmentpolicyhub.unctad.org/Download/TreatyFile/3329.
[9] On this 'second stage' of the international investment process, see UNCTAD (above fn. 4), pp. 14 et seq. and 23.
[10] See Vandevelde (above fn. 54), pp. 177 178; and Schill (above fn. 3), p. 62.
[11] On this trend, see, e.g. Dolzer and Schreuer (above fn. 54), p. 21; China has now
concluded the second largest number of BITs after Germany, see UNCTAD (above fn. 4), p. 24, figure 4.
[12] Such tendencies are especially expressed by the growing concerns about sovereign wealth funds: see UNCTAD, Transnational Corporations and the Infrastructure Challenge (2008), pp. 25 26 and 77; for the German example of a domestic law monitoring
sovereign wealth funds, see T. Voland, 'Freitag, der Dreizehnte', EuZW (2009), p. 519.

more and more intermingled. The system of international investment law should not lopsidedly reflect the one or the other extreme ideological position. (Klager, 2011, pp. 25-26)

III. THE CONTENT OF BITs

Irrespective of the number of BITs concluded, their basic characteristics are more or less the same. According to Subedi, "they are designed to cover the following five substantive areas: (i) definition of investment and investor; (ii) admission of foreign investors; (iii) fair and equitable treatment of investors; (iv) compensation in the event of expropriation; and (v) methods of settling disputes." (Subedi, 2008, p. 84)
It is typical that most BITs follow a certain pattern and contain similar provisions no matter how much the exact nature and the content of a BIT concluded between one state and another may vary with those concluded between other states. "Most BITs are designed to extend fair and equitable treatment, full protection and security, and MFN and national treatment to investors. BITs are intended to protect such investment from expropriation without compensation and against any mistreatment and to provide a legal remedy, generally through international arbitration not only between states but also between an investor and the host state, against any violations of the provisions of the BIT concerned. Some of the more recent BITs impose a ban on performance requirements and on restrictions on the expatriation of profits and investments, etc." (Subedi, 2008, p. 84)

IV. 3 CATEGORIES OF PROVISIONS

"Most BITs and investment chapters of RTAs follow a certain pattern and contain similar provisions, which may be generally divided into three categories: scope, substantive protection and dispute settlement." (Collins, 2017, p. 85)
1. Scope: After the preamble, which tends to explain the purpose of the BIT, the scope of the treaty will be to establish a definition for investment and investor in order to clarify the nature of the commercial activity which it is intended to cover, followed by conditions on the admission of foreign investors.
2. Substantive protection: The substantive protection of BIT is to establish guarantees against discrimination through two distinct yet relative standards, National Treatment and MFN. Most BITs then offer guarantees of FET and, somewhat less importantly, Full Protection and Security (FPS) along with other miscellaneous protections relating to currency transfer and the hiring of personnel. A guarantee against expropriation without compensation is found in almost all instruments.
3. Dispute settlement: Covering both state-to-state and more significantly, investor–state dispute settlement, dispute settlement features of a BIT, are normally saved until the end. (Collins, 2017, pp. 85-86)

V. THE CHANGING CHARACTER OF BITs

"Formally, BITs regulate FDI-related issues such as admission, treatment, expropriation, and the settlement of disputes at the bilateral level." (Egger & Pfaffermayr, 2004)

The Federal Republic of Germany was the first country to conclude BITs with certain developing countries in the 1960s in order to protect German investment in these countries. Thus, as a consequence we can say that BITs are a relatively recent phenomenon—they are a German invention perfected over the years by the US and other investor countries. Initially, BITs were seen as a challenge by developing countries to the international efforts to regulate

foreign investment through an international instrument adopted under the auspices of the UN. (Subedi, 2008, pp. 113-114)
Subedi explains that "as outlined in a presidential communication to Congress, the main US objectives in the conclusion of this BIT were as follows:

- Investment of nationals and companies of one Party in the territory of the other Party (investments) receive the better of the treatment accorded to domestic investments in like circumstances (national treatment), or the treatment accorded to third country investments in like circumstances (most-favoured-nation (MFN) treatment), both on establishment and thereafter, subject to certain specified exceptions;
- Investments are guaranteed freedom from performance requirements, such as obligations to use local products or export goods;
- Companies which are investments may hire top managers of their choice, regardless of nationality;
- Expropriation can occur only in accordance with international law standards: in a non-discriminatory manner; for a public purpose; and upon payment of prompt, adequate, and effective compensation;
- Investment-related funds are guaranteed unrestricted transfer in a freely usable currency; and
- Nationals and companies of either Party, and their investments, have access to binding international arbitration in investment disputes with the host government, without first resorting to domestic courts" (Subedi, 2008, pp. 115-116)

