

# Partisan Governments and ISDS Settlements

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## Abstract

Why do some states settle investor-state dispute settlement (ISDS) claims more frequently than others? This study examines how government partisanship influences the settlement of different types of ISDS claims, arising from either major or minor property rights infringements. Specifically, I argue that left-leaning governments, closely aligned with labor interests that generally favor foreign investment, are more inclined to settle ISDS claims arising from serious infringements on property rights. Conversely, the preference of left-leaning partisans for state regulatory autonomy leads these governments to be less likely to settle claims emerging from minor breaches, such as policy regulations affecting foreign investment values. Utilizing original hand-coded data on the level of international investment agreement (IIA) breaches since 2012, I find that left-leaning governments are more likely to settle ISDS claims arising from major IIA breaches, while being less likely to conclude ISDS claims associated with minor IIA breaches by settlement.

## 1 Introduction

In recent decades, there has been a significant increase in foreign direct investment (FDI) ([World Bank 2018](#)). Despite many countries transitioning from anti-foreign investment policies to more pro-foreign investment strategies, economic disputes over foreign investment continue to arise. Several dispute settlement mechanisms address international investment disputes that stem from the policy actions of individual nations. In particular, many international investment agreements (IIAs) include Investor-State Dispute Settlement (ISDS) provisions, granting foreign investors the right to file a claim against the host

nation at an international tribunal if they have suffered due to governments' policy actions. Respondent states sued under this mechanism are obliged to pay relatively high legal fees and face economic consequences if they lose a case by ruling. When losing an ISDS case, respondent states are required to pay compensation to the claimant investors. Moreover, the experience of having or losing ISDS claims, particularly those resulting from a host nation's forced divestment of investment or property rights, can lead to a decrease in FDI ([Allee and Peinhardt 2011](#); [Kerner and Pelc 2022](#)).

However, the ISDS mechanism does not always conclude with rulings from international tribunals. Respondent states may settle with claimant investors by making full or partial concessions, or by paying compensation. Approximately 20 percent of ISDS cases are settled before a tribunal ruling ([UNCTAD 2023](#)). This paper examines why some states are more likely than others to resolve their ISDS claims through settlement prior to a tribunal ruling.

The literature on the political economy of ISDS settlements has primarily focused on the type of ISDS claims and the timing of settlements. [Pelc \(2017\)](#) finds that states are less likely to settle indirect ISDS claims that arise from government policy ambitions rather than from claims stemming from host governments' outright confiscation of foreign investment. [Rao \(2021\)](#) argues that there are fewer ISDS settlements during election years, as state leaders are concerned about the political consequences of conceding to foreign investors. However, thus far, our understanding of what drives the settlement of ISDS claims remains limited.

This paper examines the role of domestic politics in influencing the likelihood of settlement in ISDS claims, arguing that partisan politics matters. Left- and right-leaning governments, comprising distinct partisan groups, have different material interests and normative preferences. The core constituency of left-leaning governments is labor, which typically benefits from foreign investment in both developed and developing economies. Consequently, workers generally favor foreign investment and oppose government actions that may trigger FDI outflow ([Pinto 2013](#)). Therefore, when facing ISDS claims that emerge

from serious government infringements on property rights, workers are likely concerned about their country being perceived as an unattractive investment destination and about losing the benefits of future FDI. When left-leaning governments are in office, they are more inclined to address these concerns by settling pending ISDS claims stemming from serious violations of IIA breaches with foreign investors. Conversely, for ISDS claims arising from government regulations, the strong normative preference of left-leaning citizens for the regulatory autonomy of sovereign states is likely to lead left-leaning governments to await the international tribunal's ruling.

To examine the effects of government partisanship and the severity of IIA breaches, I have constructed original data on the level of IIA breaches since 2012. This data enables the measurement of the likelihood of partisan governments settling ISDS claims based on the seriousness of property rights infringements of foreign investment. The empirical results from the regression analysis support my theory: Left-leaning governments are more likely to settle ISDS claims arising from major IIA breaches, while they are less likely to settle ISDS claims arising from minor breaches.

