

Michigan Journal of International Law

Volume 41 | Issue 1

2020

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Recommended Citation

Michael Faure & Wanli Ma, *Investor-State Arbitration: Economic and Empirical Perspectives*, 41 MICH. J. INT'L L. 1 (2020).

Available at: <https://repository.law.umich.edu/mjil/vol41/iss1/2>

<https://doi.org/10.36642/mjil.41.1.investor-state>

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INVESTOR-STATE ARBITRATION: ECONOMIC AND EMPIRICAL PERSPECTIVES

*Michael Faure and Wanli Ma**

I. INTRODUCTION

Legal scholars and practitioners alike have expressed increased criticism of the current dispute resolution mechanism between sovereign states and private investors.¹ That system, known as the investor-state arbitration (“ISA”) system,² is largely based on the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (the “ICSID Convention”) and is primarily governed by the International Centre for Settlement of Investment Disputes (“ICSID”).³ Investor-state arbitrations are usually administered either by ICSID or on an

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1. See, e.g., Joost Pauwelyn, *At the Edge of Chaos? Foreign Investment Law as a Complex Adaptive System, How It Emerged and How It Can Be Reformed*, 29 ICSID REV. - FOREIGN INV. L.J. 372, 372–418 (2014); Rachel L. Wellhausen, *Recent Trends in Investor-State Dispute Settlement*, 7 J. INT’L DISP. SETTLEMENT 117, 117–19 (2016).

2. Investor-state arbitration is also widely known as investor-state dispute settlement (“ISDS”) in the literature of this field. Thus, the two terms will be used interchangeably in this article.

3. William W. Burke-White & Andreas von Staden, *Private Litigation in a Public Sphere: The Standard of Review in Investor-State Arbitrations*, 35 YALE J. INT’L L. 283, 284 (2010). The functionality of investor-state arbitration is conceptualized by Sergio Puig in three ways: First, it serves to resolve disputes between foreign investors and host states; second, it aims to depoliticize investment disputes; third, it eliminates or reduces the impediments to the free flow of private investments posed by non-commercial risks. See Sergio Puig, *No Right without a Remedy: Foundations of Investor-State Arbitration*, 35 U. PA. J. INT’L L. 829, 848 (2014).

ad hoc basis under the arbitration rules of the United Nations Commission on International Trade Law (“UNCITRAL”).⁴

Developing countries, in particular, accuse the ICSID-governed ISA system of being biased toward investors.⁵ Some developing countries have withdrawn or have threatened to withdraw from the ICSID system.⁶ Many states therefore claim that the current ISA system has to be reformed to be less biased against states and to better represent their interests. In particular, states have expressed earnest concern that ISA is inappropriately modeled on commercial arbitration’s procedural rules (and the confidentiality obligations they convey), given the public interests often implicated in ISA disputes.⁷ The opaque nature of the arbitration system is often regarded as accountable for the ISA system’s legitimacy crisis.⁸ In response, the European Union (“EU”) has proposed to replace the arbitration system with

4. Andrew P. Tuck, *Investor-State Arbitration Revised: A Critical Analysis of the Revisions and Proposed Reforms to the ICSID and UNCITRAL Arbitration Rules*, 13 LAW & BUS. REV. AM. 885, 885 (2007).

5. *ICSID in Crisis: Straight-Jacket or Investment Protection?*, BRETTON WOODS PROJECT (July 10, 2009), <https://www.brettonwoodsproject.org/2009/07/art-564878>. See generally Ignacio A. Vincentelli, *The Uncertain Future of ICSID in Latin America*, 16 L. & BUS. REV. AM. 409 (2010); Diana Marie Wick, *The Counter-Productivity of ICSID Denunciation and Proposals for Change*, 11 J. INT’L BUS. & L. 239 (2011). As the U.N. Conference on Trade and Development (“UNCTAD”) notes, “There are concerns that the current mechanism exposes host States to additional legal and financial risks, often unforeseen at point of entering into the IIA and in circumstances beyond clear-cut infringements on private property, without necessarily bringing any benefits in terms of additional FDI flows [and] . . . that it can create the risk of a ‘regulatory chill’ on legitimate government policymaking.” UNCTAD, *World Investment Report 2015: Reforming International Investment Governance* 128, https://unctad.org/en/PublicationsLibrary/wir2015_en.pdf.

6. The backlash against ISA can be illustrated by the grievance of Bolivian President Evo Morales that, under the current ISA system, developing countries in Latin America have never won a dispute, while transnational corporations have always won. See, e.g., Charles N. Brower & Sadie Blanchard, *What’s in a Meme? The Truth About Investor-State Arbitration: Why It Need Not, and Must Not, Be Repossessed by States*, 52 COLUM. J. TRANSNAT’L L. 689, 691–95 (2014); Susan D. Franck, *Development and Outcomes of Investment Treaty Arbitration*, 50 HARV. INT’L L.J. 435, 436–37 (2009).

7. In form, investor-state arbitration is said to be somewhat modeled on “private” commercial arbitration, but the nature of investor-state disputes often relates to the regulatory autonomy of sovereign states and their agencies. The private nature of the arbitration system for investor-state disputes can be witnessed in the fact that: “Investment arbitrators are *ad hoc* appointees, not domestic judges holding permanent office. ICSID hearings are often conducted privately. Third parties, including civic interest groups, are permitted to participate in proceedings only if the disputing parties consent or if the applicable investment treaty so provides.” See Leon E. Trakman, *The ICSID Under Siege*, 45 CORNELL INT’L L.J. 603, 620–23 (2012).

8. Because “many ICSID tribunals continue to employ standards of review developed from the private law origins of international arbitration,” some states have started to view the legitimacy of investor-state arbitration with skepticism. See Burk-White & von Staden, *supra* note 3, at 285.

a multilateral investment court, and this idea has received support in academia.⁹

Though there is an ongoing debate over how the incentives of arbitrators vary from those of judges, it is striking that the Law and Economics literature analyzing these incentives in detail is not incorporated into that debate.¹⁰ There are a few economic studies of the ISA system,¹¹ but they do not account for the Law and Economics perspective, which pays particular attention to how various institutions and instruments affect the incentives of all parties involved. There is, meanwhile, rich empirical literature on the practice of ISA,¹² but, to the best of our knowledge, the results of these empirical studies are neither presented in an integrated manner, nor are they considered by the theoretical Law and Economics literature.

This article is intended to fill that important gap. It will contribute to the debate on the reform of the ISA system by integrating existing Law and Economics literature with empirical evidence assessing the theories that this literature promotes. This integration will provide useful and important new insights for the reform of the current ISA mechanism.

This article starts by presenting the basic Law and Economics insights into the differences between arbitration and the court system. In Part II, it highlights the arguments in favor of and against the commercial arbitration system upon which ISA is modeled by comparing that system to more traditional court-based adjudication. Part III sketches the differences between the ISA system and commercial arbitration—particularly with regard to party and adjudicator incentives, and details the contribution of those differences to the success of the ISA mechanism. Then the article moves to the rich empirical evidence available on ISA: In Part IV, we discuss how the current ISA system works (focusing on arbitration filings, claims, and awards). Part V analyzes to what extent these empirical findings substantiate the criticisms of ISA formulated in the theoretical literature

9. It warrants noting that the EU is at the vanguard, advocating the replacement of the current arbitration mechanism with a permanent investment court. “By large majority, the European Parliament substantially refused the current ISDS system, characterized as an outdated model. Notably, the critique against that system was also expressed by a number of EU Member States that so far had been pro-ISDS, such as France, Germany and the Netherlands, all calling for a permanent investment court.” Piero Bernardini, *Reforming Investor-State Dispute Settlement: The Need to Balance Both Parties’ Interests*, 32 ICSID REV. - FOREIGN INV. L.J. 38, 40 (2017).

10. Orley Ashenfelter, *Arbitration*, in THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW 88, 88–93 (Peter Newman ed., 1998).

11. See e.g., Jennifer Kirby, *Efficiency in International Arbitration: Whose Duty Is It?*, 32 J. INT’L ARB. 689, 689–95 (2015).

12. See e.g., Thomas Schultz & Cédric Dupont, *Investment Arbitration: Promoting the Rule of Law or Over-Empowering Investors? A Quantitative Empirical Study*, 25 EUR. J. INT’L L. 1147, 1147–68 (2015); Gus Van Harten & Pavel Malysheuski, *Who Has Benefited Financially from Investment Treaty Arbitration? An Evaluation of the Size and Wealth of Claimants* (Osgoode Legal Stud. Res. Paper Series, Paper No. 14, 2016).

reviewed in Parts II and III. In Part VI, we turn to potential reforms of the ISA system, considering how both theoretical law, economic analysis, and empirical findings might apply to an investment court or other proposals. The article concludes by outlining the key lessons for the international legal community drawn from comparing the theoretical Law and Economics literature that discusses adjudicative best practices to the empirical data on how the ISA system actually functions.

II. ARBITRATION VERSUS THE COURTS: THEORY

To understand some of the criticisms of the ISA system, it is worthwhile to review the principal differences between commercial arbitration and adjudication in court. Using a Law and Economics framework, we will assess the incentives for private parties to use arbitration rather than a domestic court system (Section A). Then we will focus on the other important stakeholders in dispute settlement—judges and arbitrators—and analyze the differences in their incentive structures (Section B). Finally, we will compare the social costs of arbitration and the court system (Section C).

A. *Why Arbitrate? Incentives for Parties*

Why do parties choose, during contract formation, to submit future disputes to arbitration rather than using state-provided adjudication? After all, assuming that parties are utility maximizers and cost minimizers, adjudication via state mechanisms is subsidized by the government, while arbitration is largely self-financed.

In his contribution to the Encyclopedia of Law and Economics, Professor Bruce Benson, an American academic economist, depicted commercial arbitration as a cooperative endeavor to minimize the costs of dispute resolution.¹³ Unlike judges, arbitrators tend to specialize in particular types of disputes, and parties can select arbitrators based on their specialized expertise.¹⁴ The advantage of such specialization is that arbitrators can render a decision more quickly and with less information transferred from the parties to the arbitrator than to a traditional court.¹⁵ Additionally, given the arbitrators' higher levels of expertise, error costs

13. Bruce L. Benson, *Arbitration*, in 5 ENCYCLOPEDIA OF LAW AND ECONOMICS 159, 161 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000).

14. See e.g., Charles H. Brower, *The Functions and Limits of Arbitration and Judicial Settlement Under Private and Public International Law*, 18(2) DUKE J. COMP. & INT'L L. 259, 264 (2008); Mauro Rubino-Sammartano, *The Decision-making Mechanism of the Arbitrator Vis-à-Vis the Judge*, 25 J. INT'L ARB. 167, 168 (2008).

15. Bruce L. Benson, *To Arbitrate or To Litigate: That Is the Question*, 8 EUR. J. L. & ECON. 91, 94 (1999).

may be lower.¹⁶ Benson thus maintains that arbitration is less formal than adjudicative proceedings and less expensive.¹⁷ Robert Cooter and Tom Ulen, two celebrated American Law and Economics scholars, also argue that arbitration is “much cheaper and less time-consuming than litigation.”¹⁸

Moreover, arbitrators and potential arbitrators have incentives to behave in ways that correlate to a large extent with the preferences of the disputants—or at least of their legal counsel—in relation to, among other things, the application of law.¹⁹ Another related benefit of arbitration is that parties usually have veto power in selecting arbitrators, which results in stronger incentives for arbitrators to continuously develop their own expertise and to render unbiased decisions.²⁰

An important point in that respect is the statistical “exchangeability” of arbitrators.²¹ According to economist Orley Ashenfelter, arbitrators will avoid taking extreme positions that may diminish their probability of being selected to arbitrate in the future.²² A successful arbitrator will therefore write a decision that correctly forecasts (or attempts to forecast) the decisions other arbitrators will make in similar situations. That should, in theory, lead to the exchangeability of arbitrator decisions necessary to the continued acceptability of the arbitration system.²³

There are some other advantages of arbitration that are often discussed by scholars that may incentivize disputants to arbitrate. First, arbitration is generally less adversarial than litigation, allowing disputants to continue mutually beneficial commercial relationships.²⁴ Second, arbitral proceedings can be kept confidential, minimizing reputational damage to the parties.²⁵ Professor Leon Trakman, a celebrated commercial arbitrator and trade adjudicator, believes that the possibility of maintaining “confidentiality is key to the successful practice of international commercial arbitration” because disputants are thus able to protect their trade secrets and preserve

16. According to Benson, error costs refer to the costs incurred by the disputing parties as a result of an error in judgment (or an arbitral decision in this case). *Id.*

17. Benson, *supra* note 13, at 164. In sum, while arbitrator compensation and other arbitral costs can be substantially higher than the cost of using the state-subsidized court system, parties save money on discovery and development of evidence.

18. ROBERT COOTER & TOM ULEN, *LAW AND ECONOMICS*, 450 (6th ed. 2012).

19. See Anne van Aaken & Tomer Broude, *Arbitration from a Law and Economics Perspective*, in *THE OXFORD HANDBOOK OF INTERNATIONAL ARBITRATION* (Thomas Schultz & Federico Ortino eds., forthcoming 2019).

20. Benson, *supra* note 13, at 162.

21. See Ashenfelter, *supra* note 10, at 90.

22. Orley Ashenfelter, *Arbitrator Behavior*, 77(2) *AM. ECON. REV.* 342, 343 (1987).

23. Benson, *supra* note 13, at 186.

24. *Id.* at 164.

25. *Id.*

good business relations.²⁶ Third, parties may avoid the application of state-made law where they would prefer the application of privately agreed rules, including business practice and custom.²⁷

Notwithstanding these advantages of arbitration, the literature also suggests potential disadvantages. According to Dr. Robert Kovacs, a well-known lawyer specializing in international commercial arbitration and ISA alike, there are currently substantial barriers to efficiency in international arbitration.²⁸ He points, *inter alia*, to information failures, agency cost problems, and dilatory tactics.²⁹ With regard to information failures, Kovacs notes that legal counselors may not always have the most adequate knowledge or experience in international arbitration and therefore cannot always provide accurate advice to the parties involved.³⁰ As far as agency costs are concerned, Kovacs refers to an agency relationship between lawyers and their clients which creates monitoring costs and bonding costs.³¹ Parties may, moreover, use dilatory tactics, for example by extending the process in order to delay the adverse effects that an arbitral award may have on their financial records.³²

Other concerns include fear that arbitrators may be biased, or that they are easily corruptible.³³ In arbitral practice, often “each party will appoint an arbitrator (‘party-appointed arbitrators’) and those party-appointed arbitrators will choose the other arbitrator(s).”³⁴ A common party appointment model may lead to so-called “affiliation effects,” meaning that a party-appointed arbitrator will have an unavoidable tendency to favor the party which appointed him.³⁵ In light of the goal of an independent and neutral adjudicatory mechanism, the predisposition toward a party resulting

26. Leon E. Trakman, *Confidentiality in International Commercial Arbitration*, 18 ARB. INT’L L 1, 1–2 (2002).

27. Benson, *supra* note 13, at 164.

28. Robert B. Kovacs, *Efficiency in International Arbitration: An Economic Approach*, 23 AM. REV. INT’L ARB. 155, 160 (2012).

29. *Id.* at 161–66.

30. *Id.* at 162.

31. *Id.* at 162–63. Monitoring costs are incurred by clients who are found to “lack the ability to impose significant budget restrictions, compensation policies or coercive power, nor the expertise to monitor the work of lawyers.” *Id.* at 163. In contrast, bonding costs are imposed upon lawyers through a retainer agreement and national regulation of legal professions. *Id.*

32. *Id.* at 166.

33. Benson, *supra* note 13, at 184.

34. Richard M. Mosk, *The Role of Party-Appointed Arbitrators in International Arbitration: The Experience of the Iran-United States Claims Tribunal*, 1 TRANSNAT’L LAW. 253, 253 (1988).

35. Van Aaken & Broude, *supra* note 19, at 15–16.

from the party appointment model poses significant challenges to the legitimacy of arbitration.³⁶

On the other hand, Benson rejects those arguments, as they do not sufficiently account for the importance of the arbitrator selection process, which is designed precisely to avoid bias.³⁷ Moreover, the competition between arbitrators improves arbitrator quality, especially since, in most systems, parties can veto particular arbitrators.³⁸ In any case, the use of blind appointment, which allows parties to appoint arbitrators but prevents appointees from knowing their appointing parties, has been proposed in recent years to reduce affiliation bias.³⁹

B. *Incentives of Judges Versus Arbitrators*

According to Law and Economics scholarship, arbitrators are more incentivized to provide high-quality decisions than judges. This scholarship may provide interesting lessons for the design of a potential multilateral investment court.

In a few remarkable publications, Richard Posner, a respected Law and Economics scholar and a former U.S. judge, has argued that judges are “the same as everybody else,” i.e., incentivized to maximize their utility.⁴⁰ But what precisely does utility maximization mean for a judge? Posner argues that, like for everyone else, money may play a role, but it is definitely not the only component of most judges’ utility functions.⁴¹ Judges also derive utility from non-pecuniary goods such as leisure and prestige.⁴² However, the problem is that judges do not receive pay raises as a reward for good work, and thus they may be less incentivized than arbitrators to deal with cases in an efficient manner. Correspondingly, increasing judicial caseloads will not lead to judges working harder, as that would mean sacrificing leisure, but may instead lead to judges spending less time on each case.⁴³

Consider the goals of members of U.S. Supreme Court. While political scientists largely believe that the justices focus chiefly on a single goal, i.e., “making the law more consistent with their policy preferences,” Dr. Lawrence Baum, a renowned political scientist specializing in the U.S. court

36. Sergio Puig & Anton Strezhnev, *Affiliation Bias in Arbitration: An Experimental Approach*, 46 J. LEGAL STUD. 371, 374 (2017).

37. Benson contends that, although arbitration selection mechanisms demonstrate wide variation, they always allow for prescreening of the potential arbitrators. Thus, disputants and organizations are able to filter out evidently biased candidates. Benson, *supra* note 13, at 184–85.

38. *Id.*

39. Puig & Strezhnev, *supra* note 36, at 372.

40. See Richard A. Posner, *What Do Judges and Justices Maximize? (The Same Thing Everybody Else Does)*, 3 SUP. CT. ECON. REV. 1, 2, 39 (1993).

