

# INTERNATIONAL LAW ASSOCIATION

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### INTERNATIONAL LAW ON FOREIGN INVESTMENT

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## FINAL REPORT

### Table of Contents

(1) Sources and Institutional Factors .....	3
(a) Applicable Law .....	3
(b) Interactions between Investment and Non-Investment Obligations .....	4
(c) Investment, Investor, Nationality and Shareholders .....	5
(d) Multilateral Investment Rules .....	5
(e) Trade and Investment .....	6
(f) The European Union and Bilateral Investment Treaties .....	6
(2) Substantive Standards .....	7
(a) Admission of Investments and the Right to Establishment .....	8
(b) Standards of Treatment .....	9
(c) MFN Treatment .....	9
(d) Expropriation.....	10
(e) Taxation.....	11
(f) State Responsibility and Attribution .....	12

(g) Emergency Exceptions: State of Necessity and Force Majeure .....	12
(h) Substantive Transparency .....	13
(i) Anti-corruption.....	14
(j) Corporate Social Responsibility.....	15
(k) Investment Insurance.....	16
(3) Dispute Settlement and Enforcement.....	16
(a) Methods of Dispute Settlement .....	16
(b) Procedural Transparency.....	17
(c) Independence, Impartiality and Duty of Disclosure of Arbitrators .....	17
(d) Consent to Arbitration.....	18
(e) Jurisdiction and Admissibility.....	19
(f) Investments “In Accordance with Host State Law”.....	19
(g) The Jurisdictional Threshold of a Prima-Facie Case.....	20
(h) The Relationship between International Tribunals and Domestic Courts .....	21
(i) Parallel Proceedings.....	21
(j) Compensation, Damages and Valuation .....	22
(k) Review of Awards.....	23
(l) Appellate System .....	24
(m) Compliance and Enforcement .....	24
(n) Doctrine of Precedent.....	25
(o) Tribunal’s Powers versus Party Autonomy .....	25
Concluding Remarks .....	26

This is the final report of the Committee on the International Law on Foreign Investment. It follows from the first report, presented in Toronto in 2006, by dealing in more detail with the technical legal issues seen to be central to the content and further development of this area of international law, both on a substantive and procedural level. By contrast, the first report concentrated on the main actors, major ideological influences and the main policy questions arising out of investment law issues. The present report is not a full restatement of international investment law. Indeed such a restatement could not be made in the available space. However, it may act as a “road map” to the main types of issues that a possible future restatement might contain.

The structure and content of the report follows closely the research undertaken by Committee members and, in relation to certain chapters, with the assistance of specialist external consultants towards their contributions to the *Oxford Handbook of International Investment Law* (Oxford University Press, 2008).<sup>1</sup> However, it is not a summary of the book’s contents. Rather the individually authored chapters offer a starting point for analysis of certain issues and controversies created by each field of study. The Report seeks to show where problems and inconsistencies remain. These signify the choices that will need to be made in the future development of the subject but without coming to final conclusions upon them. Such an aim would not be feasible given that international investment law is a rapidly developing field and one in which opinions as to the best way forward differ considerably. This is so because the field emerges out of treaty law which seeks to resolve uncertainties present in customary international law which itself can be described as offering an incomplete body of rules capable of dealing with all the varied aspects of the international regulation of foreign investment.<sup>2</sup> In addition the subject has been enmeshed in significant differences of opinion as to the proper balance of rights and obligations that all the main actors, whether home or host states or investors, should possess.<sup>3</sup>

This report is divided into three parts. The first, “Sources and Institutional Factors”, considers the more general conceptual issues that the development of this field of international law entails. The second part, “Substantive Standards”, covers in some detail the main issues arising out of the core substantive provisions of international

<sup>1</sup> Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds) *The Oxford Handbook of International Investment Law* (Oxford, Oxford University Press, 2008) (hereafter *Oxford Handbook*). The external consultants are: Dorothee Gottwald, Louis-Philippe Gratton, Christina Knahr, Abba Kolo, Ursula Kriebaum, Ian A Laird, Irmgard Marboe, Borzu Sabahi. This report includes two sections that have been added since the publishing of the Oxford Handbook: “The European Union and Bilateral Investment Treaties” by Anne van Aaken and “Investment ‘in Accordance with Host State Law’” by Christina Knahr.

<sup>2</sup> See further for example the Judgement of the International Court of Justice in the *Case Concerning Ahmadou Sadio Diallo* (Guinea v Democratic Republic of the Congo) Preliminary Objections, General List No.103 Judgment 24 May 2007 at para.88.

<sup>3</sup> See further the First report of the ILA Committee on the International Law on Foreign Investment, Toronto, 2006, in *ILA Report of the Seventy Second Conference, Toronto, 2006* (London, ILA, 2006) at 410 et seq.

investment agreements (IIAs) as well as certain new and emerging issue areas that may inform the future development and interpretation of such agreements. The third part, “Dispute Settlement and Enforcement”, covers the main procedural issues arising in relation to the conduct of investor-state arbitration. This is a major recent source of interpretation of IIAs, the main trends of which are covered in section two. Here the concern is to identify and analyse how the very process of investment arbitration is conducted and what types of legal questions this raises.

### (1) Sources and Institutional Factors

Under this heading, the report deals with certain general issues that arise out of the nature, structure, sources and definitions of international investment law. It begins with the question of which system of law actually applies to investment issues, whether national or international. It continues with the analysis of how investment obligations tie in with non-investment obligations. Thirdly, it addresses the definitions of certain key terms which define the subject matter of IIAs, centring on the notions of “investment” and “investor” as well as issues related to corporate ownership and shareholding as aspects of covered investments. Fourthly, the question of whether multilateral rules for investment should be developed is revisited, so as to consider whether it makes sense, notwithstanding the failures of negotiations for a Multilateral Agreement on Investment (MAI) in the OECD and the rejection of negotiations of investment rules within the WTO, to consider again the value of such an exercise. Finally the influence of international rules on trade regulation upon the development of international investment rules is discussed.

#### (a) Applicable Law

There are significant choices to be made with regard to the relationship between different systems of law as the applicable law of an investment dispute, especially in relation to investment agreements or treaties that do not address this issue explicitly.<sup>4</sup> The principle of *pacta sunt servanda* has served as a vehicle for internationalising applicable law in investment arbitration under three different approaches: (a) *pacta sunt servanda* as a choice-of-law principle (the so called “horizontal approach”, in the sense that it reflects a notion of equality, with the contract parties being on an equal footing; see *Saudi Arabia v. Aramco*<sup>5</sup>); (b) *pacta sunt servanda* as applicable law (the “direct approach”, under which the principle applies directly as part of the proper law of contract; see *Lena Goldfields v. Soviet Union*<sup>6</sup>); (c) *pacta sunt servanda* as a rationale of applicable law (the vertical approach, under which national law has to be applied, if not exhausted, prior to international law; annulment committee in *Klückner v. Cameroon*<sup>7</sup>).

However, even in relation to explicit provisions, such as Article 42 of the ICSID Convention, there is a degree of discretion in the actual interpretation of the applicable law question, depending in part on whether the tribunal is faced with a contract claim or a treaty claim. With regard to the former, while the principle of party autonomy is generally considered to be the bedrock of international commercial arbitration, yet in investment arbitration it often yields to the principle *pacta sunt servanda*. Despite the fact that the text of Article 42(1) of the ICSID Convention gives prominence to the principle of party autonomy, commentators have doubted whether an explicit choice of the law of the host state will prevent a tribunal from resorting to public international law (see annulment decisions in *Amco v. Indonesia*,<sup>8</sup> *Wena Hotels v. Egypt*<sup>9</sup>). Outside ICSID, it might well be that tribunals have a choice between the horizontal and the vertical approach (*CME v. Czech Republic*<sup>10</sup>).

With regard to treaty claims, an investor implicitly accepts the applicable law choices contained in the treaty as they are strings attached to the host state’s consent to international arbitration. On the other hand, even in the absence of a specific treaty provision, arbitral practice shows the important (albeit not exclusive) role of international law in resolving investment disputes.

In summary, it appears clear that the internationalisation of investment disputes has led to a stronger acceptance of international rules as being key to the determination of investment disputes. That this conclusion should be taken by international tribunals is perhaps not surprising, given that they represent an alternative to direct diplomatic

<sup>4</sup> See further Ole Spiermann “Applicable Law” in *Oxford Handbook* above n.1 ch.3.

<sup>5</sup> 27 ILR 117 (1963).

<sup>6</sup> *Lena Goldfields Arbitration* Cornell Law Quarterly (1950), Annual Digest 5 (1929-30)

<sup>7</sup> *Klückner v Cameroon*, ICSID Case No Arb/74/3, Award, 21 October 1983, 2 ICSID Reports 9; Decision of *ad hoc* Committee, 3 May 1985, 1 ICSID Rev-FILJ 89 (1986).

<sup>8</sup> Decision of *ad hoc* Committee, 16 May 1986, 25 ILM 1439 (1986).

<sup>9</sup> ICSID Case No.ARB/98/4, Decision of the *ad hoc* Committee, 28 January 2002, 41 ILM 933 (2002).

<sup>10</sup> *CME (Netherlands) v Czech Republic*, Final Award, 14 March 2003 (available at [http://ita.law.uvic.ca/documents/CME-2003-Final\\_001.pdf](http://ita.law.uvic.ca/documents/CME-2003-Final_001.pdf)).

solutions to international disputes. Such tribunals may not be fulfilling their appointed function should they not be guided by international, as well as national rules, applicable to the dispute before them.

**(b) Interactions between Investment and Non-Investment Obligations**

The accelerated proliferation of international investment agreements, the growing number of treaties in other international domains, and the increase of investor-state arbitrations enhance the prospects of overlap between investment and non-investment obligations.<sup>11</sup> The interactions between international investment and non-investment obligations may be controlled by two main sets of rules: (i) the regulatory rules of international law, including Articles 53 and 30 of the Vienna Convention on the Law of treaties, as well as Article 103 of the UN Charter, and (ii) the nascent body of rules emerging from international investment jurisprudence. Investment tribunals have generally not resorted to the regulatory principles of public international law. This practical disregard of the regulatory rules of general international law stands in stark contrast to the extensive reliance of investment tribunals on other rules of international law (for example on treaty interpretation). This current unawareness of investment tribunals may change in the future with regard to fundamental human rights that are recognized in public international law as *jus cogens* rules. Parties involved in investment litigation (including NGOs) are likely to invoke the superior status of peremptory norms as a justification for non-compliance with investment obligations including those contained in investment contracts (such as those stemming from stabilization clauses).

The reasons for the divergence between international investment and the regulatory rules of public international law may lie, *inter alia*, in the different aims of these branches of international law involved as well as in the distinctive characteristics of investment relations. While the regulatory rules of public international law in this sphere are quite neutral regarding the interaction among most branches of international law, investment tribunals generally strive to advance the basic goal of investment law, primarily increasing foreign investment flows. Public international law accords preference to fundamental human rights and rules related to international peace and security (via the concept of *jus cogens* and article 103 of the UN Charter) but investment tribunals have hardly dealt with such superior norms of international law. For example, the Tribunal in *Biloune v. Ghana*<sup>12</sup> found that it was not competent to decide on the alleged human rights violations inflicted upon the investor. Human rights implications of investment law are, however, raised through *amicus curiae* briefs submitted by civil rights groups and human rights NGOs, which have been accepted by a few recent arbitral tribunals.<sup>13</sup>

The second factor that may explain the above mentioned divergence relates to the fundamentally different features of investment relations. While the underlying assumption of public international law is sovereign equality, the legal relationships between host states and foreign investors are clearly asymmetric. Host states are in a superior position to influence the content of the domestic law and the relevant norms of international law (particularly with regard to treaties).

These structural differences (and others) have led investment tribunals to grant precedence to the contractual or consensual rules that have been agreed upon by host states and investors. Following the contractual stage, and during most stages of the implementation of the investment agreement, the superior position of the host state regarding influence upon the content of both domestic and international law is glaring. Consequently, investment tribunals are inclined to emphasize ‘private law’ obligations included in the investment agreement and the circumstances prevailing at this critical stage, such as the information available to both parties in this phase (foreign investors’ legitimate expectations may also derive from the host state’s legislation and such expectations may also deserve legal protection).

Investment tribunals have addressed arguments regarding inconsistencies between the investment agreement and non-investment law (mostly environmental and human rights treaties)<sup>14</sup> in a very cautious manner. Thus far, no

<sup>11</sup> See further Moshe Hirsch “Interactions between Investment and Non-Investment Obligations” in *Oxford Handbook* above n.1 ch.5.

<sup>12</sup> *Biloune and Marine Drive Complex Ltd. v. Ghana Investments Centre and the Government of Ghana*, Award on Jurisdiction and Liability, 27 October 1989, 95 ILR 184 at 203.

<sup>13</sup> See e.g. *Agua Argentinas, SA, et al. v. Argentina*, Order in Response to a Petition for Transparency and Participation as Amicus Curiae, 19 May 2005, para. 23; *Agua Provinciales de Santa Fe SA, et al. v. Argentina*, ICSID Case ARB/03/17, Order in Response to a Petition for Transparency and Participation as Amicus Curiae, 17 March 2006, para. 18. See further, Andrea Shemberg “Investment Agreements and Human Rights: The Effects of Stabilization Clauses” *Corporate Social Responsibility Initiative Working Paper No. 42* (Cambridge, MA, Harvard University, March 2008).

<sup>14</sup> See Howard Mann *International Investment Agreements, Business and Human Rights: Key Issues and Opportunities* (Ottawa, International Institute of Sustainable Development, February 2008) at 26-29 citing *Maffezini v. Spain*, ICSID Case No ARB/97/7, Final Award, 13 November 2000, at para 67 (EC environmental impact assessment); *Parkerings-Compagniet v. Lithuania*,

investment tribunal has absolved a host state from its investment obligations, or significantly reduced its responsibility to compensate the injured investor in such cases.

The nascent principles that emerge from investment tribunals' jurisprudence do not form a coherent and comprehensive body of rules that clarify the relationships between investment and non-investment obligations. The contemporary treatment of these questions by investment tribunals is rather scattered and the law in this sphere is still in a formative period. Future investment awards and investment treaties may have to further clarify the legal rules applying to this intricate sphere of international investment law, especially in the face of the possibility, alluded to above, of increased argumentation about the primacy of non-investment obligations in given cases.

