The 2012 US Model BIT and What the Changes (or Lack Thereof) Suggest about Future Investment Treaties

Lise Johnson

In April of this year the US State Department released a new version of its model bilateral investment treaty (BIT). This text, like the various models the US has used over roughly the past 3 decades, represents the US’s basic policy position when it starts negotiations on investment treaties with other countries, and is therefore an important benchmark for the outcome US investors might hope for as a result of ongoing and potential future talks with countries such as China, Russia, and India.

Overall, this new model text follows the approach taken by the US in its investment treaties over at least the past decade, indicating the US’s continued satisfaction with both its undefeated record as a respondent state in investor-state arbitrations, and the protection its investment treaties have given to US investors abroad. The rather few changes that have been made appear to reflect efforts to address concerns triggered by relatively recent developments such as the growth of investment into and from China and the global financial crisis, as well as more persistent issues regarding whether and how to reconcile investment treaties with national and international policies on environmental and labor standards.

Developing the New Model

The Obama Administration launched its formal review of the 2004 Model BIT in early 2009. That the revised text was not adopted and released until roughly three years later reflects two key realities. For one, although investment treaties, in contrast to trade agreements, have historically failed to attract much attention outside (or even within) government circles, the treaties have now gained notoriety as rather controversial agreements that have wide ranging implications for domestic and foreign policy.

Additionally, the US government subjects its treaty policy as incorporated in its model agreements to inter-agency review, public notice and comment, and expert consultation processes to identify issues, and revise and refine the agreements accordingly through changes and clarifications.

Opinions expressed during the consultation processes leading to the 2012 Model varied widely, ranging from calls for changes that would enhance investor protections, to those that would strengthen requirements for environmental protection and promotion of labor rights, to those that would more explicitly carve out government authority and discretion from potential liability. Those looking for drastic change in any of those areas, however, are likely disappointed. Although modifications were made that can be counted as small victories by those arguing that investment treaties should do more to protect investors, explicitly shield government regulatory authority, or serve broader sustainable development goals, the 2012 Model BIT is relatively unchanged from its previous form, maintaining the balance that the 2004 text struck among investor, state, and other stakeholders’ rights and interests.

This continued endorsement of the 2004 Model is notable because when that version was adopted, it departed in significant respects from the previous versions. Changes that were made in the 2004 version primarily (though not exclusively)
included those that were made to be more, rather than less, protective of governments’ regulatory authority and discretion. The modifications included those that:

- clarified and narrowed the definition of covered investments;
- changed and added language to explain and constrain the meaning of the “minimum standard of treatment” and expropriation obligations and closely guide arbitral tribunals’ interpretations of those provisions;
- provided for exceptions to the agreements’ prohibitions on performance requirements;
- codified the stance adopted by the US government in other areas of international law and some earlier investment treaties by expressly declaring that the essential security exception is self-judging;
- added language to protect host-state authority to take measures relating to financial services; and
- modified some aspects of investor-state dispute settlement, such as adding a statute of limitations, and giving state parties to the treaty additional or clearer authority to determine issues of treaty interpretation and application that would be binding on investor-state tribunals.

Some aspects of the 2004 Model also aimed to address issues of broader public concern. These included, for example, language expressly giving investor-state tribunals authority to accept submissions from amicus curiae and providing for public disclosure of information regarding the disputes; articles on labor rights and environmental protection; and text in the preamble clarifying that investment protection aims to improve living standards and should be pursued consistent with the protection of health, safety, and the environment, and the promotion of internationally recognized labor rights.

Together, the amendments, additions, and clarifying provisions in the 2004 Model BIT differentiated and continue to differentiate it from the more skeletal models and treaties of many other states, particularly European countries.

The 2012 Model: What changed and what stayed the same

As noted above, much of the 2004 Model remains intact in the 2012 text. Some of the more controversial features that were left untouched include provisions allowing for investor-state arbitration, which critics of that system have advocated eliminating; language requiring governments to provide investors the “minimum standard of treatment,” which representatives from the business community argued should be strengthened to provide more investor protection and others argued should be clarified so as to ensure adequate policy space for governments; and an article broadly precluding (with some exceptions) restrictions on transfers of capital that some have argued too tightly tie governments hands in responding to or avoiding financial crises.

