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Comparing Naughty BITs

**Assessing the Developmental Impact of
Variation in Bilateral Investment Treaties**

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Peter Chowla

Development Studies Institute, London School of Economics
peter@chowla.org

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List of Abbreviations

ANOVA	Analysis of Variance
BIT	Bilateral investment treaty
ICSID	International Center for Settlement of Investment Disputes
FDI	Foreign direct investment
FTA	Free trade agreement
GDP	Gross domestic product
MAI	Multilateral Agreement on Investment
MFN	Most favoured nation
NGO	Non-governmental Organisation
TNC	Transnational corporation
TRIM	Trade-related investment measure
TRIPs	Trade-related intellectual property rights
UNCTAD	United Nations Conference on Trade and Development
UNCTC	United Nations Centre on Transnational Corporations
UNDP	United Nations Development Programme
WTO	World Trade Organization

1. Introduction

Development policy tends to go through fads, jumping from one big thing to the next (Naim 2000). From resource shortage growth models to shock-therapy liberalisation, something is always viewed as *the* ticket to wealth and prosperity for developing countries. Recently, foreign investment saw the same treatment, transitioning from *bête noir* to king of the hill when it comes to developing country economic plans. Where foreign investors had previously been shunned, they are now pursued as means of upgrading technology, infusing capital into an economy, and providing employment. To attract foreign direct investment (FDI), the developing world creates the right 'investment climate' so that investors will flock to build new projects (World Bank 2004).

Of course, there is no such thing as a free lunch. Schemes to attract investors have trade-offs. The goals of economic policy makers are, or should be in theory, to create growth for their economies. Meanwhile, the goals of investors are, indubitably, to extract rents and make profits. These two goals seldom align, leaving a gap between expectations and realisation on both sides of the investment divide.

In fact, policy makers may focus inordinately on just attracting FDI and, in the process, may be crafting policies that actually inhibit their long-run growth prospects. This paper examines such policies in the field of investment promotion and protection by investigating bilateral investment treaties (BITs). These international agreements aim to encourage investment by guaranteeing legal protections for the property rights of foreign investors. Investors feel more secure because their rights, protected by international law, can be enforced through international jurisprudence.

However, investment treaties, which exploded in popularity in the 1990s and now number more than 2,200 agreements, also have a downside. They limit the ability of countries hosting investment projects to conduct active industrial policy. They remove some of the flexibility and policy space from economic decision making by restricting

governments from regulating foreign investments. All BITs are not the same, as they are the products of intense negotiations between two governments. The standards of international law that have developed is remarkably consistent across the agreements, but there are critical differences that determine how much the host country's policy space is constrained.

Previous analyses of BITs generally treated the entire compendium of agreements equally, seeking to determine how they were affecting investment decisions or why they were entered into. However, the variation in language, some of the treaties are as short as two pages while others extend to twenty, means that a finer analysis is needed to properly assess their developmental impact. This paper makes a preliminary attempt to break down the collection of treaties and examine their component parts. It looks at the most important subset of agreements: those between high-income capital-exporting countries and low- or middle-income countries.

The results are clear, that BITs have over time become more invasive and more restrictive of developing country policies. This evidence reinforces the idea that in the bilateral negotiating realm, developing countries are at a significant disadvantage compared to bargaining in multilateral forums (Kahler 1993). While at the World Trade Organisation, developing countries have been able to resist developed country demands for investment liberalisation (Mori 2004), bilaterally BITs have liberalised investment controls and limited policy space (Correa and Kumar 2003). In the key spheres of treatment of investors, regulation of capital movements, performance requirements and dispute settlement, capital-importing countries have faced bilateral negotiations where they have little hope of gaining concessions. Two solutions present themselves: more strategic thinking about bilateral treaty partners or a multilateral framework on investment. Given the political economy of bilateral bargaining, a multilateral agreement seems to be the most promising avenue for ensuring that developing countries retain the policy space they need to bolster industrialisation.

The paper proceeds first with the context, investigating industrial policy, the trends in thinking about foreign investment and recent analyses of BITs. In Section 3, the methodology for analysing the BIT texts is presented. The findings of that analysis are presented in Section 4. Section 5 discusses the implications and possible solutions to the dilemma of restricted policy space, before concluding in Section 6.

2. Context

2.1. Industrial Policy

The developmental and economic trajectory of a country is determined by more than just the sum of labour, capital and investment, with factors such as culture and institutions playing a significant role (North 1990). In trade, classic Ricardian competitive advantage, which says that exchange benefits everyone, ignores many factors at work in the real world. Practical experience shows us that institutions are important and that dynamic competitive advantage can be created through industrial policy. Infant industry protection can create new competitive advantages by developing new capabilities, boosting technology usages, enhancing productivity and bolstering human capital. Without protection, backward countries will be trapped with static comparative advantage and never able to advance into new markets. Through industrial policy countries can develop specialities in industries with better terms of trade than basic commodities, increasing returns to scale and higher income elasticities. This type of dynamic industrial policy requires extensive policy space for economic planning and market intervention, just the kind of space that BITs often limit.

The theory of infant industry protection found its first comprehensive expression in the writings of Fredrick List. List argued that when infant industries operate in an environment with more advanced players, they must be protected; but that the protection should be temporary, targeted, and finally gradually removed as the infant industry achieves parity with other countries (Shaffaeddin 2000: 5-6). Alexander Gerschenkron's (1962) analysis of 'institutional alternatives', interventions that help backward economies catch-up, extends this theory. In cases of great relative backwardness, state action can become necessary to remedy market failures, such as imperfect capital markets, in order to close the industrial gap (Gerschenkron 1962: 17).

Infant industry protection and promotion is a tried and tested method to achieve late industrialisation. The first users of this strategy were today's modern industrial

powerhouses: the US, UK, and Germany (Chang 2002: 19-35). East Asia provides modern cases of successful nurturing of immature manufacturing sectors. The details of Taiwanese intervention in the economy are well documented by Robert Wade (1990). Likewise, Alice Amsden's (1989) detailed account of Korean industrialisation shows how activist trade policy was extensively used. China's recent burst of growth can partially thank extensive investment regulation that ensured FDI benefited the economy (Zhang 2004: 87).

The importance of using policy strategically to create wealth is the key lesson. However, the BIT movement, particularly some of the more recent and more restrictive provisions of BITs, may not be providing the flexibility that is necessary for active industrial policy. If international investment agreements are constraining poorer countries, it is important to look at the costs and benefits of such agreements and assess which parts of these treaties are the most egregious.

2.2. Foreign Investment

2.2.1. Investment and Development

Low-income countries inevitably face resource constraints in their efforts to create economic growth. Domestic savings, even if mobilised through government intervention, are usually insufficient to fund the investment that economic models say is needed for rapid industrialisation, especially given technology gaps. Of course, the Harrod-Domar model, predicting investment being proportional to growth through the capital/labour ratio, does not wholly explain the underdevelopment of the Third World, and more sophisticated models long ago replaced it (Solow 1994: 45-46). However, new endogenous growth theories also correlate investment and growth (UNCTAD 1999: 157). Developing countries need capital, and if domestic resources are lacking then capital can be tapped from four foreign sources: aid, loans, remittances and FDI.

In the first several decades after World War II, FDI was viewed as more of a problem than a solution to the shortage of resources, as transnational corporations

(TNCs) were suspected of exploiting impoverished countries, not helping them grow. With the ascendancy of economic liberalism, the view of FDI has changed, and developing countries now eagerly seek it, hoping to boost growth (Rodrik 1999; UNCTAD 1999: 157), without the negatives associated with loans or aid. Empirical evidence on the determinants of FDI is often conflicting, especially because industry preference shifts as production processes change (De Vita and Lawler 2004: 28). The most reliable indicators are per-capita GDP, trade openness, wage levels, net exports, and economic growth (Chakrabarti 2001: 108).

FDI's benefits include better economic growth, higher wages for workers, technological spillovers, improved access to high-income country markets, and balance-of-payments improvements (Milberg 1999: 109). However, FDI is an investment choice by a TNC, and the incentive to invest comes from rents that the company expects to capture in the host country. Some foreign investments are of higher quality than others, and some can even cause welfare losses for the host (Kumar 2002: 3-5). It makes economic sense for the host government to try to capture as much of those rents as possible, making FDI more beneficial for the country (Brewer and Young 1998: 19; Morrissey 2001: 66). Aside from direct rent capture, governments want to maximise the positive spillovers on human capital and technology so that FDI furthers economic development (UNCTAD 1999: 156).

Empirical studies to quantify the benefits of FDI have shown mixed results (Gallagher and Zarsky 2005: 25). The link between FDI and economic growth is not strong, and no study has demonstrated a causal relationship (UNCTAD 1999: 336). One review of the available literature showed that the direction of causation actually tends to be the opposite of what host countries hope for, namely that FDI follows growth and does not cause it (Milberg 1999: 103; Rodrik 1999). Technology transfers, spillovers and balance-of-payments improvements then become even more important if hosts are to benefit from the investment, but it is just these kinds of regulation that

some BITs now preclude.

Regulating FDI is a long-practised tradition in high-income countries. There has been wide-spread discrimination against foreigners owning assets in the US, as well as extensive use of performance requirements, joint venturing requirements, and barriers to acquisition of domestic firms (Chang and Green 2003: 3). It is not surprising that developing countries want to regulate FDI just as mature economies did. Additionally, TNCs investing in foreign markets often have large market shares and firm-specific advantages (UNCTAD 1999: 316). FDI's correlation with oligopolistic competition, makes regulation desirable (Brewer and Young 1998: 19). Another regulatory motivation is thwarting anticompetitive and restrictive practices of TNCs such as unfair transfer pricing, price fixing, and other market manipulating activities (Morrissey 2001: 67).