## **2 Foreign Investment Protection and the ISDS System**

Among various types of international investment, foreign direct investment (FDI) is considered the most crucial for promoting economic development ([Jensen 2003](#)). FDI represents a private capital flow from parent multinational corporations to their subsidiaries in foreign nations. While portfolio or speculative investments typically aim for short-term profits, FDI tends to have a long-term investment horizon. Scholars have found that FDI promotes capital accumulation in host nations ([de Mello Jr 1999](#)) and leads to technology transfer from foreign investors to host nations ([Borensztein et al. 1998](#)). [Jensen \(2003\)](#) suggests that FDI may generate foreign exchange and promote employment. Global FDI net inflows (as a percentage of global GDP) increased about tenfold from 0.5 percent to 5.3

percent of global GDP between 1980 and 2007 ([World Bank 2018](#)). As FDI inflows have surged, attracting FDI has become one of the most crucial parts of developing countries' development strategies ([Kerner 2009](#), 75).

With the rise in FDI volumes, foreign investors and home states have created mechanisms to protect their investments. In the 1960s and 1970s, newly independent countries expropriated many foreign assets ([Kobrin 1980](#)). Although the international customary law, known as the "Hull Rule," required expropriators to pay prompt and adequate compensation, newly independent countries often refused to obey the "Hull Rule" ([Guzman 1997](#)). To substitute for the "Hull Rule," Western economies have signed IIAs, such as bilateral investment treaties (BITs), with developing nations to protect their outward investments from host governments' forced divestment ([Salacuse 2017](#)). In fact, foreign investors have been able to initiate litigation in the domestic courts of the host country. However, concerns that domestic courts might be biased or partial led to the establishment of the ISDS system. ISDS provisions in international investment treaties require national governments to delegate their adjudicative authority to international tribunals ([Elkins et al. 2006](#); [Allee and Peinhardt 2010](#)). Consequently, foreign investors can appeal to an international arbitration body, such as the International Centre for Settlement of Investment Disputes (ICSID), when a dispute arises between them and host governments.

Foreign investors file ISDS claims because of various actions of host states. Host governments sometimes commit outright expropriation of foreign investment, such as seizing foreign assets or conducting forced sales. They also revoke foreign investors' licenses or contracts when disputes arise between them and foreign investors. Foreign investors sometimes find that host governments create restrictions on the transfer of profits or dividends. These government actions not only seriously violate IIAs but also infringe upon the property rights of foreign investors. Confronted with such actions, foreign investors often find themselves unable to operate businesses in the host states. This may lead them to exit the host country and seek financial compensation by initiating an ISDS

claim. This paper classifies ISDS claims resulting from these types of government actions as major IIA breach cases.

Unlike host governments facing ISDS claims for intentionally infringing on foreign investments, many other host states are brought before international tribunals for their actions that are less intentional. At times, broad policy actions by a host government can trigger an ISDS claim, especially if a foreign investor perceives that such actions diminish the value of their investment. In other words, a host government's legal or policy changes that may affect foreign investment can be subject to review by an international tribunal ([Elkins et al. 2006](#)). For example, in 2010, Philip Morris sued the Uruguayan government for implementing anti-tobacco legislation that imposed higher tax rates on tobacco products and banned tobacco advertisements in the media, demanding \$22 million in compensation ([Castaldi and Esposito 2016](#)). Foreign investors also sometimes sue governments under ISDS when host governments impose penalties or fail to provide desired services or protections. This paper classifies ISDS claims from these government actions as minor IIA breach cases.

When sued under ISDS, a host government is required to engage in a legal dispute unless the claimant investor decides to discontinue the case. A case is concluded by a tribunal's ruling unless a respondent government and claimant investor settle, or the claimant investor voluntarily discontinues the case. Of the 740 concluded cases available in the United Nations Conference on Trade and Development's (UNCTAD) Investment Dispute Settlement Navigator ([UNCTAD 2023](#)), respondent governments won in 274 cases (37 percent), while claimant investors won in 212 cases (29 percent). International tribunals ruled in favor of neither party in 16 cases (0.02 percent). The parties settled 148 cases (20 percent), and in 90 cases (12 percent), the proceedings were discontinued without a settlement. Although respondent governments have a higher winning rate, losing an ISDS case can lead to significant financial burdens. [Wellhausen \(2016\)](#) finds that, among the concluded cases won by claimant investors, the mean award is \$508 million, although 50

percent of the awards are below \$16 million. Additionally, the average legal cost for a respondent government is \$4.56 million, which could be a relatively high burden for poor developing nations ([Allen and Overy 2017](#)).