One of the significant (and interesting) developments in recent international investment law relates to the growing role of various soft law instruments in (e.g., the ILC Articles on State Responsibility, the World Bank Guidelines, IBA rules of ethics for International Arbitrators). Future studies may analyze the factors influencing the role of soft law instruments in international investment law, and explore impact of non-binding instruments in particular spheres of investment law (e.g., substantive issues like expropriation or procedural topics like the conflict of interests of arbitrators). Such studies are likely to assist practitioners, adjudicators and scholars in clarifying the existing law, and they may contribute to the development of new rules in international investment law.

### ***(c) Investment, Investor, Nationality and Shareholders***

Major contemporary issues surround the definition of the key terms "investment" and "investor" in international investment law. The main questions in relation to the first term ("investment") have concerned the breadth of the definition of investment: whether all types of investments, be they direct or indirect, be they enterprise-based or contractually based, should be covered or whether arbitral tribunals should adopt a narrower definition that relates the coverage of the investment agreement more precisely to cross-border capital movements and to foreign direct investment by enterprises rather than individuals.

As to the second term ("investor"), nationality issues are at the core of the legal analysis. The nationality of both natural and legal persons is mainly left to national law and practice, with international law intervening where this causes uncertainty, as in the case of dual nationality of natural persons, or the host country nationality problem for subsidiaries of multinational enterprises incorporated in the host country.

A further issue has arisen in relation to the offshore incorporation of companies for the specific purpose of taking advantage of BIT protection in the host country. In this connection, especially after the *Tokios Tokelès* case,<sup>15</sup> which allowed investors of Ukrainian nationality to invoke the protection of the Ukraine-Lithuania BIT against the Government of the Ukraine, by use of a Lithuanian incorporated entity, the state of arbitral case-law raises many problems as to the actual scope of permissible jurisdiction *ratione personae* under the ICSID Convention. There are arguments both for and against this extension of jurisdiction. Indeed it could be said that the decision simply reflects the reality of global business operations and the diminishing importance of the nationality of the corporate promoters and owners.<sup>16</sup> On the other hand it may be argued that more focus should be given to the element of control in determining corporate nationality.<sup>17</sup>

### ***(d) Multilateral Investment Rules***

Despite various attempts and the existence of a multilateral institutional and legal structure for international trade, foreign investment is currently regulated, by and large, through either bilateral or regional agreements only. Surprisingly, given the significance of foreign investment in the globalising economy, no multilateral system for the regulation of foreign investment exists.<sup>18</sup>

ICSID Case No. ARB/05/8, Award, 11 September 2007, section 8.3.1. and *SPP v Egypt*, Award on Merits, 20 May 1992, 8 ICSID Rev-FILJ 328 (1993) (UNESCO World Cultural Heritage designation); on whether human rights standards can be invoked in an investment dispute: *Agua Argentinas et al. v. Argentina*, ICSID Case No. ARB/03/19, Order in response to a Petition for Transparency and Participation as Amicus Curiae, 19 May 2005, para.19; *Biwater Gauff v. Tanzania*, ICSID Case No ARB/05/22, Procedural Order 5, 2 February 2007, para 52.

<sup>15</sup> *Tokios Tokeles v Ukraine* ICSID Case No Arb/02/18, Decision on Jurisdiction, 29 April 2004, 20 ICSID Rev-FILJ 205 (2005).

<sup>16</sup> See Robert Wisner and Nick Gallus "Nationality Requirements in Investor-State Arbitration" 5 JWIT 927 (2004) at pp.942-5. See further Anthony C Sinclair "The Substance of Nationality Requirements in Investment Treaty Arbitration" 20 ICSID Rev-FILJ 357 (2005).

<sup>17</sup> See Engela C. Schlemmer "Investment, Investor, Nationality and Shareholders" in *Oxford Handbook* above n.1ch.2.. See too the *Diallo Case*, above n. 2.

<sup>18</sup> See further Stefan D Amarasinha and Julianne Kokott "Multilateral Investment Rules Revisited" in *Oxford Handbook* above n.1 ch.4.

Regardless of the answer to the “when” and “where” questions relating to future comprehensive multilateral investment rules, it is likely that they will again be the subject of future negotiations. The question of *which* result will by definition depend to a large extent on the “when” and “where”, just as it will depend on the development between now and then as regards BITs and other agreements dealing with foreign investment. A “big bang” approach, according to which comprehensive multilateral investment rules will do away with all other existing rules in one clean swoop, is unlikely. Rather, a future agreement could be of a horizontal and general nature, which could also clarify certain issues, e.g. the relationship between GATS Mode 3, TRIMs and BITs, be it through incorporation by reference, creation of a “hierarchy of norms”, or other means. This would be in addition to the inclusion of new substantive rules to the existing body of such rules, e.g. environment, human rights and core labour standards. Finally, an agreement could also break new ground by not only placing actual obligations on investors, but also allowing host countries and affected parties to seek effective enforcement of these obligations. If an agreement accomplishes what is described above, that would constitute a significant – and positive – step forward in terms of ensuring that the law on foreign investment adequately reflects the current trends in terms of subjects of international law and increased accountability of TNCs when acting abroad as foreign investors.

#### ***(e) Trade and Investment***

Within the context of globalisation, the evolution of international trade and investment law, not surprisingly, largely mirrors the evolution of other branches of state practice including its seemingly inexorable tendency towards greater integration, moving from bilateral treaty practice towards regional and multilateral arrangements of shared common principles, objectives, standards and disciplines.<sup>19</sup> Consequently, the separate orders of trade and investment increasingly intersect and interact, both with one another and with those governing issues directly affecting peoples’ lives: human rights, labour standards, health, environmental and developmental policies.

In *economic* terms, it would appear incontrovertible that maintaining an ever-increasing network of RTAs, alongside multilateral rules, produces an overall decrease in economic welfare. Interested enterprises expect stable, predictable multilateral framework conditions, regardless of whether their transactions involve trade or investment. In *legal* terms, the proliferation of RTAs among WTO Members creates a complex system of competing international rights and obligations. The consequence of this complex economic system may be the detriment of economic welfare. Small, developing countries may see value in liberalizing within regional trade arrangements as a means of working their way into the harsher competitive realities of the global economy. MERCOSUR is one example of such a grouping. However, the development of complex networks of investment relations and regulatory regimes places developing countries in a weaker position than they would occupy in a multilateral framework. Speaking at the 2001 World Economic Forum in Davos, South Africa’s former Trade Minister, Alec Erwin, stressed that the increase in trading costs due to RTAs are particularly burdensome for small corporations and traders, and hence developing countries, a cautionary tale that may equally apply to investment provisions of RTAs.

RTAs, nevertheless, may enable countries to address issues that the multilateral system is ill equipped or unable to address due to the vast and varying nature of WTO membership. The Sutherland Report also argues against the injection of “non-trade” objectives into RTAs, stating that “if such requirements cannot be justified at the front door of the WTO they probably should not be encouraged to enter through the side door.” At the end of the day, are RTAs the proper place to address these “investment and” issues? From the standpoint of economic rationale, RTAs appear to be an undesirable occurrence, although undoubtedly more so regarding trade than investment. With this in mind, could it be said that the field of politics, with all its resulting problems, has eclipsed that of sound trade and investment policy? Arguably, a return to the founding precept of the world economic order, the multilateral MFN principle, would end the legal fragmentation RTAs represent and strengthen the credibility of the multi-lateral institutions. If the current situation is allowed to persist, we run the risk of a return of the Hobbesian vision of international society, ‘and the life of man – solitary, poor, nasty, brutish, and short’.

#### ***(f) The European Union and Bilateral Investment Treaties***

The international investment law issues within the European Union (EU) are an unclear, mixed and evolving issue. A distinction needs to be made in the analysis of bilateral investment treaties (BITs) concluded amongst the EU Member States (internal dimension) and those BITs which have been concluded by member states with third countries (external dimension).

With regard to the internal dimension, comparing the protection of the EC Treaty and usual protection in BITs, several instances of legal overlap occur.<sup>20</sup> The EC Treaty guarantees market access and protects intra-EC investors

<sup>19</sup> See further Friedl Weiss “Trade and Investment” in *Oxford Handbook* above n.1 ch.6.

<sup>20</sup> C. Söderlund, ‘Intra-EU BIT Investment Protection and the EC Treaty’, 24 *Journal of International Arbitration* 455 (2007).

through the four freedoms which guarantee the free movement of goods, persons, services, and capital. These rights are actionable nationally and ultimately at the European Court of Justice (ECJ). Protection against expropriation and Fair and Equitable Treatment are not found in the EC Treaty but the core protection is deeply entrenched in national constitutions as well as protected by the European Convention for the Protection of Human Rights and Fundamental Freedoms (Art. 1 Protocol 1 for expropriation).<sup>21</sup>

The European Commission holds the view that EC law prevails over the non-conforming BITs norms as of the date of accession of new States. Nevertheless, the effective prevalence of the EC does not entail at the same moment the automatic termination of the BITs. In any event, as the BITs contain usually post-termination protection periods, a disappearance of potential conflicts may take quite a while. The Commission holds the view that also the jurisdiction of the ECJ prevails from the date of accession<sup>22</sup> but arbitral tribunals may hold a different view.<sup>23</sup> Although the Commission has asked Member States to terminate the 191 BITs, which are currently still in force between different EU States, Member States have not done so.

There have been cases against Member States under intra EU-BITs where the venue chosen was international investment arbitration. The Tribunal in *Eastern Sugar v. Czech Republic*,<sup>24</sup> for example, found jurisdiction based on the following arguments: 1) the relevant BIT had not been terminated, 2) the acts in question had been undertaken before accession, 3) the BIT protection did not conflict with the EC and therefore supremacy was not an issue, 4) there was no policy formulation by the EU on intra-EU BITs, 5) availability of investor-state arbitration between some Members States is not a discrimination of relevance under the EC.<sup>25</sup> It remains to be seen if further intra-EU BITs investment disputes will lead to the termination of them. Till that time, it is not to be expected that arbitral tribunals will defer the case to the ECJ.

With regard to the external dimension, until the recent Treaty of Lisbon (approved in October 2007 and expected to enter into effect in January 2009), the competence for concluding investment treaties has in principle remained with the member states as the EC Treaty does not provide for any competence in field of investment and non-enumerated powers belong to the Member States.<sup>26</sup> Following the approach provided for in the abandoned Draft Constitutional Treaty, the Treaty of Lisbon provides for the exclusive competence of the Union in matters concerning “foreign direct investment”, where the Council will act on the basis of unanimity (where such agreements include provisions for which unanimity is required for the adoption of internal rules).<sup>27</sup> As the Commission has long argued that European investors find themselves in a comparative disadvantaged position compared to NAFTA country investors concerning market access, it is to be expected that, upon the entry into effect of the Lisbon Treaty, the EU will negotiate more forcefully investment treaties with market access provisions also for the pre-establishment phase and try to narrow down the existing differences between EU and NAFTA country BITs. Nevertheless, it appears that as long as the Community will not exercise its new competence in this field (by negotiating new treaties), existing BITs with non-EU countries will remain in force.

## (2) Substantive Standards

In this part of the report, the main issues arising out of the existing provisions of IIAs are considered alongside certain newer issues that are emerging within the complex universe of international investment law. This is by no means a complete overview of all issues arising out of all provisions. Rather it seeks to highlight the most

<sup>21</sup> Though Art. 295 EC could be invoked to permit nationalization under due process and compensation.

<sup>22</sup> That is clarified for state-to-state dispute settlement through the MOX Plant decision, ECJ, Judgment of 30 May 2006, *Commission v. Ireland* (C-459/03). W. Shan, *The Legal Framework of EU-China Investment Relations*, (Oxford, Hart Publishing, 2005), at 64.

<sup>23</sup> C Söderlund, above n.20 at 456 et seq. finds that in no manner may the EC restrict the possibility of investor-state arbitration.

<sup>24</sup> *Eastern Sugar v. Czech Republic*, Partial Award, 27 March 2007 (UNCITRAL Arbitration, Stockholm Chamber of Commerce) (Netherlands/Czech Republic BIT).

<sup>25</sup> *Eastern Sugar v. Czech Republic*, paras. 155-180.

<sup>26</sup> However, under the case-law of the ECJ, the EC additionally possesses exclusive responsibility for external relations in those areas in which it has enacted secondary law following the latent exclusive internal competence as implied power (the *ERTA* doctrine). Thus, while the EC has non-exclusive competency over parts of investment issues - both on movements of capital and matters related to establishment, this competence has not been fully exercised. See for details P. Eeckhout, *External Relations of the European Union*, (Oxford, Oxford University Press 2004), at 58 et seq.

<sup>27</sup> Art. 133 (1) EC Treaty will be replaced by Art. 188c (1): “The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union’s external action.”

problematic questions that have arisen out of the interpretation of IIA provisions before international tribunals and in the context of doctrinal debate. Accordingly sections (a) to (d) cover the “core” issues of admission and establishment, standards of treatment, including non-discrimination and fair and equitable treatment, most-favoured nation treatment and expropriation. Then sections (e) to (g) cover issues such as taxation, state responsibility and attribution and emergency exceptions, which have a presence within existing agreements either as express provisions delimiting the extent to which an IIA can cover the issue in question, or as approaches to the interpretation of the scope of existing provisions. Then sections (h) to (j) discuss emerging issue areas that are becoming, or may become, recognised as issues for inclusion in IIAs of a new generation. These include transparency, anti corruption and corporate responsibility. Finally, the question of the use of investment risk insurance will be discussed as a significant aspect of the control of investment risk is considered in section (k).

***(a) Admission of Investments and the Right to Establishment***

The international legal principles applicable to rights of admission and establishment ultimately depend on an exercise of state discretion: only where the host country agrees by way of a treaty obligation will such rights come into existence. There is no customary international law right of entry and establishment. Furthermore, the continuing dominant trend in IIA practice has been to retain a controlled entry model and not to extend general positive rights of entry and establishment.<sup>28</sup>

On the other hand, there are sound policy reasons why a host country may wish to open up its economy and to reinforce this policy by way of binding international obligations. Indeed a rising trend of recent years has been towards the conclusion of such obligations in IIAs. These include BITs concluded with Western hemisphere countries and bilateral FTAs with investment provisions. Modalities may change depending on whether the relevant discipline focuses on ‘investment’ generally (adopting a NAFTA-like National Treatment approach to liberalisation commitments) or on ‘trade in services’—including FDI in services (adopting a GATS-like Market Access approach to liberalisation commitments).

