# International Investment Law and Foreign Direct Reinvestment*

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January 2018

**Abstract**

When a dispute arises, one goal of the law is to provide a means to return the parties to cooperation. The conventional expectation is that international investment law does not do this; rather, an aggrieved foreign investor that sues the host state "burns bridges" and divests. In this article, we use a newly constructed database of Investor-State Dispute Settlement (ISDS) arbitrations and firm-level bilateral investment to show that, in fact, foreign investors that sue reinvest in the host state at least 31% of the time (1990-2015). We find evidence that foreign investors in immobile sectors, that settle or win (more), that do not sue for direct expropriation, that sue under private contracts, and that do not face post-arbitration enforcement processes are more likely to reinvest. It remains an open question as to the conditions under which the likelihood of reinvestment is high enough for a host state to take adverse action toward a foreign investor, given the constraints generated by the de facto international investment regime.

*I thank Terrence Chapman, David Singer, Nate Jensen, Leslie Johns, Clint Peinhardt, and Carolina Moehlecke. I also thank audiences at the University of Houston, the International Studies Association, American Political Science Association, and the International Political Economy Society. For excellent research assistance, I thank Allyson Veile, Connor Smith, and students from Innovations for Peace and Development at UT Austin.

# 1 Introduction

Thousands of international investment agreements and contracts that include Investor-State Dispute Settlement (ISDS) provisions allow foreign investors to sue host states directly for compensation regarding alleged property rights violations—in ad hoc tribunals without an appeals system, without the approval of their home states, and often without exhausting local courts in the host state. Unsurprisingly, the backlash against ISDS and its potential to constrain states' sovereignty grows as more arbitrations arise.[1] As of 2016, eight states have pulled out of some ISDS-enabling treaties, and dozens more have renegotiated relevant treaty terms, sometimes en masse, although none of the 120-odd states that have been sued has eschewed ISDS altogether.[2] Such growing outcry prompts the question: what, if anything, is good about ISDS?

From one point of view, the ideal is that ISDS will resolve an investor-state dispute and facilitate a return to cooperation under the auspices of the host state's ex ante legal commitments. While the host state surely does not like paying compensation for a property rights violation, as required by pro-investor tribunal rulings, it would prefer compensation that makes breach "efficient" in economics jargon: the government takes an adverse policy action in the short-term, pays compensation to make the investor whole, and then then the relationship returns to the ex ante status quo (or better) in the long-term.[3] Further, the host state's hope would be that resolving the dispute in a legal setting, rather than in negotiations outside of formal procedures, should not in itself preclude a return to cooperation.

Many characterize ISDS arbitration as far from this ideal, a process that is a last resort for aggrieved investors in the vast majority of (or all) cases. Investors may expect that filing for ISDS arbitration escalates a conflict, pushing the host state to cut ties and retaliate by blocking the investor, whatever the arbitration outcome. If this is the case, invoking international law may generate costs to a point where investors no longer see investment as prudent. If investors in politically risky states expect conflict ex ante, they may specifically plan to earn a sufficient return on investment before that conflict arises; seeking compensation through ISDS may become the last stage of their investment strategy. Some see litigating investors as nefarious actors, intending

[1] Waibel et al. 2010.
[2] Peinhardt and Wellhausen 2016; Haftel and Thompson 2013.
[3] On efficient breach, see Rosendorff and Milner 2001; Rosendorff 2005; Pelc and Urpelainen 2015 among others.

to profit from ISDS arbitration without having made productive investments along the way.[4] A frustrated investor that does not deem itself sufficiently compensated as a result of ISDS arbitration, too, may choose to divest. In fact, a crucial characteristic of international investment law is that it does not dictate that the host state to change its underlying policy action that caused the (perceived) property rights violation. Thus, adjudication is about compensation for adverse actions and not a host state's commitment to changing the triggering adverse action or forestalling a future adverse action.[5]

Still, an aggrieved investor's view of international investment law might be consistent with the host state's more benign hopes: despite the formality of the process, an investor may attach value to fair adjudication of its claims via ISDS institutions. Priest and Klein (1984) famously model litigation as "purely economic": as litigation proceeds, parties form rational expectations of likely decisions based on information revealed in the process and direct costs, which does not in itself preclude a return to cooperation.[6] It is possible that at least some investors see the revealed information of a host state's compliance with the arbitration process as evidence of commitment to rule of law and, thus, reduced future risks.[7]

Several scholars focus on the effects of ISDS arbitration on third-party investors: ISDS is expected to trigger reputational and sovereignty costs for the host government that deter others from investing.[8] It has gone without saying that ISDS arbitration would deter claimant investors from continuing their investments. We challenge that conventional wisdom and consider variation in "reinvestment," which we define as the investor retaining investment in the host country during the ISDS arbitration process or investing in the host country after the process concludes. We ask: can international investment law facilitate a return to cooperation between an aggrieved investor and host state and, if so, under what conditions? A core contribution of this article is to take bilateral investor-state relationships seriously.

We find that 30.6% of claimant investors reinvest (223 of 729 ISDS arbitrations, filed from 1990-2014, with reinvestment assessed as of 2015). Thus, at least sometimes, an aggrieved investor

[4] As one lawyer puts it, "You have a lot of scuzzy sort-of thieves for whom this is a way to hit the jackpot." Quoted in Hamby, Chris. "The Court the Rules the World." BuzzFeed News: 28 August 2016.

[5] Contrast this with the requirements under the World Trade Organization Dispute Settlement Mechanism (DSM). Rosendorff 2005.

[6] Priest and Klein 1984: 4.

[7] On the positive relationship between FDI and rule of law, see Jensen et al. 2012.

[8] Kerner 2009; Simmons 2014; Allee and Peinhardt 2010; Wellhausen 2015*b*.

perceives that the host government violated its property rights, sues, and nonetheless reinvests. The incidence of reinvestment demonstrates that international investment law is not always as unique as it is assumed to be: ISDS can facilitate a return to cooperation, a core goal of law.