To create technology transfer, "linkages can be powerful channels for diffusing knowledge and skills between firms (UNCTAD 2001: 129)." Studies show that backward linkages in the economy are clearly determined by the presence of local-content regulation (Blomstrom and Kokko 1998: 13). However, the evidence for the effectiveness of local-content and export requirements is somewhat mixed. Empirical studies have found them to be both effective and inefficient, with large differences depending on the region, country, market type, industry and other specific characteristics (UNCTAD 2003: 120).

Performance requirements may only marginally effect TNC decisions on where to locate foreign investment, as agglomeration and macroeconomic factors are more important. (UNCTC 1991: 14; Wheeler and Mody 1992). Taylor (2000) has shown 'investment openness' to be important but performance requirements are only one of the nine factors that make up his index. Yet, by allowing developing countries more manoeuvrability, these requirements also strengthen the bargaining position of host countries when negotiating with TNCs. Without such bargaining chips, a host may need

to offer more incentives to attract FDI, thus lowering the developmental and economic benefits of the investment to the host country (Morrissey 2001: 65).

The ability to use performance requirements is one of the key areas of variation in BITs, as some of the treaties expressly ban them, constraining policy space. To preserve this policy space, BIT language should be closely scrutinised and strategies for promoting investment should be devised that do not compromise the long-term goal of industrialisation and economic growth.

2.2.2. Multilateral Regulation Efforts

Because developing countries now think of FDI as a very important component of growth strategies, it is not surprising that there have been several efforts to negotiate multilateral instruments to manage investment. One noteworthy attempt, began in 1977, was the UN's Code of Conduct on Transnational Corporations, It was a very comprehensive agreement, covering investment protection, technology transfer, restrictive business practices, anticompetitive behaviour and human rights. Given its progressive agenda and provisions which curtailed the freedom of TNCs, agreement was never reached (Correa and Kumar 2003).

The only successful binding multilateral investment regime is the WTO's Trade-Related Investment Measures (TRIMs) Agreement. This 1994 accord extended national treatment and quantitative restriction rules to FDI (WTO 1994; Bora 2002: 171). The real impact of the TRIMs Agreement is to prohibit FDI regulation that was formerly quite widely used, especially in Asia (Bora et al. 2000: 550). Local-content, export and trade-balancing requirements are no longer available to policy makers, leading many developing countries to resent the constraints on policy space that limit their ability to take full advantage of FDI (UNDP 2003: 239).

The most significant recent effort was the Multilateral Agreement on Investment (MAI). This agreement, under the auspices of the OECD, sought to give comprehensive protection to investments including those between developed

countries, which have so far generally fallen outside the purview of bilateral agreements. The MAI was divisive and eventually the negotiations fell apart because of irreconcilable differences over the agreement (Henderson 1999). Industry coalitions supporting the agreement lost interest when it became clear that the text would be watered down. The blame partly lies with public outcry due to advocacy work by NGOs opposed to the agreement (Walter 2001). With the exception of some free-trade agreements, no BITs have faced such resistance.

2.3. Bilateral Investment Treaties

2.3.1. Origin and Early Practice

BITs serve to protect the foreign investments of people and corporations based in countries outside of the investment location. The first BIT was signed by Germany and Pakistan in 1959. BITs were generally, though not always, signed between a capital-exporting country in the industrialised world and a capital-importing nation in the developing world.

In many ways BITs were insurance against expropriation and nationalisation for TNCs. A wave of takings of foreign investor property in the wake of independence and nationalist movements in the 1950s and 1960s prompted concern. This was bolstered by the collective stance of developing countries against the Hull Rule, an aspect of customary international law which called for 'prompt, adequate, and effective' compensation (Guzman 1997-1998: 645). Least developed countries were able to act collectively through UN resolutions in the early 1970s to change customary international law so that compensation for expropriated assets could be determined entirely by domestic law, significantly changing the climate for international investment (Guzman 1997-1998: 648-9). It was this very change that brought stronger and more enforceable rules against expropriation in the guise of BITs.

2.3.2. BIT Explosion

The number of BITs being signed exploded in the early and mid-1990s. There were nearly 2,000 BITs signed at the end of the millennium compared to just over 400 signed between 1959 and 1990, and now over 2,200 in the most recent count (UNCTAD 2005b). Despite the explosion of BITs, most studies of their impact were legal in nature, rather than economic or political. Only recently have BITs emerged as a topic for research in non-legal fields.

One of the thorniest questions is whether signing BITs actually increases in FDI. Egger and Pfaffermayr (2004) find a significant and large effect of ratified BITs on bilateral FDI flows using data from 19 home and 54 host countries, but just signing a BIT has little effect in their model. Hallward-Driemeier (2003), on the other hand, uses bilateral flows from 20 OECD countries to 31 developing countries over 20 years and finds little evidence that BIT signature or ratification increase FDI flows. Tobin and Rose-Ackerman (2005) look at whether the total number of BITs signed or ratified effects the total FDI flow into a developing country. Based on data from 62 countries, they find that BITs do not significantly increase the share of world FDI that a developing country receives. They also test bilateral flows and find that, for US treaties, signing a BIT does not lead to significantly greater FDI flows from US investors. This directly contradicts Salacuse and Sullivan's (2005) results that show US BITs serve to attract significantly more FDI, and are better at attracting it than other OECD country BITs. However their data covers only 30 countries for a 10 year period while Tobin and Rose-Ackerman cover a larger sample of 54 countries over 20 years. Finally, Neumayer and Spess (2005) find that the total number of BITs signed has a significant and positive influence on both total FDI a developing country receives and its share of global FDI that goes to developing countries.

Clearly, there is disagreement and contradiction in the research. Part of the variation is explained by differing methodologies. Some studies look at country dyads

while others look at the cumulative number of BITs and total FDI. Additionally, there are differences in the dependent variables as the various studies look at total FDI inflows, bilateral FDI inflows, FDI inflows as a share of global FDI and FDI inflows as a share of global FDI going to developing countries. Given the conflicting results and different model specifications it is hard to determine who is correct. The simplest conclusion is that signing BITs may slightly increase FDI but they are probably not very important, and certainly less important than other determinants of FDI like market size.

A recent paper by Elkins, Guzman and Simmons (2004) analysed the pattern of BIT signing. They find that competition is the key motivator, as developing countries vie to lure investment projects. Neumayer (2005) looks at BITs from the home country's point of view and finds that signings do not correlate with any sort of needs analysis. Namely, they are not signed to alleviate poverty but in accordance with the self-interest of the developed country partner.

2.3.3. *Changing BIT Practice*

So far, the available empirical research seems to indicate: (1) signing BITs probably slightly increases the amount of FDI a developing country receives; (2) developed countries sign BITs more often in accordance with their own interests than out of any desire to 'help' a developing country; and (3) the diffusion of BITs corresponds to a model in which developing countries are competing for FDI rather than one in which developed countries use duress to get BITs signed. This paper argues that this recent research does not delve deeply enough into the differences between the kinds of BITs being signed and their potential impact on development. The variation in provisions is considerable (Brewer and Young 1998: 77), and treating them as a single uniform set is misleading.

While the textual analysis for this paper included 27 different variables, the most important variances relate to development policy space. These include the following: national treatment, which designates that host countries must treat foreign investors at

least as well as domestic investors once an investment is made; pre-establishment rights, which remove host country rights to screen foreign investment before it is made; domestic taxation exemptions, which omit domestic tax rules from the national treatment standard; public health exemptions, which exclude any protection under the treaty for measures taken in order to protect public health; unrestricted repatriation of returns, which gives inalienable rights to investors to transfer funds; financial crisis safeguards, which allow hosts to restrict transfers during balance of payments difficulties; bans on performance requirements, which prevent hosts from attaching conditions to investment usually relating to local-content purchasing, export volumes, technology transfers, or staff nationality; and dispute resolution mechanisms, which determine how investors can settle grievances with the host countries.

Given that many of these clauses undermine developing country use of industrial policy, substantive differences are important. While developing countries are clamouring to sign BITs to increase their likelihood of receiving FDI, I argue that this competition is detrimental to efforts to spur development. The tenuous link from signing a BIT to increasing FDI to generating economic growth may be too much of a gamble given the certain costs of lost policy space.

3. Research Methodology

Since it is not valid to treat all BITs the same, the missing piece of the puzzle is to determine which BITs include which provisions, which necessitates analysing each treaty individually. This paper's goal is to scrutinise these agreements and see what patterns can be derived. Knowing why and under what conditions certain invasive clauses are included will help inform strategies for BIT adoption that preserve policy space while still providing adequate investor protection to encourage FDI.

Given the number of BITs, over 2,200, and the need to thoroughly read the actual treaty texts, it is not practical to create a full database of the agreements. Since the goal is to look at the developmental impact of the treaties, only certain types of agreements were considered. Despite a surge of South-South investment (Akyut and Ratha 2004), the most important investors are still from developed countries, which have the longest running and the most established BIT programmes. Thus, this analysis is confined to BITs between high income and non-high-income countries.

3.1. Sample Selection

The World Bank methodology (2005) is used to divide countries into groups. Efforts were made to balance regional representation. The country classifications are shown in Table 1. A full list of the treaties is contained in Appendix A.

Table 1 Countries Included

Middle-Income	High-Income	
Argentina	Australia	Italy
Malaysia	Austria	Japan
South Africa	Belgium ²	Netherlands
South Korea ¹	Canada	New Zealand
Sri Lanka	Denmark	Norway
Low-Income	Finland	Portugal
Bangladesh	France	Spain
Ghana	Germany	Sweden
Nicaragua	Greece	Switzerland
Vietnam	Ireland	UK
Zimbabwe	Israel	USA
Transition		
Czech Republic		
Georgia		
Ukraine		

3.2. Textual Analysis

The analysis looks at the major substantive variances found within BITs. In particular the focus will be on those areas that could be viewed as detrimental or beneficial for host country development. A full list of the parameters assessed when reading the treaties is available in Appendix B.

