Investment Treaties, Investor-State Dispute Settlement and Inequality: How International Rules and Institutions Can Exacerbate Domestic Disparities

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Introduction

Over roughly the past four decades, government officials from around the world have been erecting a framework of economic governance with major–but under-appreciated–implications for intra-national inequality. The components of this framework are thousands of bilateral and multilateral treaties designed to protect international investment. In many jurisdictions, the treaties have been concluded without public awareness or scrutiny or even much discussion or analysis by government officials – including those officials responsible for negotiating the agreements (Poulsen 2015) – and without an adequate understanding of how these agreements could affect intra-national inequality. Long imperceptible, the size and power of this framework for economic governance has increasingly become apparent. And governments continue to expand and entrench the framework through the negotiation of several new bilateral and multilateral agreements, including the Trans-Atlantic Trade and Investment Partnership Agreement between the European Union and the United States, the agreements China is negotiating with the United States and European Union, and the Regional Comprehensive Economic Partnership (RCEP) agreement being negotiated by sixteen countries throughout Asia and the Pacific.

International investment treaties, in short, protect multinational corporations from suffering losses due to government actions, or even government failures to act. Corporations that are wholly or partly foreign-owned can use investment treaties to sue their "host" governments for laws, regulations, court decisions, or other actions the governments take or do not take. Companies covered by investment treaties include, for example, the internationally dispersed corporate families of oil companies exploring for, extracting, or selling fossil fuels; pharmaceutical companies conducting research, manufacturing drugs, holding patents, and/or marketing or selling products; companies invested in providing water services; banks making investments and providing services; media companies; and any other variety of manufacturing and services firms that have established overseas affiliates.

There are various ways in which international investment treaties (often referred to as "international investment agreements" or IIAs) providing these protections to multinational corporations could impact inequality. In principle, they could potentially reduce inequality. For one, a key stated objective of the treaties is to promote cross-border investment by covered firms.

Those cross-border investment activities could establish operations and inject capital into areas where they are badly needed, spurring economic growth, job creation, and wage increases. To the extent that these treaties can catalyze cross-border investment activity, increasing the pay of low income workers, or increasing the tax revenue that can be used to redistribute wealth, they could help combat intra-national inequality.

Additionally, IIAs could combat intra-national inequality due to a common rule shared by most of those 3000 agreements, barring governments from discriminating against foreigners. That rule against discrimination could be used by foreign-owned companies to help challenge the nepotism and cronyism that elites within a country can use to concentrate market power and wealth within their networks (Justino and Moore 2015). IIAs, which give foreign investors and the companies they own powerful rights to enforce the treaties' rules, could be used to unlock opportunities and make market participation more equal.

But there are also worrying ways in which IIAs may exacerbate intra-national disparities between haves and have-nots in legal, political, and economic terms. Other chapters in this book have examined how the investment liberalization rules in IIAs can lead to inequality. But there are additional mechanisms through which IIAs can increase intra-national inequality in social, economic, legal, and political terms. This chapter focuses on two: the potential for IIAs to increase inequality by (1) providing unequal procedural rights for protection of wholly or partially foreign-owned firms, providing them greater power than other stakeholders both with respect to relations with the host state government, and in connection with disputes with other private parties; and (2) providing those foreign firms greater substantive standards of protection that strengthen the legal force of their economic rights and "expectations," with potentially negative impacts on competing rights and interests held by others. This chapter provides a sketch of each of these two channels, with particular reference to circumstances in the United States.

Brief Overview of IIAs – Features and Rationale

The substantive protections promised to covered companies in IIAs are broadly consistent across the more than 3000 treaties that have been negotiated. The agreements typically

> (1) prohibit host states from discriminating against partially or wholly foreign-owned companies (which this chapter refers to simply as multinational enterprises or MNEs);
> (2) require host states to provide MNEs "fair and equitable" treatment;
> (3) require governments to pay prompt, adequate and effective compensation for MNEs or MNEs' assets that they expropriate; and,
> (4) as other chapters in this book have highlighted, prevent host states from restricting MNEs' abilities to transfer capital in and out of the country.

IIAs also give MNEs powerful rights to sue their host states for alleged violations of treaty obligations, and seek compensation for breach. MNEs are able to pursue these claims through arbitration before a panel of three private, party-appointed arbitrators. This method of dispute settlement, typically referred to as "investor-state dispute settlement" or "ISDS," is a crucial defining feature of the international investment protection framework discussed in this chapter, and strengthens the force of investment protection treaties' substantive legal provisions.[1]

One key justification given for concluding these IIAs is that they are needed to protect MNEs from disadvantages suffered in host countries due to the MNEs' foreignness. There are concerns that MNEs doing business abroad lack voting power in those jurisdictions, and that foreign-owned businesses may be discriminated against in favor of locally owned firms. IIAs, it is argued, compensate for those vulnerabilities by giving MNEs special protections, which in turn may make MNEs more willing to invest their capital abroad. In this sense, IIAs can be seen as instruments that level the otherwise unequal playing field between foreign and domestic economic actors within a given country, minimizing MNEs' concerns about discrimination and political risk, and facilitating the cross-border capital flows and technology transfers that can be so crucial for advancing broad-based sustainable development.

Yet, as this chapter argues, that depiction of IIAs as equalizers needs to be challenged. As an initial matter, as arbitral tribunals have interpreted IIAs, actual "foreignness" is not a prerequisite to protection. Tribunals have extended IIAs' protections to firms in the host state that are beneficially owned by individuals or enterprises of that host state. In other words, tribunals have permitted individuals and firms from Country A to route their investments through holdings overseas in Country B, and send them back into Country A as "foreign"-owned firms. Country A's individuals and enterprises with the means and knowledge to do so can adopt this "round-tripping" strategy in order to benefit from protections offered under IIAs that are more favorable than protections otherwise offered to citizens and firms under Country A's domestic laws.[2] Indeed, the "approach to corporate nationality illustrated by [some ISDS decisions] encourages the use of round-tripping structures in developing and emerging markets" (Nougayrède 2015, 340). While not discussed at length in this chapter, this is "at cross purposes with global initiatives in favor of transparency and against corruption, money laundering and tax avoidance" (Nougayrède 2015, 340). Those initiatives, which can help combat intra-national inequality, may therefore be undermined by IIA rules that provide special treatment for investments made through round-tripping.

But even when an MNE is truly foreign owned, there are a number of reasons to question the premise that companies wholly or partially owned by foreign individuals or enterprises are disadvantaged in the host country and need special protections. First, an MNE may have the

[1] Under the traditional ISDS mechanism, modeled on international commercial arbitration, arbitrators are appointed by the parties and paid by one or both of the disputing parties. This leads, inter alia, to concerns that the arbitrators will be loyal to those who appoint them as opposed to being neutral decision makers; it also leads to concerns that the arbitrators have a personal interest in seeing a high number of cases, as this will help generate business income for them. Exacerbating these concerns is the fact that arbitrators typically operate free from the rules on independence and impartiality that typically govern judicial officials. The European Commission has recently been pushing for arbitration by a more permanent tribunal, which would address some of the concerns raised by party-appointed and party-paid arbitrators, but would still provide investors a private right of action to sue their host states to enforce treaty violations. (Coleman et al. 2017).

[2] See, e.g., Tokios Tokelés v. Ukraine, International Centre for Settlement of Investment Disputes (ICSID) Case No. ARB/02/18, Decision on Jurisdiction (Apr. 29, 2004); but see id., Dissenting Opinion of Chairman Prosper Weil, April 29, 2004.

same power to influence policy-making as a purely domestically owned company, if not more. Neither entity would have the direct right to cast a vote in elections; yet both, irrespective of ownership, could have equal indirect influence on policy issues that affect them through, for example, their own lobbying efforts and the positions taken and votes exercised by employees, consumers, suppliers, neighbors, and others with a stake in the firm's operations and how those operations are governed (Henisz 2016 and Freeman et al. 2010).