VI. FEATURES OF BITs

Researching the specifics of the BITs, several vital features could be examined: who concludes those more - capital-exporting states or capital importing states, what is the difference between phases of pro-investor attitude and phases of state-centred thinking, what is the meaning of the mechanism to expand international standards and to codify *LEX SPECIALIS,* possibilities to exhaust local remedies and ways to settle investor-state disputes.

1. Are concluded between capital-exporting states and capital importing states

"BITs are designed to facilitate foreign direct investment (FDI) from economies with abundant capital and skilled labor, i.e., mainly OECD countries, to the less developed economies." (Egger & Pfaffermayr, 2004)
"In the past, BITs tended to be concluded between capital-exporting states (developed countries such as the former colonial powers) and capital importing states (developing countries or former colonies), as indeed this was the manner in which FDI initially unfolded historically through its linkages to imperialism. Much as today, developed countries tend to be stable democracies governed by the rule of law where property rights are recognized and the judges are independent. Risk of unfair treatment in these environments accordingly tends to be negligible, which is one of the reasons that most of the world's largest corporations call these countries home. In contrast, developing countries, while often resource-abundant and attractively possessing cheap labour, tend to be associated with unstable regimes and unreliable legal systems, or at least are perceived that way by cautious firms. BITs are therefore correctly understood as commercial risk mitigation strategies." (Collins, 2017, pp. 82-83)

1.1. Changes in capital-exporting/ capital importing states paradigm

In some respects the global trends are necessitating a recasting of the old capital-importing/capital-exporting labels as many countries now share characteristics of both. The capital-exporting/capital-importing BIT paradigm has changed dramatically in recent years and given this momentous change, it is difficult to maintain that BITs should be viewed as instruments of Western colonial power (as they once may have been).[13] Now, FDI flows across the global moving towards equilibrium.[14] As mentioned previously, outward FDI from the developing world is at its highest level in history, comprising more than a third of global outward investment flows.[15] Developing states are accordingly negotiating these treaties between themselves. The use of bilateral investment agreements by developing states in part reflects the growth of FDI from these countries, particularly the large emerging markets. (Collins, 2017, pp. 83-84)

1.2.The development of the phenomenon

"This phenomenon somewhat belies the theory that IIAs are aimed at reassuring investors nervous about the exposure to political risk in unstable countries. Perhaps most curiously, developed countries continue to conclude BITs and regional trade agreements (RTAs) with investment chapters with each other. While many of these instruments are understandable in that they contain provisions aimed at liberalizing investment flows (enlarging market access to foreign firms for more spheres of economic activity), many of these instruments consist of traditional BIT-style protections such as guarantees against expropriation and access to neutral international arbitration. Such legal entitlements are presumptively available in advanced democracies committed to the rule of law. What this means in terms of the contents of IIAs and in particular their adoption of somewhat more balanced features (proinvestor and pro-state) is very much a matter of ongoing debate.[16]" (Collins, 2017, pp. 83-84)

2. phases of pro-investor attitude and phases of state-centred thinking

As Klager explains, "the conflicting ideological positions are also apparent in the political process of negotiating international investment agreements, which clearly displays the oscillation between phases of pro-investor attitude and phases of state-centred thinking.[17] Usually, developed countries in Europe and North America, as traditional capital-exporters, adopted a pro-investor attitude that was favourable to their economic activities abroad. However, quite strong reservations against foreign capital arose in the aftermath of World

