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**INVESTMENT TREATIES AT 50:
HOST STATE PERSPECTIVES**

Keynote Address of Judge Stephen M. Schwebel

A CRITICAL ASSESSMENT OF THE U.S. MODEL BIT

For more than 150 years, the policy of the United States in respect of foreign investment was positive. Initially as a developing country, from the time of the Revolutionary War to the early decades of the Nineteenth Century, the United States needed and welcomed foreign investment from the traditional source of that investment, Europe, Great Britain in particular. In the post-Civil War years, the industrialization of the United States, and the inventiveness of its citizenry, accelerated; capital as well as immigrants from Europe poured in. At the same time, investment by citizens and companies of the United States abroad grew and, by and during the

Twentieth Century, it became the world's main engine of overseas investment. The attachment of the United States to capital creation and investment, and to legal principles and institutions, conduced to its support for the promotion and protection of foreign investment, through treaty-making as well as other means.

That virtually unbroken pattern changed with the publication in 2004 of a new model bilateral investment treaty. The United States did not abandon its policy on foreign investment but it significantly modified its policy. These remarks address aspects of why and how, and weigh whether that policy change was well or ill advised.

Why? Essentially because it dawned on the bureaucracy – and the Congress – that bilateral investment treaties are bilateral, that they actually operate in more than one direction, that not only do BITs enable American companies to initiate arbitral proceedings against foreign governments but they enable foreign companies bring arbitrations against the Government of the United States. This elemental perception was forced upon the bureaucracy, and

commanded the attention of labor, environmental and other lobbies of non-governmental organizations, and eventually of members of Congress, not in a bilateral but trilateral context. Six NAFTA cases were filed by Canadian companies against the U.S. Government. The reaction was: *What? They are suing us? And through arbitration? Don't they know that the United States protects foreign investment better than anyone and that our Constitution and courts provide all the recourse that could be desired?*

One might have expected that a mature capitalist society, protective of foreign investment whatever the direction of its flow, would have taken six cases in its stride. If the United States had lost some, the Constitution and the Republic would not have been threatened. The economy would hardly have noticed. The Government of the United States is used to losing cases in its Court of Claims, a court set up to litigate cases against the Government. It has long understood that if it won all the cases in the Court of Claims, there would be no Court of Claims.

But the reaction was not so mature. On the contrary, the United States Government and elements of its constituencies reacted with alarm. The United States exerted itself to win all the cases against it regardless of the equities. In the event, it won them all, through fresh cases are pending. Whether, on the merits, it should have won every last case is open to question. In one of them, a Canadian company was subjected to a judicial lynching in Mississippi. A hundred years ago, when innocent Italians were the victims of an actual lynching not far from Mississippi, the United States apologized to the Italian Government and paid reparations. In my view, however good its technical defences, it would have done well to have settled with the Canadian victim of the judicial lynching. But the U.S. Government would have none of that. Bill Moyers, a star of public television, aired a widely watched program attacking arbitration of investment disputes. The three Parties to NAFTA issued an interpretation of the NAFTA which was not easily reconciled with some of its terms and apparent intent, a binding interpretation that was expressly

designed to rein in what they regarded as errant interpretations of NAFTA by NAFTA arbitrators. The three Governments found it appropriate to shift the goal posts of pending arbitral contests while those contests were in progress.

And, most significantly of all, the bureaucracy set about devising and publishing the revised 2004 model bilateral investment treaty.

I am, in the train of Mr. Moyers, oversimplifying, but I believe that my explanation of the origins of the 2004 Model BIT is essentially correct. Now permit me to say why I find the terms of the 2004 Model BIT in some respects ill advised.

First it is in order to place that BIT, and BITs at large, in historical context.

Customary international law in respect of the treatment and taking of foreign investment was, in the pre-BIT era, customarily contentious. Capital-exporting States generally maintained that host States were bound under international law to treat foreign investment at least in accordance with the “minimum standard of international law”. Where the host State

expropriated foreign property, it could lawfully do so only for a public purpose, without discrimination, and upon payment of prompt, adequate and effective compensation. Capital-importing States on the contrary maintained that, in matters of the treatment and taking of foreign property, host States were not bound under international law at all; that the minimum standard did not exist; and that States were bound to accord the foreign investor, at best, only national treatment, only what their domestic law provided or was revised to provide.

That great gulf between the positions of capital-exporting States and those of capital-importing States reached its extremity in 1974 with the adoption by the UN General Assembly of the Charter of Economic Rights and Duties of States. That Charter excluded international law in the treatment and taking of foreign investment and asserted the sole governance of the domestic law of the host State as interpreted and applied by its tribunals. Most of the industrialized democracies voted against the Charter or abstained in the vote, but developing countries and the Communist

bloc voted for it. As a General Assembly resolution not adopted as declaratory of international law, which plainly was not so declaratory, and whose partisan terms were sharply contested, the Charter could neither reflect nor make international law. Yet it demonstrated that the majority of the States of the international community then were not, at least collectively, prepared to sustain the more traditional rules of international law respecting the treatment and taking of foreign property. That majority did not equate with economic power. It evidenced bloc voting rather than considered, sovereign decision-making. But it was sufficient to raise the question of whether the UN General Assembly, if it cannot make international law, can unmake it.

