# CROSS-BORDER INVESTMENT:

## International Agreements and Dispute Settlement

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Cross-border investment is a powerful driver of the U.S. economy, playing an essential role in economic growth and job creation. Worldwide, the stock of foreign direct investment (FDI) reached an estimated $25.5 trillion in 2014.[1] The stock of FDI in the United States today tops $2.7 trillion.[2]

Foreign investment is generally welcomed and even wooed. It's easy to see why. In the United States, for example, foreign-headquartered companies employ 5.8 million Americans, a number equivalent to 5% of private sector employment.[3] These are good jobs that generally pay excellent wages. U.S. affiliates of foreign-headquartered multinationals tend to attract more job applicants than controversy.

Similarly, when U.S. companies invest abroad, they bring with them high wages as well as high labor and environmental standards. Working for a U.S.-headquartered company is an aspiration for many people in both developed and developing economies.

To safeguard international investments and establish rules against discriminatory treatment and expropriation, countries enter into bilateral investment treaties. Today, approximately 3,000 such treaties are in force around the world, and BITs—as they are called—have become a cornerstone of international law.

Investment treaties ensure that foreign investors are not subject to discrimination, are treated fairly, and are compensated in the event of expropriation. These investment protections are also included in many trade agreements.

Inevitably, investment disputes arise from time to time. BITs include provisions to resolve disputes called investor-state dispute settlement (ISDS). Recently, anti-trade activists have called attention to ISDS in an effort to undermine the trade and investment agreements that include these provisions.

In this context, the U.S. Chamber of Commerce is issuing this paper to provide background information on the benefits of cross-border investments. It also includes information on BITs and trade agreements, including ISDS. The principal message is that international investment—both inbound and outbound—brings significant benefits, and agreements to safeguard such investments play a valuable role in enhancing the rule of law to the advantage of workers, consumers, and companies around the globe.

## BENEFITS OF INBOUND INVESTMENT

The United States is home to more investment from abroad than any other country in the world. Across the nation, companies such as Toyota, Siemens, and Embraer have been welcomed for the contributions they make to the local economy.

Foreign companies have invested $2.7 trillion in the United States and employ more than 5.8 million Americans, according to the U.S. Department of Commerce.[4] The jobs of an estimated 21 million Americans depend directly and indirectly on investments by foreign-headquartered companies, according to a study commissioned by the Organization for International Investment (OFII).[5]

U.S. affiliates of foreign-headquartered companies support an annual payroll of more than $450 billion, with wages that top $75,000 on average. These firms account for approximately 41% of all employment in the U.S. motor vehicle industry, 41% in the U.S. chemicals industry, and 33% in the U.S. primary metals industry, according to OFII.

It's impressive that these U.S. affiliates annually spend nearly $50 billion on research and development, driving innovation and technical progress. U.S. affiliates of foreign-headquartered companies generate more than $330 billion in merchandise exports, or more than 20% of the total.[6] They also purchase more than $1.8 trillion in inputs from local suppliers and small businesses.[7] Coupled with homegrown capital and ingenuity, these investments give the United States extraordinary access to cutting-edge technology and productivity tools.

Most FDI comes from other developed economies. Companies headquartered in seven countries—Canada, France, Germany, the Netherlands, Switzerland, the United Kingdom, and Japan—account for nearly three-fourths of the value added by all majority-owned U.S. affiliates of foreign-headquartered firms.[8] However, firms from such countries as Brazil, China, and India are increasingly investing in the United States; in fact, Chinese FDI in the United States recently outpaced U.S. FDI in China.[9]

Clearly, America benefits hugely from these investments from abroad. As a nation, the United States must keep the welcome mat out and attract more job-creating investments from overseas.

## BENEFITS OF OUTBOUND INVESTMENT

Americans also derive important benefits from U.S. investment abroad. In addition to exporting, U.S. corporations can access new customers in foreign markets by investing abroad, creating foreign affiliates and becoming multinationals in the process. Sales by these foreign affiliates reached nearly $7 trillion

in 2012—a sum representing approximately 40% of U.S. multinational corporations' total sales (latest information available).[10] Many of America's largest companies earn more than half their revenue in this way.

