

Reclaiming Domestic Agency: International Investment Agreements and the  
Defence of Policy Space in Latin America

by

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## **Abstract**

The proliferation of international investment agreements (IIAs) has generated concern that developing countries are surrendering needed policy space. Investor-state dispute settlement provisions enable foreign investors to sue host states should they perceive their treaty rights to be violated. This enables foreign investors to interfere in democratic processes while constraining governments' abilities to introduce policies in defence of citizen interests. Despite the burgeoning literature on IIAs, there has not yet been an adequate analysis of how states exercise and defend policy space under the agreements. IIAs are commonly theorized as a cohesive regime that imposes similar constraints on states regardless of the context, which renders invisible the agency of domestic actors and limits our understanding of how domestic actors shape the impacts of investment rules by contesting or reinforcing their authority. This study provides a new theoretical framework that enables us to explore the role domestic actors play in shaping the impacts of IIAs. This study argues that real impacts of IIAs on policy space lies in the middle messy ground between the constraints they could potentially impose and the responses evoked at the domestic level, be it acquiescence or contestation. The power of IIAs is therefore theorized as contingent upon the heterogeneous assortment of actors, institutions and expertise involved in processes of enforcement. Policy space is also reconceptualized as fluid, dynamic and structured by multiple factors operating at once. This theoretical framework is applied to the cases of Argentina and Ecuador, focusing on disputes involving foreign-owned utility and oil companies respectively. Both cases demonstrate that signing on to IIAs does not ensure a government will abide by investment rules consistently across time. Rather, governments will introduce policies in conflict with investor rights to advance significant national interests, including the delivery of basic services and development goals. IIAs significantly raised the costs of introducing these policies however state actors employ defence strategies to mitigate these costs with some degree of success. This study challenges the assertion that IIAs constrain policy space evenly across contexts and demonstrates the importance of recognizing state agency in studies of policy space and global economic integration.

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## Acronyms

ATPA	Andean Trade Preferences Act
BIT	Bilateral investment treaty
CAITISA	Citizens' Commission for a Comprehensive Audit of Investment Protection Treaties and of the International Arbitration System on Investment
CONAIE	Confederación de las Nacionalidades Indígenas del Ecuador
ICSID	International Centre for the Settlement of Investment Disputes
IIA	International investment agreement
IMF	International Monetary Fund
ISDS	Investor state dispute settlement
ISI	Import substitution industrialization
FCN	Friendship, commerce and navigation (treaties)
GATT	General Agreement on Tariffs and Trade
LET	Ley de Equidad Tributaria (Tax Equity Law)
OECD	Organization for Economic Cooperation and Development
PGE	Procuraduría General del Estado (State Attorney General)
PJ	Partido Justicialista (Justicialist Party)
PTN	Procuración del Tesoro de la Nación (Office of the National Attorney General)
SOE	State-owned enterprise
SRI	Servicio de Rentas Internas (Internal Revenue Service)
TNC	Transnational corporation
UNASUR	Unión del Suramericanas (Union of South American Nations)
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
VAT	Value-added tax

## **1 Chapter: Introduction**

The growing breadth and complexity of global economic integration has raised concerns amongst academic and policymaking communities that governments in the developing world are sacrificing the policy space needed to raise the living standards of their citizens. The term ‘policy space’ is commonly used to refer to the freedom or flexibility governments have under international rules to deploy policies needed to govern as they see fit (Yu and Marshall 2008, 14; Gallagher 2008, 63). The rapid expansion of aid and loan conditionalities as well as trade and investment rules throughout the 1980s and 1990s, critics argue, has reduced the range of policies governments can legitimately pursue to advance public interests. Advocates of such arrangements justify the constraints they place on state action as necessary to ensure the effective and efficient operation of market forces that aid in developmental processes. However, autonomy in policymaking and implementation allows governments to tailor development strategies to the unique needs and contexts within their jurisdictions. The failure of neoliberal structural adjustment to induce inclusive economic development has demonstrated the dangers of investing blindly in market forces while neglecting local realities. In light of this failure, there is now growing consensus around the need for development strategies that are attuned to local needs and civil society demands (UNCTAD 2007a).

International investment agreements (IIAs) have come to the forefront of the debate over policy space. IIAs liberalize and protect investment flows between countries by setting out substantive and procedural guarantees against arbitrary and discriminatory forms of government intervention. As such, they provide the legal basis on which foreign

investor challenge policies introduced by host states. Their most controversial element, however, are the measures provided for investor-state dispute settlement (ISDS), which grant foreign investors the right to sue host states unilaterally via third party arbitral tribunals should they perceive their treaty rights to have been violated. This, in turn, grants international arbitrators broad reach over policy matters traditionally reserved solely to the state (Marley 2014).<sup>1</sup>

Proponents argue that IIAs help attract foreign capital and technologies to markets that are perceived to be otherwise risky by increasing the credibility commitments of host governments. Neoliberal advocates also assert that IIAs ensure the efficient and effective operation of market forces in domestic investment environments and therefore help foster economic development (Blake 2013; van Aaken 2009). Yet a rich body of literature challenges these claims. Some studies refute the assertion that IIAs help countries attract the kinds of foreign investment that best promote development (Busse et al. 2010; Neumayer and Spess 2005; Tobin and Rose-Ackerman 2005). Others find that the restrictions IIAs place on policy autonomy limits the capacity of governments to respond to citizen interests while providing foreign investors the means to interfere in domestic democratic processes (Blackwood and McBride 2006; Chang 2004, 2006; Gallagher 2005, 2008; Shadlen 2005; Wade 2003). Along these lines, numerous studies demonstrate how foreign investors use investment rules to challenge policies related to industrial development, public health, the environment, social justice and natural resource governance (Cho and Dubash 2005; Manger 2007; McBride 2006; Spears 2010; Yazbeck

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<sup>1</sup> This is in contrast to first generation IIAs introduced by western European countries in the 1960s, which required disputes to be resolved diplomatically between signatory governments.

2010). These studies support the conclusion that developing countries are sacrificing policy space in exchange for uncertain economic benefits.

Interest in IIAs has been driven both by the proliferation of the agreements in the 1990s and as well as the subsequent wave of investor claims brought against host states in recent years. By the end of 2014, foreign investors had brought 608 claims to international arbitration against 101 countries.<sup>2</sup> This wave of investor-state disputes has served as proof to critical scholars of the disastrous consequences of signing on to IIAs. After all, foreign investors initiate ISDS cases as a means to challenge government action and policy. Yet under a different light, the high number of ISDS cases also suggests weaknesses in IIA enforcement mechanisms. That is, if IIAs prevented the kinds of government action restricted by investment rules, such a high number of ISDS cases would not exist. Simply signing on to IIAs does not guarantee that a government will abide by investment rules consistently across time. Moreover, of these known cases, only 356 have been concluded, 37 percent of which were decided in favour of the host state as opposed to 25 percent in favour of foreign investors. A further 28 percent were settled out of court (UNCTAD 2014, 8). These aggregate figures gloss over the unique struggles underpinning ISDS cases; however they do suggest that investors are not always successful in leveraging the rights provided to them by IIAs.

Despite widespread debate on the value of IIAs, relatively little attention has been given to exploring how state and non-state actors defend domestic interests under the agreements and what this means for the nature of policy space in the contemporary era. Most critical analyses of the impacts of IIAs portray developing countries as passive

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<sup>2</sup> This number may be higher because some IIAs provide for fully confidential investor-state disputes arbitration and some arbitral institutions do not release information about the disputes they oversee.

victims of a global corporate agenda driven by the interests and institutions of the global North (see for example, Blackwood and McBride 2006; Chang 2006; Cho and Dubash 2005; Gallagher 2005 and 2008; Haslam 2007; Manger 2007; Shadlen 2005; Spears 2010; Yazbek 2010). Yet an increasing number of governments and civil society groups are contesting investment rules and the rights they afford to foreign investors. More than 50 countries in the developed and developing world are currently revising or have revised their IIA models to limit the rights afforded to foreign investors or to deter fraudulent investor claims. Indonesia, South Africa, Ecuador, Bolivia and Venezuela have also terminated IIAs and / or withdrawn their consent to the ICSID convention. This is while Botswana and Namibia are reconsidering their own approaches to bilateral investment treaties (BITs) (UNCTAD 2015, 109-110). Existing literature on IIAs and policy space has yet to fully grasp emergent forms of contestation.

Yet the growing contestation of investment rules raises important questions regarding the role of state and non-state actors in protecting domestic interests under the agreements: How do domestic actors, in contesting or reinforcing the authority of IIAs, shape the impact IIAs have on policy space? What strategies do they adopt and to what degree are these strategies effective? What does this tell us about the relationship between IIAs and policy space and about the nature of policy space itself? Though existing studies contribute to our understanding of the potential constraints IIAs place on policy space, authors have neglected to recognize the important role domestic actors play in shaping the impacts external arrangements have on domestic policymaking processes. In focusing on the power of IIAs in imposing constraints, we are left with one side of a more complex story.

## 1.1 Research Question

The objective of this study is to contribute to understandings of the relationship between IIAs and policy space in host states by addressing two sets of questions that have yet to be adequately addressed in the literature, namely: how do states contest the constraints posed to their policy space by IIAs and what does this tell us about how policy space is exercised and defended under the agreements? What are the mechanisms through which IIAs shape policy space in practice?

## 1.2 Central Argument

The findings in this study challenge the view that IIAs impact governments' policy space evenly across time and space and demonstrate the importance of recognizing state agency in studies of global economic integration. Foreign investors were not always successful in leveraging IIAs to circumvent government policy and the costs incurred by investor claims was significantly reduced as a result of governments' defence strategies. Therefore, while IIAs significantly increase the costs of adopting certain forms of government action, the constraints they impose on policy space must be understood as contingent upon the response of domestic actors in host states as well as the various actors, institutions and ideas with which IIAs engage in their global networks.

Neglecting to explore the conditions under which governments break from investment rules and how they contest their enforcement has misled authors into assuming that the impacts of IIAs are both inevitable and consistent across time and space. However, as this study shows, the *real* impact that investment rules have on policy space lies in the middle messy ground between IIAs' potential impacts and the local responses they evoke (e.g. resistance, acquiescence or negotiation). The capacity of IIAs

to constrain policy space must therefore be understood as resulting from, and perhaps limited by, the productive friction between domestic actors and the networks that seek to enforce them.

### **1.3 Research Design**

This study employs a comparative case study analysis of Argentina and Ecuador's experience under IIAs between 1990 and 2015. Both countries have faced a significant number of investor-state disputes brought under BITs with advanced economic partners. They are respectively the first and seventh most frequent respondent states to investor claims in the world (UNCTAD 2014, 6). Both countries were also governed by left-leaning regimes at the height of these legal battles. The 2003 election of Néstor Kirchner in Argentina and the 2006 election of Rafael Correa in Ecuador signalled a significant political shift in each country. Both administrations attempted to re-assert state authority over domestic development strategies with new forms of social and economic policy that emphasize the state's role as a purveyor of equitable and sustainable growth (Riggirozzi and Tussie 2012). Both Kirchner and Correa also openly contested the authority of investment rules and protested the systemic bias towards Western commercial interests that they perceive as an inherent feature of international arbitral bodies, notably the International Centre for the Settlement of Investment Disputes (ICSID) under the World Bank. Assessing these governments' responses to investor claims enables a detailed examination of the effectiveness of different strategies governments can employ to defend policy space from the constraints IIAs impose. However, there are important differences in the countries' political institutions and in the ideological nuances of the regimes. Moreover, Argentina recently underwent national elections, which saw the

election of Mauricio Macri, a right-wing candidate. A more detailed explanation of the case study selection and institutional characteristics of the countries is provided in the sub-section that follows.

These cases serve two complimentary roles in this study. First, they act as ‘critical cases’, which according to Flyvberg (2006: 229) have “strategic importance in relation to the general problem” and allow researchers to “achieve information that permits logical deductions such as ‘if this is (not) valid for this case, then it applies to all (no) cases’.”

The cases have strategic importance to understanding the relationship between IIAs and policy space in two ways. On one hand, they provide an optimal opportunity to examine the extent to which IIAs impact policy space when governments adopt strategies aimed at defending domestic interests from investor claims. If IIAs were observed to constrain policy space consistently across time in each case, it would lend evidence to support the argument that IIAs shrink policy space even in the most challenging of contexts (that is, despite local resistance). On the other, if governments successfully mitigate or combat the constraints IIAs impose on policy space, it would suggest the need to nuance our understanding of the relationship between IIAs and policy space, for instance, by exploring the factors that enable governments to combat such constraints.

Second, the case studies also serve a comparative purpose in that they will allow me to examine the factors that contributed to the adoption of different defence strategies and the extent to which different methods of defence are effective. Both countries were governed by left-leaning regimes at the height of the ISDS cases addressed in this study. Yet the governments adopted different strategies in defending domestic interests. While Argentina defended domestic interests under the parameters of existing rules, Ecuador

gradually withdrew from IIAs and investor-state arbitration by denouncing the ICSID Convention. Following the logic of the most similar systems design (MSSD), I can hold several factors (such as regime type and broad ideological similarities) constant while assessing the intervening factors that informed governments' decisions to break with investment rules and resist their enforcement. This, in turn, will provide insight into how investment rules are enforced and how this enforcement can be interrupted.

However it is important to note that comparing these cases represents what Anckar (2007, 390) calls a "looser application of an MSSD", which is when "the researcher never systematically matches the cases on all the relevant control variables." Rather than selecting the cases with the intention of ruling out the impact of predetermined variables, my intention is to examine inductively how variables shared across cases – such as regime ideology - interact with other variables to produce different political outcomes. In this study, I am interested in two outcomes in particular: the consistency with which investment rules are enforced, and, the nature and effectiveness of government defence strategies, including the extent to which state officials are able to defend public interests under the agreements. While private-sector actors play an important role in contesting or reinforcing investment rules in different contexts, I focus particularly on assessing state actors' relations with progressive factions of civil society as a means of determining whether state actors responded to civil society demands in introducing policies or adopting defence strategies. A more thorough discussion of the methodology used in this study is provided in chapter three.

To inform this comparative analysis, I examined the investor-state disputes in which both countries have been involved through process tracing. I focus specifically on

Argentina's disputes with privatized utility companies and Ecuador's battles with foreign oil companies. These groups of cases represent the majority of disputes in each country and the most significant challenges to government policy. Moreover, many of the cases have since been resolved which allows for an analysis of the case outcomes. ISDS cases often take more than a decade to reach an initial ruling therefore it is difficult to determine the outcomes of more recent cases, such as the claims brought against Ecuador by Canadian mining companies in 2011. I also target cases that are more than five years old because, due to the lengthy time needed for cases to gain traction and materialize, older cases best demonstrate state responses to investor claims.

Process tracing is a method in which the researcher examines various sources to "see whether the causal process a theory hypothesizes or implies in a case is in fact evident in the sequence and values of the intervening variables" (George and Bennett 2005, 6). Following this logic, I examine each dispute to assess: what informed policymakers' decision to introduce the policy challenged by the foreign investor; whether the foreign investor used IIAs to successfully circumvent government policy; and, how and why state actors sought to defend domestic interests from the claim, including the degree to which they were successful. Process tracing can also perform a heuristic function, allowing the researcher to generate new variables or hypotheses by observing inductively the basic sequences of events (George and Bennett 2005, 7). By exploring these disputes in detail, I can examine what ideational and institutional factors intervened with the influence of IIAs to shape state responses to investor claims. I also expose the unintended consequences of the state actors' interactions with foreign

investors and arbitrators. This allows me to theorize inductively how policy space is manipulated and expanded under the potential constraints imposed by investment rules.

As the goal of process tracing is to obtain information about specific events and processes, as Oisín Tansey (2007, 765) argues,

the most appropriate sampling procedures are thus those that identify the key political actors - those who have had the most involvement with the processes of interest. The aim is not to draw a representative sample of a larger population of political actors that can be used as the basis to make generalizations about the full population, but to draw a sample that includes the most important political players who have participated in the political events being studied.

Following this logic, I conducted semi-structured interviews and archival research during five months of field research in Quito and Buenos Aires. 32 semi-structured interviews (eighteen in Argentina and fourteen in Ecuador) were held with key political actors over the course of January to May 2014 and October 2014 respectively. Interview respondents included corporate and state lawyers, government officials, civil society representatives and academic experts (see Appendix 1).

I identified potential interview participants through an analysis of legal transcripts and newspaper articles. I also identified participants through snow-balling, which involves “identifying an initial set of relevant respondents and then requesting that they suggest other potential subjects who share similar characteristics or who have relevance in some way to the object of study” (Tansey 2007, 770). This allowed me to gain access to respondents not identified in publically available documents. The interviews took approximately 45 minutes to one hour and were conducted in the offices of interviewees.

Each interview was based loosely on a questionnaire consisting of open-ended questions. Questionnaires were tailored to the particular field of expertise and experiences of each respondent as my aim was not to assess the frequency of particular responses given but to gain an in-depth understanding of the investment disputes from a variety of perspectives (see Appendix 2 for details).

I also undertook archival research to identify potential interview participants and to assess how the disputes played out, the public policy debates raised by the disputes as well as state responses. Archival sources included newspapers and transcripts of government debates as well as legal transcripts published online through ICSID, the University of Victoria ([italaw.com](http://italaw.com)), Kluwer Arbitration, and the International Arbitration Reporter. Legal transcripts are not often used in political science research as sources of information, however as this dissertation shows, they offer a rich and thorough description of public policy debates, the conditions under which investor claims were brought and state legal strategies.

#### **1.4 Case Study Overview: Post-neoliberalism in Argentina and Ecuador**

Ecuador and Argentina both possess presidential democracies with weakly institutionalized political parties and strong civil societies. This stems from their long histories of military coups and populist politics as well as the relatively recent nature of their democratic transitions. Both countries have also experienced economic crises that many civil society groups associate with the failures of neoliberalism. However, while opposition to neoliberal in Argentina mounted as the economy began to falter, the anti-neoliberal movement in Ecuador mobilized virtually as soon as austerity measures were announced. Opposition to neoliberalism and political corruption in both countries

produced widespread calls for political renewal. As such, both countries came to be governed by left-leaning governments at the height of the investment disputes of focus in this study. This includes the administration of Rafael Correa (2006 - ) in Ecuador and that of Néstor Kirchner (2003 – 2007) and Cristina Fernández de-Kirchner (2007 – 2015) in Argentina. Both the Kirchners and Correa had populist appeal and have been described as ‘post-neoliberal’ because of their discursive commitment to advancing progressive policy alternatives and recouping state authority lost during neoliberal restructuring (Riggiozzi and Tussie 2012). Despite these broad similarities, there are important differences between the cases that are of potential relevance to this study, notably in terms of the subtle ideological differences between the Kirchner and Correa governments as well as the social bases on which they rose to power. As this section demonstrates, these factors have informed each government’s development agendas and, in turn, may influence their approach towards the global political economy.

I begin this section with a brief discussion of the countries’ political history, focusing on past experiences with populism and their processes of democratization. I then provide a brief overview of the civil societies that emerged in the wake of political liberalization as well as the nature of state-society relations prior to the introduction of neoliberalism. This is meant to provide the necessary contextual background for a concise analysis of the post-neoliberal shift in both countries and the subtler differences between the Correa and Kirchner administrations. I leave a more thorough discussion of each country’s neoliberal period to chapters five and six to avoid repetition. I also touch upon the basic structure of their political systems and how this might impact the relative power each government possesses vis-à-vis society and other levels of government. This

analysis will be carried forward through the remainder of this study as I examine how these factors have influenced the approaches taken by the governments towards investment disputes.

Prior to the 1980s, both countries experienced considerable political instability resulting from successive coups that deposed elected and unelected governments. Political parties have therefore historically been loose organizations with weak party discipline. Frequent internal divides in some of the larger political parties have also produced a degree of factionalism in both countries, with legislators changing party allegiances routinely during each congress. This means that governing parties often have relied on establishing alliances with smaller parties and / or executive decrees to advance policy goals (Isaacs 1993; Levitsky and Murillo 2008). Larger political parties have also depended on the populist appeal of charismatic leaders rather than policy platforms or ideology as a means of gaining support. This, in turn, has contributed to the rather fluid nature of parties' policy platforms and party allegiances.

Populism has been a persistent feature of politics in both countries. Here, populism is understood as “the top-down political mobilization of mass constituencies by personalistic leaders who challenge elite groups on behalf of an ill-defined pueblo, or ‘the people’” (Roberts 2007, 5). The most notable historic populist leaders are José María Velasco Ibarra in Ecuador and Argentina’s Juan Domingo Perón (1946-1955). Velasco was Ecuador’s first populist leader and was elected to power on five separate occasions between 1934 and 1972. A member of Ecuador’s Conservative Party traditionally dominated by land-owning elites, Velasco’s populism relied more on the charismatic quality of his campaign than on any promise of substantive political and economic

reforms. Velasco most often adopted austerity measures aimed at economic stabilization and appeasing the interests of elites. The country's brief and sporadic experiment with import-substitution industrialization (ISI), which is more strongly associated with populist politics in Argentina, occurred under military regimes in the mid-1960s and again in the 1970s (Isaacs 1993, 17 – 19).

Juan Perón gained widespread popularity in Argentina during his tenure as head of the Department of Labour under the military regime of Pedro Ramírez (1943 – 1945). Under Perón, the Department strengthened labour laws and passed sweeping social reforms aimed at improving working conditions. Perón became wildly popular with Argentina's already strong labour unions and the Confederación General de Trabajo (CGT), a leading voice of the labour movement. Perón won the 1946 election as a candidate of the Partido Justicialista (Justicialist Party or PJ), which he founded with his wife Eva Perón. Unionists were given prominent government positions, cementing the alliance between labour and the Peronist party, which committed itself to advancing social justice and economic independence (Levitsky 2005). As such, Perón instituted economic reforms aimed at rejuvenating economic growth through ISI and new labour laws that reinforced his relationship with labour (Grugel 2009, 50). However, Perón's popularity polarized Argentine society. He was removed from office in 1955 through a military coup led by economic and military elites and banned from national politics.

Perón, however, left a number of important political legacies. According to James McGuire (1997), Perón's ban from politics prevented the institutionalization of the Peronist party and discouraged unions from developing formal representation in electoral politics. Unions therefore became an important check on the power of politicians outside

of formal political arenas. ISI policies instituted under Perón were also carried forward, in one form or another, by subsequent governments until the mid-1970s. Yet it was Peronism that became most strongly associated with state intervention.<sup>3</sup> Indeed, Perón's leftist-populist nationalism was translated into a political ideology, referred to as *Peronismo*, which had an important impact in future political debates despite its varied manifestations (see chapter six) (Wylde 2011, 440). Perón returned briefly to Argentine politics in the mid-1970s however his third tenure as president (1973-1974) was cut short by his death. Perón's second wife, Isabel Perón assumed power, but was overthrown in a military coup in 1976 that saw the rise of a repressive military junta.

The military junta suppressed political opposition in what became known as the Dirty War. Estimates suggest that over 11,000 people were killed and 30,000 more 'disappeared'. Argentina's democratization came about in 1982 when domestic and international pressure forced the junta to gradually restore political liberties. This saw the return to the national stage of the PJ and the right-leaning Unión Cívica Radical (Radical Civic Union, UCR). Elections were held in 1983 that resulted in the election of Raúl Alfonsín, the UCR candidate. Democratization also saw the emergence of a strong, highly organized network of human rights groups, independent media and the return of a highly active labour movement, which had been weakened by military rule. Consensus also strengthened across Argentine society, including the military, on the importance of maintaining democratic rules and basic political freedoms. Argentina's democracy was therefore able to survive numerous political and economic crises that plagued the country

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<sup>3</sup> For a detailed account of Argentina's import-substitution industrialisation policies across governments see Belini (2012).

since the early 1980s, notably the economic crisis of 1989 that resulted in sky rocketing inflation and the more severe economic crisis in 2001(Levitsky 2005).

Unlike in Argentina, Ecuador's democratic transition was initiated by the military after it deposed the government of General Rodríguez Lara (1972 – 1976). Lara ruled over Ecuador as a personalist dictator and extended state control over the economy through ISI and the establishment of state-owned enterprises. Yet increasing fractionalization within the military regime combined with citizen demands for political liberalization weakened the regime's support base. The military junta oversaw a gradual transition towards democracy over a period of three years, including the drafting of a new constitution and rules to govern political party organisation. Numerous political parties emerged or re-emerged, including the long-standing Partido Social Cristiano (Social Christian Party, PSC) and the Concentracion de Fuerzas Populares (Concentration of People's Force, CFP) and numerous splinter parties including the Partido Roldocista Ecuatoriana, Pueblo, Cambio y Democracia and the Partido Unidad Republicana. A general election was held in 1978, resulting in a landslide victory for centre-left CFP candidate Jaime Roldos and his running mate Osvaldo Hurtado (Isaacs 1993, 127).

The civil society that emerged in Ecuador during its democratization reflected the country's unique historic experiences and population. Whereas political liberalization saw the emergence of human rights groups and return of organized labour in Argentina, Ecuador's labour movement was weak in comparison to its entrepreneurial class and had been suppressed by the military leadership, which banned strikes and demonstrations by labour unions (Isaacs 1993, 121). Instead, Ecuador's democratic transition coincided with a resurgence of indigenous organizing resulting from a renewed sense of indigenous

political identity that swept through the countryside. This manifested in 1986 with the creation of the Confederación de Nacionalidades Indígenas del Ecuador (Confederation of Indigenous Nationalities of Ecuador, CONAIE), an alliance forged between 14 indigenous nationalities and 18 pueblos (Escobar 2010, 20). CONAIE sought to rally together indigenous groups around a common call for greater cultural rights and political inclusivity. In June 1990, CONAIE led massive marches, blockades and protests that crippled the country's transportation networks. At the heart of this movement were demands for bilingual education, agrarian reform and the recognition of Ecuador as a plurinational state, meaning the acceptance and inclusion of Ecuador's diverse cultural and ethnic composition and the right to difference as a guiding principle for the country's governance moving forward (Collins 2014, 75; Lucero 2003, 32).

The composition of each country's civil societies in the wake of democratic transition laid the foundation for an eventual post-neoliberal shift. In Ecuador, indigenous groups were joined by environmental activists as some of the most vocal critics of neoliberal reforms in the 1990s and early 2000s. In 1999, a severe economic crisis hit Ecuador and prompted the government of Jamil Mahuad (1998-2000) to freeze bank deposits and dollarize the economy, measures that deepened public skepticism of politicians and neoliberal reforms. Demonstrations held by indigenous and environmental activists were joined by a broad cross-section of civil society including petroleum workers laid off from state oil companies, teachers' unions and women's organizations. The mobilization of diverse sectors of civil society served to be a powerful force as the governments of Jamil Mahuad and Lucio Gutiérrez (2003-2005) were forced out of office

after street protests gave Congress and the military grounds to unseat them (Conaghan 2008, 48).

Neoliberal restructuring and the subsequent economic crisis in 2001 also engendered significant opposition from civil society in Argentina, particularly as unemployment rates climbed. The government of Carlos Menem (1989 – 1999), which initiated the dramatic neoliberal program, privatized state-owned enterprises and introduced reforms to increase the flexibility of the labour force and reduce labour costs for businesses (Grugel and Riggirozzi 2007, 91). This was despite Menem's campaign promises to resurrect Peronist policies in the lead up to his first election. This weakened the power of the labour movement as thousands of workers were laid off from privatized businesses. The unemployed and displaced workers, who had long histories of political activism, fed the emergence of new social movements that mobilized in opposition to neoliberal reforms, including the *piquetero* (picketers) movement and consumer groups that formed in protest to the privatization of basic services. While demands for the reversal of neoliberal reforms were accompanied by a call for expanded cultural rights and a new approach to development and politics in Ecuador, activist demands in Argentina focused more on the creation of employment opportunities and access to government programs that would protect them from market insecurities. This mobilization became more extensive and widespread during the 2001 economic crisis and led to demands for political renewal (Levitsky 2005). Therefore, while the two countries have political histories that are in some ways similar, the context in which the post-neoliberal shift occurred demonstrated important differences that would inform, to some extent, the particular character of post-neoliberalism in each country.

## **New Left Governments**

Rafael Correa was elected President in November 2006 with the support of a broad-based political movement, Alianza Patria Altiva i Soberana (Proud and Sovereign Fatherland, PAIS), winning 56.7 percent of the vote in the second round (Conaghan 2008, 50). A US-trained economist, Correa had previously served as the Minister of the Economy under Alfredo Palacio (2005-2007) and gained popularity for his strong opposition to neoliberal policy. His political campaign promised to institute a Citizen's Revolution and a 21st Century Socialism. Correa also denounced the existing political party structure as exclusive and corrupt and chastised the business establishment, including banks and some media outlets for controlling politicians (Conaghan 2008, 47). This discourse earned him populist appeal and a majority government, a rare feat in a country known for its volatile party system.

Néstor Kirchner, a candidate of the rejuvenated PJ, was a relative unknown in Argentine politics prior to his 2003 election and won by only a slim margin. The election, following on the heels of the country's greatest economic crisis, was marked by considerable uncertainty and unrest. However, Kirchner's mix of labour reforms, conservative fiscal policy and the extension of social welfare programs earned him widespread popularity, particularly as the economy began to rebound. Kirchner's election was preceded by four years of strong economic growth, averaging at 9 percent a year. By 2007, opposition parties had weakened considerably which made Kirchner's re-election almost a forgone conclusion. Kirchner however chose not to run and instead his wife, Cristina Kirchner ran in his place. Cristina Kirchner was elected with 45 percent of the vote, easily defeating competitors of the centre-left Civil Coalition and the UCR. The JP,

in turn, won more than 75 percent of the governorships and together with allies from smaller political parties won 160 of 257 seats in the lower house of the National Congress (Levitsky and Murillo 2008, 16). Therefore, while populist appeal was not responsible for Néstor Kirchner's election, the widespread popularity he gained throughout his tenure as President ensured the Kirchners would remain in power for over a decade.

Both Néstor Kirchner and Correa began their presidencies by cutting their own salaries in half and enjoyed high approval ratings in their early years, with opinion polls surpassing 60 and 70 percent (Conaghan 2008, 53). This enabled Correa to achieve two easy electoral feats within a year of his election that were necessary to advance his revolutionary project. In April 2007, Correa's proposal to formulate a constituent assembly to lead the development of a new constitution received 82 percent of votes in a popular referendum. The following September, Correa's governing party was also awarded 80 out of 130 seats in the Constituent Assembly (73 out of 130 seats outright and a further 8 seats through alliances with minor political parties) installed in November to last for 180 days (Conaghan 2008, 46; Escobar 2010, 20). The new constitution, ratified in 2008 by popular referendum, was meant to provide a legal basis on which the government would transform state institutions to enhance the inclusivity of decision making processes and extend state oversight over the economy (Collins 2014).

Correa has taken advantage of the relative absence of significant political opposition and his own popularity to advance new social and economic policies. Correa used windfall profits from oil exploitation to fund (through a series of executive decrees) the extension of social programming. Among the decrees included an order to double the regular welfare payments to poor households from US\$ 15 to \$30 a month and an order

to double the amount available for housing loans. Correa also enacted subsidies that halved the price of electricity for low-usage consumers while a number of other programs were expanded to offer more credit to micro-businesses, youth and women. Ordering the expansion of social programs through decrees has enabled Correa to advance his leftist agenda free of red tape. For instance, from January to July 2007, Correa dispersed US\$ 215 million by declaring emergencies in ten sectors, including education, health and the prison system (Conaghan 2008, 54).

Correa has also implemented policies aimed at shifting resources from elites to the poor and marginalized sectors of society. For example, Correa expropriated 195 companies belonging to the Isaías Group in July 2008 in order to recover some of the assets that customers lost when corporate corruption forced the Group's bank, Filanbanco to collapse in 1998. Correa gained further support in December 2008 after he ordered a default on more than US\$ 3 billion in foreign bonds that the state treasury was able to pay. Defaulting was meant to be a symbolic protest against the terms of the debt and was framed as a necessary move taken in defence of the country's sovereignty (Becker 2016, 47).

Yet there are some contradictions in Correa's development agenda. Arturo Escobar (2010, 20) describes Correa's development agenda as exhibiting a tension between neo-developmentalism, understood as the "forms of development understanding and practice that do not question the fundamental premises of the development discourse of the last five decades, even if introducing a series of important changes" and post-development, meaning "the opening of a social space where these premises can be challenged." The 2008 Constitution, for instance, aims to enable the institutional

transformations required to advance a new model of society through a different vision of development and territorialisation while recognizing pluricultural identities and plurinationality. This new vision of development is one that advances the *sumak kawsay* (in Quechua) or *buen vivir* (Spanish), translated as ‘collective wellbeing’, reflecting the unique influence of indigenous activists. As such, the Constitution also recognizes the rights to nature, or the Pachamama, which is thought to be essential to the pursuit of *sumak kawsay* (Gudynas 2009).

Several of the policies instituted by the Correa administration do not accord with this vision of development. The national development plans developed by Correa to serve as a guiding framework for development policy borrow from dominant development discourses in stressing economic competitiveness and technological advancement with no mention of how such goals will be rectified with the pursuit of social transformation and the *sumak kawsay* (Escobar 2010, 20 - 22). Correa’s promotion of extractive industries has been particularly controversial as it has not coincided with a genuine strengthening of environmental laws and monitoring, which has brought him into repeated conflicts with indigenous and environmental groups. Correa considers the extractive sector as a tool to alleviate poverty and his modernization project is dependent upon the revenue derived from mining and oil production. Indigenous and environmental activists however assert that the constitution’s overarching recognition of the importance of *sumak kawsay* demands greater efforts to establish alternative relationships between humans, nature and development (de la Torre 2013, 460; Becker 2016, 49).

Correa has also been criticized for failing to respond to indigenous demands for agrarian reform and water redistribution and for attempting to erode indigenous solidarity.

Over 200 indigenous and environmental activists have faced accusations of terrorism for resisting resource extraction (de la Torre 2013, 461). Correa also dismantled state institutions that were previously in the hands of indigenous social movements, such as the parallel bilingual education system managed by indigenous communities outside of the Ministry of Education from 1988 to 2009 (de la Torre 2013, 460). Correa has given a more prominent role to smaller indigenous organisations that more strongly support his development plan, including the Consejo de Pueblos y Organizaciones Indígenas Evangélicos del Ecuador (Council of Evangelical Indigenous Peoples and Organizations of Ecuador) and the Federación Ecuatoriana de Indios (Ecuadorian Federation of Indians). This, combined with internal divisions over Correa's policies has weakened CONAIE's claim to be the hegemonic representative of subaltern concerns in Ecuador (Becker 2016, 52).

Moreover, despite his commitment to establishing “an active, radical and deliberative democracy”, Correa's governing practices demonstrate a preference for technocratic expertise and formally educated people (original quote in de la Torre 2014, 458). Correa has given favourable positions to technocrats from academic institutions and NGOs in the state bureaucracy to the exclusion of less-formally educated members of civil society, including indigenous peoples (Becker 2016, 51). Unlike in Bolivia, where the regime of Evo Morales engages directly with social movements through participatory mechanisms, Correa's brand of participatory politics has taken the form of popular votes and referenda rather than genuine participatory institutions. Therefore, while Correa rose to power on the support of indigenous and environmental activists, there are clear tensions in his development agenda between a concern for political inclusivity and

poverty alleviation on one hand and the desire to strengthen the country's competitive position in the global economy while relying heavily on state technocrats on the other.

The post-neoliberal development agendas of Néstor and Cristina Kirchner however were characterized by less overt contradictions. Néstor Kirchner sought to advance progressive policies within the parameters of an export-led model and conservative fiscal policy, using heterodox policies that reflected, to some extent, a return of ISI. In terms of macroeconomic policy, Kirchner introduced a *Stable and Competitive Real Exchange Rate* policy to encourage growth in the export sector, which stabilized the Argentine peso and facilitated the accumulation of foreign exchange reserves and tax revenues. This, in turn, funded the extension of anti-poverty programmes, government infrastructure spending and industrial policy, which favoured export sectors. The success of this policy was supported by record international commodity prices; however, Kirchner diverted the benefits of this trend towards encouraging growth in the manufacturing sector. Kirchner also negotiated with banks to increase access to credit for businesses and introduced selective protective tariffs designed at promoting small and medium sized businesses (Wylde 2011, 438). Central to Kirchner's social policy was the extension of conditional cash-transfers, similar to those used by Correa, which saw specific cash amounts distributed to impoverished households. This included the programs *Jefes y Jefas de Hogar Desocupados*, *Plan Familias* and *Planes Trabajar*.

Following the 2001 economic collapse, Kirchner also took a hard-line position in the country's debt renegotiations that resulted in the largest debt 'haircut' (of about 30 percent) in history and paid off the country's loan with the International Monetary Fund (IMF), significantly easing financial pressures. To appease the labour movement,

Kirchner pushed through a series of minimum-wage increases, which brought about a 70 increase in real wages. Kirchner also passed a social-security reform that extended access to unemployed and informal-sector workers and increased public investments in basic service provision almost five-fold. In terms of the judicial system, Kirchner overhauled the Supreme Court, widely believed to be corrupt and repealed laws limiting the persecution of military officers implicated in violence of the Dirty War. This earned him the support of unemployed and labour movements as well as human rights organizations. Kirchner then solidified relations with the CGT and business community by creating spaces for their participation in policy development. By the end of his first term, Kirchner had proved adept at responding to citizen demands while the post-economic recovery created new employment opportunities, placating social unrest. Néstor Kirchner therefore left the office as the most popular outgoing president in contemporary Argentine history, paving the way for his wife's election (Levitsky and Murillo 2008, 17).

Cristina Kirchner continued her husband's policies and gradually extended them in some areas. This includes steady increases to the minimum wage and an extension in scope and kind of conditional cash transfers with the creation of a new program targeted at improving child welfare, the *Asignacion Universal por Hijo*. However, Cristina Kirchner also faced mounting political opposition from private sector elites and the middle class. Many middle class households protested the continuance of foreign exchange controls and the return of high inflation. In 2008, farmers and agricultural elites held massive demonstrations in opposition to an increase on the export taxes of agricultural products, a measure that was introduced to increase state funding for subsidies on basic services as the state faced increasing fiscal pressure and economic

growth slowed. By the end of her second term growing unrest from the business sector and middle class, fed by the slowing economy, created fractions in the PJ and slowly eroded the support base on which Cristina Kirchner stood. Kirchner also became embroiled in a protracted legal dispute with the remaining creditors who failed to negotiate a debt haircut in 2005, which forced Argentina into a technical default in August 2014 (Wylde 2016, 334). This served as a divisive political issue in the 2015 elections, which Kirchner's proposed successor, Daniel Scioli, lost to centre-right candidate Mauricio Macri.

While Argentina's post-neoliberal period has seemingly come to an end, Correa has continued to mobilize public support behind his agenda despite growing opposition from indigenous and environmental groups. This is likely, in part, because of Correa's public outreach and campaign strategy. From the beginning of his presidency, Correa employed popular media outlets to convey messages directly to citizens and strengthen his populist persona. For example, Correa developed a two-hour weekly broadcast called *The President Dialogues with his Constituents*, which features on Saturday mornings on 154 stations. Correa uses the opportunity to champion government policy while scolding political opponents and, as will be demonstrated, foreign oil companies (Conaghan 2008, 53). Correa was re-elected in February 2013 with 57 percent of the vote, with members of the AP gaining 100 of the Assembly's 131 seats (de la Torre 2013, 459). This has contributed to an unprecedented degree of political stability in the country. However, much of Correa's electoral base now consists of the unorganized and marginalized urban middle - and lower- classes and small businesses owners as opposed to the more organized environmental and indigenous social movements that saw him to power

(Becker 2013, 51). This might suggest reduced pressure to adhere to the more progressive aspects of his post-neoliberal agenda.

It is important to note the considerable differences in how political power is divided institutionally in each country as Argentina's political system is more decentralized than that of Ecuador. Ecuador's political system is unicameral with weak sub-national governments. Almost all decision-making power is therefore vested in the national government and presidents are elected for four-year terms. Argentina's national government is bicameral, with legislative power divided between an upper and lower house. The country's 23 provinces and one autonomous zone (the city of Buenos Aires) exercise considerable decision-making power, for example, over resource exploitation and basic service provision. Alliance-building and negotiation between different levels of government are therefore stronger qualities of political decision-making in Argentina than Ecuador. However, the emergency measures adopted in the wake of Argentina's economic crisis in 2001 expanded the executive's powers to advance policy through decree. Such powers were retained by the Kirchners in the years preceding the crisis, although this became increasingly controversial over time. Néstor Kirchner issued 232 executive decrees during his tenure, at a rate of 4.3 a month this was comparable to Menem's own rate of 4.4 a month. Kirchner also increased the dependency of provincial governments on fiscal transfers from the federal government by opening up new sources of revenue (export duties and fees on public services) that it did not share with provinces. As a result, provinces' share of overall revenue fell of almost half of what it had been a decade prior (Levitsky and Murillo 2008, 19). Therefore, while Ecuador's political

system vests more power in the hands of the executive than does Argentina, the Kirchners were able to strengthen their authority by centralizing power, albeit temporarily.

The Kirchner and Correa administrations share broad, but important similarities in their development agendas. Both have sought to re-assert state sovereignty on the international stage through anti-neoliberal rhetoric and by contesting the authority of international financial institutions. Both governments have also introduced policies aimed at poverty alleviation. However, it is important to note that the conditional cash transfer programs, a defining feature of both governments' social policy, are not designed to prevent poverty from happening or to address its structural causes, but are instead designed to prevent individuals from falling into abject poverty. This brings them in line with the social-safety net logic championed by neoliberal advocates (Beccaria et al. 2007). Tensions therefore exist (and existed in the case of Argentina) between governments' claimed post-neoliberal development goals and the neoliberal logic reflected in some aspects of their development programming.

Moreover, although their common commitments to progressive policy alternatives that break away from stringent neoliberal policy qualify the Correa and Kirchner administrations as post-neoliberal, there are important differences in their post-neoliberal orientation. While Correa balances neo-developmentalism with post-development (but in practice has leaned towards neo-developmentalism), the Kirchners were unabashedly neo-developmentalists in their discourse and logic. Despite the Kirchners' often confrontational rhetoric against international financial institutions and neoliberal policy, Néstor Kirchner also proclaimed the need for '*capitalismo en serio*' (serious capitalism) and fiscal discipline (quoted in Wylde 2011, 439). There has also been no attempt to

embrace such concepts as pluriculturalism and plurinationality in Argentina. This is largely because the social bases which prompted the neoliberal shift are distinct in each country. There has not yet been a sub-altern voice to emerge in Argentine politics that would push the state towards a post-development model. Whether these subtle differences in postneoliberal ideology and social movements have been reflected in the governments' approaches towards foreign investors and ISDS is a question requiring further exploration.

Examining the impacts of IIAs in the context of two post-neoliberal governments allows for a thorough examination of the strategies governments may use to protect their policy space from the constraints IIAs impose and the extent to which such strategies are effective. Right-wing regimes are more likely to accept the precepts upon which IIAs are based, therefore it is difficult to determine to what extent they are constrained by IIA enforcement mechanisms as opposed to their own economic and political preferences. They are also less likely to challenge investor claims or the authority of IIA enforcement mechanisms. As such, an analysis of Ecuador and Argentina's experience under IIAs and with ISDS cases will provide the opportunity to compare the effectiveness of defence strategies and how governments might manipulate and expand policy space under the agreements. I am also interested in examining the factors that drive governments to break with investment rules and whether governments do so in response to public interests. Argentina and Ecuador therefore provide ideal opportunities to assess the power IIAs exert over policymaking processes by revealing the extent to which IIAs constrain government action in the face of domestic resistance and whether IIA enforcement

mechanisms are effective in holding the governments accountable for infringements of investor rights.

## **1.5 Chapter Outline**

In the following chapter, I critically assess existing literature and illustrate how the neglect of domestic actors in studies of policy space has limited our understanding of global economic integration and its relationship to domestic political processes. I situate this discussion within broader debates regarding the role of IIAs in attracting foreign investment and promoting substantive economic progress in the developing world. A growing body of evidence supports the conclusion that IIAs impose important limitations on the exercise of policy space while providing uncertain economic benefits. I also bridge this discussion with the emerging body of literature on post-neoliberalism in the Americas. In several Latin American countries, civil society demands for progressive policy alternatives that address market insecurities and socioeconomic and political exclusion materialized in the election of left-leaning governments throughout the first decade of the 2000s. These ‘post-neoliberal’ governments face numerous investor claims while advancing policy alternatives and have increasingly challenged the legitimacy of investor rights. These developments support the need to rethink the relationship between IIAs and policy space in a way that is better attuned to the agency of domestic actors.

Chapter three provides a new theoretical framework for understanding and analyzing the relationship between policy space and IIAs. I argue that we must move beyond understandings of policy space that view it as simply the range of policy options that exist under prevailing national and international rules. Instead, I define policy space the range of policy options policymakers perceive to be available and politically feasible,

the perceptions of which are structured by (competing) material, ideational and sociopolitical forces operating simultaneously. Conceptualizing policy space in this way enables researchers to gain greater analytical purchase on how various factors, including IIAs shape policy space in practice. I then discuss how ideational and material variables relate to perceptions of policy space.

Using the insights of constructivist scholars (Mitchell 1999; Sassen 2007, 2008; Tsing 2005), I also argue that global economic arrangements must be examined in light of their intimate interactions with local contexts. Such interaction provides global processes force and effect just as a tire requires a surface in order to spin. Yet it also generates “unequal, unstable and creative qualities” that Anna Tsing refers to as ‘friction’ (2005, 4). Friction helps define movement, cultural form and agency at all scales and can be compromising or empowering for those involved.<sup>4</sup> Understanding the global and local as co-constitutive shifts our attention toward the transformative impact of global arrangements in specific sites and how such impacts, on policy space for instance, are mediated or reinforced by local actors. Exploring policy space as a product of global-local interactions, in turn, requires a more nuanced understanding of the state that acknowledges its cohesive qualities as well as its fragmented nature. This opens up space for analyzing how different state actors interact with environmental factors to shape their response to investor claims and their likelihood to abide by the constraints investment rules aim to impose on state action. By theorizing IIAs and their connections with domestic actors in this way, I create greater space for exploring state agency and the strategies actors use to defend policy space. I also demonstrate the value of thinking

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<sup>4</sup> By ‘scale’ I refer to the socially-constructed and hierarchically arranged levels of space that constitute the ‘local’, ‘sub-national’ and ‘national’.

about the impacts of IIAs as contingent rather than inevitable and leave open the possibility that such impacts vary across time and space.

Chapter four historicizes the development of the global assemblage in which IIAs are situated. Its aim is to expose how investor-state relations were problematized over time in such a way as to render necessary legal intervention in the form of contemporary IIAs. By problematized, I refer following Li (2007, 264), to “how problems come to be defined as problems in relation to particular schemes of thought, diagnoses of deficiency and promises of improvement.” Exposing this problematization is essential to understanding what unites the various components of the assemblage and, in turn, what grants IIAs force and effect. I trace the roots of this problematization to the colonial encounter and its impacts on customary international law, which informed the founding principles of contemporary IIAs. An image of developing countries’ legal systems as inferior and backward was built upon through discourse and practice to separate the rights of foreign investors from the duties of host states so that the latter fell into the realm of what constituted ‘private law’ and the former ‘the public / international law system’. This discursive separation has had powerful implications for the power of foreign investors to challenge state action while safeguarding investors and their operations from the duties that might otherwise be imposed by public international law. Investor-state disputes were rendered not as sociopolitical disputes involving challenges to policymaking but as legal-technical controversies to be handled by experts in private law, which were seen to be less motivated by ideological or political calculations. This problematization has served to unite the diverse range of institutions, knowledges and actors meant to enforce investment rules.

In chapters five and six, I employ the theoretical framework developed in chapter three to examine the impact of IIAs on policy space in Argentina and Ecuador respectively. I examine the political circumstances that informed government officials' decisions to introduce policies in conflict with investor rights and, subsequently, how foreign investors sought to activate IIAs by translating investment rules into specific obligations for host governments. I then explore the multiplicity of actors involved in the enforcement of investment rules against host governments and the uneven ways in which investment rules were applied in both case study countries. I then analyze how processes of enforcement intersected with other ideational and material factors to shape the responses of government officials and their legal representatives. I also assess the degree to which states' defence strategies were effective in preserving policy autonomy and what this tells us about the relationship between IIAs and policy space when we include state agency. Chapter seven concludes by comparing the factors informing the countries' defence strategies and what this has meant for the overall effectiveness of the constraints IIAs pose on policy space. It then synthesizes the contributions made by this study to broader understandings of global economic integration and domestic policymaking processes.

## **2 Chapter: International Investment Agreements and Policy Space:**

### **Reclaiming the Agency of Domestic Actors**

In the last decade, scholarly attention has been increasingly devoted to exploring the impacts of international investment agreements (IIAs) on the policy space of developed and developing countries. Interest in IIAs has been driven both by the proliferation of the agreements in the 1990s as well as the subsequent wave of investor claims brought against host states in recent years. In this chapter, I critically assess existing literature on the relationship between IIAs and policy space and problematize its failure to address two related aspects: first, the role state and other domestic actors play in shaping the impacts IIAs have on policy space; and second, the specific mechanisms through which IIAs impact policy space in practice. Neglecting to fully investigate these aspects has encouraged scholars to portray IIAs as having universal and inevitable impacts across developing countries regardless of the context. As such, emphasis is typically placed explicitly on the role of foreign investors in challenging government policy and action. Yet governments do not always abide by investment rules and foreign investors are not always successful in challenging of government policy. We know little, however, about how governments contest the enforcement of investment rules and what factors limit the power of IIAs to induce constraints on government action. This is while countries, particularly those governed by Latin America's post-neoliberal regimes, have increasingly brought into question the legitimacy of investment rules.

I first provide a concise review of the literature regarding the political economy of trade policy. Scholars have widely acknowledged the political nature of trade

policymaking and have exposed the role pressure group politics, institutions, political leadership and other factors operating at the global and local level play in shaping global trade and investment rules. The politics of trade policy implementation and enforcement however, receives much less attention. This is problematic, particularly given that various actors with competing sets of interests are likely to play important roles in reinforcing or contesting the legitimacy of trade and investment rules as they are enforced against states.

I then summarize ongoing discussions related to ‘post-neoliberalism’ in the Americas to contextualize the contestation of IIAs in Latin America. Post-neoliberalism is a blanket term used to describe the left-leaning governments recently elected in Latin America (Cameron 2009; Castañeda 2006; Escobar 2010; Grugel and Ruggirozzi 2012; Ruggirozzi and Tussie 2012). These governments, elected at the national and sub-national level in countries as diverse as Argentina, Chile, Brazil, El Salvador, Ecuador, Venezuela and Bolivia among others, were elected based on their commitment to advancing progressive policy alternatives that better protect citizens from market insecurities, encourage wealth redistribution and / or enhance the inclusivity of political processes. The rise of post-neoliberal governments has had important implications for the domestic, regional and global economies; however their impact on arrangements at the global scale has not been adequately addressed. This is despite the challenges emerging from post-neoliberal governments towards global economic arrangements, including IIAs. The role of post-neoliberalism has also not yet been fully brought into debates over policy space; whether post-neoliberal countries have the policy space needed to institute their development agendas is questionable under prevailing trade and investment rules. Though there has been a return to the right in some countries like Argentina, bridging

discussions on post-neoliberalism with debates on policy space can expose the power of IIAs as a neoliberal legacy and strengthen understandings of the degree to which investment rules reduce governments' abilities to meet citizen demands.

Yet prominent approaches to the study of IIAs and policy space have difficulty in capturing and accounting for the role of states of any regime type. In the latter sections of this chapter, I critically examine ongoing debates related to the added value of IIAs in fostering substantive and sustainable economic development before focusing more explicitly on the relationship between IIAs and policy space. I argue that a more nuanced perspective that incorporates the role of domestic actors and critically explores the mechanisms through which IIAs impact policy space in practice is an essential step towards gaining a better understanding of how IIAs shape policy space in practice, the elements that mediate these impacts, and the strategies actors used to resist these impacts.

## **2.1 The Politics of Trade and Investment Policy**

The proliferation of trade and investment agreements in the 1990s generated much scholarly interest in exploring the determinants of trade and investment policy. Global power politics, policymaker preferences, the ideational influence of neoliberal philosophy, interest group lobbying and economic necessities are factors, scholars argue, that have contributed to the shaping of global trade and investment rules. Although by no means exhaustive, this section provides a brief overview of dominant debates regarding the political economy of trade policy. While scholars disagree as to which factors exert the strongest influence, the consensus is that the formulation of trade policy is fundamentally a political process involving negotiation between diverse and often competing sets of interests. While scholars have provided considerable insight into the politics of trade

policymaking, the politics of enforcing trade and investment rules against governments has not been adequately addressed. That is, little is known about how interest group lobbying and global power politics impact the implementation of trade and investment agreements. This, in turn, has meant that such factors and the practical challenges of enforcing trade and investment rules have been neglected in the literature on policy space.

At the domestic level, scholars argue that interest group politics and systems of representation have an important impact on the formulation of trade and investment rules (for a concise review see Alt et al. 1996). Scholars typically see interest groups as divided into two competing camps in terms of their likely attitude towards trade liberalization. On one side is the pro-trade camp composed of large, internationally-oriented businesses that stand more to gain from trade and investment liberalization and therefore push for the signing of new trade agreements. On the other side is the protectionist camp dominated by small businesses, industry associations and some civil society groups. Since they fear being subsumed or displaced by influx of foreign capital and imports, they are likely to oppose trade agreements outright or push for the inclusion of exemptions and long adjustment periods during trade negotiations. Some scholars have attempted to delineate more specifically pro-trade actors from protectionist actors according to industry / sectoral characteristics or factor-specificity (Irwin 1996; Frieden 1990; Midford 1993; Scheve and Slaughter 1998; Anderson 1980; Trefler 1993). Ronald Rogoswki (1987), for instance, asserts that since the owners of locally scarce factors are more likely to be domestic suppliers and the owners of local abundant factors are, in turn, more likely to export, the latter favours protectionism while the former pushes for trade liberalization. Regardless of how groups are classified, scholars that emphasise pressure group politics

assert that the competition between free trade and protectionist groups and coalitions, combined with their capacity and willingness to engage in collective actions such as vote mobilization or protest and the power they exert relative to competing coalitions, creates the ‘demand’ by society for liberalization or protection, which informs policy decisions (Alt and Gilligan 2003, 328).

These approaches have been combined with an effort to uncover the institutional conditions under which one group might be particularly influential. Such influence, scholars find, depends on the extent to which a particular group is given, or obtains, formal access to policymakers and state bureaucrats (Mansfield and Bush 1995; Rogowski 1987; Vieira 2016). In the context of a democratic state, big business constituencies, scholars argue, are typically given more privileged access to trade policy arenas because of their pro-trade stance, business expertise and because they are perceived to have more direct stakes in negotiation outcomes. They also tend to have greater human and financial resources to dedicate to opening up access to policymakers through government lobbying (Shadlen 2004; Thacker 2000). Yet, Alt and Gilligan (1994), argue that not all political systems provide the same incentives for collective action. If a political system is such that it rewards small sectoral groups, actors will be less willing to undertake the costs of organising large coalitions through which to influence trade policy. If all one has to do is influence a select number of legislators, there is no reason to waste time and resources on mobilizing support for a particular policy. However, if a political system rewards mass mobilizations (i.e. a coalition of labour unionists), then actors are more likely to organize or participate in large coalitions since doing so may result in perceived benefits.

The nature of countries' political regimes more broadly has also been associated with different approaches to trade policy. Scholars argue that democratic countries are more likely to co-operate to lower trade barriers and thus pursue trade liberalization. This is while autocratic countries are more likely to be rent-seeking and, in turn, pursue protectionist policies as a method of capturing higher rents (Milner 1999, 101; Wintrobe 1998; Mansfield et al 1997). Others have focused more on examining how structural differences in the political and party system lead to different trade policies. The degree to which decision-making power over trade policy is divided between national and subnational powers, the fragmented or polarized nature of political parties, and the presence of veto powers in the executive or legislature are all factors that authors argue may reduce or slow down the likelihood of trade liberalization (Hilner 1999, 103; see also Haggard and Kaufman 1995; Armijo and Kearney 2008). Baldwin (1986), for example, explains US import policies as an outcome of the way in which decision-making power and relations are structured between the US Congress, the International Trade Commission, and the President (and advisors).