Respondent governments may also suffer additional externalities. For instance, [Allee and Peinhardt \(2011\)](#) find that a respondent government brought before ICSID experiences a decline in FDI. If a respondent government loses an ISDS case, inward FDI is further reduced ([Allee and Peinhardt 2011](#)). [Kerner and Pelc \(2022\)](#) also find that in cases of direct expropriation claims, which arise from host governments' outright expropriation of foreign investment, there is a reduction in inward FDI.

However, waiting for a tribunal ruling is not the only option for claimant investors and respondent governments. When both parties reach an agreement on the amount of compensation the respondent state is willing to pay the claimant investor, they can settle the ISDS case. According to the Investment Dispute Settlement Navigator of UNCTAD ([UNCTAD 2023](#)), 58 countries have settled at least one of their pending ISDS cases. Both low and lower-middle-income countries, as well as high-income countries like Canada, Germany, and the United States, have reached settlements with claimants. The settlement record of high-income countries indicates that factors other than potential financial burdens from losing an ISDS case can influence a government's decision to settle.

This paper focuses on the role of domestic politics within respondent states and investigates the conditions under which respondent governments settle their ISDS cases. It also examines whether the likelihood of settlement of ISDS claims differs by partisanship of respondent governments and types of IIA breaches.

### 3 Literature Review

A small number of studies have examined why respondent states resolve their pending ISDS claims by settlement. [Pelc \(2017\)](#) finds that respondent governments are more likely

to settle when engaged in direct expropriation claims that emerge from host governments' outright expropriation of foreign investment. For direct expropriation claims, respondent governments settle 31 percent of the claims, while the average rate of settlement for indirect expropriation claims is just 12 percent. In fact, for respondent governments, the chance of losing an indirect expropriation claim is less than 20 percent. Thus, respondent governments are less likely to settle with investors when they are brought before international tribunals over indirect expropriation. Pelc's findings provide insight that respondent governments may decide to settle their ISDS cases based on their chances of winning or losing.

Several scholars have focused on the political motivation of respondent governments. Drawing on anecdotal evidence from surveys and negative media coverage of ISDS ([Chew et al. 2018](#)), [Rao \(2021\)](#) proposes that a government's decision to settle with foreign investors can trigger a backlash from citizens. She finds that the closer a government is to holding a national election, the less likely it is to settle with claimant investors. Rao implies that national leaders' decisions to settle an international economic dispute are constrained by domestic public opinion. One source of such public opposition is nationalism. [Brutger and Strezhnev \(2022\)](#) find that citizens high in national superiority are less likely to support the ISDS system after realizing that foreign investors have filed an ISDS claim against their nation.

Building on this line of research, this study examines the role of domestic politics in ISDS settlements, placing particular emphasis on the influence of partisan governments. Partisan governments have core support groups with distinct material interests, which may in turn affect the likelihood of ISDS settlements. This is because losing ISDS claims may lead to a decrease in FDI ([Allee and Peinhardt 2011](#); [Kerner and Pelc 2022](#)), and the distributive consequences of reduced FDI vary across different partisan groups. Partisan governments, which often rely on support from their core constituencies, are likely to consider these consequences. Left-leaning governments tend to prioritize the material

interests of labor, whereas right-leaning governments focus more on the interests of capital owners. Therefore, when facing a pending ISDS claim, partisan governments may opt for settlement by assessing the distributive impact of the case on their core support groups.

The political economy literature on FDI suggests that left-leaning governments and workers are concerned about the negative externalities of FDI and restrict FDI flight while still welcoming it. [Owen \(2013; 2015\)](#) argues that domestic labor is generally concerned about FDI, as it may lead to increased unemployment. The introduction of new and efficient technology by foreign firms can result in local firms losing competitiveness and potentially closing. Given that labor unions are particularly concerned about unemployment, Owen hypothesizes that countries with strong labor unions are likely to impose greater restrictions on foreign investment inflows to mitigate the risk of unemployment. [Owen \(2013; 2015\)](#) finds a correlation between higher union density and increased restrictions on foreign investment, both in the United States and in nineteen democracies.