Second, foreign-owned MNEs are more likely than domestic firms to move their operations out of the country, and can potentially use their relative mobility to gain bargaining power over their host governments (Aisbett and Poulsen 2016). Third, foreign-owned MNEs may be able to leverage their home governments and/or international financial institutions to encourage or pressure host countries to provide the companies favorable treatment. Fourth, foreign-owned MNEs may be even more closely connected to the political elite in the host country than domestic firms. And fifth, foreign-owned MNEs may be more experienced than domestic firms in using "highly skilled negotiators and lobbyists to ensure favorable government treatment in host states" (Aisbett and Poulsen 2016, 5).

Even if discrimination against MNEs were common at a time when the "global economy could much more easily be divided along national lines" and the nationality of different companies was clear, the modern era of globalization and liberalized capital flows has changed that picture (Lester 2016, 214 and UNCTAD 2016, 182). Domestic companies traditionally considered as "national champions" linked closely with domestic identity and prosperity are now often wholly or partially foreign-owned. Moreover, a firm that is popularly considered to be of or tied to its "home" country may conduct major segments of its activities and book large parts of its profits overseas. These new patterns have highlighted questions about the need and basis for distinguishing between foreign and domestic firms. (UNCTAD 2016).

To the extent governments are drawing distinctions between domestic and foreign firms, the trend among governments is to compete for foreign capital, not discriminate against it. Governments, for example, often offer incentives and establish investment promotion agencies in order to attract foreign-owned companies, and provide those firms dedicated "after-care" services designed to help keep them in the country. Indeed, some studies have shown that governments treat foreign-owned firms better than domestically owned companies (Aisbett and Poulsen 2016 and Huang 2003). Others have found that governments treat multinational corporations–whether domestic- or foreign-owned–better than purely domestic firms with no international affiliates (Aisbett 2010). Examples of discrimination against foreign-owned firms today, therefore, may be more myth than reality.

Furthermore, with the ability to structure firms across national lines and to access specialist advice from lawyers and consultants, MNEs (which may include those domestic firms involved in "round-tripping") can identify and take advantage of benefits that purely domestic firms cannot. These include benefits derived from using corporate affiliates to book profits in low tax jurisdictions, engage in trade mispricing and regulatory arbitrage, and take advantage of international tax treaties (Nougayrède 2015). Based on these practices, MNEs can pay less in taxes than their domestic counterparts. MNEs are also able to strategically locate assets outside a host state's borders in an effort to shield those assets from creditors seeking to secure payment for tax, environmental, or other liabilities. Given these modern realities and benefits enjoyed by MNEs, the case for extra special treatment for these entities through IIAs is far from self-evident.

Yet even if there were discrimination against MNEs justifying enhanced supranational protection, the solution could be much more limited than is currently provided for in IIAs. For foreign-owned MNEs to have equal protection under the law and before courts would simply require domestic and international rules preventing discriminatory treatment.[3] But IIAs typically do much more than merely require host states to grant MNEs the same rights and the same access to the same judicial remedies as domestic individuals and enterprises. Rather, IIAs require host states to provide MNEs certain standards of treatment that are often more favorable than treatment to which domestic individuals and entities are entitled. And it is this differential treatment that can undermine intra-national equality. The next section looks at how IIAs provide uniquely powerful *procedural* rights for MNEs as compared to (a) other private individuals and entities under international law, (b) governments under domestic law, and (c) other private individuals and entities under domestic law. The following section then highlights how IIAs provide MNEs privileged substantive property rights and economic power relative to other private stakeholders, creating and exacerbating inequality.

IIAs and unequal procedural rights for MNEs

In their IIAs, host states give MNEs the extraordinary power to bring ISDS claims against them in order to challenge, and seek compensation for, government conduct that breaches the IIAs' provisions. As this section explains, the power to bring ISDS claims to challenge government conduct negatively impacting MNEs is uniquely strong, as compared to the powers of other private actors under both international law and domestic law. These asymmetries in power to initiate legal action and claim relief, standing alone, are examples of inequality before the law. And, even more importantly, ISDS tribunals can then shape the substantive contours of the law in a way that generates even more inequality.

Extraordinary power under international law

ISDS is a fundamental departure from traditional practice under international law. Traditionally, only states have had the power to enforce other states' international law obligations. Only member states of the World Trade Organization (WTO), for example, are entitled to use the WTO's dispute resolution system to allege other WTO treaty parties have violated their WTO commitments and to seek remedies for breach of WTO law. Most other treaties follow this same

[3] There may be certain valid grounds for distinguishing between firms based on ownership. A number of countries have special rules and restrictions on foreign ownership for national security reasons. The presence of those rules, however, does not necessarily imply an absence of rights or remedies for improper discrimination. When, for example, U.S. President Barack Obama ordered a U.S. firm owned by Chinese nationals to sell certain assets in the US following an evaluation of the firm's investment by the Committee on Foreign Investment in the United States (CFIUS), U.S. courts were open to the firm to challenge the CFIUS process and the President's decision. The Appeals Court for the District of Columbia declared that the process and resulting decision were unconstitutional violations of the Chinese-owned company's due process rights. Ralls Corp. v. Committee on Foreign Investment in the United States, et al., No. 1:12-cv-01513 (D.C. Ct. App. July 15, 2014).

model. The terms of the treaties might benefit private individuals and corporations, but they do not provide those actors direct rights of actions to enforce the treaties' provisions.

Some international human rights treaties adopt a different approach. Under these human rights instruments, individuals and, in some cases, corporations,[4] are able to initiate claims against governments for violating their human rights. Nevertheless, there are limits on the abilities of those private actors to challenge government conduct. One key limit is the requirement that those seeking to challenge government conduct first exhaustively pursue relief through the domestic legal system. Accordingly, allegedly wrongful legislation, administrative actions, or judicial decisions of lower courts would typically need to be challenged through the judicial system before those measures or decisions could be challenged at the international level as violations of international law. Only once this requirement to exhaust domestic remedies is satisfied can private actors ask international human rights tribunals to adjudicate their claims and provide relief. This exhaustion requirement provides opportunities for governments to correct wrongs, and narrows the scope of measures that can and will give rise to international claims.

IIAs' provisions on ISDS depart from both of those approaches and give MNEs extraordinary privileges under international law. In contrast to the general norm in international law that only states may enforce other states' treaty obligations, MNEs are able to initiate ISDS proceedings to challenge a host state's breach of IIA standards. This, in turn, creates hundreds of thousands of potential claimants with the power to police compliance and seek remedies.[5] Moreover, unlike in international human rights law, arbitral tribunals have relatively consistently ruled that MNEs bringing ISDS claims are not required to first exhaust their domestic remedies. This means that MNEs are able to challenge a broad set of administrative, judicial and legislative measures before international arbitral tribunals. If they prevail in their claims, MNEs are also able to use other treaties for the enforcement of international arbitral awards to ensure governments comply with the decisions issued against them.[6] Thus, in international law, MNEs are uniquely positioned to be able to sue governments in supranational fora for the governments' breach of their treaty commitments, and enforce decisions issued in their favor.

Substantive protections given to MNEs are therefore more easily enforceable than other rights and interests–including human rights–that are protected under international law. One potential consequence of that disparity in enforcement regimes is that it will prompt governments to devote more resources to ensuring compliance with obligations regarding treatment of MNEs than to ensuring compliance with obligations owed under human rights or other treaty instruments. Another potential consequence is that, if there are tensions or arguable conflicts between observance of different treaty obligations (e.g., conflicts between protection of human rights and adherence to MNE protection standards), host states may favor adherence to the MNE

[4] Legal entities such as corporations are recognized as having rights under the European Convention on Human Rights. Other international human rights bodies, such as the Inter-American Court of Human Rights and the African Court on Human and People's Rights, however, only permit claims by natural persons.

