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This TDM Special feature "The Legacy & Lessons of Distressed & Failed Infrastructure Investments in the 1990s" was edited by:



**Dr. Ryan J. Orr**  
CRGP, Stanford University  
<http://crgp.stanford.edu/>



TDM is supported by the IBA and CEPMLP

## EDITORIAL

### The Legacy & Lessons of Distressed & Failed Infrastructure Investments in the 1990s - Introduction to the Special Issue

*Ryan J. Orr, Center for Research on Global Projects, Stanford University*

Over the past decade-and-a-half, the developing world has been witness to a boom-bust cycle of private investment in infrastructure projects—roads, power plants, water projects, railroads, and the like. Many projects that were initiated during the 1990s were subsequently renegotiated at a loss to investors or even abandoned. The General Counsels' Roundtable, formed under the aegis of the Collaboratory for Research on Global Projects at Stanford University, was established to examine the legacy and lessons of distressed and failed projects, with a special emphasis on the legal paradigm that supports such projects.

The Roundtable discussions—co-chaired by Professor Thomas C. Heller of the Stanford Law School and Barry Metzger, a senior partner of Baker & McKenzie and the former General Counsel of the Asian Development Bank—addressed several motivating questions. What were the factors that led to distressed and failed projects during the 1990s? Can we divine any trends? How did the renegotiations and workouts unfold? Can we "engineer" a more stable legal-contractual framework for emerging markets' infrastructure investments?

Participation in the Roundtable was by invitation only and involved senior legal advisors and business executives from a cross-section of project sponsors, investment funds, engineering firms, multilateral financial institutions, export credit agencies and private law firms as well as academics from across the disciplines of law, engineering, sociology, economics and political science.

In conjunction with the Roundtable, several background articles and proceedings documents were distributed to the participants. It is the purpose of this special issue to synthesize these various background articles and proceedings documents into a unified collection. The goal of disseminating the articles in this integrated format is both to make the material more accessible to a larger readership and to invite feedback.

The collection of articles presented here will be of interest to academics and practitioners interested in large-scale infrastructure development, long-term investment agreements, public-private partnerships, project finance, political risk management, renegotiation, dispute resolution, international arbitration, and bilateral investment treaties.

The first four articles were distributed in association with the first Roundtable, held January 20-21, 2005.

- Article One summarizes the rise and fall of private infrastructure in emerging markets during the 1990s, the subsequent wave of distressed and failed projects, and the global legal paradigm under which such projects have generally been arranged.

- Article Two offers a 100 page examination of the experience of independent power producers across thirteen developing countries during the 1990s; this innovative analysis took more than two years to complete and was supported by a global team of more than 15 researchers associated with the Stanford Program on Energy and Sustainable Development.
- Article Three reviews the extensive literature on the risks of private investment in infrastructure.
- Article Four summarizes key insights and implications from the First Roundtable, based on transcripts of the discussions.

Articles five through ten are those that were circulated in conjunction with the second Roundtable, held February 27-28, 2006.

- Article Five both summarizes the findings of the first Roundtable and reviews the incidence, determinants and resolutions of legal-contractual breakdowns in infrastructure investment agreements.
- Articles Six and Seven provide a rich empirical analysis of more than 1000 infrastructure concessions granted in Latin America and the Caribbean during 1985-2000, discuss policy implications based on evidence that more than 40% of these concessions were ultimately renegotiated, and illustrate the concessionaires logic when entering renegotiations.
- Article Eight compares the decisions of several recent ICSID tribunals, to examine whether ICSID interpretations of investor rights under bilateral investment treaties are converging on a stable regime for the protection of international property rights.
- Article Nine describes the new public management skills, procedures and institutions that government agencies can put in place in order to successfully implement public-private partnerships for infrastructure, and offers a benchmarking framework to measure progress within the key areas of transparency, public accountability and sustainable development, with the view that good governance can prevent investment disputes.
- The proceedings of the 2<sup>nd</sup> Roundtable are presented as Article Ten.