Most of the treaties were obtained from the online UNCTAD BIT database (UNCTAD 2005a). Some additional texts were obtained from the UN Treaty Series or directly from the websites of the contracting parties. Where possible, English texts were used to avoid translation issues. All protocols, annexes, and notes were considered. When renegotiated, only the most recent agreements was examined.

3.3. Statistical Methods

The sample of 164 agreements was not sufficiently large for a robust multivariate analysis. A thorough examination of all 2,200-plus BITs would surely produce more

¹ Though South Korea was recently reclassified as a high-income country by the World Bank, its BITs were signed when it was middle-income.

² The Belgo-Luxembourg economic union jointly negotiates BITs.

interesting results, but that task is beyond the scope of this paper. Most dependent variables of interest could only be measured at the nominal level – whether or not there was a certain clause in a BIT – limiting the available statistical procedures. Constructing an index of a treaty's potential negative impact on development may have assisted in statistical analysis, but would have required making judgements about the relative developmental importance of different treaty provisions. Given the absence in the literature of a coherent model for the potential welfare increase or decrease for specific clauses in such agreements, such an index would only be arbitrary and not meaningful. Thus, the BIT clauses are assessed individually as separate dependent variables.

For nominal dependent variables, χ^2 -based testing has been used, with phi (ϕ) used for assessing the strength of the association because of the unequal nature of the row marginals. For scalar dependent variables ANOVA-based testing is used, with eta (η) values reported to test the strength of association. As a second order examination, I checked whether the treaties, classified by presence or absence of a substantive provision, have significantly different means for the continuous independent variables. This was done with independent samples t-tests, checking and adjusting for unequal variances. The full list of dependent and independent variables with summary statistics are available in Appendix B and Appendix C.

For discontinuous independent variables I used two measures of country type, one with a tri-modal income separation (low-income, middle-income or transition country), and the other with a bi-modal classification (low-income or middle-income). This tests for differences in the treatment of transition countries. Additionally, I test for regional variation. Some regions, because of regional competition and the perception by both investors and developed country negotiators of intra-regional differences, may end up with substantively different treaties. I classified the host countries into the following categories: Latin America, Africa, Asia, or the former Soviet Union. Finally, I

use the date of signature, broken into four classifications – before 1990, from 1990 to 1995, from 1995 to 2000, and after 2000 – to test for evolution of investment protection standards.

Along with date of signature, the continuous independent variables used in the tests for differences of means were market size, income, cumulative FDI, FDI as a percentage of GDP and institutional quality; all measured in the year of treaty signing to better model how they might effect negotiations. Testing the date of signature will confirm whether treaties containing the specified clause were on average signed at a different time than those not containing the clause. I measure market size using GDP in constant 2000 dollars, logged to reduce the skewness of the variable. Income is measured as per-capita GDP at average market exchange rates in constant 2000 dollars. The gross-FDI/GDP ratio and gross FDI, calculated from the aforementioned ratio, are used to test whether countries with significant amounts of foreign investment already in place are more likely to have certain clauses in their treaties. If there are significant differences this would indicate that the existence of a BIT clause (the dependent variable) was a response to demands from existing investors rather than a protection or incentive used to attract new investment. Gross FDI is also logged to reduce the skewness of the results. Data comes from the World Bank's World Development Indicators (2005). Following Neumayer and Spess (2005), the POLCON variable (Henisz 2002) is used to test if the clause is a response to the perceived arbitrary nature of government policy towards investors.

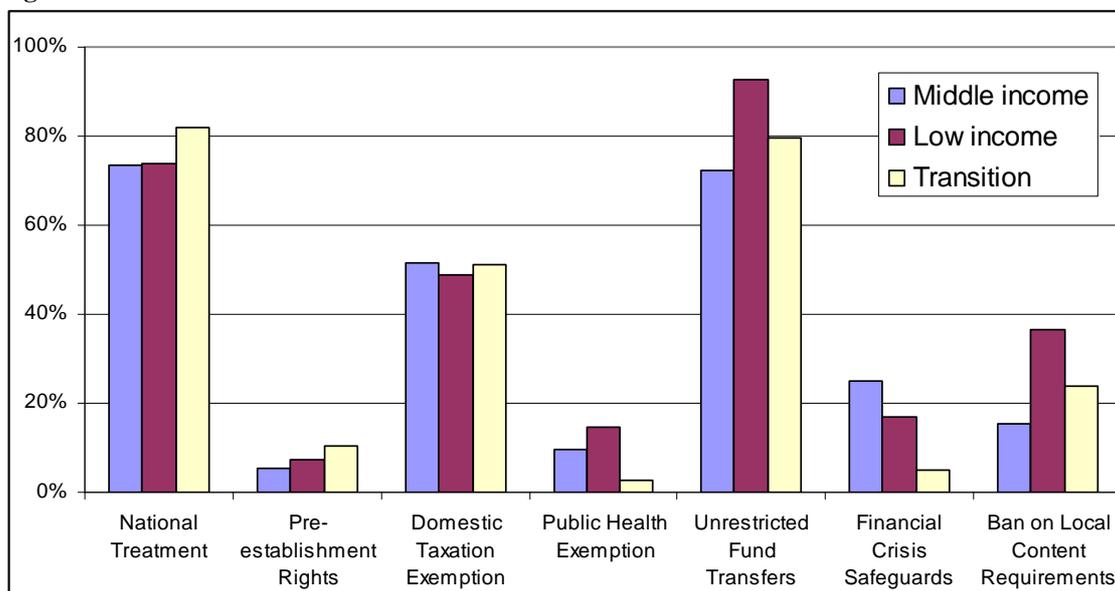
4. Findings

The purpose of the research design is to look at what factors are significantly correlated with the various clauses of BITs. This is valuable information because it may indicate that it would be advantageous to alter the negotiation strategies of developing countries to preserve more policy space for development-oriented interventions.

The most basic form of an investment promotion and protection agreement includes provisions on expropriation and nationalisation, as did all of this sample. Additionally, all of them defined intellectual property rights as one type of investment. Finally, they all included most favoured nation (MFN) clauses for investor protections.

The table of results for the bivariate associations using the χ^2 test are presented in Appendix D. The table of results for the difference in means test are presented in Appendix E. Figure 1 shows a simple bar chart looking at the percentages of treaties found to contain certain clauses for each income group.

Figure 1 Incidence of Selected BIT Clauses



4.1. National Treatment and Pre-establishment Rights

For national treatment, the only significant bivariate associations are time of

signature and region. Of those signed before 1990 nearly 50% did not include national treatment clauses while more recent treaties are more likely to include them. African countries had no treaties without national treatment clauses, while Asian countries had nearly 40% of their treaties without such clauses. To control for time, bivariate associations were rechecked for the subset of treaties signed after 1990, the point at which there was a clear break in the data. Region remains significant ($\chi^2 = 6.531$, $p < 0.01$, $\phi = 0.284$), but the association loses some strength. Examining the cross-tabulations, Africa is noticeably different, with all their treaties containing national treatment clauses, while every other region has some that do not.

In the test for difference of means of the independent variables for the treaties categorised by whether they have this clause or not, the date of signature is again highly significant. This confirms that treaties with national treatment were on average signed later than those that do not include it. There was also a statistically significant difference in the mean institutional structure, using both the full sample set and the time-controlled set. In both cases countries without national treatment clauses have more controlled governance systems with fewer decision points.

Table 2 Pre-establishment Rights Summary

Country	Total Treaties	With Pre-establishment Rights	Percentage
United States	7	7	100%
Canada	4	2	50%
Japan	4	2	50%
All Others	141	0	0%

Pre-establishment rights clauses are so rare that statistical analysis is unviable. The clearest factor is home country, as shown in Table 2. Of the 22 home countries in the sample, only the US, Canada and Japan have pre-establishment rights clauses in their treaties.

4.2. Taxation and Exemptions

All BITs include exemptions to MFN treatment for benefits derived from economic

unions or free trade areas. The entire sample also included provisions to exempt international agreements on taxation from MFN treatment.

Variance was found on whether domestic tax law is covered by the agreement. This only matters in cases where national treatment has been granted, thus the analysis was restricted to that subset of agreements. Income classification is not statistically significant, while host country region and the date of signature are. Asian countries are more likely to have no domestic tax exemptions because their treaties are older, and were signed before this innovation in BITs was developed. Only the date of signature is really significant, a result confirmed from the test for difference of the mean date of signature. Over time, more treaties have given this exemption. Since 1995, more than 50% of the agreements are now not designed to cover domestic taxation. Home country variance is also important, with certain countries, such as the US, UK and Sweden, always including domestic taxation exemptions; while others like Switzerland, Italy and the Netherlands never give such exemptions.

Given that BITs invariably include patents under the definition of investment, the existence of a public health exemption, similar to that found in the Trade Related Intellectual Property Rights (TRIPs) Agreement of the WTO, is important. Public health exemptions vary significantly over time according to the bivariate correlations, with more recent treaties being much more likely to include such protections. The number of observations are so few however, that the test for difference of means finds no significant results.

4.3. Capital Movement Safeguards

The first test is whether countries have granted unrestricted rights for repatriation of investments or whether they may restrict those rights. Because the bivariate results show statistical significance for all independent variables, I first control for the date of signature of the treaty. The cross tabulations again show a break at 1990, so time is controlled as before. Table 3 shows that no other independent variables remain

significant. The test for mean differences also finds no significant independent variables, leaving the variation in this clause unexplained beyond that more recent treaties are less likely to allow restrictions on repatriation.