We go on to explore the determinants of reinvestment. Consistent with existing theory about the limited exit options of immobile (site-specific) investors, we find that investors in such sectors are more likely to reinvest. We also show that foreign investors that settle, that win a pro-investor ruling, and that win a greater proportion of their initial claim are more likely to reinvest. We find evidence that less public disputes, characterized by foreign investors that sue under private contracts rather than international treaties, are more likely to reinvest. We find some evidence that foreign investors that claim that adverse government actions disrupted the value of their property—rather than stripping them of ownership—are more likely to reinvest. Finally, we find evidence that claimant investors that do not face post-arbitration litigation, including enforcement and/or annulment proceedings, are more likely to reinvest. Thus, structural characteristics of the investor and characteristics of the dispute and adjudication process are associated with the likelihood of a return to cooperation.

We find that formally litigating a property rights dispute does not in itself preclude future cooperation between the particular claimant investor and host state. From the host state's point of view, committing to and following through with formal ISDS dispute resolution mechanisms can correlate with much-sought-after FDI. Moreover, since ISDS compensation awards do not require the host state to change its policy, it can sometimes have its cake (take an adverse action) and eat it too (retain a foreign investor). Nonetheless, a 30.6% reinvestment rate means that the vast majority of foreign investors appear to react poorly to the need for ISDS arbitration and do not reinvest (at least in the time period close to arbitration). It remains an open question as to the conditions under which the likelihood of reinvestment might be high enough to incentivize a host state to take adverse action toward a given foreign investor, given the constraints generated by the de facto international investment regime.

## 2 ISDS and Reinvestment

Scholars continue to explore how a state's commitment to international investment law shapes the behavior of current and potential foreign investors in aggregate.[9] In contrast, the effect of law on the aggrieved investor that sues a host state through ISDS arbitration has gone unstudied. As conventional wisdom would have it, this question is uninteresting. Via ISDS, a host state can buy its way out of a property rights violation by compensating the claimant and making it whole to its ex ante position. But ISDS arbitration means that the claimant investor's worries about political risks have been realized; that the host state incurred costs through litigation and compensation; and that, in all likelihood, bridges are burned.

To challenge the conventional wisdom, we ask whether an ISDS arbitration can result in reinvestment by the (once-)aggrieved, claimant investor.[10] We draw on a new database of ISDS arbitration filings by foreign investors from 1990-2014 and count 729 ISDS arbitrations that were brought in the period.[11] Importantly, our data account for 113 arbitrations that are not present in a standard data source provided by the UN Commission on Trade and Development (UNCTAD). However, neither all ISDS arbitrations nor all characteristics of known arbitrations are public, such that we must keep in mind biases implied by selection effects and missing data. In sum, we find an overall reinvestment rate of 30.6%. Whether one considers 30.6% low or high, it establishes variation worthy of explanation—especially from the point of view of a host state weighing the benefits of an adverse action against the costs associated with ISDS arbitration.

We code reinvestment as occurring if we can find positive evidence of one of three conditions: the claimant investor stays in the host state during and after the ISDS arbitration; the claimant investor leaves during or after the arbitration but returns to the host state by December 2015; or the claimant investor is operating in the host state as of December 2015 (whether or not we know what happened in the interim).[12] We also code reinvestment as occurring when we have evidence that

[9] E.g., Sauvant and Sachs 2009; Allee and Peinhardt 2010; Simmons 2014; Poulsen 2015; Wellhausen 2015*c*.

[10] An ISDS arbitration is one where the claimant is a foreign firm(s) (or an individual investor(s)) and the respondent is a state. Commercial arbitrations in which a state-owned enterprise is the respondent are governed by different law and are outside the scope of this article.

[11] Wellhausen 2016. We ignore the 26 public investment arbitrations filed from 1965 to 1989, as the post-colonial context in which these took place makes us skeptical that more recent behaviors are analogous. See Schultz and Dupont 2014.

[12] When multiple investors are claimants, we code reinvestment as occurring if at least one claimant fits at one of these criteria. To code reinvestment by publicly traded companies, we check annual reports for the penultimate year of the arbitration process and the year it concludes to see whether the foreign investor stayed in or left the host

a subsidiary of the claimant fits one of these conditions. Indeed, continuing operations in the host state through a subsidiary—under a perhaps less publicized name—might in itself be a political risk mitigation strategy that enables the one-time claimant to reinvest without highlighting its contentious history. We either can or cannot find evidence of reinvestment, with the presumption that we are undercounting reinvestment and biasing results away from our expectations.

REINVEST is a binary variable, because the precise characteristics of investments are regularly private information. As such, we cannot consistently code the relative size of an investor's presence before, during, or after arbitration. At the extreme, a foreign investor's presence in the host state after arbitration could be a skeleton operation, incurring fixed costs but minimal variable costs. Yet even if this were the case, reinvestment is the appropriate coding. First, the counterfactual that ISDS arbitration is associated with total firm exit is regularly espoused by officials, practitioners, and scholars and thus is not a "straw man." Second, the number of ISDS arbitrations has grown precipitously since the late 1990s and especially in the 2010s. Because time has not yet given us the chance to observe investment growth in instances in which ISDS arbitration is quite recent, we do not know that minimal operations will remain minimal.[13] In sum, we see our binary REINVEST measure as an accurate conceptualization of whether international investment law can correlate with cooperation—at whatever intensity—between (once-)disputing parties.

Table 1 reports summary statistics. By the end of 2015, there are 223 instances of reinvestment around 729 ISDS arbitrations filed from 1990-2014 (30.6%). In 198 instances, we know that the claimant investor was present in the host state as of the end of 2015. In some instances, we can find evidence of what happened closer in proximity to the ISDS arbitration. The claimant investor continued operations in the host state during and after arbitration in at least 140 instances. In contrast, we find clear evidence that the foreign investor exited the host state but reinvested after arbitration in only 14 instances. These findings undercut the common notion that exit comes first and a foreign investor invokes ISDS arbitration only as a final, follow-up measure.

The 30.6% reinvestment rate we uncover establishes that reinvestment is not the norm. In

state. We then check subsequent annual reports every two years through 2015 to see whether the foreign investor was present in the host state at a later date. For companies for which annual reports are not available, we rely on searches of specialty press to find evidence of reinvestment. IAReporter is a particularly useful source. See Codebook for details.

[13] Li (2009) explores the half-life of expropriation events (but not legal actions) through their effect on state-level FDI.