Article 11, prepared as a background paper for the third Roundtable, to be held April 27-28, 2007, reviews the changes in the investment landscape in the emerging markets since the end of the 1990s, the focal issue being the rise of "new players" from within the emerging markets themselves and the competition that this creates for traditional Western players.

The remaining articles, although not presented at the Roundtable, are included here because they are

of great relevance to the topic of private infrastructure investment in emerging markets.

- Based on the study of more than 1000 infrastructure concessions in the Latin America and the Caribbean cited above, Articles 12, 13 and 14 respectively, test the impact of regulation of private infrastructure operators on sector performance, estimate the returns that investors in private infrastructure projects really made, and review the impact of price cap regulation on costs of capital, tariff-rates and levels of investment.
- Finally, Article 15 and 16 assess the evolving system of international arbitration under the BIT framework, the first offers a detailed analysis of the multi-factor approach adopted by the Tribunal of the *Azurix vs. Argentina* arbitration, and the second reviews an email discussion that played out on the OGEMID electronic discussion list under the title, "Do Investors now Ignore BITs?"



**Dr. Ryan J. Orr**  
 Collaboratory for Research on  
 Global Projects  
 Peterson Lab, Room 556i  
 Stanford University  
 Stanford, CA 94305-4020  
<http://crgp.stanford.edu/>

#### **About Collaboratory for Research on Global Projects (CRGP)**

CRGP is a collaborative undertaking between Stanford University, partner universities, private industry, and government affiliates, to advance the science and practice of planning and implementing large, complex, global projects. CRGP serves as Stanford University's primary forum for research on the organizational, legal, financial, political, social, institutional and project management aspects of global projects, and the linkages and interdependencies between various project design parameters.

The word "Collaboratory" literally means "multiple laboratories" and part of the vision of CRGP is to support a worldwide network of researchers and practitioners across the disciplines of engineering, law, sociology, economics, and finance. CRGP researchers use multiple research frameworks- ethnographic, case study, survey and computational modeling- to develop, test and deploy innovative theories, methodologies and tools.

Results of CRGP research enable leaders in government and industry to analyze and design the organizations and institutions needed to deliver complex global projects more effectively, with more sustainable outcomes.

# Legacy & Lessons of Distressed & Failed Infrastructure Investments in the 1990s

## 1. The Legacy of Failed Global Projects: Testing the Legal Paradigm

*Barry Metzger,  
Baker & McKenzie LLP*

This introductory article sets the context for subsequent articles in this special issue and introduces the notion of failed and distressed projects and the concept of the global legal paradigm. The 1990s saw an explosive growth of private infrastructure projects in emerging markets. However, a number of these projects were cancelled (failed projects) and a large number of others went through major renegotiations (distressed projects). While significant research and analysis have been done to look at these failures from administrative and public policy angles, there is little information on the roles in these failures of the legal structures and how these legal structures can be changed to improve project success rates.

Though they differ in details, the legal structures of global projects share many common attributes-(1) evaluation of the domestic legal framework and context in the host country, (2) allocation of risks and alignment of incentives with contractual structures, (3) choice of law provisions, (4) arbitration and other dispute resolution mechanisms, and (5) measures to increase transparency-which together may be called the global projects legal paradigm.

This article is provocative in nature, and puts forward more questions than it does answers, as a way to stimulate discussion, debate and future research on the global legal paradigm, and to set the context for the 1<sup>st</sup> General Counsels' Roundtable, to be held in January 2005 at Stanford University.

[Full article here](#)

## 2. The IPP Experience in Developing Countries

*Erik J. Woodhouse*

The lessons of the turbulent 1990s boom in private participation in infrastructure remain opaque. In response, the Program on Energy & Sustainable Development at Stanford University undertook a detailed review of the global experience with independent power projects-privately developed power plants that sell electricity to a public grid-in developing countries.

