Columbia Center on Sustainable Investment
A JOINT CENTER OF COLUMBIA LAW SCHOOL AND THE EARTH INSTITUTE, COLUMBIA UNIVERSITY

Columbia FDI Perspectives

Perspectives on topical foreign direct investment issues

No. 216 January 1, 2018

Editor-in-Chief: Karl P. Sauvant (Karl.Sauvant@law.columbia.edu)
Managing Editor: Matthew Schroth (mas2443@columbia.edu)

IIA provisions, properly interpreted, are fully consistent with a robust regulatory state*

by

Kenneth J. Vandevelde**

Because the explosion in the number of bilateral investment treaties (BITs) began at the end of the 1980s, contemporaneously with the emergence of the "Washington Consensus," identifying BITs with neoliberal market fundamentalism is tempting. And, because neoliberal market fundamentalism favors a minimalist state, the identification of the BIT network with that ideology often triggers concerns that BIT obligations intrude too much upon a host country's regulatory discretion, concerns exacerbated by the fact that investor-state claims alleging BIT violations first appeared soon after the Washington Consensus.

The provisions of contemporary international investment agreements (IIAs), however, trace their origins not to the neoliberalism of Ronald Reagan and Margaret Thatcher, but to the New Deal liberalism of Franklin Roosevelt and Harry Truman. Nearly all of the provisions that commonly appear in IIAs have antecedents in the 22 US postwar treaties of friendship, commerce and navigation (FCNs), concluded by the US between 1946 and 1966. These treaties reveal the vision of international economic law that gave birth to the very concept of an investment treaty and the original understanding of the key provisions that appear in most IIAs today.[1]

At the end of World War II, the Roosevelt-Truman administrations sought to promote outward US investment to provide other countries with the dollars needed for reconstruction and development and to purchase an anticipated US manufacturing surplus. One important means of promoting outward investment was to negotiate treaties for its protection.

US officials believed that Roosevelt's New Deal provided a model for the right investment climate. The New Deal had promoted economic growth through a combination of free enterprise and state capitalism, while allowing the government to regulate the economy in the public interest, subject to basic rule-of-law norms found in the US constitution. Thus, in crafting the investment provisions of the post-war FCN treaties, the US sought to obtain for her investors abroad essentially the same protections that they and foreign investors already received in the US. These protections were entirely consistent with the New Deal regulatory state, while

providing a legal framework within which investment could flourish and, in the US, had flourished.

An interagency working group developed a foreign investment policy that called for measures both to protect and to regulate international capital movements. The group eventually came to realize, however, that investment regulation would need to occur primarily at the national level and concentrated on securing investment protection through international agreements. After failing to achieve the goal of investment protection through the negotiation of investment provisions in the International Trade Organization Charter, and after choosing not to adopt a proposed bilateral treaty devoted solely to investment protection, the State Department decided that FCN treaties, which the US had been concluding since 1778, would provide the principal means for securing investment protection. By the end of the 1940s, the US had reconceived the FCN treaties as "investment treaties," although they retained their commercial and maritime provisions for several reasons, including the belief that investment promotion would best occur in a framework of broader economic relations.

In 1959, Germany and Pakistan concluded the first bilateral treaty dedicated solely to investment protection. Both countries had already concluded FCN treaties with the US, Pakistan only weeks before. In the 1960s, the Belgium-Luxembourg Economic Union, Denmark, France, Italy, the Netherlands, Norway, Sweden, and Switzerland all inaugurated BIT programs similar to Germany's. All but the last three of these had already concluded a post-war FCN treaty with the US.

With the notable exception of the provision requiring parties to observe obligations relating to investment, virtually all the provisions in these first European BITs had antecedents in the US FCN treaties. Thus, it is in the FCN treaties that countries are seen, for the first time (in the context of an investment treaty), explicating the meaning of provisions such as the requirement of fair and equitable treatment, prohibiting unreasonable or discriminatory measures, protecting against direct and indirect expropriation, and including obligations of national and most-favored-nation treatment.

These and other IIA provisions were conceived in a framework where broad exceptions for regulatory discretion were unnecessary because the substantive provisions of the treaties, apart from special circumstances such as exchange controls, would not intrude upon legitimate, nondiscriminatory and non-expropriatory regulations in the public interest. For example, FCN treaty provisions presumed that host country assurances to investors included as an implied condition the state's reserved power to regulate. When interpreted in accordance with their original understanding, the basic rule of law provisions that appear in IIAs are fully consistent with a robust regulatory state.

Those who created the first IIAs in the 1940s had a clear vision of the balance to be struck between investment protection and regulatory discretion when they drafted provisions such as the fair and equitable treatment standard. Arbitral tribunals seeking the object and purpose of IIA provisions can find their answer in that founding vision.

---

not reflect the opinions of CCSI or Columbia University or our partners and supporters. Columbia FDI Perspectives (ISSN 2158-3579) is a peer-reviewed series.

** Kenneth J. Vandevelde (kennethv@tjsl.edu) is Professor of Law at Thomas Jefferson School of Law and the author of *The First Bilateral Investment Treaties: U.S. Postwar Friendship, Commerce and Navigation Treaties* (New York: OUP, 2017), on which this *Perspective* is based. The author is grateful to José Alvarez, O. Thomas Johnson, Jan Kleinheisterkamp, and Theodore R. Posner for their helpful peer reviews.

[1] The origins of contemporary investment treaty law in the US post-war FCN treaties are analyzed in Vandevelde, op. cit., based on a review of some 32,000 pages of negotiating history housed in the US National Archives.

For further information, including information regarding submission to the *Perspectives*, please contact: Columbia Center on Sustainable Investment, Matthew Schroth, mas2443@columbia.edu.

The Columbia Center on Sustainable Investment (CCSI), a joint center of Columbia Law School and the Earth Institute at Columbia University, is a leading applied research center and forum dedicated to the study, practice and discussion of sustainable international investment. Our mission is to develop and disseminate practical approaches and solutions, as well as to analyze topical policy-oriented issues, in order to maximize the impact of international investment for sustainable development. The Center undertakes its mission through interdisciplinary research, advisory projects, multi-stakeholder dialogue, educational programs, and the development of resources and tools. For more information, visit us at http://www.ccsi.columbia.edu.

Most recent *Columbia FDI Perspectives*

- No. 215, Karl P. Sauvant, "Beware of FDI statistics!", December 18, 2017.
- No. 214, Fabrizio Di Benedetto, "A European Committee on Foreign Investment?", December 4, 2017.
- No. 213, Perrine Toledano, Olle Östensson and Kaitlin Y. Cordes, "Parsing the myth and reality of employment creation through resource investments," November 20, 2017.
- No. 212, Stephen Kobrin, "The rise of nationalism, FDI and the multinational enterprise," November 6, 2017.
- No. 211, Mélida Hodgson, "NAFTA 2.0: a way forward for the investment chapter," October 23, 2017.

All previous *FDI Perspectives* are available at http://ccsi.columbia.edu/publications/columbia-fdi- perspectives/