A problematic aspect of interest group and institutionalist accounts is that they tend to envision trade policy outcomes as driven by struggles between competing demands and visions in the absence of historic and cultural traits. Some scholars, however, have sought to expose how historical experiences and culture impact policymakers' decision making with respect to trade policy, either by shaping policymaker perceptions directly or by shaping social demands for different approaches to trade policy. Goldstein (1988) and Krueger (1997), for example, examine the various factors that affect policymakers' preferences and ideas about trade policy, focusing on the

role of changing norms in the former and political learning in the latter. Sergio Caballero Santos (2015) takes a more historic approach and argues that strong nationalist visions developed in the nineteenth century during independence struggles and the idea of a unifying project in the face of an external enemy (namely the ‘North American Other’) amongst South American countries were central factors that enabled the formulation of Mercosur as a trading bloc. Particular ideas and identity, he claims, can facilitate or impede the formulation of a collective identity, which in turn can facilitate or impede the establishment of regional integrationist projects. This stands in contrast to interest group and institutional approaches, which imply that trade policy outcomes would be the same across countries with similar domestic constituencies and institutional contexts regardless of variations in culture and historical experience.

In terms of international determinants, scholars have attributed the signing of free trade agreements to the coercive influence of economically dominant states and international financial institutions (Krasner 1976, Gilpin 1987). Indeed, advanced economies such as the United States, Canada and the European Union countries exerted significant bilateral pressure on developing countries as a means of securing more stringent commitments on trade and trade-related measures such as intellectual property, financial services and investment protection (Haggard 1995; Evenett and Meier 2008). International institutions, such as the IMF, World Bank and UNCTAD have also influenced the move towards trade liberalization by championing of neoliberal policy in the global South, enhancing countries’ participation in trade and investment negotiations through capacity-building programs, and normalizing free trade via the provision of technocratic expertise (Rodrik 1992; Stiglitz 2002; Grabel 2007). Thus, the presence and

activism of these institutions is strongly associated with the diffusion of free trade and investment agreements in the contemporary era.

Other authors also attribute the proliferation of trade agreements to the desire amongst developing countries to balance against the power of advanced economies, for example, by binding more powerful states to mutually beneficial rules as a means of protecting themselves against their opportunistic behaviour (Shadlen 2004). In his analysis of the WTO's Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), Kenneth Shadlen (2004) finds that developing countries will seek to strengthen the procedural aspects of multilateral institutions as a means of ensuring that more powerful states are subject to mutually-recognized rules. This was the case, he argues, in the formulation of TRIPS as developing countries used the negotiations to secure the availability of pharmaceutical patents essential to the preservation of public health, such as HIV/AIDS medicines. Manger and Shadlen (2014) also find that developing countries seek formal trade agreements with developed countries despite enjoying preferential market access from the generalized system of preferences and related schemes. This, they argue, stems from the desire amongst developing countries to secure stable market access and avoid the kinds of political dependence generated by the fact that developed countries, under such schemes, can unilaterally withdraw preferential access as they choose.

Increasing attention has also been directed toward examining how transnational coalitions of civil society organizations shape the global trade agenda by mobilizing public support for particular initiatives, information gathering and dissemination, and the development of policy solutions to targeted problems (Murphy 2010; Esty 1998; Scholte

2004). Although opportunities for civil society participation in trade policymaking are often limited, civil society actors working in transnational networks have been particularly successful in pushing environmental and labour concerns onto the trade negotiating agenda in the WTO and in bilateral and regional trade agreements such as NAFTA.

Along a similar line, scholars have also acknowledged the contested nature of trade disputes and dispute settlement mechanisms in the WTO. Compliance with WTO rulings, scholars recognize, is dependent largely on 'power' relationships, particularly between developed and developing countries (Walters 2011; Brown 2004). Trade agreements, Chad Brown (2004) observes, are largely self-enforcing, which makes the threat of bilateral retaliation between trade partners an underlying means of gaining compensation in dispute settlement negotiations. For developing countries, however, the ability to adopt retaliatory measures against a developed state that fails to meet its WTO obligations is impeded by the fact that most developing country markets do not consume enough imports for its trade sanctions (as the predominant retaliatory measure) to have a noticeable impact on the offending country. Developing countries have also been found to be at a disadvantage in filing a trade dispute when a trade partner breaks its WTO obligations because they have less legal capacity, which refers to the institutional, financial and human resources needed to monitor, pursue and litigate a dispute (Zeng 2013). Therefore, rather than serving to bind developed countries to an agreed upon set of rules, the WTO rules have been criticized as fundamentally bias against the poorest and underdeveloped countries who have little capacity to enforce them (Smith 2004; Brown and Hoekman 2005).

While much of the literature on trade disputes has focused on the factors that enable some states to win over others, little attention has been paid to examining the factors that lead to trade disputes in the first place and how different actors at the domestic and international level intervene in enforcement proceedings. An exception of the former trend is Hofmann and Kim (2010) who argue that political leaders have an electoral incentive to maximize economic benefits to a strategic economic sector or industry by prolonging non-compliance as long as possible. This, in turn, may result in the initiation of a complaint by a trading partner or prolong the length of an existing dispute. Strategic sectors, the authors note, are those with a large labour force or that generate a large share of the economic output of the state. Kim (2015, 288) also argues that respondent states reap several economic and political benefits from proceeding through the dispute settlement process and prolonging it. First, the respondent state may not lose and, in the case that it does lose, the state is able to maintain the disputed policy for as long as it takes the tribunal to issue a ruling. Second, respondent states can leverage an unfavourable ruling by a dispute settlement panel as a ‘political cover’ against a particularly powerful domestic group in modifying or eliminating the disputed policy (see also Allee and Huth 2006).

Despite the burgeoning interest in trade dispute settlement, there is a need to examine more fully the global and local factors that help shape how such disputes play out. Studies of trade policymaking grant recognition to the power of interest groups, political leadership and institutions in shaping trade policy yet these insights have so far made only initial incursions into studies of trade policy implementation. We know little, for example, about how interest group lobbying, economic variables, political leadership

and global power politics shape governments decisions to break with trade and investment rules and the strategies governments adopt to defend their policy choices. Moreover, there is a need to examine the ‘politics’ of dispute settlement in the context of IIAs, which has erected a different set of international dispute settlement rules and institutions than that of the WTO’s dispute settlement procedures. This study aims to help address this gap by examining the politics of IIA enforcement, particularly the agency of state actors to shape enforcement processes and the global and local factors that inform state approaches.

## **2.2 Post-neoliberal Politics in the Americas**

The wave of electoral victories by left-leaning regimes in Latin America presaged the resurgence of the developmental state in the Americas. The failure of structural adjustment programs and economic integration with the West to induce substantive and inclusive growth catalyzed dissatisfaction with neoliberalism and promoted what Riggirozzi and Tussie (2012) term ‘a political renewal’ in many pockets of the region. Left and centre-left regimes championing ideas to improve income redistribution and social services came to power, beginning with the 1998 election of Hugo Chávez in Venezuela with a commitment to progressive social policy and the promise of a ‘new socialism for the 21<sup>st</sup> century’. This was followed by the election of Ricardo Lagos, leader of the Socialist Party in Chile (2000) and Lula da Silva’s Workers’ Party in Brazil (2002), both promising to address their countries’ poor by modifying neoliberal policies. Argentina, Bolivia and Nicaragua, Ecuador, Guatemala, Paraguay, El Salvador and Honduras followed suit with (respectively) the election of Néstor Kirchner in 2003, Evo

Morales and leader of the first indigenous socialist government in 2005, the re-election of the Sandinistas under Daniel Ortega (2007), Rafael Correa (2007), Álvaro Colom (2008-2012), Fernando Lugo (2008-2012), Mauricio Funes (2009- 2014) and Manuel Zelaya (2006 – 2009).

This ‘post-neoliberal’ shift has attracted much attention from the scholarly community and has led to many attempts to distinguish post-neoliberal governments from the regimes that preceded them (Cameron 2009; Macdonald and Ruckert 2009; Grugel and Riggirozzi 2012). To Jorge Castañeda (2006, 33), post-neoliberal governments are characterized by “that current of thought, politics and policy that stresses social improvements over macroeconomic orthodoxy, egalitarian distribution of wealth over its creation, sovereignty over international cooperation, democracy...over governmental effectiveness”. However as Macdonald and Ruckert (2009) and Escobar (2010) argue, post-neoliberalism should not be understood as an era ‘after neoliberalism’ nor as a return to the leftist regimes that governed prior to the neoliberal turn. Rather, post-neoliberalism encompasses a variety of social practices and discourses that strategically engage with contested forms of neoliberal governance. Moreover, post-neoliberalism has yet to develop into a clearly definable body of material practices (Macdonald and Ruckert 2009,7; Grugel and Riggirozzi 2012, 3). Thus, it is harder to capture the nuances of the post-neoliberal turn than Castañeda suggests. Moreover, as Kenneth Roberts observes (2008, 329), where post-neoliberal governments have taken office, differences exist in the levels of social mobilization and party system institutionalization in addition to the policy orientations of their leaders. Such variation, Maxwell Cameron argues (2009, 331),

reflects the diverse conditions under which the progressive forces associated with the post-neoliberal turn emerged and evolve.

For instance, post-neoliberal governments cannot be fully understood in absence of the domestic social movements that saw them to power. Hilson and Haselip observe (2004, 38) that as the first region to undergo neoliberal reform, “Latin America has produced some of the fiercest resistance movements and political rejections of the neoliberal agenda.” Indeed, social movements laid the groundwork for the emergence of post-neoliberal governments and are critical to the advancement and survival of a leftist agenda (Becker 2013, 43; Silva 2009). Central to the political appeal of post-neoliberal governments are the commitments made to respond to local demands for greater access to the state, better welfare provision and policies that recognize cultural, communal and indigenous rights (Grugel and Riggirozzi 2012, 8). However, as the recent election of Mauricio Macri in Argentina demonstrates, such support is not guaranteed.

As illustrated in the preceding chapter in the cases of Ecuador and Argentina, the social bases on which post-neoliberal governments rose to power vary considerably: whereas Rafael Correa rose to power on a preceding wave of indigenous organising, the Kirchners’ popularity had its bases in the unemployed workers movements and the resurgence of trade union activism following the post-crisis recovery. Arturo Escobar (2010) describes the diversity of sociopolitical transformations in Latin America as a series of contrasts between two complementary, but at times competing, projects: First, there is the advancement of alternative modernizations, “based on an anti-neoliberal development model, in the direction of a post-capitalist economy and an alternative form of modernity”; and second, there are the decolonial projects “based on a different set of

practices (e.g. communal, indigenous, hybrid, and above all, pluriversal and intercultural), leading to a post-liberal society” (2010, 11). Both projects, he argues, are taking place to different degrees both within the state and in society. Hence, to truly understand post-neoliberal transformations and the different forms they take across countries, one must look at both the state and social movements as well as their inter-relationships.

A defining feature often referred to as uniting the new left is the “commitment to using state power and/or popular participation to alleviate socioeconomic inequalities and protect individuals and groups against market insecurities” (Cameron 2009, 333). Post-neoliberal governments do not entirely oppose private property or market competition but rather reject the idea that unregulated market forces can be relied on to meet social needs (Levitsky and Roberts 2011, 5). They therefore demonstrate a renewed willingness use public authority, state institutions and policies to reduce social and economic inequalities through redistributive measures, enhance opportunities for the under-privileged and provide social protection against market insecurities. As Grugel and Riggirozzi assert (2012, 4), this includes “an evolving attempt to develop political economies that are attuned to the social responsibilities of the state whilst remaining responsive to the demands of ‘positioning’ national economies in a rapidly changing global political economy.”

Many of the progressive policy alternatives sought by post-neoliberal regimes arise out of the contradictions and failures of neoliberalism (Macdonald and Ruckert 2009). Yet policy alternatives will inevitably co-exist with neoliberal legacies and are being advanced in the context of a global economy that is still heavily influenced by the

neoliberal paradigm. Free trade and investment agreements, which proliferated in Latin America during the era of neoliberal economic restructuring, are potentially the most challenging legacy, as many of the agreements contain provisions that aim to limit governments' policy flexibility. As is discussed in the sub-section that follows, investment chapters in free trade agreements and BITs are argued to effectively ban the use of industrial policies and performance requirements that might interfere in the profit-making of foreign firms (Cho and Dubash 2005). This is potentially problematic for post-neoliberal development agendas that stress an activist role for the state in economic governance.

As several studies demonstrate, post-neoliberal governments are attempting to redefine the role of the state vis-à-vis the global economy. For example, Paul Haslam (2009) explores recent changes to foreign investment policy in Chile (2000- present) and Argentina (2003 – present). He finds that both governments instituted measures to increase fiscal pressure on foreign investors in order to meet broader development goals – the former through the renegotiation of public service contracts with foreign investors and the latter by increasing the taxation on foreign mining activities. He attributes the greater willingness to leverage state authority over foreign investors to both a change in policymakers' perceptions regarding the opportunity costs associated with regulating foreign companies as well as an increase in the objective vulnerability of transnational corporations (TNCs) in the 2000s.

Similarly, Bebbington and Bebbington (2011) analyze neoliberal and post-neoliberal regimes' ways of governing extraction and socio-environmental conflicts in Peru, Ecuador and Bolivia. They find that post-neoliberal governments in Ecuador and

Bolivia took new measures to govern extractive industries in ways that distinguish them from their neoliberal predecessors. Under Correa, Ecuador passed interim mining legislation that declared stringent environmental and social controls, rescinding several concessions and freezing a series of exploratory projects until irregularities were addressed. Correa also proposed to protect Ecuador's Yasuni rainforest from destruction by companies seeking to gain entry to the rich oil deposit on which it lay, provided that the international community put half the revenue that Ecuador would have received from oil extraction into a fund Ecuador could use to pursue broader development projects.<sup>5</sup> In Bolivia, measures were taken to generate and redirect surplus for redistribution from the extractive industry, including the nationalization of hydrocarbon projects. However in both cases, a continued reliance on the extractive industries for revenues and economic performance limited governments' willingness to control the expansion of extractive projects in sensitive areas. Despite growing social opposition to extractive projects, these governments rely on natural resource exploitation as a central pillar of their development strategies and have associated it with greater social spending to help justify the expansion of extractive activities (Bebbington and Bebbington 2011).

Some attempts to reassert state authority over domestic economies have prompted treaty claims from foreign investors under IIAs. This, in turn, has generated debate about the role and value of IIAs amongst scholars, policymakers and civil society. For instance, Denis Collins (2009) provides a nuanced analysis of the Salvadorian government's decision to delay issuing a mining permit to Canada's Pacific Rim for the exploitation of

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<sup>5</sup> Ecuador's Yasuni proposal has since failed as Ecuador did not receive the funding deemed necessary to avoid opening up the area to foreign oil firms. The implementation of Ecuador's mining legislation has also been highly criticized as inadequate, which is likely due to the activism of the major mining companies within the country and Correa's continued faith in extractivism as a development tool.

the El Dorado mine. Although the government of El Salvador is open to international capitalism and TNCs, massive protests from social movements and civil society organizations against the mine's potentially destructive impacts on the environment and surrounding communities drove the government to place a freeze on granting mining licenses until a new mining law was drafted. Pacific Rim, whose pending application was subsequently frozen, responded by suspending its existing operations, terminating local staff and bringing a suit against El Salvador under the Central American Free Trade Agreement.<sup>6</sup> Similar reactions to changes in domestic economic policy and regulation have been observed throughout Latin America (see North and Young 2013; Spronk and Crespo 2008; Kaup 2010).

Yet little is known about how Latin American governments have responded to such litigations. Instead, emphasis has been placed on demonstrating the rights IIAs grant to foreign investors. There is also a need to connect the post-neoliberal turn with shifts in foreign policy and explore what such shifts mean for the future of global arrangements. For instance, evidence suggests an increasing willingness on the part of post-neoliberal governments to challenge the international investment law regime. In April, 2013, Ecuador, Venezuela, Nicaragua, Bolivia and several Caribbean states established an alliance to fight against claims made by foreign investors under IIAs. The alliance, known as the "Conference of Latin American States affected by Transnational Interests" adopted a declaration in which country members agreed to work towards establishing a permanent conference of states to deal with challenges posed by TNCs, including

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<sup>6</sup> Although Pacific Rim is based in Vancouver and Canada does not have an IIA with El Salvador, its subsidiary in the United States was able to introduce the claim on behalf of its parent company under the Central American Free Trade Agreement.

coordinating political and legal actions and information sharing (Raman 2013). This initiative led to the creation of the Southern Observatory on Transnational Corporations, which facilitates information sharing on defence strategies across member countries and provides training to government officials. Under the auspices of Unión del Suramericanas (Union of South American Nations, UNASUR), Latin American governments are also working to establish an alternative investor-state arbitration centre to act as an alternative to current arbitral tribunals that are perceived to be dominated by Western interests.

Although still in its early stages, the centre is expected to encourage local dispute reconciliation, incorporate enhanced transparency mechanisms and establish a formal appellate mechanism. There are currently no means by which host governments can appeal awards rendered by ICSID tribunals and cases are often concluded behind closed doors beyond the purview of civil society. The lack of transparency in ISDS proceedings has been a major point of contention amongst Latin American governments who face increasing demands from civil society for access to the proceedings (Grant 2015). However whether such efforts will ultimately provide Latin American governments greater protection against investor claims in comparison to the current global IIA regime has yet to be explored.

The post-neoliberal turn has also coincided with new forms of intra and extra-regional relations and institution-building that provide expanded opportunities for inter-state cooperation outside of traditional (neoliberal) economic arrangements. That is, some recently established alternative institutional structures and cooperative projects incorporate normative dimensions (including social development, community action and new forms of politics and organization) into existing practices. Riggiozzi and Tussie

(2012) distinguish two variants of regional projects that differ from traditional projects focused solely on commercial integration (e.g. the Pacific Alliance). First, there are projects that advance traditional commercial concerns (such as trade) while also seeking alternative autonomous trade and post-trade political projects, including the Central American Common Market (CARICOM), El Mercado Común del Sur (Mercosur), the Andean Community and the Unión de Naciones Suramericanas (UNASUR). Secondly, there are projects that more radically emphasize the political and social dimensions of integration with new commitments to welfare, reclaiming principles of socialism and opposition to neoliberal globalization. The most obvious example of this approach is the Alianza Bolivariana para los Pueblos de Nuestra América (ALBA) founded by Hugo Chávez. Although ALBA commits to encouraging greater intra-regional economic cooperation, its initiatives have so far focused enhancing cooperation in the delivery of regional social programs aimed at poverty alleviation, health and education (Lamrani 2012).

Several Latin American countries have also pursued stronger economic and political ties with China as an alternative to further integration with the West. The Chinese market attracts an increasing amount of Latin American exports and is a major source of imports. Chinese investors are also significant players in the region's infrastructure and extractive sectors (Kotschwar 2014). China also serves as an alternative source of financing for cash-strapped post-neoliberal governments whose relations with traditional partners in the international financial market have soured. China forgoes many of the loan conditionalities imposed by traditional finance partners (e.g. the IMF) and is seen as less likely to interfere in the articulation of countries' sovereignty

(Conaghan 2008, 56). China does not make the receipt of loans and investment conditional on the presence of an investment agreement; however it has signed new BITs with Colombia (2010) and Mexico (2007) modeled after the more stringent agreements championed by advanced economies. A growing number of studies are dedicated to exploring China's expanding influence in the region (Ellis 2009; Li 2007; Jenkins et al. 2008). However, scholars have yet to explore whether and how strengthening relations with non-traditional partners and emergent regional projects offer Latin American countries the opportunity to expand or exploit policy space in ways that traditional international partnerships do not.

Therefore, while there is a rich and burgeoning body of literature dedicated to studying the local, national and regional nuances of the post-neoliberal shift, further research is needed to examine whether these governments have the policy space needed to introduce the progressive policies they champion and that their citizens demand. There is also a need to explore exactly how the advancement of progressive policies conflict with international trade and investment rules and how governments defend their policies in the face of such conflict.<sup>7</sup> Moreover, authors have yet to explore how the demands of civil society and private-sector actors influence governments' policy space. For instance, we know little about whether and how the social movements that saw post-neoliberal governments to power influence government decision-making with respect to abiding by or breaking with investment rules. How, for example, does the advancement of ideas related to *buen vivir*, *sumak kawsay*, and the rights of nature by indigenous groups challenge the state's relationship with foreign investors? Failing to acknowledge the

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<sup>7</sup> An exception is Abugattas and Paus (2008).

influence such non-state actors exert on political decision making with respect to investor-state relations and international economic arrangements renders invisible the often-important role that local actors and social forces play in the global political economy.

### **2.3 Policy Space and International Investment Agreements**

Significant progress has been made in exploring how IIAs impede the policy autonomy of signatory countries. Yet as this section demonstrates, the literature on IIAs is characterized by significant gaps. Namely, there has not yet been a serious investigation of the role of state and non-state actors in contesting or reinforcing the constraints IIAs impose on policy space. There is also a need for further analysis and debate on how we conceptualize policy space, its relationship to domestic actors, and the forces that grant investment rules force and effect. The first subsection provides a concise review of the scholarly debates regarding the value of IIAs as a developmental tool. While proponents of the agreements claim they are a necessary means for governments in the developing world to attract foreign capital to aid in developmental processes, the evidence to support this claim is shaky at best. The second sub-section details common criticisms of IIAs and their impact on policy space. It focuses more explicitly on drawing out common assumptions about the relationship between investment rules and domestic policymaking processes and then highlights areas in need of further research if we are to understand how IIAs impact policy autonomy in practice.

## **Establishing the Global IIA Regime: IIAs as a Tool for Development or Binding**

### **Hands?**

Since the 1990s there has been an unprecedented proliferation of overlapping IIAs. According to UNCTAD (2015, 2) estimates, 3, 268 investment agreements have been placed into force as of 2014 (UNCTAD 2014). As Paul Haslam (2010, 1181) observes, foreign investment in the Americas is now governed by a multi-layered patchwork of agreements including national investment laws, BITs, chapters in free trade agreements, common markets, and multilateral institutions such as the WTO. IIAs are intended to promote, protect and liberalize foreign investment between countries through legally binding rights and obligations that aim to govern relations between states and foreign investors. Typically, IIA provisions cover the admission, establishment, operation and withdrawal of foreign-owned firms in host markets. IIAs also specify investment dispute settlement procedures, which since the emergence of more stringent agreements in the post-NAFTA era, includes providing investors recourse to international third-party arbitration tribunals should firms perceive their treaty rights to have been violated (Haslam 2010, 1183; Yu and Marshall 2008, 2). In doing so, IIAs aim to provide stability and security to investments by limiting the range of legitimate government interventions in investors' affairs and providing for compensation should investment rules be violated (Cho and Dubash 2005, 148-149).

Proponents of the agreements claim they are a necessary means to attract needed foreign capital, technology and expertise. This is particularly true for developing countries where investment environments are perceived to be risky or otherwise unfriendly because of deficiencies in domestic legal systems (Movesesian, 2008). Some

authors argue that IIAs help governments overcome credibility problems and reassure other states and non-state actors that governments will provide a friendly investment environment regardless of domestic political conditions. The rules and enforcement mechanisms contained in IIAs increase the material costs of commitment violation (Blake 2013, 798; van Aaken 2009, 507). Moreover, advocates of third-party dispute arbitration bodies such as ICSID argue that such institutions provide a neutral and efficient venue for dispute resolution. Such bodies are argued to “foster the international rule of law and an investment-friendly environment” through their independent and impartial application of investment rules (Movesesian 2008).

Much of the literature on IIAs, however, is dominated by debate over whether such agreements create or diminish the conditions needed for substantive development in practice. Several studies investigate whether IIAs induce greater foreign investment flows than would otherwise have been the case in the absence of such arrangements and find mixed results (Hallward-Driemeier 2003; Busse et al., 2010). Neumayer and Spess (2005) find that developing countries that are signatories to a larger number of BITs have attracted higher FDI inflows. However Tobin and Rose-Ackerman (2005) find that BITs did not appear to encourage FDI except in instances where there was already a low level of political risk. The authors attribute this trend to the inability of BITs to attract greater foreign investment and the likelihood that decreases in political risk are accompanied by economic liberalization, which disadvantages existing foreign investors who benefited from the closed environment and decide to exit the market (2005, 22). They therefore reject the idea that BITs are a good substitute for a favourable domestic business environment. Indeed, there is mounting evidence that suggests the strength and

independence of domestic political and judicial institutions do more to attract foreign capital than IIAs. Knack and Keefer (1995), for example, find that the quality of a country's bureaucracy, property rights and political stability had a positive and statistically significant relationship with economic performance. Rodrik et al. (2004) also provide evidence that the quality of domestic institutions is a better indicator of cross-country income levels than geography and levels of economic integration.

Other authors explore the relationship between foreign investment and economic growth more generally and have also found contradictory results (Khawar 2005; Kentor and Jorgenson 2010; Bonschier 1980, Dixon and Boswell 1996, Reis 2005). Greater access to technology, patents, business strategies and research and development (R&D) expenditures are argued to result from stronger FDI inflows and have positive spill-over effects for host economies. TNCs are also often good sources of needed employment and their presence can help alleviate balance-of-payment deficits (Blomstrom et al. 1994; Dunning 1993; Borensztein et al. 1998). Mariam Khawar (2005) finds a positive correlation between FDI and growth in income per capita in developing countries. However Khawar fails to determine whether countries' economies grew as a result of foreign investment or if countries already growing at a faster rate were more successful in attracting foreign investment. Kentor and Jorgenson (2010) find that the growth of foreign subsidiaries in developing countries between 1970 and 2000 had a direct positive effect on economic growth. However, they find that the expansion of foreign subsidiaries is inhibited by high concentrations of ownership by TNCs headquartered in the same home state.

A number of studies demonstrate that foreign investment has net positive outcomes only when other conditions are in place, such as a minimum level of human capital (Borensztein et al. 1998), backward and forward linkages between TNCs and domestic firms, and a transfer of R&D activities to the host state (Rama 2008). Such conditions are not commonly found in developing economies. Scholars also warn that foreign investment may have negative repercussions including heightened dependencies on investing countries, decapitalization (Bornschiefer 1980), escalations of economic inequality (Dixon and Boswell 1996) and a crowding out of domestic investors (Reis 2005, 1047). Authors also find that foreign investment can have negative social ramifications including environmental degradation and escalation of human rights abuses (Tienharra 2006; Jorgenson 2007; Reiter and Steensma 2010; Hilson and Haselip 2004). In light of these varied findings, governments and the international development community have expressed a concern for strengthening the kinds of national and international institutions needed to capitalize on the potential benefits of foreign investment while limiting the negative repercussions from such economic activity. Yet several scholars question whether IIAs limit governments' capacity to implement the policies required to do so.

### **IIAs and Policy Space: Common Critiques**

The failure of neoliberal adjustment and one-size-fits all development strategies to effect substantive economic progress in the developing world has encouraged renewed interest in the role of the state in development. Growing faith in domestic political institutions has been buttressed by the desire to increase country ownership over development initiatives and the move toward context-specific development strategies

(Gallagher 2005; Rodrik 2004). It is no surprise then that policy space has occupied a more prominent position in development discourses across the last decade. If domestic institutions are to play a role in establishing the conditions needed to foster inclusive growth, it follows that a degree of autonomy in policymaking is needed to ensure national development strategies best address local needs and contexts with an appropriate policy-mix.

Some proponents of trade and investment rules and loan conditionalities argue that restricting governments' policy space helps ensure that needed capital enter a country despite government corruption and inefficiencies. Restricting government action therefore helps protect citizens from harm should state institutions be captured by interest groups or the self-interest of political officials (Williamson 2004). Moreover, as Mayer (2009, 375) asserts, "the mere fact of having policy space does not imply that it is always put to good use." The effective deployment of policy space, he argues, requires that governments have a clear vision of where they want to take an economy. This, in turn, necessitates the formulation of a national development strategy attuned to local capabilities, challenges and opportunities with clear objectives, practices and monitoring mechanisms. Yet what exactly constitutes a 'clear vision' is unclear, which means it is likely left to those with the power to exercise normative influence.

Other authors argue that economic integration increases countries' policy space in some facets. Peter Evans (2005) argues that trade and investment rules provide opportunities for reform-oriented governments to shed themselves of rent-seeking firms that are dependent on state funds for survival. By saying 'my hands are tied', governments can let go of rent-seeking lobbies and build new alliances with more

productive areas of their economies. Mayer (2009, 377) similarly argues that multilateral rules enable a coordinated response to cross-border disturbances and prevent more advanced economies with a disproportionate influence from adopting beggar-thy-neighbour policies. Some authors have sought to explore more specifically how countries can better use their policy space under existing trade rules without opting out of international commitments (for example Ayala and Gallagher 2005). However, this argument downplays the more constraining influence of WTO-plus measures introduced via bilateral trade and investment agreements.

In the last decade, IIAs have come to the forefront of the debate over policy space. And they have been strongly criticised for imposing constraints on governments' abilities to raise the living standards of their citizens. This means that developing countries could be sacrificing state powers for uncertain economic benefits. There are three common arguments about the ways in which IIAs impact policy space: first, critics argue that IIAs induce a chilling effect on domestic regulation as governments fear that enacting new regulatory schemes will conflict with their obligations to foreign investors (Manger 2008; Yazbek 2010, Spears 2010; Wagner 2014-2015). IIAs are designed to provide protection to investments made abroad by locking governments into predictable regulatory frameworks (Cho and Dubash 2005, 150). Nicole Yasbeck (2010) argues that this results in foreign investors being immune to domestic regulation that acts contrary to their interests. This, in turn, can impede the introduction of regulations needed for governments to meet obligations to human rights and environmental law and to introduce development policies that address the unique circumstances of the country (Simm 2011). For example, the limitations IIAs often place on the introduction of performance

requirements for foreign-owned firms can reduce governments' abilities to harness positive spillover effects from foreign investment (Gallagher 2005; Chang 2006).

In failing to provide adequate safeguards for the exercise of government activity, the provisions contained in IIAs can also reduce governments' room for manoeuvre in developing social policy. To illustrate this point, Yazbek (2010) notes a suit instituted against the South African government over the implementation of its *Black Economic Empowerment* (BEE) program. The program was designed to promote racial diversity in the management and ownership of the economy to better reflect demographic realities. Foreign investors challenged the BEE scheme claiming that the Act's requirements (including appointing black managers and selling a 26 percent equity holding to BEE compliant partners) constituted a violation of investors' rights to protection against expropriation and to receive fair and equitable treatment.

Secondly and related to this point, common provisions contained in contemporary IIAs, such as those on fair and equitable treatment, require host states to treat foreign investors on a level playing field with domestic investors. Such provisions, scholars argue, reduce governments' abilities to introduce sector-specific industrial policy designed to promote or leverage domestic investments for industrial growth (Gallagher 2008; Chang 2004, 2006; Wade 2005). According to Chang (2004), many now-developed countries (i.e. the US, EU member states and East Asian economies) systematically discriminated between domestic and foreign investors in their industrial policy throughout early stages of their development. The benefits of non-discrimination and liberalization, Chang argues, appear to outweigh the costs only when domestic industries reach a specific level of sophistication, complexity and competitiveness. Therefore principles of non-

discrimination found in IIAs are better seen as an outcome of development and not a cause.

Lastly, signing on to IIAs can have drastic repercussions for governments' abilities to fund progressive social and economic policy without taking on additional debt, which can exacerbate financial crises (Stiglitz 2007, Van Harten 2008). The financial compensation awarded to investors under investor-state dispute arbitrations is considerable. In 2009/10, approximately 151 investment arbitration cases involved foreign investors demanding in excess of US\$ 100 million from host states. Moreover, there are considerable costs in the form of legal bills associated with such proceedings. The growing number of investor-state disputes has contributed to the proliferation of a multimillion-dollar industry of professional and highly paid legal experts trained in international investment law and arbitration. In fact, it is estimated that legal and arbitration costs in investor-state disputes average over US\$8 million per dispute and have exceeded \$30 million in some cases (depending on the length of the legal dispute) (Olivet and Eberhardt, 2012). Indeed, governments are forced to either redirect funding away from policy spending or increase tax burdens for their people in order to meet the costs of the legal disputes.

Such arguments point to the potential long-term repercussions of signing on to IIAs. We can take from these arguments that IIAs can have negative impacts on policy space at multiple stages of policymaking processes. First, IIAs are said to deter governments from adopting certain policies, including regulatory regime changes, as they might conflict with investment rules. Second, IIAs provide the means by which actors discipline governments for adopting policies during and after the policy's implementation.

Lastly, IIAs can limit governments' abilities to introduce policies in the future that require additional spending by reducing the resources available to fund their implementation. However, there has not yet been an adequate analysis of whether IIAs impact all such stages equally in all countries and at all times. Examining the stages of policymaking at which IIAs have stronger and weaker impacts can help nuance our understanding of the risks of signing on to IIAs.

Issues of policy space shrinkage are compounded by the commercial bias of arbitral proceedings observed by many analysts (McArthur and Ormachea 2008-9; Hueckel 2012; Olivet and Eberhardt 2012; Van Harten 2008). International arbitral bodies were originally established to provide a neutral venue for the resolution of investor-state disputes. Under early investment agreements (pre-1990), investors appealed to their home government to pursue claims against host-countries on investors' behalf. The establishment of third-party institutions represented an attempt to 'depoliticize' investment disputes by empowering investors to sue states directly (McArthur and Ormachea 2008-9, 560). However ICSID and other international tribunals are composed on an ad hoc basis of judges that analysts observe are educated predominantly in Western institutions and have a commercial law background (as opposed to human rights or environmental law). Critics argue that this ensures judges will interpret and apply investment rules according to commercial norms and will therefore be less sensitive to conflicts with human rights and environmental law (Olivet and Eberhardt 2012).

Arbitrators also lack the ability to interpret and apply IIA provisions in light of countries' domestic circumstances. Arbitrators must instead base their decision on the

scope of the written agreement, which contains rules criticized by analysts as overly ambiguous and broad (Yazbek 2010). Van Harten (2008) argues that the ambiguity of IIA provisions encourages “interpretive gap-filling” by arbitral judges who often interpret provisions liberally to ensure investor protection. The example he provides is the flexibility often given to definitions of nationality. Arbitrators, by interpreting the IIA’s reference to nationality broadly, allow investors to assume the nationality of a state party to an IIA solely by establishing a holding company within a party state. This encourages forum shopping, as investors strategize their claims by selecting the jurisdictional link from which to bring a claim under the most favourable conditions or make multiple claims under different IIAs in relation to the same dispute.<sup>8</sup>

Kent and Harrington (2012) and Gomez (2012) have also explored how different interpretations of the ‘necessity doctrine’ provided for in BITs and in customary international law have led to very different outcomes in investor-state disputes in the post-crisis Argentine context. The vagueness of investment rules therefore provides arbitrators a significant degree of power in deciding exactly how constraining a given provision will be on governments’ policy options (Abugattas and Paus 2008, 125). Given that arbitrators are appointed and not accountable to an oversight mechanism, such arbitral processes are criticized as interfering in the democratic exercise of countries’ policymaking processes (Van Harten 2008). The inconsistency of arbitral rulings and

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<sup>8</sup> Van Harten (2008) notes a recent case *Aguas del Tunari v. Bolivia* in which the US firm Bechtel, facing public opposition to its privatized water utility in Bolivia, migrated its firm from the US to the Netherlands, enabling it to bring a claim against the Bolivian government under the Netherlands-Bolivia BIT. He also illustrates this point using a case in which an American investor, Ralph Lauder used a Dutch holding company to bring multiple claims in a dispute with the Czech Republic. Lauder made the first claim under the Czech Republic’s BIT with the US and then under the Czech Republic-Netherlands BIT. Lauder lost the first case but won the second and was awarded a sizeable award.

disagreements with arbitrators' interpretations have increased scepticism over the impartiality and effectiveness of dispute resolution bodies.

In the last decade there has been a significant decline in the number of BITs signed per year relative to the 1980s and 1990s, a trend that authors note is largely due to the significant rise in the number of investor disputes across the globe and growing dissatisfaction with international dispute resolution bodies (Van Harten 2008, 94; Poulsen and Aisbett 2013; Jandhyala, Henisz and Mansfield 2011). To Poulsen and Aisbett (2013), the declining rate of new BITs signed is best explained by a process of political learning, whereby the rise of investment treaty claims led to a spatially and temporally dispersed delivery of information to host states about the costs associated with signing on to BITs. Taking a bounded rationality approach, the authors assert that governments, often unaware of the potential costs of BITs at the time of signing, have undergone a change in beliefs as a result of observing and interpreting experiences associated with investment disputes. Thus, many governments are now less willing to sign onto BITs.

Despite the increasing contestation of IIAs, there is still a tendency within the literature to treat IIAs as homogeneous (Simmons 2014). Most IIAs contain a standard set of provisions, for example, on performance requirements, national treatment and fair and equitable treatment and are therefore fairly similar. Paul Haslam rightly argues that the range of variation across treaties that offer more regulatory flexibility and those that do not is rather narrow (2010, 1188-89). However, since the final text of IIAs is determined through negotiations between parties with different interests and preferences, it follows that IIAs will demonstrate slight variations across time and signatory partners. For example, some authors have observed that BITs preferred by the US, Japan and Canada

exhibit higher levels of investment protection than agreements signed by other countries. They include broader definitions of what constitutes FDI (i.e. expanding coverage to incorporate intellectual property), the inclusion of a ‘right to establishment’ for foreign investors, and, increased numbers of restricted performance requirements that may be imposed on investors (Haslam 2010, 1186; Peterson 2004, 3; UNCTAD 2007, 14). Although these variations may appear narrow, it does not follow that they are insignificant in practice.

Governments concerned with the increasing prevalence of investment disputes and the power allotted to firms in IIAs have also tried to clarify investor rights by including more precise definitions in new agreements and by amending existing IIAs. This helps avoid surprises concerning the interpretation of provisions by arbitration tribunals (Yu and Marshall 2008, 2). Steps have also been taken to limit investor protection, including increasing the transparency of arbitration processes and limiting the reach of ‘fair and equitable treatment’ to that stipulated by customary international law. Several recently concluded IIAs also recognize social and environmental policy objectives by referencing these goals in the agreement’s preamble (Spears 2010, 1044). Roberto Echandi (2007, 128) finds that investment disputes have influenced the refinement of provisions and the inclusion of procedural and substantive innovations in a new generation of IIAs signed by Asia Pacific countries. Such innovations include new transparency obligations to open ISDS proceedings to a greater degree to the public and efforts to clarify the definition of concepts such as “investment” and “national treatment” to avoid overly broad interpretations by arbitral tribunals in ISDS cases (2007, 134 – 135).

Only recently have there been efforts to explore what the variation in IIAs means for their varied impacts on investor-state disputes. Allee and Peinhardt (2014), for instance, explore the significance of the variation in the procedures IIAs set out for enforcing state obligations. IIAs specify whether signatory states agree to automatically submit future investor-state disputes to international arbitration (which speeds up the process) or whether the state must agree on the course of action and consent to the jurisdiction of a particular dispute-settlement body. The need to obtain such consent ex-post opens up space for governments to delay proceedings, for example through battles over jurisdiction. IIAs also specify different arbitration venues. In addition to domestic courts, more than a dozen international bodies can be specified as dispute-settlement options, including ad hoc arbitration using the United Nations Commission on International Trade Law (UNCITRAL) rules, standing bodies such as ICSID, the Permanent Court of Arbitration, or one of several regional bodies located in Cairo, Stockholm or elsewhere. They argue that while international bodies tend to be more institutionalized with a permanent staff and a strong enforcement system, local centres must rely heavily on states to formulate rules and collect awards. This can open or close governments' avenues of legal defence, stall tactics or resistance to the enforcement of awards, which in turn can have important repercussions for the ability of governments to defend policy space under IIAs.<sup>9</sup>

Calls to recognize and further explore the implications of the heterogeneity of IIAs are growing (Simmons 2014; Busse et al. 2010, 172). This will only become more

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<sup>9</sup> The authors attribute the variation in enforcement procedures to the bargaining power of capital-exporting states. Simply put, capital-exporting states desire stronger protections because of the preferences of their domestic actors and push for more stringent provisions while using their more powerful position as leverage.

important as consensus builds around the need to reform the global IIA regime to make the system work better for equitable and sustainable development. Legal studies scholars have contributed to the debate by examining more closely how specific IIA provisions and dispute settlement procedures intersect with the exercise of policy autonomy and opportunities for progressive reform (Wagner 2014-2015; Simma 2012; Hueckel 2012).

Van Harten (2008) and Vicien-Milburn and Andrevva (2000), for instance, explore how governments use the necessity defence to defend state actions taken in a time of crisis. The necessity defence refers to the provisions found in BITs and under international law, which explicitly exempt government action taken during times of crisis from full treaty coverage. Simma (2012), however, asserts that states must take on a more active role in defining investors' rights in the negotiation stages. For instances, states could incorporate clearer guidelines as to what constitutes 'legitimate expectations', a term included in all BITs that is often interpreted broadly by foreign investors during disputes as a means to demand compensation in situations of economic and political instability. Others stress the importance of limiting arbitrators' interpretative powers as a means to enhance the legitimacy of the current system. Hueckel (2012, 306-307) argues that treaty negotiators should look to draft rules and interpretive guidelines to control arbitration outcomes *ex ante* while establishing a 'review body' to monitor the tribunals and awards *ex post*. In doing so, she argues, states can exercise greater control over arbitral tribunals, limit unpredictable outcomes for both investors and states and improve the perceptions of legitimacy by providing a more transparent ISDS system. However Marie-Lys Jaime (2014) suggests that states should take a more active role in interpreting IIAs and filling the gaps during an ISDS proceeding using the legal venues allotted to

provide tribunals clear definitions of the provisions and key concepts. Such reforms and defence strategies, should they be implemented, may exacerbate the variation between IIAs and how they are enforced against states.

There also has not yet been an adequate analysis of the role of non-state actors in studies of policy space and IIAs more generally. This is problematic, as civil society and private-sector actors may compete to advance different interpretations of investment rules and help enforce or contest them. Chang (2006) observes that in the context of open capital markets, the ability of governments to pursue particular kinds of economic policy is constrained not only by formal arrangements but also by elements that buttress the authority of IIAs as approval mechanisms of ‘sound investment environments’. Facing the (real or imagined) threat of capital flight, most developing country governments adopt policies that they think (or are told) are necessary to compliment IIAs to attract foreign capital. This includes specific forms of macroeconomic policy, corporate taxation, labour law and environmental regulation. The international media, credit rating agencies, consulting firms, private-sector associations and other actors re-enforce investment rules and related policies by monitoring adherence to IIA commitments and creating negative discourses around those that break with them. Domestic interest groups may further limit policy space as they lobby in support of IIA commitments to promote policies favourable to their interests. Economists in developing countries who are ideologically committed to free market economics also often support the authority of trade and investment rules as the necessary tool of economic development and reinforce the legitimacy of such constraints.

Despite progress towards recognizing and understanding the nuances of the global IIA regime, there is a tendency in studies of policy space to assume that the constraints IIAs impose on state action are both inevitable and universal. This is because much of the literature on IIAs and policy space borrows from the structuralist logic found in early studies of global economic integration. This is problematic as it has led to significant gaps in our understanding of how IIAs and other global economic arrangements are experienced in reality. There is a need, therefore, to further explore what the variation between IIAs means for their impact on policy space and how different actors compete to exploit such variation.

## **2.4 Knowledge Gaps**

Failure to connect the (potential) impacts that IIAs have on the policy space with the responses they invoke at the domestic level means that we are only privileged to one side of a more complex story. That is, we have yet to understand how states and local actors (namely, civil society) defend policy space and to what degree they are effective. This, in turn, harms our understanding of how the global IIA regime and its impacts are shaped, moulded and negotiated through interaction with local actors and contexts. Recent effort has been made by some scholars to investigate the messy and somewhat contradictory nature of the global IIA regime, yet there is significant opportunity for further theoretical and empirical analysis. Most notably, there is a need to theorize and analyze how variation between IIAs and their uneven enforcement opens up space for contestation and resistance by domestic actors. Examining how state and non-state actors contest the impacts of IIAs in competition with those actors that seek to enforce them can also tell us more about how the enforcement of investment rules works in practice by

revealing the repercussions of going against investment rules and how they vary across space and time. This, in turn, can also help us overcome assumptions about the inevitability and universality of IIA impacts.

The failure to examine the consequences of signing on to IIAs in light of both power and resistance reflects a deeper gap within the literature on policy space. Despite the prevalent use of the term in both academic and policymaking circles, policy space is rarely defined and less often theorized. Failure to theorize what policy space is, who owns it and its links to domestic and international determinants has led to the prevalence of analytical blind spots. Thus far, studies privilege external factors as the primary unit(s) of analysis and as the sole determinants of countries' policy options while neglecting the numerous local factors that inform governments' decisions and abilities to break with international obligations (the 'constraints'). For example, the rise of what has been termed 'post-neoliberal' governments in Latin America has been connected with greater efforts to reassert state authority over the domestic economy. Yet the consequences of this post-neoliberal shift have not yet been fully brought into analyses of the relationship between policy space and the global economy. We know little about whether and how international economic rules and arrangements will constrain the emergence of post-neoliberal policy agendas.

Future research should focus on addressing the following questions:

- How do IIAs prevent the emergence of alternative development policies and strategies?

- How do states and non-state actors defend domestic interests from the constraints imposed by IIAs and to what degree are they effective? What determines governments' decisions and abilities to defend policy space?
- What gaps, spaces and contradictions exist within the international investment legal regime that makes domestic resistance possible?
- How are IIAs enforced in the face of contestation? What are the mechanisms through which IIAs impact policy space?

There is a need to interrogate the theoretical assumptions that underpin existing studies of the relationship between IIAs and policy space: What assumptions render invisible the role of state and non-state actor in this relationship and how do we grant such actors greater agency? This, in turn, requires rethinking how we understand the nature of policy space and the diversity within the global IIA regime. In the chapter that follows, I discuss in more detail the dominant theoretical approaches to the study of policy space and expose the assumptions that have contributed to the empirical gaps outlined above. I then propose an alternative way of thinking about and analysing policy space and the global IIA regime, one that is more attuned to the agency of domestic actors as well as the co-constitutive relationship between local and global forces. This, in turn, is necessary for nuancing our understanding of the diverse nature and risks of IIAs as well as the ways in which actors in the global South respond to them, often in creative ways.

### **3 Chapter: Policy Space and the Global Assemblage of Investment Law**

In this chapter, I set out a new and innovative theoretical framework for the study of policy space under IIAs, which aims to capture the interaction between investment rules, their enforcement agents and domestic actors. In doing so, I highlight the contingent power of IIAs and the constraints they impose on state action as well as their productive potential, that is, the ways in which the enforcement of investment rules produce changes in perception and state action at the domestic level. My intention is not to diminish the costs that arise when governments break with investment rules or to advocate for stronger enforcement mechanisms. Numerous scholars have demonstrated convincingly the dangers to public interests that can arise if IIAs are effectively enforced. Rather, my intention is to provide a more complex analytical lens that is sensitive to the role played by domestic actors during processes of enforcement. I do so by drawing attention to the co-constitutive and uneven links between global processes and local forces. I argue that to better capture the real impacts such processes have on political outcomes, we must focus our analytical effort on examining the middle messy ground between the domestic and global where policy space lies.

Much of the critical literature that explores the shrinking of policy space employs a structuralist approach in which the structure of global capitalism is viewed as imposing constraints on relatively weak states. Yet neglecting to recognize the role of domestic actors and contexts in helping to shape the outcomes of global arrangements such as investment agreements means we are privilege to only one dimension of a more complex story. Governments do not always abide by international and national legal obligations

nor do they sit idly by as investors bring suits upon them. Rather, governments use different tools and resources to defend national interests, such as policy space, in ways that are not captured by structuralist theories. Neglecting to explore the conditions under which governments break from investment rules has misled authors into assuming that the impacts of IIAs are both inevitable and consistent across time and space. The *real* impact that investment rules and other international obligations have on countries' policy space, however, lies in the middle messy ground between IIAs' potential impacts and the local responses they evoke be it contestation, acquiescence or negotiation. Centering analyses on the role of state and non-state actors in contesting investment rules can also tell us more about the way in which IIAs are enforced. That is, it draws further attention to the ways in which the impacts of IIAs are contingent upon the acceptance and support of domestic and international actors.

Capturing the middle messy ground between power and resistance means that we must interrogate our assumptions, on one hand, about the nature and influence of global processes and their relationship to local actors, and on the other, the relationship between governments and the various factors that influence state capacity and perceptions of policy space. It also requires that we rethink the way in which we understand policy space itself. Structuralist perspectives portray policy space as something acted upon by externalities operating at the scale of the global. Yet policy space is a social construct, rooted to the subjective beliefs and perceptions of policymakers who are situated in changing political contexts. It is therefore fluid, easily manipulated and dynamic. It exists at multiple scales of the political (local, national, international) and is influenced by the interaction of multiple forces operating at once.

I first explore the challenges and missed opportunities provided by structuralist approaches in the study of policy space. I then reconceptualize policy space as much more fluid, dynamic and multidimensional than has been previously recognized. Following this, I outline a vision of the state following Migdal (2001) and Mitchell (1999) that envisions the state as situated within and constituted by social networks and practices. This conceptualization of the state and state-society relations enables us to recognize and account for the multiple forces influencing policymakers' decisions over whether and what kinds of actions to pursue in the face of constraints from external forces (e.g. the potential impacts of IIAs). Finally, I theorize global-local linkages and reconceptualize the global IIA regime following the insights of social constructivist scholars. Most notably, I take inspiration from Anna Tsing (2005) and Ong and Collier (2005) in arguing that we must understand the global IIA regime as a messy, inconsistent and at time contradictory assemblage constituted by, and in some ways constitutive of, local forces. I argue that we must explore in greater detail how encounters between the global IIA assemblage and local forces make IIAs effective while also challenging their smooth functioning.

### **3.1 Structuralism and State Agency: The Globalisation Debate**

A rich body of scholarship has been dedicated to exploring the social, political and economic dimensions of globalization. Originally, scholars focused investigations on understanding the impetus for, and outcomes of, the widening and deepening variety of global economic and socio-political processes. These processes have blurred analytical lines between the domestic and international and complicated internal / external dichotomies. To early theorists, globalization was viewed as an “inevitable, a singular

process across different areas, eroding the boundaries of nation-states, welfare states, and societies” (Martell 2007, 182). National economies, political sovereignty, cultures and identity were seen as being subsumed by the rise of TNCs, international organizations and Western culture (see for example Ohmae 1995; Reich 1991). A totalizing picture of globalization emerged, centered on a view of the world as undergoing a gradual process of homogenization whereby states, institutions and corporations converged in the direction of an end state characterized by Western modernity (Taylor 2005, 1029). Whether this convergence was viewed as positive (e.g. as having equalizing effects) or negative (e.g. embedding power asymmetries) varied according to the analyst. Yet on either side of the normative spectrum, calls for an end to methodological nationalism prevailed in favour of more cosmopolitan and global perspectives (Martell 2007, 174; Schmitter 2009, 46)

These views were subsequently challenged by scholars who asserted that early analysts exaggerated the power of global and transnational forces (Hirst and Thompson 1996, Weiss 1998, Doremus 1998). Early ‘hyperglobalist’ perspectives were criticized as being too abstract and relying too heavily on thin empirical observations of select industrialized countries. These abstractions allowed hyperglobalists to make generalizing claims as if global processes had the same impacts on all areas of the world evenly and with the same responses. Later theorists instead sought to illustrate the continuity of state power as well as the survival of national identities, cultures and differences under global processes. Analysts also looked beyond the Western experience to determine “whether or not globalization is received evenly and with the same response everywhere and, not surprisingly, [scholars] found signs of differentiation in its spread” (Martell 2007, 175).

The global economy was seen not as inclusive but as encouraging or cementing wide disparities, for example, between the developed and developing worlds.

Much of the literature on globalization, as Hobson and Ramesh observe (2002,5), therefore came to reflect two dominant positions regarding the relationship between the state and global processes. In one camp were scholars working from a structuralist interpretation, who assert that globalisation and global non-state actors are, if not challenging the viability of state sovereignty, then at least forcing it to adopt policies that conform to its logic as the new global reality. This includes, for instance, scholars such as Camilleri and Falk (1992), Ohmae (1990), and Reich (1991). In the other camp, scholars take an ‘agent-centric’ approach, insisting that states have the power to mitigate and even shape global structures. However, both camps have been criticised as overly reductionist in their own right: “in privileging the global, structuralists necessarily ignore the autonomous impact of domestic and national forces, while agent-centrists do not sufficiently enquire as to how the state is embedded in the global” (Hobson and Ramesh 2002, 8). Moreover, as Larner and Le Heron (2002, 416) observe, there is a continued propensity in mainstream studies for theorizing to be done from ‘the core’ (global North), which are then taken as ‘the’ stories about globalization.

More recently scholars have sought to synthesize these perspectives by highlighting global-local intersections as well as the survival of local differentiation. Global forces are understood as having transformative impacts in local sites; however more attention is paid to how such impacts might be uneven and inconsistent across time and space (see for example Brenner 2010; Hobson and Ramesh 2002; Tsing 2006; Larner and Le Heron, 2002; McMichael 1996). Such analysts, that is, seek to explore national

economic, political and cultural forces as co-existing with and in ways co-constituting global processes and institutions. Global and local processes are viewed as operating simultaneously but also in constant interaction. Although emergent, this body of scholarship encompasses a diversity of approaches.

Hobson and Ramesh, for instance, advance what they call a ‘structurationist’ perspective. This perspective begins with two observations: “that states are purposeful agents that shape and determine the global system within which they reside and, conversely, that the global system shapes states. In short, states and globalisation are mutually reflexive and are embedded in, or are co-constitutive of, each other” (2002, 10). Global processes, they argue act both as a realm of constraint that defines the parameters to which states must adapt as well as a resource pool into which states dip to enhance their power or interests in external and internal arenas. States therefore are neither passive victims of global structures nor completely autonomous agents. However they also acknowledge that states are embedded in a range of social structures, which also act to constrain or enable state action.

This structurationist theory reflects Robert Putnam’s (1988) two-level game theory whereby states, in their negotiations with international partners balance between the demands of domestic interest groups and those of their international partners to achieve an optimal outcome. Underpinning Putnam’s approach, however, is the assumption that policymakers behave according to the same rationalist approach to international and domestic affairs. The implication is that policymakers facing the same global and domestic conditions would arrive at the same decisions. This raises the risk that the policy decisions of more peripheral countries will be assessed according to a

Western European standard of rationality while the cultural, historical and socio-political complexity of the environment in which policymakers exist is ignored.

As will be elaborated upon in a subsequent section, it is important to recognize the social bases that make certain state actions possible or improbable as Hobson and Ramesh acknowledge. However the authors fail to recognize the complexity of the state apparatus, its competing parts and its social relations. Instead, they view the state as a cohesive unit that exercises a high level of autonomous decision-making, which makes them capable of balancing domestic and international pressures to pursue an optimal outcome. This is problematic, as both Hobson and Ramesh and Putnam neglect the ways in which global and local forces interact and co-evolve, and the different ways in which such interaction can place competing pressures on different parts of the state apparatus.

Other scholars have preferred to highlight the socially constructed nature of globalisation to overcome the image of an independent global arena detached from local forces into which states 'dip' (McMichael 1996; Tsing 2005; Larner and Le Heron 2002). Larner and Le Heron (2002, 415) for instance argue for the need to move beyond tendencies to portray globalisation as either a "universal, disembodied, structural, macroprocess" or as an afterthought to nation-centered analyses. Instead, they argue, scholars should discuss globalisation in terms of globalising processes that need to be deconstructed to expose the dimensions and detail of how they are constituted and how, in turn, context is constituted through such processes. Adopting the metaphor of globalising economic processes, they argue,

breaks open this mega-narrative: instead we can emphasize the emergent, create room to give agency some space, acknowledge the participation may be fluid,

informed, motivated, intentional, aspirational, hint at the constructed nature of processes and new spaces and most importantly, begin to reinsert politics and policy and reset priorities.

Globalisation, along these lines, is envisioned not as a universal meta-structure but as a project or process of becoming; one that is constituted by, and experienced through, practices and discourses intersecting at multiple scales. The result is that globalization is recognized as a diverse set of processes with no particular ending or conclusion (Martell 2007, 177).

My aim in retelling this (overly) generalized account of globalization theory is not to support existing categorizations or to review the numerous contributions. There are ample disagreements over the similarities or differences between ‘waves’ of globalization theory and into which camp particular scholars belong. Instead, my objective is to highlight the movement toward more complex, nuanced accounts of global integration and the attempts to explore the productive friction between domestic and global processes. While many scholars have shed earlier assumptions about the inevitability and universality of global processes, studies of policy space continue to rely largely on the universal meta-narrative of global economic integration whereby international economic arrangements are envisioned as impositional, consistent and homogenous; an ever expanding network of economic rules that govern space and time evenly. From this view, external phenomena operating at the scale of the ‘global’ such as investment rules are understood as having almost inevitable and universal impacts on national policy space.