The study covered thirteen countries and thirty five projects, and sought to identify the key factors

that affected outcomes across these projects. Broadly speaking, the quality of the IPP experience reflected systemic risks that exist at the level of countries, such as macroeconomic shock, electricity supply-demand balance, or nontransparent fuel markets. Notably, the sector reform efforts that were intended to mitigate these risks, in most cases, exacerbated problems by tilting the playing field against new private entrants to the historically closed electricity markets. In this environment, classic risk management methods, such as "ironclad" contracting, demand for sovereign guarantees, or resort to international arbitration, were necessary but not sufficient to protect outcomes. Rather, success rested on measures that sought to identify and reduce vulnerability to specific risks, such as reliance on transparent project procurement, effective integration of local and multinational partners, and approaching renegotiations as a possible pareto-improving process.

Some of the keys to success, such as transparent bidding, aligning incentives among stakeholders, and developing IPPs slowly, can be implemented in most cases. However, other critical factors, such as managing renegotiations, navigating foreign fuel markets and regulatory environments, and weathering stress, are open to a smaller class of investors. Many of these are domestic firms, or foreign firms committed to long-term presence in developing countries. With competition curtailed and reform generally moving slowly, it remains to be seen whether investment from this limited class will be sufficient to meet demand.

A refined version of this article is published in *New York University Journal of International Law & Politics* under the title "The Obsolescing Bargain Redux? Foreign Investment in the Electric Power Sector in Developing Countries" Volume 38, 121, (2005-06).

[Full article here](#)

## 3. Private Risk in Infrastructure

*Dr. Ashwin Mahalingam,  
The Indian Institute of Technology, Madras*

*Dr. Julie Kim,  
Rand Corporation*

Despite the setbacks of the 1997 Asian Financial Crisis, the volume of private investment in large-scale infrastructure projects has grown rapidly throughout the world over the past few decades. However, a review of this experience indicates that such projects have had a history of subjecting participants to major risks and in some cases, risks have translated into distressed and cancelled projects.

This article reviews the extensive literature on the risks of private investment in infrastructure and identifies four major categories of risks-social/environmental, host country/political, economic/financial and technological. It then reviews

the global projects legal paradigm, the model that private investors have traditionally adopted to systematically enumerate, allocate and guard against each of the possible risks. While this paradigm has been successful in mitigating many of the risks, it has also had its share of breakdowns, thus, the search must continue for a more robust paradigm. The objective of the paper is to expose and sensitize researchers and practitioners concerning the risks prevalent in private participation in infrastructure; and to summarize extant knowledge on risk mitigation techniques and lay some groundwork for future research in the area of risk management for private infrastructure.

↳ [Full article here](#)

#### 4. The Legacy of Distressed and Failed Projects, A Review and Reconceptualization of the Legal Paradigm (Proceedings 1)

Ryan J. Orr,  
Center for Research on Global Projects, Stanford University

Barry Metzger,  
Baker & McKenzie LLP

This article offers a summary of the proceedings of the 1<sup>st</sup> General Counsels' Roundtable organized by the Collaboratory for Research on Global Projects at Stanford University in January 2005. The Roundtable brought together lawyers and business executives from different sectors and academics from different disciplines to discuss the legal challenges of private infrastructure projects in emerging markets over the past decade. A central conclusion is that the legal paradigm of these global projects has not fared well. More often than not, the contractual arrangements of these projects were renegotiated, contested or cancelled. The roundtable participants identified 13 factors that contributed to distressed and failed global projects: changes in political leadership, currency exchange, public sentiment and demand for project services are frequent forces of distress. The roundtable then turned to discuss what could be done differently, and identified two future directions that the legal paradigm for global projects might follow: 1) The "*governance/partnership model*" aimed toward more built-in flexibility for the project contracts, in which possibilities and needs for changes are acknowledged, and processes for renegotiation and adjustment are established; 2) the less radical "*components approach*" which seeks to add components and structural elements (patches) into the project legal framework to address problems frequently encountered in distressed projects. Different potential components were identified. The roundtable also discussed how the increasingly popular private public partnership may be an embodiment of the governance model. Finally, important areas for further research on global project legal paradigm were proposed.