41. See RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 570 (7th ed. 2007).

42. *Id.*

43. *Id.*

system, argues that a justice may also have other goals to advance; for instance, “approval from the public and respect from the legal community.”⁴⁴ In contrast, the problem with the general judiciary, according to Posner, is that, especially for judges in the highest courts (who cannot receive further promotion), leisure may often be an important driver of their decision-making.⁴⁵ This may even lead judges to base decisions of material law on the potential for reduction of their caseload in a bid to strive for more leisure. This is an unacceptable adjudicatory practice under certain circumstances, such as when done at the cost of procedural integrity and substantive justice. This possibility (the prioritization of leisure) is already confirmed by some empirical studies.⁴⁶

Arbitrators clearly want to maximize their own utility as well, but since they face more competition than judges, the influence of market pressures on their performance may be much stronger.⁴⁷ Like judges, “[a]rbitrators have their own interests which, among other things, can include such factors as earning income, enjoying leisure time, providing ‘justice,’ establishing or preserving their reputation, advancing their own career and so on.”⁴⁸ But arbitrators will generally make decisions in order to satisfy the preferences of existing or potential parties.⁴⁹

On the other hand, Kovacs also indicates that the arbitration market is probably not as competitive as it may appear; there are high barriers to market entry.⁵⁰ Developing a positive reputation to compete as an arbitrator may take many years.⁵¹ Moreover, risk-averse disputants have a tendency to prefer arbitrators with considerable experience and would not want to take chances with new players in the market.⁵² Likewise, Posner and others argue that because arbitrators best guarantee future appointments and a constant stream of income by placating both sides, they may have a tendency to “split the difference” in their award, giving each side a partial victory.⁵³ Such a pattern mitigates claims that arbitrators favor one side or the other and could be attractive to risk-averse disputants.⁵⁴ Posner further argues that arbitrators are incentivized to “split the difference” because governments

44. See Lawrence Baum, *What Judges Want: Judges' Goals and Judicial Behavior*, 47 POL. RES. Q. 749, 754–60 (1994).

45. Posner, *supra* note 41, at 570.

46. See generally, Jef De Mot, Michael Faure & Jonathan Klick, *Appellate Caseload and the Switch to Comparative Negligence*, 42 INT'L REV. L. & ECON. 147–56 (2015) (discussing this so-called “lazy judges” literature).

47. See *supra* text accompanying notes 21–23.

48. Kovacs, *supra* note 28, at 160.

49. Van Aaken & Broude, *supra* note 19, at 14.

50. Kovacs, *supra* note 28, at 170.

51. *Id.*

52. *Id.*

53. Posner, *supra* note 41, at 558.

54. *Id.* at 559.

subsidize their courts, leaving arbitrators at a relative disadvantage.⁵⁵ Since they lack state subsidy, they need to provide some other advantage to disputants in order to stay in business.⁵⁶ But this practice is likely to render compromise awards that academics link to other forms of cognitive bias.⁵⁷ Fortunately, Benson provides an overview of empirical evidence showing that while some studies support the “split the difference” hypothesis, other studies also find substantial variants in arbitration awards.⁵⁸ He concludes that the overall evidence seems to show that arbitrators “do much more than split the difference.”⁵⁹

Thus, the Law and Economics literature informs us that because judges do not often derive pecuniary rewards from good work, arbitrators are better incentivized to provide for high-quality decision-making due to a higher level of market pressures. However, the existing barriers to the efficiency of international arbitration and arbitrators’ tendency to “split the difference” could undermine the legitimacy of arbitration.

C. Social Costs of Arbitration

When addressing the Law and Economics of any topic, the first scholars to refer to are, on the one hand, William Landes, an American economist specializing in the economic analysis of law, and Richard Posner and, on the other, Steven Shavell, a Professor of Law and Economics from Harvard University. These recognized authorities on Law and Economics have all opined briefly on arbitration, Landes and Posner rather negatively, Shavell more positively. In a joint 1979 article, Landes and Posner make the simple point that arbitration will be sought by the parties in order to benefit their own interests, but not necessarily society’s interest.⁶⁰ They argue that adjudication via courts generally creates large and public positive externalities, which is one of the reasons why the courts are subsidized by the government⁶¹: Courts create precedents and provide information on issues that are in dispute. In this way, the whole society is very likely to

55. *Id.*

56. *Id.*

57. For example, academics have referred to anchoring and extremeness aversion as examples of these cognitive biases. Anchoring means arbitrators are likely to mechanically compromise between the disputing parties’ final offers without adequate reference to the facts of the case. Extremeness aversion indicates that arbitrators may refuse to grant extreme decisions. Daphna Kapeliuk, *The Repeat Appointment Factor: Exploring Decision Patterns of Elite Investment Arbitrators*, 96 CORNELL L. REV. 47, 62–63 (2010).

58. Benson, *supra* note 13, at 181–82.

59. *Id.* at 182.

60. William M. Landes & Richard A. Posner, *Adjudication as a Private Good*, 8 J. LEGAL STUD. 235, 236, 274 (1979).

61. *Id.* at 241. For a detailed analysis of lawmaking through adjudication, see Francesco Parisi & Vincy Fon, *Lawmaking Through Adjudication*, in THE ECONOMICS OF LAWMAKING 73–83 (2009).

reap the benefits of increased clarity in legal norms and their application. In contrast, Landes and Posner argue that arbitration under-produces precedent. “Because of the difficulty of establishing property rights in a precedent, private . . . judges might deliberately avoid explaining their results because the demand for their services would be reduced by rules that, by clarifying the meaning of the law, reduce the incidents of disputes.”⁶² It is a point Posner makes again in his book *Economic Analysis of Law*, where he writes:

Since the state does not pay any part of the expense of arbitration, we should not be surprised that most arbitrators do not write opinions. The value of opinions would accrue mainly to people other than the parties to the arbitration—people who would not contribute to the expenses of the arbitration.⁶³

Although not all authors agree with Landes and Posner on these points,⁶⁴ the discussion already provides an important insight: To the extent that investor-state dispute resolution should create external benefits, that militates in favor of resolving investor-state disputes via court adjudication rather than arbitration. Note that one can relate this argument to the call for larger transparency within investor-state dispute resolution. Without transparency, it is impossible for dispute resolution mechanisms to create these positive externalities.

Shavell, in contrast, discusses why parties would opt for arbitration prior to the emergence of a dispute in his 1995 article *Alternative Dispute Resolution: An Economic Analysis*.⁶⁵ Shavell mentions three advantages of arbitration for the parties concerned: (1) it may lower the costs and risks of dispute resolution because resort to arbitration is likely to reduce the total costs of dispute resolution and to avoid exposure to unreliable jury verdicts; (2) it may create better incentives for parties to a contract to perform, thus increasing the joint value that the parties’ relationship produces, because of the greater accuracy of private dispute resolution,⁶⁶ and (3) it may reduce the number of trials because the lower costs of arbitration should incentivize parties to resort to arbitration rather than going to trial.⁶⁷

62. Landes & Posner, *supra* note 60, at 238–39.

63. Posner, *supra* note 41, at 558.

64. *Inter alia*, Benson argues that arbitration may in some circumstances create external benefits. See Benson, *supra* note 15, at 104–05.

65. See Steven Shavell, *Alternative Dispute Resolution: An Economic Analysis*, 24 J. LEGAL STUD. 1 (1995). For a summary of Shavell’s reasoning, see Lewis A. Kornhauser, *Judicial Organization and Administration*, in 5 ENCYCLOPEDIA OF LAW AND ECONOMICS, *supra* note 13, at 27.

66. Shavell expects greater accuracy because arbitrators are usually experts in a particular field and may therefore be better qualified than judges who generally deal with a great many different cases. Shavell, *supra* note 65, at 9.

67. *Id.* at 5–7.

Shavell's general insight is that Alternative Dispute Resolution ("ADR") systems like arbitration provide clear private benefits *to the parties* and should for that reason be enforced.⁶⁸ *Ex ante*, parties themselves have much better information about the risks and circumstances of their transaction than a court; when they determine that their interests can better be served through arbitration, there is reason to enforce their agreement.⁶⁹

Shavell reprised this reasoning in his well-known Law and Economics handbook, *Foundations of Economic Analysis of Law*.⁷⁰ He argued that if parties each separately choose to use the same private dispute resolution system, then that system must be making each of them better off—which is precisely the reason to enforce it.⁷¹ Moreover, if no one else is made worse off by the parties' private agreement, there is no reason for society not to enforce the agreement.⁷² Note that this assumes that only the parties to the contract are affected by it,⁷³ a proposition with which Posner and Landes would probably take umbrage.

It is interesting that the founding fathers of the Law and Economics movement apparently diverge on the benefits of arbitration. On the one hand, Shavell sees strong advantages, but his argument is based on two major assumptions: (1) that the costs of arbitration are lower than those of adjudication and (2) that arbitration has no third-party effects.⁷⁴ Landes and Posner, on the other hand, see strong disadvantages related to the fact that arbitration does not produce public good in the way that adjudication does. Their argument seems to assume that arbitrators lack the incentive to write their opinions down in the process of decision-making because arbitration is sponsored by private parties instead of public finance.⁷⁵

D. Summary

This overview of the differences between arbitration and adjudication via the courts, using a Law and Economics approach, provides various interesting insights. The main advantage of commercial arbitration is related to the potential quality of the arbitrators. Because specialized arbitrators can be selected in particular disputes, the disputants expect the quality of the decision-making to be superior, leading to reduced costs and faster decision-making. However, the Law and Economics literature also indicates that both judges and arbitrators have decision-making incentives that may not be

68. *Id.*

69. *Id.*

70. STEVEN SHAVELL, FOUNDATIONS OF ECONOMIC ANALYSIS OF LAW (2004).

71. *Id.* at 446–47.

72. *Id.*

73. *Id.*

74. Shavell, *supra* note 65, at 5–9.

75. Landes & Posner, *supra* note 60, at 238–39.

optimal.⁷⁶ For example, Judges might prefer to maximize their utility through leisure when their dockets become full, but they may also be incentivized to provide quality decisions for the sake of their reputations. On the other hand, arbitrators may have stronger incentives for high-quality decision-making as a result of competitive pressure. However, precisely because of that competitive pressure—and arbitrators’ desire to be guaranteed a stream of income—arbitrators may have a tendency to split the difference between the parties instead of always providing a “just” decision.

As far as the social costs of arbitration are concerned, some traditional Law and Economics scholars argue that arbitration is not able to generate the kinds of large and public positive externalities that are usually attributed to adjudication via courts.⁷⁷ There is little incentive for arbitrators to produce precedents, and inconsistent decisions in arbitration could potentially destroy the value of a precedential system in any case.⁷⁸

Overall, Law and Economics scholars have mixed views with respect to arbitration. For a variety of reasons, Law and Economics scholarship understands why parties often prefer arbitration to adjudication. The private benefits of arbitration may be real. At the same time the scholarship also indicates that, from a social perspective, there is a substantial disadvantage to arbitration: the absence of public good.

III. THE CHARACTERISTICS OF ISA

A large portion of the Law and Economics literature evaluating the advantages of arbitration for private parties focuses on commercial arbitration. This literature may therefore fail to reflect situational differences that are present when a state is involved in the dispute—differences that may even cause the social costs of arbitration to increase. We start by sketching the emergence and development of ISA and its position in the broader picture of investor-state dispute settlement (Section A). Next, we explain how the current ISA regime consists of multiple layers of treaties, laws, and rules; this implies that any changes to the existing ISA mechanism may entail modifications across those layers (Section B). Although ISA is modeled after commercial arbitration, we discuss substantial differences between ISA and commercial arbitration in Section C and criticisms of and reform proposals for the ISA model in Section D.

A. *The Emergence and Development of ISA*

Although ISA seems to dominate the discussions of the investment treaty regime in the academic community and media, not least due to the

76. See *supra* Part II.B.

77. Van Aaken & Broude, *supra* note 19, at 6.

78. *Id.*

publicity of negotiations over high-stakes economic pacts,⁷⁹ it is a relatively new method for resolving investment disputes. The investment treaty regime went virtually unnoticed until the early years of this century, in striking contrast with other areas of global economic governance.⁸⁰ Diplomatic channels used to be the main method by which states resolved investment disputes.⁸¹ But while diplomacy could protect investors in a foreign country to a certain extent, its political nature and associated flaws meant that it could not meet the growing need for dispute settlement between foreign investors and host states that ensued from increasing cross-border capital flows.⁸²

In the present day, foreign investors are also able to settle disputes before national courts within the territory of host states. However, investors might be loath to refer their cases to a host state's judicial branch because of inherent drawbacks that could prejudice their odds of securing indemnity. Foreign investors are likely to have little confidence in the independence and impartiality of domestic courts because the judiciary is inextricably associated with national interests. Foreign investors may also feel uneasy about the potential "hazards of delay and political pressure" that adjudication via national courts could entail.⁸³

The lack of a supranational and accessible forum for entertaining disputes that arose from foreign direct investment ("FDI") invited the creation of a new mechanism. While domestic courts are often considered to be too biased and partial to properly consider cases from foreign investors, international arbitration is thought to provide neutrality.⁸⁴ The introduction

79. These eye-catching economic pacts—concluded or not—include, *inter alia*, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership ("CPTPP"), the Transatlantic Trade and Investment Partnership ("TTIP") and the EU-Canada Comprehensive Economic and Trade Agreement ("CETA"). CPTPP and CETA have been concluded and ratified. See, e.g., Heng Wang, *The Future of Deep Free Trade Agreements: The Convergence of TPP (and CPTPP) and CETA?*, 53 J. WORLD TRADE 317, 317–42 (2019); Reinhard Quick, *Why TTIP Should Have an Investment Chapter Including ISDS*, 49 J. WORLD TRADE 199, 199–209 (2015). Notably, CETA is one of the initial steps taken by the EU to usher in innovative reform of ISA using a standing multilateral investment court. David A. Gantz, *The CETA Ratification Saga: The Demise of ISDS in EU Trade Agreements?*, 49 LOY. U. CHI. L.J. 361, 368 (2017).

80. JONATHAN BONNITCHA ET AL., *THE POLITICAL ECONOMY OF THE INVESTMENT TREATY REGIME I* (2017).

81. Won-Mog Choi, *The Present and Future of the Investor-State Dispute Settlement*, 10 J. INT'L ECON. L. 725, 725 (2007).

82. *Id.* at 727–28.

83. SURYA P. SUBEDI, *INTERNATIONAL INVESTMENT LAW: RECONCILING POLICY AND PRINCIPLE* 32 (2008).

84. Schreuer identifies avoidance of domestic courts as one of the main purposes of the ISA system. For further discussions on the perceived deficiencies of court litigation in addressing investor-state disputes, see generally Christoph Schreuer, *Interaction of International Tribunals and Domestic Courts in Investment Law*, in *CONTEMPORARY ISSUES IN INTERNATIONAL ARBITRATION AND MEDIATION: THE FORDHAM PAPERS* (2010) 71–72

of the ICSID Convention and its concomitant dispute settlement body in the 1960s, focusing on the arbitration of investment disputes instead of on the substantive protection of foreign investors,⁸⁵ has effectively filled this gap. Under this arbitration system, foreign investors are endowed with standing to launch a claim against states at the international level, thereby avoiding the need, in many circumstances, to rely on remedies available within a host state.⁸⁶ This investor-state dispute settlement mechanism is unique, though not unprecedented in other areas of international law.⁸⁷ However, for a long time, the World Bank's investment dispute settlement body did not receive many requests for arbitration from foreign investors, probably because of those investors' unawareness of the ISA system or the relatively limited amount of qualifying FDI flows, or both. The first known treaty-based investment claim was brought under the Sri Lanka-UK bilateral investment treaty ("BIT") in 1987 when a British investor alleged damage to its investment caused by a military operation by Sri Lankan security forces.⁸⁸ The entry into the new millennium marked a rapid increase in the use of the ISA mechanism, totaling over 900 cases at the time of this writing.⁸⁹

B. *The Legal Foundations of the ISA Regime*

The ISA regime, insofar as investment treaty-based arbitration is concerned, is composed of three main legal components. First, the

(Arthur Rovine ed., 2011). See also Alexandre Gauthier, *Investor-State Dispute Settlement Mechanisms: What Is Their History and Where Are They Going?* 1–2 (Library of Parliament (Canada), Publication No. 115-E, 2015), <https://lop.parl.ca/staticfiles/PublicWebsite/Home/ResearchPublications/BackgroundPapers/PDF/2015-115-e.pdf>.

85. J. Christopher Thomas & Harpreet Kaur Dhillon, *The Foundations of Investment Treaty Arbitration: The ICSID Convention, Investment Treaties and the Review of Arbitration Awards*, 32 ICSID REV. – FOREIGN INV. L.J. 459, 462 (2017).

86. The typical BIT provides a standing offer to arbitrate through which foreign investors are able to resolve covered disputes with the host state in a neutral arbitral forum. Richard C. Chen, *Bilateral Investment Treaties and Domestic Institutional Reform*, 55(3) COLUM. J. TRANSNAT'L L. 547, 554 (2017).

87. International human rights law is another area where individuals are given the possibility to directly participate in supranational dispute resolution with sovereign states on the international plane. However, human rights conventions commonly require individuals to exhaust local remedies before making direct claims. To illustrate, article 35 of the European Convention for the Protection of Human Rights and Fundamental Freedoms stipulates that the European Court of Human Rights is ready to entertain private petitions only "after all domestic remedies have been exhausted." Choi, *supra* note 81, at 729–31.

88. *Asian Agricultural Products Ltd. v. Republic of Sri Lanka*, ICSID Case No. ARB/87/3 (1990). A breakdown of a large majority of known ISA cases according to the year each was initiated is available via the Investment Dispute Settlement Navigator operated by UNCTAD. *Investment Dispute Settlement Navigator*, UNCTAD INVESTMENT POLICY HUB, <https://investmentpolicyhub.unctad.org/ISDS> (last visited Dec. 17, 2019).

89. Jason Webb Yackee, *Controlling the International Investment Law Agency*, 53 HARV. INT'L L.J. 391, 392–93 (2012); *Investment Dispute Settlement Navigator*, *supra* note 88.

protection promised by signatory states to foreign investors and their investments is derived from and enforceable through international agreements. Second, in the event of an arbitration to enforce that promised protection (or to seek compensation for its absence), the procedure of the arbitration and the protocol for subsequent enforcement of an award are governed by institutional or *ad hoc* arbitration rules, national arbitral legislation, and even an international convention. Third, though the decisions and awards issued by prior investment tribunals are not formally binding, they are understandably influential to other tribunals applying and interpreting similar investment agreements.⁹⁰

International investment agreements (“IIAs”), like national investment law and investor-state contracts, manifest state consent, which is indispensable for maintaining the legitimacy of and legal basis for ISA.⁹¹ A large majority of arbitral proceedings before investment tribunals are founded upon the dispute resolution sections of IIAs.⁹² The intricate global mesh of IIAs has established a protective network for cross-border investors by setting out a range of terms under which signatory states promise investors reasonable protection and treatment.⁹³ These terms routinely address fair and equitable treatment, national treatment, most favored nation treatment, full protection and security, and protection from expropriation.⁹⁴ National treatment and most favored nation treatment are also collectively known as non-discrimination standards that proscribe discrimination on the basis of nationality.⁹⁵

With regard to the procedural rules applicable to ISA, apart from ICSID’s Arbitration Rules and Additional Facility Arbitration Rules, other arbitration rules—such as the UNCITRAL Arbitration Rules and the rules of the International Chamber of Commerce (“ICC”) and the Stockholm Chamber of Commerce (“SCC”)—are often available to aggrieved investors

90. BONNITCHA ET AL., *supra* note 80, at 3.

91. Michael Waibel, *Investment Arbitration: Jurisdiction and Admissibility* (U. of Cambridge Fac. Of L. Res. Paper Series, Paper No. 9, 2014).

92. An international investment agreement is a generic concept employed here to refer to various breeds of economic agreements that deal with the protection and/or liberation of cross-border investments, including bilateral investment treaties (“BITs”), the investment chapters of free trade agreements (“FTAs”) and other sector-specific economic instruments such as the Energy Charter Treaty (the “ECT”). Take ICSID arbitration as an example. Parties commonly invoke BITs and other treaties as the basis upon which to launch arbitral proceedings. *Case Databases*, ICSID, <https://icsid.worldbank.org/en/Pages/cases/AdvancedSearch.aspx> (last visited Dec. 17, 2019).