By contrast, [Pinto \(2013\)](#) argues that labor, a key constituency for left-leaning governments, often favors FDI because multinational corporations tend to offer competitive wages ([Brown et al. 2004](#)) and introduce new technology to host nations, thereby improving the general productivity level of labor ([Pinto 2013; Pond 2018](#)). [Pinto \(2013\)](#) finds that left-leaning governments adopt favorable economic policies for foreign firms, such as offering low tax rates to attract greater FDI. Conversely, [Pinto \(2013\)](#) finds that right-leaning governments impose less favorable conditions for foreign investors, such as high tax rates on foreign investments, because right-leaning governments often form political coalitions with domestic capital owners who compete with foreign capital owners in the domestic market. [Pinto \(2013\)](#) finds that left-leaning governments attract greater FDI than right-leaning governments.

[Chen and Park \(2019\)](#) discover that left-leaning governments are more likely to adopt policies that attract FDI, but also implement measures to mitigate negative externalities from FDI, such as restricting the maximum percentage of foreign ownership in domestic



firms. The findings of [Owen \(2013; 2015\)](#) potentially indicate concerns among left-leaning governments regarding the negative externalities associated with Foreign Direct Investment (FDI). These policies, aimed at mitigating the negative externalities of FDI, empower domestic shareholders and labor unions with sufficient influence to counterbalance that of foreign firms, thereby reducing negative externalities. Similarly, [Pond \(2018\)](#) finds that democratic countries with established labor rights demonstrate greater openness to FDI inflows while restricting outflows to prevent capital flight. Foreign investors generally have more leverage when they can easily divest their investment to another country. By restricting capital outflow, workers and left-leaning governments are better equipped to regulate foreign investors and prevent negative externalities.

In summary, the literature suggests that although workers and left-leaning governments may approach FDI inflows with caution, they also actively seek to attract such investments due to the perceived benefits that FDI provides to workers. Considering that losing ISDS claims could result in FDI outflows ([Allee and Peinhardt 2011](#); [Kerner and Pelc 2022](#)), workers and left-leaning governments are more concerned about the outcomes of ISDS claims compared to their right-leaning governments.

However, the material well-being of partisan groups is not the sole concern of partisan governments. The core support groups within different partisan governments also have distinct normative preferences, which may influence their assessment of whether the expropriations or regulations triggering the pending ISDS case are legitimate. As a result, partisan governments pay close attention to the reactions of their core partisan groups and endeavor to resolve pending ISDS claims in a way that retains the support of these groups. Among various normative values that citizens possess, this paper focuses on the normative values of partisan groups regarding state regulatory autonomy and how these values affect settlements of ISDS claims that arise from state regulatory actions. This focus is pertinent because suing national governments over their policy actions constitutes a challenge to state regulatory autonomy.

The political economy literature finds that left-leaning constituents generally favor state intervention and regulation when addressing various economic and social issues. For instance, left-leaning parties often champion social equality and low unemployment, accepting modest levels of inflation and budget deficits. In contrast, right-leaning parties are less focused on social equality and full employment, instead emphasizing low inflation and rigorous fiscal discipline ([Franzese 2002](#)). As a result, left-leaning governments are more likely to intervene in the market actively to reduce unemployment ([Hibbs 1977](#); [Tufte 1978](#)). This literature indicates that left-leaning constituents are more tolerant of government interventions and prefer state regulations compared to their right-leaning citizens.

Environmental protection is another domain where states frequently intervene and impose regulations. Studies have found that individuals with right-leaning normative values are often more reluctant to embrace environmentalism. [Jagers et al. \(2018\)](#) argue that individuals with right-leaning normative values are often skeptical about market regulation while prioritizing economic growth. In contrast, left-leaning individuals, with deeper post-materialist normative values, show greater concern for environmental issues ([Armingeon and Bürgisser 2021](#)). In summary, the literature on political ideology indicates that left-leaning constituents are more supportive of state interventions and regulations, such as economic and social regulations, compared to right-leaning voters.