Gallagher (2005, 2), for example, argues that “existing and proposed rules for the global economy are restricting policy spaces for development in the nations that need development the most.” Robert Wade (2005, 80) similarly argues:

developing countries as a group are being increasingly tightly constrained in their national development strategies by proliferating regulations formulated and enforced by international organizations. These regulations are not about limiting companies’ options...they are about limiting the options of developing countries to constrain the options of companies operating within their borders.

The similarities found across contemporary IIAs in terms of their structure, purpose and principles have encouraged scholars to conceptualize the agreements as constituting a global legal regime (Haslam 2010; Cho and Dubash 2005; Cutler 2013; Salacuse 2010; Milner 2014). The term ‘regime’ is understood along the lines of international relations theory as a system of governance composed of principles, norms, rules and decision-making procedures that constrain and regularize the behaviour of participants (Salacuse 2010, 431). ISDS is, in turn, theorized as the enforcement mechanism through which foreign investors ensure such constraints are imposed. Moreover, because disputes are resolved outside of domestic legal systems, ISDS is argued to disable citizen-driven politics (see for example Schneiderman 2008). Claire Cutler (2013, 17), for instance, asserts that

[Investment agreements] set limits to state action in a number of areas of vital public concern, including the protection of human and labour rights, the environment, and sustainable development. They determine the distribution of power between foreign investors and host states and their societies. However, the

societies in which they operate seldom have any input into the terms or operation of these agreements.

Cutler later notes the participation of NGOs via *amicus curiae* submissions in ISDS cases, yet their inability to influence arbitrators' judgements leads her to conclude that citizens and domestic contexts have no role in shaping dispute outcomes.

While the regime perspective rightly acknowledges the power asymmetries that inform and are reproduced by investment treaties, it leads to a concomitant tendency to exaggerate the cohesiveness of investment agreements and the consistency with which investment rules are enforced. That is, theorizing ISDS as operating above domestic spaces renders invisible the intimate ways (and spaces) in which local actors engage with investment rules. This in, turn, encourages scholars to neglect how IIAs and other such arrangements are experienced differently across social, political and temporal contexts. As countries increasingly contest and fight back against perceived injustices in the global economy, the need to examine what impact this has on how global economic arrangements are experienced is now more important than ever.

As discussed in the previous chapter, structuralist assumptions have contributed to four blind spots in current understandings of the relationship between IIAs and policy space. First, the assumption that countries experience IIAs in the same way has led scholars to neglect how the impacts of such agreements are mediated, shaped and contested in their interactions with local contexts and actors. Governments can and do break with investment rules when domestic or political interests dictate. They also do not sit idly by as investors bring claims against them. Instead, they adopt different strategies aimed at defending domestic interests. Yet existing literature has not adequately

addressed the agency of domestic actors and what it means for the preservation or vitality of governments' policy space.

Second, in theorizing IIAs as representing a cohesive global phenomenon, little effort has been given to examining the gaps and contradictions inherent in the global IIA regime. This is a significant neglect as such gaps and contradictions can open up space for domestic resistance and contestation. Even slight variations between IIAs have the potential to open or close space for local resistance and alter how investor-state disputes play out. The global IIA regime also hosts several contradictions that create space for contestation. For example, the notion of state sovereignty both underpins and threatens the power of the global IIA regime. National governments sign on to international treaties as the sovereign representative of its constituents and are therefore held liable for infringements. However, states leverage their sovereign status to resist orders given by third-party international bodies. Assessing what gaps exist and how actors exploit them is vital to understanding how state and non-state actors defend domestic interests under IIAs and, in turn, the different ways in which countries experience IIAs.

Third, assumptions about the inevitability of IIA impacts has encouraged analysts to neglect how IIAs are enforced in the absence of an overarching international authority capable of superseding state sovereignty. Though international arbitral tribunals decide when a government is in breach of IIA obligations, they lack the ability to enforce the awards without the consent and cooperation of the state involved. Instead, the enforcement of IIAs depends on a disaggregated network of domestic and international actors using economic and political pressures to ensure governments adhere to investment

rules. This means that IIAs are likely to be enforced differently across space and time as different actors with interests in enforcing investment rules come in and out of the fold. By ignoring the complex and geographically dispersed network of actors and processes buttressing the authority of investment rules, authors have failed to capture what grants IIAs agency and effect over governments' decision-making and in turn, the policy space government officials perceive available.

Lastly, the top-down perspective pervasive in studies of policy space ignores the importance of (global and local) contexts. Foreign investors, legal regimes and governments are responsive to some degree to the environment in which they are situated. IIAs can be amended, cancelled or replaced according to signatories' decisions, decisions that are influenced by various factors including societal pressure and domestic economic performance. IIAs themselves also coexist and clash with a dense and evolving normative environment at various scales. A government's obligations to foreign investors can conflict with its obligations to citizens under human rights law or environmental accords. Civil society actors can use the spaces opened up by conflicts between human rights law versus states' obligations to foreign investors to advance arguments against investor claims in the defence of state action. This also helps illustrate the importance of envisioning IIAs and the global IIA regime not as static and existing in isolation, but as evolving (or decaying) institutions in dynamic interaction with its surroundings.

Understanding how IIAs impact policy space in real terms requires moving away from universalisms and toward a more nuanced approach. It also requires exposing the mechanisms by which IIAs impact policy space in practice. The actual impacts that IIAs and other forms of global economic integration have on policy space lies between the

potential constraints such agreements may impose under favourable conditions and the local responses to these constraints. As previously argued, local contestation will in turn depend on a variety of sociopolitical and economic factors. That governments and subnational actors are capable of combating such constraints has been ignored extensively within the literature. Bringing to light local agency in the exercise and defence of policy space requires adopting a theoretical approach that is attuned to the gaps and contradictions in the global IIA regime that make such resistance and contestation possible. This, in turn requires a more dynamic and fluid understanding of policy space and its relations to forces operating at multiple scales.

### **3.2 Rethinking Policy Space and the Global/Local Nexus**

Few authors have sought to theorize policy space as an object of analysis. This is a missed opportunity, as defining what policy space is, who owns it, and how it is shaped will have important analytical implications. As discussed in the previous chapter, scholars have defined policy space in various yet complementary ways. Yu and Marshall (2008, 14) and Gallagher (2006, 63) envision policy space as the flexibility or freedom governments possess under existing national and international rules to deploy policies needed to address the needs of their citizens. Romson (2012, 34), however, defines policy space as both the “room to manoeuvre” in policymaking as well as the resources needed to implement chosen policies.

In all cases, the capacity of governments to pursue policy is held as subordinate to governments’ obligations under national and international law. As Abugattas and Paus (2008,123) assert, “[policies] have to be conceptualized within the realm of possibilities,

recognizing the degrees of freedom that countries effectively have to implement policies within existing international and domestic constraints.” Yet in defining the parameters of existent policy space according to established international and national rules, analysts presuppose that policy space is already in some ways constrained. That is, there is an underlying assumption that the rules established at national and international scales effectively constrain state action.

The proliferation of international rules and norms on the environment, human rights and warfare means that states exist within a dense normative environment aimed at inciting certain forms of behaviour. Yet, the existence of such rules does not mean that states abide by them. Governments can and do adopt extra-legal policies despite conflicts with national and international obligations. The principle of state sovereignty, for example, helps guarantee governments a degree of freedom in their decision-making with respect to which international rules and incentives they follow. In this way, state actors themselves are primary determinants of national policy space in that they choose when and how to break with legal obligations. Although, breaking with international legal obligations, such as investment rules, may come at a significant cost.

Unlike Gallagher and Yu and Marshall, I do not give primacy to governments’ existing legal obligations as parameters of available policy space. Instead, I recognize and seek to understand why government resort to extra-legal policy options despite national and international obligations. I therefore define policy space as the range of policy options policymakers perceive available, the perceptions of which are structured by competing material, ideational and sociopolitical forces operating at multiple scales. By ideational factors I refer to policymakers’ perceptions about what policy options are

politically feasible and necessary given prevailing conditions. Such perceptions are shaped by policymakers' core / normative beliefs (e.g. political ideology) as well as the more malleable framing processes (or causal beliefs) that shape actors' understandings of the world around them (Béland 2009; Campbell 2004; Schmidt 2008). Both 'kinds' of ideas can evolve over time, however causal ideas evolve most rapidly depending on the actors' interactions and experiences with multiple (and sometimes competing) factors such as non-state actors, institutions and environmental conditions. With respect to perceptions of policy space, relevant factors, for example, may include material resources and trends (e.g. government revenue and declining economic performance), social mobilization (e.g. in the form of protests in demand of state action against a foreign investor), past experiences with (and knowledge of) legal structures (and their gaps) and private-sector lobby groups.

Daniel Béland (2009, 702) argues that ideas and ideational processes have relevance to policymaking in a variety of ways. First, ideas help construct the problems and issues that enter the policy agenda. Ideas about what are the most urgent issues of the day help actors to narrow down the list of issues on the policy agenda. Scholars of policy learning find that policymakers change beliefs as a result of observing and interpreting experiences, which lead to corresponding policy changes (Levy 1994; Poulsen and Aisbett 2013). As an issue comes to the fore of the policy agenda, the importance policymakers assign to it might outweigh or conflict with the significance assigned to meeting international legal obligations. It is important to note, however, that some international legal obligations (e.g. trade and investment rules) may possess more coercive power than others (e.g. international human rights law) since powerful global

actors have a large stake in their enforcement. This is particularly true when there is disconnect or conflict between the philosophy underlying the international rules (i.e. the neoliberal economic philosophy underpinning contemporary IIAs) and policymakers' normative beliefs. In a similar way, prior experience in managing investment disputes can increase policymakers' knowledge of the legal strategies and gaps they can exploit to defend domestic interests in the face of an investor claim, with important impacts on the policies adopted towards investment disputes.

Béland (2009, 702) also claims that ideational processes shape the assumptions that impact the content of reform proposals – or solutions to the policy problem. That is, ideas can take the form of assumptions that legitimize or challenge existing institutions and policies. Referencing the work of Peter Hall (1993), Béland argues that assumptions underlying prominent policy paradigms, such as neoliberalism, provide a framework of ideas and standards that specify policy goals, the instruments that can be used to attain them, and the very nature of the problems in need of addressing. Such paradigms, therefore serve to “guide learning processes through which existing policy legacies are evaluated and criticized” (2009, 705). Yet the assumptions underlying policy paradigms change over time, particularly in periods of high uncertainty when actors may turn to alternative ideas to solve new problems they face. For instance, governments more strongly influenced by neoliberal philosophy may be more likely to favour reform proposals that call for the further liberalization of domestic investment markets. For left-leaning governments, such as the Correa government in Ecuador and Morales administration in Bolivia, the more successful reform proposals have been those which call for a withdrawal from the global IIA regime. Policymakers' ideological

commitments therefore play an important role in shaping the extent to which investment rules hold legitimacy and authority over domestic decision making.

Finally, Béland (2009, 702) argues that ideas can become discursive weapons that participate in the construction of reform imperatives (or policy alternatives). Ideas, he argues echoing Blyth (2001, 4) can be used as powerful ideological weapons that allow actors to challenge prevailing arrangements and are often wielded through public discourse and framing processes that serve to convince policymakers, the public or particular groups that change is necessary. However, specific ideas only became a decisive factor under favourable institutional and political conditions. Strong institutional obstacles, Béland observes, can weaken the capacity of political actors to successfully promote policy alternatives (2009, 702). It therefore becomes important to examine how policymakers wield ideas in ways that generate support for a particular position on investment rules and throughout investment disputes.

By material resources, I refer to two dimensions of ‘materialism’: first, to both the administrative and financial capital needed to institute governments’ policy choices. These material resources should not be understood as fixed or static, but as fluctuating according to shifts in the domestic and global political economies. The second dimension of materialism to which I refer is the physical environment in which policymakers are situated. Here, I take inspiration from actor-network theory (ANT) in granting recognizing the role non-human physical objects have in structuring policymakers’ understandings and behaviour. Unlike more traditional materialist approaches, such as historical materialism which aims to expose the political repercussions of shifts in the production and structure of capital, ANT aims to expose the agency of a diverse range of

non-human objects from texts to stop signs and heavy machinery as they interact with other actants in ways that shape human behaviour.

More specifically, ANT seeks to explore the processes through which non-human actants gain agency through local practices and networks in which they are entangled (Latour and Woolgar 1979; Law 1986; Latour 1987, 2004; Callon 1986, 1991). Physical objects engage with disaggregated networks of human and non-humans through processes of *translation* and *enrollment*. Translation refers to the modification of action as it moves from one (human or non-human) actant to another. Latour's speed bump metaphor is perhaps the most famous example. A speed bump, Latour (2009) argues, has a greater effect in causing one to slow down than a verbal warning or sign cautioning one to drive slowly. Yet it only acts when brought into interaction with another – in this case, the vehicle travelling down the road and the human in charge of it. The process of bringing together or enlarging a network of actants into a programme of governance which grants actants in the network force and effect (or authority and legitimacy) is referred to by ANT theorists as *enrollment*. Yet IIAs are not intrusive objects that demand engagement as directly as a roadblock does when it is encountered by automobile drivers. IIAs are more abstract in nature and occupy the less concrete domain of the global. As is discussed in the next sub-section, the capacity of IIAs to act therefore depends on their ability to enrol a more complex and geographically dispersed network of actors with whom they can engage.

As networks expand their relations of power become reinforced, often to the point where the foundational controversies of particular actants (the means and processes whereby they were created), including IIAs, can be forgotten. This occurs as the presence

of the actant becomes internalized by others as a natural or necessary occurrence. This process ANT theorists refer to as 'black boxing'. As is discussed in chapter four, the construction of contemporary international investment law was not without contestation and controversy; however the politics of this process has been reduced to a significant extent by the economic and legal discourses that rendered IIAs as necessary legal interventions.

It is important to note that the engagement between various actants within a network can be empowering or compromising. That is, the agency of physical objects depends on their ability to enrol other human and non-human actants and ideas (i.e. knowledges and expertise) into its network and power relations. Yet this enrolment can be interrupted at various points, for instance, by external events or contestation. From this perspective, the power IIAs exert over domestic political processes is not a given, but is instead contingent on the cooperation and interaction of the multiple components in its network of power.

According to ANT then, both the distinctive properties of objects as well as the connections they establish must be analyzed to fully comprehend their significance. As Tony Porter observes (2012, 537), by shedding light on the role physical objects play in uniting transnational networks, ANT approaches have the ability to demonstrate how objects "alter how larger global forces are or are not transmitted, modified, or resisted." However, he cautions, ANT scholars often ignore or devalue the unique properties of human cognition; that is, their causal ideas and normative beliefs and how this impacts the way in which they engage with non-human actants. This is despite the need to

recognize that human actants hold unique values, beliefs and causal understandings and therefore may not engage with other actants in the same manner.

Here, IIAs are an illustrative example. From a purely constructivist perspective, IIAs can be seen as simply codifications of shared understandings that exert normative influence over states. Yet this tells us little about how the norms embedded in IIAs exert such influence and how they are translated into practice. On their own, IIAs have no inherent agency but instead draw on a specific network of actors, institutions and knowledges to retain their legitimacy and authority as a governance mechanism. Most importantly are the legal experts and expertise, foreign investors and arbitral institutions, which aim to grant IIAs authority over state decision-making. Yet IIAs also shape and are shaped through interaction in this network. Their broadly and ambiguously worded provisions often become embroiled in controversies of translation as host state and foreign investors seek to advance interpretations most favourable to their interests. Given that arbitrators are not strictly held to the jurisprudence set by past tribunal decisions, they also may translate investment rules differently. This is where the unique physical properties of IIAs have significance: the absence or presence of certain words can have an important impact on which interpretation is advanced and therefore who wins out.

In conceptualizing policy space as determined by both ideational and material factors, the potential impacts of IIAs and other economic arrangements on policy space become multifaceted. First, IIAs can have an ideational influence over policy makers' decisions with respect to what kind(s) of policy are appropriate for a given economic context (e.g. the idea that IIAs promote inward foreign investment) and / or what kind of policies can be pursued without costly reprisals from domestic interests groups or the

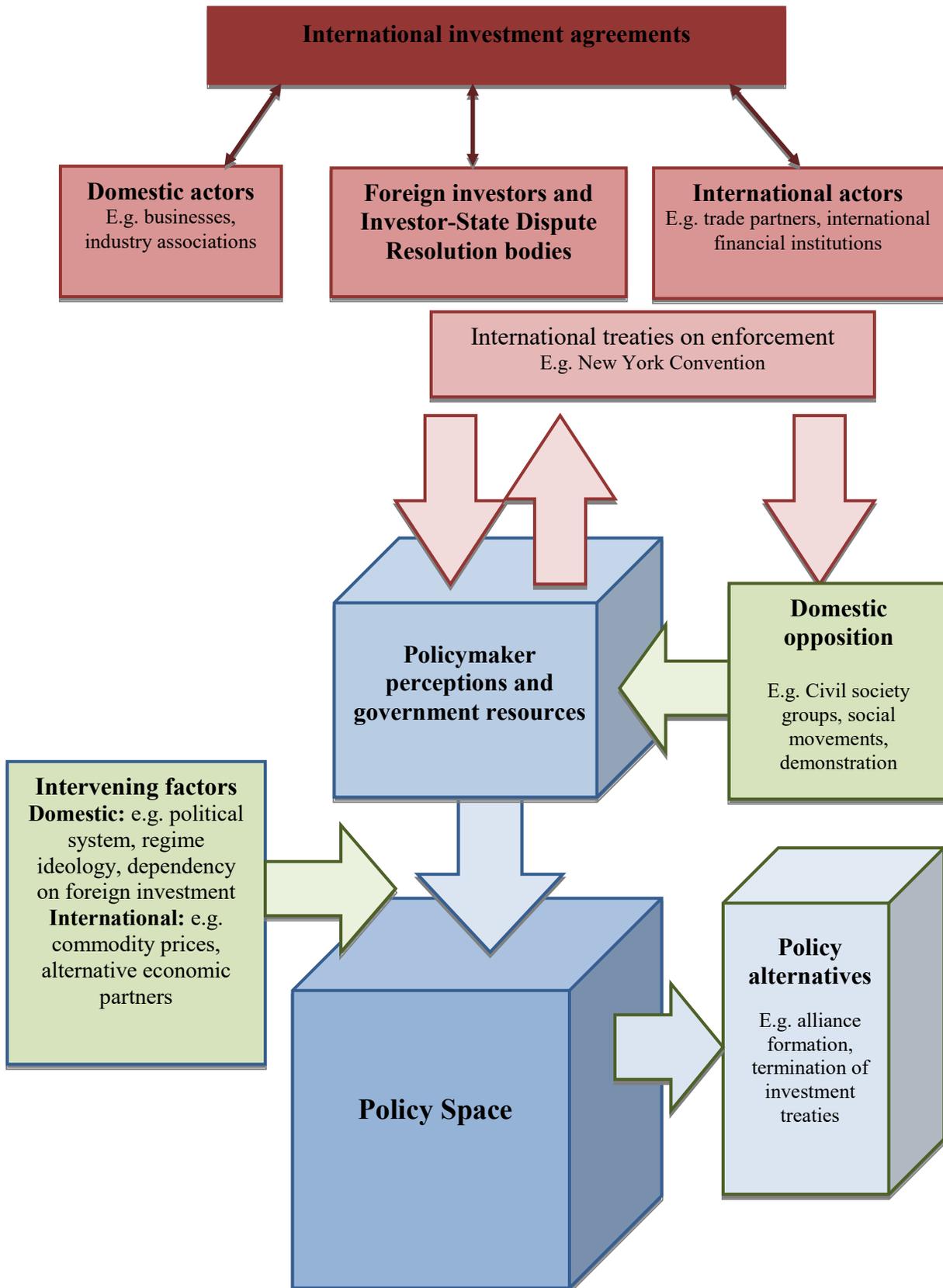
international community. For example, foreign investors often threaten governments with protracted and expensive legal battles should governments go against their IIA obligations. This, in turn, can deter policymakers' from adopting a specific policy or line of action. As will be discussed, a network of institutions has been established to support the enforcement of investment rules and discipline governments should they break from IIA obligations. The (real or imagined) threat of such discipline can impact policymaker perceptions about what policies are necessary or politically feasible. Domestic interest groups, such as chambers of commerce or private-sector associations can also seek to influence policymaker perceptions about the importance of adhering to investment rules through lobbying and threatening to withdraw political support.

Secondly, IIAs can constrain policy implementation by providing investors the means to sue governments for compensation after the policy has been chosen. This can negatively impact the resources available to governments to fund policies and programs. For example, this can occur when governments redirect revenue towards funding legal defences, to compensate investors or when economic sanctions are imposed by economic partners and aid donors on countries for digressions from investment rules. This, in turn, has an impact on governments' abilities to pursue future policy goals. This means that IIAs can theoretically constrain policy space by influencing ideational and material dimensions at both the policymaking and implementation stages.

The ideational and material dimensions of policy space, however, are structured by multiple factors in addition to international rules. For example, social mobilization against a foreign investor or an economic crisis can push the government to adopt measures that break from investment rules out of perceived necessity. Furthermore,

access to natural resources and large domestic markets help reduce countries' dependencies on external sources of wealth, which can counter international pressures on governments to abide by the rules of particular economic arrangements. Alternatively, a fall in commodity prices in an economy dependent upon the exploitation of natural resources can reduce governments' policy space by increasing dependencies on foreign capital. In more positivist terms, such factors could be understood as the 'intervening variables' in that they alter decision makers' cost-benefit analyses and perceptions about what policy options are desirable (see Figure 1). These aspects point to the importance of conceptualizing policy space as both fluid and multidimensional.

**Figure 1: Policy Space and International Investment Agreements**



Yet this raises a number of methodological challenges. The various elements that structure the material and ideational dimensions of policy space complicate efforts to isolate the impact of any individual constraint, such as IIAs. This makes it particularly difficult to assess empirically whether and how IIAs induce policy chills. How can an analyst decipher whether a government would introduce a policy in the absence of a particular IIA if the country is already a signatory to several of the agreements or is ideologically committed to the principles contained in the agreements? The logic and authority of investment rules, moreover, can be deeply internalized and not an evident factor in decision-making processes. Lastly, a researcher must not assume that policy-makers are using the full extent of the policy space available to them. It is difficult to visualize (even hypothetically) the boundaries of a governments' policy space as it is only ever visible or understood when a government is constrained or blocked in its ability to exercise it. A nuanced analysis that is attuned to the intersections of multiple variables and how investment rules and their enforcement mechanisms shape public and political debates over what policies to take is essential to this investigation.

To truly understand the ways in which domestic policy space is fluid, multidimensional and multiscalar, we must theorize the nature of the state and its relations to the rest of society and global forces. This will help us understand how the state negotiates and mediates between competing influences. Similarly, it is also necessary to interrogate the nature of global economic forces and their linkages to local actors and contexts. This will help nuance our understanding of such arrangements in a way that provides greater recognition to the agency of local actors.

### **3.3 The State in Society and the Spatiality of Policy Space(s)**

As an analytical concept 'the state' is rather ambiguous. Most social science disciplines have experienced the ebb and flow of recurrent debates on the state. Its parameters and qualities as well as the nature of its relations with the rest of society have been particular points of disagreement amongst theorists. The term's lack of conceptual clarity has been compounded by the increasing breadth and complexity of global (economic, political and social) integration, which further blurs theoretical demarcations between different scales of the political (local, national, international). It is not possible to explore all such debates in their richness and many of these debates stretch beyond the scope of this paper. However, since policy space is seen as something possessed by the state and is in some ways defined by it, it is necessary to set out theoretically what the state is, who defines its priorities, and who and what grants it capacity and legitimacy.

As Theda Skocpol (1985) observed in the introduction of the seminal work *Bringing the State Back In*, the prominent pluralist, structure-functionalist and neo-marxist theories that dominated studies of political life in the post-war era placed emphasis on society-centered ways of explaining politics and government action. The government, from these perspectives, was treated primarily as an arena within which economic interest groups, classes or social movements contended to shape public policymaking. Policy decisions were understood to be (asymmetrical) allocations of benefits among competing social groups. Yet such perspectives were limited. Analysts found such theories unable to account for initiatives government leaders took beyond the demands of social groups. Growing awareness of such limitations generated interest in bringing the state back to the centre of analyses. Comparativists therefore began

revisiting Weberian understandings of the state as a compulsory organization with control over a given territory and its population; an organization composed of interrelated administrative, legal, bureaucratic and coercive systems that aimed not only to govern state-society relations but also much of society itself. By the end of the 1980s, the 'state' came to be treated more seriously as an autonomous, institutional and social actor that is qualitatively distinct from the rest of society with its own principles and interests (Skocpol, Evans and Rueschemeyer 1985; Evans 1995). States' outward-looking orientations, the challenges of maintaining domestic order and the organizational resources available were features of the state that helped to explain autonomous state action (Skocpol 1985, 9).

Building on this position, Peter Evans (1995) aimed to account for the state's role in economic transformation. More specifically, he aimed to explain the particular qualities of the state and state-society relations that contributed to the success of some newly industrialized countries and their ability to support a range of industrial production. Such qualities are endemic of what is now termed the 'developmentalist state'. Popular debate around whether the state should be interventionist versus non-interventionist, he argues, focuses too much analytical attention on degrees of ideal-typical competitive markets. The issue was not whether states were interventionist versus non-interventionist (the 'how much') as state involvement in development was seen as a given. The more appropriate question is 'what kind' of intervention facilitated economic progress. Variations in state involvement, he argues, depend on variations in the states' internal structures and their relations to society. Different structures create different capacities for

action and define the range of roles the state is capable of playing. Success is dependent, in this case, on whether the roles fit the context and how well the roles are executed.

To Evans, a successful developmental state is one that approximates the institutionalized bureaucracy envisioned in the Weberian ideal type. Bureaucratic recruitment based on merit and the establishment of long-term career rewards would create a sense of corporate coherence amongst government members. This kind of corporate coherence is what lends the government a kind of autonomy. Yet the state is not insulated from society as Weber claimed it should be. Instead, “[policymakers] are embedded in a concrete set of social ties that binds the state to society and provides institutionalized channels for the continual negotiation and renegotiation of goals and policies” (1995, 12). A state apparatus fully autonomous from society would lack vital sources of intelligence and the networks needed to transcend private interests and promote the private implementation of collective goals. This combination of institutional coherence and connectedness Evans calls ‘embedded autonomy’ (1995, 12). Embedded autonomy, he argues, provides the basis for successful state involvement in economic transformation.

The image of the state as being institutionally cohesive with varying degrees of autonomy has been a powerful referent in mainstream approaches, both in development (structuralism, statism) and international relations theory (neorealism and rational choice theory). Yet, as critical scholars have helped illustrate, this image exaggerates the homogeneity of the state structure and ignores the fragmented and competing nature of its parts. Joel Migdal (1996) argues that using Weber’s definition of the state as uniform and constant as a starting point entails conceptualizing and measuring variation in state

structures as a distance from the ideal type. The variation and failure of states can therefore only be expressed in terms of deviation from a narrowly defined Western European standard. That is, rather than observing how things really worked, analysts focused their attention on assessing the state and its relations as an approximation to a normative model. The image of the state as a single, coherent institution marginalized the complexity of negotiations, interactions and resistances that occur in every society among multiple systems of rules and (parts of) institutions. Such an approach, furthermore, provided no means of theorizing the spheres of competing, overlapping sets of rules other than in terms of failure or weaknesses in the state's hold over society.

As an alternative, Migdal (2001, 16) offers the state-in-society approach. From this approach, the state is envisioned as,

a field of power marked by the use and threat of violence and shaped by [as well as projecting] (1) the image of a coherent, controlling organization in a territory, which is a representation of the people bounded by that territory, and (2) the actual practices of its multiple parts.

A state, Migdal observes, is perceived by those inside and outside its claimed territory as the dominant and legitimate rule maker within its geographic boundaries. Such a perception is based on an image of the state as a fairly unified, centralized and homogenous entity (or at least with fully integrated parts). This image, in turn erects two sorts of boundaries: one being the socially constructed territorial boundaries which designate specific spaces of control by different states; and the other being the social boundaries between the state (public actors and agencies) and the rest of society. Yet these boundaries are complementary: the image of territorial borders is complemented by

the notion that ‘the state’ somehow embodies the people(s) inside its lines. The ‘state’ therefore is taken as the primary and legitimate representative of its people in international circles and territorial boundaries then both delimit state control but also circumscribe it to a connected people. Moreover, the perceived boundaries between state and society (private and non-state actors) establish and reinforce the separation of public and private spheres. It is this image of the state that has served as the foundation of contemporary international institutions, including IIAs.

Inspired by Foucault’s insights on governmentality, Migdal argues that the image of the state as cohesive, or what Timothy Mitchell (1999) called the “state abstraction”,<sup>10</sup> is established, reinforced and at times threatened by the routine performance of state actors and agencies. Their practices may buttress the notion of territorial and public-private boundaries or neutralize them. For example, endless numbers of practices including visas, passports, barbed wire and electronic fences help fortify the authority of the territorial markers on maps as designating a particular state. Yet such practices often fail and can instead draw our attention to the porous or constructed nature of state borders. Migdal intends for us to move beyond privileging the laws and codes of the (imagined) state in question and prompts us to explore the often conflicting standards expressed in the practices of its parts. With this lens, what we might label as nepotism and corruption can also be looked at as a specific exercise in morality, which favours kinship ties over meritocracy (2001, 19). From the same, more expansive normative lens, a state’s

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<sup>10</sup> Timothy Mitchell (1999) argues that rather than a self-contained entity, the state is better understood as the effect of a series of techniques that enable mundane, material practices to take on the appearance of an abstract, immaterial form. The state, from this lens, is socially constituted and therefore, in reality, entirely indistinguishable from society except in its abstract form. Mitchell calls for greater recognition of porous boundary between state and society “not as a problem of conceptual precision but as a clue to the nature of the phenomenon” (1999, 77).

derivation from its obligations under IIAs may be seen not as a violation of prevailing standards regarding the treatment of foreign investors but as an attempt by state officials to protect the interest of a particular social group according to citizen demands.

Migdal also opens our eyes to the fragmented nature of the state. He calls on us to study the ways in which such parts ally and conflict with each other and with groups outside the state to further individual and collective goals. Such alliances and practices promote diverse sets of rules that are often distinct from the state's own official laws and regulations. They also serve to neutralize the territorial and social boundaries that render an image of the state as existing separate and above the rest of society. Migdal uses the concept of 'field' following Bourdieu as a descriptor of the state to encompass both image and practices. The 'field,' according to Migdal's interpretation, highlights relationships in a multidimensional space in which the symbolic element (the image) is as important as the material (practices): "in describing the state as a field of power, I want to emphasize what Bourdieu calls the 'multi-dimensional space of positions,' using the word 'power' to denote the struggles over who dominates" (1995, 22).

Understanding the state in this way is important for recognizing the spatiality of policy *space*. If states can be described as a field of power, with its multiple parts in alliance or contest with groups inside and outside the state, then policy space itself is also comprised of the diverse spaces in which negotiations between state actors and social groups take place. These negotiations, and the demands different groups place on parts of the state apparatus, can have important impacts on policymakers' perceptions regarding the policy options that are available and politically feasible should policymakers seek to stay in power, particularly in a democratic setting.

Using Migdal's theory of the state entails two levels of analysis and two paradoxical qualities of the state apparatus: one that recognizes the unified, coherent dimension of the state (in the same way that neo-statists advocate); and one that dismantles this 'wholeness' in favour of examining the contradictory and reinforcing practices and alliances of its disparate parts.

It must be thought of at once (1) as the powerful image of a clearly bounded, unified organization that can be spoken of in singular terms...(2) as the practices of a heap of loosely connected parts or fragments, frequently with ill-defined boundaries between them and other groupings inside and outside the official state borders and often promoting conflicting sets of rules with one another and with the 'official' Law (1995, 23).

In the same way, understanding the state's role and actions under IIAs and in investor-state disputes entails a similar two-level analysis. On one hand, IIAs depend upon and reproduce the image of the state as a cohesive unit. It is the state that is held accountable for infringements to investor rights, even if such infringements were caused by subnational-governments and domestic social groups. It is also the 'state' that defends domestic interests in ISDS proceedings. One dimension of the analysis should therefore focus on examining how state actors leverage the image of the state, for example by evoking rights granted to it under international law (e.g. the principle of state sovereignty), to contest the imposition of constraints on state autonomy. On the other hand, envisioning the state as constituted by multiple, competing parts enables us to focus attention on the unique relationships between its various parts and different social groups at multiple scales. It also allows us to recognize how such relationships change over time.

For example, the election of post-neoliberal governments in Latin America has come with renewed attempts to create productive relationships with different sectors of civil society. Acknowledging the intimate interactions between state actors and different social groups is essential for understanding the different ways in which perceptions of policy space might also evolve over time.

In recognizing the possibility that states would act in ways that were independent of the interests of influential social groups, neo-statists lent greater complexity to our analyses of state action. With his notion of embedded autonomy, Evans also helped draw our attention to the specific ways in which state capacity depends on the state's ability to create and leverage networks with society to achieve particular aims. Yet in relying too readily on Weberian definitions of the state, neo-statists both exaggerated the homogeneity of the state apparatus and established a normative model based on Western-European experiences with which to evaluate state performance elsewhere. In doing so, such authors glossed over the complexity and reality of state-society relations, the various practices and discourses that rendered the state intelligible as a single unit as well as the different forms and motivations behind the actions that states take.

Envisioning the 'state' as composed of fragmented and at times competing parts draws our analytical efforts toward exploring the plurality of goals pursued within the state as well as the diversity of state-society networks without prior normative assumptions. It also draws our attention not only to the networks on which state authority and capacity depend, but also to the everyday practices and negotiations that occur inside the state. From this view, there are multiple channels through which social actors can influence government decision-making and different parts of the state apparatus can react

differently. Government priorities and policy decisions are determined via agreement and/or negotiation between its various parts, each of which can be influenced by its relations and networks with diverse social groups. As will be discussed below, various parts of the state apparatus may also adopt different logics, which support national or internationally-oriented goals. State capacity is dependent on the networks it is able to establish with the rest of society as well as its ability to achieve internal consensus on policy decisions. State capacity is then expressed just as much as it is reinforced through practices and images. Understanding state action and inaction, then, entails that we consider contending forces inside the state apparatus and their varied networks with the rest of society and the global environment.

#### **3.4 Bridging the Global and Local: Investment Rules and Domestic Agency**

Economic and political geographers have contributed widely to the study of the global, particularly in their deployment of concept of scale (understood here as the socially constructed hierarchical ordering of space) and their critical examination of the spatiality of global forms (Yueng 2003, Sassen 2007). As Sassen (2007, 7) observes, the strength of social geographers in globalization studies has been the recognition of the historicity of scales and their resistance to the reification and naturalization of the national scale, a scale favoured by mainstream scholars of international relations. Global processes and institutions as well as the increasing interconnectedness of societies and political and economic systems challenge the applicability of state-centric approaches to social inquiry in contemporary times. Yet scholars such as Brenner (1999) and Yueng (2003) remind us, this does not necessitate a denial of the state's continued relevance as a major locus of power, but rather "a rethinking of the meaning of both state territoriality

and political space in an era of intensified globalization” (Brenner 1999, 41). Efforts within social geography to theorize relationships between scale, the state and global forms also provide a valuable framework within which to explore the tactics and strategies of actors systematically as we examine struggles between global and local forces (McCarthy 2005).

For example, Brenner (1999) advances a multidimensional and spatial conception of globalization. Globalization, in his view, is a dialectical process through which the movement of commodities, capital, people, images and information through geographical space is continually expanded and accelerated. This, he argues is dependent upon relatively fixed and immobile socioterritorial infrastructures that are produced, reconfigured, and transformed to enable such expanded, accelerated movement. Envisioning globalization in this way enables scholars to explore how global forms are constituted, transcend and operate at multiple physical and political (national, subnational, local) scales. It also draws our attention to the ways in which global processes remain grounded and rooted in specific socioterritorial contexts.

Anthropologists, on the other hand, alert us to the risks of an exclusively scalar approach that ignores the complexity of situated contexts through studies of global and particularistic forces that constitute inter- and intra-scalar dynamics. Ethnographers particularly tend to be attuned to the practicality of global forms and global-local encounters. In her work *Friction: An Ethnography of Global Connections*, Anna Tsing (2005) problematizes the concept of ‘global universals’ and instead seeks to expose how global forms are constituted by – and constitute – sociopolitical processes at multiple scales. Universals, Tsing argues, are always an aspiration in constant negotiation with

local contexts. That is, seemingly totalizing global processes depend on connections with locals in order to function, yet they are also shaped and limited by these very connections. Tsing develops the concept of friction to describe “the awkward, unequal, unstable and creative qualities of [global-local] interconnection across difference (2005, 4). In Tsing’s view, the ‘global’ is charged through local connections just as a wheel requires a surface in order to spin. Put in other terms, the universal becomes effective only within the context of particular historical conjunctures that give the universal both content and force. Friction is what occurs during the messy encounters between seemingly global forms and local contexts – when the tire hits the tarmac. Though global forms aspire to be universal they do not make everything everywhere the same. Instead, global forms are in constant interaction and co-evolving with the local. These interactions come to define movement, cultural form and agency at multiple scales, the effects of which can be compromising or empowering for the actors, processes, practices or ideas involved.

This dialectical view of global-local connections is useful for understanding how variation persists under global forms and for drawing attention to the significant of exploring the ‘friction’ of such encounters. As global processes weave their way over and through local sites, the local is shaped and responds in often unpredictable ways. These subtle transformations at the local scale either buttress the strength of global forms or threaten their existence and smooth delivery. This in turn helps account for how seemingly inevitable, totalizing global forms change, evolve and breakdown, however slowly, across time and space. As Tsing (2005) recognizes, it is now more common for scholars to accept the idea that marginalized groups accommodate themselves in different ways to global forces. Yet to argue global forces are in themselves congeries of

interactions with localities has been more challenging. She exemplifies these points with a brief, yet illustrative discussion of capitalism as a 'universal'. Capitalism, Tsing argues, spreads as producers, distributors, and consumers strive to make universal categories of capital, money and commodity fetishism. It is through these efforts that capitalism takes on its global form. Despite the seemingly universal nature of commodity chains, capital mobility and other evidence of its reach, capitalism is exposed as consisting of numerous uneven and awkward links. Each chink in the commodity chain is geographically situated and connected by microprocesses. Capitalist forms (the aspiring universal), then, vary across distance as they adopt a cultural specificity gained through the friction of worldly encounters with the particular. The messiness of these encounters is why the expansion of capitalism has been violent, chaotic and divisive rather than smooth and all-consuming.

If we ascribe to Tsing's worldview we are to surrender the totalizing portraits of global forms. The alternative she proposes encourages us to explore not only the dynamism of global-local connections, but also how such connections can create the abstraction and appearance of universals. Tsing also alerts us to the significance of local sites for the study of global processes and practices. To Tsing, local agency and agents are not only important because they react to the imposition or existence of global externalities, but are in fact foundational and essential to the continuity of global forms themselves. Friction, Tsing reminds us, has the ability to create new arrangements of culture and power, which encourages us to look beyond assumptions about inevitability and gradual progress towards a Western modernity. To understand what is actually going on in a globalizing era, she implores, we "let go of the universal as a self-fulfilling abstract truth [and] become embroiled in specific situations" (2005, 2).

Saskia Sassen (2007, 2008) advances similar ideas of globalization, however she is more specific in identifying the processes of global-local constitution. Similar to Tsing, Sassen argues that global formations are consequential, yet only become operative and performative when they enter the domain of the national. The national, she identifies, is a key enabler and enactor of the emergent global scale. However the entry and emergence of global regimes is predicated on, and helps to strengthen particular forms of what Sassen calls ‘denationalization’ – the gradual reorientation (through numerous highly charged, partial and specialized processes) of particular and specific components of what had been constructed as the national toward global logics and away from historically shaped national logics. Through these processes, national and sub-national formations and processes become recoded as instantiations of the global (2007, 8).

The steady adoption of global logics, Sassen claims, can be found in national policies, capital, political subjectivities, urban spaces and temporal frames. Instantiations of the global are also seen in a broad range of entities including the global operation of national firms and markets, political projects of nonstate actors, translocal processes that connect households across borders, diasporic networks and changes in the relationship between citizens and the state. However, processes of denationalization are open ended – at times, they enable and feed the construction of new global dynamics and institutions. Yet ‘structurations’ of the global continue to exist within the realm of what is still largely national and can be subsumed by powerful and persistent currents of the national. Understanding the transformation we call globalization, she argues, must include studying processes of denationalization and nationalization.

Sassen's work helps reveal the specific contents and (institutional) locations of what she sees as multiscalar globalization (Sassen 2007, 8). Her ideas of denationalization point more concretely to the unstable linkages across scales that constitute global forms. Notably, she illustrates the need to look beyond institutions as monolithic and instead as composed of disparate yet interconnected parts with the potential to operate according to different (national or global) logics. Applying these insights to the study of IIAs and policy space requires that we forgo the vision of IIAs as constituting the global extension of investor rights over states and the assumption that IIAs carry with them universal consequences for national development strategies and political processes. IIAs and the global IIA assemblage more broadly, though possessing degrees of institutional autonomy, are profoundly linked to the local. Processes of denationalization and the adoption of global logics in national and subnational public and private spheres made possible the formulation of IIAs and help to maintain their authority and enforcement mechanisms. It is the unstable qualities of these 'structurations of the global' that then threaten the status quo of the global IIA assemblage. For example, it was the adoption of neoliberal logics within state bureaucracies in Latin America that enabled the turn away from import substitution policies towards the adoption of trade and investment liberalization. This in turn aided the proliferation of IIAs. Yet in post-neoliberal countries, the failure of neoliberalism led to the resurgence of economic nationalism in state bureaucracies which now threatens the foundations on which the IIA assemblage is built.

It is important to remember that processes of denationalization do not play out the same everywhere. One reason for this is that these processes occur amongst diverse organizations and within complex multiscalar environments. Structurations of the global

are bound to reflect this variation in turn. The adoption of global logics – for example, neoliberalism – within state institutions is partial, uneven and sits uncomfortably with national logics, as local historical and socio-political contexts inevitably interfere in and shape to some degree the adoption process. State bureaucracies are therefore often characterised by a tension between nationalist and internationalist aspirations. Post-neoliberal countries, for instance, must grapple with the persistence of neoliberal legacies outside and within state institutions.

We can apply Sassen's insights to understand why IIAs are not everywhere the same. Transnational corporate actors have pushed for the adoption of stringent standards on investment protection and liberalization, which has encouraged a degree of homogeneity between IIAs signed by different governments (see chapter four). Yet IIAs demonstrate subtle variations, which in part, stems from different degrees of denationalization in the economic ministries charged with IIA negotiations. Those ministries characterized by greater tensions between nationalist and internationalist logics may be less swayed by corporate demands than those which fully embrace international logics. This is significant for understanding the power different IIAs possess as IIAs can be applied in diverse ways and even the most subtle of variations between provisional wording and scope can have important impacts on dispute outcomes.

### **3.5 (Re)Conceptualizing the Global IIA Regime as Assemblage**

If we are to envision global processes and institutions as unstable, uneven and fragmented, how do we understand their connectedness? How are IIAs situated within the broader global political (and social) economy and what grants them agency? With the failure of multilateral efforts to establish a comprehensive global framework for

investment protection, investor-state relations in the Americas, as Paul Haslam observes, are governed by a “multilayered, overlapping and inconsistent patchwork of investment agreements” (2010, 1). Investment rules, he argues, may be categorized as an intersecting regime following Kal Raustiala and David G. Victor’s notion of a regime complex: an intersecting regime refers to the confluence of partially overlapping, non-hierarchical international legal agreements and institutions within the same issue area. The key characteristics of the investment rules regime are its incompleteness (due, he argues, to its development through bilateral agreements rather than a multilateral arrangement); inconsistency in both its provisions and enforcement; unexpected governance effects due to interactions between regime components,<sup>11</sup> and a progressive domination of what he calls the ‘less liberal’ project by the ‘more liberal project’ advanced by stronger states. In this way, the regime is unfinished and expresses contradictory principles, norms and rules that lack international consensus. However, he argues, the density of this multilayered patchwork of agreements establishes an effect constituting a form of governance.

Haslam accurately captures the messy nature of the international investment legal regime in his description. Many scholars have explored various facets of this multilayered patchwork and exposed its somewhat inconsistent, gap-ridden nature. It is all the more mysterious, therefore, how such observations about the nature of the global IIA assemblage have not made it into debates about the agreements’ impacts on policy space. Such contradictions, incompleteness and inconsistencies leave space for negotiation and resistance. For example, the notion of state sovereignty, underpinned by the ‘image’ of

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<sup>11</sup> For example, most-favoured nation clauses contained in many IIAs provided unexpected linkages between agreements with less stringent provisions and those with more. Such clauses have been used by investors in order to demand concessions from governments under the standards of an agreement under which the investor is not directly covered.

the state as being the representative of its people, both maintains and threatens the authority of IIAs. Government officials, as representatives of the sovereign, sign on to the agreements and thus bind the state as well as its people and sub-national governments to the rights and obligations it lays out. However, governments have used their sovereign status to challenge the authority of investment dispute arbitration tribunals. For example, the Argentine government refused to pay for five awards rendered under international arbitration. It argued that Argentine courts had the right to rule over the enforcement of such awards and that enforcing the awards elsewhere would be a violation of Argentine sovereignty. Scholars tend to assume that IIAs are enforced in a consistent manner. In fact, similar disputes involving the same issue areas have been enforced inconsistently against the same country regardless of governments' objections to tribunal rulings (Gomez 2010). Differences across IIAs, legal strategies and the composition of tribunal arbitrators contribute to similar claims rendering different verdicts in arbitration procedures. While jurisprudence dominates in many legal systems, within international investment law past verdicts do not necessarily dictate future decisions (Van Harten 2008).

Further still, efforts have not been made to interrogate how IIAs and the standards they advance are enforced in the absence of an international authority capable of superseding state sovereignty. Though ISDS bodies such as ICSID help decide when a government is in breach of IIA obligations, they lack the ability to enforce the awards without the consent and cooperation of the state involved. Here, it is particularly useful to conceptualize the intersecting regime described by Haslam as one facet of a broader global assemblage following Ong and Collier (2005). Ong and Collier share Tsing and

Sassen's view that global processes and institutions possess a unique capacity for decontextualization and recontextualization, abstractability and movement, across diverse social and cultural contexts. Yet "the conditions of possibility of this movement are complex. Global forms are limited or delimited by specific technical infrastructures, administrative apparatuses or value regimes" (2005, 11).

Ong and Collier employ the metaphor of assemblage as a frame to capture the complexity of global processes centered on a vision of unstable, heterogeneous connections. In this quote, their particular concern for global assemblages as a mode of governance (in the Foucaultian sense) is also revealed. Global forms, Ong and Collier (2005, 12) explain:

interact with other elements, occupying a common field in contingent, uneasy, unstable interrelationships. The product of these interactions might be called the actual global, or the global in the space of assemblage. In relationship to 'the global,' the global is not a 'locality' to which broader forces are counterposed. Nor is it the structural effect of such forces. An assemblage is the product of multiple determinations that are not reducible to a single logic. The temporality of an assemblage is emergent. It does not always involve new forms, but forms that are shifting, in formation or at stake. As a composite concept, the term 'global assemblage' suggests inherent tensions: global implies broadly encompassing, seamless, and mobile; assemblage implies heterogeneous, contingent, unstable, partial and situated.

A global assemblage, then, is the practical and specific articulation of a global form. The use of *assemblage* in this context is to provide an alternative to the categories of local and

global, which cast ‘the global’ as abstraction and ‘the local’ as specificity. In the space of assemblage, global forms are one among a range of other concrete elements with which they interact in unstable configurations (Collier 2006, 400).

Central to the work on (global) assemblages is the idea of problematization. Assemblages are sites for the formation and reformation of what Ong and Collier call, echoing Paul Rabinow, anthropological problems. That is, global assemblages are domains in which the forms and values of individual and collective existence become elaborated into a specific problem to which diverse technological, political, and ethical interventions are held as the answer (Ong and Collier 2005, 4; Rabinow 2003, 47). Similar to Foucault’s use of the concept of apparatus, Rabinow argues that assemblages represent a heterogeneous network of elements (including discourses, institutions, infrastructural arrangements and knowledges) whose purpose it is to render specific situations as problems to which it proposes a solution of control and/or management. Whereas Foucault envisioned apparatuses as long-standing, durable responses to problematizations, Rabinow argues that assemblages are better understood as those recent formulations that stand in a dependent, but contingent and unpredictable relationship with problematizations: “They are comparatively effervescent, disappearing in years or decades rather than centuries” (2003, 56). Global forms assimilate themselves into new environments while coding heterogeneous contexts and objects in terms that are amenable to control and valuation.

If we apply these insights to the study of IIAs and their effects, it becomes possible to understand IIAs not as existing in a singular global form but as located in a heterogeneous network comprised of distinct components. Such components are vital in

creating the abstraction, legitimacy and authority to the global IIA assemblage necessary to give it force. On their own, IIAs are no more than written texts and possess no real agency. They rely on an interconnected network of actors and processes to imbue them with power and authority. Perhaps most important to the enforcement of IIAs are the foreign investors themselves, which, act as José Alvarez argues, “the regime’s private attorneys general” as they monitor government action and are in the driver’s seat of investor-state disputes (2009, 94-95). Yet also central to the enforcement of IIAs are the legal experts and arbitrators whose responsibility it is to interpret and apply the agreement’s provisions and, in the case of arbitrators, render awards accordingly. IIAs grant jurisdiction to one or more international or domestic court systems to which investor-state disputes are brought – most typically, these courts include ICSID and ad hoc tribunals established under UNCITRAL rules. These court systems, their institutional parameters and staff help to grant IIAs and arbitration processes effect and legitimacy.

However, once a verdict is rendered against a government, state sovereignty threatens the power of the courts to enforce their awards. As such, a system of additional courts and agreements on enforcement are needed to oversee the enforcement of tribunal rulings. This includes, for instance, the New York Convention, which makes it possible for investors to freeze state assets abroad. Yet, governments can respond to threats of asset seizure by renationalizing state assets before the threat is carried through. This is one example of the gaps that exist within this network that leave room for resistance and negotiation.

It is also necessary to consider the environment in which this assemblage exists. The mobile nature of capital in the contemporary era means that governments risk capital

flight or scaring off new investors should they be seen to deviate from investment rules (Chang 2006). Economic partners can also carry out forms of economic diplomacy or sanctions on behalf of their investors should host governments refuse to compensate. Such facets suggest that though certain actors and institutions may not necessarily be involved in the global assemblage of investment rules, they can engage with or withdraw from components of such a network as their interests dictate. In this way, the global IIA assemblage also represents a new geography of power, in that investor-state disputes are governed and enforced by authorities occupying multiple sites and scales.

Understanding IIAs as components of broader assemblages requires that we also consider the specific problematizations of collective life that made possible the formulation of IIAs between states. What experts, knowledges and reflexive practices were used in rendering investor-state relations a problem to be solved by legal interventions at the global scale? We must then also ask how this problematization shifted in the 1990s in ways that established more stringent IIAs as the solution. This process of historicizing the global IIA assemblage helps denaturalize its existence and in turn exposes its fragility and (modern) temporality. We can then also investigate whether and how recent contestation over IIAs threatens to unravel the specific problematizations that grant its authority.

There are a number of other analytical implications for the study of policy space and IIAs that arise from the theoretical discussion set out above. One is that in order to understand the impact IIAs have on policy space, it is necessary to examine on one hand how state officials construct and project an image of the state as coherent and cohesive and how this image is projected downwards (to non-state actors) as well as upwards (to

the international community) to challenge or buttress the authority of IIAs over domestic decision-making. This also requires examining how state actors achieve a consensus (or semblance thereof) between the competing (nationalist versus global) logics within the state and between its various parts. Examining the struggle between competing logics within the state apparatus and how they are influenced by multiple variables exposes the degree to which IIAs influence decision-making in real terms.

Secondly and related to this point, recognizing the heterogeneous and competing nature of the state apparatus opens the opportunity for non-state actors (e.g. private sector interest groups and social movements) to influence state decision-making and perceptions about the feasibility and desirability of policy options. This means that non-state actors help establish the parameters of policy space simultaneously with other factors. This requires that we recognize and examine how non-state actors respond to the imposition of IIAs and the different strategies they use to influence policymaker decisions or attitudes regarding the global IIA regime. Lastly, envisioning the global IIA regime as one dimension of a greater global assemblage of actors, institutions and knowledges also entails that we explore the direct and indirect ways in which IIAs are enforced as this also exposes the various ways in which this enforcement can be contested.

### **3.6 Conclusion**

Conventional critical approaches to the study of IIAs and policy space have made important contributions to our understanding of the imbalances and power relations that characterize the global political economy. However, in emphasizing IIAs as imposing structure-like constraints, such approaches marginalize the important role played by domestic actors in shaping the extent to which external elements influence the exercise of

policy space. Exposing how IIAs impact policy space in practice requires understanding the constraints they impose as potentials and as contingent upon their ability to enrol a network of actors, ideas and institutions that imbue them with force and effect. However, I argue that such potentials are mediated, reinforced or resisted as they are brought into interaction with domestic actors and contexts. Centering analyses on the role of domestic actors in contesting or reinforcing investment rules is therefore essential to exposing the extent to which investment rules impact policy space in practice. Yet this requires a more complex and multidimensional conceptualization of policy space and how it is shaped. It also entails leaving open the possibility that IIAs will have different impacts across time and space.

In this chapter, I provided a more nuanced theoretical framework that is able to capture the interaction between investment rules and their enforcement agents on one hand and state-actors and the political contexts in which they are situated on the other. In doing so, I point to the contingent nature of the power exerted by IIAs and their enforcement mechanisms, as well as the precarious constraints they impose on policy autonomy. I also allude to their productive potential, meaning the way in which investment disputes produce changes in perception and state action at the domestic level. My intention is not to diminish the costs that arise when governments break with investment rules or to advocate for stronger enforcement mechanisms. Numerous scholars have convincingly demonstrated the dangers to public interests that can arise if IIAs are effectively enforced against states. Rather, I aim to provide a more complex analytical lens that is sensitive to the role played by domestic actors under global economic arrangements. By drawing analytical attention to the co-constitutive and

contingent links between global processes and local forces, we can better capture the real impacts that such processes have in the middle messy ground of policy space.

#### **4 Chapter: The Contested Evolution the Global Investment Law Assemblage**

This chapter traces the origin and evolution of IIAs and the global assemblage in which they are situated. It then examines their diffusion throughout Latin America, a region where policymakers zealously safeguarded policy autonomy since the era of independence until the onset of neoliberalism. I pay particular attention to exposing the controversies surrounding the evolution of international investment law from the colonial encounter onwards and the role developing countries played in resisting the imposition of international rules regarding the treatment of foreign investors championed by capital-exporting countries. I then expose how investor-state relations were inscribed through prominent legal developmental discourses with particular meanings so that the treatment of foreign investors by host-states came to be identified as a ‘problem’ to which IIAs were prescribed as the answer. This problematization has legitimated the emergence of contemporary IIAs and ISDS as necessary legal interventions. The shift towards ISDS meant that a larger and more geographically dispersed network of actors and institutions are enrolled in the global assemblage of investment law to provide force and effect to investment rules. It has also meant that the foundational controversies informing the development of IIAs have become further hidden from public scrutiny.

IIAs and the body of international investment law in which they are situated have multiple and complex origins. The most influential sources include the historic rules on diplomatic protection and the treatment of foreign nationals; friendship, commerce and navigation treaties and successive generations of BITs and chapters in free trade agreements; United Nations resolutions and reports; draft articles developed by

international legal bodies, such as the International Law Commission and International Bar Association; rulings and awards rendered in legal disputes across the centuries; studies and critiques by academics and influential organizations like the United Nations Conference on Trade and Development (UNCTAD). International investment law, Joost Pauwelyn (2014, 15) argues, “was not rationally designed or entered into at one given point (e.g. when a country signs a BIT) but ...emerged over time from a series of small, historically-contingent and often accidental steps.”

A wide body of literature has been dedicated to exploring the influence of these various sources on the articulation of international investment law as well as the factors that drove the proliferation of IIAs in the 1990s (Birch and Halton 2001; Alcalá and Briones 2007; Elkins, Guzman and Simmons 2006; McLachlan 2008; Jandhyala, Henisz and Mansfield 2011). My intention is not to reiterate these arguments or to analyze the development of specific IIAs. Rather, I aim to expose the friction produced as developing countries resisted the imposition of western European interpretations of universal rules related to the treatment of foreign investors. I use the term friction in the sense outlined in chapter three to refer to the uneven, awkward and unstable interconnections between global and local forces (Tsing 2005). I then use this as a starting point on which to assess the various factors that contributed to the decline of developing country resistance and the expansion of the global IIA assemblage.