---

[13] Sornarajah, *International Law*, generally
[14] D. Collins, *The BRIC States and Outward Foreign Direct Investment* (Oxford University Press, 2013).
[15] UNCTAD World Investment Report, 2015, unctad.org/en/PublicationsLibrary/wir2015_en.pdf.
[16] Collins, *The BRIC States*.
[17] Re. the history of the BIT movement, see, e.g. J. W. Salacuse, 'BIT by BIT', Int'l Law 24 (1990), p. 655 at pp. 656 664; G. Sacerdoti, 'Bilateral Treaties and Multilateral Instruments on Investment Protection', RdC 269 (1997), p. 251 at pp. 298 302;
UNCTAD, Bilateral Investment Treaties 1959 1999, UNCTAD/ITE/IIA/2 (2000); K. J. Vandevelde, 'A Brief History of International Investment Agreements', U.C. Davis J. Int'l L. & Pol'y 12 (2005), p. 157; Bishop, Crawford and Reisman (eds.) (above fn. 53), pp. 2 7;
T. W. Wa¨ lde, 'The Specific Nature of Investment Arbitration', in P. Kahn and T. W. Wa¨lde (eds.), Les aspects nouveaux du droit des investissements internationaux (2007), p. 43 at pp. 67 91; R. Dolzer and C. H. Schreuer, Principles of International Investment Law (2008),
pp. 17 et seq.; Newcombe and Paradell (above fn. 3), pp. 1 et seq.; and Schill (above fn. 3), pp. 25 et seq.

War II and decolonisation.[18] Therefore, developed countries felt a need to secure additional and higher standards of legal protection for their investments than those offered under the domestic laws of developing host countries or under customary international law.[19]" (Klager, 2011, pp. 24-25)

Furthermore, concerning the protection of foreign capital, a way to overcome the ideological discussions and reservations was the negotiation of international investment agreements, especially BITs. "On the other side, many developing countries increasingly appreciated foreign investment as a source of capital and thereby gradually abandoned their besetting hostility towards foreign investment based on the dependency theory. Accordingly, an increasing number of developing countries entered into investment agreements, which were seen as important elements of a favourable investment climate attracting foreign investors.[20]" (Klager, 2011, pp. 24-25)

3. Mechanism to expand international standards and to codify *LEX SPECIALIS*

I found that owing to historical, geographical, cultural, political, social or economic reasons, there is a great variation in the nature of bilateral relations between states. Mainly, BITs extend the scope of the standard of treatment available to foreign investors under customary international law. Most BITs provide greater protection to foreign investors than is available under international law. They do not limit themselves to codifying the rules of customary international law, although most of their provisions would be close to customary international law, but certain other provisions may be at variance with it. (Subedi, 2008, p. 90)

Since the international foreign investment law provides only a framework of principles, it leaves a great deal of room for manoeuvre by individual states to fashion their relationship with a state of their choice in the manner they wish. States may wish to accommodate this unique or special relationship in a BIT that provides a slightly different level of treatment for foreign investors from those countries than those provided in other BITs with other states. In relation to the investment coming from such states, they may also wish to deviate slightly from international practice and provide a more favourable treatment or include special clauses. States can codify their own *lex specialis* applicable to relations between them on matters relating to foreign investment, when 'fleshing out' of the rules of international customary law on foreign investment in this way. (Subedi, 2008, pp. 90-91)

Because there is no global treaty on foreign investment law, states can through a BIT fashion their relations with other states and can also prescribe their own method of handling claims of expropriation. (Subedi, 2008, p. 91)

"Furthermore, a country which has little to offer by way of trade or one that is very keen on making its privatisation programme a success may wish to go further than other states and may offer a higher level of protection and greater threshold of compensation against potential expropriation. Conversely, a state keen to protect its environment or the rights of its workers, or wanting to exercise a greater degree of economic sovereignty, embark on new

---

[18] Especially in these times and because of the claim of a New International Economic Order by developing states, the negotiation of a BIT on an ad hoc basis was more feasible since there was no consensus on multilaterally acceptable norms: see, e.g. A. F. Lowenfeld, 'Investment Agreements and International Law', Colum. J. Transnat'l L. 42 (2003), p. 123 at pp. 123 128; and Sornarajah (above fn. 3), pp. 211 217.

[19] An overview of political risks that may affect foreign investment is provided by P. E. Comeaux and S. N. Kinsella, Protecting Foreign Investment under International Law (1997), pp. 1 22. They identify five different types of political risks: expropriation, de facto
expropriation, currency risk, the risk of political violence and the risk of breach of contract by the host state; similarly, see Rubins and Kinsella (above fn. 46), pp. 1 29.

