INVESTOR-STATE DISPUTES ARISING FROM INVESTMENT TREATIES: A REVIEW

UNCTAD Series on International Investment Policies for Development

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NOTE

As the focal point in the United Nations system for investment and technology, and building on 30 years of experience in these areas, UNCTAD, through DITE, promotes understanding of key issues, particularly matters related to foreign direct investment and transfer of technology. DITE also assists developing countries in attracting and benefiting from FDI and in building their productive capacities and international competitiveness. The emphasis is on an integrated policy approach to investment, technological capacity building and enterprise development.

The term “country” as used in this study also refers, as appropriate, to territories or areas; the designations employed and the presentation of the material do not imply the expression of any opinion whatsoever on the part of the Secretariat of the United Nations concerning the legal status of any country, territory, city or area or of its authorities, or concerning the delimitation of its frontiers or boundaries. In addition, the designations of country groups are intended solely for statistical or analytical convenience and do not necessarily express a judgement about the stage of development reached by a particular country or area in the development process.

The following symbols have been used in the tables:

Two dots (..) indicate that data are not available or are not separately reported.

Rows in tables have been omitted in those cases where no data are available for any of the elements in the row.

A hyphen (-) indicates that the item is equal to zero or its value is negligible.

A blank in a table indicates that the item is not applicable.

A slash (/) between dates representing years (e.g. 1994/1995) indicates a financial year.

Use of a dash (–) between dates representing years (e.g. 1994–1995) signifies the full period involved, including the beginning and end years.
References to “dollars” ($) are to United States dollars, unless otherwise indicated.

Annual rates of growth or change, unless otherwise stated, refer to annual compound rates.

Because of rounding, details and percentages in tables do not necessarily add up to totals.

The material contained in this study may be freely quoted with appropriate acknowledgement.
PREFACE

The secretariat of the United Nations Conference on Trade and Development (UNCTAD) is implementing a programme on international investment arrangements. It seeks to help developing countries to participate as effectively as possible in international investment rule-making. The programme embraces policy research and development, including the preparation of a series of issues papers; human resources capacity-building and institution-building, including national seminars, regional symposia and training courses; and support to intergovernmental consensus-building, as well as dialogues between negotiators and groups of civil society.

This paper is part of a new Series on International Investment Policies for Development. It builds on, and expands, UNCTAD's Series on Issues in International Investment Agreements. Like the previous one, this new series is addressed to government officials, corporate executives, representatives of non-governmental organizations, officials of international agencies and researchers.

The series seeks to provide a balanced analysis of issues that may arise in the context of international approaches to investment rule-making and their impact on development. Its purpose is to contribute to a better understanding of difficult technical issues and their interaction, and of innovative ideas that could contribute to an increase in the development dimension of IIAs.

The series is produced by a team led by James Zhan. The team members are Victoria Aranda, Amare Bekele, Hamed El-Kady, Anna Joubin-Bret, Joachim Karl, Martin Molinuevo, Anca Radu, Marie-Estelle Rey, Elizabeth Tuerk and Jörg Weber. Khalil Hamdani provides overall guidance. The members of the Review Committee are Mark Kantor, Mark Koulen, Peter Muchlinski, Antonio Parra, Patrick Robinson, Pierre Sauvé, M. Sornarajah and Kenneth Vandevelde.

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Supachai Panitchpakdi
Geneva, February 2006
Secretary-General of UNCTAD
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UNCTAD has carried out a number of activities related to the work programme in cooperation with other intergovernmental organizations, including Agence pour la Francophonie, Banco Centroamericano de Integración Económica, the CARICOM Secretariat, the German Foundation for Development, the Inter-Arab Investment Guarantee Corporation, the Inter-American Development Bank (BTD/INTAL), the League of Arab States, the Organization of American States, Secretaria de Integración Económica Centroamericana and the Secretaria General de la Comunidad Andina. UNCTAD has also cooperated with non-governmental organizations, including the Centre for Research on Multinational Corporations, the Consumer Unity and Trust Society (India), the Dutch Foundation for Research on Multinationals (SOMO), the Economic Research Forum (Egypt), the European Roundtable of Industrialists, the Friedrich Ebert Foundation (Germany), the German Foundation for International Development, the International Confederation of Free Trade Unions, the Labour Resource and Research Institute (LaRRI) (Namibia), Oxfam, the Third World Network and World Wildlife Fund International. Since 2002, a part of the work programme has been carried out jointly with the World Trade Organization (WTO).

Funds for the work programme have so far been received from Australia, Brazil, Canada, France, Japan, the Netherlands, Norway, Sweden, Switzerland, the United Kingdom and the European Commission. Argentina, Botswana, China, Colombia, Costa Rica, Croatia, Cuba, the Czech Republic, Djibouti, Egypt, Gabon, Germany, Guatemala, India, Indonesia, Jamaica, Malaysia, Mauritania, Mexico,
Morocco, Namibia, Pakistan, Peru, Qatar, Singapore, South Africa, Sri Lanka, Thailand, Trinidad and Tobago, Tunisia, Venezuela and Yemen have also contributed to the work programme by hosting regional symposia, national seminars or training events.

In pursuing this programme of work, UNCTAD has also closely collaborated with a number of international, regional and national organizations, particularly Centro de Estudios Interdisciplinarios de Derecho Industrial y Económico (University de Buenos Aires), the Indian Institute of Foreign Trade, the Legon Centre of Accra (Ghana), ProInversión (Peru), Pontificia Universidad Católica del Perú, the National University of Singapore, Senghor University (Egypt), the University of Dar Es Salaam (United Republic of Tanzania), the University de Los Andes (Colombia), the University of Campinas (Brazil), the University of Lima (Peru), the Universidad del Pacífico (Peru), the University of Pretoria (South Africa), the University of Tunis (Tunisia), the University of Yaoundé (Cameroon), the Shanghai WTO Affairs Consultation Center (China) and the University of the West Indies (Jamaica, and Trinidad and Tobago). All of these contributions are gratefully acknowledged.
# CONTENTS

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>PREFACE</td>
<td>v</td>
</tr>
<tr>
<td>EXECUTIVE SUMMARY</td>
<td>1</td>
</tr>
<tr>
<td>INTRODUCTION</td>
<td>3</td>
</tr>
<tr>
<td>I. KEY PROCEDURAL ISSUES</td>
<td>15</td>
</tr>
<tr>
<td>A. Definition of “investor” and “investment”</td>
<td>15</td>
</tr>
<tr>
<td>B. Multiplicity of forums</td>
<td>17</td>
</tr>
<tr>
<td>C. Conflict of jurisdictions</td>
<td>18</td>
</tr>
<tr>
<td>D. Treaty shopping</td>
<td>21</td>
</tr>
<tr>
<td>E. Transparency</td>
<td>22</td>
</tr>
<tr>
<td>F. Implications</td>
<td>24</td>
</tr>
<tr>
<td>II. KEY SUBSTANTIVE ISSUES</td>
<td>31</td>
</tr>
<tr>
<td>A. Right of establishment</td>
<td>31</td>
</tr>
<tr>
<td>B. National treatment</td>
<td>32</td>
</tr>
<tr>
<td>C. Most-favoured-nation treatment</td>
<td>34</td>
</tr>
<tr>
<td>D. Fair and equitable treatment and full protection and security</td>
<td>37</td>
</tr>
<tr>
<td>E. Expropriation</td>
<td>41</td>
</tr>
<tr>
<td>F. Other legal claims by investors</td>
<td>47</td>
</tr>
<tr>
<td>G. Implications</td>
<td>47</td>
</tr>
<tr>
<td>CONCLUSIONS</td>
<td>53</td>
</tr>
<tr>
<td>A. Procedural issues</td>
<td>53</td>
</tr>
<tr>
<td>B. Substantive issues</td>
<td>59</td>
</tr>
<tr>
<td>C. The role of the international community</td>
<td>61</td>
</tr>
<tr>
<td>REFERENCES</td>
<td>65</td>
</tr>
</tbody>
</table>
Annexes

Annex 1: Known investment treaty claims ............................................... 69
Annex 2: List of cases reviewed ............................................................ 71

Selected UNCTAD publications on TNCs and FDI ......................... 77

QUESTIONNAIRE .................................................................. 95

Boxes

1. Financial implications of investor-State dispute settlement ..........9

Figures

1. Known investment treaty arbitrations .................................................4
2. Disputes, by rules of arbitration .......................................................5
EXECUTIVE SUMMARY

The settlement of disputes between investors and the States in which they operate is a key aspect of the system of investment protection established in international investment agreements. Thus, the majority of international investment agreements contain provisions on investor-State dispute settlement. These provisions have been increasingly used in recent years, and this has resulted in more arbitral awards. It is the aim of this paper to take stock of, and to analyse, the nature and implications of this trend. In particular, it will consider not only the statistical aspects of this development, but also the effects of arbitral decisions on the evolution of dispute settlement procedures under international investment agreements and on the interpretation and further refinement of the substantive standards of protection that they contain.