A further issue that arises in relation to entry and establishment concerns BITs that contain wording to the effect that the definition of an investment covered by the agreement is one made “in accordance with host state law”.<sup>29</sup> This can confirm that both foreign and domestic investors have to observe local law and that only those investments that are compliant with local law can obtain protection under the BIT, including any applicable laws on entry and establishment of foreign investment. Thus a tribunal can refuse jurisdiction over a dispute where the investor has acted in a fraudulent manner that renders the obtaining of an investment contract illegal under the law of the host state, by reason of breaches of good faith and unjust enrichment rules.<sup>30</sup> Equally, where the investor obtains a contract in knowing violation of nationality of ownership requirements under host state laws, this can take the dispute outside the protection of the BIT.<sup>31</sup> On the other hand violations of host state law after the entry of the investment cannot go to jurisdiction but only to the merits of the claim.<sup>32</sup>

It could be said that the main reason for the continued dominance of the controlled entry model is inertia coupled with a certain degree of rising nationalism. Many agreements following this approach were concluded some years ago, mainly with European capital-exporting countries. They have not yet been replaced. More recent agreements, such as those with the US or Canada, which did not conclude BITs until the 1980s, or the recent FTAs, may therefore be a better indication of current practice in the field. That said, the recent trends towards more restrictive national laws and regulations, could, if more widely adopted, lead to a reinforcement of the controlled entry approach. Thus the future development of this area of international investment law is not as settled as might be imagined.

<sup>28</sup> See further Ignacio Gomez-Palacio and Peter Muchlinski “Admission and Establishment” in *Oxford Handbook* above n.1 ch.7. and see Peter T Muchlinski *Multinational Enterprises and the Law* (Oxford, Oxford University Press, 2<sup>nd</sup> Ed, 2007) at 676-78.

<sup>29</sup> For example the BIT between Chile and New Zealand states that “investment” means any kind of asset or rights related to it, “provided that the investment has been made in accordance with the laws and regulations of the Contracting party receiving it...” cited in UNCTAD *Bilateral Investment Treaties 1995-2006: Trends in Investment Rulemaking* (New York and Geneva, United Nations, 2007) at 9.

<sup>30</sup> See *Inceysa Vallisoletana SL v El Salvador* ICSID Case No Arb/03/26 Decision on Jurisdiction 2 August 2006 available at [http://ita.law.uvic.ca/documents/Inceysa\\_Vallisoletana\\_en\\_001.pdf](http://ita.law.uvic.ca/documents/Inceysa_Vallisoletana_en_001.pdf). See for analysis Christina Knahr “Investments ‘in accordance with host state law’” 4 *Transnational Dispute Management* Issue 5 September 2007 available at [www.transnational-dispute-management.com](http://www.transnational-dispute-management.com).

<sup>31</sup> See *Fraport AG Frankfurt Airport Services Worldwide v The Philippines* ICSID Case No Arb/03/25, Award, 16 August 2007 (available at <http://ita.law.uvic.ca/documents/FraportAward.pdf>). See Knahr *ibid*.

<sup>32</sup> *Ibid* at paras. 344-45.

### ***(b) Standards of Treatment***

The interpretation of international law, especially treaty law, can be a difficult task at the best of times. Practitioners in the international investment law field do not differ from those in other disciplines seeking certainty in the construction of the law. This is particularly true where the basic investment protection norms are of a very general and open-ended nature.

There can be considerable confusion in the growing number of cases in which concepts such as ‘non-discrimination’ ‘fair and equitable treatment’ and ‘legitimate expectations’ have been used to the same end, but in so many different ways.

Arguably, the case-law indicates a move towards a single standard of regulatory treatment, based upon the legitimate expectation of investors to enjoy access to rights of transparency, due process and non-discrimination in a host country or in a free trade area, as the case may be.<sup>33</sup>

Is there more to this convergence of tribunals finding liability on the basis of what is effectively a single standard of regulatory treatment? Perhaps we are indeed witnessing a more extraordinary development: i.e. the inclusion of a comparative standard of non-discrimination in the customary international law minimum standard of treatment. It is already accepted that bad faith is not a requirement for the violation of the modern minimum standard of fair and equitable treatment – and thus intent becomes less important than effect in the minimum standard analysis. Further, recent tribunals have experienced little difficulty in considering “fair and equitable treatment” as an obligation of substantive fairness that includes a prohibition against non-discrimination. If increasingly fewer tribunals draw distinctions between custom and treaty, in respect of the fair and equitable standard, the proposition may indeed attract more adherents.

In the meantime, with the accession of the principle of legitimate expectations as a “dominant element” of the fair and equitable treatment standard – a consensus appears to be forming about the importance of representations made to investors, implicit and explicit. Similarly, consensus appears to be forming in respect of the proportionality principle, which tribunals see as common to each of the standards of expropriation, fair and equitable and national treatment. The effect of such consensus is that it encourages tribunals to balance both the alleged reliance of the investor against the policy rationale for impugned state conduct – regardless of the treaty standard at issue.

Yet formalism in treaty interpretation may still prevail. Treaties are still most often drafted with the full panoply of obligations intact. Nonetheless, it is possible to say that in the jurisprudence of investment protection treaties, a single standard of regulatory treatment has been developing. It is based upon a good faith analysis of investment expectations and the reasonable protection of regulatory policy space. “Standard of treatment” or “standards of treatment” – time will tell.

### ***(c) MFN Treatment***

The most-favoured-nation treatment clause *per se* entails international obligations and rights not only among the Contracting States of the treaty incorporating it (the basic treaty), but also among these Contracting States and other States by virtue of different treaties. As a rule, a most-favoured-nation (MFN) treatment clause is not only a treaty clause, but also a source of international obligations other than those included in the basic treaty. These are new international obligations whose contents cannot totally be foreseen and identified when the basic treaty is concluded, since such contents may depend on other, sometimes subsequent, treaties.

The functioning of the MFN treatment standard as both a treaty clause and a source of international law, particularly of international legal obligations, other than international customs and treaties, presupposes that the *ejusdem generis* principle (that the imported treaty provisions be ‘of the same type’) is satisfied. So far, ascertaining this presupposition has not given rise to controversial issues within investment cases. In reality, the *ejusdem generis* principle has been discussed in depth only by the ICSID Tribunals in the *Maffezini* and *Suez* cases.<sup>34</sup> Though insufficient standing alone, some clues to determine if the *ejusdem generis* principle is met can be found in the fact that MFN treatment clauses provided in investment treaties tend to be unconditional, reciprocal and indeterminate and many treaties at stake, such as BITs, have a very similar framework.

Admittedly, the “in like circumstances” requirement found in many treaties may in the future become significant, in order to evaluate whether or not the *ejusdem generis* principle is satisfied. In this case, the particular interpretation of a MFN treatment clause adopted by a tribunal will be crucial. Certainly, the more States differentiate MFN treatment clauses in investment treaties, the more matters of interpretation and application become relevant. In any

<sup>33</sup> See Todd J Grierson-Weiler and Ian A Laid “Standards of Treatment” in *Oxford Handbook* above n.1 ch.8.

<sup>34</sup> *Maffezini* above n.14 and *Suez and Vivendi v Argentina* ICSID Case No.ARB/03/19, Decision on Jurisdiction, 3 August 2006 (available at <http://www.worldbank.org/icsid>). See further Pia Acconci “Most Favoured Nation Treatment” in *Oxford Handbook* above n.1 ch.10.

event, the fact that, at an international law level, new obligations (particularly of a substantive nature) can arise from a MFN treatment clause may be considered perfectly legitimate, as this is the perceived purpose of such a clause. The application of a MFN treatment clause to procedural matters of treatment has been highly controversial. Such application was particularly denied by the ICSID Tribunal in the *Plama* case, which refused to extend consent to ICSID arbitration through such a clause.<sup>35</sup> The latter strongly criticized the *Maffezini* decision, even though it extended sympathy towards that ICSID Tribunal as it had to deal with “exceptional circumstances”, in particular because the basic treaty which included ‘nonsensical requirements’, such as the ‘eighteen months in domestic courts’ requirement. The approach adopted by the *Plama* Tribunal and the *Telenor* Tribunal,<sup>36</sup> may be contrasted with the approach followed more recently by the *RosInvest* Tribunal, which permitted an investor to avail itself of the MFN clause in the underlying BIT in order to extend the tribunal’s jurisdiction to issues of occurrence and validity of expropriation, which were not covered by the limited jurisdiction clause in the BIT.<sup>37</sup> It is worth pointing out that States which do not want to be subject to the functioning of MFN treatment clauses are adopting a cautious line of conduct during negotiations of investment treaties. This emerges from some recent examples of international practice, such as the new Canadian Model BIT, the negotiations of the FTAA, some recent free trade agreements and the several trade and investment framework agreements concluded by the United States.<sup>38</sup>

#### **(d) Expropriation**

Since direct expropriations of foreign investment have become rare in practice, arbitral awards under the ICSID Convention and other investment dispute settlement systems have focused on the question of what constitutes an indirect taking. In particular, the issue of regulatory measures and when such measures amount to regulatory expropriations has gained much attention. A number of investment tribunals have emphasized, if not exclusively focused on, the intensity of the interference with the investors’ rights under the so-called sole-effect-doctrine. Others have equally taken into account the motives of governments, regulatory purposes, the transparency and proportionality of governmental action as well as the reasonable expectations of investors. A more recent development is reflected in a line of cases emphasizing the sovereign prerogative of regulatory powers. Under what is sometimes referred to as ‘police powers’ doctrine, a number of investment tribunals starting with *Methanex v. USA* in 2005 and *Saluka v. Czech Republic* in 2006 have held that a state does not commit an expropriation when it adopts general regulations that are “commonly accepted as within the police power of States.”<sup>39</sup> In order to delimit the legitimate regulatory space of host states, tribunals like the one in *Methanex* have resorted to the traditional legality criteria of expropriations, by stating that a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, *inter alios*, a foreign investor or investment is not deemed expropriatory. This approach, however, has not remained uncontroversial.

An analysis of the practice of investment tribunals demonstrates that actual findings of indirect expropriations have been rare. More recent examples include governmental interference with contract rights leading to a breach or termination of the contract by the investor’s business partner, as in *CME v. Czech Republic*;<sup>40</sup> the breach of contractually acquired rights with discriminatory intent, as in *Eureko v. Poland*;<sup>41</sup> various forms of interference with the management of an investment, like the arrest and expulsion of an investor or other persons who play key roles in the investment, as in *Biloune v. Ghana*<sup>42</sup> or in *Benvenuti & Bonfant v. Congo*;<sup>43</sup> or the replacement of the owner’s

<sup>35</sup> *Plama Consortium Limited v Bulgaria* ICSID Case No Arb/03/24, Decision on Jurisdiction, 8 February 2005, 44 ILM 721 (2005).

<sup>36</sup> *Plama* previous note *Telenor Mobile Communications v Hungary* ICSID Case No.ARB/04/15 Award of 22 June 2006 available at <http://www.worldbank.org/icsid>.

<sup>37</sup> *RosInvestCo UK Ltd. v. The Russian Federation*, SCC Case No. Arb. V079/2005, Award on Jurisdiction, October 2007 (available at [http://ita.law.uvic.ca/documents/RosInvestjurisdiction\\_decision\\_2007\\_10\\_001.pdf](http://ita.law.uvic.ca/documents/RosInvestjurisdiction_decision_2007_10_001.pdf)).

<sup>38</sup> See further Acconci above n.34 at 367-81

<sup>39</sup> *Methanex Corp v US*, Final Award on Jurisdiction and Merits, 3 August 2005, 44 ILM 1345 (2005); *Saluka BV v Czech Republic* UNCITRAL Rules Arbitration, Permanent Court of Arbitration, Partial Award, 17 March 2006 (available at <http://ita.law.uvic.ca/documents/Saluka-PartialawardFinal.pdf>). See further August Reinisch “Expropriation” in *Oxford Handbook* above n.1 ch.11.

<sup>40</sup> See above n.10.

<sup>41</sup> *Eureko v Poland*, Partial Award, 19 August 2005 (available at: <http://ita.law.uvic.ca/documents/Eureko-PartialAwardandDissentingOpinion.pdf>).

<sup>42</sup> See above n.12.

<sup>43</sup> *Benvenuti & Bonfant v People’s Republic of the Congo* 21 ILM 740 (1982).

management by government imposed managers, as in the Iran-US Claims Tribunal cases *Starrett* and *Tippetts*;<sup>44</sup> or different forms of revocation or denial of government permits or licenses, such as in *Goetz v. Burundi*, *Middle East Cement v. Egypt*, *Tecmed v. Mexico* or *Metalclad v. Mexico*.<sup>45</sup>

In general, investment tribunals have attempted to strike a fair balance between investor rights and the right of states to regulate. The low number of findings of indirect expropriations is likely to be re-enforced by more recent BITs and other investment agreements which provide for rather detailed and restrictive rules concerning indirect expropriation.<sup>46</sup> In effect, they often try to guard the regulatory space of states by introducing language along the *Methanex* and *Saluka* ‘police powers’ doctrine.

The low number of direct expropriations also explains why the traditional legality criteria – most BITs and other IIAs provide that expropriations have to be for a public purpose and must be made in a non-discriminatory fashion, pursuant to due process and against compensation – are rarely addressed in arbitral practice. Where states purport not to expropriate but only to regulate they do not provide for any compensation. In the few cases where investors have been directly expropriated, however, tribunals have generally reaffirmed the above-mentioned legality requirements and also broadly adhered to the distinction between compensation as a requirement for a lawful expropriation and damages as a (state responsibility) consequence for an unlawful expropriation.<sup>47</sup>

#### **(e) Taxation**

Tax is one of the most sensitive policy areas concerning the sovereign autonomy of the nation state. It is therefore with great caution, reservation, restrictions and conditions that modern investment treaties have started to impose external disciplines on the abuse of governmental tax powers against foreign investors, though there are traces in international customary law of application of traditional standards (in particular expropriation) to the use of tax powers by States to achieve indirectly the same effect as would and could have been achieved by formal expropriation.