[20] See UNCTAD (above fn. 54), p. 1; and J. W. Salacuse and N. P. Sullivan, 'Do BITs really work?', Harv. Int'l L.J. 46 (2005), p. 67 at p. 77.

developmental programmes or revisit concessions or other contracts with foreign companies may have valid reasons for wishing to include some cautionary provisions or a lower threshold of compensation against expropriation." (Subedi, 2008, p. 91)

"A BIT is a mechanism that can accommodate all such eventualities by codifying a lex specialis between the states concerned. Therefore, regardless of the number of BITs embodying the same and similar provisions, such provisions cannot necessarily be regarded as having crystallised into international law." (Subedi, 2008, p. 91)

4. **Exhaustion of local remedies**

Depending on the provisions in the BIT concerned there could be a requirement to exhaust local remedies prior to resorting to international arbitration. The Convention establishing the ICSID itself does not require the exhaustion of local remedies unless the state has conditioned its consent on this factor. It is expected that most BITs normally within a specified period of six months, prior to referring the matter to international arbitration require amicable resolution of the disputes through either consultation or conciliation. Those BITs that require the exhaustion of local remedies do nonetheless often contain an 'exit' or 'opt out' provision, allowing arbitration if a national court has not rendered its judgment within a specified period of time. Most of the BITs, particularly those concluded recently, do not require the exhaustion of local remedies and the resort to national courts as one of the many options available to foreign investors for the settlement of investment disputes with the host states. Moreover, a vast majority of foreign investors have opted for arbitration, rendering the option to go to national courts redundant. (Subedi, 2008, pp. 95-96)

Further in the text will be given two possibilities:

1. the first one when a BIT requires the exhaustion of local remedies prior to resorting to international arbitration and
2. the second one when the exhaustion of local remedies can been circumvented.

1. An instance that if a BIT requires the exhaustion of local remedies prior to resorting to international arbitration, foreign investors will have little room for manoeuvre is the BIT between Argentina and Spain. It is stipulated in the two conditions prior to the commencement of arbitration: (1) the foreign investor had to exhaust all local remedies; and (2) an 18-month period had to expire without issuance of a court decision on the merits. As will be discussed later, these requirements were a major issue in the Maffezini case because the foreign investor had not exhausted local remedies prior to resorting to arbitration. On this basis, the tribunal did acknowledge that a jurisdictional problem existed, but the requirement was circumvented by referring to another BIT between Spain and Chile which did not stipulate these conditions under the MFN principle. (Subedi, 2008, p. 96)

2. There have been other instances—eg, in the context of investment contracts—
where the requirement for the exhaustion of local remedies has been circumvented. The requirement to exhaust local remedies under the investment contract would not be applicable if a foreign investor investing under an investment contract, such as a concessions contract, is allowed to resort to BIT arbitration, ICSID or otherwise, for the settlement of contractual disputes. This was the opinion of a tribunal in the Lanco case where it was held that the investor could resort to ICSID arbitration under the BIT in spite of the existence of a forum-selection provision requiring claims to be referred to the local courts in the host country concerned. (Subedi, 2008, p. 96)

5. Investor-state settlement of disputes

Subedi talks about an innovation in the history of dispute settlement at the international level. He explains that a major feature of a modern BIT is to allow foreign investors access to international investment tribunals, such as ICSID, for the resolution of disputes between the investor and the host state. Investor–state dispute resolution was made possible for the first time in the BITs concluded since the 1960s. An investor would be entitled to take the host state to a binding, third-party arbitration, under a typical BIT, usually under the rules of ICSID, to settle any disputes involving the interpretation of the application of the BIT.[21] If the host state refuses to participate, the BIT made provision for an appointing authority to appoint arbitrators on behalf of the host state to enable the arbitration to proceed even without co-operation of the host state. (Subedi, 2008, p. 96)
BITs allow home or investor countries to extricate themselves from involvement in private investment disputes, without diminishing the effectiveness of the remedies available to investors. This is because, prior to the BIT era, investors had to look to the government of their own country for assistance when their investment was expropriated or unlawfully impaired by a foreign government. Since there were no binding, third-party dispute settlement mechanisms available for foreign investors and host states could invoke sovereign immunity and the Act of State Doctrine before any domestic courts, diplomatic protection was the only avenue open to such investors. (Subedi, 2008, p. 97)
It should be answered the question of political character of the investment dispute and two options are possible.

1. First, when state machinery decides to espouse a claim and pursue a remedy on behalf of its private investors through diplomatic channels or international arbitration, or impose economic sanctions on the alleged wrongdoer, the dispute acquires a political character.