The statistical aspects of the increased trend towards the use of investor-State arbitration are considered in the Introduction. Section I deals with procedural aspects, beginning with the question of the interpretation of the terms “investor” and “investment”, key concepts in determining which party can bring a claim. Given the often complex composition of foreign investors and their investments, this is an issue that can lead to multiple claims and multiple venues, matters that have caused some concern in the light of recent multiple disputes. In addition, the issue of possible conflicts of jurisdictions is discussed, focusing on whether the use of “domestic forum clauses” can preclude recourse to international tribunals. “Umbrella” clauses, which may allow for the international settlement of disputes arising out of investment contracts that are normally litigated before national forums, have also become the subject of recent decisions, although their scope is by no means fully settled. This section also addresses the issue of “treaty shopping” and to what extent tribunals will allow foreign investors to alter their location and ownership structures to take advantage of IIA dispute settlement provisions available in the locations in question. Finally, the question of the transparency of investor-State proceedings is addressed, an issue that has gained prominence in recent years as a result of the clash between the traditional party-based nature of international arbitration, which tends
towards the privacy of proceedings, and the increasingly central role that such dispute settlement may play in public policy development, which may require greater openness and public access.

Section II covers the major substantive interpretations of investment protection provisions in IIAs offered by international tribunals. These interpretations are far from being final, in that tribunals are free to interpret the agreement before them as they see fit, following the general rules of treaty interpretation under international law, and they are not subject to any doctrine of precedent or to the views of a final appellate body. Thus, the development of case law in this area (as in relation to procedural issues) is in a state of constant evolution. Nonetheless, certain trends are evident in relation to the interpretation of rights of establishment, the national treatment and most-favoured-nation treatment principles, the meaning and extent of fair and equitable treatment and full protection and security, the scope of protection against expropriation, especially in relation to regulatory takings, and other possible areas for future interpretation.

The paper concludes by suggesting possible developments in procedural requirements, and in the substantive interpretation of protection standards, from a perspective that seeks to ensure that the position of developing countries, in particular, is taken into account by tribunals when rendering an award. This is of special importance when it is borne in mind that developing countries are, in the main, hosts to foreign investors and their investments and may be particularly vulnerable to the potential adverse effects of investor-State litigation.
INTRODUCTION

International investment policy-making efforts to attract foreign direct investment (FDI) and benefit from it continue to intensify, and international investment agreements (IIAs) at the bilateral, subregional, regional and interregional levels further proliferate. The universe of IIAs consists of over 2,400 bilateral investment treaties (BITs), over 2,600 double taxation treaties (DTTs), numerous preferential free trade and investment agreements (PTIAs), regional economic integration agreements, and other multilateral agreements involving foreign investment.

Within IIAs, specific procedures have been put in place with respect to the settlement of disputes between private parties and the host country arising from investment. The vast majority of BITs, as well as some regional agreements and other instruments, contain provisions on investor-State dispute settlement. The usual approach to investor-State disputes in IIAs is to specify that the parties to a dispute must seek an amicable negotiated settlement. If amicable negotiations fail to resolve a dispute, international arbitration is usually the next step – either on an ad hoc or an institutional basis (UNCTAD, 2003a, 2003b).

The existence of effective dispute-settlement procedures contributes to the creation of a favourable investment climate in the host country. Foreign investors wish to ensure that, in the event of a dispute with the host country, they will have the means of resolving the legal aspects of that dispute expeditiously. Nevertheless, there have been fears about frivolous or vexatious claims that could inhibit legitimate regulatory action by Governments, as well as concerns with regard to balancing national and international methods of dispute settlement (UNCTAD 1998, 2003a, 2003b). In addition, the rather vague language of some treaty provisions (e.g. the “fair and equitable treatment” standard) and the increasing complexity of IIAs can make the outcome of arbitration less predictable.

Although provisions concerning investor-State dispute settlement have been included in IIAs since the 1960s, the use of these
provisions to institute arbitral proceedings has been rare until recently. Since 1987 – when the first investor-State dispute based on bilateral investment treaties (BITs) was recorded under the arbitral proceedings of the International Centre for Settlement of Investment Disputes (ICSID)\textsuperscript{1} – until April 1998, only 14 cases had been brought before ICSID involving BITs, and only two awards and two settlements had been issued (UNCTAD, 1998, p. 140).

However, since the late 1990s, the number of cases has grown enormously. The cumulative number of treaty-based cases had risen to at least 219 by November 2005 (figure 1), with 132 brought before ICSID (including ICSID’s Additional Facility) and 87 before other

**Figure 1. Known investment treaty arbitrations (cumulative and newly instituted cases, by year)**\textsuperscript{a}

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{figure1.png}
\caption{Known investment treaty arbitrations (cumulative and newly instituted cases, by year)\textsuperscript{a}}
\end{figure}

\textit{Source:} UNCTAD.
\textsuperscript{a} As of November 2005.
arbitration forums (figure 2). International investment disputes can also arise from contracts between investors and Governments; a number of such disputes are (or have been) brought under ICSID, other institutional arbitration systems or ad hoc arbitration but are not included in these data, except where there is also a treaty-based claim. More than two thirds (70%) of the 219 known claims were filed within the past three and a half years, with virtually none of them initiated by Governments.2

**Figure 2. Disputes, by rules of arbitration**

![Disputes, by rules of arbitration graph](image)

**Source:** UNCTAD.

*As of November 2005.

SCC = Stockholm Chamber of Commerce; ICC = International Chamber of Commerce.

These figures do not include cases where a party signalled its intention to submit a claim to arbitration, but has not yet actually commenced the arbitration; if these cases are ultimately submitted to arbitration, the number of pending claims will grow further. Some disputes are settled either before an arbitration is launched or after the arbitration procedure has started.3 The total number of treaty-based investment arbitrations is impossible to measure; the figures above are based on extensive research and interviews, but represent only those claims that were disclosed by the parties or arbitral institutions.4 Even
where the existence of a claim has been made public, such as in the case of a claim listed in the ICSID registry, often the information about such a claim is quite minimal. Similarly, from the information on the ICSID database it is not possible to ascertain whether a claim is based on an investment treaty or on a State contract. Under other arbitration rules, the details of a claim and its resolution are likely to become public only if one of the disputants discloses such information. As such, it is significant that 40% of the discovered claims occur under these rules. The actual number of claims instituted under non-ICSID rules is very likely larger than what is known.

The increase in the number of claims can be attributed to several factors. First, increases in international investment flows lead to more occasions for disputes, and more occasions for disputes combined with more IIAs are likely to lead to more cases. Second, with larger numbers of IIAs in place, more investor-State disputes are likely to involve an alleged violation of a treaty provision and more of them are likely to be within the ambit of a dispute settlement provision. Another reason may be the greater complexity of recent IIAs, and the regulatory difficulties in their proper implementation. Furthermore, as news of large, successful claims spreads, more investors may be encouraged to utilize the investor-State dispute resolution mechanism. Greater transparency in arbitration (e.g. within the North American Free Trade Agreement (NAFTA)) may also be a factor in giving greater visibility to this legal avenue of dispute settlement.

At least 61 Governments – 37 of them in the developing world, 14 in developed countries and 10 in South-East Europe and the Commonwealth of Independent States – have faced investment treaty arbitration (annex). Forty-two claims have been lodged against Argentina, 39 of which relate at least in part to that country’s financial crisis. The number of claims against Argentina peaked in 2003 with 20 claims, and dropped to 8 new claims in 2004 and 5 new cases in the first 10 or so months of 2005. Mexico has the second highest number
of known claims (17), most of them falling under NAFTA, and a handful under various BITs. The United States has also faced a sizeable number (11). India (9 claims), the Czech Republic (8), Egypt (8), Poland (7 claims), the Russian Federation (7) and Ecuador (7) also figure prominently, followed by Canada (6) and the Republic of Moldova (5).

In several instances, there have been a multitude of claims lodged in relation to a single investment or against a particular government action. In the Argentine cases, a series of emergency measures and policies have occasioned suits from several dozen companies. In the case of India, the disputed Dabhol Power project led to at least 2 BIT claims by the project companies, as well as 7 BIT claims by the project lenders. All of these claims against India have since been settled. At other times, a single arbitration may have dozens upon dozens of individual claimants, as is the case in a NAFTA arbitration against Mexico by individual investors in tourist real estate, and in the case of a NAFTA arbitration against the United States brought by more than 100 individual claimants in the beef industry.7

Arbitration cases have involved the whole range of investment activities and all kinds of investments, including privatization contracts and State concessions. Measures that have been challenged include emergency laws put in place during a financial crisis, value-added taxes, rezoning of land from agricultural use to commercial use, measures on hazardous waste facilities, issues related to the intent to divest shareholdings of public enterprises to a foreign investor, and treatment at the hands of media regulators. Disputes have involved provisions such as those on fair and equitable treatment, non-discrimination, expropriation, and the scope and definition of agreements. These disputes are yielding awards that interpret the legal obligations of the agreements, and this has caused some parties to re-examine and reconsider the scope and extent of such obligations. The vast majority of claims have been brought under BITs, several of the cases involving also contractual disputes between the State and the
investor. Several recent cases also involve disputes under the Energy Charter Treaty.

