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INTERNATIONAL INVESTMENT: THE IMPORTANCE OF RULE OF (INVESTMENT) LAW

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The "rule of law" is important, but it often is taken for granted. In the marketplace, rule of law is like oxygen: it's difficult to see, but you can't survive without it. Investment chapters of U.S. free trade agreements, which govern investment rules, have been a topic of controversy since the North American Free Trade Agreement (NAFTA) first included bilateral investment treaty (BIT) provisions as a trade agreement chapter. Despite two major reviews of U.S. policy designed to address concerns over these provisions, the critics are as vocal as ever, both here and among U.S. negotiating partners. This quarter, we will offer some context about how investor protection agreements advance the country's economic interest, as well as evidence about how these agreements actually operate.

Investor Protection and Prosperity

Capital investment enhances productivity, and fair treatment of investment encourages the investor to act in ways that generate economic growth. Any government that wishes to raise the living standards of its citizens will find it in its interest to provide decent treatment of investment. While strong property rights are the norm in the United States, it is only because of recent progress in the law of foreign investment that enterprises are today accorded respect in most economies.

Just 50 years ago, the U.S. Supreme Court observed the gulf between the views of capital exporters and importers, writing "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] Two initiatives changed the dynamic. The first was a legal process reform with the establishment of the International Centre for the Settlement of Investment Disputes (ICSID). The ICSID convention entered into force in 1966, and today 158 nations are signatories. The second was the modern BIT, which would bridge the substantive divide between the positions of capital importers and exporters with respect to fair and equitable treatment, due process protections against expropriation, and other features. The first BIT, between Germany and Pakistan, was concluded in 1959, and since then nearly 3,000 BITs and BIT-like instruments have been negotiated. Almost all of these BITs include access to the neutral arbitration of disputes, at ICSID or a similar facility.

The core investment provisions of U.S. BITs closely follow the legal principles established in U.S. law. BITs improve U.S. competitiveness by ensuring U.S. enterprises overseas operate in a fair, consistent commercial environment. A BIT ensures that firms can set up distribution networks critical to exporting, offer services to foreign consumers via affiliate offices, and are protected against discrimination and arbitrary government actions. Importantly (and contrary to statements of some critics), they do not undermine fair application of legitimate host government regulation. As a practical matter, U.S. BITs and

1. Banco Nacional de Cuba v. Sabbitino, 376 U.S. 398 (1964).

About the Scholl Chair

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Scott Miller is a senior adviser and holds the William M. Scholl Chair in International Business at CSIS. From 1997 to 2012, Mr. Miller was director for global trade policy at Procter & Gamble, a leading consumer products company. He advised the U.S. government as liaison to the U.S. Trade Representative's Advisory Committee on Trade Policy and Negotiations, as well as the State Department's Advisory Committee on International Economic Policy. Mr. Miller was the founding chairman of the Department of Commerce's Industry Trade Advisory Committee (ITAC) Investment Working Group.

International Business Developments

REPORT RELEASE

A *New Development Agenda: Trade, Investment, and Procurement,* led by Scott Miller and Dan Runde. You can read the full report here: http://csis.org/publication/new-development-agenda.

UPCOMING EVENT

April 8, 2014: "Making Trade Work for America," featuring Senator Orrin Hatch

The United States has embarked upon its most ambitious trade agenda in recent years, but many agree that the agenda will not move forward without Congress passing authorizing trade promotion authority (TPA). Please join us as Senator Orrin Hatch, ranking member of the U.S. Senate Committee on Finance, will discuss TPA and more.

INTERNATIONAL INVESTMENT: THE IMPORTANCE OF RULE OF (INVESTMENT) LAW *(continued)*

FTA Investment chapters actually enhance, rather than undermine, the rule of law by "exporting" the core U.S. legal practices that protect the interests of all investors in the United States and give states a workable basis to enhance their rule of law.

If U.S. law is the standard, what's the problem?
Many stories in the popular media focus on sensational aspects of filed cases. Set aside the fact that similar stories could be (but seldom are) written about cases filed by U.S. and foreign companies before the U.S. Court of Claims. Regrettably, many critics ignore both the benefits of fair treatment of investors and how investors have actually fared under these "special rights for corporations." Consider the results of completed investment disputes. Susan Franck of Washington and Lee University Law School has carefully examined the record of investment treaty arbitration.[2] She found that investors win disputes less than half (39 percent) of the time; and when investors do win, the average award is 3 percent of claimed damages ($10 million awarded vs. $343 million claimed). Furthermore, the outcome of the arbitration was not reliably associated with the development status of the state or the presiding arbitrator. These points may not make for good sound bites, but they are extremely relevant to the judgments made by firms facing the decision about whether to enter arbitration if they believe a state has breached its treaty obligations. This also helps explain why arbitration cases are rare: the majority of BITs in force have never had a single dispute filed.

Current U.S. policy wasn't formulated in private or without public feedback: to the contrary, the core principles of investor protection have been subject to two recent reviews. The first began in the George W. Bush administration, following the passage of the Trade Act of 2002 and resulted in the 2004 Model BIT. The second review was launched in 2009 by the Obama administration and concluded with the 2012 Model BIT. Extensive public consultation was a part of both reviews. Both reaffirmed longstanding U.S. policy that strong protection is in the U.S. interest.

There is likely an older disagreement behind the criticisms: about whether investment deserves protection in the first place. Many claims about BITs and investor-state dispute settlement (ISDS) cannot withstand scrutiny. Foreign investors are not granted "special rights": the U.S. legal system guarantees all, Americans and foreigners alike, the right to protect themselves from unfair government actions. Arbitration is not "access to secret tribunals": it's a normal feature of a wide array of commercial contracts and, in the context of investment treaties, has the benefit of depoliticizing the process versus the state-to-state alternative.
The domestic debate over trade has become weighed down by claims about "special rights for corporations," when the fundamental issue is about the rule of law, which has benefits for everyone but lacks a durable constituency to speak up for it. U.S. investment policy offers substantial benefits to the economy; those who are more secure and prosperous because of it should take note, and let their views be known.

2. Susan D. Franck, "International Investment Arbitration: Winning, Losing and Why," *Columbia FDI Perspectives*, no. 7 (June 15, 2009), http://www.vcc.columbia.edu/files/vale/print/Susan_Franck_Perspective-Final.pdf.

The Forgotten Person—School Lunch Programs

PAUL NADEAU

The *Wall Street Journal* recently ran a story explaining why school cafeterias in the United States can no longer serve tuna to students. The Department of Agriculture requires school lunches to follow a "buy American" policy, and StarKist is the only producer that qualifies under unusually restrictive rules. It catches its tuna in Southeast Asian waters on U.S.- and foreign-flagged ships and processes (skin, gut, debone, etc.) and cans the product in American Samoa. Two competitors, Bumble Bee and Chicken of the Sea, catch tuna in the same waters as StarKist, and their value chains extend to California-based processing and canning operations, yet their products do not qualify as "made in USA." When the Food and Drug Administration found that StarKist tuna fell short of health standards, rather than turn to another producer, tuna was taken off the menu entirely.

There's a lot to unpack from this story—local content requirements, rules-of-origin designations, and more. But this case and others like it demonstrate how "trade" disputes often exist to provide cover for commercial rivalry, complete with congressional representatives weighing in for their constituents. As usual, it's consumers—in this case school-age children—that bear the cost of the dispute.