2. On the other hand, when an effective dispute settlement mechanism such as ICSID is available to private foreign investors there is no need for government intervention and the politicisation of investment disputes. Thus, one of the major positive contributions made by the BITs is, to borrow the word from Vandevelde, the 'depoliticisation' of investment disputes. (Subedi, 2008, p. 97)

VII. REASONS FOR MAKING BILATERAL INVESTMENT TREATIES

In the chapter I examine the underlying reasons for accessing to BITs, such as: what is the relation between the bilateral solutions and the attempts to create a binding multilateral treaty; the reasoning of the doctrines that favoured foreign investment through theories of internationalisation of foreign investment, opposing to the doctrine of permanent sovereignty over natural resources; analyzing the state of conflicting norms; which factors influenced treaty-making in 1990s and political or legal structure being favourable creating treaties and supporting investment.

1. Attempts at multilateral treaties on foreign investment

Bilateral solutions become necessary simply because of an absence of a consensus on multilateral norms.[22] There were several unsuccessful attempts at multilateral treaties on

[21] For a detailed commentary of the ICSID Convention, see CH Schreuer, *The ICSID Convention: A Commentary* (Cambridge University Press, 2001).
[22] For a similar view in a different context, see A. Carty, 'Critical International Law: Recent Trends in the Theory of International

foreign investment protection.[23] The reasons for the failure of these attempts are obvious. Sensitive issues of sovereignty, exploitation of natural resources and internal economic policies are raised that relate to foreign investments made by large multinational corporations. It is unlikely that developing states will commit themselves readily on such issues in a binding multilateral treaty, though developed states will be keen to realise such a treaty.[24] Developing states have been striving to bring about a New International Economic Order (NIEO) in the decades after decolonisation, one facet of which is national control over all foreign investment. There has been no urgency among developing states to dismantle the gains that resulted during the period of vigour of the movement for the NIEO. So, it is not likely that developing states will give up from their efforts to establish national control as the prevailing general standard by accepting a multilateral treaty which strikes at the principle of national control. The possibility of agreeing strong rules in such an instrument remain a distant possibility, but the efforts at drafting multilateral instruments on investment will continue. This is particularly so after the global economic crisis which commenced in 2008. There is a return to regulatory control of the economy in both the developed and the developing world. In that context, it is unlikely that states will be willing to be constrained by a multilateral treaty on investment, or, for that matter, by bilateral treaties with inflexible rules. (Sornarajah, 2010, p. 183)
"Yet, bilateral treaties are different in that they are made on an ad hoc basis, and their ability to give rise to general principles is remote. In addition, such treaties could be negotiated in such a way as to suit the mutual interests of the parties, whereas a multilateral treaty cannot be." (Sornarajah, 2010, p. 183)

1.1. Towards a Multilateral Investment Court

"The discussion about a Multilateral Investment Court was triggered by the increased public criticism towards traditional investor-state arbitration – be it *ad hoc* or institutional.[25] The debate prompted the EU to consider an alternative forum for the settlement of investor-state disputes. Different political parties in the EU Parliament proposed the establishment of a permanent investment court to replace traditional *ad hoc* arbitral tribunals.[26] The European Parliament then adopted a resolution calling for the establishment of a permanent Investment Court System (ICS) with an appellate structure in new agreements negotiated by the EU. The mid-September 2015 Commission draft text of the Transatlantic Trade and Investment Partnership (TTIP) Investment Chapter 'implemented' these ideas by proposing an

Law' (1991) 2 EJIL 66.
[23] See Chapter 6 below. Early attempts are described in G. Schwarzenberger, Foreign Investments and International Law (1969),
pp. 109–20.
[24] The keenness of the developed states is also suspect after the experience of the effort at the OECD's multilateral agreement on
investment, which was an effort made entirely by developed states to create a multilateral agreement. Discord broke out
among the developed states on several provisions. This is dealt with in Chapter 6 below.
[25] Cf. e.g. Harten (2007); Schill (2007); Hachez and Wouters (2012); Kumm (2015); Cf. also the European Citizens 'Stop TTIP' initative (2017); Cf. for US opposition: Open letter by the Alliance for Justice to the US Congress (2015).
[26] Group of the Progressive Alliance of Socialists and Democrats (S&D), Position Paper on investor–state–dispute settlement mechanisms in ongoing trade negotiations, 4 March 2015, available at
https://www.socialistsanddemocrats.eu/sites/default/files/position_paper_investor_state_dispute_settlement_ISDS_en_150304.pdf
(accessed 07 December 2020).