In essence, modern treaties subject tax powers (direct taxation) to the treaty’s discipline, though there are frequently several key carve-outs including (a) limiting the scope only to specifically defined forms of taxes; and (b) limiting the number of the investment treaties’ treatment obligations (“disciplines”) applicable to tax, mainly to direct and indirect expropriation.

In addition, modern treaties contain sometimes a “joint tax veto” whereby a treaty-based claim against the exercise of tax powers can be vetoed by an agreement between the tax authorities of both home and host state or is at least subject to a delay following consultation by both tax authorities. This slow progress from the immunity of national tax powers to international disciplines to a, though still limited, coverage in modern tax treaties reflects the transition of the classic “nation state” to the “market state” which participates more fully in the institutional regime of the global economy. Other international tax instruments, e.g. recent OECD efforts at drafting a inter-state tax arbitration system that have incorporated a much more limited role for private taxpayers, reflect this cautious transition but have not gone so far as most modern investment treaties.

There is not that much arbitral jurisprudence but it is growing. A major current issue is the use of tax powers to undo, in economic effect, former privatization deals; often, general tax anti-avoidance clauses permit States to disregard of transactions carried out with a tax optimization motive. Such practices engender a collapse of legal predictability and may be injurious to the rule of law in the domestic tax treatment of foreign investment. That constitutes a serious challenge for modern investment treaties which has not as yet been resolved with any clarity in modern investment arbitration. One suggestion is that investment treaties, as a rule, should be applied so as to discipline the “abuse” of such “anti-avoidance mechanisms”.<sup>48</sup> The difficult task is to identify what is abuse of anti-tax avoidance provisions and what is simply the application of current good practices in tax authorities around the world. The suggested approach is to measure the tax conduct of a host state at issue against current good practices in legal

<sup>44</sup> *Starrett Housing Corp v Iran* 4 Iran-US CTR 122 (1984); *Tippetts, Abbott, McCarthy, Stratton v. TAMS-AFFA Consulting Engineers of Iran*, 6 Iran-US C.T.R. 219, 225 (June 29, 1984).

<sup>45</sup> *Goetz (Antoine) and Others v Republic of Burundi* ICSID Case No Arb/95/3 Award of 10 February 1999, 15 ICSID Rev-FILJ 457 (2000); *Middle East Cement Shipping and Handling Co. S.A. v. Arab Republic of Egypt*, ICSID Case No. ARB/99/6 Award, 12 April 2002 (available at <http://ita.law.uvic.ca/documents/MECEment-award.pdf>); *Tecmed v Mexico* ICSID Case No Arb (AF)/00/2, Award, 29 May 2003, 43 ILM 133 (2004); *Metalclad v Mexico* ICSID Case No Arb(AF)/97/1, 40 ILM 36 (2001).

<sup>46</sup> See for example the US and Canadian BITs discussed in Reinisch above n.39 at 423-24.

<sup>47</sup> See for example *ADC Affiliate Limited and ADC & ADMC Management Limited v. Republic of Hungary*, ICSID Case No. ARB/03/16 Award, 2 October 2006 (available at: <http://ita.law.uvic.ca/documents/ADCvHungaryAward.pdf>).

<sup>48</sup> See Thomas W. Walde and Abba Kolo “Coverage of Taxation under Modern Investment Treaties” in *Oxford Handbook* above n.1 ch.9.

systems with a developed system of rule of law, i.e. relying on comparative tax law in OECD countries and international soft law instrument which reflect such “good tax governance standards”.

**(f) State Responsibility and Attribution**

Rules of attribution play a central role in the law of state responsibility. Investment arbitration is not an exception. This is well illustrated by several arbitral awards including *Loewen*, *Maffezini*, *Salini v. Morocco*, *Tradex*, *Salini v. Jordan*, *Nykomb*, and *CME*.<sup>49</sup> These awards generally accept that the ILC Articles constitute the most authoritative statement of the law on state responsibility. In many respects, the rules and principles laid down therein are quite far-reaching. When it comes to attribution, as a matter of principle, all activities of the state, in whatever form it chooses to act, are attributable to the state. For the purposes of attribution, the state is viewed as a unity, including federal states with varying forms of administrative and political subdivisions.

Conduct of persons and/or entities which are not state organs is attributable to the state, provided the conduct in question constitutes the exercise of governmental authority.

Arbitral awards in investment disputes have become a “testing ground” for the ILC Articles. The number of awards dealing in detail with the question of attribution is still relatively modest. Even though this number will grow, the application of the ILC Articles must be characterized as being in its formative stages. As time goes by, more clarity may emerge. Based on the discussion above, it is reasonable to assume that most difficulties will arise in relation to Article 5 (*Conduct of persons or entities exercising elements of governmental authority*) and Article 8 (*Conduct directed or controlled by a State*) of the ILC Articles and probably also with respect to umbrella clauses where the so called “it” issue is particularly important.

Many, if not most, umbrella clauses refer to the entity which must observe the undertakings in question as “it”.<sup>50</sup> For purposes of attribution in the context of state responsibility, the interesting question is how to determine and/or define “it”, to which reference is made in most umbrella clauses. The reference clearly includes the state itself. “Each Party” and “Each Contracting Party” refers to the signatories of the treaties in question. But how do you define the “State”? Does it include governmental bodies – which may or may not be separate legal entities – and state-owned enterprises? Which principles and rules are to be applied to find answers to these questions? Is it possible and/or appropriate to apply international law principles of attribution to these questions, or should other rules and/or principles be applied? Arbitral tribunals have taken different approaches to the “it” problem in umbrella clauses, partly due to the different wordings of such clauses with some applying national law and others referring to international law in this regard.<sup>51</sup>

**(g) Emergency Exceptions: State of Necessity and Force Majeure**

States may raise as defences to their international investment obligations the doctrines of necessity and *force majeure*. Both have been recognized as part of customary international law by international tribunals, and both are included in the ILC’s Articles on State Responsibility. In practice, however, the elements of a necessity defence are difficult to satisfy, particularly in the realm of foreign investment when economic crisis is likely to be the foundation for the claim. This is understandable because of the concern that too malleable a doctrine would enable a State to escape its obligations. Yet it is possible that as a practical matter a necessity defence is unavailable to a State because the standards in themselves are so high, and because they must be cumulatively satisfied. The recent decision in *LG&E v. Argentina*, however, suggests that tribunal could interpret the customary international law requirements flexibly enough to permit redress in grave situations.<sup>52</sup>

*Force majeure* is potentially an easier standard to meet, in part because some of its elements are more readily established by objective measures. *Force majeure* involves an event that has already occurred, whereas necessity

<sup>49</sup>*Loewen v US* ICSID Case No Arb (AF)/98/3, Award, 26 June 2003, 42 ILM 811 (2003); *Maffezini* above n.14; *Salini v Morocco* ICSID Case No Arb/00/4, Decision on Jurisdiction, 23 July 2001, 42 ILM 609 (2003); *Tradex v Albania* ICSID Case No Arb/94/2, Decision on Jurisdiction, 24 December 1996, 14 ICSID Rev-FILJ 161 (1999); *Salini Construttori SPA and Others v Jordan* ICSID Case No/Arb/02/13, Decision on Jurisdiction, 29 November 2004, 44 ILM 573 (2005); *Nykomb Synergetics Technology Holding AB v. Latvia*, Stockholm Rules, Award, 16 December 2003 (available at <http://ita.law.uvic.ca/documents/Nykomb-Finalaward.doc>); *CME* above n.10. See further Kaj Hober “State Responsibility and Attribution” in Oxford Handbook above n.1 ch.14.

<sup>50</sup> For example by Article 10(1) of the Energy Charter Treaty: “Each Contracting Party shall observe any obligations it has entered into with an Investor or an Investment of an Investor of any other Contracting Party.”

<sup>51</sup> See for discussion Hober above n.49 at 575-82.

<sup>52</sup> *LG&E Energy Corporation v Argentina* ICSID Case No ARB/02/1, Decision on Liability, 3 October 2006, 46 ILM 1136 (2007) see further Andrea K. Bjorklund “Emergency Exceptions: State of Necessity and *Force Majeure*” in Oxford Handbook above n.1 ch.12.

involves action to protect against a future event – a “grave and imminent” peril. The mere fact of a State’s taking action may avert or alleviate the danger; at the least, its action will make it more difficult to assess what would have occurred in the absence of the action. Moreover, necessity involves the element of volition in that a State chooses not to comply with its obligation, albeit for good reason, whereas *force majeure* involves an inability to comply with the obligation.

It would be unwise, however, to conclude that a *force majeure* defence would be readily established. *Force majeure*, too, is available only in limited circumstances. First, there must be an irresistible force or an unforeseen event, and that force or event must be beyond the control of the State asserting the defence. Furthermore, performing the obligations must be “materially impossible.”

The customary international law defences of *force majeure* and necessity may not be the only safeguards available for a State to invoke. The *LG&E* and *CMS* annulment decisions suggest that the “essential security” or “public order” clause found in many investment treaties could form a basis for a State to justify suspending or even terminating its obligations that is independent of the public international law defence of necessity.<sup>53</sup> It is at least possible that the treaty-based defences will be construed to require a less stringent showing of threat to essential security or public order than are the customary international law defences.

All tribunals to date have determined that circumstances precluding wrongfulness under the ILC Articles are not self-judging. The two ICSID tribunals agree that the language of the US-Argentina BIT is also not self-judging, but language in other treaties could lead to a different conclusion.

Establishing a successful defence, whether on the basis of a treaty provision or customary international law, also requires that the tribunal establish the duration of the period during which wrongfulness is precluded, an often uncertain and subjective exercise. In addition, the issue of compensation owed in the event a State is found to have faced such a circumstance precluding wrongfulness is unresolved. The tribunals that have considered the question have diverged on whether compensation would be owed regardless of the success of any defence raised. It may be that a successful invocation of the necessity defence does nothing more than postpone a State’s compensatory obligations. In certain circumstances this suspension of obligations might be very welcome; in the long run, however, it may mean that even the successful raising of a necessity defence confers little in the way of long-term economic benefit on the State in question.

Further clarification is likely to come in the decisions on the Argentine cases that should be issued over the coming months and years. At bottom is the question of risk allocation and determining who should bear the burden in situations of unforeseen events or economic crises.<sup>54</sup> One should remember that the ILC Articles were drafted to serve general purposes; they were not drafted to serve the interests of investor-State arbitration, or even of investment generally. These principles will need to be developed in the context of investment law, and in the context of individual investors bringing cases to protect their interests. Investor-State cases may diverge from cases in which only States are the parties and their obligations to each other carry less direct pecuniary effects.

### ***(h) Substantive Transparency***

Transparency in the laws and conduct of the host State has attracted much attention both in BITs and in recent arbitrations.<sup>55</sup> In the 1980s transparency came to be known as the requirement to make all relevant laws publicly available. This trend was followed by the WTO Agreements which rank transparency as a basic principle.<sup>56</sup> Transparency has developed in US BITs as a tool to pursue the accountability of host States and to charge host States with corresponding obligations so as to establish an impartial review mechanism.<sup>57</sup> Recently it has come to be argued that accountability should also be required of investors and home States in BITs. This suggestion indicates the change of the fundamental functions of BITs adding obligations upon both investors and home States rather than

<sup>53</sup> *LG&E* previous note; *CMS Gas Transmission Co v Argentina* ICSID Case No.ARB/01/8, Decision on Annulment, 25 September 2007, 46 ILM 1136 (2007).

<sup>54</sup> See further William W. Burke-White and Andreas von Staden “Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties” 48 *Va. Jo. Int’l. L.* 307 (2008).

<sup>55</sup> See further Akira Kotera “Regulatory Transparency” in *Oxford Handbook* above n.1 ch.16..

<sup>56</sup> See GATT 1994 Article X; GATS Article III.

<sup>57</sup> See US Model BIT 2004 Articles 10 and 11.

just on host States.<sup>58</sup> It is uncertain whether such a trend will consolidate in the future, though some arbitral tribunals have required investor transparency in their dealings with host country authorities.<sup>59</sup>

As transparency has attracted more attention, arbitration awards have read a requirement to act in a transparent manner into the obligation of fair and equitable treatment.<sup>60</sup> This means that, even if transparency is not included in a BIT, it might be guaranteed by the provision of fair and equitable treatment in accordance with the context and object and purpose of surrounding the BIT. Notwithstanding the additional costs on host States connected with broader and more stringent transparency obligations, these obligations have the potential of strengthening good governance (in the exercise of legislative, administrative and judicial functions) for the benefit of both foreign and domestic investors.

### **(i) Anti-corruption**

Most cases where corruption has been an issue in arbitration fit in one of the two following types: (a) the parties involved are the investor, on the one hand, and the host state or a state owned and governed entity, on the other ('main investment contract' scenario); (b) the parties – investor and agent/intermediary – have concluded an agency agreement, which obliges the agent to engage in intermediary activities (such as giving legal and fiscal advice or consulting) in order to help the investor to obtain a public procurement contract ('agency agreement' scenario).

With regard to the effects of corruption on the main investment contract, some national laws contain mandatory rules providing for corruption itself as a primary reason for the main contract to be void or unenforceable. However, if national laws do not contain such a rule of nullity, some still hold the main contract for invalid because they consider international anti-corruption policy a primary reason for invalidity.<sup>61</sup> Others opt for a flexible treatment of the main (investment) contract; they consider the contract as *per se* valid due to the principle of State responsibility, but subject to modification, adaptation or declaration for void by an arbitral tribunal. In this solution, the investment contract remains the *causa* for the investment, which excludes restitution of the investment itself.<sup>62</sup>

Where corruption is alleged, contracts remain in any case subject to arbitration because of the principle of severability.<sup>63</sup> With regard to the issue of establishing allegations of corruption in arbitration proceedings, some arbitral tribunals demand an elevated standard of proof for corruption,<sup>64</sup> some lower the required standard of proof,<sup>65</sup> and some stick to the usual standard of proof, including circumstantial evidence.<sup>66</sup> In setting aside and enforcement proceedings, anti-corruption values may be considered as international public policy values; however, allegations of corruption should not lead to a stricter national control of arbitral awards than normal.<sup>67</sup>

Agency agreements between investors and intermediaries that contain an understanding about the bribing of foreign officials in order to secure procurement decisions are invalid. They are not affected by the prohibition of intermediaries that exist in many national laws,<sup>68</sup> but their invalidity is a consequence of the illegality of their

<sup>58</sup> See for example the OECD Guidelines on Multinational Enterprises, 2000, Guideline III "Disclosure" and see too Peter Muchlinski "Corporate Social Responsibility" in *Oxford Handbook* above n.1 at 675-78.