The next section examines how the distinct material interests and normative values of left- and right-leaning partisan groups lead to different outcomes in the settlement of ISDS claims. Additionally, the section explores whether the likelihood of settling ISDS claims among different partisan governments varies according to IIA breach types.

## 4 Theory

I argue that in considering the settlement of pending ISDS claims, partisan governments are concerned with the distributive consequences these settlements have on their core support groups, as well as the core support groups' normative evaluations of settling the claims. I also expect the settlement rate for ISDS claims by each partisan government to vary based on the severity of the IIA breach. Claims arising from major IIA breaches, such as the outright expropriation of foreign investments, are more likely to deter foreign investors from investing in the respondent state. Thus, when settling these types of claims, partisan governments are likely to be more concerned about the distributive consequences of such settlements. On the other hand, certain partisan groups may oppose settling claims arising from minor IIA breaches, such as those where government policy ambitions reduce the profitability of foreign investments, due to their normative preference for state regulatory autonomy.

### 4.1 Distributive consequences and ISDS claims from major IIA breaches

Major IIA breaches represent the most serious type of property rights infringement of foreign investment. This type of breach includes outright expropriation, which involves the transfer of foreign investment ownership from a foreign investor to a host government. Sometimes, host governments force foreign investors to sell their shares to a third party. Although less severe than outright expropriation, the revocation of licenses or contracts can make foreign investors unable to operate businesses in the host state. Restricting profit and dividend transfers also significantly infringes the property rights of foreign investors and discourages foreign investors from maintaining their investment in the host state.

The motivations for committing major IIA breaches can vary. For instance, host governments may seize foreign assets during economic or military crises to gain additional revenue for managing these crises. Withdrawal of foreign investment or the hard currency

of foreign investors might exacerbate ongoing crises. In such cases, host governments may need to directly expropriate foreign investments to decrease the negative domestic impacts resulting from the behavior of foreign investors. Besides crisis management, corruption is another main motivation for expropriating foreign investment. Evrensel (2010) and Hajzler and Rosborough (2016) find that corrupt regimes are more likely to expropriate foreign investments.

For claimant investors, experiencing serious IIA breaches discourages them from maintaining their presence in the host country. Other foreign investors may also become wary of the host government's serious violation of IIAs and consequently reduce their investment or withdraw from the host nation altogether. [Allee and Peinhardt \(2011\)](#) and [Kerner and Pelc \(2022\)](#) find that losing ISDS claims related to outright expropriation leads to a decline in inward FDI. Foreign investors who lose part of their investment may relocate their assets to other nations where host governments are perceived to respect and protect the property rights of foreign investors. [?](#) finds that approximately 70 percent of foreign claimants leave the countries where they have invested after filing an ISDS claim against the host state. Only 18 percent of the firms that sue their host states for direct expropriation remain in or return to the host state, compared to 31 percent of the firms that filed claims for non-direct expropriation events. Therefore, host countries facing ISDS claims from major IIA breaches are more likely to lose these claims and experience a decline in FDI, compared to those committing minor IIA breaches.

Consequently, when citizens become aware that their governments have committed major IIA breaches and face pending ISDS claims due to these actions, they may perceive a need for their governments to adopt measures to restore national reputation. One such remedial action is settling with claimant investors by financially compensating them for their losses. Compared to prolonging a legal battle until an international tribunal issues a final ruling, opting for settlement is less likely to negatively impact future FDI inflow. Negotiations aimed at reaching a settlement may reduce the level of conflict between

claimant investors and respondent governments. Additionally, such negotiations might encourage claimant investors to remain in the country or even increase their investment, especially if the respondent governments credibly promise to offer a higher return rate. [Wellhausen \(2019\)](#) finds that claimant investors are more likely to stay in or return to the respondent countries when their ISDS cases are resolved through settlement.

