

American University Washington College of Law

## Digital Commons @ American University Washington College of Law

---

Articles in Law Reviews & Other Academic Journals

Scholarship & Research

---

2009

### Investment Treaty Arbitration and Law & Development

Susan Franck

Follow this and additional works at: [https://digitalcommons.wcl.american.edu/facsch\\_lawrev](https://digitalcommons.wcl.american.edu/facsch_lawrev)



Part of the [Banking and Finance Law Commons](#), [Dispute Resolution and Arbitration Commons](#), and the [International Law Commons](#)

---

*Susan D. Franck\**

Tom Ginsburg's initial post raises a series of fascinating questions about the future of Law and Development. These questions encourage us to think about the utility of different methodological approaches, basic definitions, and the implications for institutional change. Investment treaty arbitration (ITA)—which gives foreign investors the right to arbitrate directly against a host government for arguable violations of their substantive investment right—provides a unique opportunity to explore these issues in a tangible manner. So I beg your indulgence as I reflect upon a specific application (namely, ITA) to highlight some of the themes raised by my fellow bloggers.

As the legitimacy of ITA becomes a matter of heated debate, who wins the dispute has become a matter of particular interest. Suggesting that ITA is unfairly tilted toward the developed world, various countries have withdrawn from World Bank dispute resolution bodies or are considering the elimination of arbitration.<sup>13</sup> Rather than relying on anecdotal evidence, supposition, or political rhetoric, it is vital to provide systematic data to aid stakeholders in the assessment of the ITA process and consider the implications for international development. Ideally, a mixed-methods approach that both (1) capitalizes on the strengths of the individualized, sociological, and qualitative approaches advocated by Katharina Pistor<sup>14</sup> and John Ohnesorge,<sup>15</sup> and (2) contextualizes specific experiences within the framework of a larger puzzle offered by broader quantitative research, could provide particularly useful insights.<sup>16</sup> Given the availability of data from public arbitration awards, this Essay focuses upon quantitative aspects of a mixed-methods approach.

Previous research has shown that although both investors and governments won investment treaty arbitration cases, the respondent states were more likely than investors to win (57.7% for states as compared with a 38.5% win rate for investors). In cases where there was a violation of the underlying international investment agreement (IIA), tribunals awarded amounts that were smaller than what investors claimed. More particularly, while investors claimed an average of \$343 million in damages, the average award was in the order of \$10 million. In sum, far more investors lost than

---

\* Associate Professor of Law, Washington & Lee School of Law.

<sup>13</sup> Susan D. Franck, *Development and Outcomes of Investment Arbitration Awards*, 50 HARV. INT'L L.J. 435, 435 (2009) [hereinafter Franck, *Development*] (link).

<sup>14</sup> See Pistor, *supra* note 5, at 169–70.

<sup>15</sup> See Ohnesorge, *supra* note 12.

<sup>16</sup> See Susan D. Franck, *Empiricism and International Law: Insights for Investment Treaty Dispute Resolution*, 48 VA. J. INT'L L. 767 (2008) (link).

won, and when investors did win, they usually received far less than they originally claimed.<sup>17</sup>

The open question was whether the outcomes reported were somehow related to variables such as the parties' or arbitrators' development background. Finding the answer to this question raises an issue echoed by John Cioffi, namely that "large-n quantitative analyses of law related variables . . . [are] deeply problematic" when "these studies lump together highly developed countries" and developing countries.<sup>18</sup> Given the possible disparate impact on the developing world, it is critical that research consider the difference in outcomes between these two groups. If outcome is reliably associated with—let alone causally influenced by—the development background of the respondent state or presiding arbitrator, serious questions about the integrity of ITA could arise.

But even recognizing the difference between developed and developing countries raises a question: what is "development status"? In the context of quantitative research, operationalizing terms properly and establishing measurement validity is one of the thorniest issues. "Development status" can mean different things to different people in different contexts. In order to benefit from standard terms and begin the process of creating more nuanced analysis, my own research started by using pre-existing measures and categories for defining development. In particular, the research considered "development status" in two ways, namely by analyzing categories, including: (1) membership in the Organisation for Economic Co-operation and Development (OECD), and (2) World Bank classification as a High Income, Upper-Middle Income, Low-Middle Income, or Low Income country.<sup>19</sup>

Although this was a relatively straightforward metric for defining the development status of respondent states, defining the "development status" of arbitrators was more difficult. Arbitrators' development status might have been measured in various ways, including pure nationality of origin, country of residence, country of legal training, number of advanced degrees, membership in professional organizations, average annual income, or some combination thereof. For the purposes of this initial, limited study, development status for arbitrators was defined as a function of arbitrator nationality, in part because of the historical focus upon arbitrator nationality and the belief that nationality is a proxy for adjudicative neutrality.<sup>20</sup> A presiding arbitrator's status was, therefore, measured by considering the OECD or World Bank classification of his/her country of origin.