↳ [Full article here](#)

#### 5. Investment in Foreign Infrastructure: The Legacy & Lessons of Legal-Contractual Failure

Ryan J. Orr,  
Center for Research on Global Projects, Stanford University

This article was prepared as a background paper for the 2<sup>nd</sup> General Counsels' Roundtable organized by the Collaboratory for Research on Global Projects at Stanford University in February 2006. Following the research directions laid out in the 1<sup>st</sup> Roundtable, the 2<sup>nd</sup> Roundtable was organized to assemble a set of leading experts with experience in the renegotiations and resolutions of disputes that played out during the 1990s following widespread breakdowns in long-term private infrastructure investment agreements.

This article provides context for the analysis, in the form of a literature review with three main topics: the *incidences* of legal-contractual failures, the *determinants* of legal-contractual failures, and *approaches to resolving* legal-contractual failures. The article aims to broaden our *descriptive* understanding of how and why foreign infrastructure investments failed or were renegotiated, and to deepen our *normative* understanding of how the current approaches and strategies to the structuring of foreign infrastructure investments can be improved.

↳ [Full article here](#)

#### 6. Granting & Renegotiating Infrastructure Concessions: Doing it Right

Jose Luis Guasch,  
World Bank

Countries in the Latin American and Caribbean region now have a wealth of experience in the process of infrastructure reform, as the process of concessioning operations to the private sector and setting up regulatory regimes and agencies started in the mid-1980s. Most of those concessions have had positive outcomes, showing extensive improvements in operating efficiency, quality of service, and service provision. Yet a number of recurrent problems, such as limited sharing by users of the efficiency gains, pervasive conflicts and renegotiations, and weak regulatory effectiveness (for example, failure to benefit the poor) have led to concerns about the concessions model and calls for its evaluation. This book takes up that call by assessing the design of concessions, the regulatory framework, the high incidence of contract renegotiation, and implications for infrastructure performance and overall welfare. The premise is that the model and conceptual framework are appropriate, yet the problems have been in faulty design and implementation that can be improved.

The book uses data from more than 1,000 concessions in infrastructure in Latin America and

the Caribbean granted during 1985-2000, analyzing the incidence and determinants of renegotiation as a proxy for performance. It concludes that while more than 40% of concession contracts have been renegotiated-and more than 70% in the water and transport sectors, that not all renegotiation is undesirable and that some should be expected and is even welfare enhancing. Opportunistic renegotiation, however, should be discouraged.

The key issue is to design better concession contracts and to induce both parties to comply with the agreed-upon terms to secure long-term sector efficiency and vigorous network expansion.

↳ [Full article here](#)

## 7. Renegotiation of Infrastructure Concessions: An Overview

*Stéphane Straub,  
University of Edinburgh*

*Jose Luis Guasch,  
World Bank*

Latin American infrastructure concession contracts in the 1990s have been plagued by numerous renegotiations, to the point that prior private investors are questioning any future involvement in infrastructure in some countries in that region. This issue has been analyzed in a series of papers by Guasch et al. (2003, 2006a, 2006b). After putting these contributions in the context of the theoretical and empirical literature on contract renegotiation, this note surveys the existing evidence on the determinants of these renegotiations and discusses the main policy implications regarding the necessity of efficient regulatory institutions and the adequate type of price regulation.

This paper formulates the theory of the behavior of concessionaires and their response to opportunity to negotiate.

↳ [Full article here](#)

## 8. A Review of ICSID Decisions Suggesting an International Property Right in Foreign Investments

*Aaron M. Nathan,  
Stanford Law School*

Recent ICSID decisions seem to point in the direction of a developing regime of international property rights held by investors against states in which they invest. The move away from diplomatic protection, into the network of bilateral investment treaties (BITs), along with the jurisprudence of the ICSID tribunals, are beginning to represent a body of legal doctrine that, at least on its face, allows international investors to establish treaty rights that are held directly by themselves.

The overarching legal question is whether the BIT framework generates property and contract rights that can be enforced against the state? This paper is a brief and preliminary analysis of some of the recent ICSID decisions, particularly which aims first to discuss the doctrinal developments in the ICSID jurisprudence interpreting BITs, while at the same time offering some initial considerations about whether the ICSID jurisprudence, together with the BIT framework, is converging on an international property regime for the protection and stabilization of investment rights.