This rise in investment disputes poses a particular challenge for developing countries. The financial implications of the investor-State dispute-settlement process can be substantial, from the point of view of both the costs of the arbitration proceedings and the awards rendered. Information about the level of damages being sought by investors tends to be patchy and unreliable. Even ascertaining the amounts sought by foreign investors can be difficult, as most of the cases are still at a preliminary stage and, under the ICSID system, claimants are not obliged to quantify their claims until after the jurisdictional stage has been completed. Claims proceeding under other rules of arbitration are also difficult to quantify. It is, nonetheless, clear that some claims involve large sums (box 1). Furthermore, even defending against claims that may not ultimately be successful costs money. A cursory review of cost decisions in recent awards suggests that the average legal costs incurred by Governments are between $1 million and $2 million, including lawyers’ fees, the costs for the tribunal of about $400,000 or more, and the costs for the claimants, which are about the same as those for the defendant.

An important caveat should be made with regard to the above figures, and hence with regard to the scope of the analysis of this paper. The latter is based only on published NAFTA and ICSID cases (with a few exceptions), and considers only those arbitral decisions (both preliminary and final awards) that are publicly available. Under several arbitration systems, the existence of a dispute and its final decisions are never made public. Even under the ICSID arbitration system, decisions of the tribunals have not all been made public. While this situation is gradually changing, it means that it is not possible to know how much arbitration has actually taken place to date, or what legal issues or factual circumstances they encompassed.
Information about the level of damages being sought by investors tends to be sporadic and unreliable. Even ascertaining the amounts sought by foreign investors can be difficult, as the bulk of cases are still at a preliminary stage and under the ICSID system claimants are not obliged to quantify their claims until after the jurisdictional stage has been completed. Claims proceeding under other rules of arbitration may also not be quantified at an early stage, and even when they are, counsel and investors tend to be reticent about disclosing such information. It is nonetheless clear that some claims involve large sums. Examples include:

- $270 million (plus substantial interest) awarded against the Czech Republic in the Lauder case (award of 3 December 2001);
- $71 million (plus interest) awarded against Ecuador in the Occidental case (award of 1 July 2004);
- $824 million (plus an additional $10 million as a partial contribution to the costs, expenses and counsel's fees) awarded against Slovakia in the CSOB case (award of 29 December 2004);
- $133.2 million (plus interest) awarded against Argentina in the CMS Gas Transmission Company case (award of 15 May 2005).
- $266 million awarded against the Republic of Lebanon, found to be in breach of the France-Lebanon BIT (UNCITRAL award of February 2005). Lebanon has sought to challenge that verdict in the courts of Switzerland, where the arbitration was sited. The arbitral award has not been published by the parties.a
- $133 million awarded against Argentina, found to be in breach of its obligations under contracts and the United States-Argentina BIT (ICSID award of May 2005). In September, Argentina introduced a procedure to annul the tribunal’s award under Article 52 of the ICSID Convention.b
- Recently, a series of three arbitrations were mounted by the majority shareholders in the Yukos Corporation, alleging a violation by the Russian Federation of the Energy Charter Treaty. These claims are for a reported total of $33 billion, which makes them the largest known claims in investment arbitration history.c

/...
Box 1 (continued)

Not all claims lead to the requested awards, however. The amount awarded for a claim is not necessarily an indication of the real financial magnitude of a case, since there are no penalties for claimants filing particularly high claims. Very large claims often end up yielding very small awards. The *Metalclad vs. Mexico* claim for $43 million, for example, led to an award of less than $17 million, and S.D. Myers, in its $70 to $80 million claim against Canada, was awarded $6 million – that is, less than 10% of the amount sought. Nor do all claims brought by businesses succeed. Indeed, a number of cases are won by States. In August 2005, for example, an UNCITRAL tribunal dismissed in its entirety a set of claims by the Canadian-based Methanex Corporation, alleging violations of investment protections in NAFTA. Methanex had claimed some $970 million in damages.

However, even defending against claims costs money. Investment treaty arbitration proceedings are expensive to mount. The Metalclad Corporation is reported to have spent some $4 million on lawyers’ and arbitrators’ fees in an arbitration against Mexico. The Czech Republic reportedly spent $10 million on its defence against two major claims brought by a European-based broadcasting firm and one of its major shareholders (Peterson, 2003). More recently, the Czech Government announced expected legal fees of $3.3 million in 2004, and $13.8 million in 2005, to fight off similar claims (Peterson, 2004). A cursory review of cost decisions in recent awards suggests that the average legal costs incurred by Governments are $1 to $2 million, including lawyers' fees; the costs for the tribunal are about $400,000 or more; and the costs for the claimant are about the same as those for the defendant.

Two recent decisions are noteworthy in as far as the allocation of costs and attorneys' fees by the tribunals is concerned:

* The Methanex tribunal in its decision of 3 August 2005 on the merits awarded the burden of the full costs to the unsuccessful claimant, including the United States' legal costs.
Box 1 (concluded)

* The Annulment Committee, in a recent decision rendered against the Seychelles, decided that all costs of the annulment procedures should be borne by the State that had challenged the first award, seemingly in an attempt to discourage frivolous annulment procedures. The Committee made it clear that an annulment proceeding does not offer a displeased litigant a fresh opportunity to second-guess an ICSID Tribunal's findings.

Source: UNCTAD.


d For the vast majority of the 219 known cases, the outcome is not known – because a decision was never made public or because the cases are still pending. Out of the 41 cases that led to an award that was made public by the time of the writing of this report, 17 cases were won by the State.

e See Thomas (2002). This case was also reviewed by a Canadian court, the cost of which is not included in this figure.


g Preliminary results of a CEPMLP/Dundee research project on economic analysis of transnational dispute management.


i CDC Group plc v. Republic of the Seychelles, ICSID Case No. ARB/02/14, Award of 17 December 2003; Decision on Annulment, 29 June 2005.
However, as a result of the publicly available cases, a growing body of jurisprudence and practice has developed that sheds additional light on the investor-State process itself and on the meaning of certain IIA provisions that have given rise to disputes. Several issues come to the fore that require consideration of the potential consequences of these cases for the interpretation and application of existing agreements and for the negotiation of new agreements, as well as for the broader policy impact.

Accordingly, section I discusses key procedural issues arising from the investor-State arbitration system. In section II, key substantive issues that have been raised in the arbitrations are considered. Each section includes an assessment of the overall implications of existing arbitral decisions, with a specific assessment of the implications of current trends on developing countries. Indeed, while the implications of the investor-State arbitration system, and of specific cases, might apply to all countries, some of the impacts of a number of issues may be more significant for developing countries. Drawing on this analysis, the concluding section provides some ideas for the way ahead, as regards procedural and substantive issues, and as regards the role of the international community.

Notes


2 The sole exception is a 2003 State-to-State dispute between Chile and Peru that was lodged in response to an investor-State claim filed by a Chilean firm, Lucchetti (Lucchetti S.A. and Lucchetti Peru S.A. v. Republic of Peru, ICSID Case No. ARB/03/4). The State-State procedure was discontinued, and the investor-State case was only recently decided.
In other instances, States have set up claims commissions to deal with investor-to-State cases, such as the Iran-United States Claims Tribunal. UNCTAD’s database includes all claims that have been brought to arbitration, including those that were settled after they had been registered. The ICSID facility maintains a public registry of claims; other arbitral mechanisms, however, do not, and this means that no official records of all claims filed are available. Furthermore, in some cases the investors or Governments involved in a dispute wish to keep it confidential, with the result that the disputants themselves may not reveal the existence of a claim.

The worldwide inward FDI stock tripled between 1995 and 2004 (from $2.8 trillion at the end of 1995 to $8.9 trillion at the end of 2004) (see www.unctad.org/wir).

The universe of IIAs has grown considerably over the past decade. At the end of 2004, it consisted of 2,392 bilateral treaties for the promotion and protection of investment (or bilateral investment treaties/BITs) (compared with 1,097 BITs at the end of 1995), 2,559 treaties for the avoidance of double taxation (or double taxation treaties/DTTs) (1,663 in 1995), and some 215 other bilateral and regional trade and investment agreements as well as various multilateral agreements that contain a commitment to liberalize, protect and/or promote investment (77 in 1995) (see www.unctad.org/iia).

In UNCTAD’s database, the beef cases against the United States are counted as one case, rather than 100, following the United States’ practice on its website. Furthermore, all of these cases pertain to the same facts and the same treaty. By contrast, the 7 Dabhol banks cases are counted as individual cases, because they pertain to the same facts, but different investment treaties.

All reviewed cases are identified in annex 2.
I. KEY PROCEDURAL ISSUES

In this section, a range of specific legal issues relating to the jurisdiction and procedures of investor-State dispute settlement and their implications for the system are considered.

A. Definition of “investor” and “investment”

One of the first issues relates to the definition of the investor entitled to use the investor-State dispute settlement procedures. In Chapter 11 of NAFTA, an “investor” can initiate the claim on behalf of the “investment” (i.e. the company established in the host country) or on its own behalf as an injured investor (Articles 1116-1117). In many other instances, the investment may also initiate the arbitration directly. This approach has been followed in BIT arbitrations to date as well, and it is quite reasonable if the objectives of protection of the investor are to be met. Accordingly, the issue of how to read the definition of who may qualify as an investor is complex.