Yet at the very time of the adoption of that Charter, at the very time of the General Assembly's embrace of the "New International Economic Order", the tide was beginning to turn. Universal multilateral agreement has remained elusive. But what is extraordinary is that, in the last forty years, some 2800 bilateral investment treaties have been signed, and some two-

thirds are in force. Today they are virtually universal in their reach. They run not only North and South, but East and West; they include former Communist States, as well as the People's Republic of China and Cuba. There are more than 600 "South-South" BITs between developing countries – a fact that vitiates the contention that BITs have been foisted by capital-exporting States on the LDCs.

There is no need to recall to this sophisticated audience the largely concordant terms of BITs. What is worth restating is that they specify terms far more specific and protective of foreign investment than ever did customary international law. And they provide for direct arbitral recourse by the investor against the host State, one of the most progressive developments of international law of the last century.

The U.S. 1994 Model BIT provided, as BITs generally do, that, "Each Party shall at all times accord to covered investments fair and equitable treatment and full protection and security, and shall in no case accord treatment less favorable than that required by international law."

In contrast, the 2004 Model BIT provides, in an article denominated “Minimum Standard of Treatment”:

“1. Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.”

“2. For greater certainty, paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the minimum to be accorded to covered investments. The concepts of ‘fair and equitable treatment’ and ‘full protection and security’ do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights...”

The differences between the 1994 Prototype and the 2004 Model BIT are striking. 1994 provided, directly, comprehensively, and flatly, as BITs the world over typically do, that the Parties shall at all times accord investments of nationals of the other Party “fair and equitable treatment” etc., and in no case treatment less favorable than that required by international law. The 2004 BIT retreats from these categorical and far-

reaching prescriptions. Each Party shall accord to foreign investments no more than “treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.” What was the floor has become the ceiling. What is more, “The concepts” – not the prescriptions but the concepts – “of fair and equitable treatment and full protection and security do not require treatment in addition to or beyond that required by that standard and do not create additional rights.”

The profound, and startling, deficiency of the 2004 provision is that there is no agreement within the international community on the content of the minimum standard of customary international law on which the 2004 BIT so centrally relies. There is not even agreement on whether the minimum standard exists. Can it be assumed that when the United States concludes with a developing country a BIT or an FTA using these 2004 terms, the parties are in agreement on the meaning and import of the references to customary international law? Can it be assumed that the developing country accepts the Hull formula? Or that

the United States accepts the Calvo Clause and the grotesqueries of the New International Economic Order? Rather than concluding treaties that invite controversy, why does not the United States adhere to provisions accepted more than two thousand times by the vast majority of States, including the United States before 2004? How can it make sense for the United States to jettison the characteristic protections of BITs against unfair and inequitable treatment in favor of invocation of a minimum standard that is hardly accepted as such?

Article 6 of the 2004 BIT is a normal provision on expropriation, except insofar as it imports a reference to the “Minimum Standard of Treatment”. But an Annex elaborates that Article 6 is intended to “reflect customary international law concerning the obligation of States with regard to expropriation.” That is a remarkable proviso, since it is incontestable that the content of customary international law on expropriation is contentious. The authors of this proviso seem to have overlooked the holding of the Supreme Court of the United States in *Banco Nacional de Cuba v.*

***Sabbatino:* “There are few if any issues in international law today on which opinion seems to be so divided as the limitations on a state’s power to expropriate the property of aliens.” (1)**

Time does not allow me to set out still further deficiencies in the 2004 Model BIT. I have done so elsewhere in one festschrift (2), which I amplify in respect of denial of justice in another (3).

Still other innovations of the 2004 BIT are unobjectionable or even desirable, such as those on transparency of the arbitral process. But for the reasons I have submitted to you, in the large the 2004 constitutes a regressive rather progressive development of international law. (4) It particularly does so in the distrust that it manifests of the international arbitral process.

But the 2004 Model BIT could be worse, and could become so in reconsideration of it now in train. There is reportedly support for providing that BITs to which the United States is a party shall not grant the foreign investor greater rights than the investor has under the domestic law of the United States. By dint of

reciprocity, U.S. investors would not have greater rights than those afforded by the law of the other State Party. How pleased Carlos Calvo would be.

And the United States may not be alone in resiling from the advances embodied in BITs. Quite apart from the return to traditional Latin American antipathy to international standards and recourse which has surfaced the last few years, there is ground for apprehending that even the European Community may, in appropriating authority over the conclusion of BITs, exclude or constrain arbitral recourse by the investor.

- 1. 376 U.S. 398 at p. 428 (1964).**
- 2. “The United States Model Bilateral Investment Treaty: An Exercise in the Regressive Development of International Law,” eds. Gerald Aksen, Karl-Heinz Bockstiegel, Michael J. Mustill, Paolo Michele Patocchi, Anne-Marie Whitesell, *Global Reflections on International Law, Commerce and Dispute Resolution, Liber Amicorum in honour of Robert Briner* (2005), p. 815.**

3. “The United States 2004 Model Bilateral Investment Treaty and Denial of Justice in International Law,”
Essays in Honour of Christoph Schreuer (2009,
forthcoming).

4. For a benign view of the 2004 BIT, see Kenneth J. Vandervelde, “A Comparison of the 2004 and 1994 U.S. Model BITs”, Karl P. Sauvant, ed., *Yearbook on International Investment Law and Policy* (2008/2009, forthcoming).