From the time of independence, Latin American countries struggled to assert their decision making authority in the context of a global political economy monopolized by European powers who claimed the right to intervene in territories abroad to preserve the commercial interests of their nationals. This reflected the enduring belief established in

the colonial encounter that the legal systems of non-European people were inferior and therefore incapable of presiding justly over matters related to foreign-owned assets. As Europe's influence in the region waned, a new era of gunboat diplomacy was instituted as the United States government jealously guarded the property and profit-making of its nationals. Yet repeated US interventions in the late 19th to mid-20<sup>th</sup> century fostered a sense of economic nationalism throughout Latin America. Towards the inter-war era, this sentiment was translated into a more concerted effort by Latin American governments to gain international recognition of their sovereign authority to decide over domestic economic policy (Ghouri 2011; Pauwelyn 2005).

Facing resistance to the solidification of their right to intervene, Western countries instead sought to separate the property rights of their nationals abroad from issues related to the sovereignty of host states. This was aided in the post-war era by the interest of international financial institutions and international legal associations in facilitating foreign investment promotion. Such actors played an important role in problematizing the domestic legal systems of developing countries as inadequate, biased and underdeveloped through their discourses. As investment flows grew, developed country governments faced mounting pressure from the international business community to provide efficient means of resolving investment disputes. Policymakers and the international legal community framed investor-state disputes as technical-legal matters involving the interpretation of commercial international law rather than as political disputes involving the application of public law and public policy. Adjudication over investment disputes, it was argued, was best vested in the hands of third party legal bodies that were detached from political influence and possessed the necessary technical-legal expertise. This

particular logic has come to underpin the legitimacy of contemporary IIAs and the international arbitral institutions charged with overseeing the resolution of investment disputes. It also has allowed IIAs to enrol a greater number of actors into their global networks.

In Latin America, the nationalist logic that informed attempts to exert state sovereignty over domestic economies until the 1970s was swept aside by recurrent debt crises. Governments' supposed economic mismanagement and inward-looking development strategies were targeted by international financial institutions and lenders as the causes of the region's growing financial burden. The subsequent adoption of neoliberal structural adjustment programs coincided with the signing of unprecedented numbers of IIAs as governments competed to attract new sources of capital from abroad. Governments also put aside their traditional reticence to surrendering their sovereignty in exchange for third-party oversight in investment disputes. As such, the controversy that surrounded the establishment and diffusion of IIAs became increasingly hidden from public view. Only in the last decade, as investor-state disputes mount, have the controversies surrounding IIAs come under renewed public scrutiny.

#### **4.1 The Calvo Doctrine and State Sovereignty in Latin America**

The 1648 Treaties of Westphalia granted the first formal recognition to the notion of modern statehood. The Treaties, however did not extend statehood to all territories. Rather, it was confined to those occupied by 'civilized' (western European) populations.<sup>12</sup> The European state became the sovereign representative of the diverse

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<sup>12</sup> For a critical discussion of the liberal philosophy underpinning the development of modern statehood and its relationship to European imperialism see Hindess (2004).

peoples existing within its territory and claimed responsibility to ensure its nationals protection in territories abroad. Yet, as this section demonstrates, the extension of statehood into the global South, which was often achieved through violent struggle, limited attempts by European states to cement their right to intervene in post-independence territories. Local governments in newly independent states contested the advancement of European interpretations of international rules related to the treatment of foreign investors and instead exerted their sovereign right to decide over domestic economic policy. Yet as the notion of modern statehood became increasingly accepted on a global scale, the state effect and, in turn, the “state-centric, sovereignty-oriented, territorially bounded global order” on which prominent international institutions have been founded (Falk 2002, 312) were put into place.

The Treaties of Westphalia also instituted some of the first formal constraints on the exercise of state sovereignty, notably by recognizing state responsibilities to grant safe passage and access, establishment or toll privileges and other rights to nationals of selected allies within their borders. However, it is important to note that these standards were intended to secure reciprocity in the treatment of nationals explicitly in Europe and therefore did not extend to colonies abroad (Miles 2013, 21). From the 17th to early 20th century, state practice built on these foundations to inform the development of a broader body of unwritten state obligations, which informed many of the first principles of customary international law. Of particular relevance are the custom of diplomatic protection and the international minimum standard of treatment of foreign nationals, the development of which was not a smooth or entirely intentional process.

In large part, these principles of international law emerged as a result of European efforts to expand trade and investment links during the colonial encounter. Non-European legal systems and trade networks found in territories abroad were gradually and forcibly displaced by the rise of a system of international law based on European conceptions of property and liberal principles of fairness, equity, justice and non-discrimination (Miles 2013, 23). Colonial powers insisted that local laws found outside of Europe could not be applied to European nationals (particularly traders) since they were already subject to the laws of their own country, which were thought to be superior. European powers extended this idea to claim that all assets owned by Europeans in the colonies could not be legitimately expropriated or nationalized through legislation enacted by local authorities. This interpretation of European property rights informed early notions regarding the international minimum standard of treatment to be afforded to foreign assets. However, these ideas were contested by local governments who rejected the claimed superiority of European nationals. As colonial territories gained independence, local authorities asserted their right to govern foreigners and their assets according to local law and customs (Subedi 2012, 8; Ghouri 2011, 191).

Latin American countries, as the first colonial territories to gain independence, led protests against European interpretations of such international legal principles, particularly the minimum treatment obligations and the use of foreign intervention by European states to secure their commercial interests in the region. Latin American authorities insisted that every state, both European and non-European, had the right to nationalise or expropriate foreign-owned assets to advance domestic interests according to the doctrine of state sovereignty and sovereign equality championed by European

authorities themselves. Local authorities also insisted that foreign nationals should not be entitled to greater protections than those afforded to nationals under local law and therefore called on European countries to surrender their claimed right of intervention (Subedi 2012, 8). Attempts by European powers to establish a system of international rules that would secure favourable treatment abroad for European nationals while also claiming universality were therefore met with resistance as Latin American officials drew attention to the contradictions of such principles.

As a result of this friction, the ‘international minimum standard of treatment’ obligation evolved to recognize the right of independent host states to expropriate foreign assets as a logical extension of state sovereignty provided that foreign nationals were compensated for the losses incurred. However, European authorities continued to insist that in instances where local law was considered ‘inferior’, which was the case in remaining African and Asian colonies, the international minimum standard of treatment would continue to apply over local law, meaning that European assets could not be legitimately expropriated under any conditions (Subedi 2012, 8 – 9). Not all local governments in these colonies and in independent Latin America accepted the obligations European powers attempted to impose. Where local governments did acquiesce, there were strong disagreements regarding the exact duties such obligations imposed on governments. Host states and European powers therefore came into repeated conflict over the treatment of foreign nationals.

Toward the end of the 19th century, European powers and the United States began to assert more strongly their right to intervene under the principle of diplomatic protection. The notion behind this principle was first articulated by Swiss legal scholar

Emmerich Vattel, who wrote that “whoever ill-treats a citizen indirectly injures the State, which must protect that citizen” (Vattel 1916, 136 as quoted in Tiburcio 2001, 34).

Nationals of the United States and European countries that had flocked to Latin America to take advantage of the region’s abundant natural resources and fledging industry found their assets subject to nationalization in the decades preceding independence and called upon their home states for solutions. Technically, under the principle of diplomatic protection, Western powers were to limit the use or authorization of force to protect assets or enforce debts held by their nationals abroad unless there was a specific denial of justice. However, it was easy for foreign nationals to allege that a denial of justice had occurred and in such instances, a foreign investor’s home state was to assume the claim as its own and present the claim against the state that injured the investment or property (Ghouri 2011, 191; Pauwelyn 2005, 21). .

Yet this solution was often ineffective and degenerated into armed conflict. Western states often retaliated against expropriations through the use or threat of force including invasions, gunboat attacks and blockages of key ports and passages (Ghouri 2011, 191; Pauwelyn 2005, 21). From the viewpoint of the investor whose assets had been expropriated, this form of diplomatic protection (or espousal) rarely provided a satisfactory solution. Home states were under no obligation to take up the claim on behalf of its national and were at times reluctant to do so because it risked disrupting political and economic relations with the host. The home state was also under no obligation to settle the dispute according to the terms desired by the investor (Vandeveldt 2005, 160).

In Latin America, the repeated threat of European interference in the early 18<sup>th</sup> century and the issuance in 1823 of the Monroe Doctrine by the United States

government fostered a deep concern amongst governments for the preservation and exercise of state sovereignty. The eventual rise of the United States as a major global power towards the end of the 19th century and increasing instances of US intervention in the region ensured that this sentiment was maintained over decades. In 1868, the Argentine diplomat and legal scholar Carlos Calvo articulated his concern for state sovereignty in his published works on international law. He asserted that no foreign investor should expect greater protection and treatment than that given to nationals of the host state. Therefore, he argued, foreign investors should submit their concerns directly to the host state's domestic legal system and not be accorded protection by foreign powers, especially not in the form of armed intervention (De Almeida 2013, 473). European and the United States governments and legal scholars rejected these arguments as it would eliminate the possibility of foreign intervention without providing a satisfactory alternative. In Latin America, however, this doctrine gained widespread popularity amongst officials who protested the use of force by foreign nationals' home states under the guise of diplomatic protection. 'Calvo Clauses' were included in numerous Latin American constitutions, domestic laws, international treaties and in some contracts signed with foreign investors (Alcalá and Briones 2007, 996; Shan 2007, 127). The global spread of European interpretations of universal standards on the treatment of foreign investors was therefore limited by the development of alternative standards by southern intellectuals.

Several bilateral economic treaties were also signed in this period, however they focused largely on establishing trade and diplomatic relations and rarely made reference to the protection of foreign assets. The exception included very broad references to the

protection of the property of foreign nationals, such as those included in Friendship Commerce and Navigation (FCN) treaties signed by the United States and some Latin American countries. For example, the *1853 Treaty of Friendship, Commerce and Navigation between Argentina and the United States* provided that “The citizens of the two contracting parties shall reciprocally receive and enjoy full and perfect protection for their persons and property.”<sup>13</sup> These treaties also required payment of compensation for expropriation and guaranteed nationals of signatory states ‘most favoured nation’ status and national treatment with respect to the right to engage in certain business activities in the territory of member states. However, the underlying logic of the treaties was to protect the property of individuals and not necessarily the assets of foreign businesses (Vandeveldt 2005, 158 – 159). For the most part, these treaties represented an effort by the United States to cement its own interpretation of customary international law principles guiding the protection of foreign investments at a time when such principles were increasingly contested. However it is important to note that these treaties did not provide for enforcement mechanisms, which means that foreign nationals continued to depend on espousal or coercive military tactics in the event of a dispute (Trakman and Ranieri 2013, 16)

By the beginning of the 20th century, the attempts of Western countries to forge a consensus on the treatment of foreign assets and the right to intervene had achieved limited success due to the resistance of post-independence states. Repeated conflicts and armed intervention only served to destabilize the consensus further. In 1902, for instance, Britain, Germany and Italy blockaded and bombed Venezuela’s ports in retaliation

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<sup>13</sup> Treaty of Friendship, Commerce and Navigation between Argentina and the United States, 27 July 1853. Available at: [Avalon.law.yale.edu/19th\\_century/argen02.asp](http://Avalon.law.yale.edu/19th_century/argen02.asp) (accessed 21 December 2015).

against the country's default on debt payments. This prompted renewed debate on the role and legitimacy of foreign intervention. Argentina's Foreign Minister Luis María Drago responded by proclaiming the use of force and armed intervention in cases involving disputes over unpaid public debts to be illegal. This announcement, which came to be known as the Drago Doctrine, reaffirmed the spirit of the Calvo Doctrine and received widespread support amongst Latin American governments (De Almeida 2013, 474).

US President Theodore Roosevelt responded by declaring to Congress that repeated wrongdoing by neighbouring (Latin American) countries, including the unwillingness of some to pay obligations, might require intervention by a 'civilized' nation. The United States had surpassed Europe as the main trading partner and adopted the role of a primary creditor with many Latin American countries by the end of the 20th century. Strengthening commercial ties meant that the United States government became increasingly interested in maintaining its right to intervene on behalf of US commercial interests, which was commonly practiced. From 1890 to the early 1930s, the United States intervened in Latin America on 43 occasions, 32 instances of which were in Central America and the Caribbean region. Particularly controversial was the persistence of US interventionism in Nicaragua, which began in 1912 and lasted over two decades. This occurred despite the international condemnation of the use of force in collecting international debts in the 1909 Hague Convention (Whitman 1959, 9; Vandeveld 2005, 161).

In the 1920s, Mexico, the Soviet Union and several Eastern European countries issued policies aimed at widespread agrarian reform that resulted in the expropriation of

land owned by foreign nationals. For the most part, the countries asserted that the social purpose of the agrarian reform initiatives meant that the land seizures did not fit into traditional categories of expropriation or confiscation and thus the state was relieved of its obligations to pay compensation. The Mexican government's delay in compensating US nationals for land expropriations resulted in particularly high tensions between the two governments. Cordell Hull, then the US Secretary of State, issued a letter to the Mexican Government insisting that,

The purpose of [Mexico's agrarian reform] program, however desirable, is entirely unrelated to and apart from the real issue. The issue is not whether Mexico should pursue social and economic policies designed to improve the standard of living of its people. The issue is whether in pursuing them the property of American nationals may be taken without making prompt payment of just compensation under international law.<sup>14</sup>

This letter encapsulated the position within the US government related to investment protection abroad: host state policy goals were irrelevant when considering whether compensation was to be awarded to a US national whose property rights were intervened.

Hull also contended that it was a fact of international law that states were obliged to pay "prompt, adequate and effective compensation" to foreign investors whose assets were expropriated, a notion that became known as the Hull Rule. In response, the Mexican government reiterated the Calvo Doctrine and asserted that states had no obligation to foreign investors under international law other than that of non-

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<sup>14</sup> Statement of Hughs (7 June 21), "The US and Mexico, International Conciliation" as cited in Miles (2013, 76)

discrimination. Rather, foreign investors had to submit their claims under host states' domestic legal systems in order for a judgement on compensation to be rendered. Moreover, it argued, state practice had never given force to the idea that states were obliged to compensate investors in such a way (Wouters et al. 2013, 28 – 29; Ghouri 2013, 194).

The United States was joined by other capital-exporting countries in championing the Hull formula as a response to developing countries' insistence on the legitimacy of the Calvo Doctrine. The concern amongst capital-exporting countries was that, in submitting claims to domestic courts in host states, compensation would be delayed or ultimately unsatisfactory in the eyes of the foreign investor. Developing countries, however, grew concerned that cementing the right to prompt and adequate compensation in international law would be used to once again legitimate the right of capital-exporting states to intervene on behalf of their nationals should host states delay payment. Gradually, an unstable consensus emerged on the right of host states to expropriate foreign assets under narrowly defined conditions provided that expropriations were accompanied by adequate and prompt compensation (Subedi 2012, 18). However it is important to note that there was still ample disagreement between countries on the meaning of this obligation, for example, whether effective compensation meant dollars or local currency (Whitman 1959, 14).

In 1924, efforts were taken up by the League of Nations to solidify a consensus on the customary rules governing the protection of foreign assets. These efforts failed, however, due to continued disagreement between developing and developed countries on central principles, including whether foreign nationals should be granted 'equal treatment'

to the nationals of host states and the duties imposed by the ‘minimum standards of treatment’ obligation. In response, Latin American countries sought to advance their own interpretations of customary international law. For instance, during the seventh International Conference of American States in 1933, Latin American countries adopted the *Convention on the Rights and Duties of States*, which included articles reflecting the Calvo Doctrine. Article 8 of the Convention also stated that “No state has the right to intervene in the internal or external affairs of another.” Article 9 further stipulates that “Nationals and foreigners are under the same protection of the law and the national authorities and the foreigners may not claim rights other or more extensive than those of the nationals.”<sup>15</sup> Article 9 reflects the notion that foreign nationals surrendered their right to protection from their home states and instead would submit disputes to the legal system of host states. The convention was therefore an important step forward for Latin American countries seeking to define international rules governing foreign investments. The US delegation adopted the convention with hesitation, which was due largely to an important and ongoing shift in US foreign policy towards Latin America (Ghouri 2013, 193).

At the same conference, the United States made public the adoption of the *Good Neighbour Policy*, a policy championed by President Franklin D. Roosevelt that sought to establish stronger relations with Latin American governments on more equal terms. Most importantly, the policy advocated non-interventionism, which meant that the US government surrendered its solid stance on the right to intervene. During the time leading up to the conference, the US government faced rising economic pressures as a result of

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<sup>15</sup> The text of the Convention can be found at: <http://www.oas.org/juridico/english/treaties/a-40.html> (accessed 12 February 2016).

the onset of the Great Depression. Public opposition within the United States mounted against extended interference in foreign affairs as an isolationist sentiment took hold (Crawley 2007, 7 – 10). This was complimented by rising anti-US sentiment within Latin America, particularly after several US interventions resulted in the rise and maintenance of regimes dominated by illegitimate dictators. It is important to note that the adoption of the *Good Neighbour Policy* did not put an end to the practice of US intervention in the region. It did, however, signify a willingness to move away from demanding that the right to intervene be enshrined in international law. Moreover, under Roosevelt, the United States took a more conciliatory approach with some governments in settling disputes over nationalizations, including Mexico's nationalization of US-owned agricultural land in 1938 (Dwyer 1998).

To summarize, from the 16th to 20th century, the protection of foreign assets abroad was for the most part a concern unique to colonial powers and stemmed from the desire to protect trade and investment routes from interference by local authorities. The practice of intervention was legitimated by a belief in the inferiority of non-European legal systems and the notion that European states had a duty to pursue retribution in instances where their nationals faced discriminatory treatment abroad. Early interpretations of customary international law principles regarding the protection of foreign investments therefore emerged as a result of European colonial expansion. Yet the nature of these principles cannot be understood in the absence of the agency of local actors in colonial territories and, particularly, in newly independent Latin America. Indeed, many of the early principles and rules formulated to govern the treatment of foreign assets abroad reflected the friction between the attempts of colonial powers to

forge a universal consensus on the treatment of foreign assets based on European interpretations and the contestation of such interpretations by non-European governments and intellectuals. Resistance to European standards strengthened as statehood was extended throughout the Americas, which provided Latin American governments a foundation on which to advance their own interpretations in emergent international institutions.

Resentment over European interventionism prompted Latin American governments to assert their sovereignty on the international stage with demands for equal treatment according to the principles established by European powers. However as the United States increased its international presence, a new voice was leant to the push for stronger investment protections, including the right of intervention. Yet the use of armed intervention by the US government served to strengthen the resolve of Latin American governments to resist Western interpretations of customary international law. The international community became increasingly divided between capital-exporting countries on one hand and newly independent states on the other as Latin American countries sought to cement their own rights, namely to decide over domestic economic policy free of foreign influence. The development of customary international law principles regarding the treatment of foreign investors was therefore unsettled and subject to much controversy. The semblance of agreement achieved by the inter-war period came to be informed by the productive friction created by the advancement of ‘universal’ principles by Western powers and the alternative standards developed in the global South. Yet such principles largely proved to be unsatisfactory for parties on either side of the debate.

## 4.2 The Post-War Integrationist Agenda

In the post-war period, several competing processes informed countries' attitudes towards consolidating formal investment rules. The chaos of the World Wars and economic troubles of the Great Depression created an interest amongst the victorious allied countries in multilateralism as a peaceful means to achieve consensus and stability in the international arena. This resulted in a concerted push for the development of international organizations and international rules to guide state behaviour. The severe economic depression that preceded the Second World War was believed by many in the West to have been exacerbated by the protectionist policies of the 1920s. As such, consensus strengthened amongst allied countries around the importance of economic liberalism. Many of the multilateral projects taken up in the post-war period therefore focused on trade liberalization. This led to the conclusion of the *General Agreement on Tariffs and Trade* (GATT) in 1947, which became the principle forum for trade negotiations but failed to address issues of investment. Early proposals from the United States to include investment rules in the GATT negotiations fell flat due to the hesitation of some members to include obligations that encroached on areas of domestic legislation and unconventional trade issues, hesitation that was particularly strong amongst developing countries. This meant that investment rules would have to be negotiated outside of multilateral trade negotiations (Vandeveldt 2005, 161- 162; Narliker 2003, 43).

As Western economies promoted the establishment of a more peaceful world order, the use of overt intervention to protect assets abroad fell out of favour. Efforts were therefore taken up by developed countries and international business organizations to push forward a separate multilateral agreement on investment rules. This included draft

proposals aimed at integrating investment protection provisions into the proposed International Trade Organization in 1948 (via the Havana Charter),<sup>16</sup> the 1949 *International Code of Fair Treatment for Foreign Investment* proposed by the International Chamber of Commerce (ICC), the *Draft Statute for the Arbitral Tribunal for Foreign Investment* and the *Foreign Investment Court* developed by the International Law Association, the 1959 *Abs-Shawcross Draft Convention on Investment Abroad*, the 1961 *Draft Convention on the International Responsibility of States for Injury to Aliens*, and finally the 1967 *Draft Convention on the Protection of Foreign Property* advanced by the OECD. All of these drafts were plagued by ample disagreement between signatories on the rights that should be afforded to foreign investors versus host countries and were ultimately abandoned (Subedi 2012, 19- 21; Miles 2013, 85; Ghouri 2014, 194).

The decolonization process following the Second World War resulted in the extension of the Westphalian state system to Asia and Africa. This meant that the state abstraction and basic architecture needed for the extension of investment rules in these regions was laid. However, it also meant that control over economic policy was vested for the first time in the governments of sovereign states, many of which achieved their independence through violent struggle with colonial powers. As their political independence increased, the priority of post-independence administrations was placed on asserting their economic independence. Most of these states inherited a system dominated by foreign ownership. Natural resource sectors were largely controlled and exploited by

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<sup>16</sup> According to Whitman (1959, 12), the Havana Charter, which was signed by 53 countries at the 1948 Havana Conference ultimately failed because the US Congress failed to ratify it because of concerns that the language was too vague and the considerable concessions made to capital-importing countries over control of foreign investments.

foreign companies under concession contracts or other agreements concluded with former colonial administrations (Subedi 2012, 21).

Contracts signed between natural resource firms and governments across the developing world were typically weighted heavily in favour of foreign investors who used their bargaining position to evince concessions from governments. Foreign companies, for instance, often paid only small sums of money to their hosts for the rights over their natural resources (Likosky 2009). Social and economic reforms adopted after independence in many of these countries aimed at nationalizing natural resources and many of the concession contracts granted by previous colonial administrations were cancelled.<sup>17</sup> The governments of newly independent states in Asia and Africa argued that such contracts ceased to have authority once the colonial territory was dissolved and an independent state established. They therefore claimed the right to review the contracts and compensate investors whose assets were nationalized according to their own determinations. Many of the contracts had been obtained through coercion and thus needed to be reassessed for their legality according to domestic law (Miles 2013, 79 – 80; Shan 2007). The advantageous trade and investment relations established by Western powers in colonies abroad therefore came under threat by domestic contestation in post-independence countries.

Post-independence states and communist countries, led by the Soviet Union, embraced the Calvo Doctrine as they believed it would help safeguard state interests and autonomy from Western powers. Calvo clauses therefore witnessed a revival in the post-

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<sup>17</sup> Perhaps the most cited examples include the nationalization of British oil assets by Iran in 1951, the expropriation of Liamco's concessions in Libya in 1955, the nationalization of the Suez Canal by Egypt in 1956 and the nationalization of sugar companies in Cuba during the 1960s. For example, Mills (2013).

war period as Africa and Asian countries included them in their domestic legislation (Ghouri 2013). The Calvo Doctrine therefore established ideational hegemony in much of the post-independence world, limiting the expansion of European standards on investment protection. Newly independent states and Latin American countries sought to formalize international recognition of their right over domestic natural resources, most notably in the newly created United Nations. In 1962, the United Nations General Assembly (UNGA) adopted resolution 1803 on the *Permanent Sovereignty over Natural Resources*. The aim of the resolution was to balance the interests of the developed and developing countries regarding the governance of natural resources by recognizing that imported capital in natural resource sectors would be protected by both national and international law. While the United States pushed for the inclusion of a commitment that would bind states to providing “prompt, adequate and effective compensation” for expropriations, the resolution provides only for an “appropriate compensation in accordance with the rules in force in the state taking such measures in the exercise of its sovereignty and in accordance with international law” (as quoted in Ghouri 2013, 197). This is largely due to the resistance amongst post-independence states to the imposition of US standards. However for the United States and other capital-exporting countries, this was an important step forward in ensuring that the treatment of foreign investment would be subject to international law and not solely the law of host states. It is important to note that the resolution preserved state-state dispute resolution, which was seen as increasingly problematic, given capital-exporting states’ growing interest in avoiding international conflict.

Once reconstruction efforts in Europe came to an end, government agencies increasingly turned their attention toward promoting economic development in the non-Communist developing world. Promoting economic development in these regions, it was thought, would decrease the possibility of future armed conflict and expand markets for the export of Western goods (Whitman 1959). The important role played by foreign capital (both private and public) in European reconstruction efforts increased faith amongst developed countries in the role that foreign capital could play in developmental processes. This received widespread support from domestic business communities looking to expand abroad. For instance, the US International Development Advisory Board, which brought together private sector representatives to advise policymakers on development policy, issued a report in 1957 stating:

We expect that, as the less developed countries achieve a substantial degree of economic development, and as they achieve a greater degree of trust in us and confidence in themselves, the opportunities for private capital will grow.

Opportunities are already growing in much of Latin America. When this occurs, private capital can, should and will take the burden of development away from government. One of the major objectives of the program we propose is to build the necessary basis for a marked increase in foreign private investment.<sup>18</sup>

Foreign investment promotion therefore came to be supported by a dual logic. On one hand, businesses in the developed world were increasingly interested in taking advantage of opportunities to expand into the developing world but were cautious of the possibility

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<sup>18</sup> International Development Advisory Board. 1957. A New Emphasis on Economic Development Abroad. Report to the President of the United States on Ways, Means and Reasons for US Assistance to International Economic Development (Washington DC), 13.

that their assets would be nationalized by administrations seeking to assert their political and economic independence. Instances of past expropriations, regardless of their domestic motive, were taken as evidence of the unpredictability of government action in post-independence states. These concerns were made more acute by the emerging consensus that armed intervention was no longer a legitimate option for home states seeking to protect assets abroad. The lack of predictability was, in turn, identified as a problem in need of resolution through more stringent and effective international legal frameworks. On the other hand, foreign investment was also increasingly seen as a means of transporting Western expertise, technologies and managerial skills into the developing world to aid in economic and institutional development. Prominent developmental discourses framed foreign capital as a key driver of economic progress, which lent foreign investment promotion a new humanitarian purpose. This dual logic, in turn, became increasingly entangled with countries' geopolitical objectives following the outbreak of the Cold War.

The repeated failure of multilateral efforts to formalize a consensus on investment rules and continued push-back from developing countries that sought a greater recognition of their right to nationalize motivated many developed countries to pursue bilateral alternatives. The objective was to cement progress towards the establishment of foreign investment protections under customary international law and therefore prevent future backsliding (Pauwelyn 2005, 24). The United States and European countries also began marketing the advantages of foreign capital to economic progress inside and outside of the United Nations (Ghouri 2013, 195). Yet the push for BITs was also strongly motivated by the desire to secure the developing world from the unfolding

Communist threat. Developing countries were promised greater inflows of foreign capital to aid in developmental processes in exchange for their political support (Gardner 1960; Pauwelyn 2005, 24; Trakman and Ranieri 2013, 16). The developmental discourses advanced by Western countries and institutions had an important ideational influence on policymakers in the global South. For developing countries, signing on to economic treaties with the West became a way of signalling their support for liberal democratic and capitalist principles and stable economic policy.

The United States and several European countries continued to sign FCN-style treaties with developing and newly independent countries in the 1950s and into the mid-1960s.<sup>19</sup> These treaties resembled their pre-war predecessors, however they contained two new obligations: an explicit coverage of corporate property (in addition to the property of individuals) and a promise to limit the use of exchange controls to allow foreign nationals to repatriate profits. The treaties also contained more specific language related to issues of investment, including the concepts of establishment, expropriation, national treatment, most favoured nation treatment and capital transfers. However the agreements maintained state-state dispute resolution mechanisms, which were most often overseen by the International Court of Justice (ICJ) as a logical extension of the traditional practice of diplomatic protection (Pauwelyn 2005).

Bilateral treaties dedicated explicitly to investment matters first appeared in the late 1950s and were championed by European capital exporters (notably Germany and Switzerland). BITs proved to be an easier method of securing investment protection abroad than FCN treaties because parties avoided having to negotiate cumbersome details

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<sup>19</sup> Such treaties were concluded with Ethiopia, Israel, Korea, Nicaragua, Iran, Colombia, Haiti, Uruguay and Pakistan in the post-war era (Whitman 1959, 13)

related to navigation and diplomatic relations (Pauwelyn 2005, 22; Vandeveld 2005, 161). The first BIT was signed in 1959 between Germany and Pakistan. This particular agreement signalled less of a step forward than a confirmation of existing protections provided under customary international law. It did, however, contain more specific language based on the burgeoning work of European legal scholars that would inform the future of investment agreements, including the concepts of non-discrimination, full protection and security, compensation on expropriation and the free transfer of capital. These concepts and their ambiguity have come to the centre of contemporary debates regarding how investment rules are to be translated. Other European countries followed this example and began integrating similar language based on the ideas of German legal scholars in BITs signed thereafter (Ghouri 2013, 197). These agreements were notable for the umbrella clause that bridged the protection of foreign investment under (public) international law with (private) contracts under host state domestic law. This, Pauwelyn (2005, 26) refers to as the “internationalization of state contracts”, meaning that states who sign on to such clauses could be held liable under the agreements not only for the infringement of investment rules but also for breaches of investor-state contracts. Most early BITs however maintained the practice of state-state dispute resolution, which meant that foreign investors continued to rely on their home governments to introduce a claim against their hosts in the event of a conflict.

Following the post-war wave of nationalizations in newly independent states, private companies pushed more efficient and reliable means of resolving disputes with host governments. Private companies witnessed the repeated failure of their home governments to ensure effective compensation for prior nationalizations and feared that

host states' domestic courts would not provide a fair assessment in future disputes. The aim of governments in capital-exporting states was to protect nationals' assets abroad from unilateral state action while divesting responsibility over investment disputes onto third parties as to avoid conflict with economic partners. For instance, developed countries established publically funded insurance schemes that enabled foreign investors to take out insurance against political risks abroad (Pauwelyn 2005, 24).<sup>20</sup> Yet the influence of capital-exporting states and private investors was limited by developing countries' continued efforts to preserve their sovereign authority over domestic economic policy. This led to the revival of the Calvo Doctrine and the repeated failure of multilateral efforts led by capital-exporting states to create a global framework on investment protection.

At the same time, the Bretton Woods institutions established to lead European reconstruction efforts faced the need to redefine their purpose in the post-reconstruction era.<sup>21</sup> At the World Bank, where capital-exporting countries had a greater voice (and voting power), the idea that foreign investment promotion could promote economic growth in the developing world gained traction (Lowenfield 2009, 49). World Bank executives therefore took an interest in defining the institution's future role in this area. A series of consultations with legal experts was convened to develop recommendations on the establishment of a centre that would provide an alternative mechanism for the resolution of investment disputes. In 1965, the World Bank announced the creation of ICSID and sold the institution to member states as a minimalist, apolitical project that

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<sup>20</sup> Advanced economies established new insurance schemes (i.e. Canada) or repurposed its insurance schemes that were originally designed to aid in European reconstruction efforts (United States).

<sup>21</sup> It is important to note that developing country officials played an important role in the foundation of Bretton Woods institutions. See Helleiner (2015).

would help states to avoid conflict by establishing an institutionally advanced option for investment dispute settlement.

Most notably, ICSID was designed so that foreign investors could bring claims unilaterally against their hosts and therefore avoid the troubles associated with convincing home governments to espouse a claim on their behalf. Indeed, states had historically proved rather hesitant to engage in formal state-state dispute settlement and few cases were brought to the ICJ (Subedi 2012, 95). By establishing a third-party institution to oversee investor-state disputes, foreign investors would also be saved the obligation of introducing claims in host states' domestic courts, which investors claimed were seen as susceptible to bias and politics. Moreover, taking the investors' home state out of the equation allowed governments to avoid becoming embroiled in protracted diplomatic disputes (Pauwelyn 2005, 26-28; Miles 2013, 6 – 7; Lowenfield 2009, 51-52). By omitting references to the substance of host state obligations and framing its development as a technical (apolitical) process, Bank executives avoided the contentious ideological debates regarding the substantive protections afforded to foreign investors that were raging elsewhere. ICSID's institutional skeleton, however, reflected a particular interpretation of arbitral proceedings that is most often found in private law.<sup>22</sup> Arbitrators were to be appointed by the parties involved, the proceedings were to be strictly confidential, arbitral awards were not subject to appeal and resolutions stressed financial compensation rather than soliciting compliance.

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<sup>22</sup> According to Parra (2012, 43), the drafting of the ICSID convention was led by Aron Brochers, an international lawyer from the Netherlands General Counsel of the World Bank, assisted by a team of internationally trained lawyers from the Legal Department including Leopoldo Cancio, Georges R. Delaume, Christopher Pinto and Piero Sella

World Bank staff began to champion ICSID in the developing world as a means to overcome credibility problems while receiving reassurance from investors' home states that diplomatic intervention would not be used. Governments were also offered the possibility of limiting ICSID's jurisdiction over disputes of a sensitive nature to quell concerns regarding the preservation of state sovereignty (Pauwelyn 2005, 28). The first BIT to grant (compulsory) jurisdiction to ICSID over investor-state disputes was the 1968 *Netherlands-Indonesia BIT*. However, very few disputes were brought under ICSID in its first years (only 25) until the 1990s (Pauwelyn 2005, 30). This is largely because many developing countries refused to sign on to the ICSID Convention in its early years due to lingering fears over the preservation of state sovereignty. The World Bank also had little capacity to persuade countries to sign on to its jurisdiction over investment disputes until the 1980 debt crisis, which considerably increased the World Bank's bargaining power. In Latin America, all countries except Ecuador refused to sign on to the agreement because of a lingering belief that investment disputes should be subjected first and foremost to local law.

The United Nations also took up efforts to define its role in investment promotion. The United Nations Commission on International Trade Law (UNCITRAL), created in 1966, convened a series of consultations with legal experts and drafted a set of Arbitration Rules to guide members' resolution of commercial disputes. Like ICSID, UNCITRAL rules are also based on the private-law model of arbitration and provide for the establishment of an ad-hoc tribunal, the members of which are chosen by the parties involved. UNCITRAL rules also provide for the confidential resolution of investment disputes and establish no linkages to host states' commitments under public international

law. However UNCITRAL rules provide a greater degree of flexibility in deciding how many arbitrators will be appointed and where the proceedings will take place than in the ICSID forum. Proceedings can be convened under a number of domestic and international legal bodies depending on the agreement reached between parties, but are most often convened under prominent institutions such as the International Chamber of Commerce, the American Arbitration Association and the Permanent Court of Arbitration (Griffith and Mitchell 2002; Tuck 2007).

The creation of these forums meant that new institutional mechanisms with their own support staff and legal experts could be enrolled into the networks of IIAs. However, the role of these tribunals was limited to that of adjudication over investor-state disputes as neither UNCITRAL nor ICSID tribunals have the authority to directly enforce investment rules or tribunal rulings. The enforcement of international arbitral awards is governed by international treaties, most commonly the *1959 Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (the New York Convention) drafted by the International Chamber of Commerce, which provides foreign investors the ability to enforce awards against state assets. However, enforcement procedures largely depend on the cooperation of the country involved, which is not guaranteed. If countries refuse to recognize the authority of the award and investors' rights of enforcement, it is up to other countries and international financial bodies to exert political and economic pressures against the country to which the award was rendered. This most commonly involves the investor's home state, reflecting the tradition of diplomatic protection.

The rise of structuralist theory as a guiding framework for economic policy in the 1960s and 1970s had a discernable impact on attitudes towards FDI and economic

integration in the region. Structuralism first emerged in the written works of the Argentine economist Raúl Prebisch, Director of the Argentine Central Bank from 1935 to 1943 and subsequently the Executive Secretary of the UN Economic Commission for Latin America (CEPAL from 1949 – 1963). Prebisch theorized the existence of an industrial, hegemonic centre and an agrarian, dependent periphery as a framework to explain the structure and function of global capitalism. Underdevelopment in the periphery, he argued, resulted from the unequal exchange relations produced by exploitative trade and investment linkages, which enriched the centre at the expense of the periphery (Love 2005, 101).

This line of thinking became influential within the United Nations Commission for Latin America and the Caribbean (Spanish acronyms are CEPAL) and a new generation of Latin American economists who became defenders of inward-looking development models at a time when Bretton Woods institutions were pushing for the adoption of outward-looking policies (Bulmer-Thomas 2003, 268). By the end of the Korean War, the terms of trade between the developed and developing world showed dramatic deterioration, which meant that “the intellectual pendulum began to swing toward import-substituting industrialization (ISI)” promoted by CEPAL staffers (Bulmer-Thomas 2003, 268). Mexico, Chile, Argentina, Colombia, Uruguay and Brazil employed ISI policies to leverage the significant industrial base they had managed to build. By maintaining high tariff barriers to industrialised goods, governments aimed to encourage the replacement of imports with domestically produced goods and therefore protect infant industries from being subsumed by foreign competition. Governments also feared the possibility of becoming dependent on foreign capital for their economic and, in turn,

political stability. They therefore adopted policies that limited the inflow of foreign investment, including screening and approval procedures, restrictions on foreign ownership, and technology transfer requirements (Gibbs 1996, 100; Baker and Holmes 1991, 7).

Venezuela, Bolivia, Paraguay, Peru and Cuba, however, maintained policies aimed at export intensification after poor experiences with inward looking policies in the first years of the post-war era. However by the 1960s, both inward-looking and outward-looking countries experienced new economic troubles. Inward-looking countries faced mounting balance-of-payment crises, rising inflation and labour strife. Outward-looking countries also suffered from balance-of-payment problems and a vulnerability to adverse external crises. Both inward and outward looking countries therefore turned to regional integration as a partial solution to their problems. For inward-looking countries, integration provided an opportunity for export promotion without the full impact of international competition and for outward-looking countries, it provided an opportunity for industrialization through regional ISI (Bulmer-Thomas 2003, 269).

Yet structuralist ideas and the emphasis they placed on policy autonomy had an important impact on the development of regional arrangements. Interest in integration in Latin America was also driven by the relative success of integrationist arrangements seen in Europe. However, while European countries renounced state sovereignty by giving authority to supranational governing bodies, Latin American countries were not willing to surrender autonomy to such an extent. Integration schemes, such as the Montevideo treaties of the 1960s and 1980s that established the Latin American Free Trade Agreement and the Latin American Integration Association, provided only for economic

cooperation while retaining decision-making largely in the hands of member states (De Almeida 2013, 479). Governments also took the opportunity to reaffirm the Calvo Doctrine. For example, the Andean Group took steps to restrict or prohibit foreign investment through the 1970 amendment to the Cartagena Agreement, originally signed the year prior. This amendment, known as Decision 24, required that foreign investors control no more than 49 percent of Latin American enterprises and forced those that owned a majority stake to divest assets, leading to considerable capital flight (Baker and Holmes 1991, 16).

Latin American countries also sought greater cooperation with other Southern partners to advance common economic interests in international fora. Most notable was the establishment of the New International Economic Order (NIEO) in the mid-1970s which brought together developing countries from diverse regions to advance issues related to the terms of trade, development assistance and tariff reductions inside the United Nations. The NIEO used its collective strength to push forward a series of resolutions that directly or indirectly supported the Calvo Doctrine. In 1974, for instance, the UNGA passed resolution 3171 affirming “the inalienable rights of States to permanent sovereignty over all their natural resources” and supporting “the efforts of the developing countries and of the peoples of the territories under colonial and racial domination and foreign occupation in their struggle to regain effective control over their natural resources.” It further declared that “each state is entitled to determine the amount of possible compensation and the mode of payment, and that any dispute which might arise should be settled in accordance with the national legislation of the State carrying out

such measures.”<sup>23</sup> Developed countries opposed the resolution as it excluded the role of international law and was therefore seen as a step backward in investment protection (Ghouri 2013, 196).

The same year, a resolution granting formal recognition to the *Establishment of a New International Economic Order* echoed the same notion of full and permanent sovereignty of states over natural resources and economic activities.<sup>24</sup> The 1974 UN *Charter of Economic Rights and Duties of States* then reiterated these principles and asserted that only states’ domestic laws, as interpreted and applied by domestic courts, governed foreign investments and that no state could be compelled to give preferential treatment to foreign investors.<sup>25</sup> However it also stated that in the case of expropriation compensation should be paid by the state adopting such measures having taken into consideration its own relevant domestic laws. This raised concerns amongst developed countries that expropriated assets would not be promptly or adequately compensated. In response, OECD countries passed the *Declaration on International Investment and Multinational Enterprise* (Ghouri 2013, 195). The Declaration provided voluntary guidelines for the governance of foreign investment and affirmed the application of international law standards, albeit without specifying their nature and meaning.<sup>26</sup>

The decolonization process and rise of communism in Eastern Europe therefore leant a new dynamic to international institutions that were forced to take more seriously

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<sup>23</sup> United Nations General Assembly. Resolution 3171 (XXVIII) Permanent sovereignty over natural resources.” Full text may be found at:

<sup>24</sup> See UNGA Resolution 3201.

<sup>25</sup> UNGA. Resolution 3281 (XXIX) Charter of Economic Rights and Duties of States. 12 December 1974. Available at: [www.un-documents.net/a29r3281.htm](http://www.un-documents.net/a29r3281.htm)

<sup>26</sup> According to Ghouri (2013: 195) the OECD’s first effort to achieve consensus on FDI governance was its 1962 Draft Convention on the Protection of Foreign Property which contained provisions on fair and equitable treatment and protection and security as well as just compensation paid effectively without delay. However the Draft failed to win the support from all OECD members and was ultimately defeated.

the unique interests of the developing world. On one hand, concern over the issue of compensation for expropriations continued to dominate policy debates in capital-exporting states. The inability to predict government action in post-independence states and the lack of guarantees against expropriation came to be identified as problems in need of addressing through the formulation of international rules. This is while governments sought to avoid conflict by downloading responsibility for investment disputes onto third-party institutions. This received strong support from foreign investors and legal experts in international financial institutions as it meant more institutionalized and predictable means of pursuing claims against host states. The promotion of foreign investment into the global South also came to be associated with a new developmental purpose, which lent a new impetus behind the development of investment rules.

Yet developing countries continued to exert influence over the international agenda with respect to investment rules. Post-independence states exercised their claimed right of expropriation as decolonization processes came to an end while also championing alternative standards of investment rules through the NIEO. Many developing countries also abstained from the ICSID Convention and sought to strength regional economic alliances to combat the economic strength of northern partners. Therefore, no single approach to, or understanding of, investor rights claimed hegemony in the international arena. Thus, while capital-exporting states attempted to forge a consensus on international investment law in the postwar period, the contradictory and inconsistent way in which investment rules developed in the postwar era reflected the influence of host states.

### **4.3 Neoliberalism and Contemporary IIAs**

The growth of multinational corporations and increasing trends toward the outsourcing of production activities in the 1970s and 1980s lent greater impetus behind the push for more stringent investment protections (Levy 2005). Global economic restructuring was aided by, and in some ways drove, the emergence of neoliberal economic philosophy as a guiding framework for government policy throughout much of the developed and, eventually, the developing world. Towards the 1980s, growing economic constraints drove many developing countries to include foreign investment promotion as a central pillar of development strategies. Prominent developmental discourses increasingly stressed investment protection and liberalization as a necessary means to attract needed foreign capital and technologies. As will be discussed, this significantly weakened the traditional resolve of many countries, particularly in Latin America, to resist the imposition of stringent investment rules and opened up unprecedented opportunities for capital-exporting states to strengthen international consensus on investor-state dispute settlement.

Because of the protectionist policies adopted by Latin American countries in the decades prior, foreign investment flows into the region declined dramatically throughout the 1970s. Governments therefore relied increasingly on loans from international banks to fill growing capital needs. Yet as Latin American economies began to falter, international financial institution and commercial bank lending became a slow trickle. Governments therefore turned to attracting private investment to meet their capital needs and began liberalizing domestic foreign investment laws by streamlining review and approval

processes, reversing limitations on equity participation and relaxing technology transfer requirements (Baker and Holmes 1991, 21).

At the same time, the ascendance of neoliberal economic philosophy in the global political economy was ongoing. Neoliberalism, which stresses the importance of freeing market forces as a means to achieve an efficient distribution of resources, has its origins as Tamara Lothian notes, in, “the world of the American technocracy, established in government and in the majority of multilateral banks and, more importantly, the world of the American universities, especially the graduate economics departments where so many candidates for Latin American elite status have trained” (1995, 175). Neoliberal thought came to inform much of the discourse and lending practices of the world’s most prominent international financial institutions by the end of the 1970s, and was partially internalized by Latin American political elites. Most notably, the so-called Washington consensus informed the stabilisation programs and subsequent Structural Adjustment Programmes (SAPs) formulated by the IMF to promote economic restructuring in developing countries suffering from heavy debt burdens and domestic capital shortages. SAPs included measures aimed at the privatization, liberalization and deregulation of domestic economies, measures that were argued to enhance local productivity and competitiveness. SAPs also required the adoption of additional incentives to attract foreign investment under the justification that foreign investment was good for domestic economic growth (Sunkel and Zuelta 1990, 37; Hilson and Haselip 2004, 28; Stiglitz 2002). This served to buttress the image of foreign investment as an engine of economic growth.

Beginning with Chile in the late 1970s, Latin American governments came to embrace neoliberal reform packages. As is illustrated in the cases of Argentina and Ecuador in chapters five and six respectively, this led to a significant restructuring of Latin American political economies. It also had an important impact on the structure and objectives of regional arrangements. For instance, the Andean Group amended its foreign investment code in 1987 with Decision 220, which loosened the national jurisdiction requirements over investment disputes. Decision 291 adopted in 1991 further reduced restrictions on providing foreign investors special treatment and derogated decision-making authority over the treatment of foreign investors to member governments (cf. Pate 1988). This amendment provided member states greater flexibility to adopt investment promotion and liberalization measures. In 1991, Argentina, Brazil, Paraguay and Uruguay also launched negotiations towards what would become El Mercado Comun del Sur (Mercosur), which aimed to establish between the countries a single market based on free trade, macro-economic and trade policy coordination, and a harmonization of economic legislation. Notably, Mercosur included two measures aimed at harmonizing foreign investment policy. This included the Colonia Protocol, which provided that all member states will permit and treat investment on a basis that is no-less favourable to domestic investors and foreign investors based elsewhere, instituted bans on expropriation and granted jurisdiction to ICSID over investor-state disputes. It also included the Buenos Aires (or ‘Third Parties’) Protocol, which forbade members from granting investments from investors based in third-party countries more favourable treatment than that granted to investors from member states (Rowat et al. 1997, 87).

As developing countries internalized the notion that foreign investment was good for development and competed increasingly for foreign capital, developed countries converged on a standard set of rules related to investment protection and liberalization. This was exemplified by the adoption by the United States in the mid-1980s of the BIT model made popular by European countries. BITs then became an increasingly popular means through which to secure consensus with developing country partners on the treatment of foreign investment throughout the 1990s. Facing greater pressure to adopt reforms that would signal their creditworthiness and reassure foreign investors that their assets would not be expropriated (Rodrik 1996, 28), Latin American countries began to sign on to investment agreements at an increasing rate.

The competitive pressure to attract foreign investment also encouraged developing countries to offer greater incentives. This second generation of BITs therefore included more stringent standards on investment protection and liberalization. Driven by the interests of domestic business groups, developed country governments pushed their developing partners to agree on investor-state arbitration clauses and expanded liberalization standards. For example, ‘foreign investment’ was often defined as broadly as possible in order to accord protection to all conceivable forms of investment (Subedi 2005, 97). By 1987, the majority of BITs included investor-state dispute resolution provisions, many of which granted consent to ICSID or UNCITRAL arbitration (Pauwelyn 2005, 30). For the most part, Latin American countries continued to insist that recourse to third-party arbitral tribunals be granted only after a genuine attempt at resolving the conflict in domestic courts had been made and an initial waiting period satisfied, reflecting the legacy of the Calvo Doctrine. However several countries made

exceptions in their agreements with the United States. The 1991 Argentina-U.S. BIT, for instance, provides foreign investors unqualified access to investor-state arbitration. This agreement, to some critics, signalled the end of the Calvo Doctrine's influence in the region (Subedi 2005, 96).

The fall of the Soviet Union in 1989 increased the bargaining power of the United States and European countries vis-à-vis the developing world in international institutions. Across the course of the 1990s, a new developmental discourse emerged that was more focused on issues of good governance following the principles of liberal democratic practice advanced by Western countries. In this discourse, the persistence of high unemployment, poverty, income inequality and the rise of black market and criminal networks in the developing world were framed as resulting from the lack of effective governance rather than as symptoms of the displacement caused by neoliberal policies. As Demmers et al. argue (1995,1),

it was not the neoliberal model that was to blame for the lack of progress, but rather the immature, corrupt and inefficient state administrations. From the early 1990s onwards, the call for *less* state has gradually been substituted by a call for a *better* state (original emphasis).

This was not a call for the return of the Keynesian welfare state, but rather an attempt to inject liberal democratic and capitalist principles further into the shrunken state apparatus.

Notions of good governance therefore usurped purely economic considerations as the primary conditionality for loans in the World Bank, IMF and other development assistance institutions. 'Good governance' was promoted as a non-ideological and apolitical project involving technical interventions aimed at building accountable and

transparent governance institutions (Demmers et al. 1995; Biglaiser and Derouen 2005, 52). This discourse served to further legitimate the extension of investment rules internationally (which also claimed to be technical, apolitical solutions) as it stressed the role of host countries in providing a stable investment climate for FDI according to the expectations of Western countries.

The ICSID Secretariat, IMF, World Bank and UN bodies such as UNCTAD therefore became important players in promoting the conclusion of second-generation BITs, either directly or indirectly.<sup>27</sup> The UNCTAD Secretariat, for instance, launched a *Programme on International Investment Agreement* in the 1990s to promote BITs by providing technical assistance, logistical support and funding for countries interested in undertaking BIT negotiations. It also facilitated meetings between interested countries for BIT negotiations. In January 1999, the UNCTAD Secretariat in collaboration with the Group of Fifteen (G-15) and the United Nations Development Program (UNDP) hosted a meeting of BIT negotiators of interested members of the G-15 near Geneva. This resulted in the conclusion of three BITs and the initiation of two BIT negotiations. It hosted similar meetings in Geneva in January 2000 that brought together six developing countries, resulting in eight BITs. A round of BIT negotiations was also held in Lima, Peru in March 2000 that resulted in two BITs and a further round was held in Japan between African, Asian and Latin American countries that resulted in 22 new agreements. The majority of these meetings were financed by European countries, while the round of negotiations in Peru was funded by the Government of Canada (UNCTAD 2000, 4).

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<sup>27</sup> It is important to note that UNCTAD was originally created by developing countries within the United Nations to balance the integrationist projects championed by developed countries, including the GATT. See Helleiner (2009).

Though the United States was a relative newcomer in the formulation of BITs, its adoption of a competitive bilateral approach had a considerable impact on the expansion of investment rules in Latin America, particularly when combined with the pressure exerted by international financial institutions to liberalize domestic investment markets. As one US BIT negotiator observed (as cited in Subedi 2012, 83),

BIT partners turn to the US BIT with the equivalent of an IMF gun pointed at their heads; others may feel that, in the absence of a rival super power, economic relations with one that remains are inevitable. For many, a BIT relationship is hardly a voluntary, uncoerced transaction. They feel that they must enter into the arrangement, or that they would be foolish not to, since they have already made the internal adjustments required for BIT participation in order to comply with demands made by, for example, the IMF...A BIT negotiation is not a discussion between sovereign equals...it is more like an intensive training seminar conducted by the United States, on US terms, on what it would like to comply with the US draft.

The 1994 North American Free Trade Agreement (NAFTA), signed between Canada, the United States and Mexico exemplified the power the US exerted over the IIA agenda in the Americas. Mexico's interest in the agreement stemmed from its desire to strengthen inbound foreign investment flows, which the country's neoliberal restructuring in the years prior had failed to stimulate.

NAFTA's Chapter Eleven on investment was the first free trade agreement to include investor-state arbitration mechanisms. It also established new standards on investment liberalization. For instance, whereas previous agreements largely retained

governments' abilities to vet investments at market-entry stages, NAFTA granted pre-establishment rights to foreign investors. It also included new national treatment obligations and further reduced the scope for performance requirements (Kurtz 2002). US negotiators pushed Canada and Mexico to agree to these standards in order to placate the demands of US-based transnationals. The standards came to inform Canada's own approach to investment rules as well as the standards advanced by some Latin American partners in their negotiations with others, including Chile and Colombia.

Having secured NAFTA, the United States and Canada sought to push forward a multilateral investment agreement built on NAFTA standards. In 1995, the OECD commenced negotiations towards the Multilateral Agreement on Investment (MAI) as a response to the rapid growth in investment flows and the unilateral and bilateral liberalization of national investment markets. Canada supported US proposals to model the MAI after NAFTA provisions, however the negotiations reached an impasse when the United States refused European and Canadian requests to exempt cultural and linguistic industries from full coverage and an emerging economic crisis crippled Asia, temporarily diluting support for further investment liberalization. The United States tried again when governments of the Western hemisphere took up negotiations toward a Free Trade Area of the Americas (FTAA) in the late 1990s. However, Brazil and its Mercosur allies sought to dilute investment protections in the interest of preserving policy autonomy. Parties were also staunchly divided on a number of trade-related issues (namely, agricultural subsidies in the United States and Canada, trade remedies and anti-dumping measures), causing the negotiations to fall apart (Kurtz 2002, 759).

With the continued failure of multilateral initiatives to formulate truly global standards on investment protection and liberalization, the 1990s witnessed a veritable explosion of BITs. By the end of 1999, 1,857 BITs were in force, 40 percent of which were between developed and developing countries. This is in comparison to the 102 BITs that had been signed by the end of the 1980s and the 69 BITs signed by the end of the 1970s (UNCTAD 2000, 3). Approximately 300 BITs were signed by Latin American countries by the end of the 1990s, 93 percent of which were signed during that decade (Ibid., 15).

As subsequent developmental discourses stressed the importance of IIAs as tools of effective economic governance, the controversies on which IIAs were founded faded from public memory. IIAs came to be viewed as a technical-legal solution to developing countries' domestic capital shortages and an efficient means of signalling governments' commitment to maintaining stable investment environments. A new, more austere generation of BITs were therefore introduced as repeated attempts to consolidate a multilateral framework for investment protection and liberalization failed. While this generation of BITs demonstrates important consistencies across models, the legacy of the Calvo Doctrine in Latin America and the unique processes involved in bilateral negotiations has led to some variation.

#### **4.4 A Rising Legitimacy Crisis or Further Entrenchment?**

As the number of BITs with ISDS provisions proliferated in the 1990s, the number of ISDS cases began to mount against host states. From 1987 to 2014, 608 cases

of investor-state arbitration were brought against 101 countries.<sup>28</sup> In 2014, 60 percent of all new cases were brought against developing or emerging economies, a significant increase from the historic average of 28 percent. This disproportionate figure is made all the more notable when considering the fact that developing countries only recently became a significant destination for foreign capital. That is, while FDI flows were concentrated largely among advanced economies at the beginning of the 1990s, only relatively recently have developing countries become major FDI recipients, the majority of which emanates from advanced economies (Birch and Halton, 2001; Spears 2010, 1043).

This wave of ISDS cases has prompted the emergence of a legitimacy crisis in various parts of the globe as a growing number of governments and civil society groups contest the power granted to foreign investors under the agreements. The ambiguous language contained in investment treaties and ISDS mechanisms is a particular source of renewed controversy as it allows third-party arbitrators, who are predominantly trained in commercial law, ample room to interpret investment rules. More than 50 countries in the developed and developing world are therefore revising or have revised their IIA models to limit the rights afforded to foreign investors or deter fraudulent investor claims. These revisions include, for instance, clarifying the scope of investment rules, reducing the kinds of foreign investment covered by the treaty, and adding specific interpretations to clarify signatory governments' intentions with specific guarantees. Indonesia, South Africa, Ecuador, Bolivia and Venezuela have also terminated IIAs and / or withdrawn

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<sup>28</sup> This number may be higher as non-ICSID cases may not be publically disclosed. ICSID is the only institution with mandatory obligations to release case information.

their consent to the ICSID convention, while Botswana and Namibia are reconsidering their own approaches to BITs (UNCTAD 2015, 109-110).