Why do companies invest in other countries instead of simply exporting? Most of these overseas investments are in sectors that cannot be served by means of exports from the United States. This includes many services as well as manufacturing operations for goods, such as detergent, cement, or potato chips, which generally cannot be shipped over long distances due to high transportation costs or barriers to trade.

For these reasons, U.S. companies invest in foreign markets to serve those markets—not as a substitute for domestic production. More than 90% of the production of foreign affiliates of U.S. multinationals is sold abroad.[11]

American companies that invest abroad tend to be excellent employers at home. Not only do U.S. multinational companies employ more than 23 million Americans, [12] the compensation they offer is nearly 20% higher than the U.S. private sector average. They also tend to create more jobs in the United States than companies focused solely on the domestic market.[13]

Investing abroad also makes U.S. companies more resilient. The U.S. Department of Commerce reports that U.S. multinational corporations added 289,000 U.S. jobs between 2007 and 2009 even as the sharpest recession in a generation caused the U.S. economy to shed more than 8 million jobs overall.[14]

U.S. multinationals have continued to concentrate their high-wage, high-skill jobs in the United States. The approximately $7 trillion in annual revenue that U.S. multinationals earn through their foreign operations helps fund their research and development activities, 84% of which continue to be performed in the United States, according to the U.S. Department of Commerce.[15] U.S. multinational corporations also generate more than half of all merchandise exports, with their foreign affiliates purchasing one-fifth of the total.[16]

## U.S. INVESTMENT AGREEMENTS

To secure the benefits of international investment, the U.S. Chamber believes that the United States should make it a priority to secure legal protections for the investments American companies make overseas. The rule of law, sanctity of contracts, and respect for property rights are the touchstones of respect for international investment, and the United States should fight for these principles in markets around the globe.

Investment agreements are an essential part of these efforts. For more than three decades, the United States has negotiated bilateral investment treaties (BITs) to protect U.S. investments abroad, and similar provisions are included in U.S. trade agreements negotiated over the past 25 years. It is a top

priority of the U.S. business community to ensure that these investment protections are included in agreements now under negotiation, including the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP).

BITs and trade agreements contain three basic parts. First, they include market access provisions to allow companies from one country to invest in the other's territory. BITs can unlock foreign markets by eliminating outright prohibitions on ownership in particular sectors as well as limitations on ownership of a controlling interest in a firm.

Second, BITs include investment protections. Investment treaties contain four core obligations that reflect these fundamental rule of law traditions, including promises that governments—

- will not discriminate against an investment on the basis of its national origin, i.e., it will provide national treatment, except as specifically provided in the treaty;
- will at a minimum provide investments of the other party fair and equitable treatment and full protection and security;
- will refrain from expropriation except for a public purpose, in accordance with due process, and upon payment of prompt, adequate and effective compensation; and
- will permit free transfers of funds relating to investments.

In short, U.S. investment agreements echo the U.S. Constitution's protections against arbitrary government actions and against taking of property without compensation. They uphold contract and property rights and help ensure transparency with respect to investment-related laws and regulations.

## INVESTOR-STATE DISPUTE SETTLEMENT

The third element in an investment agreement consists of provisions to enforce its investment protections. BITs include two forms of dispute settlement: state-state dispute settlement and investor-state dispute settlement (ISDS). State-state dispute settlement is at times workable, and investment agreements in general require the investor to consult with the government regarding a dispute as a first step. Only if such consultation fails may the investor pursue ISDS.

ISDS is included in most of the world's 3,000 BITs, the earliest of which were concluded more than four decades ago. The United States today has BITs or trade agreements that include investment protections and ISDS in force with more than 50 countries.

In practice, governments often find it convenient to grant recourse to investors via ISDS. One reason they do so is because a dispute involving a single company may be viewed as less important than bilateral issues involving national security or other priorities. From the perspective of governments, ISDS is often a convenient way to depoliticize an investment dispute and leave it in the hands of neutral arbiters.