'Investment Court System'.[27] It was further elaborated on in the November 2015 Commission proposal for Investment Protection and Resolution of Investment Disputes in TTIP.[28] First ICS were then included in the February 2016 Comprehensive Economic and Trade Agreement (CETA) text agreed with Canada[29] and in the January 2016 agreement with Vietnam.[30] After the Court of Justice of the European Union (CJEU) rendered its *Singapore* Opinion, the text of the EU Free Trade Agreement (FTA) with Singapore was modified, one agreement became two, the old fashioned *ad hoc* arbitration originally foreseen in the agreement was deleted and the ICS inserted.[31]" (Marc Bungenberg, 2021, pp. 8-9)

2. The competing doctrines on investment protection

In the modern theories there is an actual competition between supporters of theories who favoured foreign investments and competing theories of sovereignty over natural resources and were especially expressed the concerted attacks by developing states on the rules contended for by developed states. As a result, contractual regimes on the basis of which foreign investments were made were being replaced by new contractual techniques that were favourable to national control of the investment.
The previous tendency had been to create doctrines that favoured foreign investment through theories of internationalisation of foreign investment, whereas there were now competing norms such as the doctrine of permanent sovereignty over natural resources, economic self-determination and national control over all economic activities.
The rules of state responsibility and the minimum standards of treatment of aliens were being attacked by many developing states, including Latin American states. As an effect, they led to regulatory legislation in the developing world and control of the entry of investments and the subsequent operation within the host state. In stark opposition to the system of norms so constructed were those favoured by developed states that emphasised the protection of foreign investment. The legislation that was enacted during the period remains largely intact, despite the period of neoliberalism that led to the explosion of investment treaties. This discrepancy between national laws and international obligations is a reason for much of the difficulties that arise in the area. (Sornarajah, 2010, pp. 183-184)

3. The confused state of conflicting norms

"In this confused state of conflicting norms, bilateral investment treaties provided the parties with the opportunity to set out definite norms that would apply to investments made by their nationals in each other's territory. It would be wrong to subscribe to the thesis that the treaties stabilised customary international law. If there was a definite conviction as to the existence of customary international law in the area, there would have been little need for such frenetic treaty-making activity on investment protection. There was an absence of significant

[27] Commission draft text TTIP – Investment, 16 September 2015, available at https://trade.ec.europa.eu/doclib/docs/2015/september/tradoc_153807.pdf (accessed 07 December 2020).
[28] See, Section 3: Art. 9 and Art. 10, EU's proposal for Investment Protection and Resolution of Investment Disputes of 12 November 2015 (TTIP), available at http://trade.ec.europa.eu/doclib/docs/2015/november/tradoc_153955.pdf (accessed 07 December 2020).
[29] See, chapter 8: Art. 8.27 and Art. 8.28, revised text of CETA made public on 29 February 2016, available at http://trade.ec.europa.eu/doclib/docs/2016/february/tradoc_154329.pdf (accessed 07 December 2020).
[30] See, Section B: Art. 3.38 and Art. 3.39, EU–Vietnam FTA Investment Chapter: Agreed text as of January 2016, published on 1 February 2016, available at http://trade.ec.europa.eu/doclib/press/index.cfm?id=1437 (accessed 07 December 2020).
[31] Bungenberg and Reinisch (2019), para. 42.

customary international law in this area simply because it would be difficult to show that there was free consent on the part of all the developing states to the creation of any customary principles in the area. If there was such customary international law, many developing states would regard themselves as persistent objectors who were not bound by the customary law. If there was customary international law on investment protection, there was no need to confirm time and time again what already existed by making bilateral investment treaties. States, which entered into investment treaties, were not engaging in such a stultifying exercise by repeatedly confirming what already existed. On the contrary, knowing the confused state of the law, they entered into such treaties so that they could clarify the rules that they would apply in case of any dispute which arose between them." (Sornarajah, 2010, p. 184)
"There was a need for rapid development of the law in this area, but such development was not forthcoming because of the conflicts which were inherent in the area of foreign investment. Hence, states had to resort to the second-best solution by making bilateral investment treaties to ensure that, as between them at least, there would be definite rules relating to foreign investment. This is a better explanation for the rapidity with which such treaties have come about on the international scene than the explanation that they merely confirm existing customary international law or create new customary international law." (Sornarajah, 2010, pp. 184-185)