---

<sup>17</sup> Susan D. Franck, *Empirically Evaluating Claims about Investment Treaty Arbitration*, 86 N.C. L. REV. 1, 49–50, 57–62 (2007). Figures are in U.S. dollars.

<sup>18</sup> John Cioffi, *Law & Development: Past Performance Is Not Indicative of Future Results*, *infra*.

<sup>19</sup> Franck, *Development*, *supra* note 13, at 455.

<sup>20</sup> See Ilhyung Lee, *Practice and Predicament: The Nationality of the International Arbitrator (with Survey Results)*, 31 FORDHAM INT'L L.J. 603, 613–14 (2008).

Bearing in mind how “development” was operationalized in this research, and recognizing that different constructions may require different methodological approaches and definitions, the newest generation of research considered whether there was a reliable statistical link between development status and ITA outcome.<sup>21</sup> One study considered only the impact of a respondent’s development status on outcome. The results of statistical analyses demonstrated that there was no statistically significant relationship between a government’s development background and the outcome of ITA.<sup>22</sup>

A second study considered the relationship among outcome, the development status of the respondent state, and the development status of the presiding arbitrator’s country of origin. The results generally showed that outcome was not reliably associated with the development status of the respondent, the development status of the presiding arbitrator, or some interaction between those two variables. This lack of relationship held true for both: (1) winning or losing investment treaty arbitration, and (2) amounts tribunals awarded against governments.<sup>23</sup> There were, however, two statistically significant simple effects—found in one sub-set of potentially non-representative cases<sup>24</sup>—that suggested tribunals with presiding arbitrators from Middle Income countries awarded different damages in cases against High Income countries. Specifically, if the presiding arbitrator was from a Middle Income country, High Income countries received statistically lower awards than either: (1) Upper-Middle Income respondents, or (2) Low Income respondents. Awards by Middle Income presiding arbitrators for High Income and Lower-Middle Income respondents were statistically equivalent.<sup>25</sup>

The overall results cast doubt on the arguments that: (1) ITA is the equivalent of tossing a two-headed coin to decide disputes, (2) the developing world is treated unfairly in ITA, and (3) arbitrators from the developed and developing world decide cases differently. The evidence creates a basis for cautious optimism about the integrity of ITA and suggests radical overhaul, rejection, or rebalancing of procedural rights in International Investment Agreements (IIAs) is not necessarily warranted. Although the follow-up tests and limitations of the data suggest optimism must be tempered properly, a sensible approach would involve creating targeted solutions to

<sup>21</sup> See Susan D. Franck, *Considering Recalibration of International Investment Agreements: Empirical Insights*, in *THE EVOLVING INTERNATIONAL INVESTMENT REGIME: EXPECTATIONS, REALITIES, AND OPTIONS* (José E. Alvarez et al., eds., forthcoming 2009) [hereinafter Franck, *Recalibration*]; Franck, *Development*, *supra* note 13.

<sup>22</sup> Franck, *Recalibration*, *supra* note 21.

<sup>23</sup> Franck, *Development*, *supra* note 13, at 439–40.

<sup>24</sup> See *id.* at 472 (describing the two awards and outlining reasons why the awards may be non-representative although they shared a common presiding arbitrator).

<sup>25</sup> *Id.*

address particularized problems and enacting targeted reforms to redress perceived concerns about the international investment regime.

In the context of ITA, Salil Mehra's point that the "way forward for Law and Development [ ] involves embracing and addressing differences rather than seeking a universal solvent"<sup>26</sup> buttresses this need for individualized solutions. Individualized solutions, in turn, may help address the concerns raised by Mariana Prado. It suggests that scholars can and should play a vital role in the Law and Development debate. Part of that role could be encouraging the discourse to move beyond a dichotomy polarized by "unilateral blueprint" versus "context matters" models.<sup>27</sup> In the context of the resolution of international investment disputes, this means encouraging scholars to: develop methodological insights that operate on multiple levels, consider different definitions of terms like "development," recognize the limitations of inferences based upon specific methods and definitions, provide interpretive guidance about the policy implications, and—in light of those points—develop theories, subject to the research loop, that respect and reflect the complexities of variation within the population.

---

<sup>26</sup> Mehra, *supra* note 2, at 167.

<sup>27</sup> See Mariana Prado, *Should We Adopt a "What Works" Approach in Law and Development?*, *supra*.