[5] These claimants are the hundreds of thousands firms that have been established around the world, and even the various shareholders in those firms. (UNCTAD 2016; Gaukrodger 2014).

[6] These treaties are the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards, and the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of other States.

protection obligations on the basis that breach of those obligations would be more likely to trigger litigation and financial liability.

Thus, the exceptional nature of ISDS in international law threatens to result in disproportionate host government attention being paid to the rights and interests of MNEs as compared to the rights and interests of other stakeholders under international law.

Extraordinary power to challenge government action

The ability of MNEs to initiate ISDS proceedings is similarly exceptional as compared to the ability of private individuals and entities to challenge government conduct under many domestic legal systems.

Domestic jurisdictions typically employ various doctrines that both permit and restrict government exposure to litigation and liability for different types of conduct. Comprehensive immunity of governments to lawsuits is critiqued on the ground that it prevents accountability and facilitates–and even encourages–negligent or knowingly wrongful conduct. When a government erects a legal framework enabling it to act with impunity, people are right to be concerned. But this is not to say that any person or entity aggrieved by any type of government conduct should have a right to challenge that conduct, and to seek compensation or other relief as a remedy. Broadly allowing individuals and entities to contest any government action or omission that negatively impacts their rights or interests, or the rights or interests of others, could unduly tie the hands of governments seeking to adopt and enforce important measures taken in the public interest. Ultimately, excessive exposure to claims and liability could grind governments to a halt.

Decisions on whether and in what circumstances to (1) impose liability on governments and (2) compensate individuals or entities for harm, can have important behavioral impacts, incentivizing certain types of conduct and discouraging others. When shaping liability and compensation regimes, it is crucial to assess and understand those effects, and ensure that claims and remedies are designed to send the right signals and advance desired outcomes. Additionally, it is important to assess how availability of claims or remedies (or absence thereof) may be unequal in design or effect. Erecting systems that, whether in law or in practice, grant certain actors heightened powers to challenge governments can chill important regulatory policy or grant remedies for harms that only injure those actors' interests.

Based on these and other factors, domestic jurisdictions often have myriad rules on claims against the government. These rules relate to policy questions such as: which entity of government is best suited to make the appropriate determination of whether conduct is or is not lawful or appropriate (e.g., should courts make the ultimate decision on wrongfulness, administrative officials with technical expertise, legislators, or executive officials)? Should courts or administrative tribunals be able to revisit other government entities' decisions, and if so, through which procedures? What impact will allowing claims or allowing certain types of remedies have on future government performance and/or for redress to victims? Who can bring claims (e.g., those who have been directly harmed, or anyone with an interest in the outcome of an issue)? What types of harms should be actionable through a legal challenge (e.g., economic losses; losses to property; infringements of personal liberties; or government abdication of duties)? And what types of remedies should be available (e.g., monetary compensation, punitive damages, changes in the relevant law or policy)?

All domestic individuals and firms, who are *not* covered by IIAs, are bound by these rules as defined by that domestic jurisdiction. Those who are covered by IIAs, however, can either bring their claims to domestic forums subject to these rules, or bypass such domestic legal restrictions by bringing their claims under IIAs and through the ISDS system, in which such domestic procedural restrictions do not apply. Under some IIAs, MNEs can even pursue relief through domestic channels *and* ISDS simultaneously.[7]

Giving MNEs access to ISDS and the ability to sidestep domestic restraints on litigation gives MNEs greater power than non-MNEs to challenge government action and inaction. Even before an ISDS claim is filed or ISDS decision reached, the mere fact that MNEs alone have recourse to ISDS can potentially cause the government to devote greater attention and accord greater deference to the preferences and interests of MNEs than the government otherwise would; and, in some cases, this heightened attention will be to the detriment of competing preferences and interests (Van Harten and Scott 2017).

If, for instance, a government decision to issue a permit would be opposed by environmentalists, and a decision to deny the permit would be opposed by an MNE, the agency responsible for deciding which option to pursue may be influenced by knowledge that the environmentalists could not mount a lawsuit challenging the government's decision but that the MNE could sue the government for vast sums through ISDS. Similarly, when administrative and judicial enforcement of consumer protection laws are opposed by industry but supported by consumer advocates, governments may be influenced by the fact that the decision to prosecute a violator could trigger an ISDS claim by the firm, but a decision not to do so would not be challengeable by citizens the law was designed to protect. An ISDS suit by an MNE may, therefore, negatively impact the rights and interests of the MNE's competitors, consumers, employees, and creditors. More diffuse interests, such as those who benefit from or ideologically support the environmental, labor, tax, antitrust or other government policy, may also be negatively impacted by an MNE's use of ISDS to challenge relevant government conduct.

As one commentator has explained when discussing the ability of different stakeholders to sue administrative bodies and challenge regulations, the type of inequality in procedural powers that is inherent in ISDS has

> fundamental and insidious impacts on the law-generating process as well. Government agencies do not want to spend time and resources defending regulations in court. If one side of the regulatory equation generally has standing to sue, and the other side does not, agencies are likely to favor the side that can sue them in their rulemaking decisions to

[7] To the extent foreign or domestic stakeholders dislike these rules limiting litigation in a given legal system, those stakeholders can, in at least some systems, seek to change them through legislative, administrative, and/or judicial action. See, e.g., supra, n. 3 (discussing *Ralls* case).

avoid the expenditure of resources necessary to defend regulations in court, the negative publicity, and disappointment inherent in having regulations struck down (Coplan 2009).

Giving MNEs–and MNEs alone–such broad and privileged access to "judicial" review through ISDS is especially problematic in an era in which political legislative and executive branches of government are already disproportionately attentive to (or captured by) wealthy individuals and corporate interests (Andrias 2015; Drutman 2015, 71; Gilens and Page 2014; and Stiglitz 2012). Gilens' analysis of federal legislative activity in the United States, for example, finds evidence that the "political system is tilted very strongly in favor of those at the top of the income distribution," (Gilens 2012, 70) and that legislative responsiveness to the policy preferences of the middle class and poor in the United States are "virtually nonexistent," except when those preferences happen to align with the preferences of the top 10 percent in terms of income (Gilens 2012, 83). This outsized influence of the wealthy over government action, in turn, produces economic inequalities among constituents. Political scientists have highlighted how political decisions are creating and entrenching economic inequality through the issues they prioritize, and those they do not (Hacker and Pierson 2010; Andrias 2015). To combat those trends of wealth influencing politics and politics further generating wealth inequality, judicial review of government action can play a key role.

Indeed, the judicial branch of government has come to be seen by many commentators and theorists as the branch that is the most insulated from the influence of powerful, wealthy stakeholders (Schlozman and Tierney 1986), and the branch that is therefore best-placed to address and remedy the weighty influence that wealthy individuals and firms can have over legislative, executive, and administrative decisions (Andrias 2015; Schiller 2000; Peterson 2014). Consequently, that only MNEs (and their investors) are able to challenge government conduct through ISDS, in which disputes are removed from domestic courts to private arbitration by party-appointed arbitrators, can further strengthen the influence of wealthy individuals and industry over government decision-making, exacerbating domestic inequality.