4. Factors that influenced treaty-making in 1990s

Many factors influenced the increase of treaty-making in the 1990s. Sovereign lending by banks dried up because of the lack of funds for financing economic development due to loan defaults in the previous years. Because of recession in the developed economies as well as due to changes of policy the flow of aid decreased. Vigorous efforts were made to promote the free market and liberalisation of the international economy with economic liberalism as the prevailing philosophy in the United States and Europe. The increase in bilateral investment treaties in the 1990s influenced this phenomenon. They were seen as instruments that accomplished liberalisation in the sphere of foreign investment, not because they contained any norms on liberalisation itself,[32] but because of the belief that protection of foreign investment increased the flow of foreign investment.[33] The flow of foreign investment funds was seen as conducive to economic development. The view that securing foreign investment protection through investment treaties facilitated such flows was a reason given for the increase in the number of bilateral investment treaties.[34] (Sornarajah, 2010, pp. 185-186)

[32] Treaties, like the US treaty, which contained provisions on the right of entry and establishment were liberalisation treaties.
Canada, Japan and South Korea began making such treaties. But, it was possible to exclude sectors from such pre-entry national
treatment involved in the right of entry and establishment.
[33] Except for US and Canadian treaties, investment treaties seldom accepted pre-entry national treatment as an obligation.
[34] This is an untested hypothesis. Southeast Asian states which have received large investments from the United States do not
have investment treaties with that country. Stability and other factors have a greater influence on investment flows than do
investment treaties.

5. Adoption of a variety of standards

"Though the number of these treaties may be increasing, their contents indicate the adoption of a variety of standards depending on the negotiating positions of the states involved. The treaties concluded in the 1990s show the vigour of the liberalising tendencies of economic liberalism. Yet, these treaties are disparate as to content. The standards of protection are also intended to promote the flow of foreign investment. Often, the same state will accept varying standards on areas such as compensation for expropriation, the repatriation of profits and the arbitration of disputes that arise." (Sornarajah, 2010, p. 186)

The developed state will seek to extract as much protection for the investor as possible but often concedes the fact that this may not be possible.

The developing state will seek to concede as little as possible, ensuring that the treaty is consistent with its foreign investment laws and its national interests. (Sornarajah, 2010, p. 186)

6. Political or legal structure being favourable and differences regarding the period in which the treaties were made

The assumption behind the treaties is that the framework for protection they create leads to increased flows of foreign investment. This assumption is coming to be questioned.
According to Sornarajah in reality, attracting foreign investment depends more on the political and economic climate being favourable to such foreign investment than on the creation of a legal structure for its protection. (Sornarajah, 2010, p. 187)
Institutions which have promoted investment treaties have expressed scepticism of the proposition that there is a correlation between investment treaties and flows of investment. They now seem to take the view that other factors such as political stability and economic circumstances play a greater role in promoting investment.[35] (Sornarajah, 2010, p. 187)
There are also differences that reflect the period in which the treaties were made. The provisions in the early treaties are often less stringent and formulated in nebulous terms. Now, there is a tendency of increasing sophistication of the treaties as the practice develops. Thus, are tried out new dispute-settlement techniques. (Sornarajah, 2010, pp. 186-187)
I can claim that these treaties boost investor confidence in the host state and that as a result more investment flows take place. But this claim is untested. It is not empirically proven that states which conclude such treaties will receive more investments.[36] For example, many smaller developing states have signed a large number of treaties without witnessing significant inward investment flows. Nevertheless, the main expectations for developing countries concluding such treaties is the belief that they will lead to greater investor

---

[35] As indicated earlier, there is increasing economic literature on this, but the debate as to the effect of the treaties is inconclusive.
The dominant view, however, seems to be that there is little evidence of the treaties leading to significant inflows of foreign
investment.
[36] UNCTAD, World Investment Report, 2003, p. 89: 'An aggregate statistical analysis does not reveal a significant independent
impact of bilateral investment treaties in determining FDI flows. At best, bilateral investment treaties play a minor role in
influencing global FDI flows and explaining differences in their size among countries.' Similar conclusions are drawn in the
World Bank, World Development Report, p. 129: 'Countries that had concluded a BIT were no more likely to receive additional
FDI than were countries without such a pact.'