↳ [Full article here](#)

## 9. Governance in Public-Private Partnerships for Infrastructure Development

*United Nations Economic Commission for Europe,  
<http://www.unece.org/>*

This article was prepared in collaboration with experts of the Public Private Partnership (PPP) Alliance of the United Nations Economic Commission for Europe (UNECE), an organization that has been working with PPPs since the 1990s and that was a pioneer in creating the basic building blocks of PPPs. PPPs are becoming increasingly commonplace for infrastructure development. However, during the course of their development and operation, such projects frequently encounter problems resulting from a lack of governance, which decreases the benefits - fiscal, social and economic etc. - that can be drawn and increases the risks - political, contractual and financial, etc. Improving governance can help maximize the benefits and minimize the risks in PPPs. Improvement in governance requires governments to acquire new skills in public management and to establish new institutions and procedures. Governments will need to focus on supervision and regulation, rather than on direct ownership and controls.

In addition to these new skills, new sources of expertise and qualifications are required to ensure that PPPs also contribute to sustainable development. Acquiring these new public management skills, however, is not easy. One technique to assist governments and the private sector to acquire this new expertise is through benchmarking best practices in specific projects. Benchmarking of the procedures and practices involved in delivering PPP projects can highlight what needs to be done to meet the new public management standards. Currently, there are few, if any, mechanisms for benchmarking the achievement of governance in PPP projects.

This article puts forward an innovative benchmarking scheme whereby progress within the key areas of transparency, public accountability and sustainable development can be measured. This article has been iteratively refined based on reviews at the Forum on "Good Governance in PPPs for Infrastructure Development (Nov. 17, 2003), Palais des Nations Geneva, at the 3<sup>rd</sup> Meeting of the PPP Alliance in Barcelona, Sep. 2004, at a meeting of

experts under the auspices of the Canadian Council for PPPs and with the government of Canada in Toronto in Nov. 2004, and finally at the 4th meeting of the PPP Alliance in London, Oct. 2005. This article is still a working document and feedback is welcomed and will be used to enhance the final publication.

↳ [Full article here](#)

## 10. Understanding Renegotiation and Dispute Resolution Experience in Foreign Infrastructure Investment (Proceedings 2)

*Ryan J. Orr,  
Center for Research on Global Projects, Stanford University*

*Seth M.M. Stodder,  
Akin Gump Strauss Hauer & Feld LLP*

This article summarizes the proceedings of the 2<sup>nd</sup> General Counsels' Roundtable held on February 10 and 11, 2006 at Stanford University. While the First Roundtable highlighted the dismal performance of long-term infrastructure investment contracts, the discussions provided little detail with regard to how the renegotiation experiences had actually transpired or how international standards for dispute resolution are being formulated. Building on the progress of the 1st General Counsels' Roundtable, the 2nd Roundtable was convened to critically analyze the experience of legal failures-default or renegotiation-between foreign investors, host governments and other involved parties when infrastructure projects have become distressed, and to inform future public policy and project design.

This proceedings document reviews the attractions and vagaries of international arbitration under bilateral investment treaties, provides a critical analysis of both the *CMS vs. Argentina* and the Dulles Greenway cases, discusses the trade-offs between risk reduction and allocation, recognizes the reality that while projects are designed on a one-off basis failures tend to occur in clusters, and proposes a strategy to simultaneously create flexibility and certainty in long-term investment contracts as an approach to cope with changed conditions in the long-run.

This last item proposes a union of the governance and components models put forward in the first proceedings document.

↳ [Full article here](#)

## 11. Emerging-Market Infrastructure Investors: New Trends for a New Era?

*Ryan J. Orr,  
Center for Research on Global Projects, Stanford University*

*Kassia Yanosek,  
BP*

*Gregory Keever,  
Akin Gump Strauss Hauer & Feld LLP*

After two rounds of General Counsels' Roundtable at Stanford University on the legal paradigm of infrastructure investment in emerging markets, it was agreed that the investment landscape in these emerging markets has been changing rapidly since the last few years of the 1990s. Toward the end of the decade, there were increasing numbers of investments by new players from developing countries - i.e. "South-South investment" - creating new challenges and opportunities both to host governments and traditional Western players. This article provides an evidence-base analysis confirming support for this trend using data from the World Bank **Private Participation in Infrastructure** (PPI) Project Database.