93. CAMPBELL MCLACHLAN ET AL., *INTERNATIONAL INVESTMENT ARBITRATION : SUBSTANTIVE PRINCIPLES* 30 (2007).

94. *Id.* at 45.

95. Marcos Orellana, *Investment Agreements & Sustainable Development: The Non-Discrimination Standards*, 11 *SUSTAINABLE DEV. L. & POL’Y* 3, 3 (2011).

pursuing non-ICSID arbitrations.⁹⁶ There are a variety of other procedural differences between ICSID and non-ICSID arbitrations.⁹⁷ While ICSID arbitration is a self-contained system in which the recognition and enforcement of awards is regulated by the ICSID Convention, non-ICSID arbitration sometimes relies on the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the “New York Convention”) to ensure the recognition and enforcement of the investment awards.⁹⁸ In addition, in comparison to the relative futility of the local law of the arbitration situs in relation to the procedure of ICSID arbitration, non-ICSID arbitration is subject to the named seat’s local arbitration legislation, thus integrating *lex loci arbitri*.⁹⁹

Investment arbitrators are charged with stitching together the underlying investment agreements and the applicable procedural rules. In addition to applying and interpreting IIAs during ISA proceedings, arbitrators apply the parties’ chosen arbitration rules to the arbitral process to ensure its fairness, integrity, and efficiency. Ultimately, arbitral awards document how the arbitral authority has applied and interpreted the substantive provisions of IIAs so as to deal with investment disputes.¹⁰⁰ Thus, though not formally precedential, investment awards have contributed to the dynamics and evolution of the ISA regime; prior investment awards are invariably invoked by disputing parties to defend their positions and by investment tribunals to support their legal reasoning.¹⁰¹

96. ZACHARY DOUGLAS, *THE INTERNATIONAL LAW OF INVESTMENT CLAIMS* 3–5 (2009).

97. Throughout this article, arbitral proceedings that are conducted pursuant to the ICSID Arbitration Rules are “ICSID arbitrations,” while proceedings that unfold under other arbitration rules, including the Additional Facility Arbitration Rules, are dubbed “non-ICSID arbitrations.”

98. Articles 53, 54, and 55 of the ICSID Convention prescribe the recognition and enforcement of investment awards by domestic courts outside of ICSID arbitration proceedings. In contrast to the self-contained recognition and enforcement mechanism in the ICSID Convention, investment awards under non-ICSID arbitration (for instance, pursuant to the United Nations Commission on International Trade Law (“UNCITRAL”) Arbitration Rules) rely on the New York Convention for recognition and enforcement. Kamal Huseynli, *Enforcement of Investment Arbitration Awards: Problems and Solutions*, 3 BAKU ST. U.L. REV. 40, 42 (2017).

99. See, e.g., Wick, *supra* note 5, at 275–76.

100. Kathryn Gordon & Joachim Pohl, *Investment Treaties over Time—Treaty Practice and Interpretation in a Changing World* 13 (OECD Working Papers on Int’l Inv., No. 2, 2015), <http://www.oecd.org/investment/investment-policy/WP-2015-02.pdf>.

101. Dolores Bentolila, *Towards a Doctrine of Jurisprudence in Treaty-Based Investment Arbitration* 8–15, https://edisciplinas.usp.br/pluginfile.php/301823/mod_resource/content/0/DOLORES%20BENTOLILA%20-%20Towards%20a%20Doctrine%20of%20Jurisprudence%20in%20Treaty-Based%20Investment%20Arbitration%20.pdf. Notably, there is no formal or binding precedent system within the ISA regime that confines arbitrators to existing arbitral jurisprudence. *Id.* Nevertheless, Cheng and Grisel have respectively articulated that previous arbitral awards tend to come into play in the arbitration of investment awards, even though the arbitral authority is not legally bound to account for the application

C. Investment Arbitration Versus Commercial Arbitration

The emergence of international arbitration in part flows from the biases perceived by the business community in relation to litigation before national courts. The essential idea of international arbitration is to mitigate these biases by submitting a dispute between or among conflicting parties to an unbiased tribunal (or individual) in the hope that a binding arbitral award will be delivered through a process that is different from a court's procedure and formalities.¹⁰² That concept also brings the two branches of arbitration—ISA and international commercial arbitration—into close proximity.

Because international commercial arbitration predates ISA, the current ISA regime drew inspiration from the procedures used in international commercial arbitration.¹⁰³ As a result, ISA shares commonalities with commercial arbitration, including “the number and selection of arbitrators, the presentation of evidence, the conduct of hearings, and the awards.”¹⁰⁴ This relationship is further enhanced by the reliance of some non-ICSID arbitrations on procedural rules that are overwhelmingly used in commercial arbitration.¹⁰⁵

However, ISA and commercial arbitration diverge significantly in important areas despite these similarities.¹⁰⁶ Dr. Lars Markert, a legal counselor with expertise in both commercial arbitration and ISA, points to a few of ISA's differentiating characteristics, all of which are interrelated and have important consequences for the interpretation of the notion of efficiency in international arbitration.¹⁰⁷ The first major difference is that the mere involvement of the state may decrease the speed at which investor-state disputes are resolved.¹⁰⁸ Second, arbitral scrutiny over regulatory measures may adversely affect the interests of the respondent state's

and interpretation of norms and rules by prior tribunals. Tai-Heng Cheng, *Precedent and Control in Investment Treaty Arbitration*, 30 *FORDHAM INT'L L.J.* 1014, 1016 (2006); Florian Grisel, *Precedent in Investment Arbitration: The Case of Compound Interest*, 2 *PKU TRANSNAT'L L. REV.* 216, 226 (2014).

102. S.I. Strong, Essay, *Border Skirmishes: The Intersection Between Litigation and International Commercial Arbitration*, 2012 *J. DISP. RESOL.* 1, 1–2 (2012).

103. Gary Born, *A New Generation of International Adjudication*, 61 *DUKE L.J.* 775, 834–35 (2012).

104. *Id.*

105. The UNCITRAL Arbitration Rules, for instance, not only find their place in international commercial arbitration, but also play their part in ISA. Norbert Horn, *Current Use of the UNCITRAL Arbitration Rules in the Context of Investment Arbitration*, 24 *ARB. INT'L* 587, 588 (2008).

106. Lauren Willis, Book Note, *International Investment and Commercial Arbitration: An Industry Perspective*, 3 *Y.B. ON ARB. & MEDIATION* 542, 542 (2011).

107. Lars A. Markert, *Improving Efficiency in Investment Arbitration*, 4 *CONTEMP. ASIA ARB. J.* 215, 220 (2011).

108. *Id.*

citizenry.¹⁰⁹ Third, the public interest involved may favor more transparent proceedings.¹¹⁰ Fourth, and consequently, there may be demand for publication of the arbitral award.¹¹¹ Fifth, since a greater public interest is at stake, the tribunal should not only take into account the interests of the parties, but also the broader public interest involved, which may also lead to less party autonomy in the procedure.¹¹² Likewise, the public interest involved could imply that a higher investment of time and cost is justified than in international commercial arbitration.¹¹³ These differences should be taken into consideration by stakeholders in an effort to bring about either a moderate reform or an overhaul of the present design of ISA.

Anthea Roberts, an American Professor with extensive scholarship on the topic of investment arbitration, has argued that the ISA regime “grafts public international law (as a matter of substance) onto international commercial arbitration (as a matter of procedure).”¹¹⁴ This idea sheds light on additional differences between ISA and commercial arbitration: the unique need for arbitrators in investor-state disputes to understand and interpret public international law, and the divergent legal frameworks that respectively uphold the two forms of arbitration.

In commercial arbitration, the only noteworthy international instrument is the New York Convention, which was framed to promote the use of arbitration and reinforce the authority of the arbitral system.¹¹⁵ Instead, national law seems to feature more prominently in commercial arbitration than in ISA.¹¹⁶ *Lex loci arbitri* are meant to govern the procedural aspects of commercial arbitration, paralleling national substantive laws that might apply to a dispute’s merits.¹¹⁷

In contrast, international instruments feature prominently throughout all ISA proceedings.¹¹⁸ For example, tribunals are often called upon to apply the ICSID Convention itself or the Vienna Convention on the Law of Treaties (which might be invoked by investment tribunals for the purpose of

109. *Id.* Many claims filed by aggrieved investors have been targeted at government policies that promote public interests and have thus hindered the ability of host states, especially developing countries, to regulate to raise their standards of living. Kevin P. Gallagher & Elen Shrestha, *Investment Treaty Arbitration and Developing Countries: A Re-Appraisal*, 12 J. WORLD INV. & TRADE 919, 919 (2011).

110. Markert, *supra* note 107, at 220.

111. *Id.*

112. *Id.* at 221.

113. *Id.*

114. Anthea Roberts, *Divergence Between Investment and Commercial Arbitration*, 106 AM. SOC’Y INT’L L. PROC. 297, 297 (2012).

115. Karl-Heinz Böckstiegel, *Commercial and Investment Arbitration: How Different Are They Today? The Lalive Lecture 2012*, 28 ARB. INT’L 577, 579 (2012).

116. *Id.* at 579–80.

117. *Id.*

118. *Id.* at 579.

treaty interpretation),¹¹⁹ and the controversies at issue in ISA proceedings are often alleged breaches of the host states' treaty obligations under IIAs. Though national law can be relevant to the resolution of investment disputes,¹²⁰ ICSID arbitration procedures are not anchored to a particular national arbitral regime. (Non-ICSID arbitration has much closer procedural connections to national arbitral legislation.¹²¹)

The different role of public international law in ISA also requires a different scope of expertise among the arbitrators themselves. Roberts claims that ISA brings together professionals from the fields of inter-state dispute resolution and private commercial arbitration.¹²² But a different level of expertise is expected from arbitrators who handle investment disputes and those who do commercial arbitration. Whereas the wide reach of commerce determines that commercial arbitrators are supposed to have knowledge and experience in a special field,¹²³ investment arbitrators have to be knowledgeable of something much broader—public international law—so that they can apply the investment protection provisions of IIAs in a law-abiding and reasonable way.¹²⁴ Jurisdictionally, ISA involves more controversial issues and a much higher frequency of objections.¹²⁵ These differences also lead to more frequent demands for transparency, predictability and consistency in ISA proceedings than commercial arbitration.¹²⁶

D. Criticisms and Reform of ISA

The ISA system has been under serious attack from a variety of parties since 2007, culminating in the “legitimacy crisis” that has become the topic of considerable attention from—and heated debate among—legal scholars and practitioners.¹²⁷ Criticisms include, first, the claim by states and some

119. Ali Moghaddam Abrishami, *Treaty Interpretation in Investment Arbitration* by J. Romesh Weeramantry, 29 ARB. INT'L 549, 549 (2013) (book review).

120. Article 42(1) of the ICSID Convention provides that in case of a default in an agreement between the disputing parties, investment tribunals shall apply the law of the Contracting State party to the dispute and the rules of international law as may be applicable. Convention on the Settlement of Investment Disputes between States and Nationals of Other States art. 42(1), Oct. 14, 1966, 17 U.S.T. 1270, 575 U.N.T.S. 159.

121. Böckstiegel, *supra* note 115, at 580.

122. Roberts, *supra* note 114, at 297–98.

123. Böckstiegel, *supra* note 115, at 581.

124. *Id.* at 581–82.

125. *Id.* at 583. For instance, the host state's consent to arbitration may depend on: (1) whether an “investment” existed; (2) whether the claimant is a national of the alleged home state; or (3) whether the claimant really owns and/or controls the expropriated assets in the host state. *Id.*

126. Böckstiegel, *supra* note 115, at 586–89.

127. David P. Riesenberg, Note, *Fee-Shifting in Investor-State Arbitration: Doctrine and Policy Justifying Application of the English Rule*, 60 DUKE L.J. 977, 986–87 (2011).

scholars that the ISA system has a pro-investor bias and puts states in a disadvantaged position.¹²⁸ Although the pro-investor bias in ISA is difficult to prove or disprove, the perception of such a bias is pervasive.¹²⁹ The perception seems to stem from a series of underlying concerns about the investment treaty regime in general and the ISA system in particular. These include: (1) The belief of some scholars that the current international investment law regime is lopsided, with extremely unequal terms of agreement imposed on developing countries by their stronger BIT partners.¹³⁰ (2) The dissatisfaction of some states with the wide interpretive authority of investment tribunals, which results from the usually vague and open-ended BIT language.¹³¹ (3) General allegations that the outcomes of the ISA proceedings are biased in favor of investors.¹³²

Second, developing states argue that the ICSID system particularly favors investors from the developed world and disadvantages developing states, biased in favor of the Global North.¹³³ Third, and similarly, many also consider the ISA system to be elitist: Arbitrators are usually white, male, and from the developed North.¹³⁴ They are often involved in so-called “revolving doors” with a handful of leading law firms always representing the cases.¹³⁵ Fourth, contrary to theoretical assumptions about arbitration generally, ISA has become very costly and the procedures quite lengthy.¹³⁶ Fifth, because of state involvement in ISA, there is a growing sentiment that proceedings should better account for public interests than commercial arbitration, which emphasizes the private interests of investors.¹³⁷ Sixth, an even more prevalent meme among critics of investment arbitration is that the rising number of investment claims and the considerable costs of the

128. See *ICSID in Crisis*, *supra* note 5.

129. Riesenberger, *supra* note 127, at 987.

130. See Olivia Chung, Note, *The Lopsided International Investment Law Regime and Its Effect on the Future of Investor-State Arbitration*, 47 VA. J. INT'L L. 953, 962 (2007).

131. Alison Giest, Comment, *Interpreting Public Interest Provisions in International Investment Treaties*, 18 CHI. J. INT'L L. 321, 330 (2017).

132. Riesenberger, *supra* note 127, at 988.

133. See generally Brower & Blanchard, *supra* note 6; Franck, *supra* note 6.

134. See Pia Eberhardt & Cecilia Olivet, *Profiting from Injustice: How Law Firms, Arbitrators and Financiers Are Fueling an Investment Arbitration Boom*, TRANSNAT'L INST. & CORP. EUR. OBSERVATORY, at 36 (Nov. 2012), <https://www.tni.org/files/download/profitfrominjustice.pdf>.

135. *Id.*

136. See Matthew Hodgson & Alastair Campbell, *Investment Treaty Arbitration: Cost, Duration and Size of Claims All Show Steady Increase*, INT'L J. COM. & TREATY ARB. NEWS (Dec. 14, 2017), <http://www.allenoverly.com/publications/en-gb/Pages/Investment-Treaty-Arbitration-cost-duration-and-size-of-claims-all-show-steady-increase.aspx>.

137. See Alessandra Arcuri & Francesco Montanaro, *Justice for All: Protecting the Public Interest in Investment Treaties*, 59 B.C. L. REV. 2791, 2804 (2018).

arbitral process will lead to “regulatory chill.”¹³⁸ This refers to the allegation that nation states will not optimally regulate international investors due to fears of having to be the respondent state in investment arbitration.¹³⁹ (7) Finally, given the perception that states’ right to regulate is threatened by ISA, some scholars believe national sovereignty is also diminished.¹⁴⁰

The United Nations Conference on Trade and Development (“UNCTAD”), in its World Investment Report 2015, also summarized the major concerns surrounding the ISA regime. It characterized these concerns as including

that the current mechanism exposes host States to additional legal and financial risks, often unforeseen at point of entering into the IIA and in circumstances beyond clear-cut infringements on private property, without necessarily bringing any benefits in terms of additional FDI flows; that it grants foreign investors more rights as regards dispute settlement than domestic investors; that it can create the risk of a “regulatory chill” on legitimate government policymaking; that it results in inconsistent arbitral awards; and that it is insufficient in terms of ensuring transparency, selecting independent arbitrators, and guaranteeing due process.¹⁴¹

These criticisms have been repeated not only by scholars, but also in various policy documents advocating reform proposals. Some of these reform proposals, such as those launched by the EU, suggest replacing the ISA system with a permanent investment court.¹⁴² Other scholars argue for less radical reforms, making specific modifications to the current ISA system.¹⁴³

For instance, a study concerning the costs of arbitration by Susan Franck, an expert in empirical analysis of international law, points to the importance of providing more clarity, certainty, and transparency

138. Arseni Matveev, *Investor-State Dispute Settlement: The Evolving Balance Between Investor Protection and Sovereignty*, 40 U.W. AUSTL. L. REV. 348, 358 (2015).

139. Vera Korzun, *The Right to Regulate in Investor-State Arbitration: Slicing and Dicing Regulatory Carve-Outs*, 50 VAND. J. TRANSNAT’L L. 355, 383 (2017). Modern IIAs provide foreign investors with relief not only in case of direct expropriations but also for indirect expropriations. Since the most prevalent form of interference with foreign property rights today is regulatory, an apparent conflict has arisen between the regulatory interests of host States and the interests of foreign investors. Ursula Kriebaum, *Regulatory Takings: Balancing the Interests of the Investor and the State*, 8 J. WORLD INV. & TRADE 717, 717 (2007).

140. See Giest, *supra* note 131, at 331.

141. UNCTAD, *World Investment Report 2015*, *supra* note 5, at 128.

142. See Bernardini, *supra* note 9.

143. See Anthea Roberts, Essay, *Incremental, Systemic, and Paradigmatic Reform of Investor-State Arbitration*, 112 AM. J. INT’L L. 410, 415 (2018).

concerning arbitration's costs to the parties.¹⁴⁴ In a subsequent paper on the "ICSID Effect," she points to the importance of providing correct information to the parties involved in investor-state arbitration in order to correct any misperceptions they might hold concerning biases in arbitration, including but not limited to the widely-circulated view that the ICSID system is inherently biased in favor of investors.¹⁴⁵ She also advocates for new modalities of ADR, some even within the context of ICSID.¹⁴⁶ Ultimately, she argues that the international community must show that ICSID can "be a model of fairness, efficiency and justice in the field of international economic dispute resolution."¹⁴⁷

Kovacs also indicates ways to increase the efficiency of international arbitration.¹⁴⁸ He points to a variety of measures, such as choosing the best arbitrators for the dispute by focusing on their skills, ability to manage the process efficiently, and the time that they are willing to devote to arbitration; providing more information to parties about alternative arbitral procedures; and reducing lawyers' moral hazard through the proactive involvement of the parties in the dispute resolution process.¹⁴⁹ One example of lawyers' moral hazard is that, depending on their billing method, they may have incentives to apply dilatory tactics in a bid to delay the procedure for more billable hours.¹⁵⁰ Consequently, Kovacs suggests reforming arbitral pricing models to systemically punish parties who cause delays by forcing them to internalize the costs of their delay.¹⁵¹

Markert also has a variety of suggestions to improve the efficiency of ICSID.¹⁵² For example, he recommends dismissing claims for a clear lack of legal merit earlier in the arbitral process.¹⁵³ He also proposes adopting the UNCITRAL Arbitration Rules, which leave the parties with more flexibility for amendment to achieve their efficiency goals compared to the ICSID system,¹⁵⁴ and resolving smaller cases with a sole arbitrator instead of a

144. Susan D. Franck, *Rationalizing Costs in Investment Treaty Arbitration*, 88 WASH. U. L. REV. 769, 769–70, 852 (2011).

145. Susan D. Franck, *The ICSID Effect? Considering Potential Variations in Arbitration Awards*, 51 VA. J. INT'L L. 825, 909 (2011).