Particularly in some developing countries where local judiciaries may be slow, ineffective, or corrupt, U.S. companies have benefited significantly from recourse to ISDS. Even though these provisions are invoked infrequently, they serve as a positive admonition to governments to avoid arbitrary actions with regard to foreign investment.

In keeping with the Golden Rule, American officials have long recognized that the United States must accept the same obligations in investment agreements, including ISDS, that they ask of other governments. Further, forgoing enforceable investment protections in a given agreement—even with a country where the rule of law is strong—heightens the difficulty of securing such protections and enforcement remedies in future negotiations with other countries.

ISDS cannot overturn the policy decisions, laws, or regulations of any country. Indeed, all ISDS panels can do is award compensation when a government expropriates property, discriminates against investors on the basis of their nationality, or otherwise tramples on the rule of law.

## INVESTMENT AGREEMENTS WORLDWIDE

As noted, approximately 3,000 investment agreements are in force today around the globe. Germany, China, the United Kingdom, and France have each entered into BITs with more than 100 nations, and nearly all include ISDS. By contrast, the United States has entered into BITs or trade agreements that include ISDS with 54 countries.

A Chamber analysis found that the 10 countries with the most extensive investment treaty networks have entered into BITs with more than 100 countries where the United States has no investment agreement of any kind. Because investment agreements often serve to open previously closed industry sectors to investment from abroad, the absence of U.S. investment agreements with major economies such as China, India, and Indonesia at times places U.S. companies at a competitive disadvantage relative to firms from third countries.

America's continued prosperity in a highly competitive world demands that we negotiate additional high-standard investment treaties. The Chamber strongly supports ongoing BIT negotiations with China and India and believes that the United States should explore the possibility of BIT negotiations with additional markets such as Indonesia and the East African Community. As other countries

around the globe pursue their own BITs, decision makers in Washington should be wary of how these may tilt the playing field against U.S. companies should the United States lag in its own negotiations.

## CONCLUSION

International investment is a powerful driver of the U.S. economy, playing an essential role in economic growth and job creation. The United States secures significant benefits from both inbound and outbound investment, and agreements to protect such investments play a key role in enhancing the rule of law for the benefit of workers, consumers, and companies. For the sake of American competitiveness, it is crucial that U.S. policymakers continue to uphold these principles and commitments in future legislation—including TPA—as well as investment and trade agreements.

## THE VALUE OF INVESTMENT PROTECTIONS: THE CASE OF VENEZUELA

For a real-world example of the value of BITs, an unfortunate case lies close at hand. Venezuela leads the world rankings for the most ISDS cases. Today, there are 27 ISDS disputes pending against Venezuela, well ahead of second-place Argentina (22) and third-place Egypt (13). (These are investment disputes pending before the World Bank's International Center for the Settlement of Investment Disputes, to which many investment treaties refer disputes for arbitration.)

The reason so many investors have sought arbitration to settle their disputes with the government of Venezuela is simple: The government seized their property. The Venezuelan government undertook a far-reaching program of nationalizations of industry, especially between 2006 and 2008. From food companies to the oil industry, tens of billions of dollars' worth of investments were seized. ODH Consultants, based in Caracas, estimates that $53 billion in compensation is being sought in just 13 of the 27 disputes. Canada's Scotia Bank has estimated the total at $24 billion.

The government of Venezuela has taken steps to extricate itself from its investment treaty obligations in recent years. Unsurprisingly, new FDI has disappeared, and Venezuela has suffered massive capital flight.

The contrast with the United States is noteworthy. America today is home to more than $2.7 trillion in FDI—more than any other country. Meanwhile, the U.S. Department of State reports that only 22 ISDS disputes have ever been brought against the United States—over a period of more than 30 years.

Most tellingly, the United States has never lost a case. American taxpayers have never been held liable to pay damages in an ISDS dispute.

Nonetheless, ISDS is far from meaningless for the United States. American officials have long recognized that the United States must accept the same obligations in investment agreements that they ask of other governments. For this reason, recourse to ISDS needs to be an option for foreign investors in the United States.