<sup>59</sup> See for example the *Fraport Case* above n.31 *Inceysa* above n.30, *Azanian v Mexico* ICSID Case No Arb (AF)/97/2 Award 1 November 1999, 14 ICSID Rev-FILJ 538 (1999) and *Parkerings Case* above n.14.

<sup>60</sup> See *Metalclad Case* above n.45; *Tecmed Case* above n.45; *Saluka Case* above n.39.

<sup>61</sup> *American Bell v Iran*, Award in Case No. 48 (255-48-3) of 19 September 1986, 12 Y. B. Comm. Arb. 292, 292 (1987).

<sup>62</sup> Hilmar Raeschke-Kessler, Dorothee Gottwald, "Corruption" in *Oxford Handbook* above n.1 ch.15 at 601. Cf. also *Himpurna v. PLN* Final Award of 4 May 1999, 25 Y. B. Comm. Arb. 11, para. 114 (2000).

<sup>63</sup> Different in *ICC No. 1110* Award of 1963 10 Arb. Int'l para. 16 (1994) at para. 3; However, since the 1980s, consensus has been established that the severability doctrine applies also to corruption cases, *ICC No. 3916*, Award of 1982, 111 JDI 930, 931 (1984); *ICC No. 4145* Interim Awards and Final Award of 1983, 12 Y. B. Comm. Arb. 97, para. 8 (1987).

<sup>64</sup> The *Westinghouse* case, Abdulhay Sayed, *Corruption in International Trade and Commercial Arbitration* 93 (The Hague, Kluwer Law International, 2004); *The Claude Reynold Award*, ASA Bulletin 742, 747 (1995); *Himpurna v. PLN* Final Award of 4 May 1999, 25 Y. B. Comm. Arb. 11, para. 116 (2000).

<sup>65</sup> *ICC No. 8891*, 127 JDI 1076, 1079 (2000); *Oil Fields of Texas v. Iran (National Iranian Oil Company)*, Award in Case 43 (258-43-1) of 8 October 1986, 12 Y. B. Comm. Arb. 287, para. 25 (1987).

<sup>66</sup> *ICC Case No. 4145*, Interim Awards and Final Award of 1983, 12 Y. B. Comm. Arb. 97, para. 28 (1987); *ICC No. 7047* Final Award of 1994 in 21 Y. B. Comm. Arb. 79 para. 54 (1996); *ICC No. 9333*, 19 ASA Bulletin 757, para. 8 (2001).

<sup>67</sup> *Westacre v. Jugoinport*, High Court, Queen's Bench Division (Commercial Court), 19 December 1997, 23 Y. B. Comm. Arb. 836 para. 77-79 (1998); *HUBCO* Supreme Court of Pakistan, 20 June 2000, Arb. Int'l 439, 439 (2000) para. 34, 35. For a different view cf. *Soleimany v. Soleimany* Court of Appeal, 30 January 1998, 24a Y. B. Comm. Arb. 329, para. 32 (1999) (in a special case where illegality was apparent from award itself).

<sup>68</sup> *ICC 8113*, Partial award on the Applicable Law of 1995, 25 Y. B. Comm. Arb 11 (2000), *The Jürgen Dohm Award*, ASA Bulletin 216, 233 (1993).

objective.<sup>69</sup> Consequently, what has been paid in performance of such an agreement is excluded from restitution. Arbitral practice has developed a series of indications that may be used to determine whether or not the objective of the agency contract is corruption. Awards that enforce agency agreements aiming at corruption are contrary to international public policy and therefore void.<sup>70</sup>

#### ***(j) Corporate Social Responsibility***

Recent years have witnessed the rise of new concerns about the effects of investor activities in host States. These have led to increased calls for a new, more balanced, regime in international investment law, one that responds not only to the concerns of investors (for the protection and promotion of a clear, transparent and predictable investment environment) but also to the wider communities in which they operate.<sup>71</sup> Thus not only investor rights should be the focus of international investment law but also investor responsibilities. In addition, home countries may have responsibilities to oversee investors based in their jurisdictions to ensure that they operate their foreign investments in accordance with wider social and public interests in mind and that those investors are given opportunities and incentives to engage in investments that promote the sustainable development of less developed host countries in particular.

Four areas in particular stand out as being central to the substantive content of “international corporate social responsibility” (ICSR), namely, labour rights, human rights, environmental issues and corruption.

At present there are few signs that host country responsibilities will be balanced out by the introduction of corporate responsibilities in such agreements.<sup>72</sup> Indeed there are a number of major obstacles that need to be cleared for such a development to occur. First, it is hard to see where the political will for such a development will come from. Equally, newer bilateral and regional agreements are taking an even more strongly protective approach, with commitments to pre-entry protection and internationalised dispute settlement becoming more frequent, but with little to offer in relation to development concerns. Thirdly, the introduction of International Corporate Social Responsibilities (ICSR) could create major drafting and negotiating problems, including the choice of which standards to include, how detailed those standards should be, whether they could be couched in mandatory or merely hortatory language and whether they would represent an international minimum standard or something more.

In this regard, the relationship between treaty based standards and national regulatory standards would need to be addressed. In particular the issue of whether development concerns should allow for a lower standard of commitment to ICSR norms on the part of the host country would need to be considered, as would the need for technical assistance and the provision of resources to the least developed countries so that they could meet higher CSR standards. In addition, the effect of international standards on national regulatory environments would need to be clarified. Thus, clear duties of compliance with international standards will be required in the case of countries where lower standards apply, and international agreements would need to build in commitments not to lower existing standards as per the types of clauses noted above in relation to labour and environmental standards. Furthermore, progressive improvement of standards would need to be catered for by way of periodic reviews.

Notwithstanding these obstacles, the eventual inclusion of certain commitments to ICSR in future IIAs cannot be ruled out. The continued legitimacy of IIAs may require the eventual recognition of the responsibilities of investors as well as host states, not to mention home countries as well, in particular with regard to the four main areas mentioned in the UN Global Compact, namely, human rights, labour rights, environment, and corruption. If this approach were to be adopted, future IIAs may need to ensure that they refer to the major instruments in these areas as a source of standards by which the balance of rights and obligations of investors can be interpreted.

Finally, some arbitral tribunals do take into account investor conduct where this is deemed relevant in determining the nature of the respondent state’s actions, or where the actual cause of the loss to the investor is in issue.<sup>73</sup> This ‘creative’ interpretation by arbitral tribunals may be the sign of a future evolution of existing BITs and other IIAs into a new generation of more development and socially friendly arrangements responsive not only to the needs of

<sup>69</sup> *ICC No. 1110* Award of 1963 10 Arb. Int’l para. 16 (1994); *ICC No. 6286* 19 Y. B. Comm. Arb. 141 para. 22 (1999). For further examples cf. Hilmar Raeschke-Kessler, Dorothee Gottwald, above n.62 at 609.

<sup>70</sup> *Coetzee v. Paltex*, Provincial Division of the High Court of South Africa 8 May 2002, Digest by Lise Bosman, IntADR or [www.kluwerarbitration.com](http://www.kluwerarbitration.com).

<sup>71</sup> See Peter Muchlinski “Corporate Social Responsibility” in *Oxford Handbook* above n.1 ch.17.

<sup>72</sup> For a recent noticeable exception see the 2007 draft Norwegian model BIT which includes Article 32 entitled Corporate Social Responsibility. It states “The Parties agree to encourage investors to conduct their investment activities in compliance with the OECD Guidelines for Multinational Enterprises and to participate in the United Nations Global Compact” (available at <http://ita.uvic.ca/investmenttreaties.htm>).

<sup>73</sup> See further Muchlinski *Multinational Enterprises and the Law* above n.28 at 639-47 and Peter Muchlinski “‘Caveat Investor’? The Relevance of the Conduct of the Investor under the Fair and Equitable Treatment Standard” 55 ICLQ 527 (2006).

investors for protection against maladministration, but also to the calls for greater responsibility among investors and home countries for the proper conduct of investments.

### ***(k) Investment Insurance***

Many investors from capital-exporting countries are interested in investing in developing countries (including emerging markets) and are willing to assume normal risks associated with such investment. Risk is part of any economic activity and is normally rewarded through the potential financial gains from such activities. But the costs resulting from risks associated with arbitrary decisions, unstable political environments or other unforeseeable government actions – the non-commercial risks – make investment in certain countries hazardous. In the view of many investors, this is especially the case in certain developing and transition countries that do not always have a sufficiently stable political environment but do need investment to help them achieve their development goals. Many investment opportunities exist in emerging economies, but for multinational companies and small and medium-sized businesses alike, concerns about uncertain policy environments and perceptions of political risk often inhibit investment. One of many possible answers to these preoccupations rests in investment insurance provided by investment guarantee schemes.<sup>74</sup> Such schemes are of especial importance for the coverage of risks that ordinary commercial insurance will not cover. In particular investment guarantee schemes cover the types of political risks mentioned above.

Investment guarantees have evolved from a complete absence of mechanisms to the coexistence of a number of important mechanisms at the national, regional and international level – not to mention private initiatives. The US Overseas Private Investment Corporation (OPIC) and the Swiss Investment Risk Guarantee Agency (IRG) are good examples of national investment guarantee schemes. The first demonstrates the importance of US capital in foreign investment; the second was one of the very first mechanisms of its kind when it was created in 1970 and is highly representative of this kind of mechanisms in general. At the regional level, the Inter-Arab Investment Guarantee Corporation (IAIGC) is considered to be the first international guarantee organization and is one of the two existing regional schemes with the African Trade Insurance Agency (ATI). At the international level, the World Bank's Multilateral Investment Guarantee Agency, usually referred to by its acronym MIGA, is one of the most important initiatives in the domain of international investment along with the creation of the International Centre for Settlement of Investment Disputes (ICSID).

It may be said that at the institutional level most of these mechanisms foresee the possibility of interaction with other systems. The MIGA Convention contemplates possible cooperation with both national and regional agencies. The resources of the international agency may not be sufficient to guarantee non-commercial risks alone. It thus needs to act as a complement to services offered by other types of agencies. At the regional level, this holds true also for IAIGC, which has a similar provision in its charter. The national agency of the United States, OPIC, interacts with its international counterparts through coinsurance and reinsurance schemes. At first glance, these national, regional and international mechanisms are not in competition with each other. To the contrary, their founding texts enunciate the importance of cooperation between them.

### **(3) Dispute Settlement and Enforcement**

This part of the report focuses on the main issues arising out of the investor-State dispute settlement system, including those relating to enforcement of arbitral awards. Again this is by no means a complete overview of all issues; rather it seeks to highlight the most problematic questions that have arisen out of the interpretation of IIA provisions dealing with international investment arbitration. Accordingly sections (a) to (c) cover three preliminary issues of 'methods of dispute settlement', 'procedural transparency' and 'independence, impartiality and duty of disclosure of arbitrators'. Sections (d) to (g) deal with the main jurisdictional requirements of investment treaty arbitration. Then sections (h) and (i) address the 'relationship between international tribunals and domestic courts' as well as the related issue of 'parallel proceedings'. Section (j) focuses on the issue of 'compensation, damages and valuation'. Sections (k)-(m) deal with 'review of awards', 'a possible appellate system' and 'compliance and enforcement'. Finally, sections (n) and (o) address the issues of 'precedent' and 'tribunal's initiative and party autonomy' in international investment arbitration.

#### ***(a) Methods of Dispute Settlement***

Although ICSID arbitration has become the predominant method of settling investment disputes between investors and host states over the last decade, it clearly is not the exclusive one. Various other forms of mixed arbitration, as

<sup>74</sup> See further Andreas R. Ziegler and Louis-Philippe Gratton "Investment Insurance" in *Oxford Handbook* above n.1 ch.13.

regularly provided for in many BITs, are equally used in order to arrive at binding third-party dispute settlement.<sup>75</sup> The increased arbitral practice under the NAFTA, often leading to proceedings conducted pursuant to either the ICSID Additional Facility Rules or the UNCITRAL Arbitration Rules, bears witness to this development. The UNCITRAL Rules have also been applied with increased frequency in a number of recent ad hoc as well as institutionally supported arbitrations under the auspices of the PCA, the LCIA, the Stockholm Chamber of Commerce and other arbitration institutions.

The alternatives to mixed dispute settlement by arbitration, such as recourse to diplomatic protection, including the institution of proceedings before the ICJ or other inter-State courts or arbitral tribunals, are less often used in recent practice. However, it can be argued that a special form of the exercise of diplomatic protection has ultimately led to the establishment of the Iran-US Claims Tribunal which has produced a vast body of case-law, much of which is highly relevant to investment law.

In general, arbitral awards in investment disputes are complied with. Nevertheless, parties sometimes try to challenge awards, mostly by seeking their annulment in the national courts of the place of the arbitration. Though most of these attempts have remained unsuccessful, there is a high incidence of resorting to national courts in non-ICSID arbitrations. By contrast ICSID provides a “closed” system depriving national courts of their supervisory functions and reserving any control power to an ICSID annulment procedure. Although the increase of ICSID proceedings has also led to more frequent attempts to have ICSID awards annulled, it seems that this option has not so far been used excessively.

Furthermore, the relationship between international tribunals (deriving their existence from BITs) and domestic courts raises complex and controversial issues dealing with, for example, the distinction between treaty-based versus contract-based claims, the scope of umbrella clauses, and the effect of contractual forum selection clauses.

It is unquestionable that – with the significant growth experienced by investment arbitration over the last two decades – a number of inconsistent and partially conflicting decisions have been produced. Nonetheless, there is reason to believe that in the long run the growing body of arbitral awards in this field will contribute to the progressive formation and harmonisation of investment law.