A decrease in FDI typically has adverse effects on the national economy, particularly impacting labor, a core constituency of left-leaning governments. Labor often favors foreign investment due to its benefits for the working class, such as expanding employment opportunities and increasing wages (Pinto 2013; Pond 2018). Consequently, labor is likely to be especially concerned about losing ISDS claims arising from major IIA breaches, fearing the potential distributive consequences. In cases of these types of ISDS, labor might express its concern about these consequences and urge the government to settle with the claimant investor before the tribunal's ruling.

I anticipate that workers in both developed and developing economies will support the settlement of ISDS claims arising from major IIA breaches, given that FDI contributes positively to both types of economies. In developing economies, foreign investors often target the primary and manufacturing sectors, where workers can benefit from increased employment opportunities and higher wages. Conversely, in developed economies, FDI is typically more concentrated on sectors requiring skilled labor. As a result, unskilled workers in developed economies do not lose out due to FDI flight, while skilled workers gain from it. [Pinto \(2013\)](#) demonstrates that left-leaning governments in both developed and developing economies endeavor to create favorable conditions for foreign investors to attract FDI.

Some might argue that domestic capital owners, a core constituency of right-leaning parties in both developing and developed economies, may also advocate for the settlement of ISDS claims stemming from major IIA breaches due to their strong ideological commitment to property rights. However, domestic capital owners in both contexts may be

less concerned about government actions leading to major IIA breaches, as their interests might not align directly with those of foreign investors.

In developing economies, where capital is scarce, domestic capital owners aim to achieve high returns while seeking insulation from external competitors. However, the inflow of foreign capital often forces them to compete with foreign investors in their domestic markets. As a result, governments in developing economies that are pro-capital and backed by domestic capital owners may seek to limit FDI. Furthermore, mutual investment agreements between developing and developed economies tend not to favor capital owners in developing countries as much as those in developed economies. This discrepancy arises because, unlike their counterparts in developed economies who actively invest in developing countries, capital owners in developing countries generally lack the resources to invest in high-technology industries in more developed economies. Therefore, domestic capital owners in developing countries are less inclined to favor settling ISDS claims arising from major IIA breaches, as such settlements could potentially increase FDI inflow and intensify competition in domestic markets. This leads to a tendency among right-leaning governments in developing economies to be less inclined toward resolving pending ISDS claims from major IIA breaches through settlement, compared to their left-leaning counterparts.

In developed countries, capital owners are less concerned about the consequences of ISDS claims arising from major IIA breaches, largely because serious violations of IIAs, such as the expropriation of foreign assets, are rare in these economies. Consequently, the likelihood of settling ISDS claims in developed countries should primarily be influenced by the concerns of workers.

In summary, when left-leaning governments are in power, the strong demand from labor for settlement can lead these governments to seek resolution of ISDS claims stemming from major IIA breaches. This line of reasoning forms the basis for Hypothesis 1:

**Hypothesis 1:** Left-leaning governments are more likely to settle ISDS claims emerging from major IIA breaches than right-leaning governments.

## **4.2 Normative preferences and ISDS claims from minor IIA breaches**

There has been an increasing trend where foreign investors file ISDS claims arising from governments' minor IIA breaches ([Pelc 2017](#)). This type of breach often includes host governments' imposition of regulations that negatively impact the business operations and investment value of foreign investors. In many cases, foreign investors sue host countries under ISDS for broad economic and social policies that do not specifically target foreign investors. They may also initiate ISDS claims when host governments fail to provide desired services or protections. In these instances of minor IIA breaches, foreign investors do not lose the property rights of their investments, but they may just experience a decline in profits or face minor operational difficulties.

I argue that left-leaning partisans are inclined to criticize claimant investors' decisions to sue host states for minor IIA breaches. While attracting greater FDI is important, it is not the only objective of left-leaning governments and workers. Instead, when necessary, left-leaning governments often implement strict measures to mitigate negative externalities resulting from foreign investment, as noted by [Chen and Park \(2019\)](#). Moreover, left-leaning partisans typically place greater value on government regulations related to economic and social policies than right-leaning constituents. Consequently, I argue that left-leaning partisans do not support foreign investors challenging their governments in international tribunals over regulatory actions or other minor IIA breaches. This normative preference for state intervention among left-leaning partisans should lead them to disapprove of most claims by foreign investors who sue their government for minor IIA breaches, thereby discouraging left-leaning governments from settling with claimant investors.