There are several additional characteristics of IIAs and ISDS that make MNEs' unique access to arbitral tribunals extraordinarily powerful and intensify concerns that ISDS will worsen, not ameliorate, wealth's influence over lawmaking. One is that, in contrast to most advanced systems of corporate law, IIAs have been interpreted to allow direct shareholders–including even minority, non-controlling shareholders–to bring ISDS claims seeking compensation for harms to the company in which they hold shares (Gaukrodger 2014). Additionally, many IIAs permit (or have been interpreted to permit) claims by shareholders in MNEs up the ownership chain such as claims by intermediate holding companies and ultimate beneficial owners. Thus, when a measure affects a single MNE within its borders, a government may face a number of ISDS claims from that firm's various direct and indirect shareholders.[8]

When a government measure impacts a whole industry, the number of potential claims and claimants multiplies. Each separate claim will likely require the state to incur additional defense

[8] While some treaties attempt to address these issues by requiring consolidation of certain claims, or by only allowing controlling shareholders to bring claims seeking relief for harms to the company in which they hold shares, those treaties are few in number and do not offer complete solutions to the problems they seek to address.

and arbitration costs,[9] which, at an estimated USD 5 million per case per side, are significant (Hodgson 2014).[10] And, MNEs who lose their ISDS claims are only infrequently ordered to compensate states for their legal expenses (in 38 percent of the cases that MNEs lose), less frequently than the percentage of cases in which tribunals require losing states to compensate successful MNEs for their legal expenses (53 percent of cases in which states lose) (Hodgson 2014, 756).

As well as increasing states' defense costs, multiple claims also give MNEs multiple chances to win their claims. MNEs can advance different arguments and/or appoint different arbitrators with the hope that their arguments prevail in at least one of their cases. Because there is no system of precedent in ISDS arbitration binding one tribunal to decisions previously issued by another, the fact that some shareholders lose before one arbitral tribunal does not prevent other shareholders from bringing a case against the same government challenging the same measure, or from subsequently prevailing.[11] Thus, when a government seeks to shift policies in an industry where there are multiple firms with at least some foreign shareholders, that government may face a veritable barrage of ISDS litigation and potential liability, a risk that further increases the leverage of MNEs in their negotiations and disputes with host governments. Given these issues, it is foreseeable, if not expected, that firms will increasingly organize themselves, and shareholders will increasingly structure their holdings, so as to ensure that when governments act or fail to act in their interests, they can mount ISDS claims to contest or secure damages for that conduct.

Extraordinary power to challenge the rights and interests of non-MNEs

In addition to giving MNEs greater power than non-MNEs vis-à-vis the government, ISDS also gives MNEs greater power than non-MNEs in legal disputes directly between those two groups.

Assume, for example, that a domestic citizen successfully sues an MNE in the courts of the host country for harms caused by the MNE, and is awarded monetary compensation for injuries suffered. The MNE may then be able to turn to ISDS to seek to undo or otherwise eliminate the effects of its court loss. In contrast, if the MNE were to have prevailed in the domestic court proceedings, the domestic citizen would have no similar power to seek a different outcome through ISDS. With access to ISDS, MNEs thus have greater opportunities to get their desired results than their non-MNE opponents do.

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[9] States may be able to consolidate claims brought by different investors, which can minimize defense costs. Nevertheless, even if the effort to consolidate is successful, that effort itself will likely result in additional arbitration-related expenses.

[10] Hodgson found the defense costs for respondent states to average USD 4.5 million, plus the state's portion of the tribunal's costs, which averaged USD 750,000.

[11] For examples of cases involving the same investment, and same government conduct, but brought by different investors and coming to different conclusions see, e.g., (1) CME v. Czech Republic, UNCITRAL, Award, September 13, 2001, and Lauder v. Czech Republic, UNCITRAL, Award, September 3, 2001; and (2) Teco v. Guatemala, ICSID Case No. ARB/10/23, Award, December 19, 2013, and Iberdola Energía v. Guatemala, ICSID Case No. ARB/09/5, Award, August 17, 2012.

One example of a case following this pattern is *Chevron v. Ecuador*.[12] That dispute arose out of a lawsuit in which Ecuadorian citizens sued Chevron for pollution caused by oil operations in the Ecuadorian Amazon. An Ecuadorian court sided with the Ecuadorian plaintiffs, who are commonly referred to as the "Lago Agrio Plaintiffs" due to the location of the oil operations, and ordered Chevron to pay them roughly $18 billion in damages (which was reduced by an Ecuadorian appellate court decision to $9 billion). In order to avoid having to pay the Lago Agrio Plaintiffs that award of compensation, Chevron initiated an ISDS case against Ecuador.

In the ISDS proceedings, Chevron argued that the Ecuadorian legal processes that produced the award were marred by government corruption and collusion between the Lago Agrio Plaintiffs and judicial officials. Chevron also argued that, even if there were no fraud or corruption, "the Lago Agrio Judgment's factual findings, legal holdings, and assessment of damages are so unjust" that they constitute a denial of justice in breach of the IIA.[13] As part of that position, Chevron disputed a number of findings made by the Ecuadorian courts on issues such as the extent of environmental damage in the Amazonian region, the cause of contamination, and the crucial question of who is legally responsible to pay for harms done.

Through its ISDS case, Chevron asked for a number of remedies that would directly impact the Lago Agrio Plaintiffs and their ability to obtain compensation for environmental harms. Chevron, for example, asked the arbitral tribunal to declare that "Chevron is not liable for any judgment rendered in the Lago Agrio Litigation,"[14] and that the Lago Agrio judgment itself is a "nullity as a matter of international law,"[15] is "unlawful and consequently devoid of any legal effect,"[16] and is "not final, conclusive or enforceable."[17] Chevron also requested that the tribunal "order Ecuador to use all measures necessary" to prevent the Lago Agrio Plaintiffs from collecting their award of compensation.[18]

As of December 15, 2016, the ISDS dispute was still pending. Nevertheless, the arbitral tribunal issued an interim award granting Chevron's request to order Ecuador "to take all measures necessary….whether by its judicial, legislative or executive branches….to suspend or cause to be suspended the enforcement and recognition within and without Ecuador of [the Lago Agrio judgment]."[19]

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[12] Chevron Corp. v. Ecuador, Permanent Court of Arbitration (PCA) Case No. 2009-23.
[13] Chevron Corp. v. Ecuador, PCA Case No. 2009-23, Claimants' Supplemental Memorial on Track 2, para. 104 (May 9, 2014).
[14] Chevron Corp. v. Ecuador, PCA Case No. 2009-23, Claimants' Memorial on the Merits, para. 547 (September 6, 2010).
[15] Chevron Corp. v. Ecuador, PCA Case No. 2009-23, Claimants' Supplemental Memorial on Track 2, para. 199 (May 9, 2014).
[16] Chevron Corp. v. Ecuador, PCA Case No. 2009-23, Claimants' Supplemental Memorial on Track 2, para. 199 (May 9, 2014).
[17] Chevron Corp. v. Ecuador, PCA Case No. 2009-23, Claimants' Memorial on the Merits, para. 547 (September 6, 2010).
[18] Chevron Corp. v. Ecuador, PCA Case No. 2009-23, Claimants' Memorial on the Merits, para. 547 (September 6, 2010).
[19] Chevron Corp. v. Ecuador, PCA Case No. 2009-23, Second Interim Award on Interim Measures, para. 3(i) (February 16, 2012).

Thus, though Chevron's case was principally against Ecuador, it also sought to, and succeeded in, impacting the outcome of the underlying litigation between Chevron and the Lago Agrio Plaintiffs. It also succeeded in impacting the answer to the question of who pays for environmental harms caused by oil operations: those affected by the pollution, taxpayers, and/or oil companies. Under the tribunal's order, the costs of those harms will continue to be born by affected individuals and communities, not by Chevron or Ecuador.

Although affected by the tribunal's award, the Lago Agrio Plaintiffs have had no right or ability to participate in the ISDS proceedings in order to dispute Chevron's claims and protect the judgment they had fought for years to secure. ISDS is limited to claims by MNEs (or their investors) against their host states; treaties concluded to date do not permit third-parties to intervene in and join the arbitrations even if the subject of the arbitration or the arbitration itself, as in the *Chevron v. Ecuador* dispute, impacts those third-parties' rights or interests. By only allowing investors to access ISDS, and excluding full participation by affected third-parties, IIAs give rise to inequalities in procedural rights. These procedural inequalities, in turn, can exacerbate substantive inequalities such as inequalities in terms of who suffers from, who benefits from, and who pays for environmental damage.