# THE VALUE OF INVESTMENT PROTECTIONS: THE CASE OF THE TTIP

Over the past year, activists in Europe have mounted a campaign of misinformation against ISDS. They have further argued it should not be included in the Transatlantic Trade and Investment Partnership (TTIP) now under negotiation by the European Union and the United States.

In addition to the other benefits of investment protections and ISDS addressed in this report, the U.S.-EU investment relationship has some special characteristics relevant to the debate over ISDS.

As background, the U.S.-EU investment relationship is without peer. Companies headquartered in EU member states had invested nearly $1.7 trillion in the United States by the end of 2013 and directly employ more than 3.5 million Americans. Similarly, U.S. firms have invested $2.4 trillion in the EU—a sum representing more than half of all U.S. investment abroad. It's also nearly 40 times as much as U.S. companies have invested in China.

Because of this unique investment-based relationship, approximately 40% of U.S.-EU trade is intra-industry and intra-firm. Removing barriers to this trade will substantially boost the competitiveness of American and European companies in global markets.

Investment treaties and ISDS were first developed by Germany, and Germany, the United Kingdom, and France have each entered into BITs with 100 or more nations. European countries have been more aggressive than those in any other part of the world in pursuing these agreements.

However, the incomplete network of U.S.-European investment treaties leaves gaps in transatlantic investment protections. The United States has modern BITs with 9 EU member states: Bulgaria, Croatia, the Czech Republic, Estonia, Latvia, Lithuania, Poland, Romania, and Slovakia. It would be inappropriate for policymakers in the EU or the United States to suggest that U.S. investments do not merit the same basic level of protection throughout the EU, including in the 19 EU members states with which the United States has not entered into a modern BIT.

Further, investors from more than 100 countries have protections under BITs with Germany, the United Kingdom, and many other EU member states—but the United States has no modern BIT with those countries. Protections for U.S. investors under

our antiquated Treaties of Friendship, Commerce and Navigation, which date from the 1950s, fail to reflect modern commercial realities. The TTIP offers the opportunity to fill in these gaps and afford the same high standard of protection for U.S. investment in Europe across the breadth of the European Union.

Including investment protections and ISDS in the TTIP will help both the United States and the EU strengthen investment ties to other countries. If the United States and the EU were to forgo enforceable investment protections in the TTIP, it would be extraordinarily difficult to ask other countries to agree to such protections and enforcement remedies in an investment or trade agreement. Ongoing U.S. and EU investment treaty negotiations with China are a highly consequential case in point.

To ensure uniform protection of U.S. investments in the European Union and to facilitate future investment agreements elsewhere, the United States and the European Union must include enforceable investment protections in the TTIP.

## 13 MYTHS ABOUT INVESTMENT AGREEMENTS AND INVESTOR-STATE DISPUTE SETTLEMENT (ISDS)

### Myth 1: ISDS is a novel and exotic way to settle investment disputes.

**Fact:** ISDS is neither new nor exotic. Provisions for international arbitration for the settlement of investment disputes have been included in approximately 3,000 investment treaties signed by scores of countries over the past four decades. ISDS allows for neutral arbitrators to enforce the basic rights of investors as established in investment agreements.

### Myth 2: ISDS allows corporations to overturn laws and regulations.

**Fact:** Arbitrators in ISDS disputes have no power to overturn laws or regulations. On the contrary, they are charged with upholding the same kind of fundamental rule of law protections that appear in the U.S. Constitution. In the event a government has breached its obligations under an investment treaty, the only recourse ISDS arbitrators can provide is to require compensation to the investor for losses incurred.

### Myth 3: ISDS heightens the taxpayer's jeopardy in investment disputes.

**Fact:** If the United States were to engage in discriminatory or unfair actions against foreign investors, an arbitral panel might require compensation. However, of the 22 ISDS cases brought against the United States over the past 30 years, the United States has never lost a case. Foreign investors in the United States are far more likely to seek redress via U.S. domestic courts than ISDS because U.S. law affords greater protections to assure fair and equitable treatment of foreign investors than any international investment treaty. This reality incentivizes foreign investors to seek redress in domestic courts whenever possible. The U.S., state, and local governments routinely pay compensation and awards in domestic court cases to both domestic and foreign investors in such disputes. In fact, the federal government judgment fund paid out more than $3 billion in 2014 to settle cases or pay judgments in domestic litigation while it has never paid a dollar in an ISDS case.