Furthermore, workers may have little reason to be concerned about the distributive

consequences when foreign investors file an ISDS claim for minor IIA breaches. Wellhausen (2019) finds that claimant investors who sue host governments over non-direct expropriation actions are less likely to leave the respondent states compared to those who file claims for direct expropriation. Additionally, ISDS claims from non-direct expropriation do not lead to a decrease in FDI (Kerner and Pelc 2021). These findings indicate that foreign investors are less likely to exit the host country when experiencing less serious IIA breach actions by the government.

Therefore, organized labor and other left-leaning constituents benefiting from foreign investment are less likely to be concerned about potential negative distributive consequences from ISDS claims arising from minor IIA breaches. Given left-leaning citizens' preference for state regulatory autonomy and the minimal impact of negative distributive consequences on workers, left-leaning governments have little incentive to settle their pending indirect ISDS claims. This line of reasoning leads to the Hypothesis 2:

**Hypothesis 2** Left-leaning governments are less likely to settle ISDS claims emerging from minor IIA breaches than right-leaning governments.

## 5 Research Design

To test my hypotheses, I use an Ordinary Least Squares (OLS) model. My main empirical model is specified as follows:

$$y = \beta_0 + \beta_1 \text{Partisanship} + \beta_2 \text{Breach Type} + \beta_3 \text{Partisanship} * \text{Breach Type} + \epsilon \quad (1)$$

Given that the dependent variable is binary, I also include a logistic model as a robustness check to ensure the validity of the results.

To determine the effects of government partisanship and the seriousness of IIA breaches



on settlement outcomes, I analyze cases registered in UNCTAD's Investment Dispute Settlement Navigator ([UNCTAD 2023](#)). Specifically, I analyze the concluded cases filed in international tribunals from 2012 to 2022. The dependent variable, Settlement, is a binary variable coded as 1 if an arbitration proceeding is settled before a tribunal ruling, or 0 otherwise. This dataset is sourced from the Navigator, which records the status of ISDS claims.

For the independent variable, government partisanship, I utilize the economic right-left scale indicator (`execrlc`) from the Database of Political Institutions (DPI) dataset ([Scartascini et al. 2021](#)). This indicator represents party orientation regarding economic policy on a continuous scale from 1 to 3, classifying the economic positions of political parties along a right-center-left spectrum.

The second independent variable, type of IIA breach, is coded as 1 if the alleged IIA breach is serious, or 0 otherwise. To construct this variable, I hand-coded 316 ISDS cases registered on the Investment Dispute Settlement Navigator, classifying each based on whether it constituted a serious violation of an IIA. Previous research categorizes ISDS claims as either direct or indirect ([Wellhausen 2016](#); [Pelc 2017](#); [Kerner and Pelc 2022](#)). A case is considered a direct ISDS claim if it involves the host government's direct seizure or confiscation of foreign investment; all other cases are classified as indirect claims. However, many instances of non-direct expropriation can be as serious as direct ones. For instance, a government's revocation of contracts or licenses can render foreign investors unable to operate their businesses in the host state, leading to the withdrawal of their investments. The distributive consequences of this event can be substantial. For example, local unemployment can rise due to the withdrawal of foreign investment. Given that certain governments are more likely to protect the interests of their core groups from the effects of FDI flight, investigating whether they differentiate between ISDS claims arising from serious breaches and those from minor ones is important.

I include log GDP per capita as a control variable to reduce bias in my estimates. Poorer

countries are likely more sensitive to losing their ISDS claims because such losses might lead to a decline in foreign investment which is crucial for their economies. In contrast, wealthier countries, with their higher legal capacity, may perceive a lower likelihood of losing ISDS claims. Additionally, the substantial national wealth of richer countries enables them to absorb the financial impact of compensations arising from lost ISDS claims and FDI flight. Furthermore, wealthier countries are generally less likely to commit serious IIA breaches, such as confiscating foreign investments or revoking the operational rights of foreign investors.