Another example of a dispute in which the loser in domestic court proceedings turned to ISDS for relief is *Eli Lilly v. Canada*.[20] That ISDS case arose out of litigation between a generic drug company and Eli Lilly regarding the validity of two pharmaceutical patents held by Eli Lilly. When the generics company sought to manufacture and sell generic versions of Eli Lilly's patented drugs, Eli Lilly sued it for patent infringement. But the generics company prevailed, permitting it and other generic drug manufacturers to sell their versions of the drugs in Canada.

Having lost in Canada, Eli Lilly turned to ISDS under the North American Free Trade Agreement (NAFTA). In contrast to the ISDS case initiated by Chevron, Eli Lilly did not allege that there was any corruption, fraud, or breaches of due process in the underlying Canadian judicial processes. Rather, Eli Lilly alleged that Canada's courts had developed new patent law doctrines that improperly imposed new, heightened, and arbitrary requirements for patentability on firms, and that the change in requirements - and the requirements themselves- violated the NAFTA. According to Eli Lilly, the decisions by Canadian courts invalidating Eli Lilly's patents entitled Eli Lilly to at least CDN $500 million as compensation for what it claims was a wrongful interference with its intellectual property rights.

As in *Chevron v. Ecuador*, Eli Lilly attempted to use ISDS to secure a different outcome than had resulted from private litigation in the host country. It asked the arbitral tribunal to declare that the substantive contours of Canadian patent law violated the NAFTA. And again, due to how IIAs have structured ISDS, the generic drug company that had been involved in the underlying Canadian litigation could not be party to the ISDS arbitration, despite the fact that the case centered on the validity of the decisions on Canadian patent law that the generics firm had successfully fought for and secured.

[20] ICSID Case No. ARB/14/2.

Eli Lilly thus further illustrates how ISDS can provide one party in domestic litigation with extra procedural avenues to prevail over its opponent. Although Eli Lilly did not directly ask the arbitral tribunal to undo or prevent enforcement of the Canadian court judgments, the relief Eli Lilly sought–an order requiring Canada to compensate Eli Lilly for loss of its monopoly rights and other companies' use of "its" patents–could have made it cost prohibitive for Canada to uphold those court decisions.

Ultimately, Eli Lilly lost its NAFTA case. The tribunal decided that Eli Lilly had failed to prove that the shift in Canada's intellectual property laws was sufficiently dramatic or arbitrary to violate the NAFTA. Nevertheless, the arbitrators declared that it was entirely proper for ISDS tribunals to reevaluate the outcomes of domestic court cases between private litigants even in the absence of any denial of justice or evidence of corruption in those proceedings.

Cases like *Eli Lilly* have weighty public policy implications regarding incentives for and abilities of individuals and firms to innovate, the extent of openness and competition in a given market, and the pricing of medicines and other products. For example, strong patent protections such as those sought by drug developers convey monopolistic power on patent holders, which can in turn impact the relative strength and success of other firms who develop or manufacture products (e.g., favoring innovative drug companies holding patents over generics firms seeking to produce the patented technologies). Disproportionately strong patent protections also exacerbate inequality among individuals in terms of their ability to access healthcare and other goods and services derived from patented innovations (Liu 2014; Chang 2012). Consequently, ISDS may reshape the substantive contours of the law in a manner that generates more inequality among both producers and consumers.

Chevron and *Eli Lilly* underscore how ISDS grants MNEs a formidable and privileged procedural mechanism, and how investors' use of that procedural mechanism to get one more "bite at the apple" may create or exacerbate substantive inequalities between, on the one hand, MNEs and their shareholders and, on the other hand, all other stakeholders. Other ISDS cases illustrate the breadth of the problem. Investors have used ISDS to contest decisions regarding the relative rights of creditors and debtors in bankruptcy proceedings,[21] contests over land ownership,[22] citizen suits challenging permitting decisions for extractive industry operations,[23] and other unfavorable litigation proceedings and outcomes between the MNEs and other private individuals and entities before domestic courts.

Treaties could be drafted in such a way as to preclude investors from using ISDS to alter the effect of domestic litigation with other private parties. They could, for example, contain language stating that a case must be dismissed if there are individuals and entities whose interests would be affected by the ISDS proceedings, but who are nevertheless not able to join them. Treaties could also contain language giving those whose interests may be affected by the proceedings the

[21] See, e.g., Dan Cake v. Hungary, ICSID Case No. ARB/12/9, Decision on Jurisdiction and Liability, August 24, 2015.
[22] See, e.g., Awdi v. Romania, ICSID Case No. ARB/10/13, Award, March 2, 2015.
[23] See, e.g., Infinito Gold v. Costa Rica, ICSID Case No. ARB/14/5, Request for Arbitration, February 6, 2014, and Petition for Amicus Curiae Status, September 15, 2014.

right to join the arbitration as full parties (though this would potentially require them to have to incur the costs of investment arbitration, which on average have been estimated to be US$10 million per case and might not be feasible for all to pay) (Hodgson 2014). Such provisions can be found in procedural rules of domestic courts in order to prevent court decisions from overriding the rights and interests of those who are not party to the case.[24]

Even absent such express language, tribunals could also arguably invoke existing principles of international law to decline to hear cases or order relief that would impact the rights of non-parties. To date, however, tribunals have not appeared receptive to these issues or arguments. In *Chevron v. Ecuador*, for example, Ecuador argued that, pursuant to principles of international law, the tribunal should not take jurisdiction over Chevron's claims or grant its requested relief as doing so would impact the rights of the Lago Agrio Plaintiffs.[25] The tribunal, however, rejected that argument, declaring with little analysis that its hearing of the case would not impact the rights of the Lago Agrio Plaintiffs, and then issued the interim award preventing the Lago Agrio Plaintiffs from collecting their award of compensation.[26]

IIAs and unequal substantive property rights

Particularly because property rights are a zero-sum game in which "protecting the resource claims of some parties requires preventing others from using those same resources," (Lawson-Remer 2012, 151) decisions on their definition and scope are a product of a rich history and ongoing contestation (Kennedy 2011, 10). Distributions of economic, social, and political power shape property rights; and, in turn, property rights can shape those distributions of power (Kennedy 2011, 12).

Traditionally, international law has left domestic jurisdictions–and the social forces, political processes, and legal institutions within them–significant latitude to define the scope of property rights and allocate them among members of society (Sasson 2010). To the extent that international law has been relevant to protection of property, it has largely been confined to assessing whether states have violated extant or vested property rights in breach of customary international law or treaties protecting human rights (Sasson 2010).[27] Thus, international law has generally not defined or created property rights; rather, it has limited state interference with them.

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[24] See, e.g., US Federal Rules of Civil Procedure, R.19.

[25] See, e.g., Chevron v. Ecuador, Third Interim Award on Jurisdiction and Admissibility, paras. 3.83-3.85, 3.139 (February 27, 2012); Chevron v. Ecuador, Respondent Track 2 Counter-Memorial on Merits, paras. 516-525 (February 18, 2013).

[26] Chevron v. Ecuador, Third Interim Award on Jurisdiction and Admissibility, paras. 4.59-4.71 (February 27, 2012); Chevron v. Ecuador, Second Interim Award on Interim Measures, para. 3 (February 16, 2012).

[27] But see, e.g., Nigel Bankes, "Protection of the Rights of Indigenous Peoples to Territory through the Property Rights Provisions of International Regional Human Rights instruments," 3 Yearbook of Polar Law 57, 66-67 (2011); see also Sasson, pp. 66-67 (discussing Anglo-Italian Conciliation Commission, *Raibl* Claim, June 19, 1964, 40 ILR 260-288 (1970)).

IIAs, however, have changed that. Rather than merely protecting property rights as defined and redefined through domestic processes, IIAs–and, in particular, their "fair and equitable treatment" obligations[28]–have effectively become a tool for creating new property rights to be enjoyed by MNEs. These provisions, as interpreted, limit the ability of governments to take action that interfere with those IIA-created rights, and diminish the property rights of other stakeholders, undermining efforts to reduce inequality.