Table 3 Restrictions on Transfers of Funds, post-1990 Treaties

	χ^2	Phi
Tri-modal Income	2.168	0.137
Bi-modal Income	0.935	0.090
Region	3.079	0.164

Some of the treaties define the maximum amount of time considered acceptable for a transfer of funds to occur. This is usually a certain number of months after the request for transfer, though most treaties only say that transfers should occur 'without delay'. I tested for a statistical difference in the mean number of months, with results in Table 4. The date of signature showed weak statistical significance with a low strength of association. A post hoc Fischer's LSD test showed moderate significance ($p < 0.05$) for a difference between treaties signed in the first and second halves of the 1990s, with the mean value of the allowed delay declining over time.

Table 4 Allowed Delay in Funds Transfer ANOVA Results

	F	Eta
Tri-modal Income	0.883	-
Bi-modal Income ³	0.149	-
Region	0.544	-
Date of Signature	2.286*	0.210

* significant at .1 level

Finally, I see whether the treaties contain specific clauses that, in the case of financial crises, suspend any repatriation rights granted to investors. There was statistical significance for three of the variables, notably excluding bi-modal income. Thus, transition economies do have significantly different agreements in this regard.

³ Because of the bi-modal classification of the variable, an independent samples T-test was used and the resulting t statistic reported.

Both region ($\chi^2 = 6.330$, $\phi = 0.235$) and tri-modal income classification ($\chi^2 = 5.138$, $\phi = 0.211$) remained weakly significant ($p < 0.1$) after controlling for date of signature as before, but the tests were conducted with expected cell counts below 5, casting doubt on the results

The results suggest that transition countries have fewer safeguard clauses allowing delayed repatriation of assets during a balance of payments crisis. Cross checking these results with the tests for difference in means, the significance of the date of signature is confirmed. Significance is also found for the ratio of FDI/GDP and the measure of institutional quality. It is expected that there is multicollinearity as there is a significant but weak correlation between developing countries with high FDI/GDP ratios and those with less autocratic institutions. Additionally, for the entire sample the institutional quality has tended to go up over time as has the FDI/GDP ratio. There is unfortunately no way to remedy this problem in this model, but a tentative conclusion can be made that developing countries where FDI was more important to the economy were more likely to be able to extract safeguards during negotiations. This is despite the fact that over time FDI/GDP ratios went up while the likelihood of having safeguards went down.

The anecdotal evidence suggests that certain host countries end up with more safeguards. After 1990, four of Argentina's 18 treaties and three out of four of Sri Lanka's had such clauses. Developed country treaty partner is also anecdotally important with Japan's (4 of 4), Australia's (3 of 4) and Canada's (2 of 4) agreements accounting for a majority of the 14 post-1990 treaties containing the safeguards.

4.4. Performance Requirements

Bans on performance requirements are in some cases rarely observed, such as explicit bans on technology transfer requirements ($N = 6$), thus making statistical testing impractical. Bans on export requirements are nearly perfectly correlated to bans on local-content requirements ($\chi^2 = 134.577$, $p < 0.001$, $\phi = 0.944$), so only the

results for local-content requirements are reproduced.

The bivariate associations show statistical significance for all independent variables except region. Controlling for date of signature after 1990, tri-modal income remains weakly significant ($\chi^2 = 3.749$, $p < 0.1$, $\phi = 0.181$) and only weakly associated. The test for significantly different means on the continuous independent variables produced interesting results. Income is confirmed as showing significant differences between the group of treaties that include this clause and the group that do not. Market size is also shown to be significant. Table 5 shows that these differences remain statistically significant after controlling for signing date. The host economies that sign treaties with bans on performance requirements tend to have poorer people and have smaller economies.

Table 5 Performance Requirements Means Comparison Results, post-1990 Treaties

	t	DF	Eta
Market Size	2.708***	112	0.248
Per Capita GDP	2.484**	112	0.229

** significant at .05 level *** significant at the .01 level

Finally, I look at whether the treaty explicitly prohibits the host country from requiring management staff to be of any particular nationality. Only the date of signature is significant, which is confirmed in the test of means difference. Home country partner again seems to be the most significant indicator, with all the treaties of Australia and the US, three-quarters of Japan's treaties and half of Canada's agreements explicitly prohibiting such conditions on investment.

4.5. Dispute Settlement

Dispute resolution is a standard part of almost all BIT treaties, with only five agreements in the sample, all from before 1981, not including clauses on investor-state arbitration. Additionally, two further treaties do not stipulate that the state automatically consents to arbitration, one of which dates from 1979. The notable exception is the

Argentina-New Zealand treaty of 1999, which explicitly states that the investment agreement should not be considered as the consent necessary to initiate arbitration under International Centre for Settlement of Investment Disputes (ICSID) rules. In eight cases (44% of its treaties) Argentina also successfully required aggrieved investors to submit any dispute first to a domestic court before it could be taken to international arbitration. South Korea and Malaysia each have one treaty with similar conditions.

Given the uniformity in arbitration procedures specified, little variation is available to assess. The mean waiting period between when an investor notifies a host government of a dispute and when it may commence arbitration is one possible variable to test. Because there are not an approximately equal number of cases for the independent variables, it does not meet the ANOVA test specifications. Additionally, Argentina is a notable outlier, with some treaties requiring up to 2 years before international arbitration can commence so as to give time for domestic judicial proceedings. To adjust, I excluded Argentine treaties that require domestic court procedures and collapsed the date categories of 1995-2000 and after 2000, producing a three-part classification – before 1990, 1990 to 1995, and after 1995.

Table 6 Arbitration Waiting Period ANOVA Results

	F	Eta
Tri-modal Income	0.190	-
Bi-modal Income ⁴	-0.679	-
Region	1.162	-
Date of Signature	0.409	-

By eliminating the Argentine outliers and the model problems, I find that there is no statistical difference between arbitration waiting periods along any of the classifications. Scatter plots, shown in Appendix F, give no reason to think that there is any linear relationship between per capita income and waiting period. The only other

⁴ Because of the bi-modal classification of the variable, an independent samples T-test was used and the resulting t statistic reported.

variation found in this sample is in the venue for arbitration. This is probably unimportant developmentally because ICSID, ad hoc tribunals, and various chambers of commerce would probably not produce substantially different outcomes. Finally, despite talk of reform at ICSID to make it more transparent (Peterson 2005a: 128-131), none of the treaties included any transparency requirements such as open hearings or published arbitral decisions.

5. Discussion

Clearly the substantive provisions of BITs vary, prompting this preliminary examination of how and why they differ. Though it cannot be said with certainty why any particular treaty contains certain clauses without an in-depth analysis of each negotiation, the textual analysis combined with statistical techniques outlines some of the broad patterns involved. The treaties have evolved over time, leaving us to wonder whether the developing countries involved are benefiting more or less from these agreements than before. BITs and the variation in their language influence developing countries' growth strategies. If developing country governments focus solely on the perceived benefits of increased FDI there is a risk of miscalculating the net gains from such agreements because of the loss of industrial policy space. Keeping costs in mind suggests possible ways to make BITs better for development.

5.1. Reviewing Differential Outcomes

5.1.1. *Capital Movement*

Because of the increasing incidence of financial crises and the volatility in the global financial system, developing countries must worry about capital movement (Griffith-Jones and Kimmis 2003). The Asian financial crisis highlighted that even relatively well-off countries can experience irreparable economic and human welfare losses due to balance of payments difficulties (Stiglitz 2002). The question is whether capital controls to restrict the movement of 'hot money' would be possible under BITs given their provisions for unrestricted transfers of investments and returns, including portfolio capital. Because there are no precedents under international arbitration, it is difficult to judge how future arbitral tribunals will interpret BITs.

The presence of financial crises safeguards in a BIT would, of course, ease concerns. This is not as common as one would hope, with only 18% of this sample containing such an exemption. Even if a treaty includes a safeguard, in the case of a

transfer delay, an investor may still attempt arbitration claiming, through the MFN clause, the treatment of another BIT which does not give provision for such safeguards. Until the great majority of BITs include such clauses, the prospect of facing capital flight during a financial crisis, with no tools to restrict it, must be of concern. Thus, the impact of BITs on the ability of developing countries to control capital flows, outside of the presence of safeguard clauses, is an important topic.

Complicating the picture, different types of capital controls might or might not be found to violate investment agreement provisions. Malaysia, for example, assesses an exit tax in the case of short-term withdrawals. Chile imposes an entrance tax, a non-interest bearing deposit against inflows of money. Both types may be susceptible to arbitration under national treatment clauses unless they apply the same penalties to domestic investors. Tobin Tax proposals might also fall foul of BIT provisions, and sometimes countries just prohibit all capital movement temporarily. In Argentina's case, their controls, combined with price setting and other market interventions, have spawned a host of arbitrations, most of which are yet to be decided.

There are four types of BIT provisions on capital movement. Most worrisome developmentally are unrestricted repatriation clauses, which grant absolute rights to investors to transfer their funds. Little different are transfers with specified restrictions, which allow repatriation that has satisfied certain specific enumerated conditions, such as meeting tax liabilities and complying with legal proceedings. Both categories seem to completely proscribe capital controls. On the opposite end of the spectrum are provisions for transfers to be done in accordance with the law of the host country. This blanket allowance for domestic legislation is present in 20% of the sample. The vaguest provisions with the most scope for divergent interpretation are those that allow regulatory restrictions. These prevent host countries from infringing on repatriation rights except to impose administrative procedures. Treaty drafters were probably envisioning reporting requirements or other procedures to ensure that taxes are paid. It

is unlikely they were attempting to allow capital controls for the purpose of preventing capital flight, but because of the vagueness of the wording, it is open to interpretation by any arbitration tribunal.