However, this is not to say that IIAs have fallen out of favour in the majority of developed and developing countries. Advanced economies such as Canada, the United States and European Union members continue to champion the establishment of BITs as a means to attract and promote foreign investment flows. In the developing world, a number of countries have internalized the notion that BITs are good for development. In Latin America, countries have become divided in their approach to investment rules, which reflects the divergent attitude towards neoliberal economic policies found between neoliberal and post-neoliberal countries. Chile, Colombia and Mexico for example are now signing NAFTA—like investment agreements with a variety of advanced economies and with Southern partners. Brazil and Ecuador are also negotiating investment agreements, however they are modified versions meant to more strongly preserve state rights and citizen interests vis-à-vis foreign investors. For instance, they do not provide for ISDS as a dispute resolution procedure and instead return to traditional state-state approaches. They also grant explicit recognition of governments' obligations to human rights, environmental preservation and other sustainable development goals. Whether these agreements will preserve state rights is questionable, however their emergence has meant that the global assortment of BITs is demonstrating increasing differentiation.

Due to the explosion of ISDS cases, a veritable industry of legal experts, claims evaluators and arbitrators has been established. Legal and administrative costs average over US\$8 million per ISDS case and have exceeded US\$30 million in some cases (e.g. Chevron's claim against Ecuador over the Lago Agrio class action case). International

lawyers in prominent law firms charge as much as US\$ 1,000 per hour while arbitrators earn up to US\$1 million per case. However, this industry is dominated by a small group of firms based in Western European states (mostly the US and UK). Three top international law firms (Freshfields in the UK, White and Case and King and Spalding both in the US) have been involved in the majority of disputes. Moreover, only 15 arbitrators (almost all from Europe, the US and Canada) have sat on 55 percent of all known ISDS cases. Many arbitrators also act as corporate counsel, which has raised concern over potential conflicts of interests amongst host states (Olivet and Eberhardt 2012).

UNCITRAL and ICSID face growing pressure to modify arbitral rules to reduce the likelihood of a conflict of interest and to increase the transparency of dispute resolution proceedings. In the United Nations, pressure to reform ISDS rules has also come from internal sources. In 2000, UNCTAD identified the restriction of policy space as a potential barrier to development in its publication *International Investment Agreements: Flexibility for Development*. This booklet explicitly recognized the importance of ‘flexibility for development’ in IIAs – the function of flexibility being “to adopt IIAs to the particular conditions prevailing in developing countries and to the realities of the economic asymmetries between those countries and developed countries, which act as the home to most TNCs” (UNCTAD 2000, 1). UNCTAD built on this recognition with the São Paulo Consensus forged in 2004, which called on states to “take into account the need for appropriate balance between national policy space and international disciplines” (Gallagher 2005, 10). UNCTAD has therefore led reformatory efforts to increase transparency in investor-state dispute proceedings. As a response to

this pressure, UNCITRAL developed a set of rules to enhance the transparency of ISDS cases, which came into effect in 2015 during the Convention on Transparency in Treaty-based Investor-State Arbitration (UNCTAD 2014).

ICSID similarly undertook efforts to enhance the transparency of its ISDS proceedings and now releases transcripts of awards and key decisions. However it cannot be said that ISDS proceedings are entirely transparent in ICSID and UNCITRAL tribunals. Proceedings are still held behind closed doors and parties are under strict confidentiality orders not to release court materials during the case. Transcripts of legal proceedings are often released well after the decision has been taken while civil society groups are limited to submitting briefs in the form of *amicus curiae* should they aim to intervene in the legal proceedings. In Latin America, countries have undertaken efforts to establish an alternative dispute resolution mechanism under the auspices of UNASUR. Although it is still in the final stages of development, it is expected that this centre will encourage local dispute settlement, have stronger transparency mechanisms and include an appellate mechanism so that disputing parties may have awards reviewed on broader terms than what is currently available under UNCITRAL and ICSID rules. However, whether countries will be able to persuade foreign investors to consent to UNASUR arbitration is questionable given existing preferences for ICSID arbitration.

It remains to be seen whether the alternative investment treaties and arbitration mechanisms advanced by some states will better protect domestic interests from the claims of foreign investors. However, calls to reform the global assemblage in which IIAs are situated demonstrate a growing awareness that disputes involving a state as

respondent necessarily evoke considerations of public law and public interest that are distinct from an arbitration between private commercial parties.

#### **4.5 Conclusion**

The early formulation of international investment law reflected the tension between the attempts of colonial states to impose favourable standards regarding the treatment of foreign-owned assets and the rejection of these standards by non-European peoples. Resistance to European standards strengthened as statehood was extended throughout the Americas, which provided Latin American governments a legal basis on which to advance their own interpretations in emergent international institutions. The rise of the United States as a leading global power in the inter-war period lent a new impetus behind the push for stronger investment protections. Yet the consolidation of investment rules was significantly limited by the alliances created by Latin American countries and newly independent states in Asia and Africa. International investment law therefore came to reflect the productive friction between the universal standards advanced by capital-exporting states and the alternative standards developed by local governments and intellectuals in the global South.

Yet the expropriation of foreign-owned assets by newly independent countries was perceived by capital exporting states as evidence of the unpredictability of government action in non-Western countries. This lack of predictability in economic policy increasingly came to be identified in developmental discourses as a problem in need of addressing through international legal interventions. Facing resistance to the solidification of investment rules, Western countries also sought to separate the property rights of their nationals abroad from issues related to the sovereignty of host states. This

was aided in the post-war era by the interest of international financial institutions and international legal associations in facilitating foreign investment promotion. As global economic restructuring caused investment flows to grow, developed country governments faced mounting pressure from the international business community to provide efficient solutions to investment disputes. Policymakers and the international legal community increasingly spoke of investor-state disputes in technical-legal terms as commercial matters involving the interpretation of international commercial law rather than political disputes involving the application of public law and public policy. Adjudication over investment disputes, legal experts argued, was best vested in the hands of third party legal bodies that were detached from political influences and possessed the necessary technical-legal expertise. This particular logic has come to underpin the legitimacy of contemporary IIAs and the international arbitral institutions charged with overseeing the resolution of investment disputes. It also has allowed IIAs to enrol a greater number of actors into their global networks.

In Latin America, the nationalist logic informing the contestation of investment rules was swept aside by recurrent debt crises, during which ISI models and governments' supposed economic mismanagement were targeted by international financial institutions and lenders as the causes of the region's financial crises. The subsequent adoption of neoliberal SAPs coincided with the signing of unprecedented numbers of IIAs as governments aimed to signal their commitment to (neo)liberal economic policy. As an internationalist logic crept into state bureaucracies, governments also put aside their traditional reticence to surrendering state sovereignty to third-party arbitral institutions. The foundational controversies of IIAs therefore became hidden from public view as

investment rules were increasingly perceived to be a necessary means to attract foreign capital. This has allowed IIAs to enrol a greater network of actors and institutions, which is essential if IIAs are to have force and effect. Only in the last decade have the controversies surrounding IIAs come under renewed public scrutiny. The legitimacy crisis that threatens to envelope the global IIA assemblage has helped reveal the gaps and contradictions inherent within it. In the next two chapters, I examine how governments in Argentina and Ecuador have sought to exploit these gaps to defend domestic (and political) interests from the claims of foreign investors. In doing so, I demonstrate how IIAs and their global networks influence state decision-making in practice and the various strategies states adopt to ward off such impacts.

## **5 Chapter: IIAs and the Defence of Policy Space in Argentina**

Argentina is a signatory country to 55 BITs and several regional investment treaties due primarily to the country's membership in Mercosur. The Argentine government has also faced the greatest number of investor claims out of any country in the world with 58 known ISDS cases. The majority of these disputes were brought as a response to the emergency measures introduced by policymakers to alleviate the symptoms of the country's 2001 economic crisis. The high number of cases brought against Argentina demonstrates the power IIAs afford to foreign investors to challenge government policy. Indeed, conventional critical scholars often reference investor claims as evidence of the structural constraints IIAs induce on governments' policy autonomy. Yet this ignores the possibility that state actors will develop strategies to protect their policy space largely because the role of state and non-state actors under IIAs is not adequately captured by theoretical approaches that view IIAs cohesive global structures imposing constraints on relatively weak states.

Examining Argentina's experience under IIAs provides the opportunity to address two neglected aspects of the relationship between IIAs and policy space, namely how IIAs impact policy space in practice when the agency of domestic actors is factored into analyses and the mechanisms through which IIAs shape perceptions of policy space in practice. In this chapter, I explore these facets while assessing whether common assumptions about the decline of policy space hold in the context of Argentina. As previously noted, critical scholars assert that IIAs deter governments from using policies that conflict with investment rules; that IIAs provide foreign investors the ability to challenge government policy and therefore shrink government policy space; and, that

IAs reduce the capacity of governments to fund policy choices in the future after having broken with investment rules.

Policy space is multiscalar in that it exists at different levels of the political (local, subnational and national). I focus my analysis on the struggle over national policy space as it is the national government that is held liable for breaks from investment rules and therefore its policy space is more directly impacted by IAs. I do, however, recognize the role of provincial governments in aiding or hindering the defence and exercise of national policy space. I also focus predominantly on exposing the role state actors play in shaping the impacts IAs have on policy space and their relationships with more progressive or marginalized social groups. This will allow me to assess the extent to which the government's defence strategies stem from citizen demands and, in turn, whether IAs significantly limit governments' abilities to respond to public interests. Further analysis should focus more explicitly on the role of provincial governments and private-sector actors play in contesting or reinforcing the impacts of IAs in this context.

This chapter is divided into five parts. The following section explores the context in which ISDS cases were brought against Argentina. It focuses particularly on disputes brought in the wake of the country's 2001 economic crisis as this represents the majority of cases brought against the country. Understanding the impetus for these disputes requires an understanding of the regulatory standards established during Argentina's neoliberal restructuring in the 1990s, Argentina's economic collapse in 2001 and the state's attempts to renegotiate contracts with foreign investors in the wake of the crisis. The third section provides a more detailed examination of the strategies adopted by Argentina to defend its policy choices from the claims of foreign investors. Argentine

officials made an early decision to fight under the parameters of existing investment rules. Its strategy therefore focused on using different domestic pressures to thwart investor claims while leveraging gaps in the enforcement mechanisms of the global IIA assemblage to delay award payments. This has forced foreign investors to compromise in the claims that they made while allowing Argentina to defend the interests of the most impoverished citizens. The subsequent section focuses more explicitly on critically assessing the factors that gave IIAs power over policy decisions in Argentina as well as the competing factors that helped structure the state's response. It focuses particularly on the role of ideas and material factors and how such factors interacted with sociopolitical and institutional conditions to shape the impact that IIAs had on policy space in this time period (2001 – 2015). The final section concludes with an analysis of what Argentina's experience under IIAs tells us about the relationship between IIAs and policy space.

I find that IIAs did not constrain policy space consistently across time. IIAs did not deter government officials from adopting policies that went against IIA obligations to placate the symptoms of an escalating economic and political crisis. Rather, the chaos and uncertainty caused by the crisis, combined with growing demands from civil society for a solution, meant that policymakers assigned less priority to adhering to investment rules than instituting emergency measures they perceived were necessary to address the crisis. This decision however resulted in 44 costly and protracted legal battles with foreign investors, the majority of which were brought by firms active in the country's utility sector. Early on, a decision was made to fight the claims under the parameters of prevailing rules, despite the government's scepticism of third-party arbitral bodies and

their perceived commercial bias. This decision meant that the state's defence options were in some ways constricted by the legal channels set out by IIAs and arbitral rules.

The election of Nestor Kirchner in 2003 and his commitment to a post-neoliberal agenda had a considerable impact on Argentina's defence strategy as Kirchner sought to leverage domestic pressures to pressure many foreign investors to drop their claims. This included promising foreign investors new contracts in exchange for withdrawing their claims. In most instances, foreign investors agreed to increasing tariffs charged to wealthy and industrial sectors in exchange for a commitment to keep charges artificially low for poorer sectors, which was an important policy goal for the Kirchner administration and provincial governments. However, renegotiations with foreign investors were made possible by the country's post-crisis economic recovery, which meant higher industrial demand increased the profitability of utility firms. Domestic economic performance can therefore play an important role in buttressing the success of governments' defence strategies. In ISDS proceedings, Argentine attorneys argued that the emergency measures were necessary to meet the government's human rights obligations and that foreign investors must bear part of the adjustment burden as citizens and domestic businesses had done. This argument was received inconsistently by arbitral tribunals, which suggests that arbitrators engage with IIAs differently and that foreign investors are not always successful in leveraging IIAs to make demands on the state. How arbitrators translate IIA provisions help determine the degree to which the agreements effectively constrain policy space. State lawyers also proved more successful in their legal arguments over time, which suggests that capacity building and learning play an

important role in enhancing governments' abilities to mitigate the costs of investment disputes.

Overall, Argentine officials and state lawyers had some success in mediating the costs of investor claims using legal-procedural defence strategies. State officials also sought to exploit gaps in the global IIA assemblage, particularly related to its lack of an effective enforcement mechanism, to time award payments according to their interests and to negotiate discounts on the compensation owed. Their willingness to challenge tribunal orders stems from their scepticism of institutional bias amongst arbitrators and arbitral bodies. However, this has not been without reprisals from investors' home governments and the international financial community, which have decreased the country's access to international capital markets. This is particularly detrimental in light of Argentina's recurrent inflationary pressures and slowing economic growth. Yet past experiences in ISDS cases did not deter the Kirchner governments from nationalizing foreign-owned firms following the crisis, which resulted in new investor claims. The left-leaning ideological commitments of the Kirchner governments, particularly their commitment to reassert state sovereignty over the domestic economy, meant that policymakers were less likely to support the neoliberal principles underpinning IIAs and the authority of third-party arbitral tribunals, particularly if it interfered with the advancement of development objectives. This suggests that IIAs have only a weak deterrent effect in countries governed by regimes that contest the authority of investment rules and that government ideology helps shape the degree to which IIAs will effectively constrain policy space. However, Argentina's real and perceived dependence on foreign

capital, expertise and technology has limited how far policymakers in the Kirchner administrations were willing to go to challenge the global IIA assemblage.

Moreover, investor claims are likely to have a negative impact on the state's capacity to fund future programs and policies. 18 awards ranging from US\$2 million to US\$186 million (plus interest) have been rendered in favour of foreign investors. This is in addition to the legal costs of mounting a defence. Although the state's defence strategy was successful in reducing the overall costs of the disputes, the cumulative impact of these awards is well beyond the annual funding dedicated to several national programs, such as the conditional cash transfer program *Jefes y Jefas de Hogar Desocupados*.

Argentina's experience with IIAs demonstrates the role that causal and normative ideas and material resources play in shaping the impact that IIAs have on policy space. The varying textual properties across IIAs and how they engage with different actors and institutions helps to shape the extent to which they hold power over domestic policymaking processes. Argentina's experience also demonstrates that domestic economic performance can buttress or weaken the state's defence strategy against investor claims. These factors intersected with policymakers' causal and normative ideas to shape the unique impact of IIAs on domestic policymaking processes, which supports the conclusion that the impact of IIAs are likely to vary across time and space according to how they engage with local contexts and actors as well as the network in which they are situated.

## **5.1 Context and Conditions: The Neoliberal Shift and Privatization Process**

In the 1990s, Argentina underwent a dramatic period of neoliberal adjustment led by Carlos S. Menem (1989 – 1999). Menem was elected in 1989 as a candidate of the Partido Justicialista (PJ), the Peronist party traditionally associated with populism and state intervention (Rodriguez-Boetsch 2005, 305; Grugel and Riggirozzi 2007, 90). The previous administration of Raúl Alfonsín and the Radical Party (1983 – 1989) oversaw Argentina's return to democracy after years of repressive military rule. To overcome the country's growing foreign debt crisis, Alfonsín complemented heterodox economic policies with liberalization initiatives that laid the groundwork for neoliberal policies. The country however continued to sink into economic stagnation as capital flight and hyperinflation in 1989 crippled the economy (Silva 2009, 57). That year, Menem campaigned in the national elections with promises to maintain populist policies and end the political corruption that had been a common feature of preceding governments. Once he was elected, however, Menem appointed members of the right-leaning Peronist faction and prominent members of the business community to key government posts, which helped push forward the adoption of an internationalist logic in state institutions (Smith 1991, 51). Foreign creditors like the IMF, the World Bank and the United States government (who supplied technical advisors) also made economic restructuring and liberalization a requirement of renegotiating Argentina's massive foreign debt and opening access to international capital markets. The Menem government therefore began adopting sweeping neoliberal reforms aimed at rejuvenating growth by restructuring the Argentine economy (Silva 2009, 57).

Menem argued that overcoming the 1989 crisis required “a tough, costly, and severe adjustment,” requiring “major surgery without anesthesia” (as originally quoted in Smith 1991, 53). Central to the package of neoliberal reforms advocated by the IMF and economic partners in Argentina was the privatization of state-owned enterprises (SOEs). Privatization, advocates argued, would reduce state spending, improve the efficiency, quality and reach of services and stimulate the adoption of modern technologies (Baer and Montes-Rojas 2008, 325). Other reform initiatives included reductions to state-related employment, welfare system reform, administrative decentralization, and deregulating and liberalizing the Argentine economy through trade and investment agreements (Villalón 2006; Di Tella 1990). As discussed in chapter four, IIAs were gaining popularity in the developing world as a means to attract foreign capital. Beginning in 1990, the Menem administration signed 55 BITs in rapid succession with a diverse range of developed and developing country partners (UNCTAD 2015). Menem argued that such agreements would establish the clear and equitable rules necessary to ease foreign investors’ concerns and therefore raise and conserve adequate levels of needed foreign investment.<sup>29</sup> In 1994, Argentina also ratified the ICSID Convention, securing the consent investors would need to take claims to ICSID arbitration.

The Menem administration was particularly concerned with encouraging foreign investment in telecommunications, transportation, power and water and sanitation to reduce state spending and improve services that had considerably deteriorated in the last decades (Post and Murillo 2013, 118). In their bid to reduce state spending, national state

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<sup>29</sup> When presenting the Argentina – United Kingdom BIT in the Cámara de Diputados de la Nación, Menem asserted: “in the current world, the only way of establishing and conserving adequate international flows of capital is to formulate and maintain clear, equitable rules and institutions that create a satisfactory climate for investment.”, author’s translation. See Diario de Sesiones, Diputatodes de la Nacion, 29 Reunión, 9 sesión ordinaria (September 2 1992).

officials also pushed provincial governments to privatize public services administered at the provincial level, including banks, electricity distribution systems and water and sanitation services. Deficits at the provincial level and the dependence of provinces on federal fiscal transfers were seen as contributing to macroeconomic stability. Under Argentina's constitution, the country's 23 provinces and the autonomous district of Buenos Aires are granted a significant amount of political and administrative autonomy. Many provincial governments opposed Menem's neoliberal program and resisted the privatization program.<sup>30</sup> The national government had few means of coercing provincial governments to follow through with privatizations other than revising revenue-sharing arrangements to reduce federal transfers and directing World Bank and Inter-American Bank loans to fund utility upgrades in provinces that adhered to the neoliberal program. In the end, only 14 of the 23 provinces (including Buenos Aires) privatized their entire electricity distribution systems while 12 privatized their urban water and sanitation systems (Post and Murillo 2013, 117-118; Post 2014).

The provincial governments that did undertake the privatization process adopted the concession contract model, which kept the infrastructural assets in state hands while assigning investment and operational responsibilities to new private-sector owners. This model was favoured by international financial institutions, particularly the World Bank, and was also adopted by the national government. Independent regulatory agencies were tasked with monitoring investors' compliance with their contractual terms. The primary

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<sup>30</sup> Remmer and Wibbels (2000) find that provincial variation in adopting neoliberal reforms, particularly reductions in provincial bureaucracies and spending is due primarily to different needs and capacities to maintain subnational patronage networks. Many provinces protected and expanded patronage bases at the expense of national economic adjustment. This in turn forced the national government to adopt policies of 'overadjustment' that contributed to high unemployment, political tensions and electoral losses for the governing party.

interest of governments at both levels was ensuring that concessionaires abided by their contractual commitments to upgrade and expand service delivery to poor regions and, in the electricity distribution sector, avoiding electricity blackouts (Post and Murillo 2013, 118).

A central piece of the Menem government's privatization project was the *Currency Convertibility Plan*, adopted in March 1991. This Plan pegged the Argentine peso to the US dollar in order to overcome Argentina's traditional volatility to high inflation rates and give confidence to foreign investors (Haselip and Potter 2010, 1168). This scheme was also reflected in concession contracts, particularly in the utilities sectors where rates were fixed in US dollars (Stanley 2006, 6). By 1993, the sale of state assets generated capital receipts amounting to US\$18 billion (Rodriguez-Boetsch 2005, 302). The first years of the country's neoliberal adjustment (1990-1994) were therefore deemed a success as the country's annual average growth rate reached 7.7 per cent and high rates of investment contributed to macroeconomic stability (Haselip 2005, 78; Villalón 2006, 140). Argentina became the poster child of successful neoliberal reform as the international press, G7 governments and international financial institutions lauded Menem as a champion of effective government to be emulated by developing countries globally (Rodriguez-Boetsch 2005, 302).

In reality, state negotiations with foreign investors throughout the privatization process exhibited blatant forms of corruption, favouritism and clientelism (Villalón 2007, 140). Pressure from international financial institutions and a deep desire to establish its neoliberal credentials motivated the Menem administration to rush the privatization process. Officials tried to attract rapid inflows of foreign investment with generous

contracts that limited the power of provincial governments to introduce regulatory changes (Stanley 2006). Service fees were often increased prior to privatization to make SOEs more attractive to foreign purchasers. This move was intended to guarantee a comfortable level of revenue to the new owners, however it also generated public skepticism over the privatization process. Many investors also sought to reduce operating costs with drastic cuts to their labour force. For instance, seven SOEs employed approximately 222,800 workers in 1990, which was reduced to only 99, 000 workers after all but one of the companies were privatized. This created a massive pool of unemployed persons and eroded the strength of unions that had historically played an important role in channelling the voices of the working class (Rodriguez-Boetsch 2005, 306; Villalón 2007, 141).

The ascendance of neoliberal ideology and its internationalist logic in Argentina's political apparatus altered the balance of power between labour and corporate interests at the national level. Since the 1970s, Argentina's domestic private sector had thwarted attempts by the national government to liberalize the economy. Private sector groups also opposed Menem's privatization plan in its early years and attempted to destabilize or sabotage privatization programs by lobbying or bribing politicians, provoking labour unrest, funding collective action initiatives and refusing to engage in business with newly privatized companies. Yet by 1992, private sector opposition towards privatization eroded as firms began to see improvements in economic indicators and began to compete

for sales contracts. The political and institutional contexts required for the consolidation of neoliberal ideas in the national government had therefore been laid.<sup>31</sup>

As the private sector reluctantly adjusted to the neoliberal program, the traditional alliance between unions, the PJ and the working class forged by Juan Perón during his presidency in the 1950s also eroded (Villalón 2007; Silva 2009, 57; Torre 1989). Increasing unemployment and cutbacks to public services combined with continued practices of political corruption led to the emergence of new social alliances and forms of protest against neoliberal economics and political corruption. Across the mid-1990s, protests, town revolts and pickets grew in provinces that adopted privatization schemes. For the most part, demonstrators demanded job protection and the recreation of employment opportunities while denouncing ongoing political corruption. Yet demonstrations were sporadic and confined largely to impoverished urban neighbourhoods in the provinces of Santiago del Estero, La Rioja, Salta, Chaco, Entre Rios, Tucumán, Jujuy, San Juan, Córdoba, and Río Negro. They were also typically aimed at provincial governments and local political elites (Villalon 2007, 142; Silva 2009). While neoliberalism gained a strong footing in the national state apparatus, it was felt unevenly across provinces due to the resistance of provincial elites and the friction caused by the introduction of neoliberal policy.

As social unrest placed pressure on provincial governments to reverse neoliberal policies, little effort was given to maintaining the effectiveness and independence of regulatory apparatuses (Gerchunoff and Cánovas 1996; Rodriguez-Boetsch 2005).

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<sup>31</sup> For an excellent discussion of the private sector's opposition to neoliberalism in Argentina see Corrales, Javier. 1998. "Coalitions and Corporate Choices in Argentina, 1976 – 1994: The Recent Private Sector Support of Privatization," *Studies in Comparative International Development* 32 (4): 24 – 51.

Regulatory agencies were therefore subject to competing demands from investors, government officials and civil society groups for changes to the regulatory framework. Investors demanded the right to increase tariffs in order to generate greater revenue for reinvestment in service upgrades and expansion. Provincial officials however demanded delays in rate increases (even increases agreed upon in concession contracts), often in response to civil society demands, and for the levying of stiff penalties on firms for failing to make agreed upon investments. This was particularly true in the case of electrical utility firms who received large fines for electricity blackouts (Post and Murillo 2013).

External pressure and political ambitions had therefore motivated the Menem administration to adopt neoliberalism as a framework to guide social and economic policy. Yet these reforms were instituted in the presence of persistent political corruption that fed public scepticism. Reforms were also challenged by the practical limitations of advancing neoliberal restructuring in a highly decentralized state with a long tradition of patronage and an economy dependent on state-related employment. Reforms were therefore met with significant delays and opposition by many subnational authorities and social groups that continued to ascribe to a more nationalist logic. The social and economic dislocation caused by growing unemployment fed further social opposition to the privatization process. Anti-privatization protestors targeted provincial authorities and demanded reversals on privatization efforts and the creation of new employment opportunities. The friction created between attempts to institute neoliberalism and the oppositional forces it engendered at the sub-national level meant that neoliberalism's hold over the country was fragile, uneven and contested.

The early years of Argentina's neoliberal restructuring therefore left a dual legacy of particular relevance to understanding the context in which the country's ISDS cases arose. On one hand, the regulatory framework and contractual rights as well as Argentina's growing network of BITs established the legal basis on which foreign investors would bring claims against the national government. On the other, neoliberal restructuring created new social alliances that mobilized in opposition to the private sector purchasers of SOEs and pressured provincial governments for policy reversals. The country's domestic private sector, however, increasingly embraced neoliberal philosophy. Argentina's first ISDS cases as well as the ensuing wave of claims brought after the 2001 economic crisis must be understood against the backdrop of this friction.

#### **Pre-Crisis Claims (mid to late 1990s)**

Eight ISDS cases were brought against the national government in the years leading up to the 2001 crisis. The majority of these cases resulted from regulatory changes introduced by provincial governments in response to citizen demands. Two disputes arose where provinces refused to allow privatized water companies to increase tariffs on water services. The first claim was brought to ICSID in 1996 by Compañía de Aguas del Aconquija (CAA) and its France-based parent company Compagnie Générale de Eaux (CGE) who operated a water and sewage system in the Province of Tucumán.<sup>32</sup> The case is commonly referred to as Vivendi, after the French company that bought out CGE and assumed leadership of the case. As a result of privatization, consumers saw the cost of water rise by approximately 110 percent on average. Consumers also observed two periods in which the water provided was discoloured, raising concerns of

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<sup>32</sup> CAA and CGE v. Argentine Republic, Award, ICSID.

contamination. CAA was fined and the government advised the public not to pay their invoices. The province also expressed concerns that the original contract was obtained through corruption. After repeated attempts to renegotiate the terms of CGE's original contract, the province terminated the concession and took over operation of the facilities.

CGE responded by bringing the case to ICSID and accused the Argentine government of violating BIT provisions on fair and equitable treatment and expropriation in failing to intervene to prevent the province's actions. A similar case was brought in 2001 to ICSID by a US-based company, Azurix, over a dispute with the province of La Plata regarding a water concession contract purchased in the late 1990s. In both cases, companies accused provincial governments of putting political interests before contractual commitments in blocking tariff increases.<sup>33</sup>

Three additional cases were brought by electricity generation and distribution firms as a result of provincial action, yet related to the introduction of new taxes (e.g. stamp taxes) and fines. In Argentina, provinces generate tax revenue through stamp taxes, sale tax and property taxes. All other forms of taxation are left to the national government. Increases in stamp taxes were introduced in Santiago Del Estero, Neuquén, La Pampa, Chubut and Rio Negro to generate revenue in the face of declining fiscal transfers from the national government (Cuevas 2003, 5). Claims were brought by US-based companies Enron, Houston Industries and Spain-based Empresa Nacional.<sup>34</sup> The introduction of new

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<sup>33</sup> *Azurix v. Argentine Republic*, Decision on the Application of Annulment, ICSID, 1 September 2009, pg. 19 para 29; *CAA and CGE v. Argentine Republic*, Award, ICSID, pg 11 para 29 – 31.

<sup>34</sup> Enron brought a suit against Argentina in February 2001 concerning stamp taxes imposed by provincial governments in three concession areas. This claim was subsequently dropped following a settlement in Argentina courts, however Enron brought a second claim in 2003 seeking US\$ 543 million in compensation as a result of the Emergency Measures and other regulatory changes. See *Enron Corporation and Ponderosa Assets v. Argentine Republic*, award (ICSID case no. ARB/01/3 pg. 10 para 26 – 28. An award was rendered in the case of Houston Industries however it has not been made public.

taxes, investors argued, was tantamount to indirect expropriation. The majority of these cases however were dropped or discontinued following settlements with the national government. This speaks to the uneven impact that IIAs have across scales of the political. Provincial governments terminated the contracts with foreign investors while the national government was held responsible under IIAs, which suggests the policy spaces of provincial governments are more insulated from the constraints IIAs may impose.

The final group of pre-crisis claims related to contractual disputes between foreign investors and the national government. Lanco International, a US-based company, brought an ICSID claim against Argentina in 1997 after the government cancelled its contract for the operation of a port terminal in Buenos Aires. In addition, Siemens, a German technology company, secured a contract in 1998 for the provision of identity cards and the design and installation of a computer-assisted program meant to improve the country's immigration control system. After Menem's final term, the government of President De la Rúa tried to renegotiate the contract after allegations of corruption surfaced. The negotiations failed after Siemens refused to provide access to cost information. Siemens then commenced ICSID arbitration against Argentina in 2002, demanding US\$ 550 million in compensation. Argentina introduced evidence of corruption in the original contract's procurement, however the tribunal rejected the evidence on the grounds that it was untimely offered and awarded Siemens US\$ 271.8 million plus interest. While Argentina commenced an application for annulment, the US Securities and Exchange Commission published a report in which Siemens acknowledged that it had used US subsidiaries to transfer money to pay bribes to obtain contracts,

including the contract with the Argentina government. Siemens then withdrew its ICSID claim and the proceedings were discontinued (Tortorola and Gosis 2012, 18).

According to Argentine officials interviewed in 2014, the country was unprepared to address such litigations in international courts.<sup>35</sup> Though the Procuración del Tesoro de la Nación (Office of the Attorney General or PTN) was equipped with skilled lawyers, few were experienced in such areas of international litigation and possessed English language skills. In the first ISDS cases, the state was represented by the Ministry of Foreign Affairs and by outside co-counsel, including international law firms from the United States and United Kingdom. Efforts were then taken to build the PTN's in house capacity and it took over representation in ISDS cases by 2000 (Tortorola and Gosis 2012, 15). The result was that a permanent team of lawyers was established under the expanded PTN to deal exclusively with matters related to investment claims.

Only two awards of the seven pre-crisis cases were rendered in favour of investors: a US\$ 165 million award in favour of Azurix rendered in 2006 and US\$ 105 million in the case of Vivendi in 2007. The majority of pre-crisis claims were settled outside of formal arbitral proceedings or were amended to address measures taken during the ensuing economic crisis. Although settlements meant that investors withdrew their claims, the threat of ICSID claims became a method of achieving greater concessions from the government in the decade that followed. These early cases did, however, provide the impetus needed for the development of a specialized team of international investment lawyers in the PTN. This variety of institution-building as an outcome of investment disputes has thus far been neglected in approaches that do not give proper

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<sup>35</sup> According to two interviews conducted with former state attorneys of the State Attorney Offices, Buenos Aires (April 21 and 28, 2014).

recognition to the agency of domestic actors under IIAs. High profile cases such as Vivendi also helped politicize the presence of foreign investors and privatized utilities throughout the country, which threatened the ideological hegemony obtained by neoliberalism in the national government.

### **2001 Economic Collapse and Emergency Measures: Mounting Investor Claims**

Argentina's high rates of growth in the early 1990s proved unsustainable over the long term, as they were due largely to the one-off sale of SOEs (Haselip and Potter 2010, 1168). A series of external shocks led to rapidly deteriorating economic conditions in the late 1990s (Rodriguez-Boetsch 2005, 303). The country's current-account deficit leapt from US\$ 6.8 billion 1996 to US\$14.5 billion in 1998. Output plummeted and GDP fell, peaking in 2002 at a 10 percent contraction (Wylde 2011, 437). The proportion of the population living in poverty doubled from 27.1 to 54.7 percent while those living in extreme poverty more than tripled from 7.6 to 26.3 percent between 1999 and 2003 (IMF 2005, 24). Fernando de la Rúa assumed presidency in 1999 and abided by IMF recommendations to reduce the government deficit. De la Rúa raised taxes and cut government salaries, pension payments and social assistance programs as unemployment climbed. He also helped expand Argentina's network of BITs by signing on to new agreements with Algeria, the Dominican Republic and Thailand (UNCTAD 2015). In September 2001 the IMF, unsatisfied with progress in reducing government deficits, suspended Argentina's financial assistance (Rodriguez-Boetsch 2005; Wylde 2011).

In an effort to stem ongoing capital flight and prevent the collapse of the banking system, the administration froze all bank deposits, a move that came to be known as the *corralito*. The *corralito* exacerbated the challenges faced by the middle class, already

suffering from lower wages and high unemployment. By December, food riots broke out in Buenos Aires as hordes of people sacked grocery stores, to which the government responded with violent repression led by police forces. This prompted an explosion of street protests in most major cities to demand de la Rúa's resignation (Rodriguez-Boetsch 2005; Grugel and Ruggirozzi 2007, 93). In December 2001, de la Rúa stepped down and Argentina cycled through five presidents in just over two weeks until an emergency interim government, led by Eduardo Duhalde, was established in January 2002 (Wylde 2006, 438).

The uncertainty caused by the economic and political crisis prompted a search amongst policymakers for remedies. Officials began to recognize that a solution to growing deficit problems required either devaluation or a domestic price reduction to restore the competitiveness of Argentine exports (Rodriguez-Boetsch 2005, 308). In January 2002, the Argentine congress introduced a series of Emergency Measures (Law 25.562) to address the economic dislocation and growing social unrest. This included a freeze on deregulated utility rates and an end to the Convertibility Plan. The peso subsequently devalued and (temporarily) stabilized at a rate of three pesos to the US dollar. In 2000, the government had suspended the right of licenses to adjust their tariffs according to the US purchasing power index. The Emergency Measures also eliminated the right of utilities owners to calculate tariffs in US dollars and converted tariffs to a fixed peso rate, a process known as 'pesification'. This significantly reduced the value of contracts, licenses and concessions with dollar adjustment features. These measures were accompanied by the largest government default on external obligations in history (Post and Murillo 2013; Stanley 2006). Policymakers knew that such policies were likely to

have negative impacts on the operation of foreign investors and the claims brought by foreign investors against Argentina in the early 1990s raised awareness amongst state officials of the costs of introducing policies that go against IIA obligations. However, policymakers perceived the Emergency Measures to be a necessary step to placate the symptoms of the country's increasingly urgent political and economic crisis and further neoliberal reforms were not an option given that most of the public blamed them for the crisis' emergence. Meeting state obligations under IIAs was therefore less of a priority relative to advancing necessary policy solutions.

The terms of investors' original contracts proved no longer viable due to the severe strain placed on users' budgets whose incomes were also significantly devalued. Since firms' incomes were collected in pesos and their debt remained largely nominated in US dollars, many foreign investors were hit by severe financial losses (Vicien-Milburn and Andreeva 2010, 295; Stanley 2006, 4). The national government offered foreign investors two options: either renegotiate tariffs or continue with the tariff system denominated in pesos (Stanley 2006, 7). In February 2002, a Commission for the Renegotiation of Concession Contracts was established under the auspices of the Ministry of Economy and granted the responsibility of renegotiating the 59 concessions under federal jurisdiction. Similar renegotiation processes were taken up at the provincial level and were highly politically charged. In most instances, provincial and federal officials bypassed regulatory bodies to negotiate with foreign investors directly. Contract renegotiations proved successful in some instances but failed outright in others. The process was further complicated by the fact that each renegotiated contract was subjected

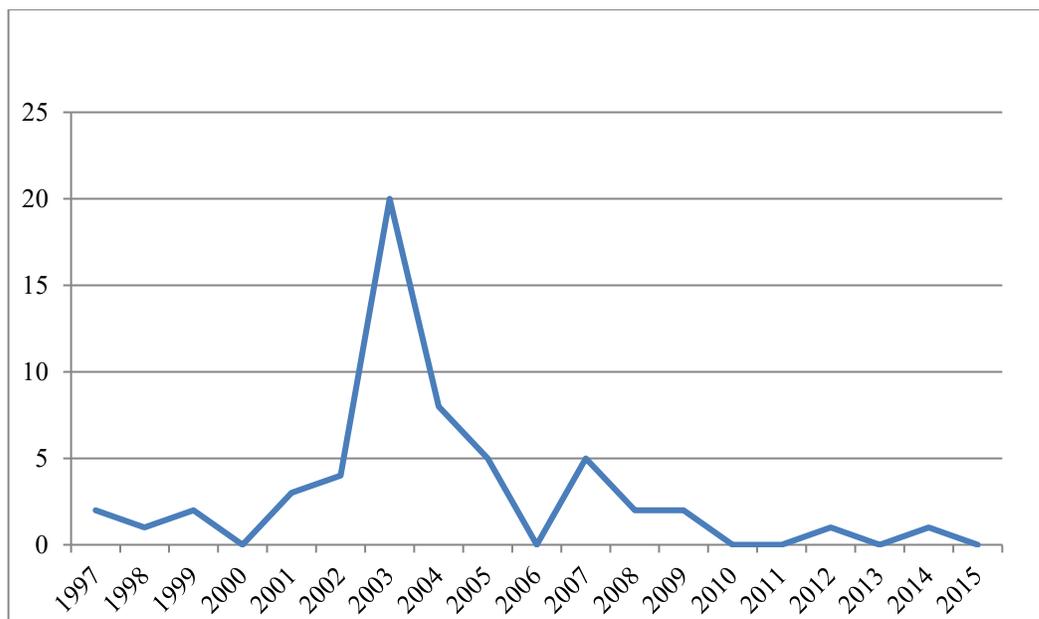
to congressional approval at the respective government level, which at times meant that agreed upon contractual changes were rejected by provincial legislatures.<sup>36</sup>

45 cases were brought against Argentina from 2002 forward in response to the Emergency Measures and failed renegotiations, all but four of which were brought to ICSID (see Figure 2). Nine claims were brought by investors in water and sanitation services and 20 from electricity and gas distribution firms (see Appendix 3). Other claimants included investors with telecoms operations (two suits) and investors with service –related contracts with the public administration. Investors most often cited the effects of the devaluation brought by the ‘pesification’ on contracts and on the rate-setting system as breaches of BIT provisions on fair and equitable treatment, full security and protection and expropriation. Four additional claims were brought by insurance and banking firms that had suffered significant losses as a result of the currency devaluation. Bondholders that held out during Argentina’s debt restructuring efforts in 2005 and 2010 were responsible for three suits brought to ICSID; however, only one of the bondholder claims is proceeding as the others have been terminated or are in the process of being terminated due to the claimants’ delays in moving the case forward.

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<sup>36</sup> Interview with Leonardo Stanley, Centro de Estudios de Estado y Sociedad, Buenos Aires (15 April 2014).

**Figure 2: Number of investor claims brought against Argentina over time<sup>37</sup>**



It is important to note that most investors filed their BIT claims to gain leverage over government officials in contract renegotiations with the aim of securing more generous contract terms (Mortimore and Stanley 2006, 23).<sup>38</sup> The costs of engaging in a potentially protracted legal battle, investors hoped, would be enough to allow them to influence government policy. However growing public opposition to private-sector service providers buttressed the bargaining position of provincial and federal governments. Consumer groups and public demonstrations demanded that policymakers take a hard line approach towards privatized service providers, which officials did without fear of political reprisals. However the political pressure from civil society in communities where utilities were owned by foreign firms also meant that officials were

<sup>37</sup> All data contained in the charts and tables are derived from the UNCTAD Investor-State Dispute Settlement Database (accessed 20 May 2015) as well as a comprehensive review of Argentine newspapers and ICSID legal transcripts found on [italaw.com](http://italaw.com).

<sup>38</sup> Interview with Author, Former member of State Attorney General Office and Representative in several ISA cases, Buenos Aires (April 23 2014).

constrained in the policy and contract concessions they could make to arrive at a settlement. This was particularly the case in provinces where officials faced upcoming elections (Post and Murillo 2013, 121). Contract renegotiations were most heavily politicized in the water sector where civil society maintained a watchful eye. In some cases, negotiators and foreign investors compromised on new investment targets (for service expansion or upgrades) rather than negotiating on the politically sensitive topic of tariff increases (Dagdeviren 2011, 30). Non-governmental organizations (NGOs) and consumer groups actively monitored the performance of privatized companies and gathered evidence of firms' underperformance to inform proposals brought to the national government for the renationalisation of the firms (see, for example, Holland 2005; Azpiazu and Castro 2012).

The 2003 election of Néstor Kirchner with his leftist platform signalled a degree of political renewal in Argentina. The magnitude of the country's economic collapse and its social and political consequences prompted many Argentines to re-evaluate domestic politics in the search of the causes of the crisis. This, in turn, provided a social basis for Kirchner's anti-neoliberal rhetoric and campaign promises to rejuvenate state sovereignty (Wylde 2006, 437; Yates and Bakker 2013, 12). Kirchner campaigned as the leader of a new political party, el Frente para la Victoria, a faction of the PJ party that advocated a stronger return to its Peronist roots. Under Kirchner, the national government established new alliances with labour and industrialists by negotiating minimum wage increases, adopting selective protectionist policies for manufacturing and encouraging labour to negotiate rather than strike. Domestic businesses had become interested in filling the gap left behind by the exit of transnational firms (Wylde 2011).

Under Duhalde, taxes on export earnings from agricultural and extractive industries were increased and the profits used to fund the implementation of conditional cash transfer programs to deal with the abrupt rise in poverty. These policies were extended by the Kirchner government despite protest from business groups, which earned Kirchner popularity amongst non-unionized workers. Tax revenue was also used to fund state subsidies for basic services, the expansion of public works programmes (largely in the provinces) and the promotion of small and medium-sized enterprises while Kirchner negotiated with banks to expand access to credit (Grugel and Riggirozzi 2012, 9- 12; Wylde 2011). Kirchner's election therefore represented a return to the nationalist logic that dominated prior to the neoliberal turn however an internationalist logic persisted in some spaces, particularly in areas dealing with foreign economic policy. The advancement of Kirchner's progressive policies moreover was conducted in the presence of neoliberal legacies, including Argentina's massive network of IIAs.

As noted in the introductory chapter, the Argentine economy began to rebound within a year of Kirchner's election. Kirchner's goal was to break the country's historic susceptibility to macroeconomic instability and maintain the momentum of economic growth through macroeconomic and industrial policy aimed at promoting export sectors (Dumenil and Levy 2006, 389; Wylde 2011, 438). Kirchner's particular brand of post-neoliberalism therefore retained an outward looking economic perspective. Most notable in terms of macroeconomic policy, Kirchner implemented and maintained a *Stable and Competitive Real Exchange Rate* that facilitated strong growth in export-oriented industries. A simultaneous boom in global commodity prices contributed to the high performance of agriculture and natural resource industries, particularly soy farmers, and

in turn led to the accumulation of foreign exchange reserves and tax revenues (Wylde 2011; Frenkel and Rapetti 2008). Kirchner diverted much of the country's financial resources toward paying off international creditors, clearing its US\$ 9.8 billion debt with the IMF in December 2005. This decision was largely driven by a desire to strengthen the country's policy space, which the Kirchner administration argued was being unjustly constrained by loan conditionalities (Grugel and Riggirozzi 2007, 99). The post-crisis economic recovery also enabled the national government to fund large scale infrastructural projects, primarily in the provinces, and begin renationalizing public services (Post and Murillo 2013, 122). In the water and sanitation sector, most of the major concessions were rescinded, including those with Suez, Enron, Saur and Vivendi who had cases pending before international tribunals. By May 2006, the proportion of the population serviced by SOEs in the water sector grew from 12 to 57 percent (Azpiazu and Bonofiglio 2006, 36).

Kirchner exploited public scepticism of privatized utility firms to buttress the government's bargaining position in negotiations with foreign investors. A new institutional platform was introduced to lead the negotiations – the Public Service Contract and Renegotiation Unit under the Ministry of Planning and Infrastructure. A central objective of the renegotiations became to incent investors to drop their claims before international tribunals (Stanley 2006). For instance, in a speech delivered in small town in the Province of Buenos Aires, Kirchner announced:

A few hours ago we were assured that some of the investors that sued Argentina [in ICSID], some Spanish companies, will gradually withdraw their claims. We will advance the same result with a significant number of companies that have yet

to abandon their claims because we are firm, that to renegotiate contracts, privatized public service companies will have to make a certain gesture to the country and that gesture is the withdrawal of their claims before international tribunals. If they want to work in the country, they will come with this gesture of solidarity. We will open our arms to those that want to produce wealth with us but not those that sue us. This is the central and essential task that needs to be met moving forward [author's translation].<sup>39</sup>

Some foreign investors suspended their claims to signal their willingness to negotiate.<sup>40</sup> For the most part, these included investors with interests in continuing their operations in Argentina and who stood to gain more in the long run from settlement (Post and Murillo 2013).<sup>41</sup> Minority shareholders and owners of companies that had already exited the Argentine market stood to gain more financially from continuing ICSID proceedings (Mortimore and Stanley 2006).

The post-crisis economic recovery also made it easier to arrive at settlements with foreign investors as it fuelled industrial demand for utilities, particularly electricity. Higher revenue from sales to industrial clients had the effect of cross-subsidizing services for residential clients, whose rates remained frozen. In many cases, the national and provincial governments allowed firms to raise rates charged to wealthy and industrial users to offset low rates for poor residential consumers (Post and Murillo 2013, 124).<sup>42</sup>

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<sup>39</sup> Presidencia de la Nación. 2005. "Palabras del Presidente Néstor Kirchner," (19 July). Available at: [www.caserosada.gob.ar](http://www.caserosada.gob.ar).

<sup>40</sup> According to Stanley (2006) these include EDESU, AES Co, Pioneer National Resources, Camuzzi, Gas Natural Ban, EDENOR, Unysis, Aguas Cordobesas, Telefonica de Argentina, Telecom and Saur.

<sup>41</sup> Interview, Leonard Stanley, Centre for the Study of State and Society, Buenos Aires (April 15, 2014)

<sup>42</sup> Olivera, Francisco (2005) "Gas Natural BAN Retira su Demanda ante el CIADI." *La Nacion*, March 15.

Capital growth therefore played an important role in expanding the government's capacity to ward off investor claims. It also helped generate confidence amongst policymakers to take a harder position in the face of investor claims throughout the contract renegotiations.

At the centre of these cases was a struggle over the regulatory powers of the state, particularly with respect to the regulation of privatized utilities and the state's autonomy in deciding how best to respond to an emerging and increasingly critical economic crisis. The national and provincial governments found themselves caught between the need to ensure cash-strapped and increasingly impoverished citizens predictable access to basic services while also appeasing foreign investors charged with service delivery. The investment rules set out in BITs, investors argued, were meant to protect them from unexpected changes in the political and economic condition of the country. However the expectation amongst foreign investors that they could legitimately expect such conditions to remain stable across the 20- or 30-year time frame of a concession contract was strongly contested by the Argentine government. As is discussed in the section that follows, the election of Néstor Kirchner in 2003 with his commitment to expanding state authority over the domestic economy had a particular influence on the defence strategy adopted by Argentina towards investor claims.

## **5.2 Argentina's Defence against Investor Claims**

Critical approaches to the study of IIAs and policy space typically assert that IIAs severely limit the capacity of developing countries to advance policies and programs aimed at advancing public interests. The cases discussed above demonstrate that IIAs provide foreign investors a means to challenge domestic policymaking processes.

However, as this section demonstrates, there are several methods through which host states combat investor claims, many of which help to mitigate the costs of investment disputes and preserve the public interest.

### **Procedural – Legal Tactics in Investor-State Arbitration**

After facing its first investor claims during the pre-crisis period, the Argentine government vowed to fight all cases against it one by one using the legal avenues available. Government officials and state lawyers were initially concerned that their participation in the cases would legitimate a system many thought to be biased in favour of the capital-exporting states that designed it. However, as one official stated,

The decision was taken to fight within the overarching system of rules. This was a political and economic decision. It was political because the Argentine state believed it had taken a legitimate and necessary step [to address the crisis] by implementing the emergency measures, but it was also an economic decision because Argentina did not have the resources to pay the claims demanded by foreign investors.<sup>43</sup>

Moreover, had Argentina not participated, the awards would have been rendered against the country despite its failure to appear. The government therefore made the decision to develop a team under the PTN dedicated explicitly to resolving investor-state disputes. However as previously noted, this team lacked experience and was faced by the challenge of developing capacities in the face of mounting investor claims. Concern over the potential repercussions of not participating and the feeling amongst officials that

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<sup>43</sup> Interview with former member of State Attorney General Office and Representative in several ISA cases, Buenos Aires (April 23 2014).

Argentina had little choice in the matter informed the government's decision to participate in the proceedings. This idea, in turn, shaped the strategy adopted by policymakers and state lawyers thereafter as it meant that the strategies state lawyers adopted were circumscribed to some extent by the avenues laid out in IIAs and by arbitral rules. State lawyers and government officials therefore became reluctant participants in the global IIA assemblage. Yet as state lawyers increased their knowledge of the legal structures involved, they became more effective in employing legal arguments to thwart investor claims and, therefore, limited the power of IIAs to impact domestic policymaking processes.

Central to Argentina's legal strategy was the 'public necessity defence' provided for in some BITs (namely *the US-Argentina BIT and France-Argentina BIT*) and the doctrine of necessity under customary international law. For instance, Article IX of the US-Argentina BIT states:

This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests.

Under international law, a state of necessity is also found to exist if certain conditions are present. Article 25 of the *Draft Articles on Responsibility of States for Internationally Wrongful Acts* provides:<sup>44</sup>

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<sup>44</sup> International Law Commission. 2008. *Draft Articles on Responsibility of States for Internationally Wrongful Acts*. Geneva: United Nations.

Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:

- A. is the only way for the State to safeguard an essential interest against a grave and imminent peril; and
- B. does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:

- A. the international obligation in question excludes the possibility of invoking necessity; or
- B. the State has contributed to the situation of necessity.

The necessity defence is therefore meant to exempt certain actions taken by contracting states in response to extraordinary circumstances from the substantive protections of treaties (Gomez 2012, 303). State lawyers argued that the measures taken in the wake of the economic crisis were the only avenue open to the state and that investors must bear part of the adjustment burden as all domestic investors and citizens had done.<sup>45</sup> Such measures, the state argued, were also necessary to ensure increasingly impoverished citizens reliable access to basic services, particularly clean water, which is in itself a human rights obligation.<sup>46</sup> By framing their argument in this way and borrowing from the

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<sup>45</sup> The government extended the emergency measures, first until December 21 2004 with Law 25790, next until December 2005 with Law 25972/04 and finally until December 2006 with Law 26077.

<sup>46</sup> See for example *Suez, Sociedad General de Aguas de Barcelona (AWG), and Vivendi v. Argentine Republic*, Decision on Liability (ICSID Case No. ARB/03/19 ) pg 98 para 252.

discourse of human rights, state lawyers sought to bring attention to the conflict between states' human rights obligations and their obligations to foreign investors under IIAs.

This decision, in turn, was largely informed by the arguments and advocacy of consumer groups and communities impacted by privatized service delivery.

Several NGOs, including the Asociación Civil por Igualdad y Justicia, el Centro de Estudios Legales y Sociales, the Centre for International Environmental Law, Consumidores Libres Cooperativa de Provisión de Servicios de Acción Comunitaria and el Unión de Usuarios y Consumidores submitted joint Amicus Curiae statements requesting that tribunals consider the state's obligations under human rights law when interpreting and applying BIT provisions. The NGOs argued that the state adopted the necessary measures to ensure communities' physical and economic access to water and that the emergency measures fully conformed to human rights law. NGOs also referenced linkages between the right to water and other human rights, including the right to life, health, housing and a basic standard of living.<sup>47</sup> Amicus Curiae submissions are the only channels through which NGOs can participate in formal arbitral proceedings. By participating via this channel, NGOs become willing agents in the global IIA assemblage, Yet in this instance, the participation of NGOs was potentially compromising to the power IIAs have to direct government action. By framing the debate as a human rights issue, NGO submissions buttressed the arguments made by the state regarding the necessity defence.

Necessity clauses reflect the recognition of policymakers that agreements based on commercial logics could intervene the pursuit of social objectives. Foreign investors,

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<sup>47</sup> Ibid. pg 99 para 256.

however, contested the interpretation of events and the necessity clause advanced by state lawyers and NGOs. Instead, corporate attorneys adhered strictly to a market logic and asserted that the Argentine government had contributed to the crisis and therefore the emergency measures did not meet the requirement of necessity. Arbitral tribunals responded inconsistently.<sup>48</sup> The tribunal overseeing LG&E's claim found that Argentina had breached the standards of fair and equitable treatment and national treatment by adopting discriminatory measures against LG&E. However, arbitrators agreed with state lawyers and found that a state of necessity had existed between December 2001 and April 2003. Arbitrators ultimately found that,

The essential interests of the Argentine State were threatened in December 2001. It faced an extremely serious threat to its existence, its political and economic survival, to the possibility of maintaining its essential services in operation, and to the preservation of its internal peace. There is no serious evidence...that Argentina contributed to the crisis resulting in the state of necessity. In this circumstance, an economic recovery package was the only means to respond to the crisis. Although there may have been a number of ways to draft the economic recovery plan, the evidence before the Tribunal demonstrates that an across-the-board response was necessary, and the tariffs on public utilities had to be addressed.<sup>49</sup>

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<sup>48</sup> According to Peterson (2012), arbitrators rejected Argentina's necessity defence with unanimous decisions in five cases (CMS, Sempra, Enron, BG and National Grid) and by a two to one majority in three cases (Suez, Impreglio and El Paso). Arbitrators accepted the defence (to some extent) in three cases (LG&E, Continental Casualty and Total).

<sup>49</sup> LGE&E v. Argentine Republic, Decision on Liability (ICSID Case No. ARB/02/1) pg. 78 para 260.

However the tribunal overseeing *CMS v. Argentina*, which was also brought under the US-Argentina BIT ruled against Argentina after finding that the government had contributed to the state of necessity:

The crisis was not of the making of one particular administration and found its roots in the earlier crisis of the 1980s and evolving government policies of the 1990s and reached a zenith in 2002 and thereafter. Therefore, the Tribunal observes that government policies and their shortcomings significantly contributed to the crisis and the emergency and while exogenous factors did fuel additional difficulties they do not exempt the [State] from its responsibility in the matter.<sup>50</sup>

CMS was awarded US\$133.2 million. The different rulings can be attributed to the ad hoc nature of arbitral proceedings whereby tribunals are constituted differently and arbitrators are not held strictly to the authority of jurisprudence. Tribunals therefore engage with investment rules differently, resulting in inconsistent outcomes.

Yet the difference in tribunal decisions also strongly reflects the ambiguity of investment rules and the wording contained in investment treaties. In almost all proceedings state lawyers and foreign investors competed to advance different translations of IIA provisions, notably those on full protection and security, fair and equitable treatment, arbitrary and discriminatory treatment, what constitutes a foreign investment and umbrella clauses.<sup>51</sup> For instance, the ‘Umbrella Clause’ of the US-

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<sup>50</sup> *CMS v. Argentine Republic*, award (ICSID Case No ARB/02/1 ) pg 95 para 329.

<sup>51</sup> Another good example is provided by the tribunal overseeing *Suez, Vivendi, AWG v. Argentine Republic*. The tribunal had a lengthy debate on the language related to ‘full protection and security’ and the different interpretations that could be accorded to different wordings of this provision. See for example *Decision on Liability* (ICSID Case No.ARB/09/3) pg. 60 - 68 para 160 – 179.