Creating New Substantive Rights through the "Fair and Equitable Treatment" Standard

IIAs require host states to provide MNEs "fair and equitable treatment (FET)." But, fundamentally, protecting MNEs' conceptions of what is fair and equitable may have unfair or inequitable impacts on others. For example, environmental laws imposing new and costly emissions standards on manufacturing plants may be viewed as unfair or inequitable from a firm's perspective unless those laws exempt existing plants that had long operated under more lax regimes and for which compliance costs would be high. But exempting such older, existing facilities would be unfair and inequitable from the perspective of those individuals living near the polluting plants who are left to disproportionately suffer the harms of air pollution from unregulated facilities (Gorovitz Robertson 1995). And are measures that provide special exceptions or flexibilities to environmental laggards fair and equitable from the perspective of manufacturing firms that voluntarily incurred costs to upgrade their facilities in anticipation of future regulation? Similar questions about the equities and inequities of law arise with respect to taxation, labor law and employee benefits, social services, tort law, and myriad other areas.

A danger with IIAs and ISDS is that they expressly only seek to ensure fair and equitable treatment of MNEs and their owners, with no meaningful opportunity for those who may be unfairly or inequitably impacted by MNEs' calls for fair and equitable treatment to present their views to tribunals. Of course, the FET obligation could be interpreted in a manner in which fairness to MNEs takes into account fairness to others; but there are no guarantees arbitral tribunals will adopt such a holistic vision of fairness. Indeed, cases decided to date suggest otherwise.

In fact, in their interpretations of the fair and equitable treatment standard, tribunals have been effectively creating new property rights for MNEs through their pronouncements that IIAs' FET obligation protects MNEs' "legitimate expectations." Specifically, arbitral tribunals interpreting and applying IIAs have created a legal doctrine through which they will protect certain expectations held by foreign investors regarding future government treatment, and will order host states to pay compensation if actual government conduct deviates from those expectations. Arbitral tribunals thereby effectively convert mere expectations regarding treatment of foreign-owned firms into legally recognized rights enforceable against the state.

The expectations that have been effectively turned into legally enforceable property rights are extremely diverse, including the right to continue to enjoy government subsidies,[29] the right to be

[28] Also relevant are tribunals' interpretation of the indirect expropriation standard. This paper, however, focuses on the FET obligation and its role as a tool for creating new property rights.
[29] Micula v. Romania, ICSID Case No. ARB/05/20, Award, December 11, 2013.

free from having to pay higher taxes,[30] the right to be awarded permits for activities such as developing hazardous waste sites,[31] the right to enjoy certain rates of return in public infrastructure projects,[32] and the right to have tariffs for public services (e.g., water or energy) determined in accordance with particular investor-approved formulas or at levels "expected" by the investors.[33] In none of these cases was the "expectation" held by the MNE clearly recognized as a "right" under the host country's domestic legal framework. Rather, the existence and nature of those rights were contested due to questions regarding the scope of the state's power to adjust economic benefits and burdens, or effects on those holding competing interests or rights claims.

For example, in *Micula v. Romania*,[34] a dispute regarding foreign-owned firms' alleged right to receive government subsidies, Romania contended that the MNEs had no vested right to continue to receive subsides in future years and that the government had the power to terminate those supports. Romania further argued that recognizing a right to continued receipt of subsidies would be inconsistent with applicable law and policy restricting government grants of subsidies due to concerns that such subsidies could result in welfare-reducing effects on competition, constituted a waste of government resources, and were an inappropriate transfer of wealth from taxpayers to select private interests.

The arbitral tribunal in the *Micula* case determined that it need not decide whether or not Romanian law had created and conferred on the MNEs' property rights to continue to receive government subsidies. Nor did the tribunal engage with the concerns underlying the government's efforts to terminate subsidies deemed to be inconsistent with policy aims, or the question of whether, based on those concerns and policies, the MNEs might have expected their government benefits would end. Instead, the tribunal decided that the MNEs had "legitimate expectations" that they would be able to continue to benefit from those subsidies and that the government's decision to terminate the subsidies violated those expectations. The tribunal then ordered the government to pay the value of those future subsidies as compensation.

The arbitral tribunal therefore effectively created and conferred on the MNEs and their investors the right to continue to receive government subsidies (at the expense of other Romanian taxpayers and business competitors). The tribunal also undermined the power of Romania's legal and political institutions to determine whether MNEs had such a right to receive government subsidies and, if so, on what terms. Arbitral tribunals in ISDS proceedings have assumed the role of identifying which economic interests are recognized and protected by the law and have assigned themselves the power to erect a property rights framework that can depart from norms established in domestic legal systems through constitutions, legislation, court decisions, or other channels. By converting investors' and MNEs' "legitimate expectations" regarding their economic activities into enforceable property rights, and requiring the state (taxpayers) to

[30] Perenco v. Ecuador, ICSID Case No. ARB/08/6, Decision on Remaining Issues of Jurisdiction and Liability, September 12, 2014.
[31] Tecmed v Mexico, ICSID Case No. ARB(AF)/00/2, Award, May 29, 2003.
[32] Walter Bau v. Thailand, UNCITRAL, Award, July 1, 2009.
[33] Teco v. Guatemala, ICSID Case No. ARB/10/23, Award, December 19, 2013.
[34] ICSID Case No. ARB/05/20, Award, December 11, 2013.

compensate investors for loss of those "rights," tribunals effect a transfer of wealth from the public to investors and MNEs.

Whose expectations are protected?

According to tribunals, "legitimate expectations" can arise from the general legal and regulatory framework in place at the time an investor makes its investment, especially when those expectations are based on government officials' representations or assurances to investors.

Those with the strongest claims to favorable "legitimate expectations," therefore, are those who have had direct communications with presidents, ministers, or other often high-level government representatives and have received promises or other encouragements regarding prospects for the investments and advantages offered by the host state's legal and businesses environment. These MNEs are frequently companies developing or operating major infrastructure projects for water, energy, and transportation services; firms engaged in exploration for and extraction of oil, gas, or minerals; and businesses constructing or operating major real estate or tourism projects. In short, companies that have the best claims to "legitimate expectations" are often firms that have benefitted from a closeness with government that most individuals and entities will never enjoy. This widens the gap between the power of those with the ear of the government and those without.

What expectations are "legitimate"?

ISDS decisions have held that investors' "legitimate expectations" based on government representations or assurances must be upheld even if those representations or assurances were non-binding or illegal under domestic law.[35] If, for instance, an executive official were to represent to a foreign-owned firm that the contract terms the MNE sought for an infrastructure project were acceptable, but a court later deemed the relevant contract invalid under the constitution or other domestic law, the firm may be able to prevail on an ISDS claim that the court decision violated its "legitimate expectations" of benefitting from the contract. Through that approach, the ISDS decision would effectively allow the executive official's representation to prevail over broader domestic legal norms.

Binding the government to (or requiring compensation for) unlawful, non-binding, and often non-public representations or commitments can upset normal separation of powers by effectively giving executive officials the ability to knowingly or negligently override or bypass limits set by the legislature. Moreover, enforcing such unlawful or unauthorized promises can encourage improper collusion between the project proponent and those in the government that support the

[35] Fraport AG Frankfurt Airport Services Worldwide v. Republic of the Philippines [II], ICSID Case No. ARB/11/12, Award, December 10, 2014, paras. 482-519; Railroad Development Corporation v. Republic of Guatemala, ICSID Case No. ARB/07/23, Second Decision on Objections to Jurisdiction, May 18, 2010, para. 146; Desert Line Projects LLC v. Republic of Yemen, ICSID Case No. ARB/05/17, Award, February 6, 2008, para. 120; Fraport AG Frankfurt Airport Services Worldwide v. Republic of the Philippines [I], ICSID Case No. ARB/03/25, Award, August 16, 2007, para. 346 (subsequently annulled on other grounds). MTD Equity Sdn. Bhd. v. Chile, ICSID Case No. ARB/01/7, Award (May 25, 2004).

proposed investment. Assume, for instance, that executive officials want to give a project proponent a broad guarantee of fiscal stability in order to encourage the project's development but, to preserve tax policy flexibility over time and to ensure tax policy is set by the legislature, those executive officials do not have authority under domestic law to provide any commitment that fiscal policies will remain unchanged. The doctrine of "legitimate expectations" means that the executive officials could nevertheless agree to a contractual stabilization clause, knowing that, once given, that contractual promise might become too costly to break.