Thus, although not satisfying all, the 2012 Model signals the Obama Administration’s approval of how the 2004 text and the treaties based on it have balanced the potentially competing goals of protecting US individuals and firms when they invest abroad, allowing government officials the appropriate freedom to design and implement legitimate public policies, and addressing broader concerns implicated by the treaties, including issues of labor rights and environmental protection.

Nevertheless, the 2012 US Model BIT does contain some new features falling into three broad categories: modifications that impose additional burdens and restrictions on host states in order to facilitate and protect foreign investment; provisions that add slight protections for government authority in the area of financial services regulation; and new language on environmental and labor issues that may better address and help avoid some of the possible negative effects that can be associated with foreign investment.

**Modifications to Facilitate International Investment**

The first category of changes includes those that add and clarify obligations of host countries and are ostensibly designed to make it easier for investors to establish and successfully operate their investments abroad. They consist of new provisions on transparency, performance requirements, and state-owned enterprises (SOEs).

With respect to the transparency provisions, the 2004 Model had imposed on state parties the duty to publish in advance, “to the extent possible,” any laws, regulations, procedures, and administrative rulings of general application that they proposed to adopt if those measures were related to issues covered by the treaty. It also required state parties to provide each other and “interested persons” a reasonable opportunity to comment on the proposed measures. The 2012 Model retains those
provisions, and supplements them by regulating the timing and manner in which governments are to disclose and accept comments on their proposed measures. The new requirements also obligate governments to publicly disclose their responses to “significant, substantive comments” received regarding proposed measures, and to publish the purpose and rationale behind the measures that are adopted. Notably, however, these new requirements do not apply to all measures proposed by all government officials or agencies; they only apply to relevant proposed regulations of general application that are issued by the central or federal level of government.

Other provisions on transparency and government regulation that the 2012 Model adds specify that host governments must allow individuals and entities from the other treaty party to participate in the host countries’ development of standards and technical regulations, as well as development of procedures to assess compliance with those standards and regulations. Host governments must also allow such participation by foreign investors on the same terms as permitted for their domestic citizens and firms. Nevertheless, there are certain carve-outs and exceptions to these requirements. In particular, the 2012 Model clarifies that they only apply to standards, technical regulations, and conformity assessment procedures developed by central government bodies; do not apply in connection with the supply of a service; and do not apply to purchasing specifications that are used by government bodies in connection with their own consumption and production. The requirements also do not apply to certain food safety or other measures taken to protect human, animal and plant life or health.

As under the 2004 Model, none of the provisions on transparency are subject to investor-state dispute settlement.

The second of the three business facilitation developments in the 2012 Model is additional language on performance requirements. New clauses explicitly bar host countries from requiring that foreign investors use or not use specific technology when such requirements are imposed in order to protect the host countries’ domestic investors, investments, or technologies. Here as well there are exceptions, including exceptions for requirements that are imposed in connection with government procurement or when necessary to protect human, animal, or plant life or health.

The third change in the business facilitation category is a new provision on SOEs. It simply clarifies that those enterprises, like government agencies and state- or provincial-level government officials, must comply with the treaties’ requirements when exercising authority delegated to them by the government.

These changes appear to reflect concerns raised by US business interests regarding challenges they have faced when investing abroad. Yet they do not represent the full set of modifications advocated by those who hoped the 2012 Model BIT would provide stronger investor protections than the 2004 or 1994 models. Nevertheless, they are not insignificant additions. From the host countries’ perspective, it may, for example, be particularly costly in terms of time and resources for developing countries to craft and implement the expanded transparency provisions called for in the 2012 Model; and from investors’ perspectives, such provisions may greatly increase the ease of doing business in host countries.

New Provisions for Governments Regulating their Financial Services

A second development in the 2012 Model is additional provisions clarifying and providing procedural and substantive protections for states regulating financial services. One procedural change allows respondent states in investor-state arbitrations to ask tribunals for an early determination of whether challenged measures are covered by specific exceptions relating to regulation of financial services and monetary policy. Another change in the 2012 Model clarifies that the treaty should not be construed to prevent state parties from adopting or enforcing certain measures relating to financial institutions, including those that are necessary to prevent deceptive and fraudulent practices in financial services.