Table 1: Reinvestment Summary*

| *Category* | *Reinvestment* | *Percentage* |
|---|---|---|
| **Total** | **223** | **30.6%** |
| Invested as of December 2015 | 198 | 27.2% |
| Retained investments during and after arbitration | 140 | 19.2% |
| Exited host state but later reinvested | 14 | 1.9% |

*Of 729 ISDS arbitrations (filed 1990-2014). "Invested as of December 2015" is not mutually exclusive with the other subcategories.

the majority of instances, bridges may in fact be burned, at least within the time period that we examine. The absence of reinvestment can mean that the host state loses the investment altogether. However, a host state could also find ways to replace that investment, which would mitigate the loss incurred around ISDS arbitration. For example, the host state could take over ownership and operate any remaining assets. The host state could also resell (or give) remaining assets to a domestic firm that replaces the investment. Note that in these cases the host state still incurs a loss from replacing foreign ownership with domestic ownership, given that foreign investors are more productive. Still, that loss may not swamp the benefits the host state derives from its adverse action.

Further, the host state may remain interested in FDI but uninterested in continuing a relationship with a litigious investor. In this case, the host state could seek out an alternative foreign investor to operate the assets; another foreign investor may be willing and able to take over ownership and operate the remaining assets of its former competitor. The 2005 ISDS arbitration *Walter Bau v. Thailand* provides a pertinent anecdote: by the time the tribunal ruled in favor of the German investor in 2009, Thailand had already hired an investor from Hong Kong to complete the toll road that Walter Bau had initially been hired to build.[14] Nonetheless, we would expect replacement foreign investors to take additional steps to guard against their own political risk, given that they enter an investment setting in which risks have been realized—and one in which tensions are perhaps heightened in the wake of litigation.

That said, reinvestment occurs. How might we understand a (once-)aggrieved foreign investor's willingness to continue operations in the host state that aggrieved it? We see reinvestment as evidence that, at least sometimes, dynamics around international investment law are not unique.

[14] Wellhausen 2015*a*.

Law can provide a set of rules on which actors can coordinate their joint expectations.[15] Rather than precluding a further relationship, formal adjudication can allow the foreign investor and host state to coordinate on adjustments to their relationship in the wake of the host state's adverse action. The presence of reinvestment demonstrates that use of formal international law is not in itself evidence that the relationship is beyond repair.

A useful way to conceptualize the resolution of and reinvestment following an investor-state dispute is through a time-inconsistency framework. Accepting FDI has become a standard development policy, because foreign investors are expected to generate the kinds of long-term growth, employment, technology transfer, and other benefits that can aid a state's leaders in their desire to remain in or otherwise benefit from power. A host state may have a long-term preference that a particular foreign investor remain productive in its territory, if the host state evaluates that the foreign investor is generating sufficient benefits. Yet the host state may face a short-term shock that motivates it to act against its long-term preference.[16]

A variety of economic and political exigencies could generate such a short-term shock.[17] For example, the host state may need to breach a contract to raise cash in bad times.[18] In good times, the host government may be motivated to reevaluate the fairness of contracted profit splits; when oil prices are high, domestic actors may be dissatisfied with the size of the gains accruing to the foreign investor. The host state may face a shock to its foreign policy goals. For example, upon taking control of Crimea, Russia nationalized all Ukrainian-owned assets (and is being sued for these actions) although Russia generally accepts FDI.[19] The host state may be moved to take adverse action against a sector or asset if, for example, foreign investors' contributions to the host economy become a low priority for a period of time. For example, during the 2008 financial crisis Belgium bailed out its domestically owned banks but did not bail out a Chinese-owned bank Ping An (and is being sued for this inaction), despite the fact that Belgium remains open to FDI in its financial sector. A host state may seek to update a regulation and prioritize that action over its

[15] Keohane 1984; Johns 2012.

[16] If the host state evaluates that a foreign investor is not bringing about sufficient benefits, its short-term and long-term preferences would align and its adverse action would not be time-inconsistent.

[17] Maurer 2013; Wellhausen 2015*c*. Weak institutions may allow the state's leaders more leeway to act on their incentives to breach. Jensen 2008.

[18] Consider, for example, Argentina's 2001-2002 choice to devalue and break the dollar-peso parity on which foreign investors' contracts were based; this action is the basis of many ISDS arbitrations.

[19] For the role nationality plays in investor-state disputes, see Wellhausen 2015*c*.

long-term interest in FDI. Such an action may even inadvertently conflict with foreign investors' property rights. For example, Slovakia argued that its re-regulation of its health insurance sector had nothing to do with the Dutch insurers who later filed for arbitration; the Slovak government claimed it had no idea that its action would be considered adverse.[20] Whatever its motive (or not), a host state can still be interested in accruing long-term benefits from a particular foreign investor despite taking an action today that conflicts with the foreign investor's interests.

Our findings of reinvestment demonstrate that ISDS arbitration can at least sometimes be a means for foreign investors and host states to resolve the costs of a host state's time-inconsistent action. Reinvestment indicates that the host state allows the claimant investor to remain in the country; ISDS arbitration is not consistently associated with a concept like retaliation, revenge, or the like on the part of the host state. Reinvestment also indicates that the foreign investor is sufficiently satisfied with the resolution of the dispute to continue to operate in the host state; invoking international law via a formal arbitration process is not consistently associated with exit. The fact that future cooperation sometimes occurs despite formal adjudication is a bright spot for a robust literature that finds positive correlations between rule of law and FDI.[21]

Under what conditions is reinvestment more likely to take place? We next use additional newly collected data to analyze which investor-state relationships are more likely to become cooperative again and which are more likely to dissolve in the wake of an ISDS arbitration. From the point of view of the host state, understanding the determinants of reinvestment can shape their decision to take an adverse action—and risk a formal adjudication process—in the first place.

## 3 Variation in Reinvestment

We hypothesize that structural characteristics of FDI; the extent of a claimant's grievance and success; the claimant's legal strategy; and post-ISDS arbitration enforcement actions are important correlates of reinvestment.

The canonical explanation for the effects of investor-state relations on investment behavior operates via sector. Some sectors are more vulnerable to property rights violations because they

[20] *HICEE B.V. v. The Slovak Republic*, PCA Case No. 2009-11.