#### ***(b) Procedural Transparency***

Increased transparency and public participation may impact upon the principles of confidentiality and privacy that have been traditionally respected in international commercial arbitration.<sup>76</sup> Due to the clear and strong public interest typically involved in investment arbitrations brought under either international investment treaties or host government agreements, however, there is a need to increase transparency and opportunities for public participation in investment arbitrations, and a concomitant need to provide rules regarding public participation to minimize the disadvantages that can be associated with it. In many respects, NAFTA Chapter Eleven tribunals have led the way among investment arbitral tribunals in providing greater transparency and public participation. Through standardized registration of claims, access to proceedings (e.g., public hearings), ability to provide input to the tribunal (e.g., *amicus curiae* briefs), and access to awards (e.g., publication), these tribunals have promoted greater public involvement and awareness, in some respects on a case-by-case basis. Amendments to the ICSID rules in 2006, as well as recent treaty practice (for example, the 2004 Central America-Dominican Republic-United States Free Trade Agreement (DR-CAFTA) and the 2007 COMESA Agreement on Investment), have also increased transparency and participation to the arbitral process.

#### ***(c) Independence, Impartiality and Duty of Disclosure of Arbitrators***

The general principles to which investment arbitrators must conform when it comes to their independence and impartiality do not fundamentally differ from those applied in international commercial arbitration disputes. Nonetheless, given the public nature of the interests underlying investment disputes, there is some concern that arbitrators sitting in these cases should be subject to more stringent requirements as to their independence and impartiality, and that more attention should be paid to the possibility of bias or potential conflicts of interest.<sup>77</sup>

The movement towards greater transparency in treaty arbitration has had a comparable effect on the accountability of arbitrators. Investment arbitration awards are often made public and can be accessible to a larger audience than the one restricted to arbitration specialists. The names of arbitrators and counsel are normally included in the awards. Given that the number of specialists working in this field remains somewhat limited, the same individuals may act as

<sup>75</sup> See further August Reinisch and Loretta Malintoppi “Methods of Dispute Resolution” in *Oxford Handbook* above n.1 ch.18.

<sup>76</sup> See further Joachim Delaney and Daniel Barstow McGraw “Procedural Transparency” in *Oxford Handbook* above n.1 ch.19.

<sup>77</sup> See further Loretta Malintoppi “Independence, Impartiality and Duty of Disclosure of Arbitrators” in *Oxford Handbook* above n.1 ch.20.

both counsel and arbitrators in treaty arbitrations. As a result, arbitrators in investment disputes are increasingly challenged on the basis of what has come to be known as "issue conflicts", that is objections over the appointment of an arbitrator who is - or has been - involved as counsel and advocate in other pending cases which share the same legal issues and whose outcome may risk impairing the arbitrator's judgment or give rise to possible bias.

Due to an apparent increase in the number of challenges, and the frequent intervention of national courts in these matters, particularly in *ad hoc* investment arbitrations, the arbitration community has been discussing whether a code of harmonised rules addressing issues of independence and impartiality of arbitrators is needed. Indeed, although professional associations have adopted guidelines for the conduct of arbitrators, these guidelines, as such, do not have binding legal force. While the idea of a "code of conduct" for ICSID arbitrators, suggested in a Working Paper of the ICSID Secretariat in the Autumn of 2004,<sup>78</sup> has, for the time being, been set aside, the arbitration community is still discussing whether the current state of play is sufficient to regulate these issues or whether it is necessary to adopt formal rules of deontology and ethics for investment arbitrators. Furthermore, the discussion is open as to whether the establishment of a neutral body, a "Challenge Facility" would be advisable. This could be composed of *super partes*, highly qualified members, and be charged with deciding upon conflicts of interests and requests for the disqualification or replacement of arbitrators.

#### ***(d) Consent to Arbitration***

Investment arbitration is always based on an agreement between the host State and the investor.<sup>79</sup> Consent is given in one of three ways: (i) a consent clause in a direct agreement between the parties (the agreement on consent between the parties need not be recorded in a single instrument); (ii) a provision in the national legislation of the host State offering consent to arbitration (the investor may accept the offer in writing at any time while the legislation is in effect often simply by instituting proceedings); (iii) a treaty between the host State and the investor's State of nationality offering arbitration to the nationals of one State party to the treaty against the other State party to the treaty (offers of consent contained in treaties must also be perfected by an acceptance on the part of the investor; at present, this method is by far the most frequently used one; most BITs include offers of consent. Multilateral treaties containing offers of consent to arbitration include the NAFTA and the ECT).

Not every reference to investment arbitration in national legislation or in treaties amounts to an offer of consent. Some just contemplate the possibility of future consent. The respective clauses must be drafted and interpreted carefully.

The scope of consent in national legislation and in treaties varies. For instance, some clauses offering consent to arbitration relate to all disputes arising from investments; others are restricted to compensation for expropriation. Some treaties restrict consent to claims involving the alleged breach of the treaty's substantive standards (treaty claims), thereby excluding claims for breaches of contract (contract claims). Some treaties contain provisions whereby the States parties undertake to observe any obligations they may have entered into with respect to investments (umbrella clauses). Violations of obligations of this kind would then amount to violations of the treaty. But not all tribunals have accepted that umbrella clauses convert contract claims into treaty claims for purposes of their jurisdiction.

Most offers of consent to arbitration are subject to procedural requirements. These typically include waiting periods to facilitate an amicable settlement. Some treaties require an attempt, for a limited period of time, to settle the dispute in domestic courts. This is not an application of the exhaustion of local remedies rule. Other treaties provide for the loss of the right to use international arbitration once the investor has turned to the domestic courts (fork in the road). Tribunals have treated these procedural requirements with some flexibility: waiting periods were discarded if there was no realistic chance of an amicable settlement; claimants were allowed to avoid the requirement to turn to domestic courts initially by invoking MFN clauses; fork-in-the-road provisions were not applied since the claims in the domestic proceedings were not exactly the same as in the international proceedings.

The relationship of consent to MFN clauses in treaties is somewhat controversial. The question is whether unspecific MFN clauses in treaties may be used to overcome limitations attached to expressions of consent. Some tribunals have held that a generally worded MFN clause covers dispute settlement and could therefore be used to import more favourable consent clauses from other treaties. Other tribunals have held that MFN clauses are restricted to the BITs' substantive standards of protection. In actual practice, MFN clauses have been applied to overcome procedural obstacles to arbitration. In most cases their application for the purpose of substituting missing consent clauses or of expanding the scope of consent was denied.

<sup>78</sup> See ICSID Secretariat *Possible Improvements of the Framework for ICSID Arbitration* (Discussion Paper, 22 October 2004); ICSID Secretariat *Suggested Changes to the ICSID Rules and Regulations* (Working Paper, 12 May 2005)

<sup>79</sup> See further Christoph Schreuer "Consent to Arbitration" in *Oxford Handbook* above n.1 ch.21.

The applicability of consent *ratione temporis* has also led to some difficult questions. Bilateral investment treaties frequently provide that they shall apply also to investments made before their entry into force. Some BITs state, however, that they shall not apply to disputes that have arisen before that date.<sup>80</sup> Even if some of the actions and events leading to the dispute may have occurred before the BIT's entry into force, the decisive time is the date at which the dispute actually began. If the consent to arbitration is limited to claims alleging a violation of the treaty that contains the consent, the date of the treaty's entry into force is also the date from which acts and events are covered by the consent.

The proper interpretation of consent clauses has also led to some debate. Arguments by respondents that an expression of consent to arbitration should be construed restrictively have generally not been successful. Some tribunals opted for an "effective interpretation" of consent clauses. But the majority of tribunals have endorsed a balanced approach to the interpretation of consent clauses which rejects both a presumption against and in favour of jurisdiction.<sup>81</sup>

Interpretation of consent to arbitration, even if it is based on national legislation or a treaty, is not simply a matter of statutory or treaty interpretation. The perfected consent is an agreement between the host State and the investor. Questions of jurisdiction arising from expressions of consent to arbitration are not subject to the law applicable to the merits of the dispute. They are governed by their own system which is determined by the mixed nature of the agreement to arbitrate in investment disputes.

#### ***(e) Jurisdiction and Admissibility***

The jurisdiction of the Tribunal is fundamental to the authority and decision-making of the arbitrators. Awards rendered without jurisdiction have no legitimacy and the absence of jurisdiction is one of the few recognised reasons for a domestic court to set aside or refuse recognition and enforcement of an award.<sup>82</sup> The various international arbitral institutions define their own jurisdictional requirements and these include the question of whether there is a dispute, the nature of the dispute that is required (subject matter jurisdiction) as well as, in some cases, personal jurisdiction. Additionally, some investment treaties contain denial of benefit provisions. Arbitral tribunals have imposed restrictions on the manner in which denial of benefits clauses may be invoked.

It is important to note the related but separate concept of admissibility. There has been no consistent approach to the distinction between jurisdiction and admissibility by investment treaty tribunals and, as such, it is the subject of much scholarship. This is in contrast to ICJ jurisprudence which has developed a clear distinction between the two concepts. In that context, an objection to the admissibility of a claim is the equivalent of pleading that the tribunal should rule the claim to be inadmissible on a ground other than its ultimate merits, whereas an objection to jurisdiction is the equivalent of pleading that the tribunal is incompetent to give any ruling at all, whether that ruling relates to the admissibility of the claim or its merits. It has been said that issues such as the existence of a legal dispute, the existence of a legal interest on the part of the claimant, or the nationality of the claim all provide grounds for a challenge to admissibility.

In the realm of investment treaty arbitration, objections based on the nationality of a claimant are, pursuant to Article 25 of the ICSID Convention, framed as jurisdictional objections as opposed to objections based on admissibility. Therefore, the manner in which an objection is worded can be important as to how the tribunal approaches it. The two approaches adopted in *Methanex*<sup>83</sup> and *Salini v Jordan*<sup>84</sup> demonstrate that the line between what is a jurisdictional objection, which if successful stops all proceedings in the case, and what is an objection based on a claim's admissibility, which does not stop the case but allows the rejection of a claim on grounds other than the merits is not always clear for investment claims. In both cases the tribunals were faced with an argument to the effect that even if all the facts alleged by the claimant were true, the claim still could not succeed. The tribunal in *Methanex* felt it necessary to consider each individual objection as either jurisdictional or going to admissibility, while the tribunal in *Salini* did not recognise this issue as one of admissibility but one going to its jurisdiction.

#### ***(f) Investments "In Accordance with Host State Law"***

The role of so-called "in accordance with host state law" clauses has gained importance in recent investment arbitrations. In *Inceysa v. El Salvador* in 2006 and in *Fraport v. Philippines* in 2007 the tribunals have for the first time denied jurisdiction because the claimants' investments had not been in compliance with the law of the host

<sup>80</sup> See examples in UNCTAD above n.29 at 19-20..

<sup>81</sup> For discussion see Schreuer above n.79 at 861-66.

<sup>82</sup> See further David A.R. Williams QC "Jurisdiction and Admissibility" in *Oxford Handbook* above n.1 ch.22.

<sup>83</sup> *Methanex Case* above n.39.

<sup>84</sup> *Salini v Jordan* above n.49.

state.<sup>85</sup> So far tribunals have consistently held that “in accordance with host state law” clauses – which are frequently included in BITs either in the definition of investment or in the provisions on promotion and protection or admission of investments – refer to the legality of an investment and not to its definition.

What is far less clear, however, is the question of how to determine whether an investment is in conformity with or in violation of national law. It remains unclear where a delimitation should be drawn between minor errors or insignificant deviations from domestic regulations and severe violations of the national law of the host state that would deny an investor or an investment the protection of a BIT. One possible threshold could be to consider simple formal errors, like in *Tokios Tokelès*,<sup>86</sup> as minor, with the investment still meeting the requirement of being “in accordance with host state law”, whereas actions either leading to civil liability or constituting criminal offences under domestic law would be illegal, consequently not being “in accordance with host state law”.

### **(g) The Jurisdictional Threshold of a Prima-Facie Case**

The prima facie test is firmly established as the threshold test for establishing jurisdiction *ratione materiae* in investment treaty cases.<sup>87</sup> The formulation of the approach and of the prima facie test, which appears to find most favour, is the following: (1) the tribunal must determine whether the claims fall within the scope of the investment treaty, assuming pro tem that they may be sustained on the facts; and (2) the tribunal should be satisfied that, if the facts alleged by the claimant ultimately prove true, they would be capable of falling within (or coming within) (or constituting a violation of) the provisions of the investment treaty. This formulation has received particular endorsement by the Tribunals in *Salini v Jordan*, *Impregilo v Pakistan* and *Saipem v Bangladesh*.<sup>88</sup> The semantic differences in wording between “falling within” or “coming within” or “constituting a violation of” appears to be of little importance.

The prima facie test has its origin in decisions of the PCIJ and ICJ. While reference is often made to the separate opinion of Judge Higgins in *Oil Platforms*, Judge Higgins' formulation of the test was whether the actions complained of “might” violate the applicable treaty.<sup>89</sup> The phrase “capable of falling within the provisions” of the treaty comes from decisions of the ICJ concerning provisional measures, and could be said to have been intended as a softer test given the relatively preliminary stage at which it is applied.

It has been questioned whether tribunals should apply the prima facie test both to the more objective issues requiring treaty interpretation and to factual issues (such as, can the alleged facts amount to expropriation) or just the latter. In his separate opinion in *Oil Platforms*, Judge Shahabuddeen favoured applying the prima facie test to both issues.<sup>90</sup> However, it appears that tribunals, where possible, seek to give a definitive interpretation of the treaty provisions at the jurisdiction stage.

Judge Higgins emphasised the absence of any jurisdictional bias in favour of claimant or respondent and this has been reiterated in a number of cases. Whether this was the case in practice in the ICJ was questioned by Judge Schwebel in his separate opinion in the *Nicaragua case*.<sup>91</sup> While some arbitral tribunals have suggested that particular regard should be given to the position of the respondent State (for example, *Mihaly v Sri Lanka*<sup>92</sup>, and *Joy Mining v Egypt*<sup>93</sup>), the consensus is that jurisdictional neutrality is to be preferred.

The identification of the three elements of the claimant's case to which the prima facie test should be applied, namely the facts of the case, the legal foundation of the case, and the relief sought, and the different approaches to each, as proposed in *Continental v Argentina*, may represent a refinement of the prima facie test.<sup>94</sup> The wording favoured by the United States and adopted in the CAFTA-DR and other treaties, as well as the recent amendments to

<sup>85</sup> *Inceysa Case* above n.30 and *Fraport Case* above n.31.