Yet overall, and despite a number of calls for more significant reforms to protect government authority to regulate in this area, these changes from the 2004 Model are rather modest. Similar to the government’s decision to leave the previous model’s provisions on free transfers of capital untouched, the lack of significant change here seems to indicate that the US Government believes its current investment treaties (with their self-judging essential security exceptions) reserve to it sufficient authority to regulate financial services and develop and implement monetary policies.
**Strengthened Provisions on Protection of the Environment and Labor Rights**

The final category of notable change in the 2012 Model BIT is the addition of stronger language seemingly designed to ease concerns that foreign investment and investment treaties come at a cost to strong environmental protection and labor rights. The 2012 Model, for instance, replaces the requirement that state parties “strive to ensure” they do not waive or derogate from environmental and labor standards in order to promote investment, with the stronger mandate that state parties simply “ensure” that they do not do so. The new environmental text also explicitly recognizes that state parties have the right to exercise discretion in terms of implementing environmental policies and regulations. This could potentially be important in shielding states from claims that selective enforcement actions are inconsistent with state parties’ non-discrimination obligations.

The labor provisions are similarly further updated and strengthened by, among other changes, broadening the scope of covered “labor laws” to include those relating to freedom from discrimination, and including a clause through which state parties reaffirm their obligations under instruments of the International Labor Organization.

In terms of enforcement, a treaty party must engage in state-state consultations regarding issues arising under the environment and labor articles if the other treaty party so requests. But apart from those consultation requirements, the articles on the environment and labor in the 2012 Model (as under previous versions) are not subject to state-state or other mechanisms of dispute settlement, arguably weakening the potential force of these provisions.

**Remaining Uncertainty: Carve-outs, issues of contention, and annexes and protocols**

Even though the US is negotiating with countries such as Australia and India, dissatisfaction with the current system of investor-state arbitration is mounting among a number of states including Australia and India, countries with which the US is or may soon be negotiating bilateral or multilateral agreements, raising questions of whether the US will be able to successfully incorporate that dispute settlement mechanism in all of its future investment treaties. Even among states that have not formally renounced investor-state arbitration, there appear to be increasing concerns regarding state signatories’ ability (or inability) to ensure that tribunals adjudicating investor-state disputes give the treaties the meaning intended by the state parties. These concerns, in turn, may be prompting states to consider expressly reserving more power for themselves in terms of interpreting and/or applying all or part of the treaties.

Adding to those pressures from states, discontent with the current practice of investor-state dispute settlement also appears to be rising from the main beneficiaries of that mechanism, the investors, who have complained about the length and costs of proceedings, and difficulties in enforcing awards. Whether and how these issues manifest themselves and are resolved in future treaties are open questions and developments to be watched.

Other open questions arise from the fact that US treaty practice from long before and through the 2012 Model has been to use different annexes to carefully sculpt the scope of the agreements. For example, the US uses these annexes to exempt certain existing measures, future measures, industries, sectors, and policy areas from the treaties’ prohibitions on discriminatory conduct and performance requirements. Actions taken by local US authorities, for instance, are typically flatly excused from having to comply with provisions barring them from favoring domestic investors or from imposing performance requirements. Countries negotiating with the US may incorporate similar reservations and exceptions, the precise content of which cannot be predicted based on the model, but which may have a significant impact on the meaning of a treaty for a given investor or investment.

Other annexes or protocols not referred to in the 2012 Model but that, based on existing treaty practice, may likewise be developed in the context of specific negotiations include those that clarify treaty standards, govern specific issues such as treatment of sovereign debt, address or require evaluation of the possibility of institutional reform of investor-state dispute...
settlement, and set forth requirements on investment promotion or other assistance. These additions—not reflected in the 2012 Model—can nevertheless be crucial for defining and assessing the potential costs and benefits of the agreements for the state parties and their investors.

In sum, the 2012 Model suggests where the US is heading in terms of its future investment treaties, indicating that the country will continue trying to balance the myriad complex interests arising from its dual role as a recipient and source of foreign investment. Nevertheless, the text still leaves much open to question, keeping attention focused where activity is now intensifying: i.e., developments in ongoing and future negotiations with India, China, Russia, and other countries.

Lise Johnson is the Lead Investment Law and Policy Researcher at the Vale Columbia Center on Sustainable International Investment (VCC), a joint center of Columbia Law School and the Earth Institute. The views expressed by her do not necessarily reflect the opinions of VCC, Columbia University, or its partners and supporters.