This article also tests the hypothesis that public-private co-ownership of infrastructure projects is increasing, and finds support for this phenomenon in the Asian region - especially in the power and water sectors - but not in the African region. Finally, anecdotally-based observations of the attitudes and behaviors of the new South-South investors are provided, with an emphasis on projects being sponsored by Chinese investors.

*"Emerging-Market Infrastructure Investors: New Trends for a New Era?" Kassia Yanosek, Gregory Keever, and Ryan J. Orr was previously published in "The Journal of Structured Finance", Winter 2007 edition. © Copyright 2007 Institutional Investor Inc. Republished with kind permission. Visit [www.ijournals.com](http://www.ijournals.com) for more information and subscription details.*

↳ [Full article here](#)

## 12. Does Regulation and Institutional Design Matter for Infrastructure Sector Performance?

*Stéphane Straub,  
University of Edinburgh*

*Luis Alberto Andres,  
World Bank*

*Jose Luis Guasch,  
World Bank*

This paper tests the impact of regulation of private infrastructure operators on sector performance, from three separate angles. The findings are that: (i) the quality of regulation is found to be a significant determinant of the divergence between the overall profitability of the concession and its corresponding hurdle rate-cost of capital, explaining around 20% of the variation. However, regulatory efforts seem to be more closely associated with keeping tariffs as low as possible for current consumers, than keeping profitability well aligned with hurdle rates of return; (ii) price caps led a significant increase of the probability of renegotiation; (iii) the existence of regulator at signing of contract reduces renegotiations; (iv) the regulators filter and dissuade opportunistic private operator led renegotiation; (v) in the case of Government-led renegotiation, the regulator acts as barrier against political opportunism; (vi) the impact of regulator is stronger in weak governance environments; and (vii) the differences in the private sector participation in infrastructure outcomes are explained to some extent by differences in the concession design and quality of the regulatory design. But the overall message is that indeed regulation matters.

[Full article here](#)

## 13. How Profitable are Private Infrastructure Concessions in Latin America? Empirical Evidence and Regulatory Implications

*Sophie Sirtaine,  
World Bank*

*Maria-Elena Pinglo,  
International Finance Corporation*

*Vivien Foster,  
World Bank*

*Jose Luis Guasch,  
World Bank*

The aim of this study is to estimate the returns that private investors in infrastructure projects in Latin America really made on their investments, to assess the adequacy of these returns relative to the risks taken, and the impact that the quality of regulation had on those returns. The study estimates

both historical and projected future returns earned by a sample of private infrastructure concessions, across a variety of Latin American countries and infrastructure sectors, and compares them against expected returns given the level of risk taken. In addition, the study examines the extent to which the quality of the regulatory framework put in place at the time of privatization contributed to maintaining a closer alignment between rates of return and hurdle rates. Two sets of returns are computed: first, "financial returns," resulting from the distribution of dividends from the concession to the concessionaires' parent companies (mostly abroad); and second, "adjusted returns," that include indirect forms of dividends.

The analysis shows that concessions are capable of generating adequate returns in the long term, and are therefore potentially interesting business proposals. Concessions in the water sector appear relatively the least attractive, while concessions in the telecommunication sector appear to be the most profitable overall. On average, concessions seem to become profitable after about 10 years of operation. However, about 40 percent of the sample concessions do not seem to have the potential to generate attractive returns, this number climbing to 50 percent in the energy and transport sectors. The analysis also highlights that returns (in particular shareholder returns) are highly volatile across sectors, concessions, and from year to year. Thus infrastructure concessions in Latin America are a high risk investment proposal, explaining why the required rates of return are so high.

Finally, the analysis investigates the quality of the regulatory regimes faced by concessionaires and finds that these do not score very highly on average, that there is a high variance in the quality of regulatory frameworks, and that the quality of regulation is a significant determinant of the divergence between initial hurdle rate and eventual concession profitability.