The analysis found only the date of signature as a statistically significant indicator for when treaties would allow legislative restriction of repatriation rights. The ability of developing countries to take pre-emptive measures to control capital flows is vital. The recent major financial crises, from Mexico's 1994 tequila crisis to the 2001 Argentine crisis indicate the systemic risks global finance poses for developing countries. BIT balance of payments safeguards may be helpful in a crisis, but do little to prevent crises. Indeed, prevention is perhaps more important than crisis response (Eichengreen 1999). If investment treaties can be used by investors to prevent developing countries from imposing capital controls, then a vital policy intervention will be lost, with potentially catastrophic consequences. Developing countries should be very aware and careful of the risks they face with this BIT clause.

5.1.2. Industrial Policy

As Section 2.1 made clear, industrial policy is a foundation of developing country efforts to achieve economic growth and industrialise in order to increase manufacturing value added. Investment treaties, however, contain numerous provisions that may constrain or hamper industrial policy as it is traditionally practised.

The standard of national treatment wipes away the foundation of infant industry protection. Foreign investors must be given the same treatment as domestic entrepreneurs and industry. The extension of this to pre-establishment rights removing governments' rights to pre-screen investments, further reduces chances for host countries to enact policies that will specifically benefit domestic entrepreneurs.

Assisting domestic entrepreneurs was often done with tax policy, subsidies, directed credit, and other business promotion schemes. Many developing and developed countries use their tax code to support certain industries. This helps local

companies with fewer firm-specific advantages compete with international conglomerates that have economies of scale, proprietary technology, and market power. However, if the tax breaks are available to multinational investors, then they will not be effective in spurring local industrial development in backward economies.

Treaties that include exemptions on domestic taxation should be better for conducting industrial policy. They give the developing country partner the space to design strategic initiatives for promoting industrialisation. Of course, giving policy space does not mean that it will be used appropriately. Having a discriminatory tax system might drive away foreign investors altogether. The key is to balance the goals of encouraging domestic enterprise and attracting foreign investors.

By rigidly defining what is considered 'treatment less favourable' than that given to local businesses, some BITs ban performance requirements. These performance requirements try to ensure that FDI is less exploitative and more beneficial for the host economy. The four categories of requirements effect: backward linkages, exports, technology transfers and employment.

Local-content requirements can effectively create backward linkages from foreign investment projects into the domestic economy. The requirements force investors to buy a certain percentage of their intermediate goods and raw materials from local providers. This promotes technology upgrading in the linked industries and increases the skills and markets for domestic producers. Local-content requirements have already been barred by the WTO's TRIMs agreement, because they are 'trade distorting' (WTO 1994). This includes conditions of establishment as well as those for receiving a benefit or advantage. Still, many BITs further prevent such performance requirements and give investors the right to take host governments to arbitration over their use.

Export and trade-balancing requirements have also been used as part of industrial policy. These come in different flavours, such as demands that a certain

percentage of production is exported, or that imports of raw materials and intermediate goods must be offset by equal value of exports of finished products. These types of requirements were also barred under the TRIMs Agreement. As shown in Section 4.4, most BITs also forbid export requirements if they prohibit local-content requirements.

Technology transfer requirements seek to ensure technological upgrading so that foreign investment benefits the host economy. These requirements, which are not actionable under the TRIMs Agreement, might force an investor to share intellectual property with local suppliers; or could require that the investor establish some research and development facilities in the country. Few of the treaties analysed, just 4%, explicitly banned technology transfer requirements, leaving room for host country policies to maximise the technological benefits of FDI. The usual caveat applies that overzealous demands for technology transfer may repel investors. Host countries must be strategic in how they use their policy space.

Finally, human capital upgrading can be facilitated by restraints on the nationality of managerial and directorial staff. The US, early in its industrial history, imposed nationality requirements on board members of banks, and Finland from the 1930s until the 1980s banned foreigners from becoming a board member or a general manager of a firm (Chang and Green 2003: 18). These requirements ensure that foreign investment improves the skills and managerial techniques of local workers. Despite their previous application, they are also coming under pressure from BITs. While less than 1% of the sample explicitly barred restrictions on the nationality of board members, 11% did so for managerial staff. The analysis found no significant correlation between host country characteristics and these provisions. The preference of the developed country partner seems to determine when these provisions are included.

Some BITs, though invasive and limiting of industrial policy space, make exclusions for certain industries. This is particularly the case for treaties that grant pre-establishment rights as the developed country partners also often want to protect

domestic producers. One way developing countries can maintain industrial policy is to exempt important sectors from inclusion in the treaties. Korea has tried this strategy during BIT discussions with the US, seeking to protect cultural industries, but the result has been an impasse in the negotiations (Kim 2005). Of the 19 treaties that have sectoral exclusions in this sample, the home country nearly always maintains more exclusions than the host country, with averages of 10.78 and 9.33 sectors, respectively. Most developing countries lack the bargaining power necessary to gain larger concessions in BIT negotiations.

5.1.3. Dispute Settlement

Arbitration has been one of the hallmarks of the investment protection regimes established by BITs. Very few BITs omit provisions allowing investors to bring complaints against states under international jurisprudence. The provision for arbitration tribunals essentially privatises the judicial process. The resulting fear of facing arbitration over every regulation that harms the interests of a foreign investor may make host countries scared to regulate (Peterson 2004; Van-Harten 2005). That clearly reduces the flexibility that governments have to manoeuvre their economies. There is also evidence that it may decrease local institutional quality (Ginsburg 2005).

The most obvious variation in dispute resolution clauses is the waiting period before arbitration can commence. While some, especially Argentina, have clauses requiring aggrieved investors to first submit disputes to local courts, these were circumvented via MFN clauses. For example, Gas Natural, a Spanish company, was allowed to proceed with international arbitration against Argentina despite the provisions of the Argentina-Spain BIT calling for domestic court action first (*Gas Natural v. The Argentine Republic* 2005; Peterson 2005b). The analysis showed no statistical difference based on host country characteristics for the length of waiting time for arbitration. It seems the waiting period is probably a fairly unimportant bargaining chip used to gain agreement on more important substantive clauses of a treaty.

The other axis of variation is where arbitration is conducted. Nearly all agreements, 92% of the sample, allowed arbitration at ICSID. Unfortunately, most treaties also included other methods of arbitration such as ad hoc tribunals under UNCITRAL rules and proceedings at various chambers of commerce, such as those in Stockholm and Paris. That is discouraging in terms of transparency reforms to arbitration procedure because BITs allow investors to venue shop for the most advantageous rules. The plethora of procedures and venues effectively stymies reform at the venue level. Without a multilateral framework, the only option is amending all BITs, an unlikely prospect.

5.1.4. *Patterns and Trends*

The clearest pattern is the importance of evolution in BIT texts over time. The date of treaty signing was significantly correlated with most of the tests for substantive variation presented in Section 4, including national treatment, taxation coverage, balance of payments safeguards and management nationality performance requirements. The inference is that certain obligations and safeguards are new practices, and not specifically related to characteristics of the capital-importing country. There may be a trade-off between safeguard clauses and more invasive provisions that remove development space. For example, a newer treaty is more likely to exempt public health action, but likewise is more likely to grant national treatment to foreign investors, making industrial policy more difficult.

This provides evidence both for and against the theory that competition for foreign investment drives the signing of BITs. Under a competitive model, capital-importing countries should progressively give away their industrial policy space to become more attractive hosts for FDI. On the contrary, there is an increase in public health and domestic taxation exemptions. For the former, this clearly departs from the competition model, meaning that it is either a product of home country preference or an area of real importance to developing countries. Meanwhile, for taxation exemptions, it

is almost certainly home country preference. The US and other industrialised countries often use their tax code for protectionist and political purposes. Carving out taxation from investment treaties allows them to maintain their tax structures.

The analysis generally supports the theory of competitive treaty signing with the caveat that certain capital exporters have specific demands. The anecdotal evidence shows that that the inclusion of many rules is up to the capital exporting country, with less variation in the agreements when viewed by home country than by host country. This applies to most provisions with two important exceptions – funds transfers and performance requirements – both of which were discussed above.

5.2. Implications for Development

Having understood the various BIT provisions and trends, what does this mean for the developmental prospects of developing countries? The statistical importance of the date of signature indicates that BITs evolved over time. Unfortunately, the trend is towards even less industrial policy space for capital importing countries. As options for strategic economic policy decrease, so do the chances that backward economies can become wealthy. However, the negative impact of bilateral agreements can be limited. Policy space can be preserved through well-structured agreements with adequate safeguards and fewer invasive integration requirements. An example is the model agreement produced by the International Institute for Sustainable Development (Mann et al. 2005). It balances the rights and obligations of all parties to preserve policy space while granting protections to encourage foreign investment.

Salacuse and Sullivan's (2005) results present a very relevant question. If signing a BIT with the US does lead to a larger increase in FDI than signing one with another OECD country, knowing why is vital. They believe that more stringent investor protections, pre-establishment rights and bans on performance requirements, are the reason. However, that conclusion has been contradicted by Tobin and Rose-Ackerman (2005) and by analyses of corporate decisions on where to locate FDI. The most

relevant factors in both qualitative and empirical analyses have been market size, and trade openness (Chakrabarti 2001). TNCs have reported that ownership restrictions, performance requirements, and other controls have not been important in their decision making (UNCTC 1991).