The concept of “investor” in the context of BITs and NAFTA has a broad scope. Consequently, foreign investors that are shareholders in an investment have been allowed to use the investor-State dispute settlement procedures, and the protections in the agreement, irrespective of whether they are majority or minority shareholders. Most IIAs regard shareholdings or participation in a company as a form of investment. Therefore, minority shareholders are entitled to submit claims in respect of their investment. In these cases, investors have standing not because they control the enterprise but because their shares constitute the investment. In one case, the shareholding amounted to 17 per cent of the investment in the host country.¹ No case to date is known that sets a lower limit on the value of a shareholding that would allow the investor-State dispute settlement procedures to be used, where such a requirement is not set out in the text of the treaty itself. In addition, shareholdings through indirectly owned and controlled subsidiaries can also give standing to the ultimate shareholder before a tribunal to bring a claim arising out of the terms of a BIT.²
The above issue should be distinguished from the issue of whether the enterprise bringing the claim is to be regarded as a foreign investor because it is under foreign control. This is of particular importance where the claim arises out of the treatment accorded to a locally incorporated affiliate of the foreign parent. Under traditional rules of diplomatic protection, the local affiliate would have the nationality of the host country, the respondent State, and so would not be entitled to protection from the home country of the parent by reason of its host country nationality. Under the ICSID Convention this potential barrier to effective dispute resolution is avoided by reason of Article 25(2)(b) of the Convention, which allows for the treatment of a local affiliate as a foreign investor where it is agreed by the parties to the dispute that it is under foreign control and that it is in fact under such control.  

As to the definition of an “investment”, apart from the case where the investor establishes a presence in the host country through an affiliate, other kinds of activities have been considered to come within this term. For example, many BITs operate with a broad asset-based definition of investment that allows portfolio investments to be covered, although there are instances where treaty coverage is expressly limited to FDI only. In addition, an investment may be constituted by a mere sales presence. A good example of this arises in the S.D. Myers v. Canada case under Chapter 11 of NAFTA. It was held that an office established in Canada by a waste management service provider from the United States to sell export services to the United States from Canada was covered as an investment in Canada. The establishment of a sales office and the commitment of marketing time were held to constitute a sufficient investment. In this case and others, market share through trade has been regarded as part of the assets of an investment, and this therefore supports the view that the operation of a sales office is sufficient to constitute an investment. Furthermore, promissory notes and other banking instruments may be considered to be investments, as have been loan agreements and construction contracts, and the setting up of a law firm.
B. Multiplicity of forums

Related to the question of who and what qualify as “investor” and “investment” respectively is the issue of multiple cases for one set of facts. Indeed, there are some instances where it has been accepted that the same facts and circumstances can be litigated by different investors in different tribunals, even when different results emerge. This could lead to situations where investors, having shares in the same investment, initiate multiple arbitrations under different corporate or personal investor names. An example of multiple proceedings on the same facts leading to opposite results are the Lauder cases, where two different investors initiated arbitrations under different BITs in different forums against the Czech Government for alleged improper interference with their investments in the television business. One investor lost its case, but the other won an award of over $300 million from the Czech Republic. The two tribunals involved held that parallel proceedings relating to the same facts were admissible on the ground that, nominally, the parties and the two BITs involved were different.

There is therefore a risk of lack of finality and the possibility that host countries could lose several times and be subject to multiple awards. While this is a risk for all host countries, the burden of such an outcome could fall more heavily upon developing countries. In addition, any cases leading to significant awards against a developing host country may require the diversion of much-needed financial resources from other areas.

This problem of multiple proceedings for the same facts was foreseen in the context of NAFTA’s Chapter 11, where a facility for the tribunals to consolidate cases based on the same set of facts was first articulated (Articles 1126 and 1117.3).

The year 2005 saw efforts towards consolidation in major NAFTA cases. At the request of the United States, three softwood lumber cases – 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 – were consolidated. On the other hand, Mexico requested the establishment of a tribunal to consider the consolidation of three claims, all concerning an excise tax on certain soft drinks. The Consolidation Tribunal in its order of May 2005, however, decided against the consolidation on grounds that the United States-based companies involved were in direct and major competition.

However, the absence, in most treaties, of any provisions on consolidating cases based on the same circumstances may inhibit this procedure under existing BITs without the express consent of all the parties involved. That said, the risks of multiple awards should not be overstated. The outcome of the CME and Lauder cases against the Czech Republic might have been a rare occurrence that was due, to a large extent, to the unwillingness of the Czech Republic to accept the consolidation of the cases, a course of action that had been proposed on several occasions. In these circumstances, it may be said that the likelihood of similar multiple actions and awards arising in the future is relatively small, provided that all parties agree to consolidation where required. In addition, it would not be difficult to draft an appropriate clause in an IIA that requires the dispute settlement body to treat an issue as res judicata where, on the basis of the facts to hand, the arbitral tribunal concludes that the issue in question has already been adjudicated in a claim brought by another shareholder.

C. Conflict of jurisdictions

A further potential risk arising out of investment dispute settlement systems in IIAs concerns the possibility of initiating international dispute settlement mechanisms at the instigation of the investor despite the existence of a “domestic forum” clause in the investment contract between the investor and the host country. Such a clause may specify that disputes arising out of breaches of the investment contract shall be settled under domestic dispute-settlement systems. Where the breach of such a contract is at issue, some recent
ICSID tribunals have held that the requirement – established in the “domestic forum” clause – to pursue breach of contract claims in domestic dispute-settlement procedures does not prevent the use of the investor-State dispute-settlement mechanism of an IIA. This is so even where the alleged breach of contract on the part of the respondent host country is central to the establishment of a breach of the investment protection obligations in the treaty.12

The rationale behind these cases is that “domestic forum” clauses relate to breaches of the contract only, while the investor-State claim relates to breaches of the treaty itself as a separate international law obligation. Accordingly, such a clause should not stand in the way of a legitimate claim, at the international level, of a breach of an international obligation. This can be viewed as a potential disadvantage to the host country, in that it may remove what appears to be a purely contractual dispute from the proper domestic forum for its resolution. On the other hand, it is equally plausible to argue that, should the “domestic forum” clause have the effect of prohibiting any international challenge to the host country’s actions, the protective purpose of the IIA would be neutralized, to the considerable disadvantage of the investor. It is this possibility that has motivated recent ICSID tribunals to take the above-mentioned position on the actual scope of such clauses.

One important issue in this context relates to the so-called umbrella clause. This clause establishes an IIA obligation to respect all the commitments or obligations entered into in contracts or other forms of agreements between an investor, investment and the host country. The effect of this provision is that breaches of investment contracts amount to a violation of the applicable IIA. However, the case law on such provisions is not uniform and has given rise to some uncertainty as to the precise scope of such clauses.13 On the other hand, umbrella clauses arise out of a number of historical precedents that make it clear that their object and purpose is to extend the protection of the IIA itself to the determination of disputes over the alleged breach of an
investment contract by the host country (Sinclair, 2004). Accordingly, such an interpretation of the umbrella clause by international arbitral tribunals appears to be consistent with its main objective.

In recent decisions, tribunals have in general followed a broad approach on the umbrella effect of treaties. However, in an April 2005 decision (Impregilo S.p.A. v. Islamic Republic of Pakistan), the tribunal limited its treaty jurisdiction over contractual claims to claims involving the State itself and not State-owned entities. In the recent case Consortium Groupement L.E.S.I. - DIPENTA v. Algeria, the tribunal emphasized the requirement that contractual claims brought before a treaty-based tribunal must also amount to a violation of the treaty standards themselves.

In the absence of clear umbrella provisions, a breach of contract by the host country may serve as another basis for investor claims. Such claims have not usually been handled directly by investor-State arbitrations. Rather, the facts and resulting findings for a potential breach of contract have been examined under the aspect of compliance with one of the “standard” obligations in a BIT. Thus, breach-of-contract issues have generally been raised as part of the background to an expropriation, national treatment or fair and equitable treatment claim.

Concerns may also arise in relation to the so-called fork-in-the-road provisions in IIAs. These “choice of forum” clauses require foreign investors to choose either a domestic or an international dispute settlement forum when a dispute arises. Such clauses are specifically intended to prevent multiple forums for one set of facts. However, fork-in-the-road provisions may not exclude the risk of having a shareholder initiate an arbitration to protect its BIT rights, while the investment (i.e. the subsidiary) initiates a domestic dispute to protect its contract or other legal rights, including those stemming from the IIA. In the face of such facts, several arbitral decisions have interpreted the “fork-in-the-road” provision as resulting in a loss of access to
international arbitration only where the dispute and the parties before the domestic courts or administrative tribunals are identical to the dispute and the parties in the international proceeding.16

In arriving at this conclusion the ICSID Tribunals may have had in mind the fact that a foreign investor may be unable to avoid being drawn into local proceedings concerning the investment. The domestic law of the host country may require a defensive approach to be taken by the investor, such as the lodging of an appeal against a regulatory ruling, or the initiation of a legal challenge to an administrative decision where time limits for action are short. In these circumstances, it may be difficult to characterize the action of the investor as a “free” choice of forum that negates the possibility of any action at the international level for breach of an IIA obligation on the part of the host country. To do so could render the protection of the relevant agreement nugatory. Indeed, the outcome of the domestic process may itself give rise to possible further claims under the IIA. A literal and absolute approach to apparent forum choices by the investor could create injustice. Thus, the exclusion of international proceedings under the “fork in the road” clause only in cases of full identity of issues and parties with domestic proceedings appears to be consistent with the protective purpose of IIAs.