[21] E.g., Li and Resnick 2003; Staats and Biglaiser 2012; Jensen et al. 2012.

are "captured," meaning that their assets are immobile or site-specific.[22] In our context, foreign investors that cannot feasibly exit would be more likely to reinvest despite adverse treatment.[23] A foreign investor with the capability of making a site-specific investment can negotiate a particularly advantageous deal ex ante, if the host state requires the foreign investor's capital and expertise. However, as time goes on and the foreign investor makes its site-specific investments, the foreign investor loses a credible threat of exit, and the deal with the host state "obsolesces."[24] Foreign investors in sectors characterized by site-specific investments may thus have significant grievances with the host state and in some cases use ISDS arbitration to adjudicate those grievances. Yet the structure of the sector implies that a foreign investor has incentives to reinvest, even if it invokes formal adjudication.[25] In contrast, foreign investors in sectors characterized by more mobile, non-site-specific investments retain better exit options, such that we expect them to reinvest less in general. In our setting, foreign investors in mobile sectors should reinvest less regardless of invoking ISDS arbitration.

**Hypothesis 1.** *An ISDS claimant is more likely to reinvest if it operates in a sector characterized by immobile, site-specific assets.*

Table 2 reports the distribution of ISDS arbitrations and rates of reinvestment by sector. We endogenously created these eleven sector categories from the data.[26] We then separate sectors by mobility. Consistent with Hypothesis 1, rates of reinvestment in immobile (site-specific) sectors are generally higher than those in mobile sectors.[27] The reinvestment rate in the canonically captured oil and gas sector is the highest. The reinvestment rate is also high for investors in utilities, which consist mainly of water and sewage concessions, power plants, and electricity distribution networks; these investments are specific to a particular market. Similarly, telecom-related ISDS arbitrations have to do with how and to whom the host state distributes licenses for cellular networks, which are demarcated by political borders and thus have limited exit options. Reinvestment rates in the

[22] Frieden 1994; Dunning 1980.

[23] Note that "captured" investors can reduce the size of their investment in a host state, but they are nonetheless more likely to continue some presence in the host state.

[24] Vernon 1971.

[25] This line of reasoning suggests that host states with many immobile (site-specific) investors would be willing to sign onto ISDS-enabling law but then go on to violate property rights without following through with ISDS arbitration processes. However, the value of such a strategy would depend crucially on the indirect effects of property rights violations on other investors' behavior. See Allee and Peinhardt 2010; Wellhausen 2015*c*, among others.

[26] In five instances, the sector of the claimant investor is unknown.

[27] This variation exists even if the reader might be dissatisfied with some of our characterizations of mobility.

transportation sector—highway, bridge, and port construction projects—are also above the mean. Reinvestment rates in mining, agriculture, and real estate are below the overall mean.

Nonetheless, foreign investors in mobile sectors are both filing for arbitration and sometimes reinvesting. Reinvestment in manufacturing is above the overall mean, and percentages in services, tourism, and finance are still far from zero. Thus, while we have evidence of high reinvestment rates among immobile (site-specific) investors, it is not a fool's errand to consider other determinants of reinvestment.

Table 2: Reinvestment by Sector

| *Sector* | *Reinvestment* | *Cases* | *Percentage* |
|---|---|---|---|
| **Immobile (Site-specific)** | | | |
| Oil/Gas | 46 | 113 | 40.7% |
| Utilities | 53 | 140 | 37.9% |
| Transportation | 18 | 53 | 34.0% |
| Telecommunications | 17 | 51 | 33.3% |
| Mining | 15 | 64 | 23.4% |
| Agriculture | 6 | 29 | 20.7% |
| Real Estate | 3 | 23 | 13.0% |
| **Mobile** | | | |
| Manufacturing | 32 | 98 | 32.7% |
| Services | 21 | 73 | 28.8% |
| Tourism | 5 | 28 | 17.9% |
| Finance | 7 | 52 | 13.5% |
| Unknown | 0 | 5 | 0% |

Next, we focus on the result of ISDS arbitration. A claimant investor invokes ISDS arbitration with the expectation that it will be compensated for the costs of the state's adverse action as a result. Sometimes, a claimant investor agrees to a pre-ruling settlement; we (like the legal community) see this as an investor win: the claimant investor is satisfied with the compensation it receives via settlement as weighted against its expectations of the tribunal's ruling and the costs of going forward.[28] A claimant investor that wins a pro-investor tribunal ruling receives compensation, although this compensation may be less than the claimant requested. Still, this outcome, like settlement, constitutes an investor win, because the claimant investor receives at least some compensation. In contrast, when the tribunal makes a pro-state ruling, the claimant investor is not compensated (and it may have to pay the host state's litigation costs). From the claimant

[28]Even an investor that abandons its case may be thought of as having received compensation at least in the sense that it caused the host state to incur costs. Settlements prior to the invocation of ISDS arbitration are not the focus of this article.

investor's point of view, the harm done by the state's adverse action is unchanged. We make the straightforward hypothesis that claimant investors that are compensated—through settlement or a pro-investor ruling—are more likely to reinvest than those that are not. Note, however, that we do not have a clear theoretical expectation of how the reinvestment should compare after settlement or an investor win, as compensation takes place in both instances.

This seemingly banal point that winning compensation is associated with reinvestment is made more interesting because of what international investment law says about host state obligations beyond compensation. In short, ISDS only concerns compensation. Across the muddy field of international investment law, there is no requirement that a host state change its underlying policy action that caused the violation. As Pelc and Urpelainen put it, "Once payment is made, investors have no further recourse: the matter is closed."[29] This is a meaningful difference between the investment world and the trade world, as the World Trade Organization Dispute Settlement Mechanism (DSM) requires states to change policies in order to return to normal cooperation.[30] Relevant here is that compensation in the absence of policy change will not necessarily restore the investment environment to its ex ante position. Even if the claimant is made whole from a financial point of view, it could still be investing in a host state that continues to enact the problematic policy. Further, even if the host state changes the underlying policy—despite not being required to do so—the claimant investor would still operate in a host state that understands adverse policies have a price but are not prohibited. One of the most important international organizations in this sphere, the UN Conference on Trade and Development (UNCTAD), specifically celebrates the notion that ISDS is about compensation but not about constraints on state policy. In fact, UNCTAD advocates for limits on investors' ability to sue in ISDS, because suits raise the specter of incentivizing policy change. In particular, UNCTAD is frustrated that arbitration goes forward even if state policies are consistent with "sustainable development goals."[31] The implication is that in such circumstances, the host state should neither be pressured to change its policies or, indeed, provide compensation for choosing those policies. With this in mind, it is a legitimate exercise to test whether winning compensation correlates with reinvestment when the law does not compel the host state to change its policy.