<sup>86</sup> *Tokios Tokelès Case* above n.15.

<sup>87</sup> See further Audley Sheppard “The Jurisdictional Threshold of a Prima Facie Case” in *Oxford Handbook* above n.1 ch.23.

<sup>88</sup> *Salini v Jordan* above n.49; *Impreglio v Pakistan* ICSID Case No. ARB/03/3, Decision on Jurisdiction, 22 April 2005 (available at <http://ita.law.uvic.ca/documents/impregilo-decision.pdf>); *Saipem S.p.A. v. The People's Republic of Bangladesh*, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007 (available at <http://ita.law.uvic.ca/documents/Saipem-Bangladesh-Jurisdiction.pdf>).

<sup>89</sup> *Oil Platforms (Islamic Republic of Iran v United States of America)* Preliminary Objection, Judgment, (1996) ICJ Reports 803 at 856 para.33.

<sup>90</sup> *Ibid* at 822.

<sup>91</sup> *Military and Paramilitary Activities in and Against Nicaragua (Nicaragua v United States of America)* Provisional Measures, Order of 10 May 1984 (1984) ICJ Reports 169 at 206-7.

<sup>92</sup> *Mihaly v Sri Lanka* ICSID Case No Arb/00/2, Award, 15 March 2002, 41 ILM 867 2002

<sup>93</sup> *Joy Mining v Egypt* ICSID Case No Arb/03/11, Award on Jurisdiction, 6 August 2004, 44 ILM 73 (2005).

<sup>94</sup> *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9, Decision on Jurisdiction, 22 February 2006 (available at: <http://ita.law.uvic.ca/documents/ContinentalCasualty-Jurisdiction.pdf>).

the ICSID Rules, suggests that some State parties want to encourage tribunals to be more robust in dismissing claims at an early stage.<sup>95</sup>

#### **(h) *The Relationship between International Tribunals and Domestic Courts***

The relationship between international tribunals (deriving their existence from bilateral investment treaties) and domestic courts is one of the most important and interesting issues of modern investment arbitration.<sup>96</sup>

Although most tribunals follow the course set in the *Vivendi* annulment decision by applying an action-based distinction between treaty-based versus contract-based claims, some tribunals prefer to attribute to international tribunals broader jurisdiction.<sup>97</sup> This broader jurisdiction includes pure contract claims, although some restrictions have been imposed, notably by requiring that the contractual parties be the same as the parties before the international tribunal.

Precisely because the basis of the distinction is the nature of the claim, classification and burden of proof as to whether a claim is merely contractual or not is essential. Tribunals have to some extent relied entirely on the claimant's submissions in this respect, although there is also significant support for the notion that some substantive review is required even at the preliminary jurisdictional stage.

A special category of jurisdictional and merits decisions involves so-called umbrella clauses. Here, there is a true divide between those in favour and those opposed to the elevation of contractual issue into international issues by virtue of the umbrella clause. The opponents use different arguments to bolster their assessment, varying from raising more fundamental objections to highlighting practical obstacles based on circumstances. At the same time, proponents have not always applied or needed to apply the umbrella clause in such a way that mere breach of contract was held to amount to a breach of international law. Further case law and writings will be required to provide guidance on the development of the theory, including the procedural consequences of the elevation. Solutions may well be dependent on revised treaty terms.

A fundamental element of the procedural consequences of a distinction between treaty and contract claims is the question whether the investor can waive his right of access to international arbitration under a BIT, or whether the right to bring a claim is not his to waive, as it is merely derivative of the state's right vis-à-vis another state.

#### **(i) *Parallel Proceedings***

Parallel proceedings, both between domestic courts and arbitration tribunals and between arbitration tribunals, is a situation which may engender a higher risk of inconsistent and conflicting decisions. In the field of investment arbitration, where issues of public interest are at stake, the risk of inconsistent decisions is a significant consideration.<sup>98</sup> The result could be that a State will be exposed to two opposite decisions in regard to the same measure (one decision condemning it for having violated its international obligations, the other not finding any responsibility, as seen in the two cases involving the Czech Republic),<sup>99</sup> which may undermine public acceptance of the adverse award.

The international dispute settlement system consists of an increasing number of permanent and *ad hoc* tribunals each of which is autonomous and not linked by a system of hierarchy to other tribunals. There is a view that those conflicts can be avoided only by specific treaty clauses providing a precedence or exclusivity of jurisdiction over certain matters, as has been provided in some human rights conventions. However, this may not necessarily be the only way, given the evidence of acceptance of *res judicata* as a general principle operative in the international order. In today's world, the current legal, social and economic framework is a moving target, open to evolution. In interpreting and applying legal principles such as *res judicata* and *lis pendens*, should one rely on legal formalism or economic flexibility? The Recommendations of the ILA Committee on International Commercial Arbitration on both *res judicata* and *lis alibi pendens* may offer guidance to arbitrators on how to view and apply these principles with a greater flexibility. A product of eminent jurists and practitioners including arbitrators, the ILA Recommendations, although non-legally binding, may constitute a first step towards recognition and more regular and less formalistic application of these principles in international arbitration.

<sup>95</sup> See Sheppard n.87 above at 957-60.

<sup>96</sup> See further Jacomijn J. van Haersolte-van Hof and Anne K. Hoffmann "The Relationship between International Tribunals and Domestic Courts" in *Oxford Handbook* above n.1 ch.24.

<sup>97</sup> *Compania de Aguas del Aconquija SA and Vivendi Universal (Formerly Compagnie Générale des Eaux v Argentina* ICSID Case No Arb/97/3, Award, 21 November 2000, 40 ILM 426 (2001); Decision on Annulment, 3 July 2002, 41 ILM 1135 (2002). See discussion in van Haersolte-van Hof and Hoffmann above n.96 at 967-71.

<sup>98</sup> See further Katia Yannaca-Small "Parallel Proceedings" in *Oxford Handbook* above n.1 ch.25.

<sup>99</sup> *CME Czech Republic B.V. v. Czech Republic* above n.10 and *Lauder v. Czech Republic* UNCITRAL Award (Final), 3 September 2001 (available at: <http://ita.law.uvic.ca/documents/LauderAward.pdf>).

Treaty law provides a number of tools for dealing with parallel proceedings by essentially requesting the investor to make a choice, usually irrevocable, among different fora. The exhaustion of local remedies, which bans an investor from bringing a municipal claim parallel to investment arbitration is now generally not required. The fork-in-the-road provision is subject to the same requirements as *res judicata* and *lis pendens*, i.e. identity of the parties, object and grounds, and in reality has been proved complex, inflexible and almost meaningless by its restrictions. The waiver included in NAFTA, recent US FTAs and the new model US BIT represents a broader forum selection provision, which is more flexible than the previous ones.<sup>100</sup> Its application has been scarce and its benefits remain to be tested further.

The umbrella clause could be seen as a preventive tool against the occurrence of parallel proceedings since it covers both treaty and contract claims which otherwise would have been submitted at the same time to domestic courts. However, no consensus has emerged yet as for its interpretation and application.

Consolidation of claims emanating from the same state measure and based on similar factual and legal elements could protect against the risk of inconsistent decisions and is a promising path. It has its roots in commercial arbitration where it is based essentially on the party autonomy principle (i.e. parties' consent), except in a few cases where national arbitration laws provide for court-ordered consolidation. In investment arbitration, NAFTA as well as a number of recent US, Canada and Mexico FTAs and the US model BIT and Canada model FIPA, provide for consolidation of claims when there are questions of law and fact in common.<sup>101</sup> Two NAFTA consolidation tribunals issued their opinions on this issue, which differ in their conclusions as to the fairness of consolidation in the circumstances.<sup>102</sup>

Recent attempts by political and legal communities to reach a consensus on the desirability of consolidation provisions in investment agreements have failed, principally because they were not convinced that their advantages exceed the disadvantages.

In the meantime and in the absence of such provision in most investment treaties, the disputing parties who wish to do so could take the initiative and ask for consolidation (or "de facto" consolidation). Arbitral institutions such as ICSID could facilitate the process by appointing the same panel of arbitrators as has already been done in some of the cases involving Argentina.

#### **(j) Compensation, Damages and Valuation**

Developments in this area of law, perhaps more so than others, are dependent upon the way modern financial practices for valuation of assets under circumstances of risk and uncertainty evolve.<sup>103</sup> The main "fashion" in the modern financial practice has been the paradigm shift from backward looking ("historic cost") to forward looking ("net present value of future cash flows") methods of valuing assets. But these modern methods are not infallible; they are continuously being supplemented by more recent financial inventions – and that is likely to continue. If we compare the "old-fashioned" historic cost method with the modern "prospective earnings potential" method, the old-fashioned method has virtues which are as well recognized by the leading investors: it provides objectively identifiable and reasonably certain inputs while the forward-looking method in essence relies on speculation. In perfect market conditions, these methods should yield the same result. While arbitral tribunals have paid lip service to modernity, they have moved cautiously and as a rule rejected "speculative elements" – which are in essence the very core of the net present value method. In these circumstances, the proper approach, for the time being, should be to use both the historic method and supplement it cautiously with calculations based on the prospective, future earnings method as only a corrective element, e.g. in cases where the historic cost method is likely to diverge substantially from the current market value. Current market value, while generally endorsed, is itself in most situations of little help as investment projects are not commodities with ready market-based price quotes, but rather very individualized projects for which market prices are rarely available – and if so, as a rule heavily fluctuating, particularly if the risk perceptions are priced in properly. The main challenge is how to avoid double recovery, in particular in cases of cancellation of long-term contracts. Reliance on the forward-looking method carries a particular risk of double recovery.

<sup>100</sup> See Yannaca-Small above n.98 at 1028-29.

<sup>101</sup> Ibid at 1034-36.

<sup>102</sup> *Corn Products International, Inc. v. United Mexican States* and *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc. v. United Mexican States*, Order of the Consolidation Tribunal, May 20, 2005; *Canfor Corp. v. United States of America*, *Terminal Forest Products Ltd. v. United States of America* and *Tembec Inc. et al. v. United States of America*, Order of the Consolidation Tribunal, 7 September 2007 at <http://naftaclaims.com/Disputes/USA/Softwood/Softwood-ConOrder.pdf>, discussed ibid at 1036-37.

<sup>103</sup> See further Thomas W Walde and Borzu Sabahi "Compensation, Damages and Valuation" in *Oxford Handbook* above n.1 ch.26.

Valuation for compensation is essentially torn between two conflicting poles: on one hand, a subjective approach where the individual situation of the investor (always volatile, changing and hard to identify objectively) is relied upon (e.g. to calculate interest rates, value an asset, identify risk relevant for discount rates) and, on the other hand, a more standardized or generic approach where an “objective” generic comparator is used to identify the value and compensation due to the investor. This approach is often found in law – e.g. in the issue of pre-quantified penalties as an expression of presumed damages. In legal history, “objective” approaches (e.g. “penalty tariffs”) seem to have been around first; the 19<sup>th</sup> century with its emphasis on individual freedom moved towards the “subjective” approach. At present, the complexity and unpredictability of individual situations suggests perhaps a reversal to an again more “objective” and “standardized” approach, in particular with respect to the assessment of damages, valuation for compensation, risk, discount and interest rates. One possibility is to start with the generic approach, use it to create a presumption for damages and only deviate if the individual situation of the investor can be shown to be significantly different and if this relevance can be shown to be known to the host state.<sup>104</sup>

A particular challenge in this area, which remains to be fully worked out in arbitral decisions, is how to calculate compensation in the case of breach of the non-expropriatory disciplines – national treatment, denial of justice and fair and equitable treatment in particular. It is premature to come up with a proposal for a conclusive set of rules here. Tribunals and counsel could make more use of non-financial remedies that can be categorized as “restitution”, in particular a preliminary order to lift a discriminatory treatment (“annulment” in administrative law terms), to redo an administrative or judicial decision in full compliance with due process or to seek other administrative remedies that provide full satisfaction to the investor and which correspond to the detriment suffered.<sup>105</sup> Only if such remedies – e.g. by interim awards – prove to be impractical or are not allowed under the respective treaty, should one consider financial compensation as the remedy of last recourse.

In this case, the currently unresolved problem is to compare the situation the investor is in due to the breach of the treaty obligation by the government with a situation the investor would have been in had the government conducted its affairs properly in compliance with the applicable treaty rules. Tribunals, so far, have tried to avoid these difficult questions by identifying easily and objectively ascertainable obligations – e.g. non-payment of contractually due obligations or over-imposition of tax duties – to determine the compensation due in such situations. It remains to be seen how the jurisprudence in this respect will develop but comparative and international administrative law could provide useful material for “benchmarking” and analogy, with its preference for injunctive “restitution” or annulment over financial compensation, its linking of compensation with the egregiousness of the relevant breach of legal rules and its balancing between legitimate regulatory and investor interests.<sup>106</sup>

### **(k) Review of Awards**

While the finality of arbitral awards is a key feature of arbitration in general, the possibility of a review (albeit limited) of the arbitral award may be deemed as an important element of international investment arbitration.<sup>107</sup> The absence of such review may undermine the trust in the investor-state dispute settlement system. The more widely used investment arbitration rules are the UNCITRAL Arbitration Rules and the ICSID Convention Rules. While ICSID offers a specific system of post-award remedy (particularly including an ad hoc annulment proceedings under Article 52), UNCITRAL Rules are silent in this respect and post-award remedies are left to rules adopted in national jurisdiction. Accordingly, UNCITRAL can reach a level of predictability only with great difficulty as municipal laws differ from state to state.

With regard to ICSID *ad hoc* annulment proceedings, there is no agreement whether the interpretation of Article 52 ICSID, laying out a limited set of grounds for contesting an ICSID award, should be a restrictive one, (as is the case for commercial arbitration) or whether, given the particular character of the disputes at hand, it would be better to adopt an extensive interpretation (with the risk that such a remedy will become more similar to a so called “appellate” system). In particular, the interpretation of Article 52(1)(e) (failure to state reasons) remains very controversial as it could make it easier for annulment committees to review the merits of the case rather than restrict themselves to review of a serious procedural defect. Equally, it will also be interesting to monitor the interpretation of Article 52(1)(b) (manifest excess of powers), especially with reference to application of the governing law. The ‘application of the incorrect law’ or the ‘failure to apply the correct law’ are not identical to the ‘incorrect

<sup>104</sup> See Walde and Sabahi *ibid* at 1115.