146. Apart from arbitration, ICSID also provides other methods of dispute resolution. These other methods are only sporadically used in this context but could lead to substantial cost and time savings. *Id.* at 912. Franck suggests that ICSID might launch initiatives to develop programs relating to "early neutral evaluation or mediation." To achieve this goal, "ICSID or other professional bodies could offer mediation guidelines or mediation-related protocols to increase ease of access to the processes." *Id.*

147. *Id.* at 914.

148. Kovacs, *supra* note 28, at 171–74.

149. *Id.* at 172–74.

150. *Id.* at 164.

151. *Id.* at 173–74.

152. *See* Markert, *supra* note 107, at 223.

153. *Id.* at 230–36.

154. *Id.* at 237–40.

tribunal.¹⁵⁵ Like Kovacs, Markert suggests that cost-allocation can be an incentive for more efficient party behavior.¹⁵⁶ Equal cost-splitting does not necessarily provide parties with the correct incentives; allocating costs against a party who raises unfounded objections may be better.¹⁵⁷ This also aligns with the suggestions made by Thomas Webster, a preeminent Canadian arbitrator, to discourage unmeritorious claims via an award of costs.¹⁵⁸

With regard to the improvement of the selection procedures of investment arbitrators, Professor Chiara Giorgetti, whose expertise includes international arbitration, puts forward a few concrete recommendations in order to preserve the integrity of the arbitral process and increase the diversity of investment arbitrators.¹⁵⁹ Her first proposal is to change the ICSID rules for challenges made by disputants against investment arbitrators because the existing challenge procedures are deficient both procedurally and substantively.¹⁶⁰ Giorgetti regards having unchallenged arbitrators decide a challenge to a fellow tribunalist, according to the ICSID procedure, as improper because that decision would put the remaining arbitrators in a difficult and uneasy situation, especially since they would be aware that they will probably have to maintain professional relations with the challenged arbitrator.¹⁶¹ She further argues that the ICSID Convention's standard of review in relation to the disqualification of an arbitrator, which is a "manifest lack of the qualities" required to be nominated, is too strict.¹⁶²

These two factors result in a threshold for a successful challenge to the ICSID system that is very hard to meet and ineffective.¹⁶³ As a result, the current ICSID challenge procedure fails to address concerns that might lead to challenge, like party-appointed arbitrators who are excessively inclined to favor their appointing parties.¹⁶⁴

Giorgetti seems to be more sympathetic to the corresponding procedure under the UNCITRAL Arbitration Rules, where the appointing authority, instead of the remaining arbitrators, are usually called to decide upon an arbitrator's challenge.¹⁶⁵ Moreover, she suggests that the International Bar Association's Guidelines on Conflict of Interests in International Arbitration

155. *Id.* at 240.

156. *Id.* at 241.

157. *Id.*

158. Thomas H. Webster, *Efficiency in Investment Arbitration: Recent Decision on Preliminary and Cost Issues*, 25 ARB. INT'L 469 (2009).

159. See Chiara Giorgetti, *Who Decides Who Decides in International Investment Arbitration*, 35 U. PA. J. INT'L L. 431, 474–85 (2013).

160. *Id.* at 474.

161. *Id.* at 477–78.

162. *Id.* at 475.

163. *Id.*

164. *Id.* at 478.

165. *Id.*

should guide investment tribunals operated under both the ICSID and the UNCITRAL rules.¹⁶⁶

To increase the diversity of investment arbitrators, Giorgetti argues that appointing authorities, secretariats, and disputants should all contribute.¹⁶⁷ First, appointing authorities should choose diverse candidates when selecting presiding or co-arbitrators or members of *ad hoc* annulment committees.¹⁶⁸ Second, the Chairman of the ICSID Administrative Council has the chance to directly contribute to the diversity of investment arbitrators since he or she is entitled to select ten of the Panel of Arbitrators.¹⁶⁹ Third, ICSID's Secretary-General should urge ICSID Contracting States to take into consideration diversity when they nominate members to the Panel of Arbitrators.¹⁷⁰ Fourth, the Secretariats of ICSID and the Permanent Court of Arbitration may, via developing a best-practice policy, encourage disputing parties to consider the promotion of diversity when they appoint their arbitrators.¹⁷¹ Last, a related suggestion is that disputing parties may be more sensitive to diversity of investment arbitrators if data on the lack of diversity is publicized.¹⁷²

E. Summary

This overview shows that ISA emerged as a system to resolve investment disputes between investors and states in the 1960s, largely modeled on the example of commercial arbitration. Most investor-state dispute resolution now takes place via ICSID, although investment arbitration also takes place in non-ICSID forums.¹⁷³ States can consent to arbitration in a variety of legal instruments, but the most common and important in practice are IIAs.¹⁷⁴ Even though investment arbitration was modeled on commercial arbitration, the involvement of the state differentiates ISA from commercial arbitration; consequently, that model may not be perfectly fit to deal with disputes between investors and states.¹⁷⁵

166. *Id.* at 480.

167. *Id.* at 482.

168. *Id.*

169. ICSID maintains a Panel of Arbitrators. Each ICSID Contracting State may designate up to four persons to serve on this Panel. In addition, the Chairman of the ICSID Administrative Council may designate up to ten persons. *Id.* at 483.

170. *Id.*

171. *Id.* at 484.

172. *Id.* at 484–85.

173. Felix O. Okpe, *Endangered Element of ICSID Arbitral Practice: Investment Treaty Arbitration, Foreign Direct Investment, and the Promise of Economic Development in Host States*, 13 RICH. J. GLOBAL L. & BUS. 217, 239 (2014).

174. *See, e.g., Case Databases*, ICSID, *supra* note 92.

175. *See* Barnali Choudhury, *Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit*, 41 VAND. J. TRANSNAT'L L. 775, 785–89 (2008).

Because the state is involved, public interest requires more transparency and less autonomy for the parties as compared to commercial arbitration.

The fact that these investment disputes are now largely dealt with via arbitration has led to substantial criticism concerning the way in which the system operates, both in regard to biases against developing states and the high costs and inefficiency of the mechanism.¹⁷⁶ But to what extent are these criticisms substantiated by empirical research? Which reform proposals are the most grounded in the data? This will be addressed in Part V.

IV. EMPIRICS OF ISA GENERALLY

We now turn to the rich empirical literature on ISA. We start by presenting the general findings on how this system is used. In Part V, we will more profoundly analyze to what extent this empirical evidence supports some of the criticisms against the current ISA system.

Here, we first stress the importance of empirical evidence (Section A) and then analyze the evidence on arbitration filings (Section B). Next, we assess the claims made in ISA, as well as the awards rendered by investment tribunals (Section C). The final Section (Section D) summarizes the findings of this Part.

A. *Importance and Limits of Empirical Evidence*

From the discussion so far, it is clear that the theoretical Law and Economics literature takes a relatively positive view of arbitration; at the least, the literature understands why parties may have a strong preference for arbitration. It can lead to speedy and cheap dispute resolution by arbitrators who have large expertise in specialized domains. Arbitration can also be kept secret, which may have advantages for business parties. But these advantages, present in international commercial arbitration, may not transfer to investor-state arbitration where public interests are involved. At the same time, the criticisms of arbitration offered by the theoretical Law and Economics literature—particularly with regard to arbitration’s lack of transparency and the risk that it consequently may not generate the positive externalities usually associated with adjudication—*do* appear to apply to investor-state arbitration.

At this point, it is important to incorporate empirical data into the analysis of ISA as a whole. Academic Law and Economics ideas of how investor-state arbitration functions are not necessarily supported by the realities of the mechanism. In this regard, empirical studies are capable of, at least theoretically, offering a more solid foundation for the evaluation of the functioning of ISA.¹⁷⁷

176. See *supra* Part III.D.

177. Catherine Rogers, *The Politics of International Investment Arbitrators*, 12 SANTA CLARA J. INT’L L 223, 233 (2014).

However, it is worth noting that empirical studies are not a panacea. Catherine Rogers, a scholar of international arbitration and professional ethics, cautions of the risk that empirical evidence will be misused in the highly politicized field of investment arbitration.¹⁷⁸ Thus, despite recognizing the value of empirical studies for analyzing investment arbitration, she suggests that due care should be accorded in the process of reading, interpreting, and adopting those empirics.¹⁷⁹

In a critique of Rogers's article, Giorgetti echoed the ideas therein by arguing that empirical studies are of constructive significance in illuminating the legitimacy crisis facing investment arbitration, but that empirics have intrinsic weaknesses that should give scholars concern.¹⁸⁰ First, the most essential variable—the “correct” legal outcome in a particular case—is often overlooked by the data used in empirical studies of ISA.¹⁸¹ Second, empirical reviews of international arbitration tend to easily confuse a finding of correlation with a finding of causation.¹⁸² Third, empirical researchers may misuse data if they predetermine the outcomes of the questions asked.¹⁸³ Fourth, results can be over-simplified because empirical researchers may be tempted to emphasize the outcomes of cases while overlooking the arbitrators' content analysis.¹⁸⁴ Still, where done properly (when “a question that can only have a yes/no answer is posited and objective criteria are evaluated”), Giorgetti concludes that these studies can be useful.¹⁸⁵

As a scholar who focuses on the interdisciplinary research of international courts and tribunals, Daniel Behn expresses a concern that empirical research on ISA is out-of-date, given the upsurge of arbitral decisions in recent years.¹⁸⁶ Behn, in his paper, highlights the problems in relation to evidence-based research in ISA: Though the transparency and public availability of investment awards have improved, they continue to pose challenges for empirical research in this field.¹⁸⁷ While much empirical

178. *Id.*

179. *Id.*

180. Chiara Giorgetti, *Is the Truth in the Eyes of the Beholder? The Perils and Benefits of Empirical Research in International Investment Arbitration*, 12 SANTA CLARA J. INT'L L. 263, 266–69 (2013).

181. Giorgetti suggests that empirical research in investment arbitration is often based on the assumption that “it is somehow possible to control for the correct legal outcome.” However, “who decides if the correct judicial decision was taken” remains unclear. *Id.* at 267.

182. *Id.* at 267–68.

183. According to Giorgetti, “empirical data in international arbitration are often embedded by ideology and policy references.” Consequently, researchers' readings and interpretations of empirical data are likely to be dictated by their ideology. *Id.* at 268.

184. *See id.*

185. *Id.* at 269.

186. Daniel Behn, *Legitimacy, Evolution, and Growth in Investment Treaty Arbitration: Empirically Evaluating the State-of-the-Art*, 46 GEO. J. INT'L L. 363, 414 (2014).

187. *Id.* at 413.

research remains to be done, Behn raises the concern that few scholars currently conducting empirically-based research are interested in evaluating investment arbitration.¹⁸⁸

Some exceptions do exist: The research project PluriCourts at Oslo University aspires to conduct a long-term empirical study on investment arbitration.¹⁸⁹ Likewise, Professor Sergio Puig is attempting to raise awareness among scholars of the importance of conducting empirical research on ISA.¹⁹⁰ By deconstructing ICSID's goals, he hopes to enable interested empirical scholars to cast the legitimacy debate of ICSID "as one more amenable to empirical evaluations."¹⁹¹ As discussed below, we hope that this paper will inspire more ISA-focused empirical research.

B. Arbitration Filing

Various studies have addressed the basic questions of who is using ISA, against whom, for what particular reasons, and in what types of cases.¹⁹² Although this data does not directly address some of the criticisms of the ISA system, it is relevant to the extent it shows, for example, that more plaintiffs come from the developed North and more defendants from the Global South. Although that data alone does not conclusively demonstrate bias in the system, it could shed light on why some states have the impression of being systematically attacked via the ISA system.

Behn studied 147 fully and partially solved ISA cases from September 2011 to September 2014, assessing whether the ISA regime has evolved and the extent to which empirical evidence supports the legitimacy critiques lodged against ISA.¹⁹³ Behn argues that, although the cases are somewhat diverse in terms of the types of cases being brought, the limited degree of diversity could raise questions of legitimacy.¹⁹⁴ During the period Behn studied, the ISA caseload was dominated by particular economic sectors, including extractive industries and electric power.¹⁹⁵ A large number of cases were brought against less developed countries and regions, notably in Latin America, Eastern Europe and Central Asia.¹⁹⁶ By contrast, plaintiffs were largely corporations from developed countries, especially from

188. *Id.* at 414–15.

189. *Id.*

190. Sergio Puig, *Recasting ICSID's Legitimacy Debate Towards a Goal-Based Empirical Agenda*, 36 *FORDHAM INT'L L.J.* 465, 502 (2013).

191. *Id.*

192. *See, e.g.*, Behn, *supra* note 186, at 390–413; Sergio Puig & Anton Strezhnev, *The David Effect and ISDS*, 28 *EUR. J. INT'L L.* 731 (2017).

193. Behn, *supra* note 186, at 363.

194. *Id.* at 412–13.

195. *Id.* at 390.

196. *Id.* at 396–97.

Western Europe and North America.¹⁹⁷ In total, 76% percent of all cases in the dataset involved claimants from developed states litigating against emerging economies or developing states.¹⁹⁸ Behn argues that diversification of claims away from this pattern—achieved by reaching out to small-scale investors and investors from developing states on the claimant side, and by integrating developed states and geographically diverse states on the respondent side—could benefit ISA legitimacy.¹⁹⁹

In another paper purporting to improve the existing literature,²⁰⁰ Rachel Wellhausen, an associate professor of government whose research interests include international investment law, conducted an empirical study on ISA cases.²⁰¹ By exploring data on ISA cases from 1990 to 2014, she documents the recent trends of ISA practice through a political science lens, as the questions discussed there are believed to have political implications.²⁰² She finds that, while a large number of cases are focused on industries with “immobile assets” such as utilities, oil, and gas, investors from the services and manufacturing sectors also filed a wealth of arbitration cases against host states.²⁰³ Her study shows that though investors from as many as seventy-three home states have filed ISA claims, 87% of cases involved investors from just fifteen states.²⁰⁴ Many of those investors were from developed states.²⁰⁵

The study also paints a picture of respondent states involved in ISA cases. Two Latin American countries, Argentina and Venezuela, topped the ranking.²⁰⁶ Other frequently sued countries include the Czech Republic, Mexico, Ecuador, Canada, Egypt, Poland, Ukraine and the United States.²⁰⁷ Notably, Wellhausen predicts that as more IIAs are signed between developed countries Northern countries will be increasingly targeted by complaints.²⁰⁸

197. *Id.* at 394–95.

198. *Id.* at 404.

199. *Id.* at 412–13.

200. She specifically mentions the intention to update Susan Franck’s *Empirically Evaluating Claims About Investment Treaty Arbitration* and to complement Thomas Schultz and Cedric Dupont’s *Investment Arbitration: Promoting the Rule of Law or Over-Empowering Investors? A Quantitative Empirical Study*. Wellhausen, *supra* note 1, at 117.

201. *See id.*

202. *Id.* at 119–120.

203. *Id.* at 123.

204. *See id.* at 124–25.

205. *Id.* at 125. U.S. investors topped that ranking in filing investment arbitrations, followed by Dutch investors. *Id.* Investors from other developed countries have also filed many arbitrations. These countries include the UK, France, Germany, Canada, Spain, Italy, Belgium, Luxembourg, Switzerland, Cyprus, Greece, Austria, and Russia. *Id.* at 124–25.

206. *Id.* at 126.

207. *Id.*

208. *See id.* at 128. Consider, for instance, the EU-Canada Comprehensive Economic and Trade Agreement (“CETA”).

Professors Schultz and Dupont also conducted quantitative empirical research on ISA cases, examining over 500 cases between 1972 and 2010.²⁰⁹ Their study sought not only to develop a factual perspective on ISA, but also to evaluate three criticisms through data analysis.²¹⁰ The first criticism of ISA they examine is that the process is functionally neo-colonialism.²¹¹ Their data shows that until the mid-to-late 1990s, investment arbitration mostly followed the pattern of “rich vs poor” and “developed vs developing,” seemingly confirming arguments about neo-colonialism in that stretch of time.²¹² However, since the mid-to-late 1990s, investors from developed states have started to sue developed host states with ever higher frequency, even exceeding the number of “developed vs developing” cases.²¹³ Based on this comparison, Schultz and Dupont conclude that the most recent data contradicts the common argument that ISA is a form of neo-colonization.²¹⁴

The second perception of ISA their study examines is whether ISA substitutes for “the rule of law in the host state,” or, in other words, whether it replaces “dysfunctional courts” and “unreliable countries.”²¹⁵ By reference to the Polity IV index—as a proxy for states’ level of democratic development—and states’ ICRG Law and Order scores, they find that before the mid-to-late 1990s the average annual polity scores and average annual law and order scores of respondent states were quite low, offering some support for the idea that investment arbitration is a substitution for lack of rule of law in certain countries.²¹⁶ However, this idea is not as plausible when data derived since the mid-1990s are considered, as countries with a higher democratic level and better respect for the rule of law were sued at international tribunals with even higher frequency.²¹⁷ The paper also observes that as a consequence of the imbalanced distribution of claims,²¹⁸ it remains plausible that certain arbitration regimes can substitute for domestic rule of law.²¹⁹

In addition, Professors Van Aaken and Broude have demonstrated that ISA has a heavy bias toward the nominating party (the investor) in terms of cost allocation.²²⁰ Correspondingly, they argue that arbitrators may have a

209. Schultz & Dupont, *supra* note 12, at 1149.

210. *Id.*

211. *Id.* at 1151.

212. *Id.* at 1156.

213. *Id.*

214. *Id.* at 1157.

215. *Id.* at 1160.

216. *Id.* at 1161–62.

217. *Id.* at 1162.

218. They find that there is a general tendency for some claims to cluster around those countries with either the best or the worst level of democracy and the rule of law. *Id.*

219. *Id.* at 1160–62.

220. Van Aaken & Broude, *supra* note 19, at 17–18.

structural incentive to grant jurisdiction, in order to guarantee a continued stream of income from the case.²²¹ This claim is supported by an earlier empirical study by Kathleen McArthur (a legal counselor) and Pablo Ormachea (an in-house counsel) on the factors that influence jurisdictional rulings issued by ICSID tribunals.²²² In the 79 cases this study covered, ICSID tribunals decided jurisdictional issues in favor of investors (*i.e.* granted jurisdiction) nearly 85 percent of the time.²²³ That research therefore suggests that arbitrators certainly have their own interests and decide accordingly, in an attempt to maximize income.

C. Claims and Awards

Another window into the operation of ISA is comparing the compensation claimed by foreign investors and the actual awards of investment tribunals, which provide important information about the size and significance of investment arbitration cases. This dimension is highly amenable to empirical quantitative study, and it has unsurprisingly attracted substantial scholarship from those that are keen to sketch out ISA empirically.

Wellhausen, for instance, examined the monetary expectations of foreign investors (in terms of the claims they asserted) and the pecuniary outcomes of arbitral proceedings (in terms of the awards parties received), as well as the contrasts between the two.²²⁴ Data on compensation claims can be difficult to find, but, in the 325 cases she examined, both from court documents and news sources, claims range from tens of thousands to billions of U.S. dollars.²²⁵ The average claim demanded by investors was \$884 million USD, though this was driven largely by the dozens of investment arbitrations in which the claimants demanded one billion U.S. dollars.²²⁶

By contrast, the compensation awarded by investment tribunals in 119 publicly available cases averaged \$508 million USD, inflated once again by a small number of large awards. In the eighty-six instances in which (1) the investor won and (2) both the compensation sought and the compensation awarded is available, Wellhausen found that in half of all rulings investors won less than 33% of their original claims. The average award was just 40%

221. *Id.* at 17.

