

Corruption and Illegality in East and South Asian Investment Agreements: An Empirical Analysis

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1. Introduction

- Asian countries seem to be striving to curb corruption and other similarly serious illegal misconduct.
 - 23 Asian states are members of the Anti-Corruption Initiative for Asia and the Pacific (ACIAP) established by OECD and ADB.
 - All Asian countries (excluding North Korea) have adopted the United Nations Convention against Corruption addressing the supply and demand sides.
 - Almost all Asian countries have domestic legislation prohibiting corruption and bribery.
- BUT corruption and bribery remain real in Asia.
 - Transparency International's Corruption Perceptions Index (TICPI) and the World Justice Project's Rule of Law Index (WJPLI) indicate that corruption and poor governance are still prevalent across Asia.
 - **Especially, Asia still seems to have difficulty controlling FDI-related corruption through international investment agreements (IIAs).**

- So there appears to be some ambivalence in Asian states' approach towards corruption and other serious misconduct in FDI.
 - They have engaged with general anti-corruption initiatives. BUT, for FDI, they have signed IIAs that are not always effective for anti-corruption.
 - Only 45 out of 2584 IIAs concluded before 2012, and 16 out of 89 IIAs signed after 2021, contained express anti-corruption clauses.
 - Legality requirements on foreign investors are pervasive in IIAs in Asia. Host states may invoke such requirements to deprive the corrupting investors of investment protection, including the jurisdiction of the ISDS tribunal. → No real sanctions against bribed host states.
- **Why this ambivalence? Is it rational, serving individual national interests? Or is it the 'bounded rationality' particularly of transitioning economies** suggested by Lauge N Skovgaard Poulsen in relation to signing up to the modern investment treaty regime?
 - **Our paper primarily investigates this empirically; but also**
 - **Can be used (normatively) for IIA drafters, advisors, researchers & international organisations trying to be rational.**

2.1 Methodology

- The empirical analysis uses data collected from UNCTAD's International Investment Agreements Navigator (the Navigator).
 - We gathered information on anti-corruption provisions and legality requirements in IIAs concluded by select countries in East and South Asia – China, South Korea, Japan, ASEAN countries (excluding East Timor) and India.
 - We used the details and texts of Bilateral Investment Treaties (BITs) and Treaties with Investment Provisions (TIPs) provided by the Navigator until 31 December 2023, which are 'in force', 'signed' and 'terminated' by that time. But our analysis focuses on BITs as stronger evidence of a party's rational strategy or otherwise.
 - We also used the Electronic Database of Investment Treaties (EDIT) by the World Trade Institute at the University of Bern to supplement missing information.

2.2 Hypotheses

- Then, we tested the following hypotheses to see if the select Asian countries have concluded IIAs rationally.
- **Re: anti-corruption provisions**
 - **Hypothesis I (H-I):** Net FDI-exporting states* are likely to adopt anti-corruption provisions in IIAs, to protect their outbound investors from corruption in investment destinations; net FDI-importing states are unlikely to be keen to conclude those provisions to avoid further liability.
 - **Hypothesis I-A (H-IA):** However, a subset of net FDI importers with very little domestic corruption will not hesitate to agree to anti-corruption clauses as these provisions will not practically affect their obligations under IIAs.

- **Re: legality clauses**

- **Hypothesis II (H-II):** Net FDI-exporting states* are reluctant to agree to IIAs containing legality clauses, to protect their outbound investors (because host states may use such clauses as defences against corruption claims), whereas net FDI-importing states (with significant domestic corruption and inbound ISDS disputes) will likely conclude legality clauses to protect their finances (and perhaps at least some officials).
- **Hypothesis II-A (H-IIA):** A subset of net FDI-exporting states with significant domestic corruption and inbound ISDS cases are more willing to adopt legality provisions to protect themselves from inbound ISDS claims for compensation under the IIA, despite such clauses disadvantaging their outbound investors bringing claims.
- **Hypothesis II-B (H-IIB):** A subset of net FDI-importing states with very little corruption are less prone to adopt legality provisions as they do not significantly increase their chances of successfully defending inbound ISDS claims.