In some domestic legal systems, courts protect against such collusive conduct by imposing strict rules against enforcement of unauthorized or illegal promises. As stated by the U.S. Supreme Court, for example, when affirming the U.S. rule that legal force will not be given to illegitimate representations by agency officials:

> If agents of the Executive were able, by their unauthorized oral or written statements to citizens, to obligate the Treasury for the payment of funds, the control over public funds that the [Constitution] reposes in Congress [governing appropriation of funds] in effect could be transferred to the Executive. If, for example, the President or Executive Branch officials were displeased with a new restriction on benefits imposed by Congress …. and sought to evade them, agency officials could advise citizens that the restrictions were inapplicable. [A legal doctrine binding the government to the officials' advice] would give this advice the practical force of law, in violation of the Constitution.[36]

Yet not only does the doctrine of "legitimate expectations" in ISDS reject that approach, favoring protection of investors' reliance interests over protection of the rule of law in the domestic legal system, but the doctrine of "legitimate expectations" could also result in an IIA breach if domestic courts, like the U.S.'s, were to refuse to enforce illegal promises. If a domestic court ruled that the fiscal stabilization provision was invalid, the MNE could bring an ISDS suit challenging that court decision as a violation of its expectations.

Recourse to ISDS also gives rise to another opportunity for improper collusion between investors and certain government officials and a mechanism to disrupt the balance of governmental powers. The executive branch which, in many countries, has control over decisions regarding litigation and settlement of ISDS claims, could simply agree as part of a settlement to abide by an unauthorized or illegal stabilization commitment in order to dispose of the case and entrench its policy preferences regarding fiscal stabilization. That settlement agreement can then be enshrined as an "award" by the ISDS tribunal, which would make it binding on the host country even if the terms of the agreement were illegal under that country's domestic law.

Even apart from any intentional corrupt collusion in settlement discussions conducted outside normal law-making processes, there are serious questions about whether and under what circumstances negotiated settlements adequately reflect the interests of all those with a stake in the litigation. Because governments serve diverse constituents with different and potentially competing interests, it may be difficult if not impossible for the government to equally and fully

[36] Richmond v. Office of Personnel Management, 496 U.S. 414, 428 (1990).

represent all views when litigating and settling cases.[37] The perspectives of some constituents– particularly those who are politically weak–may therefore not be taken into account by government positions when the government is seeking to dispose of a case.

In light of those risks and realities, at least some domestic jurisdictions have developed rules and mechanisms under domestic law to ensure that government settlements represent broader public interests and are consistent with the law, and to enable stakeholders to directly protect their interests in court. These include mechanisms allowing interested individuals and entities to intervene in disputes between the government and other private parties and challenge terms of settlement agreements; and rules requiring the judicial branch to assess whether settlement agreements are in the public interest before approving them. ISDS, however, contains no such mechanisms for third-party intervention or public interest oversight. Consequently, given the often "numerous complex and conflicting interests" at the local, regional, and/or national level that a state sued in an ISDS case may be responsible for defending, there is a real risk that the interests of the most marginalized "may become lost in the thicket of" or sacrificed in "sometimes inconsistent governmental policies."[38]

Assume the following fact pattern: an MNE seeking to develop a coastal tourism project secured a concession from national-level officials for that project and was told that the land was government-owned and not inhabited by others. Local residents, however, claimed ownership of the land and argued that, under domestic law of eminent domain, the land could not be expropriated from them to be given to another private party. The local residents then filed and succeeded on a claim before domestic courts that the concession was in fact improperly granted, and the court ordered termination of the concession. After the court award, the MNE brought an ISDS claim challenging the decision and seeking (1) an order from the tribunal mandating the government to take all steps necessary to prevent enforcement of that domestic court judgment; or (2) hundreds of millions of dollars in damages from alleged lost future profits. Indeed, there are many actual examples of tribunals similarly ordering governments to interfere in judicial proceedings or outcomes,[39] as well as ordering governments to pay hundreds of millions of dollars in future lost profits for frustrated projects.[40]

Whether because it wants the tourism project to go ahead, does not want to risk an adverse judgment and potential liability for hundreds of millions of dollars, or does not want to face the reputational costs and potential lost-future investment that an ISDS claim can bring, (Alee and Peinhardt 2011) the government entity responsible for defending the case may opt to settle the case and allow the development to proceed notwithstanding the competing rights and interests of the local citizens. If that settlement agreement is then reflected in an arbitral award, the government could argue that its international law obligations trump domestic law decisions, and

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[37] U.S. cases in support of this principle include Utah Association of Counties v. Clinton, 255 F.3d 1246, 1255 (10th Cir. 2001); Kleissler v. United States Forest Service, 157 F.3d 964, 973-974 (3rd Cir. Ct. App. 1998); Am. Farm Bureau Fedn v. United States EPA, 278 F.R.D. 98 (M.D. Pa. 2011). For a discussion of some of these issues, see Michael T. Morley, *Consent of the Governed or Consent of the Government? The Problems with Consent Decrees in Government-Defendant Cases*, 16 U. Pa. J. Const. L. 637 (2014).
[38] Kleissler v. United States Forest Service, 157 F.3d 964, 973-974 (3rd Cir. Ct. App. 1998).
[39] See supra nn. 12-19, 25-27 (discussing Chevron v. Ecuador).
[40] See, e.g., Gold Reserve v. Venezuela, ICSID Case No. ARB(AF)/09/1, Award, Sept. 22, 2014.

that therefore the domestic court decision is invalid or preempted, undermining the rights of the affected communities.

In summary, because the doctrine of "legitimate expectations" provides disproportionate protection to those with unique access to government officials, and can bind governments to promises irrespective of whether those promises are authorized or legal, that doctrine allows MNEs to distort law in their favor without having to secure support necessary for legislative or constitutional change.

Using "legitimate expectations" to protect the status quo

Protection of MNEs' "legitimate expectations" is particularly favorable to existing asset holders and powerful interests, compensating them for changes to the status quo. The general rule adopted by tribunals is that the doctrine of "legitimate expectations" protects expectations held at the time the investment is made, including that the legal framework governing or affecting an MNE will not change over time (or will not change much)[41] through court decisions, administrative actions, shifts in policies or practices, changes in legislation or other means of legal evolution.

If subsequent government conduct exceeds the MNE's "legitimate expectations," granting more favorable treatment than the MNE had anticipated at the time of the investment, then the MNE keeps those gains; but if the government frustrates the investor's expectations, the government may be ordered to compensate them for any difference between their hoped-for and actual economic position.

One likely effect will be that, over time, the legal and policy framework will become increasingly favorable to MNEs. Because IIAs typically only permit investors to initiate claims against states (neither states nor other individuals or entities may initiate IIA claims against MNEs), the outcomes of ISDS decisions will only ever be to (1) *uphold* the property rights framework as they existed under the host state's domestic law, or (2) *expand* the property rights protections enjoyed by investors under that law. ISDS proceedings will never narrow the property rights enjoyed by MNEs under host state law. Thus, beyond the specific effects that protection of "legitimate expectations" has in a particular case, the structure of the ISDS system is such that, over time, it will lead to a general expansion of the legal protections for MNEs' economic interests, and corresponding expansion of state (taxpayer) liability for conduct interfering with those interests.