222. See Kathleen S. McArthur & Pablo A. Ormachea, *International Investor-State Arbitration: An Empirical Analysis of ICSID Decisions on Jurisdiction*, 28 REV. LITIG. 559 (2009).

223. *Id.* at 568–71.

224. Wellhausen, *supra* note 1, at 132–34.

225. *Id.* at 132–33.

226. *Id.* at 133.

of the original claim. Notably, there are only six instances in which the investor won the full amount of the original claim (or more).²²⁷

Matthew Hodgson and Alastair Campbell, both legal counselors with specialization in international arbitration, have also produced a number of influential empirical studies on damages and costs in arbitration that largely corroborate Wellhausen's findings. Hodgson published his first empirical study on damages and costs in investment treaty arbitration in 2014, covering some 221 cases for which an award or decision was available from the 1980s through the end of 2012.²²⁸ Hodgson and Campbell published an update in 2017, gathering data on an additional 140 awards published since the end of 2012.²²⁹ The contrast between the two datasets not only illuminates the specific operation of ISA, but demonstrates the evolution of the dispute settlement regime in that relatively short stretch of time. They show that the mean amount claimed by investors has risen from \$491 million USD in the first study to around \$1.1 billion USD in the second.²³⁰ The second study also reveals a significant rise in the mean amount of compensation awarded to successful claimants.²³¹ It skyrocketed from \$76.3 million USD in 2012 to \$1.08 billion USD from 2013 to 2017.²³² The second study also highlights that the mean amount awarded continues to decline relative to the mean amount claimed (from 40% to 32%), indicating that the claimants continue to overvalue either their investments or the damage they incurred.²³³ Interestingly, the mean amount pursued in claims that are ultimately successful is manifestly lower than that in failed claims.²³⁴ Noting this discrepancy, Hodgson and Campbell argue that "flawed claims continue to drive up the average amount claimed."²³⁵

Separately, a study by Gus Van Harten, a professor of law with expertise in international investment law, and Pavel Malysheusk, a corporate lawyer, examined who receives monetary awards from investment

227. *Id.* at 132–33.

228. Matthew Hodgson, *Counting the Costs of Investment Treaty Arbitration*, INT'L J. COM. & TREATY ARB. NEWS (Mar. 24, 2014), http://www.allenoverly.com/SiteCollectionDocuments/Counting_the_costs_of_investment_treaty.pdf.

229. Matthew Hodgson & Alastair Campbell, *Damages and Costs in Investment Treaty Arbitration Revisited*, INT'L J. COM. & TREATY ARB. NEWS (Dec. 14, 2017), http://www.allenoverly.com/SiteCollectionDocuments/14-12-17_Damages_and_costs_in_investment_treaty_arbitration_revisited_.pdf.

230. *Id.*

231. *Id.*

232. *Id.* However, the researchers caution that large claims, such as those in the *Yukos* case, likely inflate the overall numbers and suggest that the discrepancy between the median, rather than the mean, amounts in the two surveys could serve better to grasp the increase on the size of investment awards. *See id.* Indeed, the median amount accorded in the first study is \$10.7 million USD, contrasting sharply with \$40 million USD in the second study. *Id.*

233. *Id.*

234. *Id.*

235. *Id.*

tribunals and who benefits the most from financial transfers due to ISA.²³⁶ One of the questions they addressed is whether the ISA system only benefits multinational enterprises and wealthy individuals or also small and medium-sized enterprises.²³⁷ They collected data on known ISA cases (with a focus on cases resulting in monetary awards for investors) and then linked the amounts of awarded compensation to the size and wealth of the claimants. Their research demonstrates that, in financial terms, the overwhelming beneficiaries of ISA are large companies (those with annual revenue of over \$1 billion USD), extra-large companies (those with annual revenue of over \$10 billion USD), and individuals with a net worth of over \$100 million USD.²³⁸ Ninety-four and a half percent of the aggregate compensation (93.5% if pre-award interest is included) went to these ultra-rich companies and individuals,²³⁹ while the remaining 5.5% (or 6.5%) was shared by companies with annual revenue of less than \$1 billion USD, unknown companies, and not-so-wealthy individuals.²⁴⁰

An incidental finding of this research is that extra-large companies appeared to have a much higher success rate (82.9% over 41 cases) than other claimants (57.9% over 121 cases) at the merits stage.²⁴¹ Despite the caveat that “[o]ne should approach all of the numbers presented here as approximate and keep in mind that variations in the experiences of different actors may be coincidental,”²⁴² this disparity in success rates between extra-large companies and others points to the possibility that the economic power of the claimant may sway the ultimate outcome of investor-state proceedings. How that correlation exactly works could not be examined in the study.²⁴³ One could speculate, however, that economically powerful claimants may be able to spend more to research their claims, secure excellent counsel, and select well-paid arbitrators who might be favorable to their case.

D. Summary

Already, this overview of empirical studies provides a few interesting insights for the debate over ISA. One important point is that in most investor-state arbitration cases investors from developed countries (the North) bring cases against states in the developing world (the South). However, the claimant-respondent pattern has seen changes in more recent years with more developed countries being targeted by foreign investors as

236. See Van Harten & Malysheuski, *supra* note 12, at 1–18.

237. *Id.* at 1.

238. *Id.*

239. *Id.*

240. *Id.* at 1–2.

241. *Id.* at 2, 9.

242. *Id.* at 2.

243. *Id.* at 1–18.

well. The empirical evidence also shows that investors' overall claim amounts are increasing, which understandably alarms developing countries with limited budgets.²⁴⁴ Though claim amounts are increasing, the research suggests that investors may be overestimating either the value of their own investments or of the losses they have suffered, as the ratio of the amounts awarded compared to the amounts claimed is decreasing.²⁴⁵

Another interesting conclusion is the relative success of wealthy plaintiffs.²⁴⁶ The economic power of the claimant seems to be a significant factor as far as the amount of compensation awarded and the success rate of a claim are concerned.²⁴⁷ Yet, so far there has been no empirical research examining a possible relationship between the level of the investments and the increase in the amounts claimed, which might correlate an increase in the amounts claimed in ISA to the investors' level of foreign investment.

Although these numbers explain the negative sentiments in developing countries against the ISA system, they do not provide objective and clear evidence of a bias against those countries in the way the cases are decided. That requires a further analysis of some other empirical studies conducted by scholars.

V. EMPIRICS SUPPORTING THE CRITICISM OF ISA

As indicated in this article's introduction, the question arises whether the investment arbitration system as it currently functions is as neutral as its theorists expect. Countries in the developing world (like India and some Latin American countries) look with suspicion at the international investment arbitration system.²⁴⁸ Some of these countries claim that the system is dominated by the Western world and does not provide the neutrality and impartiality which it is supposed to have.²⁴⁹ Moreover, the reasons that provide theoretical support for arbitration—that it resolves disputes more cheaply and quickly than traditional litigation—do not always apply to the ISA system due to the excessive costs involved.²⁵⁰ Consequently, critics argue that ISA may no longer generate relative advantages over national litigation.²⁵¹

244. Hodgson & Campbell, *supra* note 229; Sonia E. Rolland, *The Return of State Remedies in Investor-State Dispute Settlement: Trends in Developing Countries*, 49 LOY. U. CHI. L.J. 387, 390 (2017).

245. *Id.*

246. Van Harten & Malysheuski, *supra* note 12, at 2, 9.

247. *Id.* at 1–2, 9.

248. Trakman, *supra* note 7, at 604–05.

249. *Id.*

250. Jonathan Klett, Comment, *National Interest vs. Foreign Investment—Protecting Parties Through ISDS*, 25 TUL. J. INT'L & COMP. L. 213, 225 (2016).

251. See *supra* Part III.D for a summary of the criticisms.

In this section, we examine each major criticism of the ISA system in turn. The first question that we consider is whether the ISA system is biased in favor of investors and against states (Section A). That is related to another criticism—that decision-making in ISA is restricted to a closed circle of particular elites, mostly dominated by older, white males (Section B). The question also arises whether the traditional assumption that arbitration is fast, good, and cheap applies in practice as far as investor-state arbitration is concerned (Section C). Finally, we evaluate the extent to which ISA sufficiently incorporates the public interest (D).

A. *Bias Against States?*

As mentioned, some developing countries feel that they are the “victims” of the ISA system and that decisions are systematically made against them.²⁵² This sentiment may be supported by the fact that most ISA cases have historically been (perhaps not surprisingly) filed by investors from the North against states in the South.²⁵³ But as previously indicated, the mere fact that in many cases states from the South are defendants does not necessarily provide any evidence of a bias against the states as far as the contents of the award are concerned.

The issue of whether there is such a bias has been analyzed in detail in a variety of studies.²⁵⁴ Franck examined whether the results of investor-state arbitrations taking place within ICSID are substantially different from the outcomes in non-ICSID arbitration cases.²⁵⁵ Her study was done in response to the claim that the ICSID system is biased.²⁵⁶ Franck summarizes the criticisms on ICSID, including not only the lack of both transparency in decision-making and the possibility of appeal,²⁵⁷ but also an inconsistency of outcomes.²⁵⁸ Governments of some developing states argue that ICSID arbitration has a strong pro-investor bias, leading some states to withdraw from ICSID arbitration.²⁵⁹ Based on a detailed empirical study, however, Franck concludes that there is no difference in outcomes between ICSID

252. Franck, *supra* note 6, at 436–37.

253. See *supra* Part IV.B. It is not surprising in the sense that much foreign direct investment also goes in that direction (from the North to the South) and that investors from the North may indeed see ISA as an alternative for the court system in host countries that they may not always trust.

254. See, e.g., Julian Donaubauer, Eric Neumayer & Peter Nunnenkamp, *Winning or Losing in Investor-To-State Dispute Resolution: The Role of Arbitrator Bias and Experience*, 26 REV. INT’L ECON. 892 (2018).

255. See Franck, *supra* note 145.

256. *Id.* at 829.

257. *Id.* at 841.

258. *Id.* at 843.

259. *Id.* at 844, 846–47.

and non-ICSID arbitrations.²⁶⁰ She holds that the idea of biased decision-making by ICSID arbitration is largely based on misperceptions.²⁶¹

In contrast, the findings of a recent empirical study by Behn, Tarald Berge (a scholar with research interest in international investment law), and Malcolm Langford (a professor of law with expertise in international investment law) lend more ammunition to the proposition that the ISA system is biased against developing states.²⁶² Using a different methodology than Franck, these three scholars find that controlling for broad measures of good governance does not seem to temper the correlation between economic level and arbitration outcome.²⁶³ According to these scholars, Franck's conflation theory (that arbitration outcomes reflect differences in governance) is not plausible unless it accounts for economic development and certain aspects of governance like the presence of impartial bureaucracies and property right protection.²⁶⁴ However, the research by the three scholars maintains that a higher level of economic development on the respondent side is associated with a lower success rate on the claimant side, lending some credibility to the hypothesis that the outcome for respondent states is largely contingent on their economic power, not their governance level.²⁶⁵

There are, furthermore, other studies that warrant introduction in order to provide a more balanced picture about the claimed bias against states. Schultz and Dupont examine the extent to which the dispute settlement regime contributes to the international rule of law.²⁶⁶ The researchers conclude that investment arbitration does not contribute as much to the international rule of law as its supporters might hope.²⁶⁷ Their data shows that "the haves (the host states with a higher development status) stand a higher chance of successfully defending off claims than the have-nots (the weaker parties with a lower development status)."²⁶⁸ More precisely, outcome data from 1972–2010 show that low income countries won 50% of

260. *Id.* at 897–98.

261. *Id.* at 909. The studies by Franck and her colleagues are said to put forward an interesting theoretical argument that the impression of the relationship between arbitration outcomes and respondent states' economic development may have conflated the concerns of economic development and the concerns of respondent states' level of good governance. Daniel Behn et al., *Poor States or Poor Governance? Explaining Outcomes in Investment Treaty Arbitration*, 38 NW. J. INT'L L. & BUS. 333, 336–337 (2018).

262. Behn et al., *supra* note 261, at 381 (2018).

263. *Id.* at 337–38.

264. *Id.* at 380.

265. *Id.* at 380–81.

266. The meaning of rule of law employed in that research is "formal legality." "Formal legality requires, for instance, that the rules be formulated in general terms, that they be accessible and understandable by their addressees, and that they be applied coherently, consistently, competently, and impartially." Schultz & Dupont, *supra* note 12, at 1163–64.

267. *Id.* at 1167.

268. *Id.* at 1166.

cases against investors while high income countries had a higher win rate of 69%.²⁶⁹ This difference in success rate grew in the 1998–2010 boom in investment arbitration; developed countries won 46% of cases during that time, and developing countries won just 27%.²⁷⁰ It is the researchers' opinion that "[w]hen a dispute settlement system favors the stronger parties to such an extent, the international rule of law is pursued less than fully."²⁷¹

The empirical study by Wellhausen mentioned above also contributes to our knowledge of the outcomes out of ISA cases from 1990 to 2014. She found that across her dataset, respondent states won 38% of the time and settled 33% of the time.²⁷² When it comes to cases where U.S. investors were the claimants, respondent states won 36% of the time and settled 36% of the time.²⁷³ These results seem to be almost the same for ISA cases involving British investors (34% and 34%, respectively). Thus, one can safely argue that prominent ISA participants, such as U.S. and British investors, are not systematically prevailing over respondent states.²⁷⁴ Her research also points out that states in the Middle East, North Africa, and Europe (including the former Soviet Union) have a *higher* rate of success in investment arbitration than the aggregate state win rate of 38%.²⁷⁵ While the average success rate for Asian countries is around the mean, American countries and Sub-Saharan African countries tend to suffer from a lower probability of winning a case.²⁷⁶ Of the thirty-one ISA cases against OECD states that concluded by the end of 2014, respondent OECD states won 55% of the time.²⁷⁷ Thus, Wellhausen's study also provides support for the claim that developed countries seem to have fared better than their developing counterparts in ISA.

Additionally, through statistical analysis of the outcomes of ISA cases between September 2011 and September 2014, Behn found that the data does not seem to show a pro-investor bias among tribunals because less than half of investors' claims were successful.²⁷⁸ In fact, measured against the ICSID caseload, the data show an increase in cases where tribunals denied jurisdiction,²⁷⁹ in contrast to the expectations of the theoretical literature. Behn puts forward two possible explanations for this phenomenon. One is that the tribunals are increasing their scrutiny over the threshold issues that

269. *Id.*

270. *Id.*

271. *Id.* at 1165–1167.

272. Wellhausen, *supra* note 1, at 130.

273. *Id.*

274. *Id.*

275. *Id.*

276. *Id.*

277. *Id.* at 129–131.

278. Behn, *supra* note 186, at 373.

279. *Id.*

allow for jurisdiction over a claim; the other is that more unfounded claims are being screened out at the preliminary stage by investment tribunals.²⁸⁰

Another example of interesting empirical research was conducted by Van Harten, who validated the hypothesis that systemic bias exists in the resolution of contested jurisdictional issues in investment treaty law by reviewing a database of 115 ISA cases.²⁸¹ This research is unique because it does not track the resolution of all issues that distribute interests between the disputing parties, but rather focuses on specific issues related to the jurisdiction of the tribunals, such as whether investors are “corporate persons” or “natural persons” and the scope of covered “investments.”²⁸² Thus, unlike Behn’s research, which focuses on the outcomes of ISA cases, Van Harten’s research covers the content analysis of jurisdictional rulings. Different benchmarks for evaluation are very likely to lead to different conclusions even if the dataset is identical, and it usually is not. Van Harten concludes that, in the context of these jurisdictional issues, arbitrators seem to favor the stance of investors over that of sovereign states, *i.e.*, they favor those stances that enable them to arbitrate.²⁸³ In other words, this research provides “tentative support for expectations of systemic bias arising from the interests of arbitrators in light of the system’s asymmetrical claims structure and the absence of conventional markers of judicial independence.”²⁸⁴

B. *Elites?*

Arbitration practitioners, including arbitrators, legal counsel, experts, and tribunal secretaries, are of crucial importance for the legitimacy of the investor-state arbitration regime. Considering the fact that the perceived bias within national courts is one of the factors that prompted the establishment of this regime,²⁸⁵ one can well understand why any irregularity would raise grave concerns for the disputing parties. The impartiality and independence of ISA arbitrators, as the adjudicators in this asymmetrical decision-making system, have faced doubt for a long time.

Eberhardt and Olivet believe that investment arbitrators form a small and cohesive community. As such, they “have a tight grip on the investment arbitration system and can exert immense influence over it.”²⁸⁶ Their research finds that arbitrators from Western Europe and North America take

280. *Id.*

281. See Gus Van Harten, *Arbitrator Behaviour in Asymmetrical Adjudication: An Empirical Study of Investment Treaty Arbitration*, 50 OSGOODE HALL L.J. 211, 252 (2012).

282. See *Id.* at 211, 233–34.

283. *Id.* at 252.

284. *Id.*

285. See, e.g., Alexandre Gauthier, *supra* note 84, at 1–2.

286. Eberhardt & Olivet, *supra* note 134, at 36.

charge of 69% of cases handled at the ICSID.²⁸⁷ Among arbitrators who have adjudicated more than ten cases, the proportion of arbitrators from the two regions jumps to 83%.²⁸⁸ Of the arbitrators considered in their research, only 4% are women, with just two individuals accounting for three-quarters of cases with female arbitrators.²⁸⁹ This data points to an apparent lack of diversity among arbitrators in terms of nationality and gender.

The freshly published World Investment Report 2018 also expresses concern of the same kind.²⁹⁰ Out of the thirteen arbitrators appointed in more than thirty cases considered by the report, all of them but one is a citizen of a European or North American country, and eleven of them are men.²⁹¹ Notably, the only two female arbitrators on the list are among the three most-appointed arbitrators globally.²⁹²

Eberhardt and Olivet, meanwhile, assert that arbitrators have close links with the corporate world and share the view of businesses that protecting private interests is of extraordinary importance.²⁹³ Contrary to Jan Paulsson's dismissal of the existence of an "elite" group of arbitrators,²⁹⁴ Eberhardt and Olivet confirm that there is a group of fifteen elite arbitrators, of which Paulsson is a high-ranking member.²⁹⁵ This group of elites has considerable overlap with the World Investment Report's 2018 list of thirteen arbitrators most frequently appointed to investment tribunals.²⁹⁶ Eberhardt and Olivet's statistical work finds that together the fifteen have decided 55% of the 450 investment-treaty disputes they examined, 64% of 123 treaty disputes of at least \$100 million USD (value of investor claims), and 75% of sixteen treaty disputes of at least \$4 billion USD.²⁹⁷ They claim that all the members of the elite fifteen have sat at least once, and many

287. *Id.*

288. *Id.*

289. *Id.*

290. See UNCTAD, *World Investment Report 2018: Investment and New Industrial Policies* 95 (June 6, 2018), http://unctad.org/en/PublicationsLibrary/wir2018_en.

291. *Id.*

292. *Id.*

293. Eberhardt & Olivet, *supra* note 134, at 36.

294. PIA EBERHARDT & CECILIA OLIVET, PROFITING FROM INJUSTICE: HOW LAW FIRMS, ARBITRATORS AND FINANCIERS ARE FUELING AN INVESTMENT ARBITRATION BOOM 38 (2012) (citing David Samuels, *Roundtable: The Under 45s versus the Heavyweights*, GLOBAL ARB. REV., Nov. 1, 2006).

295. The rest on the list include: Brigitte Stern (France), Charles Brower (U.S.), Francisco Orrego Vicuña (Chile), Marc Lalonde (Canada), L. Yves Fortier (Canada), Gabrielle Kaufmann-Kohler (Switzerland), Albert Jan van den Berg (Netherlands), Karl-Heinz Böckstiegel (Germany), Bernard Hanotiau (Belgium), Stephen M. Schwebel (U.S.), Henri Alvarez (Canada), Emmanuel Galliard (France), William W. Park (U.S.) and Daniel Price (U.S.). Eberhardt & Olivet, *supra* note 134, at 38–41.

296. UNCTAD, *World Investment Report 2018*, *supra* note 290.

297. Eberhardt & Olivet, *supra* note 134, at 38.

more than twice, with another elite arbitrator on the same panel.²⁹⁸ In their opinion, these data demonstrate the influence of non-legal factors on the outcomes of investment arbitration, such as arbitrators' policy preferences, and their social and personal backgrounds.²⁹⁹

The frequency with which elite arbitrators regularly serve on the same tribunals makes the criticism of "revolving doors" in the ISA community more worrisome. The "revolving door" concept (also known as "double-hatting") refers to the practice of arbitration practitioners simultaneously holding a variety of roles in investment arbitration practice, including arbitrator, legal counsel, expert witness, and tribunal secretary. This practice is deemed as an encroachment on the impartiality and independence of arbitrators and even a fundamental challenge to the whole regime of investment arbitration more broadly.³⁰⁰ Eberhardt and Olivet found that there are a significant number of cases in which one of the elite fifteen sits on an arbitral panel, while another member of that group serves as legal counsel for either the investor or the state.³⁰¹ Some cases have even seen the concurrent appearance of up to four members of the elite fifteen.³⁰²

An ambitious research paper by Langford, Behn, and Lie (a scholar with research interest in ISA) purports to have conducted the first-ever comprehensive empirical analysis of the individuals making up the entire investment arbitration community, with a dataset covering 1,039 investment arbitration cases (including ICSID annulment proceedings) and 3,910 arbitration practitioners.³⁰³ The empirical study reveals that the revolving door continues to exist in investment arbitration and that the double-hatting accusation can be *partly* substantiated.³⁰⁴ This is because the double-hatting is not a widespread or rampant practice in investment arbitration, but it is common among a core group of influential ISA practitioners.³⁰⁵ Despite the small scale of the revolving door phenomenon, the researchers argue that it raises alarming concerns about bias, impartiality, independence, and legitimacy in the ISA regime.³⁰⁶ The mere existence of this phenomenon calls for reforms that address these concerns.³⁰⁷

These narratives confirm the impression that the ISA community is characterized by a severe lack of diversity. On the other hand, Kovacs and Fawke examined seven parameters for diversity among arbitrators and

298. *Id.* at 42.

299. *Id.*

300. *Id.* at 43.

301. *Id.*

302. *Id.*

303. Malcolm Langford et al., *The Revolving Door in International Investment Arbitration*, 20 J. INT'L ECON. L. 301, 301 (2017).

304. *Id.* at 328.

305. *Id.*

306. *Id.*

307. *Id.*

found a more mixed picture.³⁰⁸ While ISA may not be diverse in terms of gender and nationality, ISA displays impressive diversity in such areas as professional experience, legal tradition, language, and public international law expertise.³⁰⁹ Yet the field's underrepresentation in some forms of diversity—like the involvement of arbitrators from low-income countries—precisely explains continuing suspicions against ISA.

C. *Fast, Good, Cheap?*

One of the purported advantages of arbitration is that arbitration is faster, better, and cheaper than adjudication in national courts.³¹⁰ The question arises whether the ISA system meets those goals in practice and whether it is possible to meet all three goals at the same time.

Kirby compares the objectives of international arbitration to a sign at a U.S. drycleaner that says, “Fast. Good. Cheap. Pick two.”³¹¹ Parties seeking arbitration face the same dilemma: Ideally, parties want arbitration to be fast, good, and cheap, but it may be impossible to realize this “iron triangle.”³¹² In practice, there are tradeoffs between the speed of decision-making, its quality, and the costs involved, and it may ultimately be impossible to reach those three objectives at the same time.

The empirical research seems to confirm these doubts. Beginning with the first purported advantage—speed—many argue that the increasing size and complexity of investor claims have driven an increase in the length of proceedings. Compared to the mean investment arbitration length of 3.7 years recorded in Hodgson's first study, his second study—with Campbell—found that the mean length of arbitral proceedings was 4.3 years.³¹³ However, on the basis of the median length of arbitral proceedings, the difference is negligible: from 3.6 years to 3.7 years.³¹⁴ Taking all the

308. The seven aspects involved in Kovacs and Fawke's empirical study are “(i) gender, (ii) nationality, (iii) legal tradition . . . (iv) university, (v) professional experience, (vi) languages, and (vii) public international law expertise.” Robert Kovacs & Alex Fawke, *An Empirical Analysis of Diversity in Investment Arbitration: The Good, the Bad and the Ugly*, 12 *TRANSNAT'L DISP. MGMT.* 1, 3 (2015).

309. This empirical study did not include as many arbitrators in the field of investment arbitration as possible; instead, it was based on the assessment of the data with regard to the most appointed arbitrators, *i.e.*, the fifty-two individuals who have been appointed to investment tribunals on ten or more occasions. *Id.* at 26.

310. See *supra* Part II.A.

311. Kirby, *supra* note 11, at 690.

312. *Id.*

313. Hodgson & Campbell, *supra* note 229. This study covered arbitrations initiated between 2013 and 31 May 2017.

314. *Id.* The disparity between the mean and the median tribunal costs arguably results from the distorting effects of cases with dramatically large claims, as those cases would conceivably bear more technical complexities and consequentially require lengthier examination and deliberation.

data in the two studies into consideration, the mean length of investment proceedings would be four years.³¹⁵

Recall that from the Law and Economics studies presented earlier, arbitration *should* have the major advantage of speedier decision-making at lower costs, given the higher expertise of the arbiters involved.³¹⁶ But the results of some empirical studies cast doubts on these starting points. Kovacs, for example, believes that “[i]nternational arbitration is becoming too slow, too formalized and too expensive,” in comparison to what it is supposed to be.³¹⁷ Markert similarly complains that arbitration proceedings are a process that “has become too costly and inefficient.”³¹⁸ He points to anecdotal evidence suggesting that arbitration proceedings have turned from a speedy and efficient process into a longer process more closely resembling complex U.S.-style litigation proceedings.³¹⁹ Like Hodgson and Campbell, he found that arbitral proceedings under ICSID rules take longer than three years on average.³²⁰

The second purported advantage of arbitration, its quality,³²¹ is obviously much more difficult to measure. However, the previous section indicated that there is at least some evidence that there may be a bias against states and toward investors, not only in the differences in the success rate of states with different developmental statuses, but also in the claimed systematic bias towards investors in jurisdictional decisions.³²² Based on that evidence, most states in developing countries would therefore argue that the current ISA system is not “good.” It is unsurprising, then, that some states have withdrawn from the ICSID ISA system or threatened to do so.³²³

Most of the literature deals with the third advantage: Cost. Both the claimant and the respondent involved in an investment arbitration must be concerned with the costs incurred throughout the process.³²⁴ This is almost self-evident inasmuch costs spent on an arbitral proceeding have a direct and distinct impact on the financial profits of both investors and states.

315. Hodgson & Campbell, *supra* note 136.

316. *See supra* Part II.A.

317. Kovacs, *supra* note 28, at 155.

318. Markert, *supra* note 107, at 216.

319. *Id.*

320. *Id.* at 217 (finding that ICSID proceedings take an average of 3.6 years).

321. We focus here on the expectation that arbitration will provide for a neutral and unbiased forum for dispute resolution as the crucial element of a “good” mechanism.

322. *See supra* Part V.A.

323. Victorino J. Tejera, *Unraveling ICSID’s Denunciation: Understanding the Interaction Between Articles 71 and 72 of the ICSID Convention*, 20 ILSA J. INT’L & COMP. L. 423, 424 (2014).

324. Albert Jan van den Berg, Note, *Time and Costs: Issues and Initiatives from an Arbitrator’s Perspective*, 28 ICSID REV. - FOREIGN INV. L.J. 218, 218 (2013).

Some costs of arbitration include fees for arbitrators, administration, legal representation, witnesses, and experts.³²⁵ In addition to these external costs paid to third parties, the parties themselves obviously also have internal costs, for instance, the costs needed to collect and preserve evidence. The latter are, however, often much more difficult to calculate. Susan Franck's detailed study found that the costs of investment treaty arbitration have become substantial and that an assignment of even partial costs to one party could represent more than 10% of an average award.³²⁶ She also found that there is large uncertainty with respect to those costs.³²⁷

The OECD suggests, after conducting a survey on publicly available information about ISA costs (external costs), that the mean cost of recent ISA cases has totaled over \$8 million USD, exceeding \$30 million USD in some cases.³²⁸ Hodgson and Campbell reach a similar conclusion, though the specific data samples addressed by the scholars have an impact on their research outcomes. Their empirical study shows that, in their dataset of 177 cases, the mean party cost is \$7.4 million USD for claimants and \$5.2 million USD for respondent states.³²⁹ Generally, the larger the claim filed by an investor, the higher the cost of the case, but there are outliers as well.³³⁰

The high cost incurred by arbitral proceedings has been identified as one of the two gravest concerns about international arbitration among in-house counsel, the other being the excessive duration of proceedings.³³¹ Eberhardt and Olivet point to the experience of the Philippines to demonstrate the overwhelming costs of ISA. The developing state spent \$58 million USD defending two cases against German airport operator Fraport.³³² In the Philippines, this same amount is equivalent to the annual salaries of 12,500 teachers, the cost of vaccinating 3.8 million children, or building two new airports.³³³

These expenditures do not necessarily go to arbitrators.³³⁴ The lion's share ends up in the pockets of the legal counsel that the parties appoint to

325. Eberhardt & Olivet, *supra* note 134, at 15; Diana Rosert, *The Stakes Are High: A Review of the Financial Costs of Investment Treaty Arbitration*, INT'L INST. FOR SUSTAINABLE DEV. 1, 8 (July 2014), <http://www.iisd.org/sites/default/files/publications/stakes-are-high-review-financial-costs-investment-treaty-arbitration.pdf>.

326. Franck, *supra* note 144, at 814.

327. Franck suggests that the determination of cost-related issues is largely unpredictable due to uncertainty with regard to how and on what basis tribunals will decide costs. *Id.* at 838–839.

328. OECD, *Investor-State Dispute Settlement*, at 18 (2012) [hereinafter OECD, *ISDS*], <http://www.oecd.org/investment/internationalinvestmentagreements/50291642.pdf>.

329. Hodgson & Campbell, *supra* note 229.

330. *Id.* at 4.

331. OECD, *ISDS*, *supra* note 328, at 8.

332. Eberhardt & Olivet, *supra* note 134, at 15.

333. *Id.*

334. *Id.*

represent them throughout the proceeding; the costs of representation are estimated to average more than 80% of the cost of a single ISA case.³³⁵ Arbitration lawyers charge several hundred dollars per hour per person, with prices reaching over \$1,000 per hour per person at elite law firms.³³⁶

In contrast, the fees paid to arbitrators average about 16% of the whole sum of the costs of an individual case.³³⁷ Hodgson and Campbell found that the mean tribunal cost at the end of 2012 was \$746,000 USD, with a median cost of \$590,000 USD.³³⁸ Nevertheless, the cost of arbitrators' fees is steadily increasing, just like other arbitration costs: The mean tribunal cost from 2013 onwards increased to \$1,118,000 USD, with a median amount of \$905,000 USD, an increase of around 50%.³³⁹

Noticeably, relevant arbitration rules have set out different methods for the determination of the tribunal costs.³⁴⁰ For instance, within the framework of ICSID, the rules and regulations indicate that each arbitrator in the tribunal is entitled to earn \$3,000 USD per day for meetings or other work in connection with the proceeding.³⁴¹ In contrast, the UNCITRAL Arbitration Rules allow tribunals to determine their own fees in accordance with some flexible conditions, such as that the amount should be "reasonable," "taking into account the amount in dispute, the complexity of the subject matter, the time spent by the arbitrators and any other relevant circumstances of the case."³⁴² As of the end of 2012, UNCITRAL tribunals were 10% more costly than ICSID tribunals, although that gap seems to be shrinking.³⁴³

Administration and registration fees payable to arbitral institutions, instead of to investment tribunals, only account for a minor part of arbitration's overall cost, at about 2%.³⁴⁴ Similarly, the relevant arbitral institutions also apply different rates for the services that they provide for disputing parties.³⁴⁵ For instance, the SCC and ICC provide for an exact amount of administrative fees that must be paid by parties based on the amount in dispute, which means that the amount does not vary with the

335. OECD, *ISDS*, *supra* note 328, at 18; Eberhardt & Olivet, *supra* note 134, at 15.

336. A survey conducted by Global Arbitration Review in 2014 shows that the three law firms with the most experience representing claimants and respondents in ISA include Freshfields Bruckhaus Deringer (123 cases), White & Case (37 cases) and Curtis Mallet-Prevost Colt & Mosle (29 cases). Rosert, *supra* note 325, at 9; OECD, *ISDS*, *supra* note 328, at 19; Eberhardt & Olivet, *supra* note 134, at 19.

337. OECD, *ISDS*, *supra* note 328, at 18.

338. Hodgson & Campbell, *supra* note 229, at 2.

339. *Id.*

340. Rosert, *supra* note 325, at 10–11.

341. *Id.* at 10.

342. See G.A. Res. 65/22, UNCITRAL Arbitration Rules, arts. 40–41 (Dec. 6, 2010).

343. Hodgson & Campbell, *supra* note 229, at 3.

344. OECD, *ISDS* *supra* note 328, at 18; Rosert, *supra* note 325, at 12.

345. Rosert, *supra* note 325, at 12.

duration of the arbitral proceeding.³⁴⁶ ICSID, on the other hand, charges \$32,000 USD in administrative fees annually, so longer disputes are more expensive.³⁴⁷

One proposed reform of the ISA system in this regard is the creation of a more aggressive cost allocation system, which could force losing parties to pay a large share of the costs of their adversaries. Such a mechanism could provide parties with substantial incentives to limit or reduce unreasonable costs and to instead pursue efficient party behavior.³⁴⁸

Currently, applicable procedural rules and investment treaty provisions usually leave arbitrators some discretion to allocate the costs and fees between the disputing parties as they deem reasonable.³⁴⁹ Both the ICSID and UNCITRAL rules for the apportionment of costs and fees “leaves significant room for argumentation and arbitral discretion,”³⁵⁰ contributing to the uncertainty in disputing parties’ expectations of the costs and fees incurred by ISA proceedings. The most prevalent method applied by arbitral tribunals is “pay your own way,” requiring each side to cover their own counsel and expert fees and to share the tribunal costs.³⁵¹ This means that whatever the outcome of an arbitration is, respondents, and therefore taxpayers, have to pay millions in legal fees.³⁵²

By using an empirical study to analyze the efficiency of cost-allocations in investment arbitration,³⁵³ Webster concluded that it is doubtful whether the current rules on cost-allocation within ICSID, which do not require cost-shifting, sufficiently deter unmeritorious claims.³⁵⁴ More recent ISA cases have seen arbitrators switch methods, shifting at least some of the costs to the losing party.³⁵⁵

A cost-shifting approach, however, could be regarded as a double-edged sword for sovereign states.³⁵⁶ Though governments would incur less of the costs for legal counsel and expert advice when they secure victory,

346. *Id.*

347. *Id.*

348. *See* Markert, *supra* note 107, at 241.

349. Rosert, *supra* note 325, at 13.

350. David Smith, Note, *Shifting Sands: Cost-and-Fee Allocation in International Investment Arbitration*, 51 VA. J. INT’L L. 749, 750 (2011).

351. Rosert, *supra* note 325, at 13.

352. Eberhardt and Olivet quoted the case *Plama Consortium v Bulgaria*, in which the arbitral tribunal found that the claims filed by the investor were fraudulent. However, in the award, Bulgaria only obtained \$7 million USD as compensation for legal fees incurred, accounting for shortly more than the half of the sum. OECD, *ISDS*, *supra* note 328, at 21; Eberhardt & Olivet, *supra* note 134, at 15.

353. Webster, *supra* note 158, at 470–71.

354. *Id.* at 502, 505–506.

355. OECD, *ISDS*, *supra* note 328, at 21.

356. Smith, *supra* note 350, at 750.

their liability for legal and expert costs would grow when their states lose.³⁵⁷ While there is mixed evidence on whether investors are favored in terms of cost allocation,³⁵⁸ a study by Rosert finds some indications that “states are slightly more likely to be ordered to pay a share of the investors’ costs when the investor wins than [when] the inverse is the case.”³⁵⁹

D. Public Interest?

There are three other critical issues mentioned in the empirical literature with respect to investor-state arbitration. The first relates to its lack of transparency, the second relates to its lack of attention to environmental issues, and the third concerns whether there might be means to achieve the desirable depoliticization of investor-state disputes.

The issue of transparency is a major part of ISA’s legitimacy crisis.³⁶⁰ As international rules and norms are starting to gain the momentum to shape areas of domestic policy long regarded as exclusive to nation states,³⁶¹ domestic stakeholders have been embracing the cause of transparency throughout ISA.³⁶² Against this backdrop, Emilie Hafner-Burton (a Professor of International Justice and Human Rights) and David Victor (a Professor with expertise in international law and regulation) examined secrecy in international investment arbitration by conducting an empirical study covering the 246 ICSID investment arbitration cases that were concluded between 1972, when the first case was registered before ICSID and the beginning of 2012.³⁶³ The statistics they reviewed show that about 40% of cases were kept secret.³⁶⁴ The authors suggest that secrecy in investment arbitration serves as a flexibility-enhancing device precisely when enormous publicity would go against the interests of the disputing parties.³⁶⁵ Despite the great efforts made by the arbitral scene to boost transparency in investment arbitration, Hafner-Burton and Victor hold the opinion that those reforms are, in part, failing because the disputing parties

357. Joachim Pohl, *Societal Benefits and Costs of International Investment Agreements: A Critical Review of Aspects and Available Empirical Evidence* 48 (OECD Working Papers on Int’l Inv., No. 01, 2018), <https://www.oecd-ilibrary.org/docserver/e5f85c3d-en.pdf>.

358. OECD, *ISDS*, *supra* note 328, at 22.

359. Rosert, *supra* note 325, at 14.

360. See, e.g., James D. Fry & Odysseas G. Repousis, *Towards a New World for Investor-State Arbitration Through Transparency*, 48 N.Y.U. J. INT’L L. & POL. 795, 806–07 (2016).

361. William Burke-White & Anne-Marie Slaughter, *The Future of International Law Is Domestic (or, The European Way of Law)*, 47 HARV. INT’L L.J. 327, 327 (2006).

362. See Stephan W. Schill, Editorial, *Five Times Transparency in International Investment Law*, 15 J. OF WORLD INV. & TRADE 363 (2014).

363. Emilie M. Hafner-Burton & David G. Victor, *Secrecy in International Investment Arbitration: An Empirical Analysis*, 7 J. OF INT’L DISP. SETTLEMENT 161, 164 (2016).

364. *Id.* at 169.

365. *Id.*

prefer “to use pre-judgment settlement to hide procedural and substantive outcomes.”³⁶⁶

In that context, they put forward three proposals to promote transparency in ISA.³⁶⁷ They suggest that sovereign countries could incorporate clauses “demanding the mandatory disclosure of all awards (as in the UNCITRAL reforms) and settlements” or even require parties to “request the tribunal to embody the settlement in an arbitral award” in their future investment treaty practice.³⁶⁸ In addition, they propose that changes can be made to the ICSID Arbitration Rules, instead of the ICSID Convention (whose change would require the consensus of all of the Convention’s Contracting States), to require the Secretariat to publish the basic terms of a settlement upon the consent of the disputing parties.³⁶⁹ Last, in their opinion, other informal improvements may also contribute to a higher level of transparency in ISA, such as the establishment of best practices for disclosure and arbitrators’ proactive encouragement of the parties to disclose settlement information.³⁷⁰

Another point of controversy surrounding the legitimacy of the ISA regime is the tension between environmental protection and the protection of investor rights. Some of the critics of ISA raise the concern that the regulatory power of sovereign states to enact laws and regulations to protect the environment for the general good of the public is severely circumscribed by the international investment regime, either because states fear being sued in international tribunals or because they fear having to pay compensation to investors.³⁷¹ In a bid to test the hypothesized negative impact of ISA on environmental protection, Behn and Langford compiled a database of more than 800 registered cases and looked into the environmental cases specifically.³⁷²

Their empirical study obtained some surprising and interesting results: First, the win-loss ratio for claimants in environmental cases showed no significant divergence from that of all ISA cases.³⁷³ On the one hand, in those cases in which the claimant failed, the arbitral tribunals recognized the protection of the environment as a part of the legitimate defense presented by the respondent states. On the other hand, in cases where the claimants prevailed, the tribunals seemed to view the legitimacy of environmental

366. *Id.* at 161.

367. *Id.* at 181–82.

368. *Id.* at 181.

369. *Id.* at 181–82.

370. *Id.* at 182.

371. Daniel Behn & Malcolm Langford, *Trumping the Environment? An Empirical Perspective on the Legitimacy of Investment Treaty Arbitration*, 18 J. OF WORLD INV. & TRADE 14, 15 (2017).

372. *Id.* at 16.

373. *Id.* at 47.

protection measures with suspicion.³⁷⁴ Behn and Langford argue that the languages of some of these findings in favor of investors may indicate that investment tribunals have not yet fully embraced “the importance of environmental arguments and their values [in] the adjudication of these kinds of disputes.”³⁷⁵

The researchers found that of the forty-seven environmental cases they studied, there were only four cases in which investors challenged domestic legislation, and all four cases culminated in the failure of the investors.³⁷⁶ This indicates that the erosion of sovereign states’ regulatory autonomy by ISA might not be so grave as envisaged.³⁷⁷ The researchers also found that challenges put forward by claimants against specific non-legislative measures (e.g., the cancellation of concessions or contracts) in the extractive industries and the water and waste sector are likely to be favored by arbitral tribunals, but claimants fared quite poorly when they targeted generally applicable measures, particularly those banning the import or sale of products for the sake of environmental protection.³⁷⁸ Another striking finding is that in environmental cases developing states seem to fare better than developed states.³⁷⁹

The depoliticization of investor-state disputes—transferring the disputes “from the political arena of diplomatic protection to a judicial forum with objective, previously agreed standards and a pre-formulated dispute settlement process”³⁸⁰—is another issue of public interest. In an OECD Working Paper, Pohl was unable to discern a unified concept or scope of “depoliticization,” but indicated that it is usually understood to serve three ends: the enhancement of (1) intergovernmental relationships; (2) relationships between companies and their home governments; and (3) competition among firms.³⁸¹

The depoliticization of investment disputes was not only a major objective during the preparatory stage of the ICSID Convention, but it is still recognized by the present literature as an important policy goal of the ISA system.³⁸² However, it is unclear whether the depoliticization effect emanated from ISA, or the scope of this effect.³⁸³ Owing to the very limited empirical evidence available, Pohl was unable to draw a conclusion on the extent to which IIAs, through ISA mechanisms, depoliticize investor-state

374. *Id.* at 47–48.

375. *Id.* at 48.

376. *Id.*

377. *Id.*

378. *Id.*

379. *Id.*

380. Ursula Kriebaum, *Evaluating Social Benefits and Costs of Investment Treaties: Depoliticization of Investment Disputes*, 33 ICSID REV. - FOREIGN INV. L.J. 14, 15 (2018).

381. Pohl, *supra* note 357, at 48–50.

382. *Id.* at 50.

383. *Id.* at 50–54.

disputes.³⁸⁴ There is limited anecdotal evidence, however, suggesting that notwithstanding the existence of ISDS, IIAs lead to more, rather than less, diplomatic interaction between states concerned in dispute resolution.³⁸⁵ In addition, Pohl showcases sources indicating that the depoliticization effect of ISDS is at least open to doubts, as recent cases have witnessed simultaneous political activities by investors' home states to protect their nationals, for example via diplomatic protection, in parallel to the ongoing investor-state arbitration.³⁸⁶

E. Summary

The empirical evidence that we reviewed in this section provides some support for the complaints from developing countries about an alleged bias in investor-state arbitration, even though the studies are not one-dimensional.³⁸⁷ A first, often-quoted study by Franck found that there is no empirical support for a bias toward investors in the ICSID system.³⁸⁸ However, later studies seem to indicate that investors who are largely from the North do have a higher probability of success in investor-state arbitration compared to developing states.³⁸⁹

Of course, one should also be careful in interpreting the empirical finding that investors from the North have a higher probability of success in ISA than defendant states from the South as clear evidence of bias.³⁹⁰ After all, the default expectation should not necessarily be that investors and states should have equal rates of success in ISA. There may also be substantive reasons to assume that one party (the investor) might do better in ISA than the other (the state). That could be the case because ISA is investor-initiated, or it could be because of the nature of ISA disputes: They are brought by investors when a state has allegedly violated its obligations under a bilateral investment treaty. Assuming investors are utility maximizers, they are not likely to resort to ISA without any factual or legal bases.

In any case, there is clear evidence that investor-state arbitration is dominated by a small, insular elite of arbitration practitioners with strong

384. *Id.* at 50–55. Still, Pohl seems to have limited confidence in the depoliticization effect of ISDS, saying “[b]ased on available empirical evidence, IIAs thus do not appear to mechanically depoliticise disputes, but they may provide greater comfort for governments to refrain, at their discretion, from intervening or limiting their intervention.” But he also admits that “[w]hether or not IIAs make a positive contribution to any of the ultimate goals of depoliticization in practice, however, remains uncertain in the absence of sufficient empirical evidence.” *Id.* at 54.

385. *Id.*

386. *Id.* at 50–54.

387. *See supra* Part V.A.

388. Franck, *supra* note 145, at 909.

389. Daniel Behn et al., *supra* note 186, at 369–70.

390. *Id.* at 369–70.

contacts in the corporate world.³⁹¹ These elite arbitrators overwhelmingly come from the North, thus substantiating the feelings of discomfort from the South.³⁹² It is, at first blush, not theoretically clear why old, white males from the North would be overrepresented in ISA. The cause could either be supply-driven (implying that it is primarily those types of people presenting themselves as arbitrators), demand-driven (meaning that parties primarily call on those types of people to serve as their arbitrators), or potentially a combination of both. Even though it is difficult to find a precise cause for the overrepresentation of particular groups, the important point is that it does give support to the suspicions of Southern states against the ISA system.

Finally, the assumption that arbitration is cheap and speedy seems to be contradicted by the practice of investor-state arbitration.³⁹³ The evidence shows that ISA's procedures are both extremely costly (with some scholarship indicating particularly high costs for developing countries, compared to their limited public budgets) and very lengthy.³⁹⁴ Although it is difficult to compare the length and costs of ISA proceedings to the average court procedure around the world, the fact that some states (notably developing states) stepping away from the ISA system shows that these countries feel more comfortable with their judiciaries handling investor-state disputes. In sum, the empirical evidence reviewed seems to substantiate the calls for reform of the system.

VI. ANALYSIS

Given the empirical studies we have reviewed in the past two sections, it will come as no surprise that there are calls to reform the system.³⁹⁵ Indeed, the empirical evidence substantiates these calls.³⁹⁶ Though both the empirical studies and the Law and Economics literature could furnish inspiration for the reform of ISA, the Law and Economics literature on arbitration generally does not account for the practice of ISA. The empirical studies reviewed in this paper not only bring some of the concerns about the legitimacy of ISA into focus, but also stimulate maneuvers to shed the burdens that are haunting the ISA regime.

391. Eberhardt & Olivet, *supra* note 134, at 36.

392. *Id.*

393. *See supra* Part V.C.

394. Eberhardt & Olivet, *supra* note 134, at 15.

395. Stephan W. Schill, *Reforming Investor-State Dispute Settlement (ISDS): Conceptual Framework and Options for the Way Forward*, E15 Task Force on Investment Policy, INT'L CTR. TRADE & SUSTAINABLE DEV. 1 (July 2015), <http://e15initiative.org/wp-content/uploads/2015/07/E15-Investment-Schill-FINAL.pdf>.

396. *See supra* Parts IV & V.

A. *The Law and Economics Literature and ISA Reform*

Law and Economics scholars emphasize that arbitrators, as opposed to judges in domestic courts, are likely to specialize in a particular type of dispute.³⁹⁷ This is at least as true in investment arbitration as in commercial arbitration. The resolution of international investment disputes via arbitration in most cases involves the application and interpretation of protective provisions enshrined by IIAs, thus raising a demand for arbitrators to have relatively specialized knowledge and experience in the field of public international law.³⁹⁸ In fact, the community of investment arbitrators is much smaller than that of commercial arbitrators, because many commercial arbitrators do not feel comfortable dealing with investor-state disputes or simply are not chosen by disputing parties for that purpose.³⁹⁹ Although there has not been a systematic investigation into the background of all the arbitrators involved in ISA, many of the most prominent figures in this community have rich knowledge of and experience in public international law.⁴⁰⁰

Under Law and Economics theories of arbitration, this specialization of investment arbitrators should not only lure foreign investors away from litigation in national courts, but also contribute to lowering costs for disputing parties and improving the efficiency of dispute resolution.⁴⁰¹ It follows that any attempt to reform ISA should not overlook the value of adjudicators specialized in public international law, as this specialization arguably leads to better decisions and lower costs for disputants. For this reason, Colin Brown (Deputy Head of Unit, Legal Aspects of Trade Policy and Dispute Settlement, Directorate General for Trade, European Commission), suggests that a multilateral investment dispute resolution mechanism should carefully consider the qualifications of adjudicators.⁴⁰²

Other advantages of arbitration over litigation seem to have less application in the ISA context. For example, investment arbitration does not seem to be less adversarial than litigation; foreign investors almost always

397. Rubino-Sammartano, *supra* note 14, at 168.

398. Böckstiegel, *supra* note 115, at 582.

399. *Id.*

400. To give an example, background research on the fifteen elite arbitrators identified by Eberhardt and Olivet shows that all these big names have a long track record of experience in state-state disputes or have received education or training about public international law. See Eberhardt & Olivet, *supra* note 134, at 38–41.

401. Benson, *supra* note 15, at 94.

402. Brown mentioned a striking phenomenon: The qualification requirements of many international tribunals seem to echo those of the International Court of Justice. Colin M. Brown, *A Multilateral Mechanism for the Settlement of Investment Disputes. Some Preliminary Sketches*, 32 ICSID REV. - FOREIGN INV. L.J. 673, 682 (2017) (“The Court shall be composed of a body of independent judges, elected regardless of their nationality among persons of high moral character, who possess the qualifications required in their respective countries for appointment to the highest judicial offices, or are jurisconsults or recognized competence in international law.”).

file claims directly against host states at the international level.⁴⁰³ That sovereign states have to bear the liability as a result of ISA, even if it was a state's political sub-division that breached that state's treaty obligations toward foreign investors under IIAs, could even exacerbate the antagonism between the disputing parties.⁴⁰⁴

Turning to the oft-claimed advantage that disputing parties are able to maintain the privacy of their dispute resolution at their discretion, confidentiality does not seem to be appreciated as much in the ISA context as in the commercial arbitration context. Critics have long condemned the lack of transparency at all stages of investment arbitral proceedings.⁴⁰⁵ In recent years, though, ISA has witnessed increased transparency, exemplified by the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration (2014)⁴⁰⁶ and the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration.⁴⁰⁷ These efforts certainly contain loopholes, however, and challenges for boosting transparency in ISA still remain.⁴⁰⁸

In addition, with regard to the freedom to choose applicable law, businesspeople are unlikely to have that much discretion to avoid the application of state-made law in ISA because, as Professor Christoph Schreuer (a respected authority in international investment law) points out,

403. Jeswald W. Salacuse & Nicholas P. Sullivan, *Do BITs Really Work: An Evaluation of Bilateral Investment Treaties and Their Grand Bargain*, 46 HARV. INT'L L.J. 67, 77 (2005).

404. Lawrence L. Herman, *Federalism and International Investment Disputes*, INT'L INST. FOR SUSTAINABLE DEV. (July 12, 2011), <https://www.iisd.org/itn/2011/07/12/federalism-and-international-investment-disputes>.

405. INT'L BAR ASS'N., *Consistency, Efficiency, and Transparency in Investment Treaty Arbitration: A Report by the IBA Arbitration Subcommittee on Investment Treaty Arbitration 1*, 53 (Nov. 2018) [hereinafter IBA Arbitration Subcommittee Report], <https://www.threecrownsllp.com/wp-content/uploads/2018/12/InvestmentTreatyArbitrationReport2018.pdf>.

406. The UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration aim to increase the level of transparency in investment arbitral proceedings conducted pursuant to the UNCITRAL Arbitration Rules through provisions focusing on publication of information at the commencement of arbitral proceedings, publication of documents, submission by a third person, submission by a non-disputing party to the treaty and hearings. See G.A. Res. 68/109, UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration, arts. 2-6 (Dec. 16, 2013). In addition, article 1(3)(a) of the Rules effectively constricts disputing parties' ability to keep their disputes and the dispute resolution process under the carpet. It provides that: "The disputing parties may not derogate from these Rules, by agreement or otherwise, unless permitted to do so by the treaty." *Id.* art. 1(3)(a).

407. The United Nations Convention on Transparency in Treaty-based Investor-State Arbitration is intended to expand the scope of application of the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration. See generally G.A. Res. 69/116, The United Nations Convention on Transparency in Treaty-based Investor-State Arbitration (2015).

408. JOHAN BILLIET ET AL., INTERNATIONAL INVESTMENT ARBITRATION: A PRACTICAL HANDBOOK 41-42 (2016).

“[s]ome questions that are relevant to a tribunal’s jurisdiction are governed by domestic law.”⁴⁰⁹

There are also some situations in which the Law and Economics literature suggests that commercial arbitration might be flawed, and those flaws are also present in ISA. For example, the Law and Economics literature comparing the incentives of judges to those of arbitrators suggests that party-appointed arbitrators may not really be the best choice for the resolution of investor-state disputes.⁴¹⁰ Given the broad discretion that disputing parties usually have to choose adjudicators in arbitration,⁴¹¹ one might imagine that disputing parties would spare no effort to appoint an arbitrator who is more likely to side with them. According to celebrated arbitrators Jan Paulsson and Yves Derains, this affiliation effect—and its attendant moral hazard—does exist in commercial arbitration, as well as in ICSID arbitration.⁴¹²

This innate deficiency of the party-appointed arbitrator system could drag any given investor-state dispute into a run-off between the arbitrators who were appointed by the investor party and the state party, respectively, and many frequent investment arbitrators are believed to be polarized (either biased towards investors or states).⁴¹³ Although the presiding arbitrator could be expected to pour oil on troubled waters in such a situation, the party-appointment system casts doubt on the independence of investment tribunals and arbitrators.⁴¹⁴ This is not to say that arbitrators in ISA are not figures of high moral character and good conscience, or that a presiding arbitrator could not act as a check on rest of the tribunal. However, the risks associated with the partisan arbitrator system could be averted by changing the method for the appointment of adjudicators.

One way to remove the nexus between disputing parties and adjudicators is through Brown’s sketch of the adjudicator-selection system. In that system, parties would rely on a multilateral investment court to select their adjudicators, and they would be stripped of the power to determine who would sit on a particular case.⁴¹⁵

As discussed above, Law and Economics scholarship also suggests that arbitrators seeking to maximize their utility ought to pursue a constant flow of income. They are, therefore, subject to considerable market pressure as they issue awards.⁴¹⁶ It follows then, that there is a lurking risk that

409. Christoph Schreuer, *Jurisdiction and Applicable Law in Investment Treaty Arbitration*, 1 MCGILL J. DISP. RESOL. 1, 4 (2014).

410. Van Aaken & Broude, *supra* note 19, at 15–16.

411. Benson, *supra* note 13, at 162.

412. David Branson, *Sympathetic Party-Appointed Arbitrators: Sophisticated Strangers and Governments Demand Them*, 25 ICSID REV. - FOREIGN INV. L.J. 367, 391 (2010).

413. *See* Brown, *supra* note 402, at 678.

414. *Id.*

415. *Id.* at 683.

416. Van Aaken & Broude, *supra* note 19, at 14.

investment arbitrators may be prone to “split the difference” in the process of decision-making, with arbitrators tempted to put the satisfaction of the disputing parties before the facts and applicable laws in a particular case. Meanwhile, the affiliation effect in ISA is intensified further by the asymmetrical nature of investor-state disputes. As mentioned earlier, challenges to investment arbitrators are hard and often ineffective, particularly in the context of ICSID arbitration.⁴¹⁷ Consequently, arbitrators are more willing to express either a consistent pro-investor or pro-state stance, marketing themselves to either foreign investors or sovereign states in order to increase their chances of appointment to investment tribunals,⁴¹⁸ than they would be if the system had a more effective challenge procedure, which opposing parties could use to penalize arbitrator bias. Branson also points out the risk of “replacing judges, government ministers and professors . . . with lawyers who require arbitration fees for their livelihood,” and who therefore have additional moral hazard.⁴¹⁹

The incentive for investment arbitrators to maximize their utility also raises suspicion about their decisions at the jurisdictional phase (not just in their rulings on the merits), since a negative jurisdictional ruling diminishes their profits from a particular case.⁴²⁰ This concern about the legitimacy of ISA appears difficult to address under the current operating mechanism because it is heavily reliant on the commercial arbitration model where arbitrators are remunerated by disputing parties.⁴²¹ Again, Brown’s proposal of an investment court seems to effectively diminish, if not remove, this exact concern.⁴²²

He envisions a system of full-time adjudicators who would be remunerated regardless of the number of cases that they handle.⁴²³ Under these circumstances, adjudicators would be able to devote themselves to delivering high-quality decision-making in accordance with facts and applicable laws, rather than worrying about responses to their decisions that may threaten their income.⁴²⁴ On the other hand, it is worth repeating the caution from the Law and Economics literature that salaried judges may

417. Giorgetti, *supra* note 159, at 475.

418. Joost Pauwelyn, *The Rule of Law Without the Rule of Lawyers? Why Investment Arbitrators Are from Mars, Trade Adjudicators from Venus*, 109 AM. J. INT’L L. 761, 787 (2015).