confidence by dispelling any impression of risk associated with the country in the past. "Thus, Sri Lanka, after the fall of its socialist government which had embarked on a course of nationalisation, entered into seven treaties in three years, whereas it took Singapore and Malaysia twelve years to accomplish the same. There is nothing to show that there were greater investment flows into Sri Lanka than into Singapore and Malaysia as a result of these treaties." (Sornarajah, 2010, p. 187)

VIII. CONCLUSION

When exploring BIT's, the significant moment to determine for the progress of BITs is that one when the idea to secure a particular level of international protection for foreign investments became binding in nature. In that context, the 'era of modern investment treaties' began with the first bilateral investment agreement (BIT) between Germany and Pakistan concluded in 1959.
The reasons for the expansion of BITs is in the mind of developing countries, due to the victory of market ideology facilitated by the collapse of the Soviet bloc and the debt crisis of the 1980s
In general, understanding their essence is dependent from the relevant FDI-related issues such as admission, treatment, expropriation, and the settlement of disputes at the bilateral level.
A BIT is a mechanism to govern investment relations between developed and developing countries. The majority of such treaties are between a developed and developing country but there are also some treaties concluded between the developed countries themselves containing provisions on investment protection, the number of such treaties is small.
The standard of protection available to foreign investors under customary international law is strengthened by the provisions of BITs and FTAs because there is no internationally negotiated global instrument on foreign investment law.
One important reason to conclude BITs is certainly the fact that they have instilled a sense of security in foreign investors despite that there is no credible evidence to suggest that BITs have increased the flow of foreign investment from developed countries to developing countries. The key benefit that these treaties have provided is the assurance to foreign investors that should something go wrong within the host states due to governmental interference, then they have an international legal remedy.
However, most of the foreign investors do not have any obligations towards the host countries under a BIT. With a few exceptions, most of them do not include provisions about the preservation of the environment or the protection of human rights by foreign investors in the countries where they do their business.
Finally, bilateral investment solutions play a key role as a means for advancement of foreign direct investment and their further studying will be very beneficial for development of the field of international investments law.

References:

Books:

1. Bungenberg, M., Griebel, J. & Hindelang, S. eds., 2011. *International Investment Law and EU Law.* Heidelberg(Germany): s.n.
2. Collins, D., 2017. *An Introduction to International Investment Law.* Cambridge: Cambridge University Press.

3. Dolzer, R. & Schreuer, C., 2008. *Principles of International Investment Law.* Oxford: Oxford University Press.
4. Kinnear, M. et al. eds., 2016. *Building International Investment Law.* Alphen aan den Rijn: Kluwer Law International.
5. Klager, R., 2011. *'Fair and Equitable Treatment' in International Investment Law.* 2011 ed. Cambridge: Cambridge University Press.
6. Kozyakova, A., 2021. *Foreign Investor Misconduct in International Investment Law.* Cham(Switzerland): Springer.
7. Miles, K., 2013. *The Origins of International Investment Law.* Cambridge: Cambridge University Press.
8. Schneiderman, D., 2008. *Constitutionalizing Economic Globalization.* Cambridge: Cambridge University Press.
9. Sornarajah, M., 2010. *The International Law on Foreign Investment.* 3rd ed. Cambridge: Cambridge University Press.
10. Subedi, S. P., 2008. *International Investment Law - Reconciling Policy and Principle.* Oxford and Porland, Oregon: Hart Publishing.
11. Trakman, L. E. & Ranieri, N. W. eds., 2013. *Regionalism in International Investment Law.* Oxford: Oxford University Press.

Articles:

12. Desbodes R. & Vicard V. (2009). Foreign direct investment and bilateral investment treaties: An international political perspective. *Journal of Comparative Economics* 37 (3), 372-386
13. Neumaer E. & Spess L. (2005). Do bilateral investment treaties increase foreign direct investment to developing countries? *World Development 33 (10), 1567-1585*
14. Egger P. & Pfaffermayr M. (2004). The impact of bilateral investment treaties on foreign direct investment. *Journal of Comparative Economics* 32 (4), 788-804
15. Kerner A. (2009). Why Should I Believe You? The Costs and Consequences of Bilateral Investment Treaties. *International Studies Quarterly* 53, 73-102