INTERNATIONAL INVESTMENT DISPUTES

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International investment takes place in the context of private contracts between private parties or a private party and a host state government, amidst an increasing proliferation of international investment agreements between states at bi-lateral, multi-lateral, sub-regional, regional and inter-regional levels. These public international law agreements between states typically provide a mechanism for private investors to seek compensation from states for a breach of the investor's international law rights, whether or not the state in question has signed a private contract with the private party.

International investment agreements include over 2,495 bi-lateral investment treaties (BITs)[1], numerous preferential free trade and investment agreements as well as multi-lateral investment agreements. Some 70 BITs were signed in 2005 alone. The growth of international foreign investment has also seen a proliferation of stabilisation agreements made between developing country governments and foreign private investors many of which contain international investor-state dispute settlement provisions.[2]

It is increasingly common for bi-lateral Free Trade Agreements (FTAs) to include investment protection provisions, as well as provisions on trade in goods and services, intellectual property rights and trade facilitation.[3] FTAs may overwrite or supersede the provisions of earlier BITs concluded between the same countries. The potential benefits of FTAs are particularly attractive to capital-importing countries. For its part, the US has used its FTAs to pursue a policy of "*competitive liberalisation*" to obtain commitments that exceed those contained in existing multilateral agreements, such as the WTO Trade-Related Investment

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[1] As of end 2005 - http://www.unctad.org/en/docs/webiteiia20069_en.pdf.
[2] Peru alone has concluded more than 400 such agreements between 1993 and 2004.
[3] See details of this trend for OECD countries at http://www.oecd.org/dataoecd/13/62/35032229.pdf.

Measures (TRIMS) agreement, or the General Agreement on Trade and Services (GATS) in the area of trade in services.

These international investment agreements confirm the international norm by which private investors are typically recognised as having standing under investment treaties to bring international arbitral proceedings against states.

Claims by investors

There are two principal means by which a private investor from one state can bring an international arbitration claim concerning its investment in a second, host state. First, if there is a contract between the investor and the host state (or state agency or state entity) the contract may contain an arbitration clause by which the investor and host state consent to submit disputes to arbitration. The clause may specify arbitration under the auspices of, for example, the ICC, the Stockholm Chamber of Commerce (SCC) or under the UNCITRAL Rules. Often, the arbitration clause in an investor-state contract will specific arbitration under the auspices of the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention).

Second, there may be an international investment agreement (such as a BIT) between the investor's home state and the host state where the investor makes its investment. The BIT will typically provide a direct right on the part of the investor to international arbitration against the host state (without the need for there to be a contract between the investor and the host state, its agencies or state entities). The BIT may specify a particular type of arbitration, such as ICSID, UNCITRAL or SCC arbitration.[4]

To take advantage of the substantive protections offered to the investor by the BIT (e.g. protection from expropriation without prompt and adequate compensation, the guarantee of fair and equitable treatment and the guarantee against arbitrary or discriminatory treatment by the state) the investor has to qualify as an "investor" under the BIT making an "investment" as defined in the BIT. If the arbitration mechanism being invoked under the BIT is that of ICSID the jurisdictional requirements set out in the ICSID Convention must also be satisfied.

[4] A third, less frequently used, route for an investor to bring international arbitration proceedings against the host state is by means of a specific provision to do so in the host state's national investment legislation.

Increase in investment treaty claims

The first BIT was signed in 1959.[5] Early BITs contained reciprocal undertakings by which each state guaranteed a minimum standard of treatment to investors of the other signatory state. They did not confer rights on investors as against the host state. Private parties had no standing under international law. Since the 1960s the trend has been to allow foreign investors to bring actions directly against host states.

The cumulative number of treaty-based cases brought before tribunals under the auspices of the World Bank's International Centre for Settlement of Investment Disputes (ICSID) and other arbitration tribunals rose from 5 in 1994 to a total of 219 by November 2004 with at least 42 cases launched in 2005. Over 61 states have been brought before an international tribunal, 31 of which were developing countries. Prior to 1997 there had been 23 ICSID arbitrations in the previous 14 years. Since 1997 there have been 65 concluded ICSID cases and there are currently more than 105 pending cases of which 57 relate to South American governments, the large majority arising from Argentina's 2002 financial crisis. 143 states have signed the ICSID Convention.[6]

Whilst the ICSID arbitration facility is the only facility to maintain a public registry of investment treaty claims the actual number of such claims is likely to be higher than the available figures indicate as a number of treaty-based claims are known to be proceeding outside ICSID. Many international investment agreements allow investors to choose between ICSID (including the ICSID Additional Facility) and *ad hoc* arbitration using, for example, UNCITRAL arbitration rules. Institutional arbitration rules have also been agreed for some of these disputes (including the arbitration rules of the ICC, LCIA, SCC and various regional arbitration centres, including Singapore and Cairo).

Investor-state arbitration proceedings concern foreign investments in both pre-establishment and post-establishment phases and involve all kinds and types of foreign investment, including privatisation contracts and state concessions. Industry sectors include oil and gas, mining, construction, water, telecoms, brewing, banking, hotel management, TV, waste management and textiles. The range of state measures complained of in these arbitrations include emergency laws put in place during financial crises, re-zoning of land, measures on

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[5] Pakistan/Germany.
[6] Statistics from "Latest Developments in Investor-State Dispute Settlement Monitor No 4 (2005)

hazardous waste facilities, rules for divestment of shareholdings in public enterprises to a foreign investor and media regulation. The investment claims have concerned issues of fair and equitable treatment, non-discrimination, expropriation, and regulatory measures "tantamount to expropriation".

Multilateral investment treaties

Claims brought under multilateral investment treaties constitute a significant further development in the evolution of a global foreign investment dispute resolution system.

The North American Free Trade Agreement (NAFTA) between the US, Canada and Mexico allows the private investor to select arbitration under the ICSID Convention (provided both are parties to the Convention), the Additional Facility Rules of ICSID (provided either but not both is a party to the Convention) or the UNCITRAL Rules.

NAFTA has given rise to numerous claims. It may be noted that true ICSID arbitration under the ICSID Rules is not available to NAFTA investors because neither Canada nor Mexico have ratified the ICSID Convention. Accordingly, review of or recourse against an award made pursuant to NAFTA will be left to the courts in the seat of the arbitration. Likewise, the scope and procedure of the review will be determined by the applicable international commercial arbitration legislation at the seat.

In Asia the 1987 ASEAN Agreement for the Promotion and Protection of Investments contemplates several methods of dispute resolution, including ICSID arbitration, for resolving disputes between member states and an investor from another member state. However, the disputing parties are required to agree on the particular system of arbitration, failing which the dispute is to be submitted to neutral *ad hoc* arbitration.

Energy Charter Treaty

The 1994 Energy Charter Treaty (ECT) is a multilateral investment treaty intended to provide treaty protection to investors of the signatory states in respect of investments and activities in the energy sector. The ECT was signed in June 1995 between 49 countries (most OECD, CIS and East and Central European countries) and the European Community and became effective in 1998.[7] The signatories also include Japan, Australia and Mongolia (but not the

[7] Currently some 51 states and the European Communities have ratified the ECT.

US and Canada). Russia and Norway have not ratified the ECT but Article 45(1) provides for provisional application prior to ratification.

Under Article 26 of the ECT disputes that cannot be settled amicably can be submitted at the choice of the investor (only) to national courts or to arbitration under the treaty. The investor can choose arbitration under the ICSID Convention, the ICSID Additional Facility, UNCITRAL Arbitration Rules or the SCC in respect of alleged breaches of the obligations under Part III of the ECT (non-discriminatory treatment, the international minimum standard obligations of "fair and equitable" treatment and "most constant protection" (Article 10), compensation for losses and prompt, adequate and effective compensation in case of nationalisation (Article 12), undertakings in respect of expropriation (Article 13) and transfers of capital and payments (Article 14)).

The first award under the ECT was issued in December 2003 in a claim by a Swedish firm against the Republic of Latvia arising out of an electricity project.[8] To date there have been relatively few cases under the ECT.[9] However, the recent US$28.3 billion claim by Group Menatep in UNCITRAL arbitration proceedings commenced against the Russian Federation under the ECT in February 2005, alleging expropriation of the Group's majority shareholding in Yukos, has been described as the largest known investment treaty claim to date.

Most signatories to the ECT have also become signatories to the European Convention of Human Rights (ECHR), adopted in 1950 and which came into force in 1953. Article 1 of the Additional Protocol provides protection to all persons (national and foreigners) from unreasonable and uncompensated interference with property. The ECHR has until now been mainly relevant for domestic investors and reflects a greater recognition of state prerogatives than is to be found under BIT protection regimes. Recourse to the European Court of Human Rights will in most circumstances be of limited practical assistance. The jurisdiction of the Court will only arise when local remedies have been exhausted. The Court's ability to award compensation has to date also been of limited practical value.