Given that all BITs require compensation for expropriation of an investment, the investor protections necessary to encourage FDI would be present even in a more balanced treaty. The race to the bottom is merely a dangerous by-product of competition to secure foreign investment. Policy makers in developing countries who agree to stringent BITs that constrain policy space are not likely to find themselves receiving more FDI than those that hold out for better agreements. Guzman (1997-1998) found that developing countries flocked to provisions for compensation for expropriation in the bilateral realm, while simultaneously eschewing them in multilateral forums. The same is continuing today as developing countries have opposed multilateral negotiations on investment in the WTO while ceding their policy space in the bilateral sphere.

Weighing up the costs and benefits of BITs is no easy task. There is no coherent theoretical justification for how partial investment liberalisation will create net welfare improvements because the factor markets for labour, capital and trade are highly imperfect. One needs to proceed empirically to assess whether foreign investment has contributed to the welfare of developing countries that receive it. Then this would need to be empirically linked to the signing of BITs. More BITs might lead to more FDI, but *both* links in the chain are still debated topics. The costs of the investment in terms of lost policy space and increased risk due to opening the domestic economy to the global financial system must be considered. The question remains as to whether the FDI brought by BITs is more valuable than the costs. However, the loss of policy space from signing a BIT is assured, while the gains from foreign investment are uncertain.

5.3. Potential Investment Agreement Strategies

5.3.1. Improved Bilateralism

As BITs may bring increased FDI, they should not be completely rejected. Instead, they should be made more conducive to development. Much as development agendas are being debated at the WTO and other international organisations, a development agenda needs to be created for investment regimes.

This developmental focus would ensure that BITs grant adequate safeguards for public health and financial crises. It would also clarify the right of host countries to regulate, eliminating the fear of spurious arbitration claims. The agreement text could say that the treaty should not be interpreted so as to preclude the signatories from taking measures for the economic welfare of their countries.

Allowing performance and technology transfer requirements, though anathema to TNCs, would guarantee that FDI could be made beneficial to the host economy. Another strategy is to include sectoral exclusions in all BITs, allowing industrial policy in important areas of the economy. That would secure policy space, allowing countries to dynamically select and protect important sectors that are vital to industrialisation strategies.

Such modifications would be very difficult to achieve. With much of the ground already ceded in BITs concluded with OECD countries, renegotiations are unlikely. That does not bode well for the countries already committed to deep integration through BITs, but other countries can still avoid the worst of the agreements. Generally capital importers first approach capital exporters proposing a BIT at which point the developed country produces their model text as the starting point for negotiations. If signalling and protection of basic property rights are the most important aspects of BITs for attracting FDI, developing countries should be choosier about who they sign agreements with. Avoiding demanding treaty partners who ban performance requirements and grant few safeguards, may prove to be viable. Instead, the

developing country should pick partners that are likely to sign treaties with the most development policy space preserved. Of the high-income countries, New Zealand, the UK and Israel come to mind as treaty partners with relatively lenient treaties.

Most agreements do not limit the protections only to companies that are controlled by nationals of the treaty partners. Thus US investors who want to invest in a country without a US BIT can easily channel their investment through foreign subsidiaries in a country that is a treaty partner. The most famous case of this is the Dabhol Power plant in India, whose American foreign investors channelled their funds through subsidiaries in Mauritius to take advantage of the Mauritius-India BIT (Bechtel Enterprises 2003). India might view the negative arbitration decisions in the wake of the shut down of the power plant as negative, but a different outlook highlights that the Mauritius-India BIT encouraged foreign investment while not subjecting India to a US BIT with very invasive integration requirements.

As a country's industry matures it may then wish to seek more FDI from demanding partners such as the US and Japan. That was the strategy followed by Korea, which did not overly liberalise its investment regime through BIT obligations until its 2001 treaty with Japan which granted pre-establishment rights to Japanese investors and banned performance requirements. By that time, Korea had already joined the ranks of the OECD and enjoyed per capita incomes of more than \$10,000. This gradual approach will give the policy space needed for developing countries to use industrial policy when they need it most.

5.3.2. *Multilateral Framework*

Unfortunately, the above strategy does not solve the collective action problem. As competitors for foreign investment each race to provide the best incentives and protections, it would be hard for any country to take a gradual approach and hold out on deep integration (Elkins et al. 2004), unless it possessed unique characteristics such as a very large internal market, like China. Collective action is best maintained at

the multilateral level.

Developing countries have successfully used coalitions to obstruct undesirable negotiations at the WTO (Narlikar 2003), including stalling investment issues (Mori 2004). The side-effect has been increased bilateralism, isolating developing countries in one-on-one negotiations with powerful developed countries. It is then not surprising that capital importers have been facing eroding terms and conditions in their bilateral agreements. Those conditions are only likely to get worse over time and impinge even more on the policy space of developing countries.

The developing world would be better off with a multilateral regime that is more friendly to their needs (Brewer and Young 1998: 235). This was tried, albeit unsuccessfully, with the UN Code, as discussed in Section 2.2.2. It exemplified that a comprehensive multilateral investment regime could balance the rights and obligations of all three parties: home, host and investor. If developing countries could create a balanced multilateral system, they would then have the ability to combat the restrictive business practices of TNCs. Additionally, a multilateral framework on investment incentives could work to put an end to the race to the bottom in terms of regulation and tax incentives, allowing host countries to gain more from FDI and maintain progressive labour and environmental standards. A multilateral framework could also include a code of conduct on technology transfers, which would ease the process of closing technology gaps.

Pursuing a multilateral strategy may be risky, and could lead to deadlock as it did in negotiations over the UN Code. It would probably also not put a halt to developed countries pursuing their agendas through bilateral negotiations (Drahos 2001), nor developing countries competing for FDI projects. But the alternative of only bilateral accords is clearly worse. Obstruction of a multilateral agenda on investment only pushes developed countries into pursuing more bilateral accords. But in the bilateral realm there is almost no chance that an individual developing country could ever hope

to introduce the kind of obligations on investors and home countries that were included in the UN Code.

While the mid-1990s explosion of BITs has levelled off, the new trend is to include investment chapters in free trade agreements (FTAs). These chapters incorporate the provisions of the most restrictive BITs but none of the safeguards and investor obligations that would be included in a comprehensive multilateral investment regime. As it is still relatively early in the life cycle of the FTA movement, there may yet be time to create a multilateral framework on investment that incorporates a development agenda. It could be written to supersede the existing spaghetti bowl of BIT provisions, bring rights and obligations to all parties in foreign investment, and preempt FTA efforts to fully liberalise the investment regime of developing countries. The alternative, a bilaterally negotiated investment regime with only host-country obligations and little or no industrial policy space, is simply not enticing.

6. Conclusion

As globalisation has increased since the 1980s so has the use of BITs as a mechanism for protection of investments from expropriation. This trend peaked in the mid 1990s, with more than 1,000 bilateral agreements completed within a few years. This significantly changed the investment landscape, opening up developing country economies to both direct and indirect investment. Concurrently, the ability of developing countries to conduct industrial policy was constrained through international agreements. The WTO began limiting the options for how developing countries could protect their infant industries and spur industrialisation. BITs have further reduced policy space.

The most important evolution in BIT practice over time was more stringent deep integration requirements. Bans on certain performance requirements, increasing grants of national treatment and pre-establishment rights and fewer restrictions allowed on transfers mean that developing countries are facing eroded policy space regardless of their market size or wealth. Only in the case of banning local-content and export requirements do host country characteristics matter, as larger and richer nations are able to avoid the provisions that restrict their industrial policy. That bodes ill for smaller poorer countries as they try to attract FDI in increasingly desperate attempts to spur growth through infusions of foreign capital. The competition between countries for foreign investment has further weakened bargaining positions and reduced policy space through more inflexible BIT provisions.

It is difficult to assess whether the benefits of new investment outweigh the costs in loss of the ability to conduct industrial policy. While short-run gains from FDI may be welcome, the long-term implications of BITs are unfortunate. Future research could fruitfully look at whether increases in FDI predicted from signing BITs are correlated with any specific clause such as bans on performance requirements. That would help quantify the potential benefits of signing up to deep integration in investment regulation.

Expanding the dataset by examining the treaties of more countries would clarify the relationship between different substantive provisions and increases in FDI and better reveal under what conditions developing countries accede to such provisions. Further research would also usefully look at a broader array of BITs, particularly the increasingly popular South-South agreements.

However, further research is *not* necessary to see that bilateral negotiations present a very different dynamic than multilateral negotiations. The evolution of the investment regime through BITs has significantly impinged on developing countries' policy space. This should serve as a wake-up call to those who disdain multilateral investment frameworks. The prospect, under status quo arrangements, is more BITs and then FTAs which include investment chapters. As competition takes its toll and developing countries are unable to exert any collective action because of the bilateral nature of negotiations, policy space will be eroded even further. The only chance for a balanced investment regime, which imposes rights and obligations on all parties to ensure that everyone benefits from FDI, would be through a multilateral framework which takes precedence over the current fractured bilateral rules. Such a multilateral regime, a sort of resurrected UN Code, would allow developing countries to bargain collectively to oppose the restriction of their policy spaces through deep integration requirements on investment regulation. The next challenge is convincing all governments that a balanced multilateral agreement is in their interests.