Argentina BIT provides that each party “shall observe any obligation it may have entered into with regard to investments.” CMS lawyers argued that this clause held Argentina liable for implementing the emergency measures as it broke with their rights under the contract and under Argentine law. State lawyers, however, argued that its dispute with CMS was purely contractual in nature and therefore was not covered under the umbrella clause of an international treaty.<sup>52</sup>

Government officials firmly believed that ICSID and the arbitrators comprising tribunals had an institutional bias towards Western commercial interests. This is because, lawyers argued, arbitrators are trained in Western institutions and come from a primarily commercial/private law background. State lawyers asserted that arbitrators’ lack of training in areas of human rights and environmental law lent a particular bias to their readings of investment treaties and the provisions that might protect states from liability to foreign investors in times of crises. For instance, one state lawyer asserted:

There is an entire set of public international law that applies to these circumstances. Contracts between an investor and the state do not exist in a vacuum. They interact and overlap with international and domestic legal obligations. But when we [state lawyers] tried to introduce the state’s international public law obligations, we ended up speaking past each other. [Foreign] investors and arbitrators were only interested in interpreting the lines of the contracts and investment agreements strictly.<sup>53</sup>

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<sup>52</sup> *CMS v. Argentina*, Award (ICSID Case No. ARB/01/8) pg 96 para 298-299.

<sup>53</sup> Interview with Author, Former member of State Attorney General Office and Representative in several ISA cases, Buenos Aires (April 23 2014).

The lack of transparency surrounding ISDS cases makes it difficult to determine an exact dollar amount in claims brought against the country, however scholars estimate that the total damages brought against Argentina in the post-crisis period amounted to approximately \$17 billion (Goldman 2007, 478).

The Executive's perceptions of ICSID bias also informed the strategy adopted by state lawyers throughout the disputes. Officials' suspicions of ICSID bias were buttressed by Argentina's early losses in ISDS cases, which were taken as evidence of arbitrators' preference for private-law interpretations of investment rules. State lawyers were instructed to fight every award rendered in favour of investors through whatever means necessary.<sup>54</sup> However the decision of executive officials to participate within the confines of the legal system meant that its options were curtailed by the institutional channels laid out by third-party bodies. Article 53 of the ICSID convention, for instance, requires that contracting states recognize and enforce an award as if it were a final judgment in that state in stipulating the following:

The award shall be binding on the parties and shall not be subject to any appeal or to any other remedy except those provided for in this Convention. Each party shall abide by and comply with the terms of the award except to the extent that enforcement shall have been stayed pursuant to the relevant provisions of this Convention.

This provision also restricts the review of ICSID awards via appellate bodies and instead makes possible the stay of the award's enforcement to allow for time to request interpretations of IIA provisions, a revision to the award, or annulment. Article 52

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<sup>54</sup> Interviews with former members of the State Attorney General Office and Representatives in several ISA cases, Buenos Aires (April 2014).

stipulates the grounds on which parties can seek annulment of an arbitral award, including: the tribunal was not properly constituted, the tribunal manifestly exceeded its powers, there was corruption on the part of a member of the tribunal, there was a serious departure from a fundamental rule of procedures, or that the award failed to state the reasons on which it is based. This means that reviews of awards rendered occur on very narrow grounds and will be dismissed only due to flaws in arbitral procedures rather than (mis-) interpretations of law or context. The limitations placed on review procedures as spelled out by the ICSID Convention makes it a powerful actant in the global IIA assemblage if states buy into its authority. The PTN attempted to nullify tribunal awards rendered against Argentina according to ICSID's specified criteria. This proved successful in several instances, leading to part or the entire award being thrown out because of a procedural misstep. For instance, awards have been overturned in three of the five cases in which arbitrators had unanimously rejected Argentina's necessity defence. This includes a US\$ 106 million award rendered in favour of Enron in 2007 and a \$ 185 million award in favour of BG Group (Peterson 2012).<sup>55</sup>

While proceedings were ongoing, government officials publically challenged the lack of transparency in arbitral proceedings, the process by which the arbitrators are selected and the fact that investors were allowed to forum shop, meaning that investors select the agreement and tribunal most likely to provide a favourable judgment. Several state lawyers also criticized the freedom with which foreign investors can determine the damages demanded from the state. Often there are enormous discrepancies between what an investor seeks in damages versus the state's own assessment of foreign investor losses.

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<sup>55</sup> According to Peterson, Luke Eric (2012). "Analysis: Latest Split Amongst ICSID Arbitrators over Argentina's Necessity Defence Reflects Wider Chasm," Investment Treaty News, January 29.

Such discrepancies exist because arbitral rules (e.g. under the ICSID and UNCITRAL conventions) do not provide for standard practices or evaluation techniques with which to determine legitimate damages. The concern, in the case of Argentina, was that foreign investors had not calculated the damages based on what they would have lost if Argentina had not implemented the emergency measures. Foreign investors, state lawyers argued, had calculated damages based on the assumption that business would continue “as usual” and not based on the damages that would have resulted from the economic downturn had the government not instituted the emergency measures.<sup>56</sup>

Argentine officials made public its concerns about the systemic bias in part as a means to generate public support for its approach towards investor claims. Most controversially, Argentine officials declared that all awards rendered by ICSID are not enforceable unless reviewed by the country’s domestic courts.<sup>57</sup> Horacio Rosatti, Argentina’s Justice Minister, argued that ICSID arbitral decisions should not be held as supreme over Argentina’s own constitution and must be reviewed by Argentine courts for compatibility (Goodman 2007, 479). It was commonly believed when the system was created that contracting states would voluntarily comply with ICSID awards according to Article 53. The costs of non-compliance, in terms of potential losses to the state’s international reputation as providing a friendly investment climate, which can also lead to capital flight, and the threat of limiting access to World Bank funding or international credit, were considered enough to create incentives for “good behaviour” (Lin 2012). However, this idea of automatic enforcement failed to gain traction amongst Argentine

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<sup>56</sup> Interview with former member of the State Attorney General Office and representative in several ISA cases, Buenos Aires (April 28, 2014).

<sup>57</sup> All awards submitted to Argentine courts for enforcement were subject to a three percent fee. See *Urbaser SA v. Argentine Republic*, Decision on Jurisdiction (ICSID Case No. ARB/07/26) pg 68 para 201.

officials and state lawyers who had stronger ideological commitments to regaining state authority sacrificed to neoliberal restructuring under the Menem government. Instead, Argentina refused to pay outstanding awards to several awardees for failing to have the award reviewed by Argentine courts, including CMS, Azurix, Vivendi, Continental Casualty and National Grid. This, Argentine lawyers asserted, did not amount to a contravention of the ICSID Convention but was in line with it since the provision itself was broad and open to interpretation.

This move attracted scorn from the international community, particularly international financial institutions and investors' home-countries. In 2012, the United States suspended Argentina's preferential trade status under its Generalized System of Preferences in retaliation against Argentina's failure to enforce arbitral awards in favour of US investors (Fox and Rosenberg 2013, 56). A US Trade Representative issued a media statement urging the government to pay the awards, as "this would allow us to consider reinstating Argentina's GSP eligibility and promote the growth of a mutually beneficial US-Argentina trade and investment relationship."<sup>58</sup> Representatives of Argentina's foreign ministry dismissed the statement as an attempt to oblige Argentina to violate federal law. The US then blocked Argentina's access to World Bank loans with the support of the United Kingdom (Allen & Overy 2013).<sup>59</sup>

Argentina's decision to engage in the arbitral proceedings meant that its response was to an extent informed by the institutional parameters and ideas embedded within (and buttressing the legitimacy of) international arbitral bodies. The institutional restrictions

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<sup>58</sup> Palmer, Doug. 2012. "Obama says to suspend trade benefits," Reuter (26 March).

<sup>59</sup> See Allen & Overy. (2013) "Argentina settles five investment treaty awards."

<http://www.allenoverly.com/publications/en-gb/Pages/Argentina-settles-five-investment-treaty-awards.aspx> (accessed 9 February 2015)

on annulment and appeal, for instance, limited the opportunities available to state lawyers to challenge tribunal rulings. Moreover, the ambiguous nature of investment rules and the subjective dimension of arbitral proceedings meant that arbitrators applied investment rules inconsistently across cases. Some of this inconsistency can be attributed to the subtle variations between IIAs in their wording of key provisions, yet it also speaks to the different ways in which human actors engage with and interpret IIAs. Over time, the Argentine executive built its capacity to manage the disputes by creating a team with the authority and legal training required to engage in such procedures. Although state lawyers lacked initial expertise, they proved more adept at defending state interests over time as demonstrated by their ability to overturn several awards previously rendered against the state. It cannot be said that arbitral rules strictly dictated state action. The ambiguous nature of the ICSID Convention's wording and scope enabled Argentine lawyers to interpret key rules, such as Article 53, opportunistically. Indeed, the government's failure to pay several awards rendered against it was argued to fit within the confines of the ICSID Convention. However, challenging the authority of international arbitrations came at a cost both in terms of Argentina's international reputation and its economic links with key partners.

These procedural-legal tactics used by state lawyers and the Executive have had limited success. Of the 58 cases brought against Argentina, 27 have reached a verdict, eight were rendered in favour of the state and 18 in favour of foreign investors (see Table 1). This suggests that when the proceedings do reach the decision on liabilities (preliminary ruling) stage, foreign investors are much more likely to receive a favourable outcome than the state.

**Table 1 Status of ISDS Cases Against Argentina**

Source: UNCTAD 2015.

Status	In favour of Investor	In favour of State	Settled / Withdrawn or Suspended	Pending	Total
Number of Cases	18	8	23	9	58

### Domestic Pressures

The national government also sought to exploit foreign investors' interests in staying in the Argentine market by using domestic instruments to pressure investors to drop their ISDS claims. Most notably, these instruments include the commissions established to renegotiate contracts at the national and provincial level. In many instances, government officials negotiated tariff increases for wealthy and industrial customers in exchange for commitments to keep the tariffs artificially suppressed for poorer communities. This line of agreement was reflected in many renegotiated contracts, provided that firms withdrew their ICSID claims. For example, in the case of *Suez and Aguas de Barcelona v. Argentina*, foreign investors withdrew a \$105 million ICSID claim after agreeing with the province of Córdoba to a rate increase of 25 to 50 percent for medium-income neighbourhoods and up to 100 percent for the wealthiest sectors.<sup>60</sup> Kirchner also made repeated public statements asserting that companies must drop their claim to renegotiate as a demonstration of solidarity with the Argentine public. This was complimented by constant media attention on the renegotiation processes.

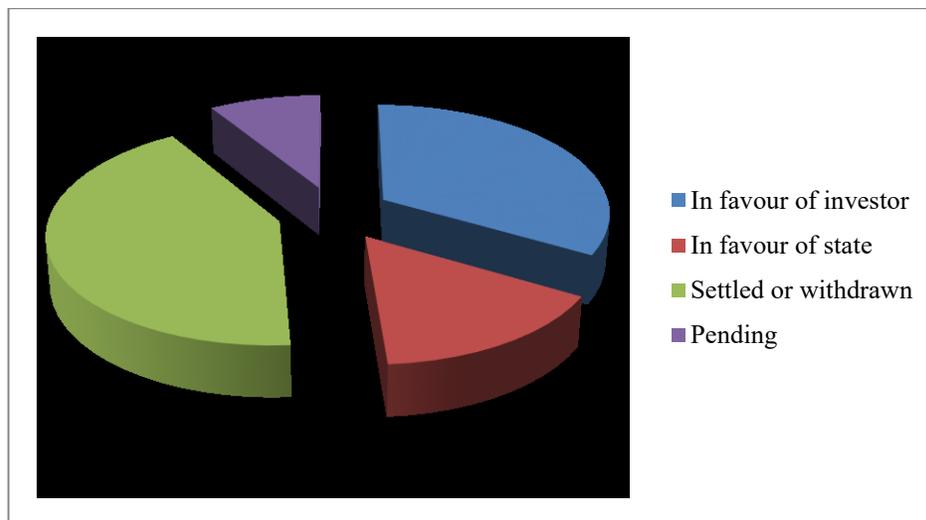
It is important to note that this strategy was limited in some ways by the jurisdictional divisions between the national and provincial governments with respect to utility sectors. Though provincial governments emulated the national government's

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<sup>60</sup> Brundell, Robin. (2005). "Cordoba Congress Approves Renegotiation of Water Utility Concession." *Business Insight in Latin America*, December 29.

renegotiation strategy, the success of negotiations in the provinces was highly dependent upon the support of provincial legislatures and senates. In some instances, renegotiated contracts were struck down once they reached provincial legislatures. This was typically because of concerns that the concessions made to foreign investors were too generous, particularly as provincial officials faced the brunt of social pressure for affordable services.<sup>61</sup> However, overall this strategy was successful in having 40 percent of the crisis claims brought against Argentina withdrawn (see Figure 3).

**Figure 3: Current status of crisis cases against Argentina**



### **International Partnerships**

Another action the Kirchner regime has undertaken to increase its policy space in the light of constraints imposed by IIAs and other factors is to strengthen relations with

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<sup>61</sup> For instance, the Senate of the Province of Mendoza rejected the proposal to increase tariffs on water service delivery negotiated with the EDF International, Saur and Leon who then brought an ICSID claim against the national government. See for instance *EDF International, Saur International, and Leon Participaciones v. Argentine Republic*, Certificate (ICSID Case No. ARB/03/23) pg 240 para 1018.

South American neighbours and non-traditional economic partners, most notably China. Rising intraregional and Chinese investment represent two alternative sources of capital, particularly with respect to China, which is an increasingly significant trade partner and lender in Latin America. For instance, in 2004, President Hu of China committed to investing \$20 billion in Argentina, much of which would target the country's energy and transportation industries (Paz 2014, 8). Argentina also joined Ecuador's initiative to establish an alternative investor-state arbitration mechanism under the auspices of UNASUR. Argentina hopes to use its experience in ISDS cases to inform the centre's development and to include this centre as the primary dispute resolution body in its BITs moving forward.<sup>62</sup> Representatives of member states met in Montevideo, Uruguay to finalize the text of the agreement in January 2016, however the text has not yet been made public. Therefore, Argentina's experience with ISDS cases and investor claims has prompted the country to pursue alternative international partnerships. In this way, investor-state disputes under IIAs fostered a degree of policy experimentation that Argentine officials may have been unlikely to engage in in the absence of investor claims. The availability of alternative partnerships also strengthened the Kirchner administration's confidence to contest the authority of ICSID and IIAs.

### **Limitations**

Under Cristina Kirchner who succeeded her husband in the presidency in 2007, Argentina signalled a more accommodating approach to foreign investors. In 2013, Argentina announced it would pay five outstanding awards to foreign investors in the form of sovereign bonds at a discounted rate. This was part of an effort to strengthen ties

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<sup>62</sup> Interview with the Author, Former member of the State Attorney General Office and representative in several ISA cases, Buenos Aires (April 23, 2014).

with the United States to gain the country's support in Argentina's negotiations with the Paris Club over outstanding debt. In the last few years, Argentina has made a concerted effort to re-open the country's access to international capital markets, which was significantly restricted by the country's debt default and feuds with governments over Argentina's failure to pay the outstanding awards.<sup>63</sup> Argentina remains heavily dependent on capital and technology from foreign firms and therefore continues to seek foreign investment. This is particularly true in its oil and gas sectors, as Argentina has yet to obtain the technical and financial capacity to adequately exploit its vast shale oil and gas reserves.

Many policymakers feared that withdrawing from BITs might scare away potential foreign investment or lead to greater capital flight at a time when Argentina's relationship with the international financial community is tenuous.<sup>64</sup> The Kirchners faced pressure from more nationalist opposition parties to terminate BITs however the Fernández de Kirchner administration continued to believe that maintaining IIAs is necessary to renew investment flows from the United States, Japan and Europe as these countries seek to strengthen ties with emerging markets.<sup>65</sup> The idea that BITs are necessary to promote economic development, which was popularized in the region throughout the 1990s, has therefore had a lasting impact in Argentina despite the election of a post-neoliberal government.

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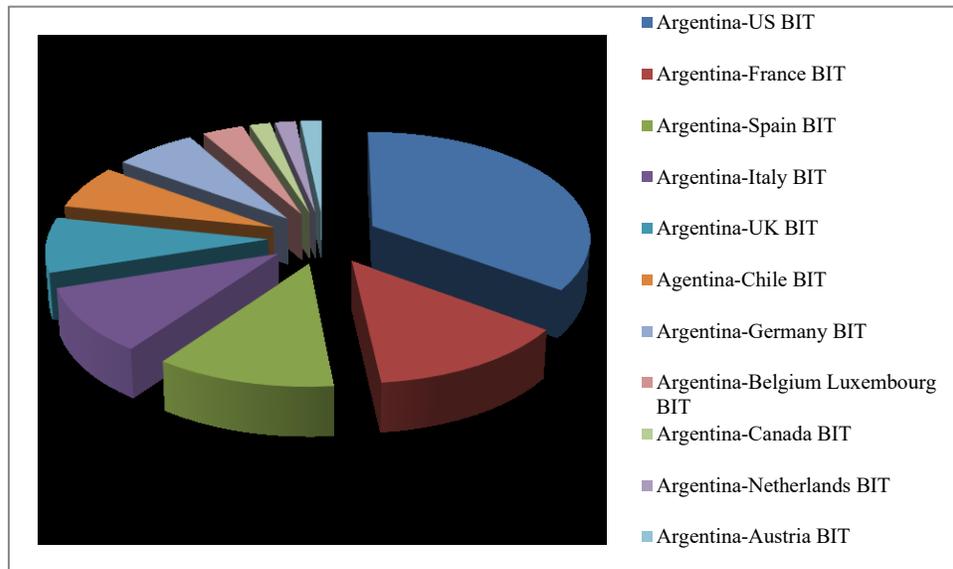
<sup>63</sup> See for example: 2011. "Cristina confía en que respaldo de Obama influya en la negociación con el Club de París," *IProfesional* (6 November 2011). Available at: <http://www.iprofesional.com/notas/125275-Cristina-confa-en-que-respaldo-de-Obama-influya-en-la-negociacin-con-el-Club-de-Pars>

<sup>64</sup> This was the consensus amongst bureaucrats and state lawyers interviewed throughout the course of field research

<sup>65</sup> 2011. "Cristina confía en que respaldo de Obama influya en la negociación con el Club de París," *IProfesional* (6 November 2011). Available at: <http://www.iprofesional.com/notas/125275-Cristina-confa-en-que-respaldo-de-Obama-influya-en-la-negociacin-con-el-Club-de-Pars>

**Figure 4: Number of investor claims brought under each BIT**

Source:UNCTAD 2015



However Fernández de Kirchner also renationalized Spanish firm Repsol's majority stake in the oil company YPF to increase the country's control over its natural resource sector. YPF responded by threatening to bring a claim to ICSID, however Argentina agreed to compensate Repsol for its losses, which amounted to \$5 billion. Argentina's settlement with Repsol removed a hurdle to the establishment of joint ventures between YPF and other foreign companies. YPF recently secured a \$1.2 billion agreement with Chevron for the exploitation of the Vaca Muerta shale field and a \$1.2 billion agreement with Total (UNCTAD 2014, 63). Therefore, while officials' continued faith in IIAs as a means to promote economic development limited its willingness to withdraw from the global IIA regime, Argentina's experience in ISDS cases has not deterred it from adopting policies that conflict with IIA obligations.

Argentina's decision to defend its policy choices under the parameters of prevailing investment rules has had mixed success. While it has helped the country to avoid costly payments in damages, simply engaging in the proceedings is costly. Administrative fees for ICSID tribunals have tended to hover around \$1.3 to \$1.6 million. In instances where cases are withdrawn due to settlement, investors and the state are often ordered to split the fee payment. However, in cases such as *EDF v. Argentina* and *National Grid v. Argentina*, the national government was ordered to pay the majority of administrative fees. This does not include the costs of state lawyers and other legal representatives.

### **5.3 Factors Informing Argentina's Response to Investor Claims**

In this section, I assess more closely how competing factors interacted to shape the influence that IIAs have had over policy space in Argentina. As discussed in chapter three, I define policy space as the policy options that policy makers perceived to be available and politically feasible given prevailing global and local conditions. Such perceptions are shaped not only by the constraints IIAs seek to impose on state action but also by policymakers' understandings of citizen needs and demands, their normative beliefs, and their institutional and sociopolitical environments.

#### **Material Factors**

As discussed in chapter three, I define the material factors that impact policy space as both capital (government revenue and debt levels for example) as well as the non-human objects that help structure policymakers' activities and understandings. Along the lines of ANT, I argue that IIAs can be seen as a particular technology and actant situated within a broader assemblage of human and non-human actants, including for example arbitral

tribunals, experts and treaties on enforcement that are meant to govern investor-state relations. A purely constructivist approach might envision international agreements such as IIAs as codified norms that reflect shared understandings and therefore lack any degree of autonomous power (Porter 2012, 533). Yet IIAs must be envisioned as objects with distinctive textual properties that connect and engage with a network of transnational and domestic actors through processes of translation and enrolment. Through these processes, IIAs structure the activities of various actors with whom they engage.

The particular textual properties of IIAs can open or close space for state resistance, help steer how investment disputes play out, and define who is to be legitimately involved. The IIAs signed by Argentina in the 1990s are similar in principles and purpose. They enable investors to bring disputes against host states to international dispute resolution bodies, enrol a particular network of transnational legal experts and expertise (arbitrators and international lawyers) and legal texts on enforcement and induce parties to engage in a style of arbitration procedures that helps define the dispute as a commercial / legal matter (as opposed to a dispute over state sovereignty or human rights). This particular style of arbitration demands that parties discuss the dispute, its events and state actions using the legalistic language contained in the agreements and arbitral rules. This helps insulate the dispute from broader social and public concerns as such concerns do not fall under the parameters of IIA provisions and there is no particular means of discussing how they might be relevant to the case at hand outside of limited scope of the necessity defence.

The content of IIAs is notable not only for what it stipulates but also for what it leaves out as the ambiguity of investment provisions provides a large degree of latitude to

arbitrators to interpret the rights they provide (Van Harten 2008). This encourages competition amongst parties to advance a particular interpretation of investment rules most favourable to their interests. Of particular relevance to the crisis cases were statements on fair and equitable treatment, full protection and security, indirect and direct expropriation and definitions of foreign investment. Argentine lawyers and corporate representatives sought to advance competing interpretations of how the text should be translated into specific obligations and how state action broke with these obligations. In those cases that were not withdrawn because of a settlement, arbitrators most often agreed with foreign investors' interpretations of such provisions. A decisive factor in many of the disputes was arbitrators' different interpretations of the 'necessity defence'. However, it is important to note that the power of IIAs as 'actants' can be significantly curtailed if governments refuse to recognize their authority, disengage from the global IIA regime or contest their superiority over domestic law. For instance, Argentine officials did not hesitate to introduce emergency measures after the crisis despite their awareness that doing so would likely prompt claims by foreign investors. Moreover, while arbitrators interpreted investment rules liberally, Argentina exploited the ambiguity of the language included in the text of the ICSID Convention to assert that ICSID awards must be reviewed by Argentine courts to be enforced. In this case, foreign investors had to lobby their home-governments to institute sanctions on Argentina to put pressure on the government to retract this policy. Argentina only conceded award payments to foreign investors when it meant that doing so would reopen the country's access to international capital markets. Therefore, the power of IIAs to structure state action and its defensive tactics is linked in important ways to the real and perceived performance of the Argentine

economy. This suggests that capital and ideational processes intersect with the material properties of IIAs to shape the power IIAs hold over policymaking and defensive actions.

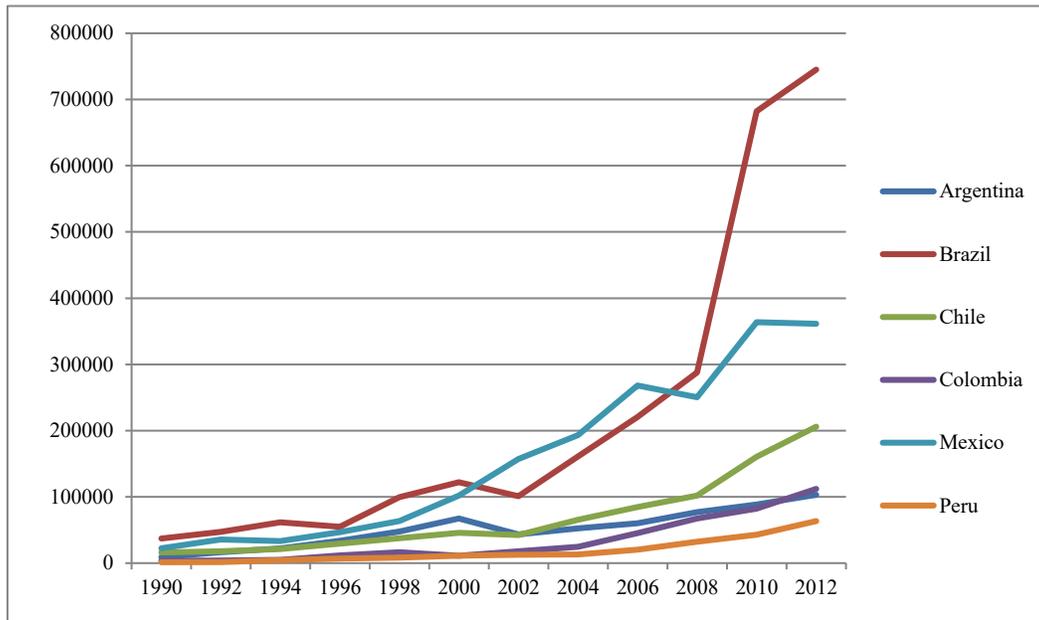
### **Capital**

The Argentine government's ability to ward off investor claims during this time period was also influenced by the country's fluctuating economic performance. As discussed, Kirchner's emphasis on export-growth oriented policies and macroeconomic stability in the post-crisis period helped facilitate impressive domestic economic growth. These policies were complimented with favourable global commodity prices and in turn granted Argentina a greater degree of independence from international capital (Wylde 2014, 2000). As the economic recovery began to replenish government coffers post-crisis, the government had greater room to manoeuvre in terms of expanding state-owned service delivery and negotiating tariff increases that would avoid drastic price increases for the most impoverished, which was a major policy goal of the Kirchner administration.

More recently Argentina has faced escalating inflation rates and decelerating economic growth. This, combined with Argentina's limited access to international capital markets following the crisis has turned the government's attention towards strengthening relationships with international financial institutions. Future economic growth in Argentina is also challenged by deteriorating infrastructure and a lack of technology and capital to exploit the country's recently discovered wealth of oil and gas deposits (OECD 2015). Yet Argentina is not attracting the same levels of investment as other high and middle-income countries in South America (see Figure 5). Attracting foreign investment has become a central concern of the Fernández de Kirchner administration. Real and perceived dependencies on foreign investment, and the lingering notion that IIAs are a

tool to attract greater foreign capital flows, informed Argentina’s decision not to withdraw from BITs.

**Figure 5: Foreign investment stocks in South American middle income states<sup>66</sup>**



### Ideational

In chapter three I also discuss the ways in which ideas and ideational processes structure policymakers’ understandings about the policy options available and politically feasible. According to Béland (2009, 702), ideational processes help construct the problems and issues that enter policy agendas, shape the assumptions that impact the content of proposals for reform, and can become discursive weapons that participate in the construction of proposals for reform. However, ideas “only become a decisive causal factor under specific institutional and political conditions” (Ibid.). In this section I assess

<sup>66</sup> Data was compiled from the UNCTADstat database. Available at: [www.unctadstat.unctad.org/](http://www.unctadstat.unctad.org/) [accessed February 12, 2015).

how such ideational processes intersected with institutional and political conditions to determine the power that IIAs held over Argentina's policy space.

As Argentina's economy stagnated towards the end of the 1980s, international financial institutions and aid donors pressured the newly elected Menem administration to adopt a package of neoliberal reforms through loan and aid conditionalities. This more coercive attempt to transfer policy ideas combined with the Menem administration's own desire to restructure the Argentine economy resulted in the wave of neoliberal reforms instituted in the 1990s. As discussed in chapter four, IIAs gained popularity in the developing world as countries vied to attract foreign capital in the midst of privatization programs. Developed countries championed the agreements as a necessary and efficient means to attract foreign capital to developing markets that are perceived to be otherwise risky investment environments. Menem echoed this logic as he promoted the agreements in domestic policymaking circles, which has left a powerful ideational legacy on how IIAs are perceived in the Argentine government.

Across the 1990s, the Menem administration used coercive levers to push provinces to participate in privatization efforts and in doing so acted as a primary transfer agent for neoliberal reforms. However civil society opposition to these reforms raised awareness amongst provincial policymakers of the costs of SOE privatizations. Civil society and consumer groups framed the debate over privatization as a struggle over fundamental human rights. This prompted some provincial governments to withdraw regulatory concessions given to foreign investors, resulting in Argentina's first arbitral claims. These initial disputes created growing awareness in the national government of the rights afforded to foreign investors under IIAs and helped foster concerns about the

fairness and impartiality of ICSID in overseeing investor-state disputes. As previously noted, policymakers were also sceptical of ICSID because of its affiliation with the World Bank and the strong historic influence of capital-exporting states over that institution.

Argentina's economic collapse and the ensuing social and political dislocation in 2001 and 2002 created a moment high uncertainty as Argentina cycled through successive governments. As Blyth (2002) argues, in periods of high uncertainty, the assumptions embedded in dominant policy paradigms lose salience as actors seek alternative ideas to solve the problems they face. The economic downturn and dramatic rates of unemployment and poverty served as evidence to the Argentine public and left-leaning political elites of the failures of neoliberalism. Public skepticism of international financial institutions, particularly the IMF, also grew as citizens and political elites blamed the institution for encouraging Argentina's adoption of destructive economic practices (Wylde 2011). As the crisis gathered steam, anti-neoliberal protestors grew in numbers and gathered support from across classes. Gradually, protestors 'jumped scale' by targeting the national government directly with calls for greater protections from market insecurities and a return to economic nationalism. At the height of the crisis, the Duhalde administration instituted emergency measures that it perceived were necessary to address the immediate needs of Argentine citizens regardless of whether such measures broke with the country's international obligations under IIAs.

Throughout the ensuing wave of investment disputes, Argentina framed its response to the crisis as an issue of human rights, echoing the same arguments used by anti-privatization protestors. This resonated unevenly with arbitral judges, who offered at

times contradictory verdicts on whether Argentina's actions were excused as a case of necessity. Foreign investors however framed the issue as a private commercial dispute and encouraged arbitrators to strictly interpret the text of the agreements in isolation of the messy entanglement with international human rights law. As discussed, arguments based on private law/commercial interpretations of the text and events surrounding the crisis had more success in arbitration. This is likely because arbitrators are trained in commercial law and have no institutional obligations to weigh citizen needs and states' public policy rights with investor rights unless they are explicitly outlined in the text of the agreement. This demonstrates a particular ideational bias of arbitrators towards commercial interpretations of IIAs, which challenges states' abilities to defend public interests.

The wave of investment disputes resulted in a process of political learning whereby the concerns of officials about the impartiality of the global IIA regime were confirmed by the state's initial losses. Argentina's decision to defend domestic interests under the parameters of existing rules reflects concerns about the country's dependency on foreign investment as well as the ideology and interests of the Kirchner administration. While many foreign investors brought claims to persuade government officials to grant greater concessions in contract renegotiations, this threat was mitigated by the Kirchner administration's interest in reversing the privatization of public services and widespread public support for this initiative. Therefore, the influence of investors' threats was mediated by the government's beliefs about what was necessary to address Argentina's developmental needs.

What is more salient in terms of the ideational impacts of IIAs is the normative influence they have in defining what is a ‘friendly investment environment’. Argentina’s failure to withdraw from BITs and ICSID stands in tension with the government’s combative discourse towards ICSID and its arbitrators. However, the Kirchner administrations balanced aims to reassert state sovereignty with a more outward-looking development model while diverting export earnings towards the extension of social programming. Therefore, Argentina’s strategy in fighting ISDS cases and the impact of IIAs on policy space has been largely influenced by the regime’s left-of-centre, outward looking agenda and the lasting normative legacy of IIAs within the administration.

#### **5.4 The Impact of IIAs in Argentina**

In this section, I conclude with an assessment of what the Argentine case tells us about how IIAs impact policy space and contrast this to common assertions found within the literature, namely that IIAs deter governments from adopting policies, discipline governments for derivations from IIA obligations, and that IIAs can reduce governments’ abilities to fund policy implementation in the future.

*A. IIAs deter the use of policies that conflict with investment rules consistently across time.*

There is little evidence to support the conclusion that IIAs automatically deterred governments at the provincial and federal level from pursuing policies that conflict with investment rules. Both prior to and throughout the crisis, national and provincial governments implemented policies in response to what they perceived were important social needs despite conflicts with their obligations to foreign investors. Moreover, despite ample experience in ISDS cases, the Kirchner administrations continued to

nationalized major firms (e.g. Aerolíneas Argentinas and YPF), which demonstrates the ineffectiveness of IIAs and experiences in ISDS litigation to deter particular forms of government action in the context of a regime that contests the authority of investment rules. This suggests that governments' decisions to abide by investment rules are influenced by broader sociopolitical, material and ideational factors. Therefore, the power that IIAs hold over governments' policy space is contingent upon favourable conditions and varies across time as such conditions evolve. This challenges the common assertion found in the literature that IIAs have an inevitable and universal impact on policy space.

*B. Foreign investors and other actors are always successful in disciplining governments for breaking with investment rules.*

Of the 58 ISDS cases brought against Argentina, 18 cases have been rendered in favour of the investor and only eight have been decided in favour of the state. This suggests that when cases reach the final stages of the arbitral proceedings, foreign investors are more likely to win out. However, it is important to note that Argentina's strategy of seeking annulments has been effective in substantially reducing the costs of the cases and in having some cases overturned (see Appendix 1). In most cases, the compensation demanded from foreign investors greatly exceeded what arbitrators awarded the investor in their final rulings.

Under Néstor Kirchner, the Argentine government maintained a strict stance against allowing tariff increases for some sectors and in this way preserved some of its decision-making autonomy with respect to regulatory changes while conceding in some areas. In some instances, the Argentine government successfully used the renegotiations to incentivize investors to drop their claims. This suggests that in instances where foreign

investors have long-term interests in the host market, they are more susceptible to the use of domestic pressures by host states that are aimed at thwarting arbitral claims.

Argentina's legal strategies evolved across time as state lawyers became more adept at using different legal procedural tactics to defend actions taken during the crisis and exploiting holes in the global IIA assemblage. The necessity defence proved successful in some instances however the inconsistency with which its criteria were interpreted and applied by arbitrators illustrates both an opportunity and challenge for state lawyers. Gaps in the IIA assemblage, particularly related to its lack of an effective enforcement mechanism, allowed Argentina greater flexibility to time award payments according to its interests and to negotiate discounts on the compensation owed to investors. However, this has not been without reprisal from investors' home governments. Indeed, the United States and United Kingdom have leveraged their international presence and influence over international financial institutions to pressure Argentina to adhere to tribunal rulings. Argentina's feuds with foreign investors have also been a factor in limiting the country's access to international capital markets. Yet Argentina's experience under IIAs suggests that states that initially lack the capacity to ward off investor claims over time may develop greater capacities to fight back.

Following the crisis, Argentina experienced significant capital flight as a number of foreign investors exited the market. More recently, Argentina has succeeded in attracting a number of large investment projects, most notably by US oil and gas companies that are drawn to the country's shale oil fields. As of 2012, FDI stocks in Argentina amounted to approximately US\$103 billion, which is 50 percent higher than Argentina's pre-crisis peak at \$67 billion in 2000. However, foreign investment has yet

to reach the growth rates experienced by other middle-income countries in South America, some of which are also governed by post-neoliberal regimes. Argentina's failure to attract high rates of incoming FDI is the result of a variety of factors in addition to its high profile disputes with foreign investors, including the imposition of capital controls, renationalizations, the perceived unpredictability of the political regime and a perceived lack of autonomy in the country's judicial system. Therefore it is hard to isolate the impact of ISDS cases and Argentina's defense on overall investment flows and capital flight. However, state-led investment from Southern partners, most notably China and Brazil, provided a temporary source of needed foreign capital. More recently, both countries have faced sputtering economic performance, which may reduce their capacity to drive investment towards Argentina in the future.

*C. IIAs reduced the government's abilities to fund policies and programs in the future after breaking with investment rules.*

Several awards rendered against Argentina remain unpublished and many more have yet to be enforced by foreign investors due to Argentina's insistence that such awards be reviewed in its domestic courts. In light of the mounting interest of award payments in such cases, it is difficult to arrive at a final amount in terms of the cost these cases will have for government revenue. The known awards rendered in favour of investors have varied between US\$2.8 million to US\$ 186 million plus interest. This is in addition to the costs of hiring legal experts and the fees associated with bringing a claim to ICSID, which are typically born by the party that loses the case. For example, in *EDF International, Saur and Léon Participaciones v. Argentina*, Argentina was ordered to pay ICSID fees of over US\$ 1.6 million. Although the cost of each award may not appear to

be a significant amount relative to overall state spending, the combined impact of multiple awards rendered when combined with the costs of mounting a legal defence can have a significant impact on the state's ability to fund programs in the future. For example, Argentina dedicated \$500 and \$600 million to fund *Jefes y Jefas* in 2002 and 2003 respectively. The program aimed to provide income support for families with dependents who had lost their main source of income as a result of the crisis (Galasso and Ravallion 2003, 3). Although Argentina expanded its conditional cash transfers to provide new forms of assistance to children (e.g. the Universal Child Allowance), the costs of investment disputes can dramatically curtail the funding pool available for such programs in the future.

## **5.5 Conclusion**

Argentina's experience under IIAs demonstrates that investment rules have had an inconsistent impact on policy space across time. IIAs did not automatically deter the government from adopting policies that conflict with investment rules, such as the adoption of emergency measures following the 2001 crisis. Moreover, the ability of foreign investors and external actors to discipline the Argentine government for adopting such measures has also been inconsistent as Argentina has proved adept at leveraging domestic pressures and legal-procedural tactics to thwart investor claims while exploiting holes in the global IIA assemblage. This has helped reduce the overall amount owed to foreign investors, although many awards have yet to be enforced against the country.

In some instances, investor claims prompted policy experimentation by the Argentine government. Argentina established a new team of lawyers under the Auditor General to fight investor claims. Although the team was initially inexperienced and

lacked expertise in investor-state arbitration, it strengthened its capacity over time and became more successful in combating investor claims as demonstrated by the awards overturned. It also used the contract renegotiation units to pressure investors to pending lawsuits. Moreover, Argentina's pursuit of stronger ties with regional partners to combat perceived biases in current ISDS bodies represent new policies that would not have existed in the absence of investor claims. In this way, Argentina's fight with foreign investors can be said to prompt an expansion of policy space rather than serve as a constraint.

This case demonstrates the importance of examining the impacts of IIAs on policy space in light of domestic resistance and responses. It provides evidence to support the argument that IIAs have uneven impacts across time and space. Therefore, we must move past the underlying assumptions in current studies, which portray IIAs as cohesive and monolithic global processes with universal outcomes and instead explore the nuances of investor-state disputes and the various gaps that make local resistance possible.

## **6 Chapter: IIAs and the Defence of Policy Space in Ecuador**

Like Argentina, Ecuador has faced a considerable number of investor claims that have been highly politicized domestically. At 22 known ISDS cases, Ecuador is the seventh most frequent respondent state out of any country in the world (UNCTAD 2015). This is particularly remarkable given that Ecuador's economy is much smaller than other frequent respondent states such as Argentina and Mexico. While the majority of investor claims brought against Argentina stem from the disruption caused by the economic crisis, the claims brought against Ecuador are rooted primarily in the attempts across governments to redefine the conditions under which its hydrocarbons sector is governed. The claims more specifically relate to the changes introduced to Ecuador's system of value added tax reimbursements; efforts to increase the government's share of profits derived from oil exploitation via the introduction of a windfall tax; and, contract interruptions caused by social opposition.

As in the previous chapter, I will investigate two neglected dimensions of the relationship between IIAs and government policy space, including: how IIAs impact policy space when the agency of domestic actors is brought into the centre of analyses; and, the mechanisms through which IIAs shape perceptions of policy space in practice. I explore these facets while assessing whether common assumptions about the decline of policy space hold in the context of Argentina, namely, that IIAs deter governments from using policies that conflict with investment rules; that IIAs provide foreign investors the ability to challenge government policy and therefore shrink government policy space; and,

that IIAs reduce the capacity of governments to fund policy choices in the future after having broken with investment rules.

In this case, I find that IIAs did not have a consistent impact on Ecuador's policy space across time. Rather, successive administrations introduced policies aimed at capturing a greater share of the profits flowing from foreign oil companies. Prior to the 2006 election of Rafael Correa, policymakers' decisions to introduce such policies were informed largely by civil society demands and a fear of political reprisals. Once Correa was brought to power, further regulatory changes were introduced to advance the government's development agenda. This suggests that IIAs have a weak deterrent effect in countries where social activism demands that governments break with IIA commitments, particularly in the context of governments who do not adhere to the ideological principles underpinning IIAs.

Like Argentina, Ecuadorian officials have had some success in mitigating the costs of investor claims using legal-procedural tactics however much of its legal defence was contracted out to prestigious international law firms, which meant that its legal team avoided the learning curve experienced by Argentine attorneys. Ecuador has also sought to exploit gaps in the global IIA assemblage; however the Correa administration went further than the Kirchners by withdrawing from some of its components. Most notably, this includes withdrawing from the ICSID Convention and terminating several BITs. Ecuador's withdrawal from the global IIA assemblage is informed by the ideological principles of the Correa administration, which aims to reassert state authority over the governance of Ecuador's domestic economy. The costs of investor claims, in this case, have been outweighed by the increase in revenue captured by the changes in regulatory

policy, which suggests that the investment disputes may not have a strong impact on Ecuador's ability to fund future programs and policies in the context of high oil prices. However, the recent decline in global oil prices may prove challenging in this regard. Ecuador's experience with IIAs also demonstrates the role that causal and normative ideas and material resources play in mediating the impact that IIAs have on policy space. This, in turn, supports the need to nuance our understanding of the relationship between IIAs and policy space.

### **6.1 Context and Conditions: The Neoliberal Shift and Resource Politics**

Scholars have characterized Ecuador's neoliberal path as one dominated by policy discord, reversals and obstacles to market reform (Thoumi and Grindle 1992; Perreault and Valdivia 2010, 691). Yet as Hey and Klak (1999) observe, there was still a gradual convergence over the course of the 1980s and 1990s across four ideologically diverse governments towards the acceptance of neoliberalism as a guiding framework for social and economic policy. President Osvaldo Hurtado (1981-1986) was the first to set the country on a neoliberal path, however he focused primarily on austerity measures while economic restructuring was left to subsequent administrations. Still, Hurtado's shift to the right marked an important break from the populist, state-led capitalism that characterised previous governments, particularly the military regimes that preceded him (Perreault and Valdivia 2010, 692).

Hurtado, who served as Vice-President in Ecuador's first civilian government, assumed presidency in 1981 after the death of President Roldós (1979 – 1981). Almost immediately Hurtado was confronted with a series of economic crises and growing unrest by a strengthening labour movement that had become dissatisfied over the course of the

military regimes with delays in agrarian reform and failed commitments to increase the minimum wage. Hurtado tried to placate the crisis by imposing higher taxes on corporations and the upper class, but it was not enough, particularly in light of dropping global oil prices. Hurtado eventually accepted an IMF-approved stabilization program as a condition of rescheduling the country's growing debt burden. The program required the introduction of policies that devalued the *sucre*, cut state spending on subsidies on fuel and basic foodstuffs and postponed major development projects. Hurtado also modified the *Hydrocarbons Law* to attract foreign investors, offering 11 new exploration blocks to foreign firms who undertook exploration activities under service contracts (Corkill and Cubitt 1988, 52). The entry of foreign firms into Ecuador's hydrocarbons sector attracted immediate public opposition, particularly amongst workers' unions.

Since 1971, oil exploration and exploitation remained under the control of the government via Petroecuador, which was originally established in 1971 as *Corporación Estatal Petrolera Ecuatoriana* (CEPE, translated as the State Petroleum Company of Ecuador). A coup in 1971 resulted in the rise of a left-leaning military junta. The coup was driven in large part by popular dissatisfaction with the approach adopted by the previous government after vast oil deposits were discovered in the Amazonian basin. Under the previous government, the rights to exploit oil deposits were sold immediately to foreign-owned firms under generous contract terms that many felt were one-sided (Corkill and Cubitt 1988, 24). Moreover, given the central role played by oil production in the country's development, many citizens saw the sale as the giving away of the country's interests (Perrault and Valdivia 2010, 692).

Following the 1971 coup, the military junta nationalized all subsurface resources and retracted the concessions given to foreign oil companies, forcing them to renegotiate. This allowed the government to introduce a new system of taxes, rents and royalties. CEPE was given the responsibility of managing the marketing, exploration, refining and eventually production activities. By 1977, the first national refinery also began operating in Esmeraldas, which was intended to allow the Ecuadorian government to capture greater value-add from oil production (Perrault and Valdivia 2010, 692). The influx of state revenue from oil exploitation was directed towards funding the expansion of social programs (namely related to education and health) as well as the institution of ISI policies. This included the establishment and expansion of state-owned enterprises and the expansion of domestic credit lines via banking and credit corporations (Corkill and Cubitt 1988, 28 – 30). The domestic consumption of petroleum products was also heavily subsidised. ISI policies were in turn accompanied by a significant agrarian reform program that reflected the regime's nationalist development strategy.

Oil production under the hands of the state contributed to a general feeling of economic progress and modernization within the public and therefore came to be embedded, as Perreault and Valdivia argue, in the national imaginaries of Ecuadorians as a vital aspect of the state's nation-building project. This, in turn, fostered a consciousness of petroleum-citizenship, which was felt most strongly by those employed in CEPE and the state refinery (2010, 692). This particular consciousness had a lasting impact on how foreign oil companies were perceived as it increased public skepticism over the re-entry of foreign oil companies in subsequent decades.

The return of civilian rule in 1979 created greater space for the emergence of civil society groups in Ecuador. Among the first to capitalize on this space were workers' unions, including in the hydrocarbons sector. Unions mobilized in opposition to Hurtado's neoliberal reforms, which were largely seen as an attempt to minimize the power of the labour movement that had developed within state-led enterprises. In 1989, CEPE was re-organized into Petroecuador, a conglomerate of affiliated enterprises that each had a distinct role in exploration, production and commercialization. The restructuring was advanced by government officials as a necessary move to eliminate inefficiency and encourage foreign investment (Montúfar 2000). However this move initiated a wave of protest by unionized petroleum workers, a wave that was buttressed by successive attempts to privatize the state-owned oil pipeline in the early 1990s.

The neoliberal transition in Ecuador progressed most rapidly under the administration of Durán Ballén (1992-1996). Ballén led Ecuador's right-wing Partido Social Cristiano (PSC) and pushed neoliberal reforms under the guise of a 'modernization' project. This project was widely supported amongst Ecuador's international-oriented business groups pushed for an end to the state-led economic development models that had historically monopolized Ecuador's developmental path. SOEs were privatized in conjunction with the elimination of traditional protections and subsidies given to domestic firms and strategic sectors. Ballén signed on to 16 BITs and reformed the country's system of land ownership to attract foreign investment. Most notable was the 1994 Agrarian Reform Law, which made it more difficult for peasants to obtain legal rights to land simply by occupying it. This exacerbated tensions between the national government and indigenous groups, tensions made more acute as extractive firms took

over lands occupied by indigenous communities (Hey and Klack 1999; Thoumi and Grindle 1992).

As discussed in chapter one, Ecuador witnessed a resurgence of indigenous organizing in the 1990s led in part by the Confederación de las Nacionalidades Indígenas del Ecuador (CONAIE – Confederation of Indigenous Nationalities of Ecuador). Indigenous activism has a long history in Ecuador, however a renewed sense of indigenous identity and political consciousness swept through the country in the 1970s and 1980s. CONAIE emerged from this wave and sought to exploit the opportunity by rallying together indigenous groups around a call for greater cultural rights and political inclusivity. CONAIE led massive marches, blockades and protests that crippled the country's transportation networks in what became known as the June 1990 uprising. At the heart of this movement were demands for bilingual education, agrarian reform and the recognition of Ecuador as a plurinational state, meaning the acceptance and inclusion of Ecuador's diverse cultural and ethnic composition and the right to difference as a guiding principle for the country's governance moving forward (Collins 2014, 75; Lucero 2003, 32).

The neoliberal initiatives adopted by governments also served as a rallying point for indigenous activists who joined with other popular sectors, including workers' unions and campesino movements, to oppose further neoliberal reforms. Indigenous activists began to refer to the movement as the *pachakutik*, which in Kichwa language, meant a return in time or cultural rebirth. In 1995, the Pachakutik movement mounted a national campaign aimed at blocking the passage of a neoliberal reform package proposed by Ballén. Public sector workers, urban activists, women's organisations, human rights

activists and environmentalists joined in the Pachakutik to defeat a referendum on the reforms, which would have opened up the doors to the privatization of public sector enterprises (Collins 2014, 73).

Yet growing anti-neoliberal activism did not prevent Ballén from instituting a process of *apertura petrolera* (opening the oil sector to foreign participation), which included the adoption of generous incentives for private investment. State oversight over the oil sector was drastically reduced as were taxes on the imports of machinery, equipment and supplies needed by foreign firms to engage in exploration and exploitation activities (Perreault and Valdivia 2010, 693). The system of contracts granted to foreign oil companies was also significantly modified to increase incentives for foreign investors, open downstream activities to private investment and expand the Trans-Ecuadorian Oil Pipe System. This included replacing the previous system of service contracts with a production-sharing contract model via amendments to the country's Hydrocarbons Law in 1993. Under service contracts, private oil companies provided the services needed in the production of oil in return for which the companies were reimbursed for costs, including interest as well as a service commission. Petroecuador assumed the costs of oil exploration and production as well as the ownership and exportation of the oil produced. Critics of the contract model argued it constrained the country's ability to attract foreign investment since the profits available to private companies were minimal. Under the new production-sharing contracts, the risk of oil exploration and exploitation was downloaded

to private companies in exchange for a share of the oil produced (that was largely exported), which allowed oil companies a greater share in the profits.<sup>67</sup>

Foreign oil companies rushed into the Ecuadorian market to exploit new opportunities created for profit-making under the new contract system. Foreign investment in exploration and exploitation increased from US\$ 90 million in 1991 to US\$ 1,120 million in 2001. Known reserves increased markedly, from 2,115 billion barrels in the mid-1990s to 4,630 billion by 2004 (Stanley 2008, 5 – 7). The sudden flood of foreign-owned oil companies engendered greater mobilizations from indigenous and environmental groups against petroleum extraction. These groups began to protest the repercussions of oil exploration and extraction, pointing to issues of land appropriation and concentrations, detrimental health impacts, and the marginalization of indigenous livelihoods (Perreault and Valdivia 2009).

Opposition to neoliberal reform within civil society deepened over the late 1990s and into the next decade. In 2000, a coup driven by indigenous groups and military personnel resulted in the ousting of then-president Jamil Mahuad. Mahuad had authorised a major bank bailout and instituted a freeze on depositors' bank accounts after an economic crisis in 1999 crippled the banking sector. The 2000 coup was as much about opposing Mahuad's continued use of austerity measures as it was about fighting government corruption, which was perceived to be rampant amongst political elites given their close ties to the banking sector. Popular movements also came to embrace a broader call for the notion of plurinationalism, which lent the anti-neoliberal movement a more urgent concern for the reformulation of Ecuador's political institutions (Collins 2014, 75).

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<sup>67</sup> *Burlington Resources Inc. v. Republic of Ecuador*, Decision of Liability (ICSID Case No. ARB/08/5) pg. 8 – 10.

Mahuad was succeeded by his Vice President, Gustavo Noboa (2000 – 2003) who began to re-evaluate the terms on which foreign oil companies operated in Ecuador. This included restricting some of the generous tax incentives granted to the companies, a decision that resulted in Ecuador's first BIT claims.

### **Big Oil and Tax Policy: The First Wave of Claims**

Under the Hydrocarbons Law, foreign oil companies received reimbursements of value added tax (VAT) paid for goods and services for use in the production of oil for export. Until August 2001, oil companies received reimbursements for VAT like any other exporter in the country. However, that month the *Servicio de Rentas Internas* (SRI – the Internal Revenue Service) introduced a reinterpretation of the tax law and announced that oil companies' VAT payments did not qualify for such reimbursements. SRI officials claimed that the VAT reimbursements were never meant to be applied to the imports of foreign-owned oil firms because the firms already received generous tax-related incentives in their concession contracts. The oil firms however attributed the change to the government's political interests given the increased politicisation of the hydrocarbons sector. The SRI withheld almost US\$200 million in anticipated reimbursements from various oil companies and in some cases demanded the reimbursement of VAT credits already doled out to oil companies. This prompted claims by US-based Occidental, Spanish firm Repsol and Canada's EnCana under their countries' respective BITs with Ecuador (Ghaemmaghami 2003/4; Peterson 2004).<sup>68</sup>

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<sup>68</sup> A similar claim related to changes in the implementation of VAT was brought by Noble Energy related to the withdrawal of VAT reimbursements for natural gas purchases. This claim was dismissed as the claimants failed to prove that the allegations against Ecuador constituted a violation of BIT provisions.

According to an official of the Procuraduria General del Estado (PGE), Ecuador was also largely unprepared to address investor claims. As in the case of Argentina, few state lawyers possessed the necessary English language skills to participate fully in international arbitrations or knew of the technical procedures associated with ICSID and UNCITRAL arbitral cases. According to one former government official,

When Ecuador was served with its first notification [of a pending arbitral suit], the Attorney General gathered everyone together and asked who spoke English. The first one to raise their hand was assigned the task of leading the state's defence. I'm being facetious but it isn't far from the truth.<sup>69</sup>

A team designated the *Asuntos Internacionales y Arbitraje* (International Issues and Arbitration) was established under the PGE and charged with the responsibility of defending national interests in investor-state disputes. However, unlike Argentina, this team has acted largely as an oversight mechanism as much of the state's legal defence has been contracted out to prestigious international law firms based in the United States and the United Kingdom, which work in collaboration with domestic law firms based in Quito. The PGE team therefore acts as a mechanism through which the Executive maintains tight control over the state's defence strategy through its supervision of external lawyers rather than formulating the legal strategies directly.

Occidental accused the Ecuadorian government of breaching the US-Ecuador BIT provisions on national treatment, fair and equitable treatment and full protection and security. In its 2004 decision, the UNCITRAL arbitral tribunal found Ecuador had

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<sup>69</sup> Interview with Author, Former member of State Attorney's Office and representative on several cases, Quito (October 9, 2014).

breached its BIT commitments in two ways: first, by going against the national treatment provision in failing to treat Occidental investments as favourably as other investments. Since VAT reimbursement continued to be received by firms engaged in other export sectors, Occidental alleged that it had been subject to discriminatory treatment. Secondly, Ecuador was found to have failed to provide a transparent and predictable framework for planning, given the SRI's confusing and somewhat vague taxation policies that the tribunal argued resulted in 'arbitrariness'. In its final award decision, the tribunal found that, "OPEC [Occidental] undertook its investments...in a legal and business environment that was certain and predictable. This environment was changed as a matter of policy and legal interpretation, thus resulting in the breach of fair and equitable treatment."<sup>70</sup> Occidental was awarded US\$ 75.075 million in damages plus interest.

This ruling reveals the extent to which processes of translation matter in shaping the power BITs have to constrain policy space. The national treatment provision of the United States-Ecuador BIT stipulates that, "Each Party shall permit and treat investment, and activities associated therewith, on a basis no less favorable than that accorded in like situations to investment or associated activities of its own nationals or companies".<sup>71</sup> Occidental's attorneys argued that because companies involved in the export of other goods, particularly flowers, mining and seafood products, continued to receive VAT reimbursements, denying the same reimbursements to oil companies amounted to discriminatory treatment. The particular phrase "in like situations" contained in the provision, the attorneys argued, does not refer to industries or companies involved in the

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<sup>70</sup> *Occidental Exploration and Production Co. v. Republic of Ecuador*, Award (UNCITRAL Case No. UN3467), pg 68, para 196.