* Classification of legality clauses

- Article 1.1 of the United Arab Emirates-Vietnam BIT (2009) provides that:
The term “investment” shall mean every kind of asset in the territory of one Contracting Party invested by an investor of the other Contracting Party in accordance with the laws and regulations of that former Contracting Party ...
→ This provision provides robust protection for the host state where the home state’s investor commences arbitration. We call legality provisions of this kind “direct legality clauses (provisions)”.
- BUT (1) ‘legality in the scope of application clauses’, (2) ‘legality in the [promotion and] admission of investment clauses’ and (3) ‘legality requirements linked to the substantive standards of investment protection’ require foreign investors to follow the home states’ domestic laws indirectly and thus offer less protection for the host state.

* FDI-Exporting States v FDI-Importing States?

• FDI Exporting Countries

	Japan	South Korea	Brunei (?)
Outbound Stocks (million USD)	1 948 555.4	647 568.0	N/A
Inbound Stocks (million USD)	225 367.1	272 328.0	6 797.8

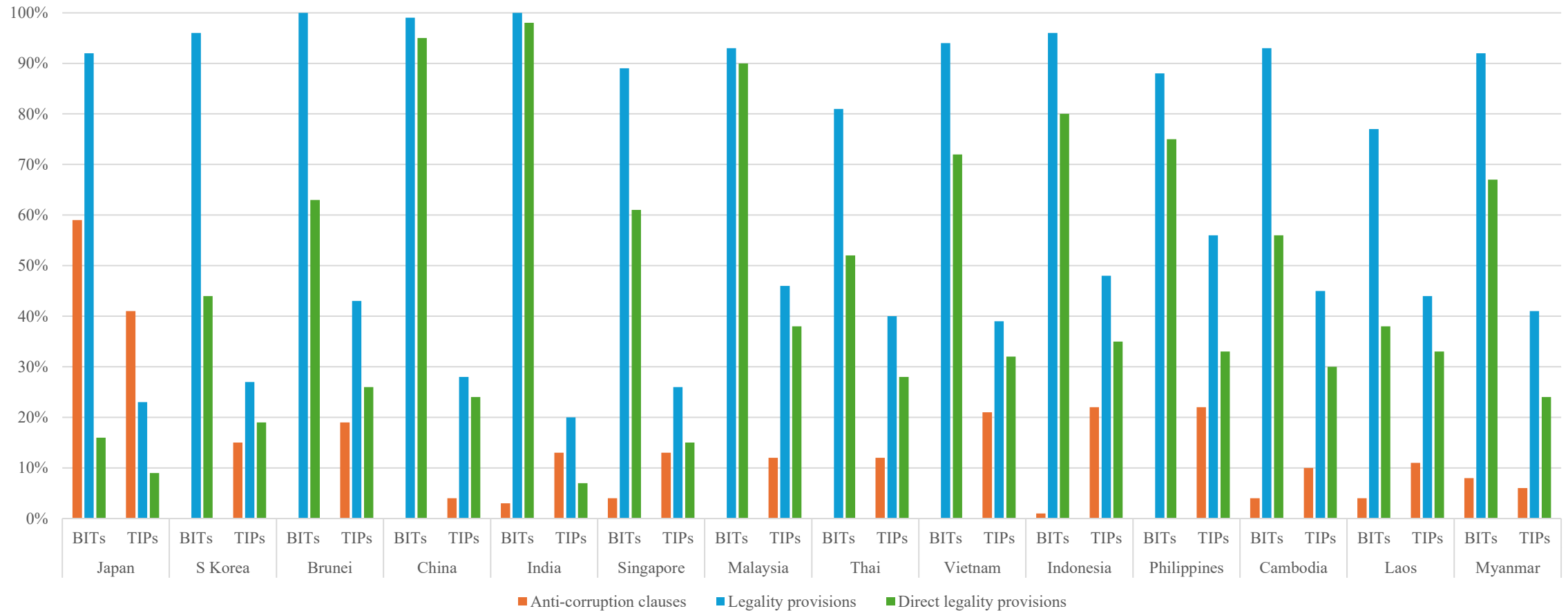
• FDI Importing Countries

	China	Cambodia	Indonesia	Laos	Malaysia
Outbound Stocks (million USD)	2931 653.0	1 418.4	103 941.2	94.7	137 654.7
Inbound Stocks (million USD)	3822 449.4	44 537.1	262 920.0	12 736.0	199 205.9