[Full article here](#)

## 14. Price Caps, Efficiency Payoffs, and Infrastructure Contract Renegotiation in Latin America

*Antonio Estache,  
World Bank*

*Lourdes Trujillo,  
Universidad de las Palmas de Gran Canaria*

*Jose Luis Guasch,  
World Bank*

Twenty years ago, as the United Kingdom was getting ready to launch the privatization of its public services, Professor Littlechild developed and operationalized the concept of price caps as a regulatory regime to control for residual monopoly conditions in these services. Ten years later, Latin American countries, as they embarked into their own

infrastructure reforms, also adopted the price cap regulatory model.

Relying on a large data base on the factors driving contract renegotiation in the region and a survey of the literature on efficiency gains, Estache, Guasch, and Trujillo assess the impact of this regulatory regime in Latin America. They show that while the expected efficiency gains were amply achieved, these gains were seldom passed on to the users. Instead they were shared by the government and the firms. Moreover, the adoption of price caps implied higher costs of capital and hence, tariffs, and brought down levels of investment.

↳ [Full article here](#)

## 15. Legitimate Regulation vs Regulatory Expropriation in Public Infrastructure Investments after *Azurix*: A Case Study

*Francesco Costamagna,  
Università Commerciale L. Bocconi of Milan*

*Azurix v. Argentina* represents the first case in which an international arbitral tribunal decided on the merit of a disputed water privatization. The dispute was brought about by the US-based water firm *Azurix*, which sought compensation for losses related to measures adopted by the Buenos Aires Province. The ICSID Tribunal was required to deal with a number of highly controversial issues. This comment focuses on the expropriation claim put forward by *Azurix* and it analyses the multi-factor approach adopted by the Tribunal to complement the international doctrine on regulatory expropriation. The latter rests on the effect doctrine/policy powers exception to determine the distinction between legitimate regulation and regulatory expropriation.

The *Azurix* Tribunal found it insufficient, notably with regard to public utilities, and sought to complement it by resorting to the proportionality test, although, so far, the tool has played little part in the international arbitral practice. Its adoption would seemingly help to find a better balance between public interest and investors' rights, by bringing within the same framework both quantitative and qualitative considerations. The *Azurix* Tribunal also took into consideration investor's legitimate expectations, as an additional factor to assess the substantiality and the reasonableness of State's interference. In the end, the Tribunal held that no expropriation had occurred, finding the impact of *Argentina's* measures to fall below the required severity threshold.

Yet, the multi-factor analysis articulated in this Award allows for a more balanced approach toward a highly sensitive topic, which is likely to represent a major challenge for the international investment protection regime.

↳ [Full article here](#)

## 16. The Impact of BITs on FDI: Do Investors Now Ignore BITs?

*Ryan J. Orr,  
Center for Research on Global Projects, Stanford University*

On Nov. 29, 2006, an email post by Susan Rose-Ackerman under the title "The Impact of BITs on FDI-One More Time" on the OGEMID electronic discussion list initiated a pleasant and informative cascade of follow-on discussion and debate. After seven responses to Susan's initial email, a second thread of more than ten emails were transmitted under the title, "Do Investors now Ignore BITs?"

This article offers a two-page synopsis and a transcript of this string of discussions. Major points raised in the dialogue are as follows: Empirical work by Rose-Ackerman & Tobin and Yackee suggests that while BITs encourage FDI into host countries, the marginal impact on an individual country decreases - or even disappears - as the overall number of BITs worldwide grows; second, disentangling a BIT or even its individual components from the overall investment regime of a host state is an extremely difficult undertaking; third, from the perspective of large multinational firms the existence of a BIT may be irrelevant because these firms have sufficient bargaining power to negotiate a legal framework that is a complete substitute for a BIT; fourth, the existence (or lack of) a BIT plays a negligible, if any, role in investors' decisions to commit capital; fifth, the excessive costs of BIT arbitrations, both in terms of legal fees and time to obtain a remedy, are limiting the growth and usefulness of the system; and finally, despite the challenges facing the investor-state system, there is more awareness of the benefits of BITs today than ever before.

↳ [Full article here](#)

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