<sup>71</sup> Ecuador-United States Bilateral Investment Treaty. Available at: <http://www.state.gov/documents/organization/43558.pdf> (accessed 15 February 2016).

same sector, such as oil producers, but to all companies engaged in exporting even if it encompasses different sectors.<sup>72</sup> Ecuador's attorneys however asserted that the same text, "in like situations", could only mean that all companies in the same sector must be treated alike. By denying the VAT credit to all oil companies regardless of their nation of origin, Occidental had been subject to equal treatment.<sup>73</sup> The arbitrators agreed with Occidental's interpretation and applied the national treatment provision as broadly as possible.

Moreover, by holding Ecuador accountable for 'regulatory uncertainties' under BIT provisions, the arbitrators established a potential precedent that countries could be held liable for changes to regulatory regimes based on the sheer fact of the regime's complexity. As Susan Franck (2005, 678) argues,

No regulatory framework is absolutely clear and free of inconsistencies... Particularly because many countries have complex regulatory regimes that provide significant interpretative discretion to implementing authorities and government regulators, adopting such a standard in future cases involving regulatory inconsistency could well have unanticipated adverse effects. On one hand, it might mean that states will be liable for regulatory regimes that are considered too vague or unclear. On the other hand, it might also mean that states will potentially be liable- for changing the 'business and legal environment'- if they attempt to correct a lack of clarity or enact a new regulatory framework.

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<sup>72</sup> *Occidental v. Ecuador*, award, pg 60 para 168.

<sup>73</sup> *Ibid*, pg 61, para 171.

Although tribunals are not bound by precedent, arbitrators often use prior tribunal decisions to inform their interpretation of IIA provisions, which raises the risk that the Occidental Tribunal's broad interpretation could be applied elsewhere.

However, the same claim over VAT credits brought by different companies under different IIAs rendered a very different translation by arbitrators. The tribunal overseeing Encana's claim, which was also convened under UNCITRAL rules, found that the company's supposed entitlement to VAT refunds was excluded from the scope of the BIT. Article XII of the Canada-Ecuador BIT exempts taxation measures from treaty coverage unless it can be proven that the measure amounted to a specific instance of expropriation. In its ruling, the tribunal found that "in the absence of a specific commitment from the host State, the foreign investor has neither the right nor any legitimate expectation that the tax regime will not change...during the period of the investment." The tribunal further argued that,

nothing in the record suggests that the change in VAT laws or in their interpretation brought the companies to a standstill or rendered the value to be derived from their activities so marginal or unprofitable as effectively to deprive them of their character as investments.<sup>74</sup>

The tribunal therefore held that although the company did have a right under Ecuadorian law to VAT refunds, the SRI had not expropriated this right in denying the refunds. This conclusion was supported by the fact that several other foreign-owned oil companies had successfully challenged the denial of VAT credits in Ecuador's domestic court system

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<sup>74</sup> *EnCana Corporation v. Republic of Ecuador*, Award (UNCITRAL Case No. 3481), pg 49 – 50, para 173 – 174.

and won awards with which the SRI promptly complied.<sup>75</sup> Slight variations in BIT wording can therefore have an important impact on their power to constrain policy space. Yet it is also important to note that the standard of ‘national treatment’ provision shared by the BITs was interpreted by the EnCana tribunal more narrowly than the Occidental tribunal. Foreign-owned oil companies were compared in relation to counterparts within the oil sector and not across, as ‘like companies’ were restricted to companies operating within the same sector. The fact that tribunals are composed on an ad hoc basis comprised of three different members means that tribunals do not engage with investment rules in the same way, which can also expand or constrict the scope of BIT provisions and therefore the power to impact policy space.

Occidental’s win in its suit over VAT refunds was subsequently challenged by Ecuador’s attorneys in London’s Court of International Arbitration, albeit unsuccessfully. In 2004, then-President Alfred Palacio instructed the Attorney General to initiate a review of Occidental’s contract and practices to ensure that the company had complied with the contract’s terms throughout its operation. The Attorney General’s office found that Occidental had breached its contract with the state by failing to make the requisite investments and by selling off a 40 percent stake in its concession to a Canadian company, Alberta Oil Corporation (AEC) without proper ministerial authorization. This act went explicitly against the Hydrocarbons Law in addition to Occidental’s contract.<sup>76</sup> The Attorney General subsequently demanded Petroecuador to declare the contract was terminated. Petroecuador notified Occidental of its alleged contractual breach and gave the company 10 business days to respond.

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<sup>75</sup> *Encana v. Ecuador*, pg. 54 – 55 para 188 – 198.

<sup>76</sup> *Occidental v. Ecuador*. Award, pg. 61 para 174 – 176.

In the early months of 2005, anti-foreign investor groups of demonstrators began to protest in the streets of Quito, congregating in front of Occidental offices. Protestors included a diverse range of workers, campesinos, indigenous and middle class activists that demanded the cancellation of Occidental's contract, a call that was also taken up by Presidential candidate Rafael Correa. Petroecuador executives were called before the National Congress to explain why the termination had experienced so many delays. In April 2005 after days of violent protest in Quito, the Ecuadorian Congress ousted President Gutierrez and replaced him with Alfredo Palacio. The following June, during a major strike, a number of government officials including the new Minister of Energy and Mines signed a resolution stating:

The Minister of Energy and Mines and the President of Petroecuador...commit to undertaking all of the necessary steps for the departure from Ecuador of the companies Occidental and EnCana AEC for having violated the juridical norms of the country.

The Minister, under pressure from members of the Congress, then informed Occidental of the causes for the contract's termination.<sup>77</sup>

In May 2006, upon the Minister's further hesitation, Correa led street protests outside Occidental offices and called for the closure of Occidental. Civil society groups then threatened to impeach President Palacio after it was made public that the Minister was considering a settlement with the oil firm. Shortly after, on May 15 2006, the Minister issued a Caducidad (termination) Decree, formally terminating Occidental's

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<sup>77</sup> Occidental v. Ecuador, award, pg. 65 – 66..

contract and ordering the company to turn over its assets to Petroecuador.<sup>78</sup> The following day, Petroecuador employees began to take over Occidental offices while the army was sent to guard the oil facilities. Civil society demands the threat of impeachment therefore outweighed Palacio's concern for abiding by contractual obligations and the state's obligations under the Ecuador-United States BIT.

Occidental, joined by other US business groups, lobbied the United States Government House Committee on International Relations to pressure Ecuador to provide the desired tax reimbursements. They also demanded that the US government discontinue ongoing FTA negotiations and suspend Ecuador's benefits under the Andean Trade Preferences Act (ATPA) if Ecuador did not comply. FTA negotiations were brought to a halt. A spokeswoman for the US Trade Office issued a media statement denouncing Ecuador's seizure of Occidental assets. The statement also announced that no further free trade discussions were scheduled and that countries must "obey the rule of law with respect to foreign investors" if they hoped to be a free-trade partner of the United States.<sup>79</sup> US financial aid to Ecuador also declined over the two years during which the dispute played out. While USAID spent just over \$40 million on its development programs in the country in 2004, this number was almost halved by 2006. The US government did not however retract Ecuador's ATPA status as it would have risked the country's refusal to co-operate in the War on Drugs, a significant US foreign policy priority in the Americas (Ghaemmaghami 2003/4). The Government of Canada, however, took no official action aimed at disciplining the Ecuadorian government.

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<sup>78</sup> Ibid., pg. 67, para 197 – 199.

<sup>79</sup> "Ecuador oil move prompts US ire," BBCNews 17 May 2006.

While investors' home states often become significant actors in the enforcement of investment rules, their ability and willingness to penalize states that go against IIA obligations is imperfect. Home states have their own set of competing foreign policy concerns and, as chapter four discusses, became increasingly hesitant in the post-WWII era to intervene on behalf of their investors abroad. The ability of IIAs to enrol governments as enforcement agents can be interrupted by the state's foreign policy concerns outside of the dispute at hand. This, in turn, means that IIAs will be enforced unevenly across time and space if the respondent state fails to abide by tribunal orders.

Occidental responded to the contract termination with a second arbitral claim, which was brought to ICSID in 2006. In this case, the tribunal found that Ecuador had acted in accordance with its legal rights in cancelling Occidental's contract according to the contract terms and the Hydrocarbons Law. However, the tribunal also found that the measures Ecuador took in cancelling Occidental's contract without compensation exceeded what the tribunal found to be an appropriate response. Occidental was awarded \$1.77 billion, the full amount that Occidental may have earned if it had operated the original concession area on its own. This was particularly controversial in Ecuador because Occidental had already sold 40 percent of the area over to AEC who had transferred the stake to a Chinese company before the award was rendered. Moreover, Occidental had already received payment for the unauthorized sale of the area, which was one of the primary reasons given by Ecuadorian officials for the contract's termination.<sup>80</sup> This case was also remarkable in terms of the tribunal's willingness to exert its judgment over determining what an appropriate government response is to a breach of domestic law.

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<sup>80</sup> *Occidental v. Ecuador*, award, pg. 326

That is, it was less a matter of public policy than it was a matter of Ecuador's right to penalize TNCs according to the law of the land.

One of the tribunal arbitrators, Bridgette Stern, issued a scathing dissenting opinion, expressing her deep concern with how her colleagues calculated the damages awarded. She wrote,

I consider that the consequence of the fault committed by the Claimants [Occidental], when they violated the Ecuadorian law, is overly underestimated and insufficiently taking into account the importance that each and every State assigns to the respect of its legal order by foreign companies...

The majority's position on the effect of the Farmout Agreement is, in my view, so egregious in legal terms and so full of contradictions, that I could not but express my dissent. In my view, there are two major questionable aspects in the majority's approach...the first is the analysis of the question of the effectiveness of a legal act under Ecuadorian law, which is based on a total lack of reasons, with the consequence that I was not able to follow the "reasoning" from point A to point B, as well as gross errors of law in the purported interpretation of the content of Ecuadorian law; the second, which in my view is even a more serious matter, is the manifest excess of power of the Award nullifying a contract concerning a company which not only was not a party to the arbitration, but moreover...could not be considered, being a Chinese company, as an investor over which the Tribunal had jurisdiction under the US/Ecuador BIT.<sup>81</sup>

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<sup>81</sup> *Occidental Exploration v. Republic of Ecuador*, Decision on Annulment (ICSID Case No. ARB/06/11) pg. 22.

Ecuador's attorneys initiated annulment proceedings against the award using the same translation and argument developed by Stern. State lawyers claimed that the tribunal had manifestly exceeded its powers by interfering in Ecuador's domestic legal processes and that the damages awarded were unfairly calculated. In 2015, an annulment tribunal upheld the original ruling but agreed in part that the original award had been miscalculated. The award was therefore reduced to \$1.06 billion.<sup>82</sup> Although it was not considered a win by Ecuadorian officials, the annulment proceedings did help to substantially reduce the final amount owed.

Though Ecuador was at first unprepared to address the claims, the government rapidly increased its capacity by hiring international law firms. This allowed Ecuador to exploit the expanding network of legal experts experienced in international arbitration. The disputes, however, served to increase public opposition against foreign oil companies, opposition that forced the Palacio government to terminate Occidental's oil contract under threat of impeachment. The generous damages awarded to Occidental further fed opposition to the jurisdiction of third-party arbitral tribunals who were widely seen as defenders of TNC interests. These concerns became intertwined with calls for a reversal of neoliberal policies and the reformation of national political institutions.

### **Hydrocarbons Law 42: The Windfall Tax**

The boom in oil prices after 2002 led to soaring oil production and a sharp increase in the country's crude exports. By 2005, the price of a barrel of oil had more than tripled and continued to rise steadily.<sup>83</sup> By June 2008, Ecuadorian crude prices had

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<sup>82</sup> *Occidental Exploration v. Republic of Ecuador*, Decision on Liability (ICSID Case No. ARB/06/11). pg. 133. para 586.

<sup>83</sup> *Burlington v. Ecuador*, pg. 13 para 24.

risen from US \$15/bbl to nearly US\$ 120/bbl. As growing profits flowed to foreign oil companies, increasing demands came from civil society for greater benefits from the extraction of the country's natural resources. The profits of foreign oil firms were perceived to be excessive given the country's high instances of poverty. In August 2005, the *Contraloría General del Estado* (State Comptroller General), which acts as an external auditing body for state agencies regarding the use of public funds, undertook an audit of existing contracts with oil companies. It concluded that the increase in oil prices generated extraordinary profits and that existing contracts should be renegotiated. In November 2005, then-President Alfredo Palacio announced the government's objective to renegotiate contracts in order to provide the state with a greater share of revenue from crude oil sales.<sup>84</sup>

In 2006, the Ecuadorian Congress amended the country's *Hydrocarbons Law 42* and placed a 50 percent tax on oil exports when oil prices exceeded a benchmark level. This level varied according to the type of crude found in the concession and the original price set out in the concessionaire's contract. The preamble of the new *Hydrocarbons Law* (No. 2006-42) referenced Ecuador's responsibility to "defend the natural heritage of the country and preserve the sustainable growth of the economy, as well as balanced, equitable development for the collective good." It also referred to Article 247 of the Ecuadorian Constitution, which states that "subsoil resources are the inalienable and imprescriptible property of the Ecuadorian government and, therefore, its exploitation must take place on the basis of national interests and in accordance with the principle of reasonability." Oil companies and the Chamber of Manufacturers of Pinchincha brought

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<sup>84</sup> *Perenco Ecuador Ltd. v. Republic of Ecuador*, Decision on Remaining Issues of Jurisdiction and on Liability (ICSID Case No. ARB/08/6), pg. 22 – 23, para 84 – 89.

suits against the government to Ecuador's Constitutional Court to challenge the changes to the law. The Court responded by confirming the constitutionality of the amendments and ruling that the changes did not violate Ecuadorian civil law concerning the contracts.<sup>85</sup> Private-sector actors who opposed the amendments were therefore given little means to influence their implementation. Oil firms were given 45 days to submit new contractual terms conforming to the modified Hydrocarbon Law.

In November 2006, Ecuador's presidential election resulted in the rise of Rafael Correa who campaigned on promises to institute a 'Citizen's Revolution' and '21<sup>st</sup> Century Socialism', involving the turning back of neoliberal policies and the creation of more participatory democratic processes. By framing his political agenda in this way, Correa and the Alianza País gained populist appeal and a majority government composed of nationalist sectors of society, a rare feat in a country known for its volatile and fragmented party system (Acosta and Polga-Hecimovich 2011; Conaghan 2008; Collins 2014). Correa promised voters he would respond to calls for political renewal by convening an assembly to write a new constitution that would redesign governmental institutions and provide a legal basis on which the state's central role in regulating and managing the economy would be renewed (Conaghan 2008, 51).

In October 2007, the administration of the newly elected President Rafael Correa issued a decree, further amending the *Hydrocarbons Law* and increasing the State's share of revenue from sales above the benchmark price from 50 percent to 99 percent. Shortly after, the government passed the *Ley de Equidad Tributaria* (LET, the Tax Equity Law), which aimed to open negotiations with oil companies to avoid the application of Law 42

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<sup>85</sup> *Perenco v. Ecuador*, pg. 27, para 101.

provided that companies agree to ‘fairer terms’ for the allocation of oil revenues. The LET stipulated that the levy on extraordinary profits would be reduced to 70 percent provided that companies agreed to transfer their contract into transitory agreements to signal their willingness to eventually adopt a service contract. In January 2008, Correa gave a public radio address during which he declared that oil companies had three options: comply with the 99 percent windfall tax; agree to transfer the existing contract into a service contract following the old model, or divest their assets in which case Petroecuador would assume control of the oil field.<sup>86</sup> Correa’s primary objective was to convince firms to convert existing contracts into service contracts, which gave the government greater control over oil exploitation and revenue. Companies were given 45 days to renegotiate contracts or otherwise continue with the 99 percent windfall tax.<sup>87</sup>

Contract renegotiations were then suspended by Correa in April 2008 after he announced that all existing agreements were to be terminated within a year and new service contracts employed regardless of ongoing negotiations.<sup>88</sup> Several companies refused to comply with the new terms as well as the windfall tax and instead brought claims to ICSID and UNCITRAL. This included claims by Repsol, Murphy, Burlington and Perenco. In the case of Perenco and Burlington, companies that shared a concession area, Ecuadorian officials responded to the claim by seizing the company’s oil, which it claimed was necessary to auction in order to pay for the company’s outstanding debt related to the windfall tax. Perenco applied to an ICSID tribunal for a provisional measure, asking the tribunal to intervene. The tribunal ordered that Ecuador refrain from

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<sup>86</sup> *Burlington v. Ecuador*, pg. 19, para 37 – 38.

<sup>87</sup> *Ibid.*

<sup>88</sup> *Perenco v. Ecuador*, pg. 34, para 123.

collecting payments owed and by pursuing any action against Perenco until the case was resolved.<sup>89</sup> Ecuador responded in a letter to the tribunal, stating:

Ecuador...is not in a position to implement certain of the [Tribunal] recommendations at this time, in so far as they would restrain Ecuador from enforcing Law 42 against Perenco or the Consortium of which it is a member. Law 42 and its implementing Decrees...were enacted at the highest levels of government, and have been upheld by the Ecuadorian Constitutional Court. Under the circumstances, Law 42 must be applied and enforced, lest the integrity of the legal order be undermined.<sup>90</sup>

Burlington and Perenco subsequently suspended their operations after Ecuadorian officials continued to confiscate oil from their concession areas. Ecuador responded by declaring *caducidad* (*termination*), effectively terminating the companies' contracts and seizing control of the area. Perenco appealed to French diplomats, who pressured Ecuador to discontinue its actions against the companies, however this was to no avail.

The tribunal overseeing Perenco's claim ruled that the first amendment to the *Hydrocarbons Law*, which instituted a 50 percent levy on extraordinary profits, did not amount to a violation of the treaty as it was a matter of taxation deemed appropriate by local courts. However it ruled that the 99 percent levy, in combination with Ecuador's attempts to use the levy to incent the transferring of contracts, violated investor rights to fair and equitable treatment. Moreover, the declaration of *caducidad*, it ruled, amounted to a direct form of expropriation despite Ecuador having the right to operate the oil fields

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<sup>89</sup> *Perenco v. Ecuador*, pg 49 para 169-176.

<sup>90</sup> *Perenco v. Ecuador*, pg. 51, para 177.

in the company's absence.<sup>91</sup> As of the time of writing, an award in the form of damages has been reserved for a future ruling, however Perenco is demanding a minimum of US\$ 440 million.<sup>92</sup>

Since Burlington and Perenco shared the oil concession, Burlington's claim reflected the same issues. However, Burlington also accused Ecuador of violating the BIT provision on 'full protection and security' for its failure to protect the company's exploration and exploitation activities in two of its concession blocks from local indigenous opposition. Burlington alleged that indigenous groups living in and around its concession areas violently attacked their operations and uttered death threats. In one of the blocks, indigenous groups set fire to the company's camp and kidnapped several employees. Burlington responded by evoking a '*force majeure*' clause in the contracts and suspended activities until the company could reach a settlement with indigenous communities. When negotiations failed, Burlington accused the Ecuadorian government of not doing enough to assist the settlement procedure and provide security to the company's installations, personnel and activities.<sup>93</sup> In 2012, the tribunal overseeing Burlington's claim ruled that Ecuador had violated the BIT by expropriating Burlington's concession area without compensating the company. However, the Tribunal also declined jurisdiction over Burlington's claim regarding indigenous opposition because the

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<sup>91</sup> Perenco v. Ecuador, pg 230 – 231.

<sup>92</sup> Constante, Soraya. "Ecuador Litiga con las Grandes Petroleras," El Pais, 14 November 2015.

<sup>93</sup> *Burlington Resources Inc. v. Republic of Ecuador*, Decision on Jurisdiction (ICSID Case No. ARB/08/5) pg. 9 – 10, para 26 – 36.

company had not forewarned Ecuador of this particular aspect of its claim in good time.<sup>94</sup> An award on damages is pending.

The ICSID tribunal overseeing Murphy's claim also ruled that companies had failed to give prior notice to Ecuador of their pending claims and therefore the mandatory six-month waiting period in the BIT had not begun. The case was therefore deemed inadmissible due to the Calvo-clause inspired provision. Another claim was taken up by Murphy under UNCITRAL rules in 2011, however the case has yet to reach a decision and is tied up in a dispute over whether UNCITRAL holds jurisdiction over the matter.

At the heart of these cases is a conflict between Ecuador's obligations to foreign investors under IIAs and the demands of civil society groups that oppose the sale of natural resources to foreign companies. This opposition has been strengthened by repeated conflicts between oil firms and the indigenous groups and communities living within and around concession areas. Since 2001, successive administrations have taken steps to harness a greater share of the profits emanating from the oil sector as a direct response to civil society demands. Fear of political reprisals also drove the Palacio administration to terminate Occidental's contract. IIAs however have provided foreign investors legal channels through which they can challenge threats to their profit-making. In Occidental's second claim, this resulted in the largest award rendered in favour of a foreign investor in history. Ecuador has had some success in defending itself from the claims, yet the awards rendered in favour of investors amount to over \$ 1.169 billion not including pending cases. However, according to the Ministry of Finance, government

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<sup>94</sup> Most BITs provide that claimants must notify governments of its claims six months prior to formally submitting the claim. This is intended to provide the respondent an opportunity to resolve the dispute prior to the claim being brought.

revenues derived from the oil sector increased from US\$ 2.211 billion in 2005 to US\$ 8.675 billion in 2008, reaching a high of \$12.935 billion in 2012.<sup>95</sup> This suggests that the costs of the investor claims prompted by the introduction of the windfall tax and changes to VAT credits are outweighed by the added revenue captured by the state. Yet these disputes have served to confirm the public's skepticism over foreign oil companies, skepticism which became particularly acute with the rising conflict between Chevron Oil and residents of Lago Agrio.

### **Chevron and Lago Agrio**

In 2006, US oil giant Chevron accused the Ecuadorian government of violating the US-Ecuador BIT in its failure to deal fairly and timely with multiple breach-of-contract cases filed against the state in Ecuadorian courts by its subsidiary Texaco Petroleum between 1990 and 1993. At the time of Chevron's original filing in 2006, the domestic lawsuits had been pending for over 13 years. However the timing of Chevron's claim was criticized as an attempt to pressure the Ecuadorian government to intervene in a class action lawsuit brought by residents of the Amazon rainforest against Chevron underway in Ecuador's courts.<sup>96</sup> The class action suit stemmed from a dispute over Texaco's operations in the country between the 1970s and 1990. In 1993, Amazon residents brought the suit against Chevron to US courts and alleged that Texaco had dumped 18 billion tons of waste in the rainforest, resulting in severe environmental damage, cancers, birth defects and miscarriages in surrounding communities. Chevron challenged the residents' claims on the ground that the cases should be heard in Ecuador,

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<sup>95</sup> Ministerio de Finanzas. 2013. Información del Sector Público no Financiero 2000 – 2012. Available at: <http://www.finanzas.gob.ec/category/estadisticas-fiscales/> (accessed 15 February 2016).

<sup>96</sup> Diaz, Fernando Cabrera (2009) "Tribunal Rejects Ecuador's Jurisdictional Objections in Dispute with Chevron." *Investment Treaty News*. January 5.

not the United States. A US judge agreed and proceedings were then taken up in Ecuador in 2003 in *Lago Agrio v. Ecuador*.<sup>97</sup>

Despite Chevron's endorsement of the Ecuadorian judiciary in the class action case, the company argued during ICSID proceedings that the autonomy of Ecuador's constitutional, electoral and supreme courts had declined since 2004 and caused delays in resolving its pending breach-of-contract cases. Chevron further argued that this constituted a violation of the *US-Ecuador BIT*'s provisions on fair and equitable treatment. Ecuador countered by arguing that Chevron's investments in the country ended before the BIT's enforcement in 1997 and that the agreement could not be applied retroactively. The tribunal found that while Texaco withdrew its operations before the BIT's enforcement, the breach of contract cases pending in Ecuadorian courts constituted an investment and therefore fell under the BIT's jurisdiction. In March 2010, the tribunal awarded Chevron almost US\$ 700 million in damages, however this was later reduced to US\$96 million in a 2011 ruling.<sup>98</sup>

Following its loss in the class-action lawsuit, Chevron filed another claim in September 2009. Chevron alleged that Ecuador's judiciary committed fraud in addition to legal and procedural errors and had unfairly favoured its citizens, therefore abusing its criminal justice system in violation of the BIT. Chevron requested it be granted relief that would effectively excuse it from having to pay the almost \$US18 billion awarded to Lago Agrio plaintiffs. This case is unique in that instead of claiming damages from Ecuador in the form of compensation, Chevron aimed to use the tribunal to strip the award from

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<sup>97</sup> Vis-Dunbar, Damon (2006). "Chevron Warns Ecuador on BIT Claim as Contract and Environmental Disputes Persist." *Investment Treaty News*, July 26.

<sup>98</sup> *Chevron Corporation v. Republic of Ecuador*, Final Award (UNCITRAL Case No. 34877), pg 141.

Ecuadorian residents, who are not parties to the BIT arbitration. Ecuador argued that because Chevron's request interfered with the rights of non-parties to the arbitration, the tribunal should not exercise jurisdiction over the dispute, however this argument was rejected. In January 2012, the tribunal ordered Ecuador to "take all measures necessary to suspend or cause to be suspended the enforcement or recognition within and without Ecuador of any judgment against [Chevron] in the *Lago Agrio* case."<sup>99</sup> In response, the Lago Agrio plaintiffs filed a petition for precautionary measures with the Inter-American Commission on Human Rights, explaining the ways in which Chevron's request for relief and the tribunal's orders violated plaintiffs' rights. The plaintiffs later withdrew the petition after an Ecuadorian court ruled that the ICSID tribunal had no power to compel Ecuador's courts to violate Ecuador's human rights obligations.

At the time of writing, a final award in this case is still pending; however an interim award rendered by the tribunal suggests that Ecuador may be found liable for having released Chevron's subsidiary under a prior environmental remediation agreement signed in the 1990s before Chevron's subsidiary exited the market (UNCTAD 2015). If the award is rendered in Chevron's favour, Ecuador could be held accountable for the class action award. This dispute has been particularly controversial in Ecuador given the protracted dispute Lago Agrio plaintiffs went through during the class action suit. Should Ecuador be held responsible for denying Chevron justice in failing to intervene in the class action suit, it will only reconfirm public perceptions regarding the Western commercial bias of third-party arbitral institutions.

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<sup>99</sup> *Chevron Corporation and Texaco Petroleum Company v. Republic of Ecuador*, First Interim Award on Interim Measures (PCA Case No. 2009-23), pg 16.

The Chevron case is less a challenge to public policy than a challenge to Ecuador's domestic legal processes and political space, meaning the opportunities available to civil society to voice demands on the state. A similar challenge was made by Occidental in its second claim, in which the company demanded damages for the expropriation of its assets despite the fact that the expropriation was legal under the firm's contract with the state and Ecuador's *Hydrocarbons Law*. As discussed above, Occidental's win in this case represented an unprecedented extension of arbitrators' oversight over domestic legal processes. The risk in these cases is that IIAs are being leveraged by foreign investors and third party arbitrators in order to extend arbitrators' oversight over countries' domestic legal systems and that countries can be held accountable for smoothing the way for foreign investors that face opposition by civil society groups. It, in turn, may provide an avenue to foreign companies to escape their legal commitments in host-states, as is demonstrated by the Occidental case.

All oil sector cases demonstrate to some extent the potential power of IIAs to bind states to a neoliberal development model once that model has been put into place. Successive efforts introduced by governments to re-define the conditions under which foreign oil companies operate in Ecuador have been strongly contested by foreign investors under BITs with the support of their home-government. While Ecuador has been successful in defending its regulatory changes in some instances, it has also taken on considerable costs to advance important developmental objectives. Ecuador's advantage is that the revenue captured by the regulatory changes have exceeded the direct costs of investor claims however in countries that lack rich resource endowments, their ability to take on the costs of investor claims while introducing post-neoliberal policies may be

dramatically curtailed. Moreover, as is discussed in the preceding section, the strong opposition from a diverse range of civil society groups against foreign oil companies and the politicization of third-party arbitral tribunals has allowed the Correa administration to challenge the authority of the global IIA assemblage without fear of domestic political reprisal.

## **6.2 Ecuador's Defence against Investor Claim**

Conventional approaches to the study of IIAs and policy space suggest that BITs severely limit the capacity of developing countries to enact legislation or carry out policies in favour of the public interest. The cases discussed above certainly suggest that IIAs provide a powerful tool for transnational companies to limit the policy options of host states. However, as this section demonstrates, there are several avenues available to host countries that are willing to challenge investor claims, some of which have been successful in mitigating the costs of investment disputes.

### **Procedural-Legal Tactics in Investor-State Arbitration**

Ecuador has fought each investor claim on its merits within the parameters of arbitral proceedings. Similar to Argentina's approach, Ecuador has challenged the jurisdiction of each arbitral tribunal using the legal channels provided to assert that the disputes would be better addressed by Ecuador's domestic courts. The cases against Ecuador, however, deal most often with matters of taxation, which are typically addressed under domestic administrative and legal bodies. In the VAT cases, for instance, Ecuador's counsel argued that changes to the country's tax regime fell under the authority of its domestic legal system, an argument that was received inconsistently across arbitral tribunals. Ecuador's attorneys have objected most strongly to the authority of ICSID

tribunals as opposed to UNCITRAL tribunals as the Correa administration believes ICSID to be dominated by Western corporate interests. According to Luis Guamangate, National Assembly member and member of the Alianza Pais, “The [ICSID] system as it currently stands is heavily biased in favour of the transnational companies that these [investment] agreements are meant to protect.” ICSID arbitrators also come from a small pool of international lawyers and legal experts who state officials believe have an inherent bias towards Western interests due to their training in Western institutions.

Belief in ICSID’s systemic bias has informed much of the strategy state lawyers have adopted towards combating investor claims. For instance, Ecuador has consistently challenged the way in which ICSID arbitrators are chosen. According to the rules governing ICSID arbitrations, each tribunal is to have three members, two of whom are chosen by parties to the dispute and one additional arbitrator is appointed by ICSID. According to Ecuadorian officials, this means that state interests will typically be outweighed, as the majority of tribunal members are chosen by parties that favour commercial interests. Similar to the case of Argentina, Ecuador has also made repeated attempts to dismiss arbitral members out of a suspicion of bias or conflict of interest however such attempts are rarely successful.

It is important to note that Ecuador’s skepticism toward ICSID has not prevented state attorneys from using ICSID rules to pursue counter-claims against foreign oil companies. In 2011, state attorneys filed a counter claim against Burlington and Perenco for environmental and infrastructural damage in the companies’ joint concession area and demanded \$2.549 billion from the companies to pay for an environmental assessment and

clean up.<sup>100</sup> Ecuador alleged that an external audit of the concession areas had revealed significant volumes of contaminated soil and underground water pollution in breach of the concession contract and Ecuador's domestic environmental laws. Expert witnesses from Petroamazonas (an offshoot of Petroecudaor), the company leading the external audit and the San Francisco de Quito University were brought in to attest to the environmental damage. In its interim decision, the Tribunal ordered an external audit to be conducted by its own expert panel in order to assess the environmental damages. Therefore, rather than reject ICSID rules entirely, Ecuador is seeking ways to interpret them and manoeuvre under them in a way that would enhance the government's ability to hold the companies responsible for perceived infractions of domestic law. It is also important to note that unlike Argentina, Ecuador has paid the awards rendered in favour of investors after annulment attempts confirmed the awards.

Since many of the claims against Ecuador are relatively recent,<sup>101</sup> it is difficult to determine the degree to which Ecuador has had success in thwarting investor claims through the legal channels available. However, of those cases for which a ruling has been given, Ecuador has won a favourable award more times than it has lost, which suggests the country has been more successful than Argentina in earning a favourable award (see Table 2). Ecuador's higher success rate is likely due to a variety of factors, including the nature of the dispute, the lines of legal defence available (Ecuador was often able to take advantage of BITs' exemptions on matters of taxation) and the composition of the legal team. In hiring prestigious international law firms with the technical and human resources

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<sup>100</sup> *Perenco Ecuador Limited v. Republic of Ecuador*, Interim Decision on the Environmental Counterclaim (ICSID Case No. ARB/08/6), pg 7 para 34.

<sup>101</sup> A single arbitral claim can take more than ten years to complete.

required, Ecuador was also able to avoid the learning curve experienced by Argentina’s legal team. The disadvantage, however, is that Ecuador’s Attorney General Office will not be as likely to retain the same institutional memory with respect to ISDS cases and procedures nor will it have access to the same domestic pool of experienced international lawyers in the future. Although estimates of Argentina’s own legal costs are not available, it is likely that contracting out legal defences to international law firms is also more expensive than hiring state lawyers.

**Table 2 Current Status of ISDS Cases against Ecuador**

Status	In favour of Investor	In favour of State	Settled / Withdrawn or Suspended	Pending	Total*
Number of Cases	4	5	3	10	22

\*Number of cases where information is publically available

Source: UNCTAD Investor-State Dispute Settlement Database (accessed 20 May 2015).

### **Domestic Pressures**

Outside of the arbitral proceedings, the Ecuadorian government has proved adept at leveraging different forms of social and traditional media to raise awareness about the injustices it perceives in the international arbitral system. Much of the government’s confrontational discourse has been directed at foreign oil companies and ICSID. Since being in power, Correa has used public radio addresses, twitter, televised appearances, press meetings and print media to scold oil companies, particularly Occidental and Chevron, for undertaking actions against the public interest. The PGE has also been instrumental in supporting an anti-Big Oil discourse by developing and releasing Youtube videos portraying high profile disputes (Occidental, Chevron, Burlington and Perenco) in

five to ten minute video clips.<sup>102</sup> The PGE also releases regular updates on the cases it is fighting and has been in regular contact with major media outlets as the cases develop. Details of case proceedings, the legal and procedural costs of the disputes, and the amount awarded to successful foreign investors have also been published on the PGE's website.

This public outreach and media campaign is driven by a dual logic. On one hand, it is a response to civil society demands for information and transparency. Given the highly politicized nature of the disputes and the oil sector more broadly, civil society groups have monitored the arbitral proceedings closely and have pressured the government for more inclusive processes. Early on, failure to keep the public informed about the proceedings led to demands by civil society groups for the resignation of PGE officials. PGE resources have been stretched thin by the numerous cases brought against the country and the need to disseminate information to the public in a timely manner.<sup>103</sup>

On the other hand, it has also been driven by a desire to mobilize public opposition against foreign oil companies to solidify the government's bargaining stance vis-à-vis the oil companies and to create a public discourse around the image of Correa and the governing party as defenders of Ecuador's sovereignty and public interests. This reflects Béland's (2009, 702) argument that particular ideas can be wielded by policymakers to generate public support for an initiative aimed at challenging a prevailing arrangement. The images and discourse used in the PGE's public outreach campaigns, for instance, depict corporate claimants as devils fighting against Ecuador's

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<sup>102</sup> Most video clips are also linked to the PGE's website. See for example: [http://blogoxy.pge.gob.ec/?page\\_id=1757](http://blogoxy.pge.gob.ec/?page_id=1757).

<sup>103</sup> Interview with former state attorney with the State's Attorney Office (October 9, 2014)

public interests (see Illustration 1). Mobilizing public support around the government as the state defender also has the effect of buttressing the government's political support in a public where the presence of foreign companies has historically been heavily contested. It has also led to a sense of nervousness amongst domestic law firms representing corporate clients in investor-state disputes. Attorneys in such law firms have been concerned over the possibility of having a public smear campaign launched against them by government officials that could tarnish their professional reputation and personal relationships.<sup>104</sup> This is compounded by threats made by the government to pursue criminal charges against foreign investors' legal representatives.

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<sup>104</sup> According to interviews with two former members of corporate claimants' legal teams in Quito (October 15 and October 21 of 2014).

**Illustration 1 Depiction of ISDS Proceedings Developed by the Attorney General  
Office for Public Outreach**



Translation: “And what about the laws of my country?”

Source: Procuraduría General Del Estado. 2014. Available at: [www.pge.gob.ec](http://www.pge.gob.ec) [retrieved 14 April 2014].

**Disengaging from the Global IIA Assemblage**

As part of Correa’s project of political and institutional renewal, the Ecuadorian government began to assess their options to withdraw from aspects of the global IIA regime. In 2007, Ecuador notified ICSID that it would not consent to arbitration for disputes concerning the exploitation of natural resources (Cadena and Montañes 2007, 154). The notification dated 4 December 2007 stated:

The Republic of Ecuador will not consent to submit to the jurisdiction of the International Centre for Settlement of Investment Disputes (ICSID) disputes that

arise in matters concerning the treatment of an investment in economic activities related to the exploitation of natural resources, such as oil, gas, minerals or others. Any instrument containing the Republic of Ecuador's previously expressed will to submit that class of disputes to the jurisdiction of the Centre, which has not been perfected by the express and explicit present notification, is hereby withdrawn by the Republic of Ecuador with immediate effect as of this date.

This move was more symbolic than practical, as Ecuador granted prior consent to ICSID without exempting natural resource sectors during the ratification of various BITs. To exempt a sector from any aspect of the BIT, including its dispute settlement provisions, countries must identify such restrictions in the negotiating stage. Moreover, the Ecuadorian government also included recourse to ICSID over disputes in many of the concession contracts it signed with oil companies.<sup>105</sup> This meant that Ecuador's consent to ICSID jurisdiction is woven into a variety of points throughout the global IIA assemblage.

Ecuador's refusal to submit to ICSID arbitration for these classes of disputes was tested in *Murphy v. Ecuador*. The Murphy tribunal found that neither the ICSID Convention nor the BIT "allows parties to withdraw from its application with immediate effect." Moreover, the *Vienna Convention on the Law of Treaties* only provided for the termination of a treaty by agreement of the contracting states, which Ecuador had failed to obtain.<sup>106</sup> The Tribunal therefore rejected Ecuador's objection to ICSID jurisdiction over natural resource disputes. Ecuador responded by announcing that it would consider contracts with oil companies void unless ICSID is removed as a potential venue for

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<sup>105</sup> Interview with former attorney for claimant against Ecuador, Quito (21 October 2014).

<sup>106</sup> *Murphy v. Ecuador*, Decision on Jurisdiction, pg. 22 para 86.

arbitration. As an alternative, Ecuador offered Chile's Centre for Arbitration and Mediation and has begun integrating this venue as the preferred arbitration mechanism in contracts with foreign oil companies (Diaz 2008, 6).<sup>107</sup>

In 2008 Ecuador denounced BITs with El Salvador, Cuba, Guatemala, Honduras, Nicaragua, the Dominican Republic, Paraguay, Uruguay and Romania. This denunciation received widespread support within the National Assembly, which passed the ratifying legislation to formally terminate the agreements. Government officials argued that the agreements failed to bring significant benefits to the Ecuadorian economy and could serve as instruments for 'forum shopping' investors in the future.<sup>108</sup> However it is important to note that cancelling BITs does not have automatic effects. Most BITs contain a 'survival clause' that makes the agreements' provisions applicable for an additional 10 to 20 years following the agreement's termination.

The passing in Ecuador of a new constitution in September 2008 provided a new legal basis on which Ecuador could withdraw from the global IIA assemblage. Article 422 of the new constitution prevents the Ecuadorian government from ceding the country's sovereign jurisdiction to international arbitration entities outside of Latin America via international treaties or arrangements. This provision is, in part, a manifestation of the widespread dissatisfaction in Ecuador with arbitral rulings and highly publicized battles with oil companies (Gomez 2012).<sup>109</sup> Under international law, countries cannot use national legislation, including their constitutions, to escape

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<sup>107</sup> Interview with former attorney that represented corporate claimants in ISA proceedings, Quito (October 21 2014).

<sup>108</sup> Interview, Adrián Cornejo, Secretaría Nacional de Planificación y Desarrollo (National Planning and Development Secretariat), Quito (October 12, 2014).

<sup>109</sup> Under international law, countries cannot use national legislation to escape obligations under international treaties. However Ecuador's Constitution gives explicit supremacy to constitutional provisions over international treaties.

commitments made under international treaties. However the 2008 constitution gives itself explicit supremacy over international treaties. The Correa administration's refusal to accept the supremacy of international law has also informed its dismissal of tribunal orders in some ISDS cases, most notably Ecuador's continued confiscation of Perenco's oil despite tribunal orders to stop.

The approval of the 2008 Constitution granted the government increased legitimacy to pursue two additional measures regarding the global IIA assemblage. First, Ecuador moved to formally denounce the ICSID convention as a violation of Article 422. The request was adopted in July 2009 with widespread Congressional support. Secondly, Correa requested approval from the National Assembly to denounce additional BITs on the grounds that they also conflicted with the 2008 constitution.<sup>110</sup> This was met with strong protest by Ecuador's internationally-oriented business groups who argue that the country's decisions are scaring away needed investments. The National Assembly returned Correa's request to the executive office on the grounds that such a move required the prior ruling of the Constitutional Court (Gomez 2012, 462-463).

The Constitutional Court ruled that most of the BITs contained provisions that were unconstitutional and granted the National Assembly the authority needed to denounce them. Thus far, Ecuador has denounced eleven BITs, most recently those with Germany and Romania (UNCTAD 2015). Most surprisingly, Ecuador has not withdrawn from its BIT with the US, under which the majority of investor claims have been brought (See Figure 1). Ecuadorian officials argued that this is because the BIT continues to

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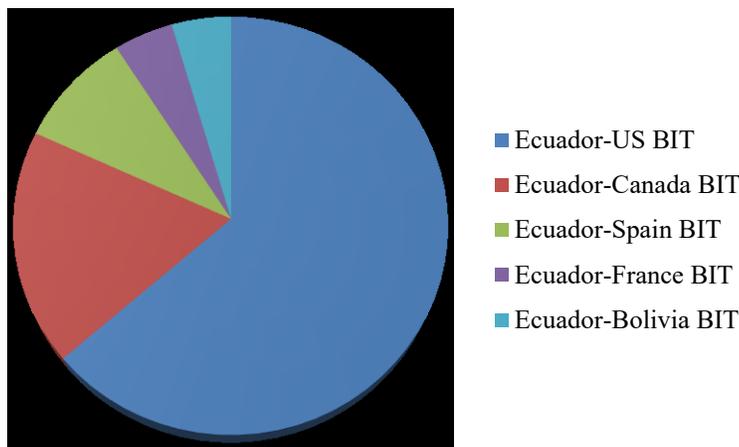
<sup>110</sup> This included BITs with Finland, Sweden, Canada, China, the Netherlands, Germany, France, the United Kingdom and Ireland according to Galindo (2012, 253).

provide Ecuador with economic benefits in helping to secure foreign investment.<sup>111</sup>

Therefore, while the disputes with US oil companies have prompted the re-evaluation of Ecuador's position towards IIAs, there are limitations in how willing the country is to go in terms of isolating itself from the global IIA assemblage. Indeed, Correa's hesitation to withdraw from the US-BIT speaks to the power of the ideas constructed around IIAs in the 1990s which framed the agreements as a necessary means to attract and maintain foreign investment.

**Figure 6: Number of Investment Disputes brought under IIAs**

Source: UNCTAD 2015.



In October 2012, the Correa administration established the *Citizens' Commission for a Comprehensive Audit of Investment Protection Treaties and of the International Arbitration System on Investment* (CAITISA). CAITISA is modeled after a similar commission established to audit the country's foreign debt and is composed in equal numbers of foreign experts, government officials and civil society representatives (four

<sup>111</sup> Interview with Luis Guamangate, National Assembly Member and member of Alianza País (October 8, 2014).

representatives from each sector). The Commission is responsible for auditing the constitutionality of Ecuador's remaining BITs and the country's performance in investor-state disputes. The Commission was also asked to propose legal and political alternatives regarding BITs and the international arbitration system.<sup>112</sup>

Although the discourse surrounding this Commission is steeped in the same language of political inclusivity that is characteristic of the 'Citizen's Revolution,' its members have been handpicked by the executive and are known to have left-leaning sympathies and a nationalist logic. Many of the Commission's members also served on a commission established in 2008 that was charged with reviewing Ecuador's foreign debt arrangements. The latter commission found that the debt agreements Ecuador had entered into under previous governments were unjust, which prompted the Correa government to default on almost \$3.2 billion in global bonds. This decision dramatically limited the country's access to international capital markets. In the draft report, the CAITISA recommends that Ecuador denounce existing BITs and negotiate new instruments in the form of unilateral contracts with foreign investors or investment treaties based on a revised model. It does not comment on the content of BITs except for a broad recommendation to exclude ISDS clauses and specify investor obligations.<sup>113</sup>

### **Reforming the Global IIA Assemblage**

Ecuador has also led several regional initiatives and alliances aimed at increasing Latin America's ownership over investor-state relations and arbitration. In June 2009, at

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<sup>112</sup> Interview, Adrián Cornejo, Secretaría Nacional de Planificación y Desarrollo (National Planning and Development Secretariat), Quito (October 12, 2014). This section is also informed by an interview with Javier Achaide, member of the Commission for a Comprehensive Audit of Investment Protection Treaties and of the International Arbitration System, Quito (October 21, 2014).

<sup>113</sup> According to interviews held with former attorney for corporate claimants against Ecuador, Quito (October 15 and 21, 2014). Update on CAITISA report can be found in IISD. 2016. "Ecuador's Audit on Investment Treaties: CAITISA Reports Leaked," Investment Treaty News, 29 February.

the meeting of the Organization of American States, Ecuador's Foreign Minister Fander Falconi called for the establishment of an alternative arbitration center under the auspices of UNASUR. This initiative was re-stated by Correa at a 2012 UNASUR meeting during which he stated:

Under international investment agreement, whomever wants to can being a claim against a sovereign state to centers of arbitration, in many cases ICSID, to defend their interests. [Arbitrators] always decide in favour of Big Capital and not in favour of the truth. The recent award rendered in favour of Occidental demonstrates the side that ICSID is on (author's translation).<sup>114</sup>

Correa's call for the establishment of an alternative arbitral mechanism has since received widespread support from Latin American partners. Though negotiations are ongoing, Ecuador's priorities have focused on three areas:

One is to incorporate greater rules of transparency, particularly in the selection of arbitrators. Secondly, we want to establish a more consistent and institutionalized appellation body and third, to incorporate rules that are more responsive to governments' constitutional obligations in ways that do not require the government to surrender its autonomy (author's translation).<sup>115</sup>

Ecuador also led the establishment of an alliance known as the *Conference of Latin American States Affected by Transnational Interests* with Bolivia, Cuba, Nicaragua, Venezuela and several Caribbean countries. Alliance members agreed to encourage

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<sup>114</sup> Office of the President of Ecuador. 2012. "Ecuador Proposes the Creation of a Regional Arbitration Centre at UNASUR." November 30. Available at: <http://www.presidencia.gob.ec/ecuador-propone-a-unasur-la-creacion-de-instancias-de-arbitraje-regional/> (accessed October 21, 2014).

<sup>115</sup> Interview, Adrián Cornejo, Secretaría Nacional de Planificación y Desarrollo (National Planning and Development Secretariat), Quito (October 12, 2014).

information-sharing and to coordinate political and legal actions related to investor-state disputes. This has resulted in the establishment of the Southern Observatory on Transnational Corporations, an institution meant to facilitate information sharing on defence strategies while providing training to government officials to build their capacity to defend state interests during investor-state disputes (Third World Network, 2013).

It is important to note that Correa and his administration continue to support BITs in principle, provided that they are modified to more strongly preserve national interests. Ecuador developed a new model BIT entitled “Investment for Development Agreement”, which contains explicit references to government responsibilities to protect the environment and sustainable development interests of its public over the interests of foreign investors. This model recently informed Ecuador’s Trade for Development agreement with the European Union and will be used as a basis on which to negotiate future agreements.<sup>116</sup>

The Correa administration’s attempts to reform the global IIA assemblage represent an effort to redefine investor-state arbitration in a way that provides governments with a greater degree of flexibility to promote development objectives and protect domestic interests while remaining in the parameters of prevailing investment rules. Officials believe that under the current global IIA assemblage, “There is no room for advancing progressive social and political objectives under such arrangements

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<sup>116</sup> Interview, Adrián Cornejo, Secretaría Nacional de Planificación y Desarrollo (National Planning and Development Secretariat), Quito (October 12, 2014). It should be noted that Ecuador essentially acceded to an EU agreement with Peru and Colombia, therefore Ecuador’s ability to alter the text of the investment chapter was minimal. The chapter does however contain the more progressive provisions desired by Ecuador on the environment and sustainable development.

[author's translation]."<sup>117</sup> Correa therefore does not reject the fundamental purpose and principles of BITs but rather seeks to achieve a fairer balance between corporate and public interests. Whether such mechanisms will be effective in opening up greater space has yet to be tested.

### **International Partnerships**

While Ecuador's actions have been heavily criticized by the US government and US business groups, as with Argentina, the availability of other economic partners has provided Ecuador with an alternative to strengthening traditional economic ties. Some economic partners, including the European Union, appear to be more tolerant of Correa's reformist approach towards the global IIA assemblage than its traditional trade partners, notably the United States. As in other petro-states, the exploitation of oil remains central to Correa's modernization project. Revenues from the oil sector have been used to expand the funding of social programs and state subsidies (Perreault and Valdivia 2010, 692). Correa is therefore seeking to enhance commercial ties with non-traditional partners including China, Russia and the Middle East, countries that are perceived to be less likely to interfere in the articulation of Ecuador's sovereignty and have interest in its natural resources (Conaghan 2008, 56). Chinese firms have been particularly aggressive towards the Ecuadorian market, and have bought out several concession areas previously owned by US and Canadian investors that existed Ecuador following investment disputes, including the area once operated by EnCana.

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<sup>117</sup> Interview, Luis Guamangate, National Assembly Member and member of Alianza País (October 8, 2014).

### **6.3 Factors Informing Ecuador's Response to Investor Claims**

In this section, I assess more closely how competing factors interacted to shape the influence that IIAs had over policy space in Ecuador. As discussed in chapter three, the policy space available to policymakers is defined largely by the perceptions of policymakers themselves as they interact with their material and political environments. Such perceptions are shaped by ideational and material factors, including policymakers' causal and normative beliefs, the resources available and the properties of nonhuman actants, the most relevant of which in this case are IIAs.

#### **Material Factors**

As in the case of Argentina, minor variations between IIAs and the way in which arbitrators engaged with them had an important impact on the degree to which foreign investors have been able to leverage IIA provisions to challenge Ecuador's policies. However, Article 422 of Ecuador's 2008 Constitution, which prevents Ecuador from ceding jurisdiction to third-party arbitral tribunals outside of Latin America can be seen as an attempt to interrupt the linkages between the country and particular components of the global IIA assemblage. Indeed, the Article has been used to legitimate Ecuador's withdrawal from ICSID jurisdiction and, by extension, the oversight of ICSID arbitrators. It has not (yet) been used to limit the jurisdiction of arbitral proceedings convened under UNCITRAL tribunals, which are also conducted outside of Latin America. The reasons for this are discussed more fully in the sub-section below.

Capital flows have played a dual role in Ecuador's disputes with foreign owned oil companies. On one hand, rising oil prices from 2002 to 2005 and the profits flowing to foreign oil companies served to strengthen civil society perceptions that foreign oil

companies were benefiting from Ecuador's natural resources while Ecuadorians remained impoverished. This, in turn, increased demands for government action aimed at capturing a greater share of the profits from oil exploitation. Government officials were therefore encouraged to break with IIAs under threat of dismissal. This suggests that domestic needs for capital can intersect with social forces to interrupt the potential constraints IIAs place on policy space. On the other hand, the expanded revenue captured by government officials after the introduction of the windfall tax increased the capacity of the Correa administration to challenge the authority of the global IIA assemblage. The introduction of the windfall tax was widely supported by the Ecuadorian public and political officials and generated support for Correa's fight against foreign oil companies. The costs of investor claims were also outweighed by the expanded revenue captured by the state. It also helped insulate the Correa administration from the threats of traditional economic partners, such as the United States, as Correa was able to maintain and expand state spending using oil revenues. External partners therefore had few levers with which to pressure the Correa administration to adhere to investor demands. However, since oil prices have hit a new low in global markets, Correa may be less willing to challenge foreign oil companies in the future. Moreover, Ecuador's continued dependence on foreign investment and technologies has limited how far the government is willing to go to break with the global IIA assemblage.

### **Ideational Factors**

Towards the late 1990s and early 2000s, growing civil society activism and demands for a greater share in the benefits from oil exploitation increased policymakers' perceptions of political risk and reprisal. This led the Noboa administration (2000-2003)

and the Palacio (2005-2007) administration to institute some of the first regulatory changes in the oil sector, which were aimed at capturing a greater degree of the revenue from oil extraction. Public opposition to foreign oil companies was further fed by the claims introduced by oil companies against Ecuador under IIAs and Ecuador's loss in high-profile cases. The Correa administration has harnessed this activism to support his political position and the fulfillment of its post-neoliberal project.

Ecuador's approach to the global IIA assemblage has been strongly informed by the left-leaning ideology of the Correa administration, particularly the concern for reasserting state authority that was perceived to have been lost to the introduction of neoliberal policies. However, it is interesting to note that much of Correa's protest against the global IIA assemblage has been directed explicitly at ICSID rather than other third-party tribunals more generally. In recent years ICSID has taken steps to increase the transparency of investor-state disputes under its jurisdiction, including by publishing the awards and major decisions on its website. Ironically, tribunals established under UNCITRAL rules have fewer obligations to open their proceedings and do not publish legal transcripts online. Yet, UNCITRAL tribunals have been less politicized in Ecuador than ICSID tribunals. This is likely due to the fact that most cases brought against Ecuador before it denounced the ICSID convention in 2008 were brought to ICSID (see Appendix Four). However, three of the most controversial disputes prior to 2008 were convened under UNCITRAL rules. This includes Occidental's first claim (over VAT credits) in 2002, EnCana's 2003 claim and Chevron's 2006 claim related to allegations that Ecuador failed to deal in a timely manner with breach-of-contract suits brought against the state in the 1990s.

The skepticism amongst members of the governing party, Alianza País, about ICSID bias stems from ICSID's affiliation with the World Bank, an institution that historically has been dominated by the neoliberal ideology and interests of the United States and other Western powers who exercise significant voting power in the institution. The World Bank is also seen as closely allied with the IMF, which played an important role in pushing forward the adoption of neoliberal reforms in Ecuador. Ecuadorian officials object less to the authority of UNCITRAL tribunals because the United Nations has historically helped preserve the interests of developing countries.<sup>118</sup> UNCITRAL's governing body is also composed of 60 member states elected by the General Assembly and is structured in a way that ensures representation of the world's geographic regions, economic and legal systems. Ecuador was elected to the Commission in 2013 for a term of six years.<sup>119</sup> UNCITRAL tribunals are therefore believed to be less susceptible to the influence of Western powers. However there is no evidence to support the argument that UNCITRAL rules help states to better preserve domestic interests. Moreover, as discussed in chapter four, United Nations institutions, such as UNCTAD, played an important role in promoting the diffusion of the global IIA assemblage in Latin America during the 1990s.

As in Argentina, the idea that IIAs are a necessary means to promote economic development has had a lasting impact in Ecuador, despite the Correa administration's ideology. Fears of capital flight and of scaring away future investments have deterred the Correa administration from cancelling BITs with traditional economic partners, including

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<sup>118</sup> This is according to interviews with two advisors to National Assembly members held in Quito on October 7 and 8, 2014 and an interview with Luis Guamangate, National Assembly member, Quito (October 8, 2014).

<sup>119</sup> UNCITRAL. 2015. "Origin, Mandate and Composition of UNCITRAL" Available at: <http://www.uncitral.org/uncitral/en/about/origin.html> (accessed February 15, 2016).

the United States-Ecuador BIT under which most investor claims have been brought. The ideational legacy of IIA promotion has therefore limited how far Correa is willing to go to isolate Ecuador from the global IIA assemblage. Correa's advancement of a reformed model of IIA, which suggests that officials continue to believe that IIAs help attract foreign investment. This is despite that, as discussed in chapter two, there is little evidence to support the argument that IIAs do in fact help countries to attract greater levels of foreign investment than would otherwise be the case in the absence of such an agreement. Correa's preference for retaining investor-state arbitration in Latin America also speaks to a renewed sense of solidarity with Latin American partners. This sense of solidarity has also informed Correa's efforts to establish an alternative arbitration centre under the auspices of UNASUR.

#### **6.4 The Impact of IIAs in Ecuador**

In this section, I conclude with an assessment of what the Ecuadorian case tells us about how IIAs impact policy space and compare these insights against common assertions found within conventional critical literature on IIAs. Namely, I assess whether such assertions continue to hold in light of this case study.

*A.: IIAs deter the use of policies that conflict with investment rules consistently across time*

This case demonstrates that IIAs have had varying and inconsistent impacts across time. Ecuadorian officials were largely caught off guard by the first claims brought by foreign investors related to the VAT credit changes. However, investment rules failed to deter the government from adopting further changes to its tax regime thereafter. Investor claims only fueled civil society opposition and the Correa administration's resistance to

the authority of ICSID and its arbitrators. However it should be noted that the Correa administration's negotiations with oil companies that did not bring an arbitral claim have been highly secretive. The continued operation of many foreign oil companies in Ecuador suggests that oil companies have received incentives to stay in the market, which may include reductions to the application of the Windfall tax.