[8] Nykomb Synergetics Technology Holding AB (Sweden) v Latvia. Arbitration Institute of the SCC – Case no. 118/2001

[9] *AES v Hungary* ICSID Case No. ARB/01/4 resulted in a settlement; *Plama v Bulgaria and others* Case No. ARB/03/24 is currently before ICSID.

ICSID arbitration

The ICSID Convention provide a framework within which foreign investors can refer a dispute with a state party directly to arbitration under the auspices of ICSID provided consent is obtained in writing (Article 25.1). By virtue of the ICSID Convention international law can now be applied directly to the relationship between the investor and the host state. This system was initially restricted to cases in which the state of the investor and the state-party were both parties to the ICSID Convention.

In 1978 the ICSID Additional Facility was created which allows recourse to the main elements of the ICSID system even if only one party is a party to the Convention, provided both parties to the dispute had given their consent. The parties use ICSID Rules and supervisory personnel outside the ICSID Convention framework. As with awards obtained under UNCITRAL Rules, the finality of such an award will be subject to any judicial review mechanism(s) in the place of arbitration.

ICSID amended its Rules of Procedure for Arbitration Proceedings (ICSID Arbitration Rules), its Arbitration (Additional Facility) Rules and its Administrative and Financial Regulations as of 10 April 2006. The amended ICSID Arbitration Rules create an expedited procedure for provisional measures (Rule 39); provide a new mechanism for raising preliminary objections to frivolous claims (Rule 41); clarify the rules governing arbitrator disclosure (Rule 6) and fees (Rule 14) and provide for greater transparency by provisions for acceptance of *amicus* submissions by third parties (Rule 37), public attendance at hearings (Rule 32) and the publication of awards (Rule 48).

ISSUES IN INVESTOR-STATE ARBITRATION

Sovereign immunity

The general trend in international arbitration is for tribunals to refuse to permit state entities to rely on restrictive provisions of their own law to challenge the validity of an arbitration agreement they have previously entered into. In response to such arguments tribunals invoke principles of good faith and estoppel.[10] An arbitration agreement to which a state is a party is generally deemed to constitute a waiver of sovereign immunity because such an arbitration

[10] *Framatome v. Atomic Energy Organisation (Iran).*

agreement (a specific forum selection agreement) would be in direct contradiction to an assertion of immunity.

No unilateral withdrawal of consent

Article 25.1 of the ICSID Convention provides that where both parties have consented to the jurisdiction of ICSID "*no party may withdraw its consent unilaterally*." Article 26 of the ICSID Convention provides, "Consent of the parties to arbitration under this Convention shall, unless otherwise stated, be deemed consent to such arbitration to the exclusion of any other remedy." Accordingly, if a court of a state party to the ICSID Convention were to issue an anti-suit injunction in respect of an ICSID arbitral proceeding the state would be in violation of its international legal obligations under the ICSID Convention and in violation of customary international law. In customary international law it has long been accepted that if a state that refuses an alien person or company access to its courts it commits a denial of justice. That principle would equally apply to a state refusing access to the arbitral process to which it has agreed. Such an action may also be considered a violation of international public policy.[11]

Consent to arbitrate

A state's consent to arbitrate (e.g. under the auspices of ICSID) may originate from one of three sources. First, consent to jurisdiction under the ICSID system was originally seen as deriving from the express agreement contained in the arbitration clauses of investment contracts between the investor and the host state. Second, the basis of consent was significantly widened by provisions contained in BITs amounting to a standing offer by the host state to submit to, e.g. ICSID arbitration. That offer is accepted when an investor from the other signatory state to the BIT issues a Request for ICSID arbitration. Such blanket consents became more commonly contained in BITs from the 1970s onwards. They mean that a state effectively consents to arbitrate against foreign parties at large provided the BIT conditions are met. Third, it has also been recognised that consent to arbitration may be given by way of a unilateral promise by a state contained in its internal investment legislation.[12]

[11] Benteler v. Etat Belge ad hoc award 18th November 1983.
[12] SPP v. Egypt ICSID (1984).

Different investment treaties may contain a variety of different dispute resolution mechanisms. Many BITs permit only the private investor to choose the method of dispute resolution provided in the treaty. The options are often between the courts of the host state or international arbitration. If the private investor selects arbitration the options are usually ICSID (including the ICSID Additional Facility where the state party to the investment treaty has not ratified the Convention) and the UNCITRAL Arbitration Rules. Some treaties also include ICC arbitration as an option and others allow the parties to agree on a type of arbitration not expressly specified in the treaty. The ECT allows the private investor a wide choice of arbitral options including SCC arbitration.

Some BITs bar access to international arbitration where the investor has already chosen a different resolution path e.g. by commencing proceedings in the host state courts. Such "fork-in-the-road" provisions may prevent an unsuspecting investor who has commenced proceedings from subsequently taking the international arbitration "fork" offered in the treaty as an alternative to the courts. Accordingly, legal advice should be taken and the treaty carefully examined for the existence of such a provision before any court proceedings are commenced.

A BIT may provide that the specified dispute resolution method can only be resorted to after a "cooling off" or conciliation period has elapsed.

Exhaustion of local remedies

Article 26 of the ICSID Convention provides that, unless otherwise stated, consent to arbitration under the Convention is deemed consent to such arbitration to the exclusion of any other remedy. This implies a waiver by the host state of the right to require the exhaustion of local remedies. However, Article 26 further provides that such a right to require the exhaustion of local remedies may be expressly reserved as a condition of the state's consent and state parties to BITs have done so in several instances.[13]

Recourse against investor-state Arbitration Awards

The autonomous character of ICSID arbitration is set out in Article 26 which provides that the consent of the parties to arbitration under the ICSID Convention shall, unless otherwise

[13] e.g., the Rumania - Sri Lanka BIT 1981 which provides "*... each Contracting Party hereby requires the exhaustion of local administrative or judicial remedies as a condition of its consent to conciliation or arbitration by the Centre.*"

stated, be deemed consent to such arbitration to the exclusion of any other remedies. By submitting to ICSID arbitration the parties have agreed, and have the assurance, that the administration of the ICSID rules will be exempt from scrutiny or control of domestic courts in states that are parties to the ICSID Convention.

Article 54 of the ICSID Convention provides that each Contracting state shall recognise an award rendered pursuant to the Convention as binding and enforce the pecuniary obligations imposed by that award within its territories as if it were a final judgment of a court of that state.

The ICSID Convention creates a supranational system which excludes appeal and forecloses challenges to awards (for example, on traditional New York Convention grounds).[14] The Convention supplies the sole remedies available to a losing party, namely: (1) as to the interpretation of the meaning or the scope of the award; (2) revision of the award on the grounds of discovery of a previously unknown factor of decisive importance; and (3) annulment of the award by an *ad hoc* Review Committee.

Article 52 of the ICSID Convention provides for the grounds of annulment, which are: (1) the tribunal was not properly constituted; (2) the tribunal manifestly exceeded its powers; (3) there was corruption on the part of a member of the tribunal; (4) there has been a serious departure from a fundamental rule of procedure; or (5) the award failed to state the reasons on which it is based.

The ICSID Additional Facility does not provide a procedure for review or recourse against awards, which will be left to the courts in the place of arbitration. However, Article 1136 of NAFTA (Finality and Enforcement of an Award) provides that a disputing party may not seek enforcement of a final award under the ICSID Additional Facility or UNCITRAL Arbitration Rules until three months have elapsed from the date the award was rendered and (1) no disputing party has commenced a proceeding to revise, set aside or annul the award; or (2) a court has decided such an application and there is no further appeal.

[14] *Mobil Oil Nz Ltd v. Attorney-General* [1989] 2 NZLR 649; 4 ICSID Reports 117 in which the New Zealand courts observed that ICSID arbitration constituted a self-contained machinery functioning in total independence from domestic legal systems.

In the case of non-ICSID Convention awards arising under investment treaties, both the investor and the state party will potentially have recourse against the award in the courts of the place of arbitration, depending upon the applicable *lex arbitri*.

In the recent English High Court decision in *Republic of Ecuador v Occidental Exploration and Production Company*[15] Occidental had obtained an award against Ecuador in UNCITRAL arbitration proceedings seated in London under the US-Ecuador BIT. Ecuador sought to challenge the award under section 67 of the English Arbitration Act 1996 on the basis that the tribunal had wrongly interpreted an article in the US-Ecuador bilateral investment treaty addressing how the treaty applies to disputes related to "*matters of* taxation". The court rejected the argument put forward by Occidental to the effect that the challenge was not justiciable by the English courts since it would require the court to adjudicate upon rights arising out of a treaty entered into by independent sovereign states on the plane of international law. The court held that it was entitled to consider the BIT to decide the scope of the arbitration agreement and whether the award was within its terms, so as to determine the right of challenge granted to the parties under English domestic law (under section 67 of the Arbitration Act 1996). The court subsequent dismissed the application by the Government of Ecuador to challenge the award.

Interpretation of BITs

BITs are international law treaties but also normally become part of the contracting state's national law upon ratification. BITs set out their own scope of application, define the protections to be granted to the investment and the investor and the consequences in case of breach of the treaty.

A BIT will normally provide for the resolution of disputes arising out of the investment between the two contracting states (state-to-state disputes) or between an investor from one contracting state and the host state (investor-state disputes). However, the contents of BITs and their wording varies, not only as between BITs but also between the various BITs concluded by a state.

Arbitrators deciding state-investor disputes apply the provisions of a BIT to the facts of the dispute, whilst having regard to the BIT's dual legal character of national and international

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[15] English Commercial Court [2006] EWHC 345 (Comm)

law, the general principles of private international law and, where appropriate, the national laws of the disputing parties.

In interpreting investment treaties in the context of investor-state disputes a subjective approach to interpretation will be of limited value as the individual investor has not negotiated the terms of the BIT. The common principles for the interpretation of public law treaties (including BITs) are set out in the Vienna Convention on the Law of Treaty (Vienna Convention on the Law of Treaties 1969), Article 31 of which provides for General Rules of Interpretation. Article 31(1) provides, *"... [a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.*"

Meaning of "investor"

A frequent objection to jurisdiction in state-investor arbitrations concerns the question of whether a claimant is an "investor" within the meaning of the BIT (and, where the arbitration is under the auspices of ICSID, whether the claimant also qualifies as an "investor" under the ICSID Convention).

In the case of natural persons most BITs define an investor as a person who is a citizen of a party to the treaty. Nationality will normally be determined by the party's national laws. In cases of dual nationality the person's "effective nationality" usually prevails. In some BITs the definition of investor is broadened to include natural persons who are permanent residents.

In the case of "juridical persons" or "legal entities" (including a company) BITs commonly use different criteria to determine an "investor" under the treaty. Common law countries normally use the place of incorporation to determine nationality. Civil law countries tend to rely on the place of management or the seat.

Some BITs use control of the company by nationals of a state party as the sole criterion to determine a company's nationality. In other BITs this is used as an alternative to the seat or constitution criteria.

In *Asia Corporation et al. v. Indonesia*[16] P T Amco, an Indonesian company controlled by an American entity, entered an agreement for investment that included an arbitration clause providing for arbitration under the ICSID Rules. That agreement was accepted by the Indonesian government. The ICSID tribunal found that the Indonesian government had thereby accepted that P T Amco should be treated as a national of another contracting state (the US) for the purposes of Article 25.2(b) of the ICSID Convention.

In *Banro v. Congo*[17] Banro Resource Corporation was the Canadian parent company that signed a concession agreement with the Congolese state. The concession agreement contained an ICSID arbitration agreement. No BIT existed between Congo and Canada. Banro Resource Corporation subsequently transferred its rights under the concession agreement to Banro American Resource, a wholly-owned U.S. subsidiary. A BIT existed between Congo and the U.S. The tribunal found that Banro American could not avail itself of its Canadian parent's consent to ICSID arbitration under the concession agreement as Banro Resource did not have the requisite nationality at the time the concession agreement was entered into and therefore could not transfer any valid consent to Banro American.

Meaning of "investment"

Only investments falling within the scope of the particular BIT will form the basis of a claim in substance under the BIT. In an ICSID arbitration the investment also has to qualify as an "investment" under the ICSID Convention.

Most BITs provide their own definition of an investment that includes a broad general description which frequently refers to either "every kind of asset" or (in the case of U.S. BITs) to "every kind of investment". These general definitions are commonly illustrated by non-exhaustive lists of examples, including movable and immovable property, participation in companies,[18] money claims, rights to performance, intellectual and industrial property rights and concessions or similar rights.

Article 1139 of NAFTA contains a detailed definition of investment narrower than that found in typical BITs, excluding claims for money related to the sale of goods or services or short term credit in connection with a commercial transaction such as trade financing.

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[16] ICSID Case No. ARB/81/1.
[17] Award 1 September 2000 17 ICSID Rev-FILJ 382 (2003).
[18] e.g. *CMS Gas Transmission Company v. Argentina* 17 July 2003 42 ILM 788 (2003).

Indirect investments (e.g. the placement of funds in foreign markets) or the acquisition of existing investments by third parties give rise to further issues of interpretation.

In *Fedax v. Venezuela*[19] promissory notes were endorsed from a Venezuelan company to Fedax N.V., a company based in the Netherlands. Venezuela refused payment of the notes. The tribunal considered that as loans qualify as an investment under the ICSID Convention and promissory notes are evidence of a loan they fell within the meaning of "every kind of asset" in the Netherlands-Venezuela BIT. The acquisition of promissory notes by the Dutch claimant therefore constituted a foreign investment.

In *Mihaly v. Sri Lanka*[20] the tribunal held that expenses incurred in bidding for a public contract would not be protected as investments under the BIT (partly due to an express disclaimer made by the state when inviting bids in that case).

Treaty protection may be extended to indirect owners, including minority shareholders, through corporate vehicles of the requisite nationality.

In *Gami Investments, Inc. v United Mexican States*[21] GAMI, a US company, brought an expropriation claim under NAFTA in its own right in respect of its 14.18% minority shareholding in GAMI, Mexico's fourth largest sugar producer.

In *Waste Management v United Mexican States*[22] (Number 2) Waste Management, Inc., a US company, pursued its claims for expropriation under Chapter 11 of NAFTA in its own right in respect of its indirect interest in Acavarde, a Mexican company which had entered into a concession agreement for waste disposal services with the municipal authorities in Acapulco. Acavarde was a wholly-owned subsidiary of a Cayman Islands company, Acavarde Holdings Ltd., which was in turn wholly-owned by Sun Investment Co., another Cayman Islands company. At the time the concession agreement was entered into, Sun Investment Co. had been acquired by US Sanfill Inc., a US company owned and controlled by Waste Management, Inc., such that Acavarde could be described as a wholly-owned subsidiary of Waste Management, Inc. for the purpose of the claim under NAFTA. The tribunal held that

[19] ICSID Case No. ARB/96/3.
[20] *Mihaly International Corporation v Sri Lanka* ICSID Case No. ARB/00/2.
[21] Award, 15 November 2004
[22] ICSID Case No. ARB/(AF)/))/3, 30 April 2004 (NAFTA)

the nationality of the investment (as opposed to that of the investor) was irrelevant in determining whether the investor has the nationality of a party to NAFTA.

Protection of investments under BITs

The rights to protection of investments under a BIT derive from international law principles. With a view to encouraging foreign investment, BITs provide the investor with a variety of general protections. These standards generally entitle the investor to carry out its business free from unreasonable and discriminatory measures. Any violation of these rights by the host state (for example by expropriation, nationalisation or other forms of hindrance, deprivation of property, reduction of investor's rights by regulatory measures by the host state) may constitute a breach of the BIT entitling the investor to claim damages.

Expropriation may include "de facto expropriation", "creeping expropriation" or "indirect expropriation" which describe actions equivalent to a formal deprivation of property rights, destroying the economic value of the investment, e.g. if the state deprives the investor of its rights to use, let or sell its property by reason of a change of law.

In determining a claim for damages for breach of a BIT the tribunal will not normally have to judge whether the actions taken by the host state comply with the law of the host state, but must decide whether those actions are a breach of the treaty applying international law.

In *Metalclad Corporation v. United Mexican States*[23], under NAFTA Article 1110 (expropriation) the ICSID (AF) tribunal found that that expropriation included not only outright seizure but also covert or incidental interference with use of property which had the effect of depriving the owner, in whole or in significant part, of the use or economic benefit reasonably to be expected from the property, even if not necessarily to the obvious benefit of the host state. The tribunal held that the state's actions in permitting or tolerating the conduct of the municipality concerned amounted to unfair and inequitable treatment that breached NAFTA Article 1105. The host state's actions also included participating or acquiescing in the denial to the investor of the right to operate, notwithstanding the fact that the project had been fully approved by the federal government.

Some BITs go further by addressing the continuing requirements of the investment. For example, facilitating the employment of personnel from the host state, or providing positive

[23] Decision under ICSID Additional Facility, August 2000

rights with regard to the investment including the right to transfer money or know-how and the right to transfer profits, access to raw materials, liquidation of the investment and the making of related laws.

BITs normally contain clauses according to which the host state provides for treatment of the investor and the investment that is “fair and equitable” and often also for “full protection”. The assessment of what is fair and equitable is not to be determined by the host state in accordance with the standards used for its own nationals. Rather, that assessment has to be made in accordance with general principles of international law.

To provide an investor with “full protection and security” the host state is obliged to ensure that the agreed and approved security and protection of the foreign investor’s investment will not be withdrawn or devalued either by amendment of laws or by actions of its administrative bodies or agencies. It has also been held to have been breached where a state fails to maintain proper law and order.

BITs frequently provide for “most favoured nation” treatment, guaranteeing that foreign investors and investments are not to be treated less favourably than domestic investors or investments or less favourably than investors and investments from other foreign nations (including protections provided under BITs). Nearly all BITs list actions which will not be deemed to be treatment less favourable.[24]

Compensation for expropriation

Principles of international law will apply to the issue of compensation for expropriation and the question of whether expropriation is in the public interest. Expropriation clauses in BITs generally do not prohibit states from exercising expropriations or nationalisations. Rather, they aim to protect investors from unlawful expropriation; in particular, prohibiting any expropriation without full, prompt and effective compensation.

BITs frequently contain provisions setting out the conditions under which expropriation is permitted against payment of compensation, referring in particular to the public purpose or interest served by the expropriation. In accordance with general principles of international

[24] e.g. the German Model Treaty Article 3 provides: “Measures that have to be taken for reason of public security and order, public health or morality shall not be deemed “treatment less favourable””.

law BITs frequently state that expropriations must be non-discriminatory with regard to the nationality of the investor, the procedure and the compensation granted.

BITs frequently require "adequate, full and prompt" compensation to the expropriated investor.

The UN has passed several resolutions addressing expropriation, including the United Nations Resolution on Permanent Sovereignty on National Resources (Resolution 1803) which provides that, in compliance with generally acknowledged principles of international law, nationalisation and expropriation shall only be based on public utility and national interests, and the investor shall be paid appropriate compensation in accordance with the rules in force in the state taking such measures in the exercise of its sovereignty, and in accordance with international law.

Some BITs provide a basis for calculation of compensation. U.S. BITs frequently determine that compensation shall be:

> *"... equivalent to the fair market value of the expropriated investment before the expropriatory action was taken or became known, whichever is earlier; to be paid without delay; include interest at a commercial rate from the date of expropriation; be fully realizable; and be freely transferable at the prevailing market rate of exchange at the date of expropriation."*

The World Bank "Guidelines on the Treatment of Foreign Direct Investment" provide:[25]

> *"... the compensation will be deemed "adequate" if it is based on the fair market value of the taken asset as such value is determined immediately before the time at which the taking occurred or the decision to take the asset became publicly known."*

Compensation for breach of fair and equitable treatment

There is longstanding international jurisprudence that compensation should be awarded for breach of the international law on the international minimum standard of treatment or fair and

[25] Chapter IV.

equitable treatment. In the *Chorzow Factory* case[26] the Permanent Court of International Justice stated the principle in the following terms:

> "*The essential principle contained in the actual notion of an illegal act is that reparation must, as far as possible, wipe-out all the consequences of the illegal act and reestablish the situation which would, in all probability, have existed if that act had not been committed. Restitution in kind or, if this is not possible, payment of a sum corresponding to the value which a restitution in kind would bear; the award, if need be, of damages for loss sustained which would not be covered by restitution in kind or payment in place of it – such are the principles which should serve to determine the amount of compensation due for an act contrary to international law*."

> In *Amco v. Indonesia*[27] the arbitral tribunal provided the following guidance: "*It is well settled that the measure of compensation ought to be such as to approximate as closely as possible in monetary terms to the principle of restitution in integrum...,"* so that Claimants are "*put are in the position [they] would have been in, had they received the profits of the [investment agreement]."*

Requirement for consultation

As a pre-condition to formal arbitration most BITs require that an attempt is made at amicable settlement or "consultations for the purpose of finding a solution in a spirit of friendship." The time period for such consultations typically varies between three, six and twelve months, while in some cases no time limit is fixed. These requirements are frequently not strictly enforced by arbitral tribunals and may in some cases be treated as procedural rather than substantive requirements.

Applicable law of the dispute

The arbitral tribunal must decide the investment dispute according to the law applicable to the dispute. The investment contract or the BIT may contain an express choice-of-law clause.

Relatively few BITs contain explicit rules with regard to the law applicable to the merits of the dispute. If the BIT refers to the applicable law, reference is frequently made to "… the

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[26] Permanent Court of International Justice, Chorzow Factory Case, Merits, 1928, Series A No. 17, at 47 (as quoted in S.D. Myers, Inc. v. Canada, UNCITRAL Arbitration, Award on Damages (2002) at para. 311.
[27] Footnote 16 supra.

provisions of this Agreement, the international agreements both contracting Parties have concluded and the generally recognised principles of international law." It is generally accepted that the law applicable to the merits of a BIT dispute are principles of public international law, although some commentators have argued for the application of *lex mercatoria* or even equity provisions.

Article 42.1 of the ICSID Convention provides that, in the absence of agreement, the tribunal in an ICSID arbitration shall apply the law of the contracting state party to the dispute (including its rules of conflict of laws) and such rules of international law as may be applicable or, upon the parties' specific agreement, even on the basis of *ex aquae et bono*. The usual approach in a treaty arbitration is that the wording of the treaty, as the *lex specialis*, is decisive in the interpretation of the parties' rights and duties under that treaty. Only after it has been applied should the state party's national law be considered. A basic principle of international treaty interpretation is that international law, including the wording of the treaty itself, overrules national law in case of conflict.

RECENT DEVELOPMENTS IN INVESTMENT TREATY ARBITRATION

Nationality requirement

An issue arises as to whether protections intended to be given to an "investor" of a signatory state under a bilateral investment treaty may be inadvertently extended where the tribunal adopts an overly strict rather than purposive approach to the nationality requirement.

This issue highlights the potential for "treaty shopping" i.e. structuring investments through corporate vehicles located in jurisdictions which have investment treaties with the country in which the investment is to be made. It will be apparent that some of the above definitions of "investor" and "investment" allow the possibility of structuring investments through a chain of two or more holding companies, each of which may be located in different jurisdictions having investment treaties with the country in which the investment is made, allowing the possibility of multiple claims under the respective treaties in respect of the relevant investment interest. To address this, many BITs contain "denial of benefits" provisions whereby the Contracting State Parties reserve the right to deny the benefit of the treaty to any company controlled by nationals of a third party state.

The situation may also arise in which nationals of a signatory state to a BIT use a vehicle in the other signatory state to seek treaty protection in respect of their indirect investments in their own country.

In *Tokios Tokeles v. Ukraine*[28] Tokios Tokeles was a business enterprise established under the laws of Lithuania but 99% owned by Ukrainian nationals. Tokios Tokeles established a wholly-owned subsidiary in the Ukraine to carry on the business of advertising, publishing and printing in the Ukraine and elsewhere. They alleged that the Ukraine had engaged in actions affecting the Ukrainian subsidiary in breach of the Lithuania-Ukraine BIT, Article 1(2)(b) of which defined "investor" as "any entity established in the territory of Lithuania in conformity with its law and regulations". The BIT contained no "denial of benefits" provision.

The Respondent asserted that Tokios Tokeles was merely a nominal Lithuanian legal entity controlled by Ukrainian nationals and that the capital used was of Ukrainian origin, such that:

> *"…to find jurisdiction in this case would be tantamount to allowing Ukrainian nationals to pursue international arbitration against their own government, which … would be inconsistent with the object and purpose of the ICSID Convention"*

By a majority decision the ICSID tribunal constituted under the BIT nevertheless held that Tokios Tokeles was an investor within the meaning of the BIT noting that:

> *"…the treaty contains no additional requirements for an entity to qualify as an "investor" of Lithuania…Even assuming, arguendo, that all of the capital used by the Claimant to invest in Ukraine had its ultimate origin in Ukraine, the resulting investment would not be outside the scope of the Convention...The origin of the capital is not relevant to the existence of an investment…[I]n our view, the ICSID Convention contains no inchoate requirement that the investment at issue in a dispute have an international character in which the origin of the capital is decisive."*

In a November 2005 majority decision by an ICSID tribunal in *Aguas del Tunori v Bolivia*[29] the tribunal dismissed Bolivia's objections to jurisdiction made on the basis that the claimant was "controlled" by the US-based Bechtel Corporation and that the Netherlands shareholders,

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[28] Decision on Jurisdiction 29 April 2004.
[29] ICSID Case No. ARB/02/3.

by virtue of which Bechtel claimed the benefit of the Netherlands-Bolivia BIT, were merely "shell" companies which did not exert any real "control". Bolivia argued that the companies were set-up by Bechtel in 1999 in a post facto attempt to claim the benefit of the BIT. The majority of the tribunal held that:

> *"If an investor cannot ascertain whether their ownership of a locally incorporated vehicle for the investment will qualify for protection, then the effort of the BIT to stimulate investment will be frustrated."*

Definition of "investment"

In the case of *Mitchell v Democratic Republic of Congo*[30] an ICSID award was given in favour of the claimant whose law firm premises were sealed, documents seized and two lawyers imprisoned. The tribunal found that Mitchell, a US citizen, was an investor with an investment in the Democratic Republic of Congo (DRC), protected by a DRC/US BIT. The BIT was breached by the expropriation of Mr Mitchell's assets. The "investment" was constituted by the existence of property and files, documents and similar items, and rights over know-how and goodwill.

An application to annul the award was made under Article 52 of the ICSID Convention. The ad-hoc committee annulled the award, finding that there was no "investment" because the business did not constitute a "*contribution to the economic development of the host state*". The ad-hoc committee found that this was a requirement under the Convention, although not under the relevant BIT, and that the tribunal's award had said nothing about the contribution of the firm's services to the economic development of the host state. The ad-hoc committee therefore concluded that the award was tainted by a failure to state reasons.

Treaty claims/contract claims and "umbrella clauses"

Where there is a BIT as well as a private contract, the question has arisen in a number of investor-state arbitrations whether the arbitral tribunal constituted under the BIT has jurisdiction to resolve claims based on breach of contract, as opposed to claims amounting to breaches of international law standards under the BIT. The relevant contract may frequently include a jurisdiction clause which refers contractual disputes to another forum.

[30] ICSID Case No. ARB/02/07

In *Lanco International Inc. v. Argentine Republic*[31] a claim was brought under the US-Argentina BIT. The underlying contract between the investor and an agency of the Argentine government contained an exclusive jurisdiction clause submitting contractual disputes to a domestic administrative court in Argentina. The tribunal relied on Article 26 of the ICSID Convention which provided that consent to ICSID arbitration is "*to the exclusion of any other remedy*". The tribunal held that the exclusive jurisdiction clause in the contract did not prevent the submission of disputes to ICSID arbitration pursuant to the dispute resolution provision in the BIT. Moreover, the tribunal considered that the contractual agreement to submit disputes to an "administrative" tribunal could not be considered a previously agreed dispute-settlement procedure.

In *Vivendi v. Argentina*[32] the concession contract also contained a submission to the administrative courts in Argentina but the claims went beyond the scope of the concession agreement. The ICSID Annulment Committee drew a distinction between claims based on a breach of contract and claims based on breaches of treaty standards:

> "*In a case where the essential basis of a claim brought before an international tribunal is a breach of contract, the tribunal will give effect to any valid choice of forum clause in the contract [but] where the "fundamental basis of the claim" is a treaty laying down an independent standard by which the conduct of the parties is to be judged, the existence of an exclusive jurisdiction clause … cannot operate as a bar to the application of the treaty standard.*"

The Vivendi Annulment Committee observed that a state could breach a treaty without breaching a contract, and vice versa.

Some treaties elevate breaches of an investment contract with an investor by a state to the status of a treaty violation by means of an "umbrella clause"; for example, "*each Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by investors of the other Contracting Party*".[33] Current arbitral jurisprudence allows submission to investment treaty arbitration of claims based on a violation of the applicable treaty and, depending on the wording of the treaty, of other claims including those based on

[31] 5 ICSID Rev. 367 (1998).
[32] *Compania de Aguas del Aconquija SA and Vivendi Universal v Argentine*, Decision on Annulment July 2002.
[33] Switzerland-Philippines BIT Article X(2).

alleged violation of the parties' contract. Often private parties seek to take advantage of an umbrella clause in a BIT to avoid unfavourable contractual choice of law and jurisdiction clauses contained in contracts with a host state.

Two ICSID arbitrations illustrate the tension between a literal interpretation of the relevant BIT provisions and a wider contextual approach.

In *SGS (Societe Generale de Surveillance S.A.) v. Pakistan*[34] the parties had entered into a pre-shipment inspection agreement (the "PSI Agreement") providing for all claims to be resolved by arbitration in Pakistan. In 1998 SGS commenced proceedings in the Swiss courts alleging Pakistan's unlawful termination of the PSI Agreement. Those claims were eventually dismissed. Pakistan commenced arbitration against SGS under the PSI Agreement arbitration clause in 2000 and related proceedings were brought in the Pakistan courts. In 2001 SGS filed a Request for Arbitration at ICSID under the Switzerland-Pakistan BIT. Pakistan objected to the ICSID tribunal's jurisdiction on the basis that the dispute arose out of a contract rather than under the BIT. However, SGS asserted that the contractual disputes were elevated to treaty disputes by virtue of the "umbrella clause" at Article 11 of the BIT which provided:

> *"...either contracting party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other contracting party."*

The tribunal accepted that a literal reading of Article 11 would support SGS's position but rejected SGS's argument. The tribunal held that to permit the claim under Article 11 would be to impose consequences "*... so far-reaching in scope, and so automatic and unqualified and sweeping in their operation, so burdensome in their potential impact upon a Contracting Party"*.

The tribunal reasoned that such a result would enable investors to nullify the effect of dispute resolution provisions contained in state contracts. Rather, the tribunal held that:

[34] 6 August 2003 18 ICSID Rev. FILJ 301 (2003).

> *"Article 11 of the BIT should be read in such a way as to enhance mutuality and balance of benefits in the inter-relation of different agreements located in differing legal orders."*

The tribunal in *SGS v. Philippines*[35] reached an opposite conclusion on the meaning of a different BIT's umbrella clause. SGS wished to pursue claims for monies due under a comprehensive import supervision services agreement (the "CISS Agreement"). Article X(2) of the Switzerland-Philippines BIT provided: *"…each Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by investors of the other Contracting Party.*"

SGS asserted that this "umbrella clause" elevated contract claims into treaty claims. The tribunal adopted a literal interpretation of Article X:

> "*…interpreting the actual text of Article X(2), it would appear to say, and to say clearly, that each Contracting Party shall observe any legal obligation it has assumed …"*

However the tribunal did not follow the literal meaning of Article X to its full extent:

> "*Article X(2) makes it a breach of the BIT for the host state to fail to observe binding commitments, including contractual commitments, which it has assumed with regard to specific investments. But it does not convert the issue of the extent or content of such obligations into an issue of international law."*

Thus, whilst the ICSID tribunal accepted jurisdiction under the BIT to enforce contractual obligations, it held that the extent or content of those obligations fell to be determined pursuant to the dispute resolution provisions in the CISS Agreement. The majority of the tribunal granted a stay to allow the specified tribunal (the Philippine courts) to hear and decide those issues.

In 2006 an ICSID tribunal in *El Paso v Argentina*[36] rejected an argument by El Paso that contractual breaches should be considered breaches of the US-Argentina BIT. The tribunal held that to elevate such breaches would be "*destructive of the distinction between the*

[35] Decision on Jurisdiction 6 August 2003 18 ICSID Rev. FILJ 301 (2003). SGS v. Philippines: ICSID Case No. ARB/02/6

[36] El Paso v. Argentina:- ICSID Case No. ARB/03/15 (US/Argentina)

national legal orders and the international legal orders" and would open the floodgates to claims for breaches of national laws.

In *Eureko*[37] a Dutch company with a 20 percent share in a Polish insurance company entered into a share purchase agreement with the Polish state Treasury. Shares were to be sold to Eureko in stages under a privatisation process. The share purchase agreement was governed by Polish law and contained a jurisdiction clause referring disputes to the Polish courts. When the government delayed privatisation Eureko claimed relief under the Netherlands-Poland BIT. Eureko claimed that the Polish state had breached the public international law right to fair and equitable treatment. The BIT required each state to "*observe any obligations it may have entered into with regard to investments of investors of the other contracting party*". A majority of the three-member tribunal concluded that this provision should be construed as an umbrella clause which elevated the state's contractual breaches to the international law plane.

Most favoured nation clauses

Most Favoured Nations ("MFN") clauses often appear in BITs. They therefore apply only to arbitration brought pursuant to a BIT rather than pursuant to a private contract to arbitrate.

Many BITs contain a clause providing that a qualifying investor under the BIT can avail itself of the rights offered by the host state to nationals of other (third) states where those rights are more favourable. The issue arises as to whether this treatment extends to procedural as well as substantive rights.

In the *Maffezini* case[38] the tribunal found that the MFN clause in the Argentina-Spain BIT encompassed international dispute resolution procedures found in another BIT with Argentina. This suggested that an MFN clause could be applied to procedural as well as to substantive rights under the investment treaty.

In *Gas Natural v Argentina*[39] the tribunal ruled that the MFN clause in the Spain-Argentina BIT entitled the investor to invoke the more favourable dispute resolution provisions found in the investment treaty between the US and Argentina. The investor was thereby entitled to ignore the requirement in the Spain-Argentina BIT to have recourse to the local courts for a

[37] Eureko B.V. v. Poland
[38] ICSID Case No. ARB/03/10 Decision of Tribunal on Preliminary Questions of Jurisdiction 17 June 2005.
[39] ICSID Case No. ARB/03/10

period of 18 months before resorting to international arbitration. The tribunal treated access to arbitration as part of the substantive rights offered under the BIT and rejected Argentina's contention that the MFN clause did not extent to "procedural" matters.

However, the tribunal made no reference to the earlier decision in *Plama Consortium Limited v Bulgaria*[40] in which the tribunal held that the MFN clause did not incorporate by reference dispute settlement provisions set-forth in another treaty. The Plama tribunal ruled that the MFN clause did not apply to procedural matters because there was no express indication to that effect in the relevant treaty.

In *Telenor*[41] the Norwegian claimant sought to use a Hungary-Norway BIT to invoke an MFN clause to take advantage of provisions for a consent-to-arbitration which would allow them to bring a claim for "fair and equitable treatment". The BIT Hungary-Norway BIT only provided for recourse in respect of expropriation claims. The tribunal refused to take jurisdiction to hear the claim, stating "*in these circumstances, to invoke the MFN Clause ... Is to subvert the intention of the parties to the basic treaty, who have made it clear that this is not what they wish.*"

In the *Suez* case[42] the tribunal upheld reliance on an MFN clause by Spanish claimants in a claim against Argentina arising out of the Argentine financial crisis. The claimant's sought to use provisions in the France-Argentina BIT to avoid a requirement to pursue local court remedies for 18 months before launching international arbitration. The tribunal held that since the MFN clause was worded to include "all matters" it could find no reason why the dispute resolution procedure should be excluded.[43]

Defence of necessity/essential security interest

CMS v Argentina[44] was the first case to reach the award stage of the billions of dollars of claims against Argentina following its 2002 financial crisis. CMS, a minority shareholder in the Argentine firm Transportadora de Gas del Norte (TGN), filed its claim at ICSID in 2001.

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[40] ICSID Case No. ARB/03/24 Decision on Jurisdiction 8 February 2005.
[41] Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A. v. Argentine Republic: ICSID Case No. ARB/03/19
[42] Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A. v. Argentine Republic: ICSID Case No. ARB/03/19
[43] The same decision on jurisdiction was reached on similar grounds in the National Grid case (National Grid PLC v Argentine Republic ICSID Case No. ARB/03/19 decision of 20 June 2006
[44] Decision of 12 May 2005

Initially, the firm objected to a freeze on contractually agreed tariff adjustments which had been intended to increase gas prices adjusted in line with a US inflation index. Subsequently, the investor also objected to a series of emergency measures adopted by the Argentine authorities in early 2002 in response to that country's growing financial crisis. Certain of these measures resulted in CMS being paid in (increasingly devalued) pesos, contrary to the contractually agreed terms. The tribunal accepted that the Argentine government had breached CMS's right to fair and equitable treatment.

Among Argentina's defences were that its actions had been necessary to avert an imminent economic and social collapse. The doctrine of necessity is to be found in customary international law. Argentina also argued that its actions fell under the general exceptions provisions of the BIT, which permitted parties to take measures "*necessary for the maintenance of public order ... or the protection of its own essential security interests*." These arguments were rejected by the Tribunal.

In *LG&E v Argentina*[45] the tribunal accepted a similar defence of necessity by the Argentine Government. The tribunal found that the Argentine Government was absolved from a duty to pay compensation for damages incurred during the 17 month period of its financial crisis, when Argentina was held to have been in a state of necessity. The tribunal held that Argentina was nevertheless liable for damages related to violations occurring outside of that 17 month period. In giving its award the ICSID tribunal rejected LG&E's claims that it had suffered expropriation and arbitrary measures contrary to the US-Argentina BIT, but held that Argentina was in breach of its treaty obligations fair and equitable treatment, treatment in accordance with international law, and the obligation to refrain from discriminatory measures impairing investments.

Parallel proceedings/conflicting decisions

There has been a growing awareness of the potential difficulties that arise from separate and parallel investment arbitration proceedings arising from the same or similar events between the same or related parties.

Parallel proceedings often involve the same set of facts and the same applicable law arising under different BITs being determined by different tribunals. The dramatic proliferation of

[45] ICSID Case No. ARB/02/1

investment treaties between states has greatly increased the options available to aggrieved investors. The notorious cases of *CME v. Czech Republic* and *Ronald Lauder v. Czech Republic*[46] resulted in two arbitration awards reaching different conclusions based on the same set of circumstances, albeit the arbitrations were initiated by different parties under two separate investment treaties.

The tribunal in *Joy Mining Machinery Ltd. V. Egypt*[47] expressed the position commonly adopted by international arbitration tribunals:

> "*There has been much argument regarding recent cases, notably SGS v. Pakistan and SGS v. Philippines. However, this Tribunal is not called upon to sit in judgment on the views of other tribunals. It is only called to decide this dispute in the light of its specific facts and the law, beginning with the jurisdictional objections*."

The decisions of prior tribunals are nevertheless routinely cited by the parties in argument before subsequent tribunals and referred to in subsequent investment arbitration awards. Whilst prior decisions in international investment arbitrations have no strict precedential effect, regard is had to relevant prior decisions such that the development of an international arbitral jurisprudence may be observed.

Res judicata and *lis pendens* have been recognised as general principles of international law. *Res judicata* is a claim, issue or cause of action which is the subject of a judgment, award or other determination considered final as to the rights, questions and facts which are the subject of the dispute. Re-litigation or reconsideration of the particular matters decided, between the same parties, is generally barred, principally on public policy considerations. A "triple identity" test is normally applied, of parties, cause and subject matter.

There seems to be a widespread acceptance that arbitral awards may have *res judicata* effect.[48] The Iran U.S. Claims Tribunal has observed:

> "*As to the alleged risk the Respondents could be subject to multiple liabilities, the Tribunal notes … the principles of res judicata or estoppel would bar Amoco in most*

[46] Case RH 2003: 55; UNCITRAL Award September 2001.
[47] ICSID case ARB/023/11 Award on Jurisdiction 6 August 2004.
[48] *Amco v. Indonesia* Decision on Annulment 16 May 1986 1 ICSID Reports 509.

> *if not all, legal systems from successfully prosecuting a claim, the merits of which have finally been determined by this Tribunal*".[49]

Many commentators believe that addressing the problem of multiple proceedings and inconsistent decisions is likely to be a major challenge for investor-state arbitration in the near future[50].

Some of the potential conflicts arising out of individual disputes might be addressed by consolidation of proceedings or the joinder of additional parties. However, such consolidation or joinder will normally require the agreement of the parties and such agreement will be difficult to obtain.[51]

Under Article 1126 of NAFTA separate claims involving common question of fact and law may be consolidated if it is "in the interest of the fair and efficient resolution of those claims" to bring them under the purview of a single tribunal. This has recently occurred in the case of ongoing NAFTA arbitrations brought by a number of Canadian forestry products companies against the US, under a "Consolidation Tribunal" made in November 2005 at the request of the US government.[52] In making its order, the first to order consolidation of parallel NAFTA investor-state arbitrations, the NAFTA Consolidation Tribunal specifically acknowledged the controversy caused by the conflicting *CME/Lauder* arbitrations.

Appellate body vs ad hoc annulment

Possible solutions to the issue of conflicting or inconsistent arbitral decisions have included suggestions for a new investment arbitration appellate body:

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[49] Iran-U.S. Claims Tribunal Case No. 56 (Chamber Three) Award No. 310-56-3 Partial Award, 14 July 1987 para. 18.

[50] Cremades & Cairns "*Contract and Treaty Claims and Choice of Forum in Foreign Investment Disputes*": "Arbitrating Foreign Investment Disputes: Procedural and Substantive Legal Aspects " (Kluwer 2004). As further examples of apparently inconsistent decisions, the tribunal in the ICSID Decision of 6 February 2007 in *Siemens A.G. v Repuiblic of Argentina* ICSID Case No. ARB/03/08 distanced itself from the tribunal's assessment of expropriation as a matter of proportionality in *Techicas Medioambientales Tecmed S.A. v The United Mexican States*, Case No. ARB(AF)/00/2, whereas in the same year the tribunal in *Azurix v. Argentina* ICSID Case No. ARB/01/12 followed the *Tecmed* test. Meanwhile, several cases in 2006 distanced the reasoning of the tribunal in *Plama Consortium Limited v. Republic of Bulgaria* ICSID Case No. ARB/03/24, which refused to interpret a Most Favoured Nation (MFN) clause to extend the available claims beyond those for expropriation. By contrast, *Telenor Mobile Communications A.S. v. The Republic of Hungary* ICSID Case No. ARB/04/15 the tribunal did extend the available claims from expropriation to fair and equitable treatment by virtue of an MFN clause.

[51] The problems of inconsistency faced in the CME/Lauder v. Czech Republic arbitrations could have been mitigated if the parties had been able to agree the proposal for consolidation.

[52] *Canfor Corporation, Tembec et al.*

> "*The case for an integrated system of administering international justice is a strong one, not least in terms of the consistent development of the law. It is strongly arguable that cases are better decided by judges of experience than by arbitrators selected ad hoc for the purpose of a single case. Arbitration is, however, an important component of the international system and cannot be done away with. We should contemplate the possibility that its value may be enhanced if it is linked to a system of appeal.*
>
> *The choices before us are simple. One alternative is to have no appeals at all – in the sense of review of the merits. ... Another is that we have the present unregulated and haphazard system – which is developing empirically without any real planning and may not be entirely satisfactory. The third is that we go the whole way and try to establish a proper appeals arrangement. But if we are to do that, how is it to be structured? The solution to this last question is so fraught with difficulties that we may find that, despite its idealistic appeal, it is not a practical alternative*."[53]

An appellate body to review investment treaty decisions would provide the perception of consistency and predictability which would in turn assist in legitimising and institutionalising investor-state dispute settlement, making the system more sustainable.

The latest US Free Trade Agreements and the new US Model BIT address the possibility of the establishment of such an appellate body as follows:

> "*If a separate multilateral agreement enters into force… that establishes an appellate body for purposes of reviewing awards rendered by tribunals constituted pursuant to international trade or investment agreements to hear investment disputes, the Parties shall strive to reach an agreement that would have such appellate body review awards rendered... in arbitrations commenced after the appellate body's establishment*."[54]

On 15 October 2004 ICSID released a "*Discussion Paper About Possible Improvements to the Framework for ICSID Arbitration*". This raised for discussion the prospect of a single appeal mechanism, as an alternative to multiple appellate mechanisms arising from different

[53] "*Aspects of the Administration of International Justice*", Elihu Lauterpacht. Published May 1991.
[54] Article 10.19.6 US-Chile FTA; Article 15.19.10 US-Singapore FTA; Article 28.10 new Draft US Model BIT.

investment treaties. The proposal was that ICSID would pursue an Appeals Facility on the basis that this would operate as a single appellate mechanism.

The features of such an ICSID Appeals Facility (set out in an Annex to the Discussion Paper) would include a set of Appeals Facility Rules adopted by the ICSID Administrative Council, such that no treaty amendments would be required, for use in conjunction with ICSID cases, ICSID Additional Facility cases and *ad hoc* UNCITRAL Arbitration Rules cases. Availability of the Appeals Facility would depend upon the consent of the parties to the dispute. The Appeals Facility Rules would provide for the establishment of an appeals tribunal of 15 persons selected by the ICSID Administrative Council upon nomination by the ICSID Secretary General. Appeals would be heard by a three-member appeals tribunal appointed by the Secretary General after consultation with the parties.

Grounds for an appeal would be the existing five grounds for annulment of an ICSID Award under Article 52 of the ICSID Convention, clear error of law or serious errors of fact (narrowly defined to preserve deference to findings of facts of the arbitral tribunal). The Appeal Tribunal would have the power to uphold, modify, reverse or annul the award. If the award was annulled, modified or reversed either party could submit the case to a new arbitral tribunal.

However, in a second Discussion Paper on procedural reforms issued by ICSID on 2 June 2005 these proposals for an appeals facility were shelved, having regard to feedback received from member-governments and others, with the observation that if such an appeals facility is to be brought into being, ICSID would be its natural home. [55]

The inconsistency of decisions continues to cause concern and was one of the reasons for the proposal to create an appeals facility.

Despite the various discussion papers and proposals, the new ICSID rules which came into force on 10 April 2006 for arbitration agreements agreed after that date do not contain a provision for appeal.

[55] See, for example, the submissions by the Geneva-based South Centre, reflecting feedback received from a grouping of developing countries, at http://www.southcentre.org/. There report suggests that third party submissions tend to be hostile to developing countries, and that ICSID should take further steps to include developing countries in discussion of its reform proposals.

Recent decisions have provoked additional concerns that the current ICSID arbitration annulment process is leading to annulment decisions straying into the area of substantive review of the original award.[56] The *George Mitchell ad hoc* committee annulment decision referred to above[57] has been criticised on this basis. Although the decision was based on the finding that the original tribunal failed to state its reasons in its award, according to some commentators the annulment committee went further in its analysis than was appropriate.

The Committee set out its own view of what Mitchell needed to do to qualify as an investor: "*in the opinion of the committee it is necessary for the contribution to the economic development or at least the interests of the state…to be somehow present in the operation…it would be necessary for the award to indicate that…the claimant had concretely assisted the DRC, for example by providing it with legal services*". Some commentators have argued that this statement not only exceeds the purpose of the *ad hoc* annulment committee but is also a novel characterisation of the law, in that it requires that services be provided to the host state.

Investment treaty arbitration and public interest/*amicus* briefs

The nature of the issues that arise in investment treaty arbitrations have led to increasing calls for greater flexibility in the admission of submissions from interested third parties (*amici curiae*) as well as for access by the public to open hearings in appropriate cases.

In *Mondev International Ltd. v. United States* a NAFTA tribunal concluded there was no confidentiality requirement under the ICSID Additional Facility Rules which prevented the U.S. (pursuant to a Freedom of Information Act request) from unilaterally releasing the contents of its communications regarding the arbitration.[58]

A well-publicised and colourful illustration of the sensitive issues of national and public concern that may arise in investment treaty arbitrations is provided by the NAFTA arbitration of *Loewen Group Inc. and Ray Loewen v. United States*.[59] This was the first case lodged against the United States under NAFTA. The Loewen Group ("LGI") was a Vancouver-based "death care" business that became one of the largest funeral home operators in North

[56] As was stated by the Vivendi *ad hoc* annulment committee "provided the reasons can be followed and relate to the issues…their correctness is beside the point in terms of article 52(1)(e)". (Decision of 3 July 2002).
[57] ICSID Case No. ARB/02/07.
[58] ICSID Case No. ARB(AF)/99/2.
[59] ICSID Case No. ARB (AF)/98/3 Decision on Competence and Jurisdiction 5 January 2001.

America. LGI bought a funeral home in Jackson, Mississippi that entered into funeral insurance contracts with O'Keefe, a local competitor.

O'Keefe sued LGI in the Mississippi state court. During the jury trial O'Keefe's lawyers used (in the words of the ICSID tribunal) xenophobic and racist invective against Loewen and LGI which the judge did nothing to prevent. The jury awarded damages against LGI in the amount of $500 million. The Mississippi appeals procedures required LGI to post a bond of 125% of the verdict appealed against as a condition of a stay of execution, pending the appeal. LGI was unable to raise this amount. As O'Keefe threatened immediate seizure of their assets LGI paid O'Keefe $170 million to settle the claim.

LGI and Loewen filed an investment arbitration against the U.S. under Chapter XI of NAFTA under the ICSID Additional Facility Rules. The NAFTA tribunal held that a court judgment can be considered a governmental "measure" giving rise to liability for discrimination, failure to grant "fair and equitable treatment" and expropriation without adequate compensation. The arbitrators held that the combination of anti-Canadian rhetoric, arbitrary court procedures, the excessiveness of the jury verdict and the effective lack of a right of appeal combined to constitute a "denial of justice" and a breach of the NAFTA obligation to provide qualifying investors with fair and equitable treatment.

However (and to the surprise of some commentators), the tribunal dismissed the case on two grounds. Firstly, LGI had not sufficiently exhausted available local remedies, as required under NAFTA:

> "*Too great a readiness to step from outside into the domestic arena, attributing the shape of an international wrong to what is really a local error (however serious) will damage both the integrity of the domestic judicial system and the viability of NAFTA itself...*".

Secondly, due to a bankruptcy reorganisation, LGI had lost the requisite Canadian nationality and the tribunal held that it no longer had jurisdiction to decide the case under NAFTA. There is some question whether there is such a "continuing nationality" requirement under public international law, requiring the claimant to have the requisite nationality up to the time of the award. It is generally considered sufficient to have the requisite nationality at the time the claim arose and at the time the claim was brought. In addition, LGI had also failed to

establish discrimination because it been unable to identify an American investor in "like circumstances".

In October 2005 the Colombia US District Court rejected an application by Mr. Loewen to vacate the award, on the basis that the application was time-barred, and that the award had dispensed with the NAFTA Chapter 11 claims of both the Loewen Group and Loewen himself.

The amended ICSID arbitration rules apply to arbitration agreements entered into after 10 April 2006 and make express provision for the tribunal to permit *amicus curiae* briefs in article 37(2) of the ICSID Rules. Under article 32(2) third parties may apply to the tribunal for permission to attend an ICSID hearing.

The *Biwater Gauff* case[60] concerned alleged expropriation of the claimant's investment in water and sewerage systems in Dar es Salaam, Tanzania. Five NGOs petitioned the tribunal for permission to make *amicus* submissions, attend the hearing and have access to documents. They maintained that the dispute raised issues of public health, human rights and sustainable development in the region. The tribunal stated that to determine whether to permit written *amicus* briefs it would consider whether (1) the submission would address an issue within the scope of the dispute; (2) the submission would assist the tribunal to determine an issue by bringing a perspective, knowledge or insight different to those of the parties; and (3) the non-party has a significant interest in the proceedings.

In reaching its decision the tribunal reiterated that article 32(2) did not afford non-parties general standing in the arbitration, but restricted them to the right to make submissions to assist the tribunal. The tribunal decided to permit the five petitioners to provide a joint written submission of no more than 50 pages. The petitioners were not permitted access to documents because the tribunal considered that sufficient information was in the public domain to enable them to address the issues in which they had an interest.

Suez v Argentina[61] was initiated under the previous ICSID rules in which there was no express provision for the tribunal to permit *amicus* briefs. The claimants commenced arbitration proceedings against the Argentine Republic to recover losses allegedly sustained

[60] Biwater Gauff (Tanzania) Ltd v. United Republic of Tanzania:- ICSID Case No. ARB/05/22.
[61] Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A. v. Argentine Republic:- ICSID Case No. ARB/03/19, decision delivered on 17 February 2007.

in respect of their investments in water distribution and treatment services in Buenos Aires. Following its economic crisis in 1999 the Argentine government devalued the peso which resulted, the claimants alleged, in the expropriation of their investment.

In January 2005 five NGOs filed participation petitions. In May 2005 the tribunal refused access to hearings, deferred a decision on access to documents and set down conditions by which the NGOs could apply for leave to make submissions. The tribunal subsequently granted the applications, founding jurisdiction to permit *amicus* briefs on article 44 of the ICSID Rules and under its residual power to decide procedural questions not covered by the ICSID rules.

Free Trade Agreements

The United States-Australia Free Trade Agreement was the first post-NAFTA Free Trade Agreement (FTA) the U.S. was scheduled to sign with another capital-exporting state. The final text was signed on 8 February 2004 and contained no provisions on investor-state arbitration. Recent FTAs that the U.S. has signed with capital-importing countries do not include investment chapters or investor-state dispute resolution based upon NAFTA.

Both the U.S.-Chile and U.S.-Singapore FTAs add language to the "fair and equitable treatment" standard to the effect that it "prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments". This has been described by some commentators as a regressive retreat by the US to bare minimum standards of investment protection.

In response to recent decisions on the effect of MFN clauses (referred to above) clear limitations on MFN clauses have been included in the most recent draft of the U.S.'s Model Bilateral Investment Treaty.[62]

These developments reflect a growing disquiet amongst U.S. policy makers concerning some of the unintended consequences of the existing investment treaty regime:

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[62] The Central American Free Trade Agreement (signed by the parties in August 2004) includes a footnote to the article dealing with most favoured nation (MFN) treatment:
"*The Parties note the recent decision of the Arbitral Tribunal in Maffezini ICSID Case No. ARB/97/7. The Parties share the understanding and intent that this clause does not encompass international dispute resolution mechanisms such as those contained in Section C of this Chapter, and therefore could not reasonably lead to a conclusion similar to that of the Maffexini case*".

> *"Many business and political leaders [in the United States] still support arbitration as the preferred method to resolve disputes between host countries and foreign investors. However ... the United States [is now] pursuing a course and a tone quite different from when negotiating NAFTA. Moreover, vocal opposition to investment arbitration has been expressed by important segments of the media and several non-governmental organisations ... after claims for unfair treatment were filed against the United States government, arbitration looked different than when American companies were the investors."*[63]

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[63] Guillermo Aguilar Alvarez and William W. Park *"The New Face of Investment Arbitration: NAFTA Chapter 11"* 2004 Mealey's International Arbitration Report (January).

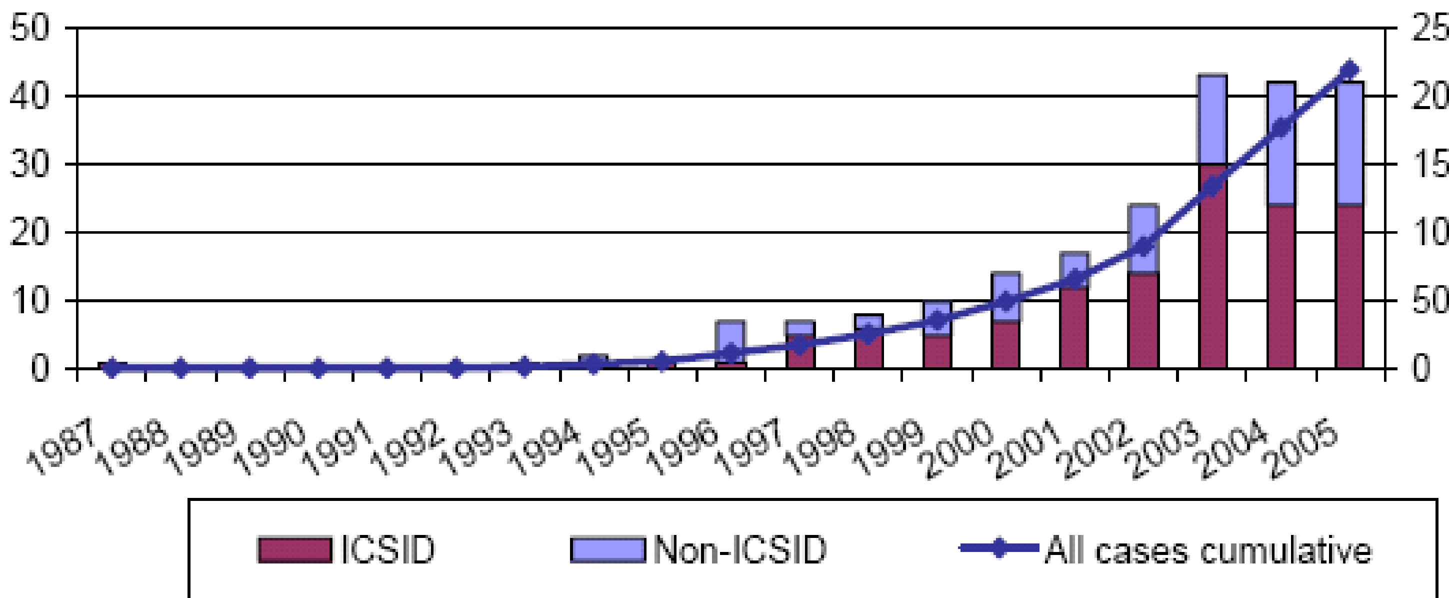
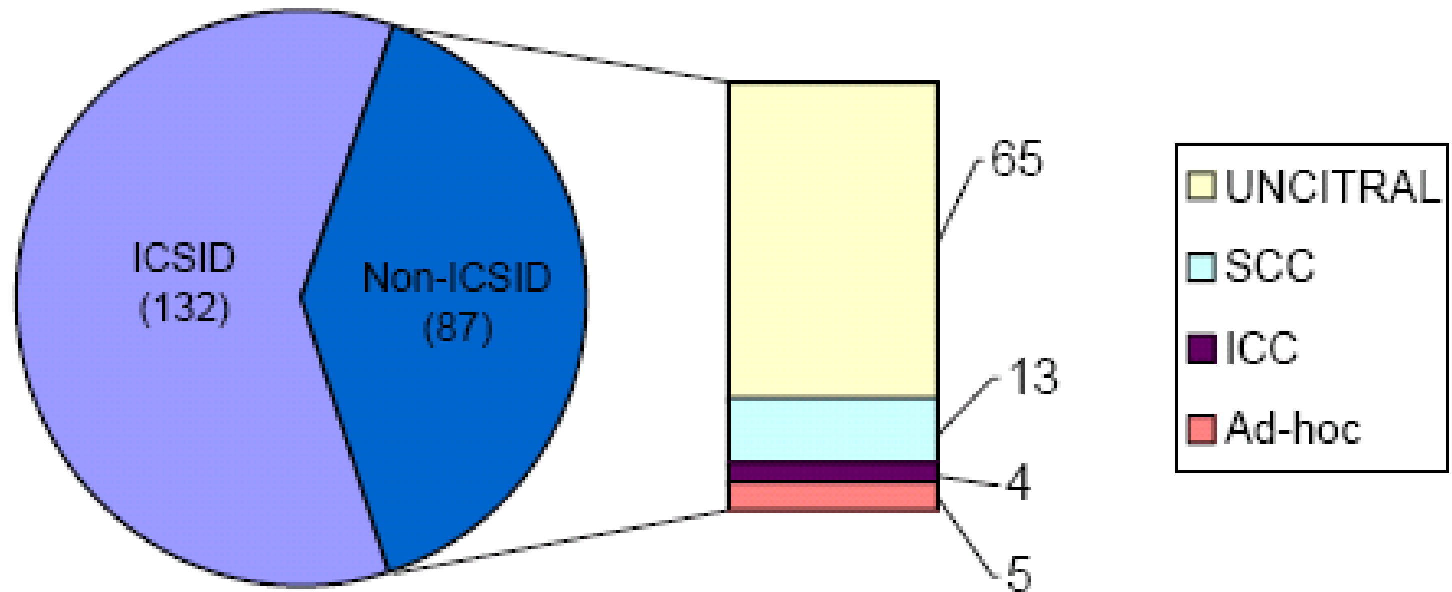


Figure 1. Known investment treaty arbitrations, (cumulative and newly instituted cases, by year) a/

a/ means as of November 2005

Figure 2. Disputes by forum of arbitration a/



a/ means as of November 2005