<sup>105</sup> See for example the approach of the tribunal in *Goetz v. Burundi* above n.45.

<sup>106</sup> See Walde and Sabahi above n.103 at 1082-89.

<sup>107</sup> See further Vladimir Balas “Review of Awards” in *Oxford Handbook* above n.1 ch.27.

application of correct law'. Despite several attempts to annul or set aside investment awards under either domestic rules or ICSID rules, there are only a handful of instances where this has occurred.<sup>108</sup>

### ***(l) Appellate System***

Most successful judicial systems are accompanied by an appellate process. However, the need for accommodating such a mechanism in disputes processed through arbitration systems has not necessarily been apparent. The need to place 'consistency and coherence' as sacrosanct -- as the basis for an appellate system -- needs to be considered with some degree of caution. From a development perspective, until there is agreement on a multilateral investment agreement, a treaty-specific appeal system may be preferable.<sup>109</sup> A principal concern about the efforts to introduce an appellate system in the investment sphere is that it seeks to add to the coherence and development of international investment law through a somewhat back-door non-transparent route. Furthermore, a development friendly appellate system requires in particular a focus on its apparatus of interpretation, on participatory rights and technical assistance.<sup>110</sup>

### ***(m) Compliance and Enforcement***

At this point in time, anecdotal evidence would suggest that state respondents in investment arbitrations have complied with their international obligations by abiding by final awards.<sup>111</sup> However, there are a number of examples in which Respondents have resisted execution in domestic courts. In the 1980s certain ICSID cases involved a challenge to the enforcement of investment arbitration awards by State Respondents. These cases were *Benvenuti & Bonfant v. Congo*,<sup>112</sup> *SOABI v. Senegal*,<sup>113</sup> before the French courts and *LETCO v. Liberia*,<sup>114</sup> before the US courts. There was some confusion on the part of these courts as to the proper scope of their powers, and ultimately as to the appropriate level of deference when faced with a request for enforcement through the processes of recognition and then execution. The end result was that a clear distinction between recognition and execution, as envisioned by the drafters of the ICSID Convention in Articles 53 and 54, has been accepted though not without some difficulty.

Since that time, there have been very few cases. The two most recent cases *AIG Partners v. Kazakhstan*<sup>115</sup> and *Sedelmayer v. Russia*<sup>116</sup> clearly demonstrate the major weakness in the system for enforcement of investment awards - the continued role sovereign immunity plays in limiting the means by which investors may execute against "State" assets under domestic legal systems.<sup>117</sup>

<sup>108</sup> See *ibid* at 1147

<sup>109</sup> See further Asif H. Qureshi "An Appellate System in International Investment Arbitration?" in *Oxford Handbook* above n.1 ch.28.

<sup>110</sup> *Ibid* at 1168

<sup>111</sup> See further Alan S. Alexandroff and Ian A. Laird "Compliance and Enforcement" in *Oxford Handbook* above n.1 ch.29.

<sup>112</sup> *SARL Benvenuti & Bonfant v People's Republic of the Congo*, ICSID Case No. ARB/77/2, Award, August 8, 1980, (1993) 1 ICSID Rep. 330 ("Benvenuti & Bonfant"). On December 23, 1980, the Paris Tribunal de grande instance refused enforcement and execution of this tribunal's award, but the decision was not published. However, a good review of the key elements of the decision are located at (1993) 1 ICSID Rep. 368. On June 26, 1981, the Claimants appeal to the Cour d'appel was successful with the adverse decision of the Tribunal de grande instance overturned. See (1993) 1 ICSID Rep. 369-72.

<sup>113</sup> *Société Ouest Africaine des Bétons Industriels (SOABI) v Senegal*, ICSID Case No. ARB/82/1, Award, February 25, 1988, (1991) 6 ICSID Rev-FILJ. 125, (1994) 2 ICSID Rep. 114 ("SOABI"). Again, the decision against the Claimant of the Tribunal de grande instance has not been published. The Cour d'appel provided its decision in favour of the Claimant on December 5, 1989 and reports of that decision may be found at 2 ICSID Rep. 337. The decision of the Cour de cassation was issued on June 11, 1991 and is reported at (1991) 6 ICSID Rev. -FILJ 598 (1994) 2 ICSID Rep. 341.

<sup>114</sup> *Liberian Eastern Timber Corporation (LETCO) v Republic of Liberia*, ICSID Case No. ARB/83/2, Award, March 31, 1986, (1994) 2 ICSID Rep. 346 ("LETCO"). There are three U.S. District Court decisions published in regard to the LETCO enforcement proceedings: (1) U.S. District Court, Southern District of New York, September 5, 1986, (1987) 2 ICSID Rev. -FILJ 187 (1987), (1994) 2 ICSID Rep. 384; (2) U.S. District Court, Southern District of New York, December 12, 1986, (1986) 650 F.Supp. 73 (S.D.N.Y.), (1994) 2 ICSID Rep. 385; (3) U.S. District Court, District of Columbia, April 16, 1987, (1987) 659 F.Supp. 606 (D.D.C.), (1994) 2 ICSID Rep. 391.

<sup>115</sup> *AIG Capital Partners Inc and another v Republic of Kazakhstan*, [2005] EWHC Comm. 2239, October 20, 2005, available at [www.bailii.org/ew/cases/EWHC/Comm/2005/2239.html](http://www.bailii.org/ew/cases/EWHC/Comm/2005/2239.html).

<sup>116</sup> *Sedelmayer v. Russian Federation* (Germany/Soviet Union BIT), Decision on Jurisdiction and Final Award, 7 July 1998. The Sedelmayer arbitration was conducted under the Stockholm Chamber of Commerce Arbitration Rules.

<sup>117</sup> Alexandroff and Laird above n.111 at 1185.

With the maturity of investment arbitration, and with more final awards in the future, the issue of enforcement and particularly execution will become increasingly important. It raises the possibility of actions by state respondents seeking to avoid enforcement of awards which could lead to the weakening of this remedial process.

For investment arbitration to be a complete system of justice, the enforcement of the will of the arbitral decision makers is a critical and final element of that system. The international law delict of denial of justice holds a basic requirement on domestic systems that the judgments of courts must be enforceable. No less a standard may apply to international investment arbitration. Applying the concept of denial of justice to international investment arbitration, there is a strong argument that state parties to a BIT or the ICSID Convention have no less an obligation to maintain a “decent” and available system of justice with respect to the investment arbitration system they have created. Although there is yet to be an example, the question arises whether there may be an independent action for an investor to make a new claim against the respondent for failure to enforce the original award. The question would, of course, remain as to how that award would become enforceable.

As the case-law indicates, domestic courts that have been seized with the issue of enforcement and execution of final awards have been largely deferential. In the context of challenges to recognition of ICSID awards, there has been no successful challenge. The problems that have arisen have related to the application of the sovereign immunity defence, which is endorsed in the ICSID Convention Article 55. Although a number of respondents have argued that courts should not be deferential to investment arbitration awards, most courts have rejected those arguments and maintained a high level of deference.<sup>118</sup> Whether this high level of deference by domestic courts to arbitral awards continues will remain an open question for the foreseeable future. More critically though is the difficulty placed in front of claimants where the respondent State Party refuses to satisfy the award and the claimant has been forced to identify assets that can withstand the sovereign immunity claims raised by State respondents. Thus enforcement and execution remain a problem for claimants.

#### ***(n) Doctrine of Precedent***

Reliance on past decisions is a fundamental feature of any orderly decision process. Drawing on the experience of past decisions plays an important role in securing the necessary uniformity and stability of the law. The need for a coherent case law is evident. It strengthens the predictability of decisions and enhances their authority.

It is well-established that the doctrine of precedent, in the sense known in the common law, does not apply in international adjudication, including investment arbitration.<sup>119</sup> In other words, tribunals in investment arbitrations are not bound by previous decisions of other tribunals. A doctrine of precedent is difficult to apply to a series of unconnected arbitrations governed by public international law. Tribunals in investment disputes, including ICSID tribunals, often cite previous decisions of other tribunals. Individual tribunal decisions have persuasive force and compel the respectful attention of tribunals confronted with similar cases.

Consistency is certainly one of the key objectives in developing international investment jurisprudence. Looking at the practice, it appears that occasional views expressed by States parties to treaties on the meaning of particular provisions are not a viable method to achieve uniformity of interpretation. Possible solutions may include: (a) creation of institutionalized mechanisms to achieve official, uniform interpretations of the relevant treaty terms; (b) creation of an appeals facility that would open the possibility to review decisions by a standing appellate body; (c) provision for preliminary rulings while the original proceedings are still pending (under such a system a tribunal would suspend proceedings and request a ruling on a question of law from a body established for that purpose).<sup>120</sup>

Most tribunals are aware of the role they play in developing legal principles. They see it as part of their responsibility to elaborate the applicable principles of international law. In this way, investment treaty awards can play a role in counteracting the increasing fragmentation of international law.

#### ***(o) Tribunal's Powers versus Party Autonomy***

Investment disputes may be carried out under a variety of arbitration rules, ranging from the ICSID rules and Convention to the UNCITRAL rules and the arbitration law of the country where the arbitral tribunal has its venue.<sup>121</sup> There is thus no uniformity in procedure, including also the issue of the tribunal's powers in respect of the arguments made by the parties. As a general rule, the parties' submissions determine the scope of the dispute and hence the tribunal's mandate. The arbitral tribunal is not supposed to exceed the powers thus conferred on it by the

<sup>118</sup> See Alexandroff and Laird *ibid* at 1187.

<sup>119</sup> See further Christoph Schreuer and Matthew Weniger “A Doctrine of Precedent?” in *Oxford Handbook* above n.1 ch.30.

<sup>120</sup> *Ibid* at 1200-1205.

<sup>121</sup> See further Giuditta Cordero Moss “Tribunal's Powers versus Party Autonomy” in *Oxford Handbook* above n.1 ch.31.

parties. There are situations, however, in which the arguments made by one or more parties may require integration or further elaboration: for example, if the defendant does not participate in the proceedings.

The power of the tribunal is ultimately limited by the rules on jurisdiction as well as any mandatory rules of procedure contained in the applicable instruments, rules and arbitration law. The power of the tribunal is also limited, indirectly, by the criteria for determining the validity and enforceability of an arbitral award, and, in particular, by the principles of excess of power, adversarial proceeding and procedural irregularity. These principles are fundamental in most arbitration rules and laws that an investment dispute may be subject to. Within the framework set by these common principles, there does not seem to be a uniform approach as to the extent to which the tribunal may or shall integrate or develop arguments that should have been made by the parties, both in respect of questions of fact and in respect of questions of law.

On the one hand, some systems assume that the tribunal has a neutral role and does not interfere with the autonomy of the parties. Under this adversarial system, traditionally ascribed to the Common Law systems but not found in its pure form any longer, arbitrators listen to the parties' arguments and confine their own role to deciding which of these deserves to win. Particularly in the field of commercial arbitration legal doctrine often focuses on the consensual character of arbitration and emphasises that the arbitral procedure should be left totally to the parties.

Other systems, mainly the Civilian systems, promote a more judiciary and interventionist role, inspired by the maxim *iura novit curia*. Under this system, the tribunal is allowed or even expected to draw own factual conclusions and develop a legal argumentation independently of the arguments made by the parties. Both in the field of commercial and of investment arbitration, legal doctrine affirms that the tribunal enjoys ample room for independently evaluating the presented evidence, legal arguments and sources, and for requesting additional information and thus introducing new elements in the proceeding.

The tribunal has to respect the applicable arbitration rules and laws. These permit a certain independence from the arguments made by the parties, as long as the jurisdiction and the factual scope of the dispute are not exceeded, and the adversarial principle is safeguarded by giving the parties the possibility to comment on the arguments developed by the tribunal.

### **Concluding Remarks**

The preceding overview of what the Committee has identified as the major issues arising out of contemporary developments in international investment law shows how complex and multifaceted this area of international law is becoming. Equally it is noticeable that full consensus does not exist on all aspects of this law. It is still a new and evolving discipline, one that is subject to significant political currents and specific commercial social and economic interests. That said, it is clear that this area of law will continue to offer many challenges for its successful development. In particular, a major challenge is the need for greater clarity and consistency in the interpretation of specific treaty standards. Although each treaty may be unique as the product of the negotiations between the contracting parties, the degree of similarity between treaty formulations should encourage an element of uniform interpretation of provisions. At the very least the same treaty should be uniformly interpreted in all cases in which it forms the basis of a dispute.

In addition, while the legal basis of this area of law lies in distinctive treaties, the need for a uniform and predictable process of interpretation, and agreed approaches to substantive rights and duties in treaties, would appear to arise out of the very functions of this area of law: to allow host countries to attract and to benefit from foreign investment and for investors to enjoy a transparent, secure and predictable investment environment. Thus it is a field that combines both commercial and public law concerns and requires a balancing of rights and obligations to ensure that these complementary aims are achieved. This may require the highlighting of the social and economic consequences of investment activity upon host countries, as through increased awareness of the need to ensure that corporate social responsibility standards are respected by investors, through the possible introduction of new investor and home country obligations in new generations of agreements, and through the clarification of the scope of the host country's right to regulate alongside the existing rights of investors for protection of their assets. Equally, a more development-oriented approach may be needed. Indeed countries are already experimenting with such issues in new model agreements as has been noted above.

Finally, a further long-term objective for the development of this field should be to promote alternative methods for the resolution of investment disputes apart from arbitration. The latter should be seen as a last resort remedy, given the increasingly adversarial nature of the process. The rise in investment disputes submitted to arbitration in the opening decade of the 21<sup>st</sup> century has pushed international investment law towards a more litigious character. While this may be a welcome and interesting development for international lawyers, it has to be asked whether this field should take on such a character. Given that the main aim of the parties to foreign investment contracts is to offer economic development for the host country in return for a reasonable rate of profit for the investor, disputes

should not form the "*leitmotif*" of this subject. Rather co-operation and long-term collaboration should play this role. Indeed co-operation and collaboration have been the principal characteristics of the field for many years and it is to be hoped that it will continue to operate in such a fashion. International lawyers have a major role to play in the realisation of this situation and it is hoped that the present Report will make a modest contribution to that process.