However, it is important to note that Ecuador has hesitated to cancel its BITs with large economic partners such as the United States. This is despite the fact that the majority of investor claims brought against it have been under the US-Ecuador BIT. This is because there is a continued belief that BITs help attract needed investments and that cancelling them may lead to capital flight or stymies on incoming foreign investment. Ecuador remains highly dependent on foreign capital and technology to exploit its natural resources, which limits the country's willingness to isolate itself from the global IIA regime. Therefore, although Ecuador's resistance to the authority of investment rules and arbitral tribunals means that they have little deterrent effect when it comes to the government's economic and development agenda, the norms and expectations the global IIA regime continues to hold over the Ecuadorian government has deterred it from taking further measures.

*B. Foreign investors and other actors are always successful in disciplining governments for breaking with investment rules.*

As of the time of writing, Ecuador has lost four cases brought against it and has won out in five (see Table 2). This suggests that Ecuador's team of lawyers has been more successful than not in defending domestic interests. However, the awards rendered against Ecuador in the cases that it has lost have been severe. Occidental's award was the

largest ever handed down in the history of investor-state disputes. The Chevron case also demonstrated arbitral tribunals' willingness to judge the appropriateness of government responses to contractual breaches, even when the actions taken by the government are within its legal rights according to domestic legislation. Correa has leveraged its losses in investment disputes to fuel domestic opposition to select oil companies and buttress public support behind its reformatory agenda. However politicizing the oil industry in such a way has also restrained the concessions governments can make to oil companies now and in the future.

Ecuador's failure to recognize the authority of arbitral bodies over domestic legislation highlights the limitations of enforcement mechanisms in the global IIA assemblage. Ecuador has paid several awards rendered against it, however whether it will choose to do so in the future is questionable. This is particularly true in light of the constitutional barriers it has erected to the authority of the global IIA regime. The availability of regional and extra-regional economic partners has given it extra latitude to maneuver in the face of diplomatic pressures from traditional trade partners. While the US drastically reduced its financial aid to Ecuador following the VAT disputes, it has remained rather insulated from the effects as social spending has been funded largely by the state's oil and mining revenue. This has been compounded by high oil prices across the last decade, which has given Ecuador a degree of independence from global capital markets. However, as oil prices continue to sink the country is more likely to feel the disciplinary effects of its hard lined approach in investment disputes.

*C. IIAs reduced the government's abilities to fund policies and programs in the future after breaking with investment rules.*

As of the time of writing, Ecuador has paid a total of US 181.5 million in compensation to foreign investors for three investor claims (see Table 2). In addition, according to government figures, the PGE has paid more than US\$44.1 million in legal costs for only 11 cases rendered against it. This does not include the costs of legal representatives, arbitral fees and compensation in 12 pending claims, including the \$1.016 billion award rendered in favour of Occidental. This award alone accounts for 1.76 percent of Ecuador's annual GDP in 2013 figures or almost 25 percent of the country's entire spending on health. Yet, Ecuador's poverty rates have steadily declined from 32.8 percent in 2010 to 22.5 percent in 2014 while the country's GDP has risen, reaching \$US 100.9 billion in 2014 from \$46.8 billion in 2006.<sup>120</sup> This suggests that the costs of restructuring the oil sector and reversing neoliberal policies may be outweighed by long-term benefits. Yet, this growth is heavily dependent on Ecuador's oil wealth therefore, whether it can be maintained in light of fluctuating oil prices is questionable.

Similar to the case of Argentina, Ecuador's experience with economic restructuring under IIAs demonstrates the importance of examining the impacts of IIAs on policy space in light of domestic agency. It supports the conclusion that the constraints IIAs impose on countries' domestic policymaking processes are contingent and can be mediated by defence strategies. While both Ecuador and Argentina demonstrate significant limitations in how far they are willing to go to challenge the global IIA regime, government officials in both countries have been adept at leveraging domestic resources and building institutional capacities that help to mitigate the costs of investor claims. While IIAs have significantly increased the costs of going against investor rights in both

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<sup>120</sup> According to World Bank statistics available at: <http://www.worldbank.org/en/country/ecuador> (accessed 15 February 2016).

case studies, understanding the real outcome of IIAs on policy space requires examining the middle messy ground between the constraints IIAs impose and domestic resistance.

## **7 Chapter: Reclaiming State Agency under Investment Rules**

As the cases of Ecuador and Argentina demonstrate, governments do not always abide by international legal obligations nor do they sit idly by as investors bring claims against them. Rather, governments use different tools and resources to defend domestic interests, such as policy space, with some degree of success. These dynamics are not captured by theoretical approaches that stress the cohesiveness and structural powers of IIAs. In this chapter, I compare the impacts of IIAs in both case studies to draw out some general conclusions regarding the relationship between IIAs and policy space when we factor in the agency of state actors. I then assess the different factors that informed each government's response to investor claims, focusing particularly on the Kirchner and Correa governments. Lastly, I summarize the theoretical contributions of this study and acknowledge its limitations, which correspond to the areas I then identify for future research.

### **7.1 Policy Space and the Messy Middle Ground**

Examining the friction created by interactions between the global IIA assemblage and domestic actors and contexts provides a more complex and nuanced understanding of when and under what conditions investment rules infringe upon the capacity of state actors. As discussed in chapter two, critical scholars have often made the claim that IIAs lock states in to investor-friendly regulatory frameworks by deterring the use of policies that break with investment rules. Yet this is not true in all cases across all contexts. The high number of investor-state disputes in recent years demonstrates that governments, knowingly or not, break with investment rules. In this section, I examine the conditions

under which state officials in Argentina and Ecuador broke with investment rules and discuss what this tells us about the nature of policy space under IIAs.

IIAs did not deter governments from adopting policies that conflict with investor rights under IIAs. In Argentina, the government adopted measures that policymakers believed were necessary to placate the symptoms of an increasingly urgent political and economic crisis. This is despite their awareness that such policies would negatively impact foreign investors and were therefore likely to infringe upon investors' treaty rights. The decision to introduce the emergency measures was informed by the crisis conditions as well as the perceived need to ensure citizens affordable access to basic services including water, which is a human rights obligation under public international law. Perceptions of the necessity of these measures were reinforced by nationwide protests and civil society demands for state action in defence of the public interest. This case therefore demonstrates that officials will break with IIA obligations in a crisis context and to meet human rights obligations.

In Ecuador, the decision of state officials in the Palacio administration to begin modifying the regulatory framework governing oil exploitation was influenced by civil society demands for greater benefits from oil production and by massive protests against specific companies such as Occidental. In the Occidental case, it was the threat of impeachment that eventually prompted President Palacio to terminate Occidental's contract and expropriate its assets. When Correa was elected president in 2006, further regulatory changes were made as officials perceived it to be a necessary means to advance Correa's development goals and the Citizens' Revolution. This suggests that

governments can and will break with investment rules to meet civil society concerns and to advance development objectives.

In both cases, policymakers believed that adhering to investment rules was not a politically viable option given the social unrest and urgent demands for state action. This suggests that domestic political conditions, as they interact with policymakers' causal beliefs, can shape policymakers' perceptions about which policies are necessary and politically feasible. In both cases, policy space was expanded to include policy options deemed illegitimate under IIAs. This challenges the common assertion in IIA literature that investment rules lock states in to particular regulatory frameworks as it demonstrates that governments can and do go against investment rules to advance significant public interests. We therefore must nuance our assertions about how and in what contexts IIAs might deter certain forms of government action or prevent the emergence of policy alternatives.

Yet it is important to note that IIAs significantly raised the costs of introducing these policies. Foreign investors leveraged the agreements to sue their hosts unilaterally, which resulted in costly and protracted legal battles. This includes an original award against Ecuador of \$1.7 billion, one of the largest awards to be rendered in favour of a foreign investor in history. Yet governments employed different defence strategies aimed at mitigating these costs with some success. An in-house team of lawyers were established under the State Attorney General to lead Argentina's legal defence. This team proved increasingly effective over time as demonstrated by the number of awards that were successfully annulled. The Kirchner government also leveraged domestic pressures to incent foreign investors to drop the cases pending against it with the cooperation of

provincial governments. This led to a number of cases being settled, which imposes fewer costs on the state in terms of legal fees and potential compensation. The Kirchners also exploited gaps in the enforcement mechanisms of the global IIA assemblage to avoid paying awards. This strategy resulted in the reduction of the awards owed as foreign investors sought to negotiate as a means to encourage the Kirchner government to provide payment.

The Correa administration however hired prestigious international law firms well-endowed with the human resources and technical expertise needed to fight investor claims in legal proceedings. This allowed it to avoid the steep learning curve experienced by Argentina's legal team. Correa also sought to mobilize public opinion behind his defence strategy through media campaigns and public outreach to pressure foreign investors to drop their claims. Though oil companies were not persuaded to drop their claims, public support behind Correa's tough stance in the investment disputes did reduce the potential political fallout from an unfavourable award rendered. Ultimately, Correa adopted a strategy of selective disengagement, which resulted in the government's withdrawal from the ICSID Convention and the cancellation of several IIAs with smaller economic partners. Yet, as discussed, Ecuador has not made similar attempts to block the authority of other arbitral bodies.

Moreover, investment rules were not applied evenly across cases, as demonstrated by the contradictory rulings delivered by tribunals in different disputes involving the same government action and similar contexts (i.e. the contradictory rulings delivered in *LGE v. Argentina* and *CMS v. Argentina* regarding whether the 2001 economic crisis met the conditions of necessity). This suggests that tribunal composition may have an

influence on dispute outcomes as different arbitrators engage with and translate investment rules differently. It also demonstrates the importance of domestic contestation. By competing to advance alternative interpretations of investment provisions, state legal representatives and corporate representatives encouraged the uneven application of investment rules. This is particularly true across similar cases brought under different IIAs, as subtle variation across IIA provisions tends to enhance the uneven ways in which investment rules are applied.

While both cases demonstrate that IIAs have a weak deterrent effect in unfavourable political climates, they also suggest that IIAs significantly raise the costs of policy implementation when arbitrators deem those policies to be in violation of investment rules. However, attempts to enforce investment rules against both states encouraged state actors to engage in policy experimentation and institutional capacity-building. Argentina developed an in-house team of lawyers, which became increasingly effective over time. State officials in both governments also pursued stronger relations with non-traditional economic partners as a means to counteract the repercussions of going against investment rules and arbitral awards. They have also promoted the establishment of alternative arrangements to govern investor-state relations, such as Ecuador's *Investment for Development* treaties and the International Arbitration Centre under UNASUR. This suggests that the enforcement of investment rules does not only produce potential constraints on state action. Rather, the productive friction between the global IIA assemblage and domestic actors resulting from processes of enforcement can encourage state actors to engage in policy experimentation in ways they may otherwise

not have. In the next section, I discuss more fully the different factors contributing to each state's defence strategy.

## **7.2 Global-Local Interactions and State Defence Strategies**

Despite their common post-neoliberal orientation, the Kirchner and Correa governments took different approaches in contesting the enforcement of investment rules. The Kirchners preferred to defend public interests under the parameters of prevailing investment rules, albeit not without bending them according to officials' own interpretations. This is while Correa gradually withdrew from components of the IIA assemblage, including the ICSID Convention and several IIAs with more minor economic partners. This has weakened the country's linkages to the global IIA assemblage, although not substantially. Ecuador has not denounced its IIAs with larger economic partners under which most investor claims have been brought. Investors may continue to bring claims against Ecuador, although any claims involving investments made after Ecuador's denunciation of the ICSID Convention in 2008 will have to be brought to UNCITRAL tribunals, which have not proven to be more state-friendly. In this section, I examine the global and domestic factors informing the different approaches taken by each government. This will further our understanding of how policy space is shaped by the productive friction generated by the interaction of investment rules and global and local contexts.

As previously noted, the contestation of foreign investors by civil society groups in both countries encouraged policymakers to introduce policies that conflicted with investor rights. It also influenced the defence strategies each government adopted during ISDS proceedings. In both cases, civil society opposition to foreign investors buttressed

the strength of state actors' bargaining position vis-à-vis foreign investor claimants as state officials could take a hard line without the fear of political reprisals if failing to arrive at a negotiation meant that the state risked an unfavourable award being delivered in ISDS proceedings. Yet it also reduced the scope for bargaining in some instances where state officials sought a settlement. This was the case in Argentina, where officials aimed to reach a settlement with foreign investors in exchange for a commitment on the part of the investor to drop its treaty claim. In cases involving water service providers, which were particularly politicized, state negotiators were restricted in the concessions they could make with foreign investors to arrive at such a settlement. It is also possible that domestic private-sector pressure helped inhibit the Kirchners from withdrawing from the global IIA assemblage. Private-sector actors and industry associations involved in exporting opposed the government's tough stance towards foreign investors as well as their combative discourse towards IIAs and third-party arbitrators, however state officials denied this influence. Civil society demands were given particular priority in part due to the governments' post-neoliberal orientation and their commitment to strengthening ties with progressive factions of society. The political context in which policymakers were situated was therefore an important influence on the governments' approach towards investor claims.

The political ideologies of policymakers also had an important influence on the states' defence strategies. Both the Correa and the Kirchner governments sought to rejuvenate the state's relations with more progressive sectors of society as a means of advancing their post-neoliberal development agendas, which made them particularly susceptible to civil society demands for state action against foreign investors. The

contestation of neoliberal philosophy by the majority of policymakers in government also meant that proposed solutions to the problem of defending domestic interests against investor claims would not be circumscribed by neoliberal assumptions. This opened up space, in turn, for the contestation of investor rights and ICSID jurisdiction. Many policymakers felt that IIAs and ICSID possess a systemic bias towards the interest of TNCs. They were therefore less likely to prioritize adherence to investment rules and arbitral awards, particularly when it interfered in the articulation of state sovereignty and the pursuit of public interests. Yet this translated into very different approaches towards the global IIA assemblage. Though Argentina has faced more than twice as many claims as Ecuador, the Kirchners did not make any substantive attempts to withdraw from the global IIA assemblage, unlike Correa. This reflects the more subtle differences in their political ideologies.

Despite their common post-neoliberal orientation, there were important differences in form and practice between the Kirchner and Correa governments. Correa's development agenda demonstrates tensions between neodevelopmentalism, with its emphasis on economic competitiveness, and post-development goals, including the pursuit of plurinationalism and *sumak kawsay* (collective wellbeing). The former objectives require a more substantive re-thinking about how society is governed in ways that extend beyond dominant developmental approaches. In practice, Correa has demonstrated a stronger commitment to neodevelopmentalism by exploiting the extractive sector to fund his modernization project, however he has sought to balance this project with a pursuit of postdevelopment goals by redefining domestic governance structures to enhance their inclusivity. Correa's willingness to challenge existing

governance structures has filtered into his foreign economic policy as he has been at the forefront of calls for the establishment of alternative regional and extra-regional alliances, including the International Arbitration Centre under UNASUR and the Southern Observatory on Transnational Corporations. These institutions are aimed at enhancing southern solidarity to combat perceived exploitative North-South economic relations.

The Kirchners, however, did not pose any serious challenges to dominant development discourses despite their combative rhetoric towards international creditors and neoliberal policy more broadly. Rather, the Kirchners sought to employ industrial policy and targeted social programming to strengthen the country's competitive position in the global political economy without seeking to reform its existing structures. As such, the Kirchners were more willing to play within the parameters of prevailing international rules, although bending them to some extent. The combative rhetoric employed by the Kirchners towards ICSID and international arbitrators should therefore be understood more as an attempt to generate public support behind their defence strategies than as reflecting a genuine attempt to redefine investor-state relations. Although, it is important to note that the Kirchners also initiated Argentina's participation the formulation of UNASUR's International Arbitration Centre.

Ecuador's vast oil reserves and the revenue captured from oil production has also reduced pressures to appease the international financial community, which gives confidence to policymakers seeking to challenge the status quo of investment relations. Indeed, the windfall tax introduced by Palacio and extended by Correa led to the capture of significant oil revenues, which swelled government coffers. Concession areas vacated by US-oil firms after investment disputes have been quickly taken over by Chinese

companies. The emergence of alternative, non-traditional investment partners like China has therefore played an important role in weakening the power of IIAs as investors' home states have less capacity to exert economic pressures in the event that Correa breaks with investment rules.

Economic factors also had an important influence on Argentina's approach towards foreign investors. Argentina's post-crisis economic recovery helped buttress the bargaining power of state officials during contract renegotiations with foreign investors as the government was able to nationalize firms that refused to settle on new contract terms. Yet Argentina's economic growth was dependent in part on a momentary boom in the global prices of agricultural exports and the state's increased spending put a severe strain on government coffers over time. As this occurred, Cristina Kirchner faced increased pressure to regain access to international capital markets closed by the country's debt default. Kirchner therefore negotiated a settlement on unpaid awards with several foreign investors to appease the international financial community. Ecuador's own economic growth has also been dependent on favourable global commodity prices, namely the price of oil which has declined considerably in recent years. Whether this will inform Correa's future approach towards foreign investors is a question for further research. Yet, both cases demonstrate that global capital flows and domestic economic performance hold sway over countries' defence strategies.

Both governments have demonstrated limitations in how far they are willing to go to challenge the status quo of investor rights, although to varying extents. The Kirchner's maintenance of IIAs has already been observed, but it is interesting to note that Ecuador has also not terminated IIA with several major economic partners. This includes the

United States-Ecuador bilateral investment treaty, under which the majority of investor claims against Ecuador have been brought. The Kirchner and Correa governments' common hesitancy to withdraw from IIAs reflects both the real and perceived dependency of both countries on foreign investment and the ideational influence of IIAs. The economies of both countries depend on foreign capital and technologies, particularly to exploit natural resources, which was a growing interest of Cristina Kirchner. Despite their contestation of investment rules and their perceived bias towards corporate interests, both the Kirchner and Correa governments believed that withdrawing from IIAs would risk capital flight or the inability to attract future foreign investment. This reflects the ideational legacy established by the developmental discourses that identify IIAs as necessary legal interventions to attract foreign investment. As discussed in chapter two, this is despite the lack of substantive evidence that IIAs help attract greater levels of foreign investment than would otherwise have been the case in their absence.

The way in which powers are delegated within the countries' political systems also matters. The weak institutionalization of political parties in both countries made the governments' defence strategies dependent to a degree on the populist appeal of its leaders. Néstor Kirchner's revival of the Partido Justicialista's Peronist roots earned him widespread support amongst diverse sectors of civil society, the National Congress and most provincial governments. Opposition to Néstor Kirchner's approach towards investors was therefore confined to only a small group of private sector actors. Support from provincial governments also made possible the strategy Kirchner employed during contract renegotiations. Since jurisdiction over water and electricity is vested in provincial governments in most areas, Kirchner required provincial co-operation during

contract renegotiations. However, as noted in chapter five, this was not always guaranteed as provincial legislatures sometimes voted down negotiated contracts. Dwindling public support and increased divisions within the governing party ultimately forced Cristina Kirchner to take a more conciliatory approach towards some foreign investors, as demonstrated by her willingness to pay outstanding arbitral awards that she had previously refused to honour. Correa's defence strategy did not depend on the co-operation of subnational governments as powers are more strongly vested in the executive. Correa has also been able to exert a considerable degree of influence over the state's defence strategy given his central role in the establishment of the governing party, Alianza Pais. His own personalistic popularity with the middle class moreover has ensured that his strategy maintained public support despite growing opposition to his leadership from indigenous and environmental groups.

Both cases demonstrate that the willingness and capability of governments to break with investment rules and mitigate the costs of investor claims are influenced by domestic and global factors. This includes domestic economic performance, which can be closely related to global economic trends. In resource-based economies and those dependent upon agricultural exports, fluctuating global commodity prices can be particularly important. I find that strong domestic economic performance buttressed governments' abilities to fight against investor claims while declining economic performance made the government of Cristina Kirchner more likely to acquiesce to investor demands. Argentina's experience suggests that states can become increasingly effective in warding off investor claims as state officials become more experienced in ISDS proceedings. Civil society activism and demands for state action was also a

motivating factor in governments' decisions to break with investment rules and take a hard stance against investor claims. Yet these factors were filtered by policymakers' ideological beliefs, which informed their decision on which policy responses to public problems are available and politically feasible. In the context of post-neoliberal governments, policymakers appeared to be particularly receptive to civil society demands for state action against foreign investors and were less likely to prioritize adherence to investment rules over the pursuit of significant public interests. Whether similar civil society demands would be as well received by governments where neoliberal ideology is more prominent is a question for further research.

### **7.3 Theoretical Contributions**

In this study, I have argued that policy space is best understood as the range of policy options that policymakers perceive to be available and politically viable. Such perceptions are influenced in large part by policymakers' ideas and their political and material surroundings. Defining policy space in this way turns our attention to the ways in which domestic factors, such as economic performance and civil society activism, intersect with global factors, such as the ideational influence of investment rules, to shape policy space at the same time. It also opens up space for exploring the factors that lead governments to contest the enforcement of investment rules and ultimately, to defend domestic interest from investor claims. Policy space from this light is fluid, easily manipulated and exercised at the domestic level. Conceptualizing policy space in this way also helps us move beyond normative assumptions about the legitimacy of international rules.

Policy space has typically been defined as the range of policy options available to states under existing national and international rules (Yu and Marshall 2008, 14). Understanding policy space in this way tells us nothing about the causal mechanisms through which existing rules constrain policy space in practice. It also ignores the possibility that governments can and do pursue policy options deemed illegitimate by international law. Ignoring the range of policy options governments can pursue outside of existing legal arrangements and the factors that motivate them to do so risks reifying prevailing international rules as effective and sanctioned constraints on state action. From this perspective, government decisions to break with investment rules may appear illegitimate even if such decisions are made in the public interest.

Yet examining policy space as determined simultaneously by multiple global and local factors requires a more nuanced understanding of IIAs and their power than the dominant approach provides. IIAs have most often been theorized as constituting a global regime - a system of governance composed of principles, norms, rules and decision-making procedures that constrain and regularize state action (Salacuse 2010, 431). From this lens, IIAs operate above domestic spaces and in isolation from the agency of domestic actors. While this perspective rightly acknowledges existent global power relations, it has also encouraged scholars to assume that investment rules are applied evenly across time and space regardless of domestic contexts and the response of state actors. It also has led scholars to neglect the intimate ways and spaces in which local actors engage with investment rules.

I have argued that IIAs are better understood as components of a global assemblage constituted by a heterogeneous assortment of institutions, actors, expertise

and physical objects. From this perspective, the power IIAs exert over domestic political processes is not a given, but is instead contingent on the cooperation and interaction of the multiple components in its network of power. Theorizing IIAs in this way risks under-emphasizing structural forms of power in the global economy. Certainly the establishment and functioning of the global IIA assemblage has not been in the absence of asymmetrical power relations. However, using the metaphor of assemblage turns our attention towards the gaps and inconsistencies inherent in the global IIA assemblage that open up space for contestation and resistance. This, in turn, allows us to explore the different ways in which domestic actors disrupt the smooth enforcement of investment rules.

Both cases analyzed in this study have revealed important gaps and inconsistencies in the global IIA assemblage. For instance, while the broad wording and scope of some provisions has been criticized as allowing undue powers of interpretation to arbitrators (see Van Harten 2008 for example), it has also enabled state actors to contest the rights that foreign investors claim under IIAs. It is through these struggles of translation that investment rules come to be applied unevenly across time and space. It is therefore necessary to consider the physical properties of IIAs as actants and how other kinds of actors within their broader networks might translate them differently when analyzing the extent to which investment rules constrain policy space in any given context. The enforcement of IIAs was also muted in some ways by the fact that governments did not voluntarily abide by tribunal orders. In such instances, foreign investors rely heavily on their home states to discipline hosts. Yet, as VAT disputes in Ecuador demonstrate, investors' home states may be unwilling to undertake disciplinary

actions against hosts if it interferes with the pursuit of other foreign policy options. Theorizing IIAs not as a cohesive regime but as a disaggregated network of interconnected components enables us to capture these dynamics, which will in turn strengthen our understanding of the various factors that enable or disrupt the ability of IIAs to place constraints on state action.

Applying Anna Tsing's notion of *friction* to study the interconnections between the global IIA assemblage and domestic spaces allows us to acknowledge the ways in which global processes and domestic contexts are co-constituted through every day interactions. From this lens, domestic agency is not separate or distinct from the global IIA assemblage but is instead implicated in its functioning. That is, state actors and institutions, by contesting or reinforcing the impacts of IIAs, occupy a central role in the assemblage itself. State responses to the enforcement of investment rules therefore become an essential component in understanding the extent to which IIAs constrain policy space in any given context. Yet understanding the state's responses to the imposition of investment rules, in turn, requires opening up the state exposing its own heterogeneous nature.

As such, I follow Joel Migdal (2001) in envisioning the state as both an abstraction and a manifestation of multiple, at times competing, parts. These parts occupy a common field of power and project an image of the state as being cohesive and unified through the everyday practices of its parts and their interactions with society. This understanding of the state has two advantages for studying the relationship between IIAs and domestic policy space. First, it encourages us to examine how the image of the state is implicated in the functioning of the global IIA assemblage. The 'state' is both a

fundamental building block of contemporary international institutions yet the rights ascribed to it, such as state sovereignty, was also used by state officials in Ecuador and Argentina to contest enforcement processes. Second, understanding the state as fragmented and dispersed within a territorially defined area encourages us to study its diverse relationships with society. Understanding the intimate inter-relationships between state actors and institutions and civil society is essential for explaining why governments chose to break with investment rules and the defence strategies they adopted towards investor claims. This, in turn, encourages us to recognize the complex spatiality of policy *space*, as we explore how policymakers' perceptions are influenced by negotiations with society across domestic sites.

This theoretical framework encourages us to nuance our understandings of the power IIAs exert and the causal pathways by which they act on governments' policy space. It enables us to embrace state agency as a fundamental component of the relationship between IIAs and policy space and to expand our understanding of the constraints IIAs impose are mediated, contested or reinforced at the domestic level. This is essential, as the real impact IIAs have on policy space lies in the middle messy ground between the power IIAs exert and the responses they evoke at the domestic level.

#### **7.4 Limitations and Future Lines of Research**

Nothing in this study should be taken as an argument for the strengthening of IIA enforcement mechanisms or as support for the stringent IIAs popularized in the 1990s. There are many studies that convincingly demonstrate the risks to public interests of signing on to IIAs. The evidence that demonstrates their added benefit to attracting foreign investment is also shaky at best. Rather, this study is meant to shed light on how

state actors contest the imposition of investment rules and what this tells us about the nature of policy space in the contemporary era. As such, this study examines the relationship between IIAs and policy space in a democratic setting where governments contest the authority of investment rules. Investment rules may have a stronger constraining influence in countries governed by governments that adhere to neoliberal philosophy or where civil society demands for the protection of public interests are greatly outweighed by private-sector lobby groups that promote adherence to IIAs. This study provides only limited insights on the degree to which investment rules might constrain policy space in countries where investment rules hold greater legitimacy or where governments are not held responsible to their citizenry through democratic elections. In such a case, state actors may play an important role in reinforcing the legitimacy of investment rules and help to buttress the authority of such rules over domestic decision making processes. However, it is important to note that isolating the independent impact of IIAs in this context would also be challenged by the fact that investment rules may simply reinforce the government's policy inclinations. Further research should explore the role of right-leaning governments in defending domestic interests and / or reinforcing the impacts of IIAs in democratic and potentially authoritarian political systems.

The second limitation relates to the difficulty of examining the extent to which investment rules induce a 'policy chill'. Policy chill is not often defined but is understood here to refer to the disuse (or avoidance) of policies that might otherwise have been implemented in the absence of an external deterrent (such as investment rules). It is hard to discern whether a government would have instituted a policy in the absence of

investment rules if all other variables were held constant as policymakers may have internalized the norms contained in investment agreements. Such norms are also promoted in the discourse of international financial institutions, economic partners and many international development organizations. Thus, it is difficult to isolate the impact of IIAs on policy chill in any given context.

Fourth and related to the above points, there is a need to examine more explicitly the role private sector and international actors play in reinforcing the legitimacy and constraining influence of IIAs on policy space beyond the foreign investor. This study has focused its analyses on state actors and institutions in defending public interests and, as such, foregrounds state actors' relationships with civil society groups. Isolating the role private sector actors have played in these countries and in others requires further analysis and interviews with private-sector actors such as industry associations and lobby groups. Further analysis should also focus on revealing the role international financial institutions, such as multilateral lending banks and credit-rating agencies as well as inter-state organizations, play in reinforcing the power of investment rules and their enforcement mechanisms.

Lastly, given the mobile nature of capital in the contemporary era, governments that go against investment rules risk capital flight or scaring off new investment when they break from IIA obligations (Chang 2006). While the possibility may deter governments from breaking with investment rules, it is beyond the capability of this study to measure the degree to which investment flows declined as a result of investor-state disputes and the responses adopted by governments. Foreign investors' decisions on whether to invest in a particular market are informed by a complex variety of factors, including the degree

of political risk. Assessing the extent to which Ecuador and Argentina's approaches to thwarting investor claims has impacted investment levels therefore requires a much deeper and thorough analysis than this study can provide. This study therefore focused on the idea of capital flight and the role it played in informing governments' decisions to adopt particular strategies towards mitigating the costs of investor-state disputes.

## **7.5 Governing the Global Economy**

The findings in this study challenge the view that IIAs impact governments' policy space evenly across time and space and demonstrate the importance of recognizing state agency in studies of global economic integration. Foreign investors were not always successful in leveraging IIAs to circumvent government policy and the costs incurred by investor claims was significantly reduced as a result of governments' defence strategies. Therefore, while IIAs do significantly increase the costs of adopting certain forms of government actions, the constraints they impose on policy space must be understood as contingent upon the response of domestic actors in host states as well as the various actors, institutions and ideas with which IIAs engage in their global networks.

Neglecting to explore the conditions under which governments break from investment rules and how they contest their enforcement has misled authors into assuming that the impacts of IIAs are both inevitable and consistent across time and space. However, as this study shows, the *real* impact that investment rules have on policy space lies in the middle messy ground between IIAs' potential impacts and the local responses they evoke (e.g. resistance, acquiescence or negotiation). The capacity of IIAs to constrain policy space must therefore be understood as resulting from, and perhaps

limited by, the productive friction between domestic actors and the networks that seek to enforce them.

This study makes two additional contributions to our understanding of global economic governance in the contemporary era more broadly. First, it demonstrates the importance of factoring in domestic agency into studies of global economic arrangements and policy space. State actors play an important role in shaping the extent to which external variables shape domestic political processes and decision-making. As such, it suggests the need to examine the state's role in mediating other kinds of constraints, such as trade rules and aid and loan conditionalities. This will improve our overall understanding of when and under what contexts global economic arrangements influence state action in practice. It will also expand our understanding of how states defend domestic interests against external constraints. Second, it lends further evidence to support the conclusion that global economic processes are not experienced everywhere the same and in fact have varied impacts across localities. The global diffusion of neoliberal philosophy and policy in the 1980s and 1990s has encouraged some scholars to postulate an inevitable alignment of economic policy at the domestic and global level. However this study demonstrates that neoliberal arrangements, such as international investment rules, are subject to contestation and are not always effective in shaping state action. This suggests that neoliberal globalization itself is experienced unevenly across space and may hold less hegemonic influence than many theorists acknowledge. It demands however that we examine more closely variegated outcomes produced by the friction between global processes and their interaction with actors and institutions in domestic spaces.

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## **Appendix 1: List of Interviewees**

### **Argentina**

- Andrés Asiain, Department of Economics, Government of Argentina, April 2014.
- Anonymous, Department of Economics, Government of Argentina, 4 April 2014
- Anonymous, former attorney for corporate claimant against Argentina, Buenos Aires, 21 May 2014.
- Anonymous, former attorney for corporate claimant against Argentina, Buenos Aires, 8 May 2014.
- Anonymous, former state attorney with the Office of the Attorney General, Buenos Aires, 21 April 2014.
- Anonymous, former state attorney with the Office of the Attorney General, Buenos Aires, 28 July 2014.
- Anonymous, former state attorney with the Office of the Attorney General, Buenos Aires, 28 April 2014.
- Anonymous, former political official, Buenos Aires, 12 May 2015.
- Anonymous, representative of international financial institution, 30 April 2014
- Anonymous, representative of international financial institution, 30 April 2014
- Javier Echaide, Professor of Public International Law, Argentine University of Business, Buenos Aires, 9 April 2014.
- Jose Fernandez Alonso, Universidad Nacional De Rosario, Buenos Aires, 16 April 2014
- Juan Pablo Bohoslavsky, UN Economic Commission on Latin America and the Caribbean, 16 April 2014
- Leonardo Stanley, Center for the Study of State and Society, Buenos Aires, 15 April 2015.
- Luciana Ghiotto, Representative of civil society group (ATTAC), 23 April 2014
- Norberto Ariel Martins Mogo, Department of Foreign Relations, Government of Argentina, Buenos Aires, 23 April 2014.

### **Quito, Ecuador**

- Adrian Cornejo, Secretaría Nacional de Planificación y Desarrollo (SENPLADES, National Planning and Development Secretariat), 12 October 2014
- Alicia Granda, Comision Ecumenical de Derechos Humanos, 10 October 2014
- Anonymous, Acción Ecologica, 22 October 2014
- Anonymous, Advisor to National Assembly member, 8 October 2014
- Anonymous, Advisor to National Assembly member, 7 October 2014
- Anonymous, Former attorney for claimant against Ecuador, 15 October 2014
- Anonymous, Former attorney for claimant against Ecuador, 21 October 2014

- Anonymous, Former state attorney, Attorney General's Office, 9 October 2014
- Anonymous, Former attorney with a domestic law firm that assisted on several cases as Ecuador's legal representative, 15 October 2014
- Anonymous, Former attorney with a domestic law firm that assisted on several cases as Ecuador's legal representative, 21 October 2014
- Anonymous, Universidad Andina Simón Bolívar, 14 October 2014
- Diego Ramirez, Former attorney for claimant against Ecuador, 28 October 2014
- Ernesto Vivares, FLACSO – Ecuador, Department of Politics and International Relations, 6 October 2014
- Fernando Martin, Department of Economics, FLACSO- Ecuador, 6 October 2014
- Javier Echaide, Commission for a Comprehensive Audit of Investment Protection Treaties and of the International Arbitration System on Investment, 21 October 2014
- Luis Guamangate, National Assembly member and Alianza País member, 8 October 2014
- Santiago Vásquez, Secretaría Nacional de Planificación y Desarrollo (SENPLADES, National Planning and Development Secretariat) , 12 October 2014

## Appendix 2: Questionnaire Samples

### State Legal Representatives

- When were you hired on to represent the state and in which cases did you participate?
- What was your legal and educational experience before participating on the state's legal team?
- How prepared (qualify: experienced, knowledgeable) were state lawyers and government officials to manage investor-state disputes when you were hired?
- From your understanding, what informed the government's willingness to participate in the legal proceedings?
- What was the relationship like between your legal team and government officials?
  - How much autonomy did you have in deciding the state's legal defence?
- What instructions were you given from government officials (clarify: the executive) related to the state's legal defence?
- What legal strategies did you use during the legal defence?
- Were different legal strategies used during different cases (within the same sector, between different sectors, and across time)?
  - Why were different strategies taken?
  - How effective or ineffective were these strategies?
- Did the state's legal team face different challenges defending state action from different kinds of foreign investors (clarify: across different sectors, across time)
- What were the most challenging aspects of defending the state throughout the legal proceedings?
- Do you believe investor-state dispute settlement procedures are bias?
  - If yes, in which ways? How did state lawyers try to address these biases?

### Claimants' Legal Representatives

- Had [the legal firm] taken on a legal case involving an investor-state dispute prior to [case name]?
- How many lawyers were on the [claimant's] legal team and what kind of prior experience did they have in these matters?
- Why did [claimant] bring this suit against [Ecuador/Argentina]?
  - What government action prompted the case?
  - What was the motivation behind bringing the claim – did [claimant] want to achieve a settlement or compensation?
  - Which provisions of the IIA did the government violate?
- How effective in your opinion was the state's legal team?
  - What made them particularly effective or ineffective?
- Do you believe investor-state dispute settlement procedures are bias?
  - If yes, in which ways? How did [legal firm] try to address these biases?
- Was your client subjected to any pressure outside of court to drop the claim?

- If yes, who exerted this pressure?
- To what extent was it effective?

### **Government Officials (Argentina)**

- Please tell me more about your current position and responsibilities
  - How long have you been in this role?
  - Which other departments have you worked in?
- From your knowledge, why did Argentina introduce the emergency measures in 2001?
- How did Argentina respond to the claims brought to ICSID after the crisis?
- Were you involved in the decision-making related to how Argentina would respond to investor claims?
- How prepared was Argentina to participate in the cases?
- Do you believe that investor-state arbitration is biased and how so?
- Why has Argentina decided to maintain its investment agreements?
- Do you believe that IIAs are a necessary part of Argentina's economic development strategy?
- Why did Argentina refused to compensate foreign investors for outstanding awards?
- Why did it ultimately agree to compensate these investors after denying the responsibility to do so?
- What does Argentina hope to attain by building UNASUR's dispute resolution body?

### **Government Officials (Ecuador)**

- Please tell me more about your current position and responsibilities
  - How long have you been in this role?
  - Which other departments have you worked in?
- From your knowledge, why did Ecuador introduce the changes to the VAT credits? The windfall tax?
- How did these disputes impact the governments' relations with society? Foreign investors?
- How did Ecuador respond to the investor's claims in arbitral tribunals?
- Why did the government hire an external legal team?
- Why did Ecuador withdraw from the ICSID Convention?
- Why did the government cancel IIAs?
- Why hasn't the government terminated the agreement with the United States and other economic partners?
- Will Ecuador sign on to new investment agreements?
- What does Ecuador hope to attain by building UNASUR's dispute resolution body?
- Do you believe that ICSID is bias in any way?

### Appendix 3: Argentina Investor-State Disputes\*

\*All monetary awards are in USD unless otherwise indicated.

Pre-Crisis Cases	Details	Government Policy at Issue	Outcome
Compañía de Aguas del Aconquija SA and Vivendi Universal SA v. Argentina (ARB/97/3)	Year:1997 Treaty: Argentina-France BIT Venue: ICSID Sector: Water and Sanitation Services	Provincial government of Tucuman refused to allow tariff increases and fined company for failure to meet service delivery and reinvestment targets. Province supported consumer groups' boycott of bill payments and terminated contract following failed renegotiations. National government held liable for not intervening to ensure security of investment.	Initial demand by investor: Status: <b>In favour of investor</b> Amount awarded: US\$ 105 million plus interest  * Argentina paid in the form of a bond at an approx. 25 percent discount)
Lanco International Inc. v. Argentina (ARB/97/6)	Year:1997 Treaty: Argentina-United States BIT Venue: ICSID Sector: transportation	National government's cancellation of contract to operate Terminal 3, Port of Buenos Aires	Initial demand: not public Status: <b>Settled</b>  *minority share holder
Houston Industries Energy Inc. v. Argentina (ARB/98/1)	Year:1998 Treaty: Argentina-United States BIT Venue: ICSID Sector: Energy	Implementation of new taxes and fines in province of Santiago del Estero	Initial demand by investor: not public Status: <b>In favour of investor</b> Amount awarded: not public
Mobil Argentina SA v. Argentina (ARB/99/1)	Year:1999 Treaty: Argentina-United States BIT Venue: ICSID Sector: Energy	Not public	Initial demand by investor: not public Status: <b>Settled</b>
Empresa Nacional de Electricidad v. Argentina (ARB/99/4)	Year:1999 Treaty: Argentina-Chile BIT Venue: ICSID Sector: Energy	Enforcement of Stamp Tax in province of Neuquén.	Initial demand: not public Status: <b>Settled</b>

Azurix Corp v. Argentina (ARB/01/12)	Year:2001 Treaty: Argentina-United States BIT Venue: ICSID Sector: Water and Sanitation Services	Provincial government of Buenos Aires refused to allow tariff increases and fined company for failure to meet service delivery and reinvestment targets. Province supported consumer groups' boycott of bill payments and terminated contract following failed renegotiations. National government held liable for not intervening to ensure security of investment..	Initial demand: \$608.417 million Status: <b>In favour of investor</b> Amount awarded: \$165,240,753 plus interest  * Argentina paid in the form of a bond at an approx. 25 percent discount)
Enron v. Argentina (ARB/01/3)	Year:2001 Treaty: Argentina-United States BIT Venue: ICSID Sector: Energy	Suspension of right to index tariffs to US Purchasing Price Index; modified to include claims regarding emergency measures	Initial demand: #343,954134 Status: <b>In favour of investor, overturned in favour of state</b> Amount awarded: \$106.2 million (cancelled)
Siemens AG v. Argentina (ARB/02/8)	Year:2002 Treaty: Argentina-Germany BIT Venue: ICSID Sector: Information technology services	Cancellation of contract by the national government after concerns about corruption arose.	Initial demand: \$283,859,710 million Status: <b>In favour of investor</b> Amount awarded: \$217,830439 plus interest  *Argentina sought annulment after US government made public report of corruption. Parties settled out of court.
<b>CRISIS CASES</b>			
<b>Water</b>			
Suez, Sociedad General de Aguas de Barcelona SA and Vivendi Universal SA v. Argentina (ARB/03/19)	Year:2003 Treaty: Argentina-France BIT; Argentina-Spain BIT Venue: ICSID	Emergency measures, cancellation of contract	Initial demand: 1,012 million Status: <b>In favour of investor</b> Amount awarded: \$223,043,289 to Suez; \$123,276,448 for AGBAR; \$37, 261,504 for Vivendi *under annulment proceedings
Anglian Water Group (AWG) PLC v. Argentina	Year:2003 Treaty: Argentina-United Kingdom BIT	Emergency measures, cancellation of contract	Initial demand: included in ARB/03/19 litigation Status: <b>In favour of investor</b>

	Venue: UNCITRAL		Amount awarded: \$21 million *under annulment proceedings
Suez, Sociedad General de Aguas de Barcelona SA and Interagua Servicios Integrales de Agua SA v. Argentina (ARB/03/17)	Year:2003 Treaty: Argentina-France BIT; Argentina-Spain BIT Venue: ICSID	Emergency measures, cancellation of contract	Initial demand: \$218,582,840 Status: <b>In favour of investor</b> Amount awarded: unknown  *most claims were dismissed but tribunal ruled that Argentina violated fair and equitable treatment provision.
EDF International SA, SAUR International SA and León Participaciones Argentinas SA v. Argentina (ARB/03/23)	Year:2003 Treaty: Argentina-France BIT Venue: ICSID	Emergency measures, cancellation of contract	Initial demand: Status: <b>In favour of investor</b> Amount awarded: \$136,138,430
Aguas Cordobesas SA, Suez, and Sociedad General de Aguas de Barcelona v. Argentina (ARB/03/18)	Year:2003 Treaty: Argentina-Spain BIT Venue: ICSID	Emergency measures, cancellation of contract	Initial demand: \$105 million Status: <b>Settled</b>
Azurix Corp. v. Argentina (ARB/03/30)	Year:2003 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures, cancellation of contract	Initial demand: not public Status: <b>Discontinued</b>
SAUR International v. Argentina (ARB/04/4)	Year:2004 Treaty: Argentina-France BIT Venue: ICSID	Emergency measures, cancellation of contract	Initial demand: Status: <b>In favour of investor</b> Amount awarded: \$39,990,111  *Argentina also ordered to pay SAUR legal fees, \$686,500 and ICSID fees of €1,486,975.
Impregilo SpA v. Argentina (ARB/07/17)	Year:2007 Treaty: Argentina-Italy BIT	Emergency measures, cancellation of contract	Initial demand:\$119,362,503 Status: <b>In favour of investor</b> Amount awarded: \$ 21,294,000

	Venue: ICSID		
Urbaser SA and Consorcio de Aguas Bilbao Biskaia, Bilbao Biskaia Ur Partzuergoa v. Argentina (ARB/07/26)	Year:2007 Treaty: Argentina-Spain BIT Venue: ICSID	Emergency measures, cancellation of contract	Initial demand: not public Status: Pending
<b>Energy</b>			
CMS Gas Transmission Company v. Argentina (ARB/01/8)	Year:2001 Treaty: Argentina-United States BIT Venue: ICSID	Suspension of clause that tied tariffs to US Produce Price Index; amended to include emergency measures	Initial demand: \$261.1 million Status: <b>In favour of investor</b> Awarded: \$133 million  *award was bought out by Blue Ridge Investments in June 2008 and sought to enforce the award in United States
AES Corporation v. Argentina (ARB/02/17)	Year:2002 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures	Status: <b>Settled</b>
LG&E Energy Corp., LG&E Capital Corp., and LG&E International Inc. v. Argentina (ARB/02/1)	Year:2002 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures	Status: <b>In favour of investor</b> Amount awarded: 57.4 million
Sempra Energy International v. Argentina (ARB/02/16)	Year:2002 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures	Status: <b>In favour of investor, overturned on annulment</b> Amount awarded:
Camuzzi International SA v. Argentina (ARB/03/02)	Year:2003 Treaty: Argentina-Belgium and Luxembourg BIT Venue: ICSID	Emergency measures	Status: <b>Settled</b>
Camuzzi International SA	Year:2003	Emergency measures	Status: <b>Settled</b>

v. Argentina (ARB/03/07)	Treaty: Argentina-Belgium and Luxembourg BIT Venue: ICSID		
Enerdis SA and others v. Argentina (ARB/03/21)	Year:2003 Treaty: Argentina-Chile BIT Venue: ICSID	Emergency measures	Status: Settled
Electricidad Argentina SA and EDF International SA v. Argentina (ARB/03/22)	Year:2003 Treaty: Argentina-France BIT Venue: ICSID	Emergency measures	Status: settled
EDF International SA, Saur International SA and Léon Participaciones Argentinas v. Argentina (ARB/03/23)	Year:2003 Treaty: Argentina-France BIT Venue: ICSID	Emergency measures	Initial demand: Status: In favour of investor Amount awarded: \$136,138,430  *administrative fees charged to national government, \$1,631,298.
Gas Natural SDG SA v. Argentina (ARB/03/10)	Year:2003 Treaty: Argentina-Spain BIT Venue: ICSID	Emergency measures	Status: Settled
El Paso Energy International Company v. Argentina (ARB/03/15)	Year:2003 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures	Initial demand: Status: In favour of investor Amount awarded: \$43 million
Pan American Energy LLC and BP Argentina Exploration Company v. Argentina (ARB/03/13)	Year:2003 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures	Status: Settled
Pioneer Natural Resources Company v. Argentina (ARB/03/12)	Year:2003 Treaty: Argentina-United States BIT	Emergency measures	Initial demand: \$80 million Status: Settled

	Venue: ICSID		
BG Group PLC v. Argentina	Year:2003 Treaty: Argentina-United Kingdom BIT Venue: UNCITRAL	Emergency measures	Status: <b>In favour of investor, overturned in state's favour,</b> Amount awarded: \$185 million (cancelled)
National Grid v. Argentina	Year:2003 Treaty: Argentina-United Kingdom BIT Venue: UNCITRAL	Emergency measures	Initial demand: \$112,400,000 Status: <b>In favour of investor</b> Amount awarded: \$53.592.439 million  *state also ordered to pay 75 % of admin costs of tribunal valued at \$1,347,835.
Total SA v. Argentina (ARB/04/1)	Year:2004 Treaty: Argentina-France BIT Venue: ICSID	Emergency measures	Status: <b>In favour of investor</b>
Wintershall Aktiengesellschaft v. Argentina (ARB/04/14)	Year:2004 Treaty: Argentina-Germany BIT Venue: ICSID	Emergency measures	Initial demand: \$479 million Status: <b>In favour of state</b>
BP America Prod., Pan American Sur SRL, Pan American Fuegoina, SRL and Pan American Continental SRL v. Argentina (ARB/04/8)	Year:2004 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures	Status: <b>Settled</b>
Mobil Exploration and Development Inc. Argentina and Mobil Argentina SA v. Argentina (ARB/04/16)	Year:2004 Treaty: Argentina-United States BIT Venue: ICSID	Emergency measures	Status: Pending
Compania General de Electricidad SA and CGE Argentina SA v. Argentina	Year:2005 Treaty: Argentina-Chile BIT	Emergency measures	Status: <b>Settled</b>

(ARB/05/2)	Venue: ICSID		
United Utilities International Limited (UUIL) v. Argentina	Year:2004 Treaty: Argentina-United Kingdom BIT Venue: UNCITRAL	Emergency measures	Status: Settled
<b>Misc.</b>			
Metalpar SA and Buen Aire v. Argentina (ARB/03/5)	Year:2003 Treaty: Argentina-Chile BIT Venue: ICSID	Emergency measures	Status: In favour of state
Telefonica SA v. Argentina (ARB/03/20)	Year:2003 Treaty: Argentina-Spain BIT Venue: ICSID	Emergency measures	Status: Settled
Continental Casualty Company v. Argentina (ARB/03/9)	Year:2003 Treaty: Argentina-United States BIT Venue: ICSID Sector: Insurance	Emergency measures	Status: In favour of investor Amount awarded: \$2.8 million  *accepted necessity defense on most claims but found Argentina liable for some damages
France Telecom v. Argentina (ARB/04/20)	Year:2004 Treaty: Argentina-France BIT Venue: ICSID Sector: Telecommunications	Emergency measures	Status: Settled
CIT Group Inc. V. Argentina (ARB/04/9)	Year:2004 Treaty: Argentina-United States BIT Venue: ICSID Sector: Finance	Emergency measures	Status: Settled
RGA Reinsurance Company v. Argentina	Year:2004 Treaty: Argentina-	Emergency measures	Status: Settled

(ARB/04/20)	United States BIT Venue: ICSID Sector: Finance		
Daimler Chrysler Services AG v. Argentina (ARB/05/1)	Year: 2005 Treaty: Argentina-Germany BIT Venue: ICSID Sector: Auto leasing	Emergency Measures (Capital controls, end to Convertibility Plan)	Status: <b>ICSID declined jurisdiction</b>
TSA Spectrum v. Argentina (ARB/05/5)	Year:2005 Treaty: Argentina-Netherlands BIT Venue: ICSID Sector: telecommunications	Emergency measures	Status: <b>In favour of state</b>
Bank of Nova Scotia v. Argentina	Year:2005 Treaty: Argentina-Canada BIT Venue: UNCITRAL	Emergency measures	Status: <b>Settled</b>
Ablacat and Others v. Argentina, formerly Giovanna Beccara and others v. Arg (ARB/07/5)	Year:2007 Treaty: Argentina-Italy BIT Venue: ICSID	Debt default	Status: Pending
Giovanni Alemanni and others v. Argentina (ARB/07/8)	Year:2007 Treaty: Argentina-Italy BIT Venue: ICSID	Debt default	Status: Pending (in danger of termination because of claimants failure to pay fees)
HOCHTIEF Aktiengesellschaft v. Argentina (ARB/07/31)	Year:2007 Treaty: Argentina-Germany BIT Venue: ICSID Sector: civil engineering	Emergency measures	Status: <b>In favour of investor</b> Amount awarded: Parties instructed to negotiate on how to move forward.

Ambiente Ufficio SpA and others v. Argentina	Year:2008 Treaty: Argentina-Italy BIT Venue: ICSID Sector: Bondholders	Debt default	Initial demand: €\$6,534,256; US\$562,000 Status: ICSID Tribunal discontinued for failure of claimants to proceed in good time.
Impregilo SpA v. Argentina (ARB/08/14)	Year:2007 Treaty: Argentina-Italy BIT Venue: ICSID Sector: infrastructure	Emergency measures	Status: Settled
ICS Inspection and Control Services Limited v. Argentina (PCA case no. 2010-9)	Year:2007 Treaty: Argentina-United Kingdom BIT Venue: UNCITRAL Sector: Administrative services	Emergency measures	Status: In favour of state
<b>POST-CRISIS CASES</b>			
Asset Recovery Trust v. Argentina (ARB/05/11)	Year: 2005 Treaty: Argentina-United States BIT Venue: ICSID Sector: Finance	Not public	Status: Cancelled by tribunal for claimants' failure to pay fees needed to move forward
Repsol SA and Repsol Butano SA v. Argentina (ARB/12/38)	Year:2012 Treaty: Argentina-Spain BIT Venue: ICSID Sector: Energy	Renationalization of firm's shares in YPF state oil company.	Initial demand: \$10 billion Status: Settled
Teinver SA, Transportes de Cercanias SA and Autobuses Urbanos del Sur SA v. Argentina (ARB/09/1)	Year:2007 Treaty: Argentina-Spain BIT Venue: ICSID Sector: transportation	Renationalization of Aerolineas Argentina	Initial demand: \$1 to 1.5 billion Status: Pending

Casinos Austria International and Casinos Austria v. Argentina (ARB/14/32)	Year:2014 Treaty: Argentina-Austria BIT Venue: ICSID	Not public	Initial demand: not public Status: Pending
Salini Impreglio SA V. Argentina (ARB/15/39)	Year: 2015 Treaty: Argentina-Italy BIT Venue: ICSID Sector: infrastructure	Not public	Initial demand: not public Status: Pending

## Appendix 4: Ecuador Investor-State Disputes Involving Oil Companies\*

\*all monetary awards are in USD unless otherwise indicated.

Cases	Details	Government Policy at Issue	Outcome
Occidental Exploration v. Ecuador (UN3467)	Year: 2002 Treaty: United States-Ecuador BIT Venue: London Court of International Arbitration	Introduction of changes to tax legislation resulting in the withdrawal of credits related to value-added tax.	Initial demand by investor: \$201.5 million Status: <b>In favour of investor</b> Amount awarded: \$75 million
Encana Corp. v. Republic of Ecuador (UN3481)	Year: 2003 Treaty: Canada-Ecuador BIT Venue: London Court of International Arbitration	Introduction of changes to tax legislation resulting in the withdrawal of credits related to value-added tax.	Initial demand by investor: \$80 million Status: <b>In favour of state</b> Amount awarded: 0
Occidental Exploration v. Ecuador (ARB/06/11)	Year: 2006 Treaty: United States-Ecuador BIT Venue: ICSID	Claim arose due to the termination of the company's contract for the exploration and exploitation of hydrocarbons in Block 15 of the Amazon region.	Initial demand by investor: \$1 billion Status: <b>In favour of investor</b> Amount awarded: \$1.7 billion  *award later reduced to \$1.016 billion following annulment proceeding.
Chevron v. Ecuador (PCA 34877)	Year: 2006 Treaty: United States-Ecuador BIT Venue: Permanent Court of Arbitration	Claim arose out of seven breach-of-contract suits filed by subsidiary Texaco against the state in the 1990s. Chevron alleged an egregious delay of all Texaco suits by the Ecuadorian judiciary.	Initial demand by investor: \$649 million Status: <b>In favour of investor</b> Amount awarded: \$77.7 million
Perenco v. Ecuador (ARB/08/06)	Year: 1998 Treaty: Ecuador-France BIT Venue: ICSID	Amendments to Hydrocarbons Law No. 42, including the introduction of a windfall levy on oil revenues at 99 percent.	Initial demand by investor: \$440 million Status: <b>In favour of investor</b> Amount awarded: TBD
Murphy v. Ecuador	Year: 2008	Amendments to Hydrocarbons Law No. 42,	Initial demand by investor: Unknown

(ARB/08/4)	Treaty: United States-Ecuador BIT Venue: ICSID	including the introduction of a windfall levy on oil revenues at 99 percent.	Status: <b>Dismissed</b> Amount awarded: 0
Burlington v. Ecuador (ARB/08/5)	Year: 2008 Treaty: United States-Ecuador BIT Venue: ICSID	Amendments to Hydrocarbons Law No. 42, including the introduction of a windfall levy on oil revenues at 99 percent.	Initial demand by investor: Status: <b>In favour of investor</b> Amount awarded: TBD
Chevron v. Ecuador (2009-23)	Year: 2009 Treaty: United States – Ecuador BIT Venue: Permanent Court of Arbitration	Alleged government misconduct in class action litigation proceeding taken against its subsidiary Texaco by residents of the Amazonian rainforest	Initial demand by investor: \$18 billion Status: Pending Amount awarded:
Murphy v. Ecuador (AA434)	Year: 2011 Treaty: United States-Ecuador BIT Venue: Permanent Court of Arbitration	Amendments to Hydrocarbons Law No. 42, including the introduction of a windfall levy on oil revenues at 99 percent.	Initial demand by investor: Unknown Status: Pending Amount awarded: