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CLIENT ALERT

How Companies Can Use International Investment Agreements to Open Markets and Protect Their Investments

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Companies that operate internationally face an increasingly complex business environment, in large part because of uncertainty created by governments. Whether because of their political cultures and commitment to the rule of law, their international economic and foreign policies, or their use of state-controlled companies, governments are affecting markets in more ways and to a greater extent than they have in the past. To deal with this uncertainty, global companies need to do more than overcome the traditional business challenges. They also need to address the regulatory, policy, and geopolitical risks that governments create for them.

International investment agreements (IIAs) are one of the most effective tools for companies to manage this uncertainty. IIAs are government-to-government agreements – such as bilateral investment treaties (BITs) and the investment chapters of free trade agreements (FTAs) – that provide binding legal rules regarding one country's treatment of companies from another country and their investments. They typically protect a wide range of "investments" (such as companies, equity interests, debt instruments, contract rights, intellectual property rights, and licenses and permits) and apply to government action at both the federal level and the state and local level.

IIAs provide internationally engaged companies with a broad range of legal protections when they invest in challenging foreign markets, including the following:

- **National Treatment/Most-Favored Nation Treatment:** A government may not treat foreign companies or their investments any worse than it treats its own companies and investments or those of a third country. This means, for example, that a government may not subject an automotive manufacturing facility owned by a parent company in an IIA partner country to more stringent licensing requirements than it subjects to its own carmakers or those owned by third country investors.

- **Fair and Equitable Treatment:** A government must provide foreign companies' investments with "fair and equitable treatment," which generally includes due process in judicial and administrative proceedings and protection from arbitrary and capricious government treatment. So, for instance, if a machine tool company established a factory in a foreign country to produce for that market, but after two years the government of that country were to revoke the company's permits without providing an opportunity for judicial or administrative review, the company might have a valid claim that the host government failed to provide it "fair and equitable treatment."

- **Full Protection and Security:** A government must provide foreign companies' investments with "full protection and security," which means that it must offer a reasonable level of police protection and law and order to ensure the investments' physical and legal security." Thus, the government of a country experiencing civil unrest must take reasonable measures to prevent damage to a factory owned by a company headquartered in a country with which it has an IIA.

- **Expropriation and Nationalization:** A government may not expropriate or nationalize foreign companies' investments without paying compensation. This includes "indirect" expropriations, such as punitive tax measures that effectively deprive a company of the ability to run its business. For example, an oil services company with a subsidiary in an IIA partner country that is forced to pay "fines" for infractions of various environmental regulations equal to 200 percent of its annual revenue could have a claim that such a measure is an indirect expropriation for which it is entitled to compensation.

- **Performance Requirements:** A government may not mandate that foreign companies or their investments meet certain types of "performance requirements," such as requirements to use a certain amount of "local content," transfer technology to domestic producers, or purchase or use domestically developed technology. For instance, a government may not require that the local subsidiary of a medical device company of an IIA partner country transfer robotic prosthetic limb technology to its own health care companies or providers.

- **Umbrella Clause:** A government must comply with its contractual obligations to companies of their IIA partners and their investments; a failure to do is a breach of the IIA as well as of the contract. So, if a host government were to breach a contract term with the local subsidiary of a parent company of an IIA partner relating to the timing for zoning approvals, the parent company may be able to pursue relief under both the IIA and the contract itself.

Beyond these and other important rights, IIAs allow foreign companies to take governments to binding international arbitration for alleged breaches of the agreement. "Investor-State arbitration" is an extremely powerful tool for companies to enforce their IIA rights, for many reasons. First, it is **direct** – a company can take a government to arbitration without having to persuade its own government to espouse or otherwise support its claim. Second, it is **independent** – arbitrators are typically selected by both parties and hearings occur in a neutral international setting, both of which protect the company from the uncertainty of domestic court systems. Third, it is **flexible** – the company generally chooses the arbitration institution and rules, which gives it further influence over the process. Finally, it is **enforceable** – awards against host governments are generally enforceable in countries that have signed international agreements relating to the enforcement of foreign arbitration awards, such as the New York Convention.

In addition, companies may be able to use one or more IIAs to seek relief. In particular, some IIAs allow companies to pursue investor-State claims against a host government even if the company invests indirectly into a country through a third country (provided the company owns or controls both the third country subsidiary and the host country subsidiary that has been harmed by the government). Similarly, in some cases a parent company can initiate an investor-State claim through a subsidiary in another country that itself has an IIA with the host country (provided the third country subsidiary owns or controls the host country subsidiary).

In an increasingly uncertain global business environment, IIAs can help companies ensure that they are treated fairly, enjoy a level playing field, and can enforce their rights in difficult foreign markets. IIAs should be an important element of a company's business strategy throughout its investment activities, from its initial evaluation of the legal and political risks of investing in a market, to its decisions about how to structure its operations, to how it navigates local regulatory and policy hurdles, and, finally, to its efforts to constructively and effectively resolve disputes with the government that do arise.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

George D. Ruttinger
Partner – Washington, D.C.
Phone: +1 202.624.2670
Email: gruttinger@crowell.com

Ian A. Laird
Partner – Washington, D.C.
Phone: +1 202.624.2879
Email: ilaird@crowell.com