## 6 Preliminary Results

Table 1: **Descriptive statistics**

<b>Statistic</b>	<b>N</b>	<b>Mean</b>	<b>St. Dev.</b>	<b>Min</b>	<b>Median</b>	<b>Max</b>
Settlement	316	0.2	0.4	0	0	1
Left	126	2.0	0.9	1	2	3
Major Breach	247	0.4	0.5	0	0	1

Table 1 summarizes the descriptive statistics. The mean of the dependent variable, ISDS settlement, is 0.2, and it shows that approximately 20 percent of ISDS claims are concluded by settlement. The mean and median of the first main independent variable, government partisanship, is 2, suggesting that the dataset's left, center, and right governments are well balanced. The mean of the second independent variable, IIA breach type, is 0.4, indicating that about 40 percent of the ISDS claims are arising from major IIAs breach.

Table 1 summarizes the descriptive statistics. The mean of the dependent variable, ISDS settlement, is 0.2, indicating that approximately 20 percent of ISDS claims are concluded by settlement. The mean and median of the first main independent variable, government partisanship, are both 2, suggesting that the distribution of left, center, and right governments in the dataset is well balanced. The mean of the second independent variable, IIA breach type, is 0.4, indicating that about 40 percent of the ISDS claims arise from major IIA

breaches.

Table 2 summarizes the main regression estimates from the OLS and logistic models. The estimates in Table 2 support the hypothesis that left-leaning or centrist governments are more likely to settle ISDS claims arising from major IIA breaches than right-leaning governments. They also show that left-leaning or centrist governments are less inclined to settle ISDS claims arising from minor IIA breaches than right-leaning governments. The coefficients for Per Capita GDP (log) indicate that wealthier countries are less concerned about losing their ISDS claims and FDI, possibly due to their superior legal resources or national wealth.

Table 2: Government partisanship and ISDS settlement

	<i>Dependent variable:</i>	
	Settlement	
	<i>OLS</i> (1)	<i>logistic</i> (2)
Left	−0.265 (0.167)	−2.244 (1.560)
Major Breach	−0.028 (0.049)	−0.314 (0.448)
Per Capita GDP ( <i>log</i> )	−0.076** (0.038)	−0.547* (0.291)
LEFT * Major Breach	0.146* (0.077)	1.151* (0.667)
Constant	0.913** (0.380)	3.832 (2.921)
Observations	99	99
R <sup>2</sup>	0.101	
Log Likelihood		−37.565
<i>Note:</i>	*p<0.1; **p<0.05; ***p<0.01	

## 7 Discussion

This study primarily contributes to the literature on the politics of ISDS settlements. By integrating the economic interests and normative values of interest groups and partisan constituencies, it enhances our understanding of why some countries are more likely to settle ISDS claims than others. The partisan theory of ISDS settlements also sheds light on why certain countries are sued less frequently under ISDS. For example, foreign investors might be reluctant to sue left-leaning governments if their policy actions reduce investment values. This hesitance may stem from the belief that left-leaning governments, aligning with their core constituencies' preference for state regulatory autonomy, are less inclined to settle ISDS claims associated with minor IIA breaches.

Furthermore, this study advances our understanding of how partisan heterogeneity impacts international economic cooperation. While international relations scholarship has primarily focused on the roles of regime types and macroeconomic conditions in international cooperation ([Milner 1997](#); [Mansfield et al. 2002](#)), the influence of partisanship has been less explored ([Schneider and Urpelainen 2014](#)). By focusing on the dynamics of expropriation and the subsequent settlement stages, my partisan theory of international economic dispute settlement highlights the differences in how parties approach restoring compliance in international economic cooperation.

This research also contributes to the literature on the politics of ISDS claims empirically. Foreign investors initiate ISDS claims against national governments for various reasons, ranging from outright expropriation to the implementation of certain regulations. The reactions of host governments and their citizens are likely to differ based on the actions that trigger these ISDS claims. However, many scholars do not distinguish between types of ISDS claims or rely solely on the Investment Dispute Settlement Navigator's classification of direct and indirect ISDS claims. Many indirect ISDS claims, including those arising from the government's revocation of contracts or licenses, are as severe as outright expropriation in terms of property rights infringement. The new dataset, which includes information

on the types of IIA breaches that trigger ISDS claims, enables scholars to explore more dimensions of the politics surrounding the ISDS system.

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