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Appendices

Appendix A Treaties Analysed

Host Country	Home Country	Date Signed	Language
Argentina	Australia	Aug 1995	English ⁵
Argentina	Austria	Aug 1992	German
Argentina	Belgium	Jun 1990	French
Argentina	Canada	Nov 1991	English
Argentina	Denmark	Nov 1992	English
Argentina	Finland	Nov 1993	English
Argentina	France	Jul 1991	French
Argentina	Germany	Apr 1991	English
Argentina	Greece	Oct 1999	English
Argentina	Israel	Jul 1995	English
Argentina	Italy	May 1990	Italian
Argentina	Netherlands	Oct 1992	English
Argentina	New Zealand	Aug 1999	English
Argentina	Portugal	Oct 1994	Unavailable
Argentina	Spain	Oct 1991	English
Argentina	Sweden	Nov 1991	English
Argentina	Switzerland	Apr 1991	French
Argentina	UK	Dec 1990	English
Argentina	USA	Nov 1991	English
Bangladesh	Belgium	May 1981	English
Bangladesh	France	Sep 1985	French
Bangladesh	Germany	May 1981	English
Bangladesh	Italy	Mar 1990	English
Bangladesh	Japan	Nov 1998	English
Bangladesh	Netherlands	Nov 1994	English
Bangladesh	Switzerland	Oct 2000	French
Bangladesh	UK	Jun 1980	English
Bangladesh	USA	Mar 1986	English
Czech Republic	Australia	Jul 1991	English
Czech Republic	Austria	Oct 1990	German
Czech Republic	Belgium	Apr 1989	French
Czech Republic	Canada	Nov 1990	English
Czech Republic	Denmark	Mar 1991	English
Czech Republic	Finland	Nov 1990	English
Czech Republic	France	Sep 1990	French
Czech Republic	Germany	Oct 1990	German
Czech Republic	Greece	Jun 1991	English
Czech Republic	Ireland	Jun 1996	English
Czech Republic	Israel	Sep 1997	English
Czech Republic	Italy	Jan 1996	Italian

⁵ Where possible English or French treaties were analysed though some were unavailable in those languages. Additionally some treaties that match the sample criteria were unavailable through the UNCTAD database, UN Treaty Series and the host and home country websites. They have been excluded from the statistical analyses.

Host Country	Home Country	Date Signed	Language
Czech Republic	Netherlands	Apr 1991	English
Czech Republic	Norway	May 1991	English
Czech Republic	Portugal	Nov 1993	English
Czech Republic	Spain	Dec 1990	English
Czech Republic	Sweden	Nov 1990	English
Czech Republic	Switzerland	Oct 1990	French
Czech Republic	UK	Jul 1990	English
Czech Republic	USA	Oct 1991	English
Georgia	Belgium	Jun 1993	French
Georgia	France	Feb 1997	French
Georgia	Germany	Jun 1993	German
Georgia	Greece	Nov 1994	Unavailable
Georgia	Israel	Jun 1995	English
Georgia	Italy	May 1997	Unavailable
Georgia	Netherlands	Feb 1998	English
Georgia	UK	Feb 1995	English
Georgia	USA	Mar 1994	English
Ghana	Denmark	Jan 1992	English
Ghana	France	Mar 1999	French
Ghana	Germany	Feb 1995	German
Ghana	Italy	Jun 1998	Unavailable
Ghana	Netherlands	Mar 1989	English
Ghana	Switzerland	Oct 1991	French
Ghana	UK	Mar 1989	English
South Korea	Austria	Mar 1991	English
South Korea	Belgium	Dec 1974	English
South Korea	Denmark	Jun 1988	English
South Korea	Finland	Oct 1993	English
South Korea	France	Dec 1977	French
South Korea	Germany	Feb 1964	English
South Korea	Greece	Jan 1995	English
South Korea	Israel	Feb 1999	Unavailable
South Korea	Italy	Jan 1989	English
South Korea	Japan	Mar 2002	English
South Korea	Netherlands	Oct 1974	English
South Korea	Portugal	May 1995	English
South Korea	Spain	Jan 1994	English
South Korea	Sweden	Aug 1995	English
South Korea	Switzerland	Apr 1971	English
South Korea	UK	Mar 1976	English
Malaysia	Austria	Apr 1985	English
Malaysia	Belgium	Nov 1979	English
Malaysia	Denmark	Jan 1992	English
Malaysia	Finland	Apr 1985	English
Malaysia	France	Apr 1975	French
Malaysia	Germany	Dec 1960	English
Malaysia	Italy	Jan 1988	Italian
Malaysia	Netherlands	Jun 1971	English
Malaysia	Norway	Nov 1984	English
Malaysia	Spain	Apr 1995	English
Malaysia	Sweden	Mar 1979	English
Malaysia	Switzerland	Mar 1978	French
Malaysia	UK	May 1981	English

Host Country	Home Country	Date Signed	Language
Nicaragua	Denmark	Mar 1995	English
Nicaragua	Finland	Sep 2003	English
Nicaragua	France	Feb 1998	French
Nicaragua	Germany	May 1996	English
Nicaragua	Netherlands	Aug 2000	English
Nicaragua	Spain	Mar 1994	English
Nicaragua	Switzerland	Nov 1998	French
Nicaragua	UK	Dec 1996	English
Nicaragua	USA	Jul 1995	English
South Africa	Austria	Nov 1996	German
South Africa	Belgium	Aug 1998	French
South Africa	Canada	Nov 1995	English
South Africa	Finland	Sep 1998	English
South Africa	France	Oct 1995	French
South Africa	Germany	Sep 1995	German
South Africa	Greece	Nov 1998	English
South Africa	Italy	Jun 1997	Unavailable
South Africa	Netherlands	May 1995	English
South Africa	Spain	Sep 1998	English
South Africa	Sweden	May 1998	English
South Africa	Switzerland	Jun 1995	French
South Africa	UK	Sep 1994	English
Sri Lanka	Australia	Nov 2002	English
Sri Lanka	Belgium	May 1982	English
Sri Lanka	Denmark	Jun 1985	English
Sri Lanka	Finland	Apr 1985	English
Sri Lanka	France	Apr 1980	French
Sri Lanka	Germany	Feb 2000	English
Sri Lanka	Italy	Mar 1987	Italian
Sri Lanka	Japan	Mar 1992	English
Sri Lanka	Netherlands	Apr 1984	English
Sri Lanka	Norway	Jun 1985	English
Sri Lanka	Sweden	Apr 1982	English
Sri Lanka	Switzerland	Sep 1981	French
Sri Lanka	UK	Feb 1980	English
Sri Lanka	USA	Sep 1991	English
Ukraine	Austria	Nov 1996	German
Ukraine	Belgium	May 1996	French
Ukraine	Canada	Oct 1994	English
Ukraine	Denmark	Oct 1992	English
Ukraine	France	May 1994	French
Ukraine	Germany	Feb 1993	German
Ukraine	Greece	Sep 1994	Unavailable
Ukraine	Israel	Jun 1994	English
Ukraine	Italy	May 1995	Unavailable
Ukraine	Netherlands	Jul 1994	English
Ukraine	Spain	Feb 1998	English
Ukraine	Sweden	Aug 1995	Unavailable
Ukraine	Switzerland	Apr 1995	English
Ukraine	UK	Feb 1993	English
Ukraine	USA	Mar 1994	English
Vietnam	Australia	Mar 1991	English
Vietnam	Austria	Mar 1995	German

Host Country	Home Country	Date Signed	Language
Vietnam	Belgium	Jan 1991	French
Vietnam	Denmark	Aug 1993	English
Vietnam	Finland	Sep 1993	English
Vietnam	France	May 1992	French
Vietnam	Germany	Apr 1993	German
Vietnam	Italy	May 1990	French
Vietnam	Japan	Nov 2003	English
Vietnam	Netherlands	Mar 1994	English
Vietnam	Sweden	Sep 1993	English
Vietnam	Switzerland	Jul 1992	French
Vietnam	UK	Jul 2002	English
Zimbabwe	Denmark	Oct 1996	Unavailable
Zimbabwe	France	May 2001	French
Zimbabwe	Germany	Sep 1995	English
Zimbabwe	Italy	Apr 1999	Unavailable
Zimbabwe	Netherlands	Dec 1996	English
Zimbabwe	Portugal	May 1994	Unavailable
Zimbabwe	Sweden	Oct 1997	English
Zimbabwe	Switzerland	Aug 1996	French

Appendix B Dependent Variables Summary

Variable	N	Mean	Std Dev	Min	Max	Description
Intellectual Property Rights	153	1	0	1	1	Test to see if definition of investment covers intellectual property rights
Control Clause	153	0.10	0.298	0	1	Test to see if host countries can deny rights to home country investors that are controlled by nationals of a third party
Pre-establishment Rights	152	0.07	0.260	0	1	Test for a clause to grant pre-establishment rights to foreign investors
Most Favoured Nation Treatment	153	1	0	1	1	Test for a most favoured nation clause
National Treatment	153	0.76	0.430	0	1	Test for a national treatment clause
Domestic Tax Exemption	152	0.51	0.502	0	1	Test for exemption on domestic taxation rules
Health Exemption	152	0.09	0.290	0	1	Test for an exemption on measure for public health
Unrestricted Repatriation	152	0.80	0.404	0	1	Test for unmitigated rights being granted to investors to transfer funds without restriction
Financial Crisis Safeguards	152	0.18	0.383	0	1	Test for a provision for host countries to restrict funds transfers during balance of payments crises
Repatriation Delay	152	0.53	1.358	0	6	Maximum number of months that it may take for a host country to transfer funds after a request by an investor
Managerial Nationality Requirements	152	0.11	0.316	0	1	Test for a clause preventing host countries from prescribing that a certain percentage of managerial staff must be a specified nationality
Board Nationality Requirements	152	0.01	0.114	0	1	Test for a clause preventing host countries from prescribing that a certain percentage of board members must be a specified nationality
Residence Clause	152	0.31	0.464	0	1	Test for a provision that exhorts host countries to speed visa and residency procedures for investors
Export Requirements	151	0.21	0.410	0	1	Test for a clause banning export performance requirements on foreign investors