	Myanmar	Philippines	Singapore	Thailand	Vietnam	India
Outbound Stocks (million USD)	N/A	67 280.1	1 595 380.9	179 828.1	14 545.0	222 556.8
Inbound Stocks (million USD)	38 427.5	112 964.6	2 368 396.2	306 163.0	210 471.3	510 718.5

3. Anti-Corruption Provisions and Legality Clauses in IIAs

Graph 1: IIAs Containing Anti-Corruption Clauses and Legality Provisions (Ratio)



3.1 FDI-Exporting Countries: Their Compatibility with Hypotheses

	Japan		South Korea	
IIAs (Number)	BITs (37)	TIPs (22)	BITs (105)	TIPs (26)
Number (and ratio) of treaties having anti-corruption provisions	22 (59%) [H-I]	9 (41%) [moderate H-I]	0 (0%) [not H-I]	4 (15%) [not H-I]
Number (and ratio) of treaties having legality clauses	34 (92%) [not H-II]	6 (27%) [H-II]	101 (96%) [H-IIA]	7 (27%) [not H-IIA]
Number (and ratio) of treaties having direct legality clauses	6 (16%) [H-II]	2 (9%) [H-II]	46 (44%) [moderate H-IIA]	5 (19%) [not H-IIA]

- [] – The country’s compliance with the hypothesis. H-I is Hypothesis I, H-II is Hypothesis II, and so on.
- **50% as the dividing line for (dis)satisfaction** and 30% for moderate (dis)satisfaction.
- **Black shading** – rational behaviour for direct legality provisions in BITs.
- **Dark shading** – rational behaviour for anti-corruption provisions in BITs.
- **Light shading** – rational behaviour for any legality clauses in BITs.

* Japan

- Japan's approach to anti-corruption and legality clauses appears to be rational, although it was slow to expand its IIA programme.
 - Accelerated BIT signings from Second Abe Administration (2012-2020).
- But Japan maybe influenced by status quo bias: still using anti-corruption provisions whose effects need more scrutiny, viz
 - Article 10 of the Cambodia-Japan BIT (signed in 2007) states: “Each Contracting Party shall ensure that measures and efforts are undertaken to prevent and combat corruption regarding matters covered by this Agreement in accordance with its laws and regulations”.
 - Such ‘best efforts’ clauses are in 22 (59%) out of 26 BITs signed by Japan.

3.2 FDI-Importing Countries: Their Compatibility with Hypotheses

	China		India		Singapore	
IIAs (Number)	BITs (145)	TIPs (25)	BITs (86)	TIPs (15)	BITs (54)	TIPs (39)
Number (and ratio) of treaties having anti-corruption provisions	0 (0%) [H-I]	1 (4%) [H-I]	3 (3%) [H-I]	2 (13%) [H-I]	2 (4%) [not H-IA]	5 (13%) [not H-IA]
Number (and ratio) of treaties having legality clauses	143 (99%) [H-II]	7 (28%) [not H-II]	86 (100%) [H-II]	3 (20%) [not H-II]	48 (89%) [not H-IIB]	10 (26%) [H-IIB]
Number (and ratio) of treaties having direct legality clauses	138 (95%) [H-II]	6 (24%) [not H-II]	84 (98%) [H-II]	1 (7%) [not H-II]	33 (61%) [not H-IIB]	6 (15%) [H-IIB]
	Malaysia		Thailand		Vietnam	
IIAs (Number)	BITs (71)	TIPs (26)	BITs (42)	TIPs (25)	BITs (67)	TIPs (28)
Number (and ratio) of treaties having anti-corruption provisions	0 (0%) [H-I]	3 (12%) [H-I]	0 (0%) [H-I]	3 (12%) [H-I]	0 (0%) [H-I]	6 (21%) [H-I]
Number (and ratio) of treaties having legality clauses	66 (93%) [H-II]	12 (46%) [moderate H-II]	34 (81%) [H-II]	10 (40%) [moderate H-II]	63 (94%) [H-II]	11 (39%) [moderate H-II]
Number (and ratio) of treaties having direct legality clauses	64 (90%) [H-II]	10 (38%) [moderate H-II]	22 (52%) [H-II]	7 (28%) [not H-II]	48 (72%) [H-II]	9 (32%) [moderate H-II]