419. Branson, *supra* note 412, at 391.

420. Recall that from the introduction of tribunal costs in Part V.C, the ICSID rules and regulations indicate that each arbitrator in the tribunal is entitled to earn \$3,000 USD per day for meetings or other work in connection with the proceeding. Rosert, *supra* note 325, at 10. The UNCITRAL Rules also require tribunals to consider, for instance, time spent by arbitrators. See G.A. Res. 65/22, UNCITRAL Arbitration Rules, *supra* note 342, art. 41.

421. Brown, *supra* note 402, at 679.

422. *Id.* at 687.

423. *Id.* at 679.

424. *Id.*

have less incentive than arbitrators to deliver high-quality decisions.⁴²⁵ Thus, to ensure that the judges of a multilateral court are motivated to perform well, the designers of such a court should remember that judges derive utility from more than one source and use a mixture of reasonable arrangements to motivate their performance.⁴²⁶

The Law and Economics literature also warns of the social cost of arbitration. Recall that Landes and Posner preferred litigation to arbitration because of the positive externalities generated by litigation. This position provides tentative support for the proposal to replace the current arbitral system with a court for resolving investor-state disputes, as court litigation not only dispenses justice to disputing parties, but also produces public good. Society as a whole benefits when court litigation generates precedents and incentivizes adjudicators to provide detailed reasoning for their decisions.⁴²⁷

However, in the context of ISA as it is today, this logic may not stand so firmly. First, as discussed above, the arbitration community has already taken steps to increase transparency in ISA proceedings in recent years in recognition of the considerable public interests often involved in investor-state disputes. Second, as mentioned in Part III, investment tribunals in practice tend to refer to previous investment awards to either reinforce their own arguments or contradict the opinions of prior tribunals.⁴²⁸ At the same time, investment awards have become more accessible to the public, generating positive externalities similar to court precedent by enlightening disputing parties and society in general. But it is equally true that the inconsistency of outcomes in ISA has made it difficult for investors and states to predict the outcomes of their actions if arbitration is pursued.⁴²⁹ Third, a closer examination of investment awards issued by various tribunals, which not infrequently consist of dozens of pages, would pose a

425. POSNER, *supra* note 41, at 570.

426. For instance, since salaried judges derive utility from public approval as well, ensuring high-level transparency and public access to the adjudicative process might provide an additional incentive for adjudicators to perform well. In addition, an appointment system with a fixed term which is renewable may also help. Baum, *supra* note 44, at 754–60.

427. Landes & Posner, *supra* note 60, at 238–39.

428. Cheng, *supra* note 101, at 1016; Grisel, *supra* note 101, at 226.

429. N. Jansen Calamita, *The (In)Compatibility of Appellate Mechanisms with Existing Instruments of the Investment Treaty Regime*, 18 J. WORLD INV. & TRADE 585, 586–87 (2017). Indeed, an increasingly accepted view in academia seems to be that inconsistent awards (and annulment decisions if applicable) “threaten the sustainability of the international investment regime,” and that a greater degree of consistency in investment arbitration is desirable. IBA Arbitration Subcommittee Report, *supra* note 405, at 7. Irene Cate, a Clinical Assistant Professor, argues that consistency would contribute to the equitable treatment of litigants, ensure the continuity and predictability of the legal system, and promote the legitimacy of decision-making. Irene M. Ten Cate, *The Costs of Consistency: Precedent in Investment Treaty Arbitration*, 51 COLUM. J. TRANSNAT’L L. 418, 448–56 (2013).

head-on challenge to the statement that arbitrators deliberately avoid the clarity of rules and norms by not writing down their opinions.⁴³⁰

The increased transparency in ISA proceedings as well as investment arbitrators' willingness to write down their opinions show that there are particular features of ISA that do not specifically map onto the Law and Economics analysis of commercial arbitration. Still, some of the important points mentioned in the Law and Economics literature (that arbitration does not generate positive externalities in the same way as court decisions) remain relevant today and may provide arguments for a reform of ISA toward a multilateral investment court.

B. *Empirical Studies and ISA Reform*

The empirical studies discussed in this article do not represent an exhaustive overview of all the empirics available in this domain. The broader empirics themselves also do not deal with every criticism of ISA in the literature.⁴³¹ For example, the inconsistency of arbitral decisions is cited as a major concern threatening the predictability and legitimacy of ISA.⁴³² Yet there seems to be no systematic, empirical research efforts examining whether outcomes are indeed inconsistent.⁴³³

Empirical studies remain important in the debate concerning the reform of ISA, however. The empirical studies *have* shown a clear picture of changes in the pattern of arbitration filings.⁴³⁴ Whereas the traditional pattern of ISA pitted foreign investors from developed states against less developed states, more and more developed states are being brought to arbitration by foreign investors.⁴³⁵ Considering that the outward FDI flows from developing countries have become more significant in the past couple of decades,⁴³⁶ the pattern of filings in ISA is likely to shift further with more participation from developing country investors on the claimant side.⁴³⁷ This transition, if it happens, may provide evidence that ISA is not a political tool against less developed states and should not be demonized as such.

430. POSNER, *supra* note 41, at 558.

431. UNCTAD, *World Investment Report 2015*, *supra* note 5, at 128.

432. IBA Arbitration Subcommittee Report, *supra* note 405, at 7.

433. Existing literature on the topic of inconsistent awards in ISA, however, commonly refers to cases with similar facts but divergent outcomes as examples to showcase the lack of consistency in the system. *See, e.g.*, Leah D. Harhay, *Investment Arbitration in 2021: A Look to Diversity and Consistency*, 18 SW. J. INT'L L. 89, 94–97 (2011).

434. *See supra* Part IV.B.

435. *See* Schultz & Dupont, *supra* note 12, at 1151–57.

436. Sayeeda Bano & Jose Tabbada, *Foreign Direct Investment Outflows: Asian Developing Countries*, 30 J. OF ECON. INTEGRATION 359, 360 (2015).

437. For instance, Chinese and Indian investors alike seem to resort to ISA more frequently since 2010 compared to the pre-2010 period. *Investment Dispute Settlement Navigator*, *supra* note 88.

In addition, empirical work has led to the concerning conclusion that developed countries have consistently higher success rates than less developed countries in the ISA proceedings initiated against them.⁴³⁸ Although there could be possibly dozens of reasons that account for this disparity, and the disparity itself is not adequate evidence that the ISA regime is severely biased against Southern countries, the perception of bias within ISA may gradually lead developing countries to lose confidence in this dispute resolution system. In light of the general disadvantages of the Southern countries in global politics and economics, it is important that any initiative aiming to reform the current system gives due attention the concerns of these countries.

A lack of diversity within the arbitration community is also a consistent source of worry.⁴³⁹ While the ISA arbitrator community is diverse in a few aspects, there is a severe lack of diversity in terms of gender and geographical representation.⁴⁴⁰ The dominance of ISA by elderly, white, male arbitrators not only aggravates the negative impression of the Southern countries concerning ISA but also threatens the (perceived) fairness of the system since “diverse decisionmakers are more likely to avoid cognitive biases and group-think in decision making.”⁴⁴¹ The lack of involvement of arbitrators from the Southern countries could in part result from the fact that the legal services industries in those countries are in general less developed than those of Northern countries. This, in turn, can be traced to more fundamental issues, such as economic power, social systems, and legal traditions.⁴⁴²

However, a dearth of Southern arbitrators is not an excuse for not making changes to increase representation from Southern countries. The International Court of Justice and the World Trade Organization have already set good examples of inclusiveness.⁴⁴³ Furthermore, the few female arbitrators within the elite fifteen are recognized and commended by the arbitration industry and disputing parties at least as often as the male arbitrators are, further corroborating that the artificial barrier for female

438. Schultz & Dupont, *supra* note 12, at 1167.

439. See *supra* Part V.B.

440. Kovacs & Fawke, *supra* note 308, at 26–27.

441. Andrea Kay Bjorklund, *The Diversity Deficit in Investment Arbitration*, EJIL: TALK! (Apr. 14, 2019), <https://www.ejiltalk.org/the-diversity-deficit-in-investment-arbitration>.

442. Kovacs & Fawke, *supra* note 308, at 25.

443. For instance, Pauwelyn found out that while ICSID arbitrators are predominately Europeans and Americans, WTO panels are more inclusive and include more representation of developing countries. Pauwelyn, *supra* note 418, at 769–72. Article 9 of the Statute of the ICJ states that, “At every election, the electors shall bear in mind not only that the persons to be elected should individually possess the qualifications required, but also that in the body as a whole the representation of the main forms of civilization and of the principal legal systems of the world should be assured.” Statute of the International Court of Justice, art. 9 (Apr. 18, 1946).

arbitrators to enter into investment arbitration should be demolished.⁴⁴⁴ There is, however, the need to emphasize once again that diversity and inclusiveness is inherently valuable since it relates to the sociological and even normative legitimacy of an adjudicatory regime.⁴⁴⁵

Another conclusion that may be readily drawn from empirical studies is that the amount of compensation claimed by foreign investors and awarded by investment tribunals has skyrocketed, and it shows no signs of slowing down.⁴⁴⁶ Though this dramatic rise could be a natural outcome of the development of global FDI activities and thus does not necessarily pose any challenge to the ISA regime itself, the tremendous interests concerned require a reform of ISA to ensure fairness, integrity, and transparency. The increase in compensation also stimulates us to consider whether it is still reasonable to let *ad hoc* tribunals deal with investor-state disputes that involve such enormous interests and complicated issues.

Despite the fact that the skyrocketing costs could be a consequence of increasingly complicated cases and the increased resources that countries pour into dispute resolution, increased costs constitute a threat to a sustainable development of the ISA regime.⁴⁴⁷ First of all, the higher costs involved in ISA make it difficult for less wealthy individuals and enterprises to gain access to international arbitration, making participation in ISA a privilege that serves the interests of an exclusive group of powerful individuals and companies.⁴⁴⁸ Second, increased costs impose an even heavier burden on the budgets of the Southern countries, which may ultimately nudge those countries to withdraw from ISA, shaking up the basis of the whole ISA regime.⁴⁴⁹

There are a variety of reform proposals on this front: The government of Thailand, for instance, suggested that, because governments lack an international body which specializes in independent and low-cost ISA advice for developing countries, they have to endure the steep price of legal services provided by international law firms.⁴⁵⁰ The academic community

444. Eberhardt & Olivet, *supra* note 134, at 36.

445. Bjorklund, *supra* note 441.

446. Hodgson & Campbell, *supra* note 229, at 3.

447. OECD, ISDS, *supra* note 328, at 9.

448. “It appears that a number of ISDS claims by investors have been discontinued due to the refusal or inability of the investors to pay the costs.” *Id.*

449. The government of Morocco, for instance, emphasizes that “the increase in the cost of arbitration has given rise to growing dissatisfaction with international arbitration, particularly with regard to its impact on the public policies and sustainable development of States.” UNCITRAL Working Group III, Possible Reform of Investor-State Dispute Settlement (ISDS), Submission from the Government of Morocco, on Its Thirty-Seventh Session, U.N. Doc A/CN.9/WG.III/WP.161 (2019).

450. UNCITRAL Working Group III, Possible Reform of Investor-State Dispute Settlement (ISDS), Comment by the Government of Thailand, on Its Thirty-Fifth Session, U.N. Doc. A/CN.9/WG.III/WP.147 (2018).

supports this call for the establishment of a legal assistance center to alleviate the strain on developing countries' budgets.⁴⁵¹

Rosert also suggests other measures to bring the costs involved in ISA down.⁴⁵² First, there is still room for arbitration procedures to be streamlined so that both arbitration costs and legal fees can be reduced.⁴⁵³ For instance, it was suggested that there could be "mandatory direction or encouragement of parties to arbitrate disputes via a sole arbitrator rather than a panel of three arbitrators in smaller value or less complex disputes."⁴⁵⁴ Second, sovereign states and the broader international community should endeavor to build up their capacity to defend claims by foreign investors on their own, tempering their reliance on pricey international law firms.⁴⁵⁵ Third, more efforts to discourage frivolous and inflated claims could also help to reduce the adverse influence of high costs, including more frequent use of cost-shifting policies.⁴⁵⁶

VII. CONCLUDING REMARKS

In this article we attempt, for the first time, to integrate the Law and Economics literature concerning arbitration with empirical evidence concerning how ISA functions in practice. There is a striking difference between the theoretical assumptions and reality. The traditional Law and Economics literature assumes that arbitration is speedy and inexpensive.⁴⁵⁷ But it is not clear to what extent those assumptions are really met in ISA. There are increasing complaints about relatively high costs and lengthy procedures that almost rival those of the American judiciary.⁴⁵⁸ In that respect, it is not surprising that scholars, parties, and practitioners are calling for reform, since some of the traditional benefits of arbitration do not always seem to hold.

Another assumption in the Law and Economics literature is that arbitration generates exchangeable decisions. Ashenfelter's model assumed that arbitrators tend toward "the middle of the road" awards, since extreme positions do not lead to new appointments.⁴⁵⁹ Outliers were not expected. However, in the practice of ISA, there are complaints that many frequent

451. Rosert, *supra* note 325, at 15.

452. *Id.*

453. *Id.*

454. IBA Arbitration Subcommittee Report, *supra* note 405, at 39.

455. Rosert, *supra* note 325, at 15.

456. *Id.*

457. COOTER & ULEN, *supra* note 18, at 450.

458. Markert, *supra* note 107, at 216.

459. Ashenfelter, *supra* note 22, at 343.

investment arbitrators tend to be biased in favor of either the investor side or the state side.⁴⁶⁰

Interestingly, the Law and Economics literature is generally critical of arbitration; despite its ability to provide private benefits to parties (at least the assumed benefits of lower cost, better information, and speedy decision-making), scholars are concerned about its social costs.⁴⁶¹ According to this thinking, the public good of adjudication is lost as a result of the secrecy in arbitration. Precisely for that reason, one can understand the calls for transparency, especially in investor-state arbitration. Indeed, an empirical study introduced above found that 40% of the cases covered were kept secret, indicating that lack of transparency is an unsettled problem in the ISA system.⁴⁶² Given the public interest involved (going beyond the mere interest of the private parties in the dispute), transparency in ISA has the advantage of creating positive externalities. The recent trend in the ISA practice, with the publication of the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration and the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration, shows the signs that transparency is improving. For the same reason, many reformers call for allowing institutional appeals of arbitral awards. Not only could this be a means of error correction, it could have a harmonizing effect to avoid inconsistent decisions and promote higher quality decision-making by adjudicators.⁴⁶³

The most important argument against arbitration stressed in the Law and Economics literature is its lack of positive externalities.⁴⁶⁴ It is also questionable whether the traditional economic argument supporting commercial arbitration applies to the same extent to ISA. Commercial arbitration is supposed to be fast, cheap, high-quality, and impartial.⁴⁶⁵ Yet some argue that ICSID decision-making is slow, extremely expensive, and (as a result of the bias in selecting arbitrators) also not as impartial as developing countries would prefer.⁴⁶⁶ The empirical evidence supports this position.⁴⁶⁷ Moreover, the fact that elderly, white, and male arbitrators—largely connected to the corporate world—often arbitrate cases also provides at least a suggestion of bias toward investors and against

460. Brown, *supra* note 402, at 678. *But see supra* text accompanying notes 53–59 (discussing the split-the-difference critique).

461. *See supra* Part II.C.

462. Hafner-Burton & Victor, *supra* note 363, at 169.

463. Brown, *supra* note 402, at 683–84.

464. *Cf.* Landes & Posner, *supra* note 60, at 238–239.

465. *See supra* Parts II.A & II.B.

466. Franck, *supra* note 144, at 829.

467. *See supra* Part V.

developing countries.⁴⁶⁸ In that sense, it is not surprising that developing countries are very critical of the current ICSID model.⁴⁶⁹

The Law and Economics literature shows that both judges and arbitrators strive for utility maximization.⁴⁷⁰ But judges are, in most legal systems, nominated for life,⁴⁷¹ and, especially at the highest level, cannot obtain more income by providing better quality decisions.⁴⁷² The incentive structure of the judiciary is therefore different than that of arbitrators, who are nominated for specific engagements and are more likely to be selected in future disputes if they appear reasonable and avoid decisions that are overly punitive.⁴⁷³ Those different incentives have to be taken into account if dispute resolution concerning investment moves toward a court system. How can such a system guarantee that its new judges will still have adequate incentives for high quality decision-making in the public interest?

It is also interesting to note the growing trend of empirical literature on investment-related disputes.⁴⁷⁴ Especially striking are the number of studies that are related to the question of why developing countries have negative sentiments concerning ISA.⁴⁷⁵ Most claimants are indeed investors from the developed world, and most claims are launched against developing states.⁴⁷⁶ The amounts claimed (but not necessarily the amounts awarded) are also rising to levels alarming to developing countries.⁴⁷⁷ And there seems to be some evidence of a bias in favor of investors from the North, even though the results of empirical studies are nuanced in this regard.⁴⁷⁸ Consequently, the subjectively negative perception of the ISA system is understandable, especially since arbitrators largely come from the North and have very strong connections to the corporate world to which the claiming investors are connected.⁴⁷⁹

For that reason, it is also not surprising that a large amount of literature deals with suggestions to reform the system, either within the current ICSID model or by moving toward alternatives.⁴⁸⁰ In that respect there is undoubtedly much more to be addressed; some ideas that warrant consideration exceed the scope of this paper, like the actual desirability and

468. See *supra* Part V.B.

469. See Rolland, *supra* note 244, at 390, 401.

470. Posner, *supra* note 40, at 39–40; see Kovacs, *supra* note 28, at 159.

471. Brown, *supra* note 402, at 677.

472. See POSNER, *supra* note 41, at 570.

473. *Id.* at 558–59.

474. See *supra* Parts IV & V.

475. See *supra* Parts IV.B & V.A.

476. See *supra* Part IV.B.

477. See *supra* Part IV.C.

478. See *supra* Part V.A.

479. Eberhardt & Olivet, *supra* note 134, at 36.

480. See Roberts, *supra* note 143, at 410.

empirical support for an investment court rather than the current ISA system, and whether such a court should be multilateral or bilateral. However, at the least, the theoretical Law and Economics literature and empirical studies reviewed in this paper both provide some support for development from the current *ad hoc* arbitration system to a more institutionalized investment court system. Though concrete issues relating to institutional design could not be discussed in any amount of detail at this stage, some of the literature introduced here—for instance, the remarkable publication by Brown—holds useful insights for those issues.

An interesting question is whether it is possible to develop a third way: A hybrid model between pure arbitration and a pure court system that would in some way or another keep “the best of both worlds.” Judicialization would have the economic advantage of generating public good as a result of transparent and public decision-making. But some of the advantages of the traditional arbitration system (like the higher expertise of arbitrators) could provide input for the reform of the system. For example, adjudication could take place via courts with independent judges specialized in investor-state arbitration, and parties would benefit from this capacity-building, relying on judges’ expertise for effective and speedy decision-making. On rendering their decisions, the judges would be providing a public good: transparent, precedential interpretation of the parties’ agreement. If those judges come from different regions of the world (and not only the “white” North) a higher degree of acceptability in the developing world could be virtually guaranteed. Moreover, under these conditions, decision-making could probably be even cheaper and speedier than under the current *ad hoc* arbitration model.