[29] Pelc and Urpelainen 2015: 257.
[30] Rosendorff 2005.
[31] UNCTAD "Investment Policy Framework for Sustainable Development," 2015.

**Hypothesis 2.** *An ISDS claimant is more likely to reinvest if it settles the arbitration before its conclusion or wins a pro-investor ruling.*

Of the 729 ISDS arbitrations filed from 1990-2014, 137 remain incomplete. Of the 592 completed arbitrations, settlement occurred in 34%, the investor won in 29%, and the state won in 34%.[32] The coding for settlement includes a public notice of settlement and/or the discontinuation of the arbitration tribunal. It also includes ISDS arbitrations in which tribunals record no legal action that moves the arbitration forward for at least 10 years. A pro-investor ruling is any tribunal ruling in which the state was found to have acted unlawfully. A pro-state ruling is any tribunal ruling that results in no liability for the state; such rulings include outcomes based on jurisdictional issues as well as outright rulings that the claimant's complaint is without merit.[33]

Table 3 reports summary statistics on reinvestment by case outcome. The reinvestment rates for settlement and investor win are higher than reinvestment in the case of state win, as expected. Nonetheless, the 23.8% reinvestment rate for state win demonstrates that the outcome of ISDS arbitration in itself is insufficient to fully explain reinvestment trends. Additionally, in 24.8% of incomplete arbitrations, the claimant investor has reinvested (meaning that it has stayed in the host state during the arbitration process). That reinvestment takes place before a dispute is adjudicated, too, is worthy of further explanation.

Table 3: Reinvestment by Outcome

| *Winner* | *Reinvestment* | *Cases* | *Percentage* |
|---|---|---|---|
| Settlement | 79 | 200 | 39.5% |
| Investor | 57 | 172 | 33.1% |
| State | 48 | 202 | 23.8% |
| Incomplete | 34 | 137 | 24.8% |
| Unknown | 5 | 18 | 27.8% |

Hypothesis 2 implies that the greater the compensation a claimant investor receives, the more likely it is to reinvest. A key measure of the size of the investor's loss is its initial claim in ISDS arbitration filings.[34] We divide the awarded compensation by the investor's initial claim to generate a percentage measure of the claim won.[35]

[32]The combined 63% settlements and pro-investor tribunal rulings suggest to some that investors benefit greatly from the system. Simmons 2014.

[33]In 18 instances, the outcome of a completed arbitration is unknown.

[34]We assume that the amount of claim-size inflation is randomly distributed across the data.

[35]We code only the main amount claimed and exclude ancillary claims regarding interest. If the claimant investor

**Hypothesis 3.** *An ISDS claimant is more likely to reinvest if it wins a larger proportion of the compensation sought.*

We have data on both the initial claim and the award in 339 instances.[36] Of these, 191 claimant investors were awarded 0 compensation (56.3%). Among those that were awarded compensation, the mean percentage won is 36.7%. Table 4 provides summary statistics on reinvestment by the percentage won. Reinvestment rates are generally higher when the investor wins more of its claim, although there are some exceptions.

Table 4: Reinvestment: Size of Compensation

| *Percentile* | *Claim Won (%)* | *Reinvestment* | *Cases* | *Percentage* |
|---|---|---|---|---|
| 0-50th | 0% | 54 | 191 | 28.3% |
| 51-75th | 24.2% | 14 | 64 | 21.9% |
| 76-90th | 52.7% | 19 | 51 | 37.3% |
| 91-95th | 77.7% | 9 | 16 | 56.3% |
| 99th | 100% | 4 | 14 | 28.6% |

Next, we consider whether the type of adverse action of which a host state is accused affects the likelihood of reinvestment. The types of legal claims available to an aggrieved investor are determined by the treaty or contract invoked. All allow claims of direct expropriation. Direct expropriation is the taking of property without consent, which means that the state's adverse action changes the ownership of otherwise foreign-owned property. The most extreme form is full nationalization, but direct expropriation occurs whether the state takes ownership of any expropriated assets or otherwise resells them without the claimant investor's consent. When investors claim direct expropriation, we expect less reinvestment. Simply, when as a result of the state's adverse action the claimant investor owns less property in the host state (if any), it has less ability to reinvest. Additionally, direct expropriation is the most severe realization of political risk, in the sense that the foreign investor is deprived of the ability to earn any profits from the expropriated property. More extreme realized risk is more likely to deter an aggrieved investor.

In contrast, other legal claims available to foreign investors in treaties and contracts concern the host state's adverse impact on the foreign investor's operations and its expected profits.

offers a range, we choose the lowest amount requested. Per Hypothesis 2 we would expect the percentage of the claim awarded in a settlement to track with reinvestment. However, settlements are so rarely public information that we have very little confidence that those few settlements that leak are representative.

[36] We do not expect data to be missing at random, nor do we have a full theory explaining variation in data availability. Thus, tests of Hypothesis 3 should be taken with a grain of salt.

These claims include indirect expropriation; fair and equitable treatment; a minimal standard of treatment, including denial of justice; full protection and security (or similar); arbitrary, unreasonable, and/or discriminatory measures; national treatment; most-favored-nation treatment; transfer of funds; and umbrella clauses. When these claims are invoked, the investor accuses the government of reducing the value of its investment, but the investor does not accuse the government of having illegitimately taken over ownership of its assets. In the absence of direct expropriation, the claimant investor still owns its property in the host state and thus can more easily continue to invest. We expect more reinvestment in instances when the claimant investor does not invoke direct expropriation.[37]

**Hypothesis 4.** *An ISDS claimant is more likely to reinvest if it does not invoke the legal claim of direct expropriation.*

In 474 instances, investors claims are reported in public records.[38] In the vast majority of cases, claimant investors do not invoke direct expropriation. Reinvestment rates among these investors are higher than those that invoke direct expropriation alone or in combination.

Table 5: Reinvestment by Expropriation Claim

| *Type* | *Reinvestment* | *Cases* | *Percentage* |
|---|---|---|---|
| Direct | 13 | 74 | 17.6% |
| Direct + Any other claim | 8 | 50 | 16% |
| Any other claim | 111 | 350 | 31.7% |

Next, we hypothesize that cases that are kept more private are more likely to be associated with reinvestment. In these instances, both the foreign investor and the host state can better "save face" while returning to cooperation after a dispute. A public arbitration may effectively advertise the foreign investor's problems in the host state, and that advertisement may make current and potential shareholders wary of reinvestment. Further, a host state engaged in a very public dispute may find that domestic audiences prefer to ostracize the litigious investor rather than reconcile with it. In short, publicity can take incentives to return to cooperation off the table. If reinvestment is a desirable goal, this argument suggests a downside of the move toward greater transparency in

[37] Pelc (2016) argues that cases in which indirect expropriation is invoked are of lower quality. This coincides with the argument that a claim of direct expropriation indicates greater realized political risk.

[38] We code initial claims rather than resolved claims, as an investor might see itself as having been directly expropriated—and predicate its reinvestment on that—whatever the legal outcome. Additionally, because of judicial economy tribunals typically do not adjudicate all claims.

ISDS arbitration.

**Hypothesis 5.** *An ISDS claimant is more likely to reinvest if its ISDS arbitration is private.*

Clearly, if an ISDS arbitration made it into our data, it is not private. We approximate privacy by focusing on the legal instrument invoked by the claimant investor. If the claimant investor invokes a public, international treaty in order to access ISDS arbitration, other foreign investors (and their law firms) with access to that treaty are likely to be interested in how that treaty is applied. We see this as making the case more public, in the sense that more potentially interested actors find it useful to follow it and pay attention to the outcome. In contrast, when a claimant investor invokes its own specific contract with the host state, other actors are less interested in the case because it is less applicable to their situations. We characterize this as making the arbitration more private, in the sense that interested actors are less likely to incur the costs of closely following the proceedings. In Table 6 we separate reinvestment by legal instrument invoked. As expected, the reinvestment rate when a contract with the host state is invoked is higher than when a BIT is invoked or when any IIA is invoked. We also include the reinvestment rate when domestic law in the host state is invoked, for which we do not have strong priors. The rate falls between that for contracts and international treaties.

Table 6: Reinvestment by Legal Instrument Invoked*

| *Type* | *Reinvestment* | *Cases* | *Percentage* |
|---|---|---|---|
| Contract with Host State | 30 | 70 | 42.9% |
| Domestic Law of Host State | 28 | 77 | 36.4% |
| Bilateral Investment Treaty (BIT) | 153 | 523 | 29.3% |
| International Investment Agreement (IIA) | 189 | 642 | 29.4% |

*Categories are not mutually exclusive, as claimants can invoke multiple instruments.

Finally, while there is no formal appeals process in international investment law, initial rulings can be followed by annulment and/or enforcement processes. Annulment is only possible at one venue, the World Bank's International Center for the Settlement of Investor Disputes (ICSID). The criteria for annulment are very limited, to questions of procedure rather than questions of the accuracy of tribunal rulings. Annulment processes can be invoked by the host state or the claimant investor, which may be interested in creating a clean slate that can facilitate another "bite at the apple." Claimant investors may also have other motivations, for example, to dispute a tribunal ruling that they pay host state costs. Whether annulment is filed by the host state or the claimant

investor, the ISDS arbitration itself has not fully resolve the investor-state dispute. We expect any reinvestment to be foregone or delayed.

Following arbitration in any venue, parties are generally allowed to challenge rulings in the domestic courts of the seat of arbitration, that is, under the domestic law of the state in which the arbitration is physically held. For example, when sued under NAFTA, Mexico is within its rights to apply to domestic Canadian courts to challenge a ruling in favor of a US investor, if the tribunal was constituted in Canada.[39] However, this is still not an appeals process. Even if a pro-investor tribunal ruling is set aside in the seat of arbitration, it does not necessarily remove the state's obligation to pay the award, because there is not binding precent in the complicated de facto international investment law regime.[40] Consistent with this, host states filing for set-asides are not necessarily rejecting payment of compensation. Still, delay in compensation payment by the host state conflicts with the spirit of resolving the dispute in a timely way—whatever the law allows.[41] Whichever party files for a set-aside, the investor-state dispute has not been resolved by the ISDS arbitration. Thus, reinvestment should be limited.

Altogether, international investment law is predicated on voluntary host state compliance with compensation awards. Even host states interested in FDI may face pressure to not pay awards. ISDS rulings have been inconsistent, even across the same set of facts, and host governments are frustrated over the lack of an appeals process. These aspects of international investment law have led practitioners, scholars, and host states to question its legitimacy.[42] In the end, compensation awards require the host state to effectively pay taxpayer money directly to foreign corporations. Publicity around these characteristics of the de facto international investment regime has lead to domestic unrest and influenced election outcomes in the developing world.[43] Thus, domestic pressures in particular might have an effect on compliance rates.

If the state does not pay the award to the foreign investor's satisfaction, the onus is on the investor to get the award enforced. Under the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention), 156 signatory states have committed

[39] See, for example, Mexico's challenges to the award made in *Cargill v. Mexico*.

[40] Much contemporary litigation circles around the implications of set-asides. Bishop 2009.

[41] We are more interested in the optics around enforcement procedures rather than their legality.

[42] See Bishop 2009; Howse and Teitel 2010; Van Harten 2012; Simmons 2014; Schultz and Dupont 2014; Haftel and Thompson 2013, among others.

[43] Peinhardt and Wellhausen 2016.

to recognize international arbitration awards including those from ISDS proceedings. Foreign investors look to enforce their awards in domestic courts of third-party states that (1) are signatories and (2) in which the host state holds significant, accessible assets.[44] Accessible assets are those that are not subject to sovereign immunity protections. Assets that are part of legitimate international state activity generally cannot be seized, such as embassy property or central bank assets, although whether or not any particular asset qualifies is often the subject of litigation. (Host states are accused of making themselves "enforcement-proof" when they take steps to keep assets out of claimants' reach.) In 2012, the attempted seizure of an Argentinian military ship docked in Ghana—disallowed by a ruling under the International Law of the Sea—is an extreme example of US investors' attempts to enforce their award.

Foreign investors sometimes choose to file for enforcement in the domestic courts of the host state. Host states, too, sometimes challenge rulings in their own courts, using them as a sort of appeals venue. While foreign investors are free to choose this path, the law in many if not all cases precludes the host state from going to its domestic courts after an ISDS arbitration. Indeed, the motivation behind ISDS arbitration has been to adjudicate disputes outside of host state courts that may be biased toward the host state. In brief, follow-on filings in the host state's domestic courts also indicate that the investor-state dispute is not fully resolved and the state is not fully compliant, reducing reinvestment.

Enforcement proceedings are costly and complicated. Once initiated, they can turn into a war of attrition between the foreign investor and a recalcitrant host state, often pulling diplomats into the fray. Sometimes, foreign investors agree to settlements on ISDS awards, for example, accepting a portion of the award today, agreeing to a payment plan, agreeing to be paid in a different currency, or accepting payment in bonds. Whatever the circumstances, the necessity of enforcement proceedings clearly indicates that the ISDS arbitration did not resolve the dispute and/or lead to immediate host state compliance. In these instances, reinvestment should be less likely. In contrast, when neither annulment nor enforcement proceedings take place, we presume that the claimant investor is sufficiently satisfied with the arbitration outcome and the host state's compliance so as to choose not to pursue the case further. Thus, reinvestment should be higher.

[44]For example, foreign investors have tried to enforce ISDS compensation awards in states including the US, the UK, France, Luxembourg, Germany, Sweden, Austria, Denmark, and Canada.

**Hypothesis 6.** *An ISDS claimant is more likely to reinvest if the arbitration is not followed by annulment or enforcement proceedings.*

Our variable No enforcement proceedings equals 1 when the initial ISDS tribunal ruling is not followed by annulment processes and/or formal enforcement proceedings of any kind. Note that we are surely undercounting the number of foreign investors that are frustrated with the state's willingness to pay and speed in paying ISDS compensation awards.[45] Table 7 provides summary statistics on reinvestment in the presence of follow-on proceedings. Average reinvestment in the case of annulment or judicial enforcement is below the overall mean.

Table 7: Reinvestment by Annulment and Enforcement Proceedings*

| *Enforcement* | *Reinvestment* | *Cases* | *Percentage* |
|---|---|---|---|
| Annulment (ICSID) | 25 | 93 | 26.9% |
| Formal Judicial Enforcement | 18 | 66 | 27.3% |

*Categories are not mutually exclusive.

# 4 Empirics

In this section, we test our hypotheses in separate, stripped-down models as well as in horse-race models to shed light on their relative explanatory power. Each line in the data codes the reinvestment status (as of December 2015) of the claimant foreign investor in each of the 729 ISDS arbitrations brought in the period 1990-2014. We use logit as the outcome is a bivariate one, indicating whether reinvestment took place in the period or not. We reduce the sample to completed ISDS arbitrations when the testing the hypothesis requires this is the correct comparison category: settlement or investor win; percentage of award won; and presence of annulment/enforcement proceedings. We control for a time trend counting the years since filing (beginning at 1990). Standard errors are clustered by host state.

Table 8 reports results. We find positive and significant effects on our measures testing Hypotheses 1-3 and Hypotheses 5-6: Immobile, Settlement/Investor win, % Claim won, ISDS through contract, and No enforcement proceedings. The coefficient on No claim

[45] For example, a publicly traded firm might be interested in keeping its trouble in getting compensated somewhat private, lest shareholders worry that delays unduly adversely affect the firm's bottom line. Still, the idea that claimant investors resorting to ISDS arbitration might be willing to make concessions after winning, like keeping payment delays private, suggests in itself an interest in returning to cooperation.

of direct expropriation (Hypothesis 4) is positive as expected but imprecisely estimated and not significant. All of the Hypotheses tested on the subset of completed ISDS arbitrations find support; the magnitude of the effect is greatest for % Claim won.[46] Taken together, these simple regression models reinforce the trends suggested by summary statistics presented above.

Table 8: Reinvestment: Bivariate Relationships

| | (H1) | (H2) | (H3) | (H4) | (H5) | (H6) |
|---|---|---|---|---|---|---|
| Immobile | 0.467** | | | | | |
| | (0.206) | | | | | |
| Settlement/Investor win | | 0.646*** | | | | |
| | | (0.219) | | | | |
| % Claim won | | | 0.932** | | | |
| | | | (0.395) | | | |
| No claim of direct exprop. | | | | 0.316 | | |
| | | | | (0.359) | | |
| ISDS through contract | | | | | 0.613* | |
| | | | | | (0.329) | |
| No enforcement proceedings | | | | | | 0.389* |
| | | | | | | (0.200) |
| Time trend | -0.0158 | 0.00456 | 0.0217 | -0.0136 | -0.00495 | -0.0000627 |
| | (0.0183) | (0.0191) | (0.0237) | (0.0239) | (0.0218) | (0.0203) |
| Constant | -0.766** | -1.269*** | -1.368*** | -0.959 | -0.825* | -1.053** |
| | (0.336) | (0.374) | (0.454) | (0.587) | (0.451) | (0.460) |
| Only completed arbitrations? | No | Yes | Yes | No | No | Yes |
| Observations | 729 | 574 | 339 | 426 | 719 | 574 |

Clustered standard errors (by host state) in parentheses.
* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

In Table 9, we test our Hypotheses in the same models. In Model (1), we include those covariates for which the appropriate sample is the full set of ISDS arbitrations filed in the period. In Model (2), we add those covariates for which only completed ISDS arbitrations are relevant. All coefficients of interest remain positive, as expected, although most are imprecisely estimated and insignificant. In Model (1), only our indicator of private arbitrations, ISDS through contract, retains significance. In Model (2), which limits the sample, No claim of direct expropriation becomes significant as does the added variable No enforcement proceedings. % Claim won approaches significance.

[46] Recall, however, that the public data underpinning this measure is likely subject to selection issues.

Table 9: Reinvestment: Full Specifications

| | (1) | (2) |
|---|---|---|
| Immobile | 0.0558 | 0.0931 |
| | (0.277) | (0.321) |
| Settlement/Investor win | | 0.434 |
| | | (0.427) |
| % Claim won | | 0.787 |
| | | (0.631) |
| No claim of direct exprop. | 0.342 | 2.092** |
| | (0.339) | (0.907) |
| ISDS through contract | 1.174* | 1.269 |
| | (0.644) | (1.289) |
| No enforcement proceedings | | 0.517* |
| | | (0.304) |
| Time trend | -0.0156 | 0.0298 |
| | (0.0242) | (0.0310) |
| Constant | -1.001* | -4.106*** |
| | (0.555) | (1.212) |
| Only completed arbitrations? | No | Yes |
| Observations | 426 | 275 |

Clustered standard errors (by host state) in parentheses.
* $p < 0.1$, ** $p < 0.05$, *** $p < 0.01$

What conclusions might we draw from Tables 8 and 9? These tests are, of course, quite far from sufficient to establish causal relationships. Nonetheless, we generally find evidence in line with our expectations. Increased reinvestment correlates with investors in sectors with limited exit options; investors that settle or win (more); investors that do not claim that the host state took over ownership of their property; investors that adjudicate disputes under the terms of contracts with the host state; and investors that do not face post-arbitration litigation. In further tests, we find that these positive correlations are robust to including considerations of the institutional setting of ISDS (i.e. ICSID or UNCTAD); arbitrations brought under international treaties (i.e. BITs or other IIAs); and host region fixed effects.[47] Although statistical significance is unstable, consistent signs suggest that a host state can systematically generate intuitions about which claimant investors are more likely to stay despite ISDS arbitration. We would expect a state that is host to the kinds of investors and involved in the kinds of disputes summarized in Hypotheses 1-6 to benefit from

[47] See replication files.

more reinvestment.

Consider this illustration of what ISDS arbitration and associated reinvestment looks like in practice. Three foreign manufacturers sued Mexico under NAFTA Chapter 11, in response to a 20% tax on soft drinks passed in 2001. That tax applied to high fructose corn syrup-sweetened drinks—an industry segment dominated by foreign investors—but not to cane sugar-sweetened drinks—dominated by domestic and often state-owned Mexican producers. The tax was found to be illegitimate, and two of the foreign manufacturers won awards in 2007 (US$34 million) and 2009 (US$58 million), which Mexico paid. In each case, the manufacturer reinvested in Mexico. However, Mexico was frustrated with the large award Cargill received in 2009, of US$78 million. The state's argument was that the tribunal had exceeded its jurisdiction and awarded Cargill compensation based not just on its direct investments but also on exports. Because no appeals process exists in ISDS, Mexico began post-arbitration litigation: it applied to get the award set aside in domestic Canadian courts, as the hearing physically took place in Canada. Cargill waited while Mexico lost several cases but ultimately, frustrated with the delays, filed for enforcement of the award in New York. Mexico relented and agreed to pay in 2013. After this resolution, Cargill announced a US$7.2 billion expansion plan in Mexico from 2015-2018, which celebrates "its 50-year presence in Mexico...with more than 1750 employees in 13 states and 30 facilities."[48]

Clearly, one illustration allows us no leverage on adjudicating six hypotheses.[49] What we mean to highlight with this illustration is that the explanatory variables on which we have focused are integral to retelling the story of investor behavior around ISDS arbitration. In this illustration, reinvestment took place, although aspects of the dispute push the likelihood of reinvestment in different directions. Pushing toward reinvestment, the claimants won large awards. Additionally, as the host state's action did not change ownership, the investors did not claim direct expropriation. Pushing against reinvestment, these firms in the manufacturing sector do not make immobile, site-specific investments and thus have more exit options. They sued under NAFTA, raising publicity around the arbitrations. And, one of three faced enforcement proceedings. In short, even in this cherry-picked case, we cannot link all our explanatory variables of interest to the realized

[48] "Cargill animal nutrition premix plant in El Salto, Mexico completes $5 million expansion." Cargill News Release: 13 August 2015.

[49] To make matters more complicated, Mexico repealed the tax in 2007 and has since moved to privatize the cane sugar industry (although ISDS requires neither of these actions). Thus, reinvestment took place in a different policy environment.

outcome. What we hope the reader takes away is that the explanatory variables we identify are relevant, observable, theoretically reasonable, and capable of being weighed by host states and foreign investors (that must make decisions despite being plagued by identification problems).

# 5 Conclusion

By counting and then slicing up instances of ISDS arbitrations and reinvestment, this article establishes that reinvestment does take place, although one's perspective on its rarity could vary. The incidence of reinvestment demonstrates that invoking international investment law need not burn bridges with the host state, despite that common expectation among practitioners and observers. Next, empirical trends show evidence consistent with several likely correlates of reinvestment. Reinvestment is linked to the structure of a foreign investor's sector and qualities of the dispute and the law through which it is adjudicated. Both foreign investors and host states are capable of observing—and responding to—such variables.

What does evidence of reinvestment mean for our expectations of host state behavior? In particular, might a high likelihood of reinvestment spur the state to breach in the first place? Host state incentives have been lurking behind this article. To a host state weighing the decision to breach, whatever domestic political benefits might come as a result of breach could be augmented by the potential for reinvestment. If reinvestment is a possible benefit of breach (or a means of minimizing its costs), reinvestment might make breach more "efficient." Consistent with the concept of efficient breach from law and economics, the host state could breach today, make the aggrieved investor financially whole to its ex ante position, and still derive benefits through reinvestment tomorrow.[50] Thus, host states may be emboldened in the presence of the correlates explored here.

Nothing of what is argued here establishes that current ISDS provisions are normatively the best way to organize the adjudication of investor-state disputes. Certainly, the usefulness and fairness of the de facto international investment regime are topics of considerable scholarly and public debate. This article contributes to that debate by specifying and providing evidence on one possible upside in terms of reinvestment: rather than consistently destroying bilateral

[50] For consideration of efficient breach in the realm of international law, see Posner and Sykes 2011; Pelc 2010; Guzman 2002. Pelc and Urpelainen (2015) argue that breach-and-pay systems that allow the state to violate agreements but compensate affected parties should be particularly common in investment treaties as compared to trade treaties.

investor-state relationships, international investment law can sometimes reinvigorate FDI from the aggrieved investor itself.

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