D. Treaty shopping

Another factor of concern is the possibility of “shopping” by foreign investors for a “home country of convenience” – that is, the seeking of home countries that have treaties with host countries where investments are to be made. The potential for such treaty shopping was recognized in the drafting of Chapter 11 of NAFTA, which includes a provision allowing a party to deny the benefits of the agreement to investors that have no “substantial business activities” in their putative home country (article 1113.2). Similar clauses can be found in BITs (e.g. in United States BITs and a number of ASEAN country BITs), reflecting the intent of the agreements to protect only bona fide
transnational investments between the home country and the host country. The absence of such a “denial of benefits” provision may allow virtually any type of home country linkage to be sufficient to allow a claim to proceed.

In principle, therefore, a contracting party to a BIT, or other IIA, may expressly guard itself against “treaty shopping”. Conversely, this party may permit the benefit of the IIA to pass, on the basis of a share transfer, from a holding company in a non-contracting party to one located in a contracting party by expressly accepting such a change. On the other hand, the party in question could, in view of the underlying economic reality of the case, insist that the nationality of the directors, or the effective location of ultimate control, determine whether the benefit of the IIA should extend to the investor and its investment. This conclusion can be drawn from the ICSID Tribunal decision in the Autopista case. This case allowed the application of the ICSID Convention to an investment where the original investors from Mexico, which has no BIT with the host country, Venezuela, transferred their shares to an affiliate in the United States, which does have such a BIT. This decision was influenced by the fact that Venezuela had the opportunity to review and reject this share transfer but chose to accept it. Thus, much of the responsibility for controlling “treaty shopping” is assigned to the host country. It must decide whether to take a liberal or a strict approach to such cases.

E. Transparency

Under several arbitration systems the existence of a dispute, its documents and pleadings, and often its decisions, are not made public. This situation is due to the fact that the investor-State dispute settlement system is based on international commercial arbitration, which came into existence as a tool for the settling of international commercial disputes between private parties, mainly on technical legal grounds not involving public policy issues. While confidentiality in private disputes is warranted, this may not be the case when arbitral tribunals rule on
matters of broad public concern that can arise out of the regulation of a major investment project by host countries.

In the light of this situation, there have been efforts in recent years to increase the transparency of investor-State disputes. Thus, ICSID has produced a web-based list of its past and current cases, and a party to ICSID proceedings has always had the right to release awards and other decisions into the public domain unilaterally unless there was an agreement between the parties to the contrary. The ICSID Secretariat has had the authority to publish significant extracts of decisions since 1984 where the parties do not agree to publish an award. The recent proposals for the review of ICSID procedures suggest that although “the Centre shall not publish the award without the consent of the parties, the Centre shall, however, promptly include in its publications excerpts of the legal reasoning of the Tribunal (Amendment to Arbitration Rule 48, ICSID, 2005).

The most advanced application of transparency principles is found in NAFTA’s Chapter 11. It mandates public notification of the filing of disputes, and its arbitration process has become increasingly open over the past several years. In line with the interpretative statement of the NAFTA Free Trade Commission, the websites of the three NAFTA parties now provide routine access to notices of arbitration, claims and counterclaims, memorials, procedural decisions and substantive decisions and awards. All hearings in the Methanex v. United States case were open to the public. The United States has gone beyond this approach in its Free Trade Agreement negotiating model by providing for hearings open to the public and has already applied it in the United States-Singapore and United States-Chile Free Trade Agreement Chapters on Investment, as well as in the United States-Uruguay BIT. Canada has set out similar provisions in its revised model BIT.

These developments may contribute to a culture where transparency, and public access to and broader public understanding of
investor-State dispute settlement will become the norm rather than the exception.

**F. Implications**

The procedural issues addressed above have given rise to a number of concerns with regard to the proper functioning and overall legitimacy of the investor-State dispute settlement. First, there is continuing debate over whether it is appropriate to use international arbitration as a means of dispute settlement that may rule on public policy issues without having the same levels of safeguards for accountability and transparency as are typically required for domestic juridical systems. Second, the investor-State dispute settlement system is usually exclusively available to foreign investors, and, to the extent that the relief available under this method may not exist under domestic procedures, this may be said to put domestic firms at a disadvantage. Much here depends on the existence of analogous domestic remedies. Third, there is a risk that tribunals will not decide “like cases” in a like manner, since there is no obligation for them to do so. Hence, not only developing countries, but also developed countries may view the process of international dispute settlement in this field with some concern, especially when it comes to deciding on matters of national and international public policy (UNCTAD, 2003a, p. 6).

Developing countries will continue to be mainly capital-importing countries. They are therefore likely to bear the brunt of a potential increase in investor-State dispute settlement cases. This creates a financial concern for these countries as the costs of the cases can be significant when the tribunal’s costs, arbitrator fees, fees and disbursements by lawyers, as well as the time involved in preparing the cases, are all accounted for. Developed countries have a greater capacity in most cases to afford and manage increases in international proceedings, although, here too, the costs may be considerable.
In addition, the recent situation of Argentina shows the existence of a risk that developing countries may be subject to extensive use of investor-State arbitrations as the result of a major economic crisis. Developing countries may have fewer options available to respond to financial or political crises than developed countries. If each such event can trigger dozens of international arbitrations, this could create a major problem for such countries. On the other hand, such cases may be the result of policy misjudgements on the part of host countries, the effect of which is to undermine the expected profitability and value of a foreign investment. In such circumstances, recourse to investor-State dispute settlement mechanisms may be understandable, especially where a satisfactory out-of-court settlement of any claims on the part of the foreign investor has proved to be elusive. Even then, it is not at all certain that the investor will always have a strong case. Much depends on the surrounding facts and issues, on the degree of knowledge that the investor possesses of the prevailing economic and political conditions in the host country, and on the degree of speculative risk freely undertaken by the investor.23

Of course, there can also be potential positive impacts of the increase in arbitrations. Perhaps the most identifiable one would be an increase in confidence with regard to investing in developing countries that comply with their IIA obligations directly or pursuant to arbitration decisions. The sense that developing countries are “playing by the rules of the game” that is created by entry into the agreements in the first place could be enhanced. There is also the possibility that the experience with initial investor-State cases will motivate developing host countries to improve domestic administrative practices in order to avoid future cases. This would raise important capacity and capacity-building questions. Some recommendations in this regard appear in the conclusions.
Notes

1 CMS Gas Transmission Company v. Argentine Republic, ICSID Case No ARB/01/8, Decision on Jurisdiction, 17 July 2003 (United States/Argentina BIT), where the distinction between a minority shareholder, with rights to initiate an arbitration, and the controlling shareholder, or the investment, is seen as increasingly accepted under international law. See also Lanco International Inc. v. Argentine Republic, ICSID Case No. ARB/97/6, Decision on Jurisdiction, 8 December 1998 (United States/Argentina BIT), where a 17 per cent shareholding was sufficient to be considered an investment. This is also seen in the series of Lauder arbitration cases (see below).

2 Azurix Corp. v. Argentine Republic, ICSID Case No. ARB/01/12, Decision on Jurisdiction, 8 December 2003 (United States/Argentina BIT).

3 See, for example, the Vacuum Salt award (Vacuum Salt Products Limited v. Ghana, ICSID Case No ARB/92/1, Award, 16 February 1994). Here, the Tribunal considered, in all the circumstances of the case, that an enterprise with a 20 per cent foreign shareholding was a national enterprise of the respondent State and so not entitled to bring a claim. It stressed that ”foreign control...does not require, or imply, any particular percentage of share ownership. Each case arising under [ICSID Convention Art. 25.2.b] must be viewed in its own particular context, on the basis of all facts and circumstances. There is no 'formula'. It stands to reason, of course, that 100 per cent foreign ownership almost certainly would result in foreign control, by whatever standard, and that a total absence of foreign shareholding would virtually preclude the existence of such control. How much is 'enough', however, cannot be determined abstractly...” (para. 43)). See, in this context, also Tokois Tokelés v. Ukraine, ICSID Case No. ARB/02/18, Decision on Jurisdiction, 29 April 2004; Dissenting Opinion, 29 April 2004 (Lithuania/Ukraine BIT).