3.2 FDI-Importing Countries: Their Compatibility with Hypotheses (cont'd)

	Indonesia		Philippines		Cambodia	
IIAs (Number)	BITs (74)	TIPs (23)	BITs (40)	TIPs (18)	BITs (27)	TIPs (20)
Number (and ratio) of treaties having anti-corruption provisions	1 (1%) [H-I]	5 (22%) [H-I]	0 (0%) [H-I]	4 (22%) [H-I]	1 (4%) [H-I]	2 (10%) [H-I]
Number (and ratio) of treaties having legality clauses	71 (96%) [H-II]	11 (48%) [moderate H-II]	35 (88%) [H-II]	10 (56%) [H-II]	25 (93%) [H-II]	9 (45%) [moderate H-II]
Number (and ratio) of treaties having direct legality clauses	59 (80%) [H-II]	8 (35%) [moderate H-II]	30 (75%) [H-II]	6 (33%) [moderate H-II]	15 (56%) [H-II]	6 (30%) [moderate H-II]
	Laos		Myanmar			
IIAs (Number)	BITs (26)	TIPs (18)	BITs (12)	TIPs (17)		
Number (and ratio) of treaties having anti-corruption provisions	1 (4%) [H-I]	2 (11%) [H-I]	1 (8%) [H-I]	1 (6%) [H-I]		
Number (and ratio) of treaties having legality clauses	20 (77%) [H-II]	8 (44%) [moderate H-II]	11 (92%) [H-II]	7 (41%) [moderate H-II]		
Number (and ratio) of treaties having direct legality clauses	10 (38%) [moderate H-II]	6 (33%) [moderate H-II]	8 (67%) [H-II]	4 (24%) [not H-II]		

* China

- The pattern in China's BITs suggests quite rational behaviour considering the country's FDI-importing country status (for now).
 - China has a large BIT network: 145 treaties.
 - No BITs contain anti-corruption provisions, whereas 138 BITs (95%) contain direct legality clauses.
- But it would be rational for China to transition away from legality provisions to protect its increasing outbound investors when the outbound FDI stocks exceed the inbound stocks (many years later).
 - 'One Belt One Road' initiative sharply increased Chinese FDI abroad after 2013.
 - FDI into China has fallen dramatically since (before) the COVID-19 pandemic.

* Singapore

- Singapore's BIT approach to anti-corruption clauses appears to be irrational, probably influenced by some status quo bias.
 - Clauses referring to corruption are included in only two (4%) of 54 BITs, yet a virtually corruption-free country like Singapore should not mind agreeing to anti-corruption provisions even as a net FDI importer.
 - Singapore concluded the first BIT in 1972 having no anti-corruption clauses when it was still working to eliminate corruption. It started performing impressively in the CPI in 1995 (always in the top in the ranking until today), but BITs concluded later do not contain anti-corruption provisions. → Status quo bias by negotiators/drafters?
- Singapore is also partly irrational in retaining many legality clauses in BITs – 33 (61%) among 54 BITs have direct clauses (but less than say China)
 - Unlike China, Singapore has almost no corruption, and indeed no known inbound ISDS claims, so pressing to include a legality clause is not needed for defensive purposes.
 - And if Singapore expects exporting more FDI, it should stop agreeing to legality clauses. Recent BITs still contain legality clauses, suggesting some possible status quo bias.

* Thailand

- Thailand's economy has developed strongly by attracting FDI since the 1980s (albeit especially into manufacturing)
- The country has had a few high-profile cases concerning corruption and other serious misconduct.
 - Alleged in *Kingsgate v Thailand* case under Australia FTA (settled?)
- However, its overall approach to FDI-related corruption is rational.
 - None of Thailand's BITs have anti-corruption provisions
 - 22 BITs (52%) have direct legality provisions – although could rationally press for more.

4. Conclusions

- Overall, South and East Asian net FDI-importing states and some FDI-exporting states have generally achieved rational outcomes in negotiating IIA provisions for FDI-related corruption.
- Their TIP strategies sometimes appear more irrational. Eg, see the direct legality provisions agreed by India and Singapore as the ratio of their TIPs having such provisions is significantly low – respectively 7% and 15%. But TIPs are usually more varied than BITs, and the latter provide better evidence of IIA strategies.
- There are further complexities, eg, countries transitioning from FDI importers to exporters. Nevertheless, our research suggests Asian states adopt quite rational strategies, or they could do so - which IIA drafters and policymakers need to consider when considering interfaces with corruption.