This effect of protecting the status quo against change that negatively impacts MNEs can also entrench or increase inequality among firms by safeguarding the power of market incumbents as compared to new players. If, for example, a government decides to remove or decrease subsidies given to existing businesses (e.g., coal-fired power plants), and/or increase subsidies given to potential new competitors (e.g., generators of renewable energy), that may trigger an ISDS claim for breach of the FET obligation by the incumbents. Similarly, if the government passes new

[41] See, e.g., Tecnicas Medioambientales Tecmed S.A. v. Mexico, ICSID Case No. ARB(AF)/00/2, Award, para. 154 (May 29, 2003).

environmental or other obligations that would impose new costs on firms, it may readily agree to exempt incumbents from having to comply so as not to trigger a dispute, thereby favoring incumbents relative to newcomers.

In addition to disadvantaging those competitors without access to ISDS, the ability of MNEs to entrench favorable aspects of the status quo harms other interests that would benefit from adjustments to law and policy. As one scholar studying the powerful impact of money in slowing US lawmaking has concluded, "[w]ealth interests affect inaction disproportionately and benefit from it uniquely" (Andrias 2015, 425-26). Indeed, FET provisions are not the only forces against change. Scholars studying legal trends have found a general status quo bias limiting legal reform in democratic states (Gilens and Page 2014, 74 and Hacker et al. 2015, 183) and political scientists have identified the phenomenon of drift, through which vested, non-majoritarian interests can work behind the scenes to prevent voters and other public interests from updating the legal framework to take into account changing circumstances (Hacker et al. 2015, 184). Thus, inequality-entrenching policy stagnation appears to be a reality even in the absence of IIAs and ISDS, though IIAs and ISDS provide new and powerful channels for counteracting legal and policy adjustments.

Notably, MNEs have relied on FET protections to prevent legal systems from evolving to combat three of the most inequality-inducing effects that can arise from property rights systems– negative externalities, abusive practices of monopoly rights holders, and undue appropriation of gains. The first, negative externalities, result from property rights holders seeking to maximize gains from their uses of property by pushing costs onto others (Merrill 2012). A typical example of this is a company that, when producing a product for sale, generates harmful pollutants and is able to dispose of those pollutants in the air, in water, or on land owned by the general public who will then suffer the harms and bear the costs of such pollution. The second negative effect property rights protections can generate is the risk of abuse of monopoly powers through which the holder of a monopoly right can extract onerous payments from those seeking to use or benefit from that right. One example of this is when a pharmaceutical company holds a patent over a life-saving drug for which there are no substitutes, and for which the company can therefore charge sick patients an exorbitant price; another example is when a company has a monopoly over the right to distribute and sell water, and can set high prices for that essential resource without fear of losing consumers to competitors. A third negative consequence that systems of property rights protections can produce is a direct increase in inequality that can arise when systems allow the rights-holder to appropriate all of the gains in value attributable to the right it holds (Merrill 2012). This aspect of property rights systems through which "property beget[s] more property" can be positive in that it can "create an incentive for the owner to work hard to make the resource" it holds "productive and valuable" (Merrill 2012, 2093). Yet always allowing property rights holders to uniquely capture all of the gains from the property they hold can also lead to growing inequality. As Merrill has described:

> [N]ot all gains in the value of resources are attributable to the skill and industry of the owner. Some will be due to rising market demand for resources generally; others will be due to sheer luck…The portion that can be attributed to luck or general conditions of scarcity represents a kind of built-in multiplier, whereby those that have property get more property without regard to their individual effort or desert (2093).

Problematically, government efforts to address each of those negative and inequality-exacerbating effects of property rights systems can be–and have been–successfully challenged under IIAs. Investors have used ISDS to, for example, secure compensation for environmental laws and decisions that seek to minimize or avoid environmental externalities;[42] regulate tariffs or tackle anti-competitive pricing in provision of public services;[43] or limit intellectual property rights, and assess "windfall profits taxes" seeking to capture a greater share of gains derived from the rising price of natural resources (i.e., gains not derived from the investor's increased efficiency or skill).[44] These types of decisions, which are based on a relatively singular focus on MNEs' expectations, do not take into account the broader implications that such protections have for inequality.

Some scholars have argued that property law can increase equity and inclusiveness if the notion of what is protected "property" were expanded, and a greater set of interests were folded within the definition of "property" rights (Super 2013). While that may be possible, the FET standard (coupled with the ISDS system) is a particularly non-inclusive approach, permitting only MNEs and their shareholders to expand and enforce their property rights (Van Harten and Malysheuski 2016). Compounding the problem, IIAs correspondingly reduce the power of those who are excluded from or marginalized by status quo systems of property rights protections to improve their situation by "destabilizing" existing norms (Rosser 2015, 465 and Peñalver and Katyal 2010, 1). When changing property rights systems would require government action that interferes with MNEs' expectations, governments may lack the will and resources to risk IIA-based retribution.

Concluding Remarks

As described above, IIAs provide MNEs privileged access to procedural remedies and strong substantive protections that favor MNEs' property rights and expectations, creating and exacerbating inequality among a diverse group of other stakeholders. Furthermore, they allow MNEs to entrench the status quo, favoring incumbents and MNEs' interests more generally. More analysis could usefully demonstrate how these two particular channels operate in theory and practice. To what extent do claims or threats of claims result in governments devoting their time, resources and policies to the interests and needs of MNEs within their borders? To what extent do MNEs engage in roundtripping to exploit these procedural and substantive benefits? To what extent do MNEs use the extra legal route provided by ISDS to insulate themselves from the effects of generally applicable domestic law, to prevent, stall, or reshape redistributive policies, or to modify outcomes in litigation between domestic parties? A number of known ISDS cases illustrates each of these practices and effects, but the extent of the trends has not been well-

[42] See, e.g., Bilcon v. Canada, PCA Case No. 2009-04, Award on Jurisdiction and Liability, March 17, 2015.
[43] See, e.g., EDF v. Hungary, UNCITRAL, Award, December 4, 2014; Teco v. Guatemala, ICSID Case No. ARB/10/23, Award, December 19, 2013.
[44] See, e.g., Murphy Exploration and Production Co. v. Ecuador, Permanent Court of Arbitration, Award, February 10, 2017; Perenco v. Ecuador, ICSID Case No. ARB/08/6, Decision on Remaining Issues of Jurisdiction and Liability, June 30, 2011.

researched, in part because of the confidentiality of MNE-government interactions and in part of because of the challenge of isolating government motivations.

Additional research could also interrogate other channels through which IIAs might impact intra-national (and international) inequality. Relevant areas of inquiry could include research on the amount, destination, distribution, and effects of monetary compensation awarded under the treaties;[45] the impact IIA rules limiting use of performance requirements or subsidies aimed at developing economic opportunities for socioeconomically disadvantaged individuals or communities; the ways in which IIA policies are developed at the domestic level and the influence that such policy input has on policy outputs and impacts; and the effects of IIA rules requiring that host governments accept and respond to MNE input on proposed and/or actual laws and regulations. Finally, further research could explore whether and how IIAs could be enlisted as a tool to combat intra-national inequality. As the system of international economic governance is expanding, and as intra-national inequality is increasing, it is crucial to understand the links between the two phenomena and how law can be used to advance, and not undermine, equality.

[45] Research could build, for example, upon Gus Van Harten and Pavel Malysheuski, Who Has Benefitted Financially from Investment Treaty Arbitration? An Evaluation of the Size and Wealth of Claimants, 12 Osgoode Hall Law School Legal Studies Research Paper Series, Research Paper No. 14 (2016). Additional research could, for instance, trace the ultimate destination of compensation (e.g., to the firm itself, owners in the host country, owners in the home country, or owners in a tax haven).

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