4 S.D. Myers, Inc. v. Canada, UNCITRAL, First Partial Award, 13 November 2000 (NAFTA).

5 For example, Pope & Talbot, Inc. v. The Government of Canada, UNCITRAL, Interim Award on Merits, 26 June 2000; Award on Merits, 10 April 2001, Award on Damages, 31 May 2002; Award on Costs, 26 November 2002 (NAFTA); Award on Merits, paragraphs 96-98; S.D. Myers v. Canada, op. cit. See also separate opinion by Schwartz in S.D. Myers on this point, paragraphs 45-46.
See, for example, NAFTA Article 1139 for an IIA textual reference to the broad meaning of an investment. Tribunal decisions under a BIT are seen in *FEDAX N.V. v Republic of Venezuela*, ICSID Case No. ARB/96/3(1), Decision on Jurisdiction, 11 July 1997, and Final Award, 9 March 1998 (The Netherlands/Venezuela BIT); *Československá Obchodní Banka v. The Slovak Republic*, ICSID Case No. ARB/97/4, Second Award on Jurisdiction, 1 December 2000 (Czech Republic/Slovak Republic BIT); *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Jordan*, ICSID Case No. ARB/02/13, Decision on Jurisdiction, 9 November 2004 (Italy/Jordan BIT); and *Autopista Concesionada de Venezuela v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/00/5, Decision on Jurisdiction, 27 September 2001, and Final Award, 27 September 2003. For a recent restrictive decision on the concept of investment see *Joy Mining Machinery Limited v. Egypt*, ICSID Case No. ARB/03/11, Decision on Jurisdiction, 6 August 2004 (United Kingdom/Egypt BIT).


See, for example, the express recognition of this in *CMS Gas Transmission Company v. Argentine Republic*, op. cit., paragraph 86.


The risk of multiple international arbitrations has led some arbitrators to note that this situation has the potential to bring the arbitration system into disrepute. See Brower (2002, B.9).


*Alex Genin, Eastern Credit Limited v. Republic of Estonia*, ICSID Case No. ARB/99/2, Award, 25 June 2001 (United States/Estonia BIT); *CMS Gas Transmission Company v. Argentine Republic*, op. cit.; *Compañía de
In several cases, tribunals have looked into the issue of the application of an umbrella clause. This began with two cases concerning one investor (Société Générale de Surveillance, SGS), but the judgements were rendered under different BITs by different arbitral tribunals and led to contradictory results. In *SGS v. Pakistan* (*SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13, Decision on Jurisdiction, 6 August 2003 (Swiss Confederation/Pakistan BIT)), the tribunal held that the umbrella clause does not mean that breaches of contract are automatically "elevated" to the level of breaches of international treaty law. By contrast, in *SGS v. Philippines* (*SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6, Decision on Jurisdiction, 29 January 2004 (Swiss Confederation/Republic of the Philippines BIT)), the award having been made half a year later than *SGS v. Pakistan*, the tribunal expressly disagreed with the analysis of the latter and held that, by virtue of the umbrella clause, the failure of the host State to observe binding contractual commitments made it a breach of the BIT. This issue is the subject of some debate today. For a detailed analysis of these awards in the context of the "umbrella clause" issue, see Schreuer (2004) and Waelde (2005). Further cases are *Noble Ventures v. Romania* (Case No. ARB/01/11), *Eureko B.V. v. Poland*, (Partial award), *Joy Mining v. Egypt* (ICSID Case No. ARB/03/11, Decision on Jurisdiction, 6 August 2004), and *Sempra Energy Int. v. Argentina* (ICSID Case No. ARB/02/16).

13 For a detailed analysis of these awards in the context of the "umbrella clause" issue, see Schreuer (2004) and Waelde (2005). Further cases are *Noble Ventures v. Romania* (Case No. ARB/01/11), *Eureko B.V. v. Poland*, (Partial award), *Joy Mining v. Egypt* (ICSID Case No. ARB/03/11, Decision on Jurisdiction, 6 August 2004), and *Sempra Energy Int. v. Argentina* (ICSID Case No. ARB/02/16).

14 Decision on Jurisdiction, 22 April 2005 (ICSID Case No. ARB/02/2).

15 Decision on Jurisdiction, 10 August 2005 (ICSID Case No. ARB/03/8).

16 See *Compañía de Aguas del Aconcagua & Vivendi Universal* (formerly *Compagnie Générale des Eaux*) v. *Argentina Republic*, Decision on Annulment, op. cit. An example of multiple cases by different investors
and the investment is also *Alex Genin, Eastern Credit Limited v. Republic of Estonia*, op. cit., paragraphs 331-333; see also *Ronald Lauder vs. Czech Republic*, op. cit., paragraph 163; *Enron and Ponderosa Assets v. Argentine Republic*, ICSID Case No. ARB/01/3, Decision on Jurisdiction, 14 January 2004 (United States/Argentina BIT), paragraph 98; *Azurix Corp. v. Argentine Republic*, op. cit., paragraph 90; and *CMS Gas Transmission Company v. Argentine Republic*, op. cit., paragraph 80. For a detailed analysis of the ”fork in the road” clause, see Schreuer (2004).


21 See Article 10.21.2 of the Central America-Dominican Republic-United States Free Trade Agreement (DR-CAFTA). This Agreement was concluded in 2004, but has not yet been ratified by all parties. For the Singapore-United States Free Trade Agreement, see http://www.ustr.gov/new/fta/Singapore/final.htm, Chapter 15; for the Chile-United States Free Trade Agreement, see http://www.ustr.gov/new/fta/Chile/final/index.htm, Chapter 10; and for the Uruguay-United States BIT, see http://www.ustr.gov/assets/World_Regions/Americas/SouthAmerica/assetuploadfile4406728.pdf. Note that the United States-Chile and the United States-Singapore FTAs are in force; the United States-Uruguay BIT is not yet in force.
This was explicitly recognized by the tribunal in a recent case: the tribunal stated that “although different tribunals constituted under the ICSID system should in general seek to act consistently with each other, in the end it must be for each tribunal to exercise its competence in accordance with the applicable law, which will by definition be different for each BIT and each respondent State” (SGS Société Générale de Surveillance S.A. v. Republic of the Philippines, Decision on Jurisdiction, op. cit., paragraph 97).

See Eudoro Armando Olguín v. Republic of Paraguay, ICSID Case No. ARB/98/5, Award on Jurisdiction, 8 August 2000; Final Award, 26 July 2001 (Peru/Paraguay BIT).
II. KEY SUBSTANTIVE ISSUES

In this section, the main substantive legal grounds for decisions in the cases under review are considered. These are highly important as authoritative interpretations of the substantive obligations contained in IIA provisions. Indeed, the decisions of tribunals are a subsidiary means for the determination of rules of international law. In addition, IIAs are dynamic instruments that evolve over time to meet the needs of both investor/investment protection and the scope of host country rights of regulation, especially in the context of the development needs of countries. In these circumstances, a major task of international tribunals is to strike a balance between these concerns in the interpretation of IIA provisions. Whether existing decisions have done this is a source of controversy among various interested parties. On the other hand, certain trends of reasoning can be discerned on major issues. Accordingly, this part of the paper will identify such trends, where they exist, and consider their impact on the balance of rights and obligations of investors and host countries in the light of development concerns.

A. Right of establishment

Pre-establishment rights extend certain treaty protections to the stage when an investor is attempting to make or is making its investment in the host country (UNCTAD, 1999b, 1999c). To date, apart from United States and Canadian BITs, few such agreements grant rights of establishment, although this is becoming a more common element in other IIAs, notably in bilateral and regional free trade agreements with investment provisions or chapters. As most BITs do not include pre-establishment rights, this has not been the focus of many ICSID decisions. At the time of writing, only one case, Mihaly International Corporation v. Sri Lanka, has addressed the issue.¹ In this case, the question arose as to whether pre-investment expenditure on the part of the United States-based claimant amounted to an “investment” under the ICSID Convention that could therefore be protected under the pre-establishment provisions of the United States-Sri Lanka BIT. The tribunal held that the claimant had failed to show that such expenditure amounted to an investment in the absence of
evidence of the admission of the planned investment.\textsuperscript{2} This case leaves open the possibility that, once an investment has been admitted, such pre-investment expenditure may be protected under a BIT that extends to the pre-establishment phase.

NAFTA, and NAFTA-type agreements such as the Japan-Singapore FTA, provide for the application of national treatment to the pre-establishment phase subject to country-specific exceptions.\textsuperscript{3} Such exceptions can permit for the exclusion of certain sectors and industries from pre-establishment obligations. This “negative list” approach to exceptions can be contrasted with a “positive list” approach, such as that adopted under the market access provisions of the GATS, which extend pre-establishment protection only to sectors or industries specifically included in the schedule of commitments of a host country party to the IIA in question. Thus, IIA provisions themselves set limits on the extent of liberalization and protection that the pre-establishment provisions of an IIA can provide. An example is the Canadian model Foreign Investment Promotion and Protection Agreement (Annex IV), which excludes from dispute settlement a decision by the Canadian authorities as regards an acquisition of a domestic company.