### Myth 4: ISDS isn't necessary because domestic courts can handle investment disputes.

**Fact:** As noted, foreign investors in the United States usually have good reasons to take their disputes to U.S. courts and not ISDS. However, domestic law in other countries at times provides inadequate protections for U.S investments; for instance, it often fails to bar discrimination against foreign investors on the basis of their nationality. This important national treatment obligation, which is a hallmark of investment agreements, would be meaningless without an enforcement mechanism such as ISDS.

### Myth 5: Use of ISDS is exploding.

**Fact:** Few disputes are brought to arbitration under ISDS. According to UNCTAD, a total of 512 investor-state disputes were filed between 1987 and 2012. This is a remarkably small number of disputes given that:

- The stock of foreign direct investment worldwide is estimated at $25.5 trillion;
- The number of investment agreements worldwide is approximately 3,000; and
- A 25-year period was examined.

In fact, Susan Franck of the Washington and Lee University School of Law found that the ISDS provisions of 97% of all BITs have never been used.

### Myth 6: ISDS gives investors the whip hand.

**Fact:** Under ISDS, investors usually lose. One-third of disputes end in a settlement, and governments win twice as often as investors in cases that go to arbitration. Even when an investor prevails, the compensation awarded tends to be a small fraction of the amount originally sought.

### Myth 7: ISDS limits governments' ability to regulate.

**Fact:** ISDS does not limit the ability of governments to issue regulations to protect public health, the environment, and worker and consumer safety. The commitments governments make in investment agreements are straightforward: Governments agree (1) not to discriminate on the basis of the nationality of the investor; (2) to afford fair and equitable treatment and full protection and security; (3) to expropriate an investment only for a public purpose, with due process and upon payment of prompt, adequate, and effective compensation; and (4) to guarantee freedom of transfers related to an investment.

### Myth 8: ISDS confers special rights for corporations.

**Fact:** There is nothing "special" about ensuring fair treatment of cross-border investment under international law or arranging for neutral arbitration of a dispute. Moreover, since 2004, the U.S. Model BIT has expressly stated that investment agreements do not create greater rights for foreign investors than those enjoyed by domestic investors.

### Myth 9: ISDS undermines sovereignty.

**Fact:** Investment treaties are an expression of sovereignty, not a limitation on it. Governments always retain the right to impose non-discriminatory measures to protect public health, the environment, and worker and consumer safety, and ISDS panels cannot overturn those regulations.

### Myth 10: ISDS lets multinational corporations sue governments any time they fail to make a profit.

**Fact:** Investment agreements and ISDS uphold standards of fairness, not profits. If a government breaches obligations it has undertaken in an investment agreement, an arbitration panel may award compensation for harm to investments. Breaches of an investment agreement occur only where there is corrupt, biased, or arbitrary application of regulation that harms an investment. Further, arbitration panels have an exemplary track record of determining appropriate levels of compensation. According to Public Citizen—an organization that actively cultivates fear of international investment agreements—the average recovery is approximately 15% of the original claim in instances in which the investor prevailed.

### Myth 11: ISDS is just for big business.

**Fact:** Most ISDS cases are not brought by big companies. The OECD has found that only 8% of the all ISDS claims were brought by multinational corporations. Rather, the companies that bring ISDS cases tend to be small businesses seeking protection against discrimination and other unfair practices.

### Myth 12: Arbitration under ISDS is conducted in secret tribunals.

**Fact:** There is nothing secret about investor-state arbitration. Proceedings are open and documents are available to the public under rules established in U.S. investment treaties. Interested parties such as environmental organizations and public interest organizations can and do file amicus submissions.

### Myth 13: Pending ISDS cases promise shocking outcomes.

**Fact:** The arguments of anti-ISDS activists tend to rely on hypothetical scenarios or cases that have been initiated but not yet decided. By contrast, the real-world record shows that when a government has acted in a non-discriminatory manner and affords investors due process, it always wins.

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