Variable	N	Mean	Std Dev	Min	Max	Description
Local-Content Requirements	151	0.23	0.423	0	1	Test for a clause banning local-content performance requirements on foreign investors
Technology Transfer Requirements	151	0.04	0.196	0	1	Test for a clause banning technology transfer requirements on foreign investors
Arbitration	152	0.97	0.179	0	1	Test to see if investor-state arbitration is permitted
State Consent	147	0.99	0.116	0	1	Test for whether the host state automatically consents to arbitration
Domestic Courts	147	0.07	0.253	0	1	Test for a requirement that investor-state disputes first be submitted to a domestic court before international arbitration
Arbitration Waiting Period	147	5.442	4.133	0	24	Number of months an investor must wait after notifying the host state of the dispute before it can be submitted to international arbitration
ICSID	146	0.92	0.265	0	1	Test if investor-state arbitrations can happen at ICSID
ICSID Additional	147	0.27	0.447	0	1	Test if investor-state arbitrations can happen at ICSID's Additional Facility
UNCITRAL	147	0.52	0.501	0	1	Test if investor-state arbitrations can happen at ad hoc tribunals using UNCITRAL rules
Sector Exclusions	152	0.12	0.324	0	1	Test if certain industrial sectors can be excluded from coverage under the agreement
Treaty Duration	149	11.14	2.855	5	20	Number of years of the agreements initial validity, the minimum period before the treaty can be cancelled
Coverage Extension	151	12.66	4.028	5	20	Number of years of extension of the legal protections from the agreement in case the treaty is cancelled by one of the parties
Covers Pre-existing Investment	153	0.97	0.178	0	1	Test for coverage of investments made before the signing of the treaty

Appendix C Independent Variables Summary

Variable	N	Mean	Std Dev	Min	Max	Description
Date of Signature	165	Nov 1991	7.14 (yrs)	Dec 1960	Nov 2003	Date of treaty signing
Gross FDI Percent	115	1.998	1.976	0	9.172	Accumulated FDI as a percent of host country GDP in the year of signing
log Gross FDI	115	8.401	1.806	0	10.42	Log of Gross FDI, obtained by multiplying Gross FDI percent by the GDP of the host country
Log GDP	164	10.4974	0.639	9.35	11.75	Log of host country GDP in constant 2000 US dollars
GDP per capita	164	2607	2726	211	11935	Per capita GDP of the host country in constant 2000 US dollars
POLCON (Henisz 2002)	152	0.2386	0.200	0	0.5993	Measure of institutional credibility that measures the ability of governments to make credible commitments

Appendix D Bivariate Association Results

Dependent Variable Tested	Tri-modal Income	Bi-modal Income	Region	Treaty Date
National Treatment	1.110 (0.085)	0.456 (0.055)	16.364*** (0.327)	22.237*** (0.381)
Domestic Taxation	0.587 (0.071)	0.886 (0.088)	7.035* (0.247)	12.707*** (0.332)
Public Health Exemption	3.525 (0.152)	0.715 (0.069)	3.005 (0.141)	9.422** (0.249)
Fund Transfer Restrictions	6.737** (0.211)	6.597*** (0.208)	8.242** (0.233)	9.304** (0.247)
Financial Crisis Safeguards	6.857** (0.212)	1.332 (0.094)	15.023*** (0.314)	14.720*** (0.311)
Local-Content Performance Requirement	6.668** (0.210)	7.813*** (0.227)	0.288 (0.044)	8.717** (0.240)
Management Nationality Restrictions	0.932 (0.078)	0.023 (0.012)	1.673 (0.105)	7.888** (0.228)

Figures reported are Pearson's χ^2 with phi values in parenthesis.

* significant at .1 level, ** significant at .05 level, *** significant at the .01 level

Appendix E Test of Mean Difference Results

Dependent Variable Tested	Date of Signature	Gross FDI Percent	log Gross FDI	Log GDP	GDP per capita	POLCON
National Treatment	-3.554***	-2.158**	-1.776*	-1.162	-1.778*	-2.897***
Domestic Taxation	-3.081***	-0.724	-0.048	-0.845	-1.133	-0.575
Public Health Exemption	0.200	0.047	1.084	-0.339	0.186	0.719
Fund Transfer Restrictions	-1.612	-0.324	0.808	-0.063	0.699	0.987
Financial Crisis Safeguards	2.393**	3.177***	1.945*	-0.329	0.994	2.245**
Local-Content Performance Requirement	-1.402	0.029	1.863*	2.261**	2.133**	1.662*
Management Nationality Restrictions	-2.044**	1.078	-0.307	-0.129	-0.337	-0.547

Figures reported are t statistics, adjusting for unequal variances when necessary.
 * significant at .1 level, ** significant at .05 level, *** significant at the .01 level

Appendix F Scatter Plots for Scalar Variables

Figure 2 Maximum Delay in Repatriation of Assets by Host Country Income

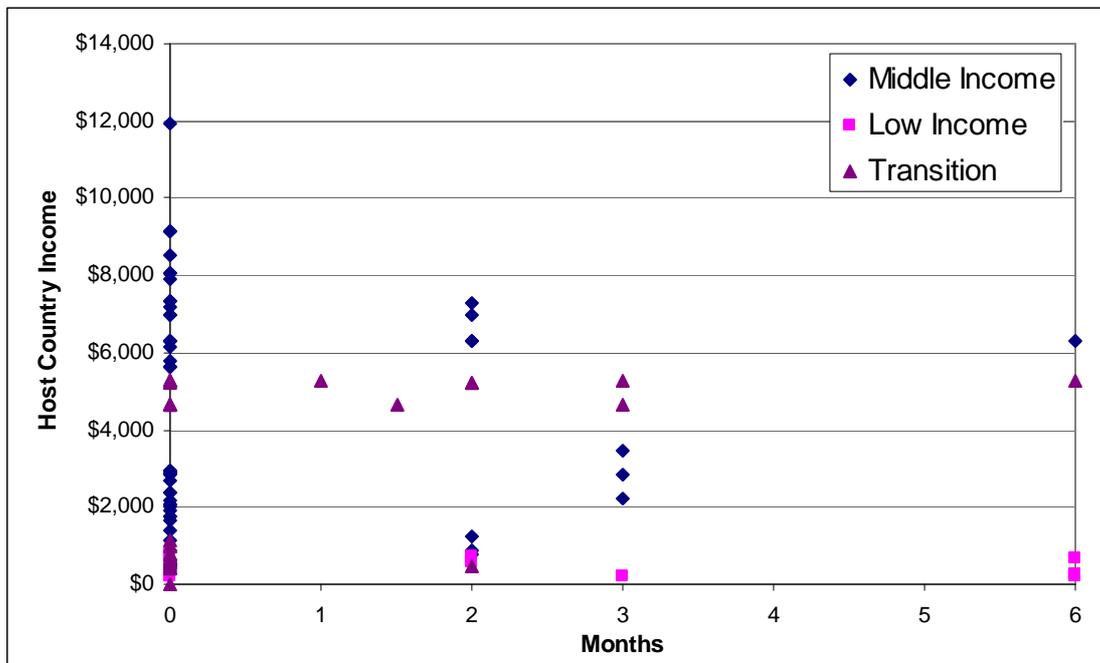


Figure 3 Arbitration Waiting Period by Host Country Income

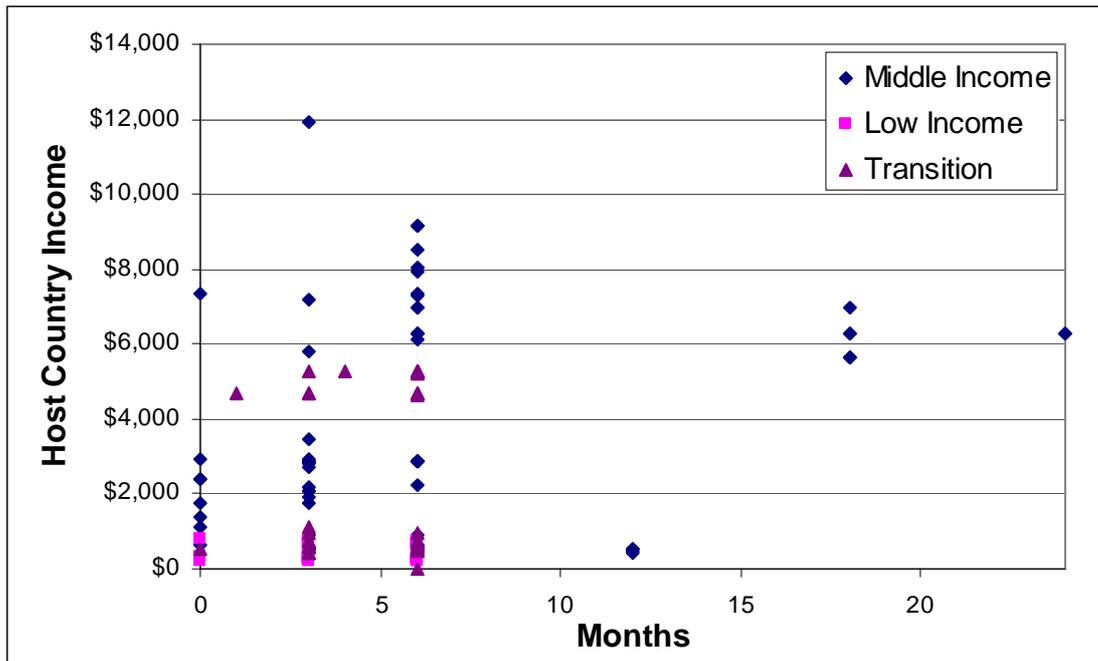


Figure 4 Coverage Extension After Treaty Cancellation by Host Country Income