B. National treatment

One of the main expectations arising from an investment agreement is that foreign investors will not be subject to discriminatory treatment by the host country, including through legal, administrative or other decision-making. The principle of non-discrimination is usually formulated in a provision on national treatment that requires treatment “no less favourable” than that provided to domestic investors “in like circumstances”. The scope of a national treatment obligation spans the establishment, operational and winding-up stages of an investment, and, as noted earlier, in a number of IIAs it also encompasses the pre-establishment phase of the investment (UNCTAD, 1999c).
The key to the national treatment issue is the comparison with the treatment received by domestic investors in “like” or “similar” circumstances. The scope of the analysis is not limited to de jure legal or administrative discrimination, but encompasses treatment that appears to be discriminatory in fact or to lead to discriminatory impacts, namely de facto discrimination. For example, in the case of Marvin Roy Feldman v. The United Mexican States the tribunal accepted that the national treatment principle was intended to protect against discrimination because of the foreign status of the investor. However, it also stated that there is no requirement to show that a breach of national treatment was expressly due to the investor’s nationality. Rather, the de facto difference in treatment could stand on its own, “at least in the absence of any evidence to the contrary”. In other words, de facto differences in treatment were sufficient to create a presumption of discrimination. Similarly, in S.D. Myers v. Canada, the tribunal took the view that:

“in assessing whether a measure is contrary to a national treatment norm, the following factors should be taken into account:

* Whether the practical effect of the measure is to create a disproportionate benefit for nationals over non-nationals;
* Whether the measure, on its face, appears to favour its nationals over non-nationals who are protected by the relevant treaty” (para. 252).

Interpretation of national treatment provisions also requires a determination of which entities or activities serve as the reference point for ascertaining the type of treatment to be given. Here, the concept of “like” circumstances – which is often mentioned explicitly in IIAs – becomes an important premise of the application of the national treatment standard. However, national treatment provisions typically do not identify the criteria by which similarity or likeness is to be established. The issue has arisen in a number of investment disputes. In
S.D. Myers v. Canada, for example, the tribunal focused on whether the domestic and foreign businesses in question were in commercially competitive sectors. Thus, while the Myers investment was in a sales office seeking to export PCB wastes, and the domestic comparison group was actual PCB waste disposal facilities, they were found to be in like circumstances as one could take away business from the other.\(^6\) It must be noted, however, that the Myers decision likewise states “[that] the assessment of like circumstances must also take into account circumstances that would justify governmental regulations that treat them differently in order to protect the public interest”.\(^7\) This view is repeated in the subsequent NAFTA decision in Pope & Talbot, Inc. v. The Government of Canada.\(^8\)

In sum, the standard for the national treatment obligation in its interpretation by arbitral tribunals remains open to further refinement. The cases reviewed have accepted a standard of both de jure and de facto discrimination based on a case-by-case analysis of the impact a measure has on a foreign investor. This allows for an examination not only of measures that clearly show difference of treatment between foreign and domestic investors that is favourable to the latter, but also of measures that are, on their face, non-discriminatory but have the effect of according less favourable treatment to foreign as compared with domestic investors in like circumstances. The Methanex tribunal has recently looked into the precise scope of the term ”like circumstances”.\(^9\) It took a narrow approach to the requirement “in like circumstances” by asking whether the activities of the foreign investor were comparable to economic activities in the domestic sphere, rather than the broad approach used in S.D. Myers and drawing upon the precedents in the area of international trade. Thus, there is currently no uniform interpretation of the “in like circumstances” requirement.

C. Most-favoured-nation treatment

As a second component of non-discrimination, IIAs typically include a requirement that a foreign investor be accorded the highest
standard of treatment available to an investor from any other foreign country, also known as most-favoured-nation (MFN) treatment.

Until recently, this standard was thought to be less important than the principle of national treatment from a litigation perspective. Today, however, it is the subject of some controversy as to whether it can be used to broaden the scope of an investor’s procedural and substantive rights beyond those in the agreement under which it claims protection and which contains an MFN clause.

The issue arose following the arbitration in Maffezini v. Spain, although it was actually not the first to face this issue. In Maffezini, the Argentine investor in Spain was allowed to use a more beneficial time requirement in the arbitration process found in the Chile-Spain BIT (as opposed to the Argentina-Spain BIT under which the claim was filed). The tribunal accepted this as an application of the MFN principle, subject to the limitation that it did not override public policy considerations of the parties to the negotiations. On this basis, the more favourable procedural treatment was applied.

Since Maffezini there have been a further three major cases dealing with the applicability of the MFN standard to dispute settlement before ICSID (Salini, Siemens and Plama). While Maffezini and Siemens favour the application of MFN status to dispute settlement, Salini and Plama say, at least in principle, the opposite, focusing on the intention of the parties as the decisive factor. In this view, only where the parties to the BIT have a clear and unambiguous intention of incorporating – by the operation of the MFN clause – dispute settlement provisions from other treaties will this be possible.

Although primarily concerned with the applicability of the MFN provision to dispute settlement, the Maffezini case has also raised questions as to whether substantive protections that are greater in a BIT with another country can now be relied upon in any BIT arbitration by any foreign investor. The trend regarding this issue is becoming more
restrictive. This is due to the extended application of the condition noted above in the *Maffezini* case to ensure that any third-party provision should not be of such a nature as to impact on the underlying “bargain” in the BIT that is the basis of the claim. As a result, recent cases have limited the possible application of such third-party treaties to situations where the additional rights do not impact on the balance of rights in a significant way so as to “go to the core of matters that must be specifically negotiated by the contracting parties”. While it is difficult to determine with precision when such a test has been met, it does display a greater degree of restraint than originally feared in the immediate aftermath of the *Maffezini* decision.

However, a recent decision by an ICSID tribunal in the *MTD Equity Bhd v. Chile* case has suggested a broader notion in this regard. The tribunal considered that “the fair and equitable standard of treatment has to be interpreted in the manner most conducive to fulfill the objective of the BIT to protect investment and create conditions favorable to investments”. Consequently, obligations “that can be construed to be part of the fair and equitable treatment of investors” found in other investment agreements “would be covered by the [MFN] clause”. Accordingly, the tribunal felt that the inclusion of standards found in other BITs concluded by Chile with third countries was “commensurate with this purpose”. The tribunal justified this reasoning by pointing to the fact that the Contracting Parties found it prudent to exclude, from the coverage of the MFN clause, matters relating to tax treatment and regional cooperation, matters that were alien to the BIT. On the other hand, matters falling within the coverage of a BIT were not excluded and so could be considered under the MFN clause. This approach can certainly broaden the coverage of a BIT. However, the tribunal required that the provision relied on in a BIT with a third country fall within the ambit of the fair and equitable treatment standard. Thus, only those provisions that are specifically relevant to the clarification of obligations under the BIT containing the MFN clause may be considered.
D. Fair and equitable treatment and full protection and security

One of the most debated issues in arbitral disputes under investment agreements is the meaning of the standards of “fair and equitable treatment” and “full protection and security” (UNCTAD, 1999d). The fair and equitable treatment standard has been applied in BITs and NAFTA cases. Indeed, this standard has recently emerged as a significant ground for a finding of breaches of the investment agreement by the host country. Among the circumstances where this standard has been applied to find a violation of host country obligations are the following:

- The non-renewal of a land-fill operations licence in Mexico;\textsuperscript{18}
- The requirement to produce what was termed as “excessive documentation” for export permits in the forestry sector in Canada;\textsuperscript{19}
- The improper transfer by a government official of funds from a private bank account in Spain;\textsuperscript{20}
- The failure to give full notice directly to a shipowner regarding the impending seizure of a ship (notice was placed on the ship, however).\textsuperscript{21}

In addition, the breach of the “legitimate expectations” of an investor has emerged as an element in assessing the scope of factors and issues to be weighed in a decision on the fair and equitable treatment standard.\textsuperscript{22}

The standard originated in customary international law on the protection of the property of aliens. This origin is recognized in key BITs and NAFTA cases. The threshold for this standard was articulated in \textit{S.D. Myers v. Canada}, where the tribunal held that a breach of the fair and equitable treatment standard, in Article 1105 of NAFTA, “occurs only when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective”.\textsuperscript{23} This determination
was subject to two considerations. First, it had to be made in the light of the large measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders; and, second, it had to take into account any specific rules of international law that were applicable to the case. This approach was supported in the judicial review of the *Metalclad* decision. A similar approach was taken in *Genin v. Estonia*, a case that followed the privatization of a bank in Estonia. The tribunal defined fair and equitable treatment to include “acts showing a willful neglect of duty, an extreme insufficiency of action falling far below international standards, subjective bad faith, or a willful disregard of due process.”

Other arbitrations under both NAFTA and BITs have further considered the implications of this standard. For example, in *Pope & Talbot, Inc. v. The Government of Canada*, it was held that the standard applies to conduct that requires a failure of due process that surprises the observer, a standard that would be more “rigorous for evaluating what governments do to people and companies”. This was applied to reach a finding against Canada for what was seen as overly aggressive use of administrative powers to gather information on the export levels of the company's forest products, the subject matter of the arbitration. In the *Mondev v. United States* case, concerning property transactions in Boston between a Canadian developer and the city of Boston, the tribunal noted two further key elements in relation to fair and equitable treatment, in the context of a challenge against the treatment received by the investor before the local courts. First, the standard is intended to provide a level of real protection to investors and it is evolutionary in character. Second, a tribunal does not have unfettered discretion to decide when the standard is breached, but must reach its assessment on the basis of relevant sources of international law.

In applying these general parameters, the tribunal made it clear that it did not have the function of an appeals court. Rather, the conduct of the courts in question had to be clearly improper and discreditable. It also noted, however, that the modern standard did not require that a
State, or an agency of the State, be acting in bad faith.\textsuperscript{30} The absence of a need to show bad faith is also found in \textit{Loewen v. United States}.\textsuperscript{31} This is another NAFTA case focusing on judicial process following a civil suit against Loewen, a Canadian funeral services company. The tribunal in this case stated that what needed to be shown was “manifest injustice in the sense of a lack of due process leading to an outcome which offends a sense of judicial propriety”.\textsuperscript{32}

In the case of \textit{Tecmed v. Mexico}, the tribunal focused on the breach of expectations of the investor as being subject to the fair and equitable treatment rule.\textsuperscript{33} The tribunal considered the fair and equitable provision as a principle of good faith conduct, adding that it required host countries to act in a manner that is consistent, totally transparent and free from ambiguity.\textsuperscript{34} Several administrative law principles were considered to be particularly relevant, most notably that laws must be applied that respect the purposes of those laws, and that decisions and permits cannot be arbitrarily revoked. All of these issues were collectively considered in \textit{Tecmed}, but arguably each of these conditions may also independently be a part of the minimum international standard of treatment legally required today.

The overall result of the decisions to date is that fair and equitable treatment provisions may be construed as no longer applicable solely to what would be considered egregious abuses of government power, or disguised uses of government powers for untoward purposes, but to any open and deliberate use of government powers that fails to meet the requirements of good governance, such as transparency, protection of the investor's legitimate expectations, freedom from coercion and harassment, due process and procedural propriety and good faith. In addition, it is relevant to consider whether the treatment is in breach of representations made by the host State that were reasonably relied upon by the investor.\textsuperscript{35} Where regulatory and administrative processes are less developed, the potential risk of a finding against the host country involved may become greater in the light of these developments. This may create compliance problems. On
the other hand, the cases also take into account the actual circumstances under which the foreign investor operates.\(^\text{36}\) Thus, legitimate expectations can be construed in relation to the reality of the commercial risk the investor undertakes. This will include factors such as the familiarity of the investor with the host country and its economic, administrative and procedural practices, the degree of speculative risk freely undertaken by the investor, and the extent of the latter's compliance with legal requirements.

The standard of *full protection and security* for foreign investment has a particular application to periods of insurrection, civil unrest and other public disturbances, including illegal disturbances (although it is not explicitly limited to those circumstances). It encompasses damage or losses sustained by an investor as a result of such violent episodes, whether directly due to government acts or to the lack of adequate protection of the investment by government officials or police. While this standard has been primarily used in situations of violence, there are also examples of its application in non-violent situations in the sense of a legal protection and security.\(^\text{37}\) Despite the more limited nature of this obligation, it is of considerable relevance to developing countries in particular, where different forms of civil strife and interference with legal rights remain more frequent, and where the lack of adequate protection is a commensurate problem in many cases. At least three ICSID cases have focused on this obligation in recent years.\(^\text{38}\)

In the course of these cases, the tribunals have indicated that the obligation is not one of result – that is, it is not a complete insurance policy against any and every loss due to some form of civil strife. However, the standard of care required has been set at a fairly high level. For example, comparisons with treatment of domestic nationals in cases of similar strife have been rejected. Arguments of incapacity or higher priorities in responding to the circumstances of the strife have also been rejected as a basis for a defence to a claim. In essence, while not an obligation of result, an obligation of good faith efforts to protect
the foreign-owned property has been established by these recent cases, without special regard for the resources available to do so. This has been referred to as a standard of “due diligence” on the part of the host country. As a result, this standard should be understood as being very much a “living” one. It places a clear premium on political stability, and the obligation of host countries to ensure that any instability does not have negative effects on foreign investors, even above the ability to protect domestic investors.

E. Expropriation

The basic principles of customary international law on expropriation state that foreign-owned property may not be expropriated or subject to a measure tantamount to expropriation, unless four conditions are met: the measure is for a public purpose; it is taken in accordance with applicable laws and due process; it is non-discriminatory; and full compensation is paid. One important conceptual problem has been the subject of litigation and debate in recent years, namely the kind of government acts that constitute expropriation and that are therefore subject to compensation. The main types of government takings that lie within the concept of expropriation include (UNCTAD, 2000):

- **The actual taking of property by direct means**, including the loss of all, or almost all, useful control of property. This can be done by transferring all foreign-owned assets in an industry or sector into national ownership (nationalization) or by the taking of specific assets (expropriation).

- **Indirect taking**, where a measure that does not directly take property has the same impact by depriving the owner of the substantial benefits of the property. This category has been subdivided between:
- *Creeping expropriation*, that is, the use of a series of measures in order to achieve a deprivation of the economic value of the investment. In this case, no individual measure in itself would amount to an expropriation; and
- *Regulatory expropriation*, where a measure is taken for regulatory purposes but has an impact on the economic value of the asset owned by the foreign investor sufficient to be deemed an expropriation.

Regulatory expropriation has become particularly important in recent years. Given that public policy goals may not always be achieved through voluntary compliance on the part of private owners of productive assets, a degree of regulation by the State is inevitable. The major problem is to distinguish between a legitimate exercise of governmental discretion that interferes with the enjoyment of foreign-owned property and a regulatory taking that requires compensation. Therefore, a balance needs to be struck between achieving the public policy goals in question, which could reduce the value of privately owned assets, and the preservation of the economic value of those assets. In the context of development policy this may create particularly sensitive problems, given the limited resources that may be available to the developing host country to offer full compensation and the possibly greater urgency in the need for governmental action on policy grounds to secure the achievement of development policy goals (UNCTAD, 2003c, p. 111).

The issue attracted considerable attention during the unsuccessful OECD-based negotiations on the Multilateral Agreement on Investment (MAI), in part because of concerns that arose out of the NAFTA case *Ethyl Corporation v. Canada.* This case involved a Canadian ban on imports of a gasoline additive, MMT. The Ethyl Corporation, an American importer of MMT into Canada, brought a challenge against the legislation instituting the ban under Chapter 11 of NAFTA. The Government of Canada settled the claim for some $13 million, representing the costs and lost profits suffered by Ethyl as a
result of the ban. This caused alarm over the possibility that IIAs could be used to limit host country powers to regulate in the field of environment, public health or similar areas. It also gave rise to fears that the prospect of investor-State arbitration, arising out of alleged regulatory takings, could result in a “regulatory chill” on the grounds that concern over liability exposure might lead host countries to restrict a necessary regulation.

Regulatory taking was also a key issue in the Metalclad v. Mexico arbitration under NAFTA. The tribunal found that a measure to prevent the use of land as an underground landfill and establish it as a State wildlife protected area was a measure tantamount to expropriation and required compensation. In making this determination, the tribunal ruled that the actions of the municipal and regional governments had denied the use of the land to the claimant, contrary to the assurances given by the Federal Government, thereby depriving the owner of the expected benefit from the land. This part of the award was upheld on judicial review.

However, the initial group of subsequent NAFTA cases that addressed regulatory takings includes language suggesting that regulations will not normally be seen as expropriations. S.D. Myers is perhaps the most often cited of these cases. On the other hand, the focus of analysis has turned towards the effect of a measure on a foreign investor, not the purpose of the measure (Mann and Soloway, 2002). This approach, if taken too far, could lead to the risk of a regulatory chill as noted above. However, the emphasis on the exceptional nature of regulatory takings, if followed by tribunals, should reduce this risk.

In this regard, the reasoning of the tribunal in Marvin Roy Feldman v. The United Mexican States is instructive. This case was brought under Chapter 11 of NAFTA by a United States investor who alleged that he had suffered a regulatory taking as a result of the discriminatory application of taxation measures to exports of tobacco
products from Mexico. In this connection, the tribunal identified the main issue as being whether the actions of a Government “constitute an expropriation or nationalization, or are valid governmental activity”. While the tribunal went on to state that Governments may have many ways of driving a company out of business, it also noted that:

“At the same time, governments must be free to act in the broader public interest through the protection of the environment, new or modified tax regimes, the granting or withdrawal of government subsidies, reductions or increases in tariff levels, imposition of zoning restrictions and the like. Reasonable government regulation of this type cannot be achieved if any business that is adversely affected may seek compensation, and it is safe to say that customary international law recognizes this.”

On the facts, although the tribunal found a violation of the national treatment standard, it held that the acts of the Mexican Government did not constitute an indirect expropriation. It noted in this regard that not every business problem of a foreign investor could amount to an expropriation under NAFTA.

In *Tecmed v. Mexico*, the tribunal stated its view that regulatory measures were covered by the same rules on expropriation as other types of government measures. The effect on the investor was considered to be the primary test to apply, much as in the other recent cases. This included the economic impact and a test that considered the loss of rights of the investor. However, the tribunal, in this case, seems to have set a higher bar of the degree of impact, looking to see whether the “negative economic impact of such actions on the financial position of the investor is sufficient to neutralize in full the value, or economic or commercial use of its investment without receiving any compensation whatsoever”. It continued:
“Under international law, the owner is also deprived of property where the use or enjoyment of benefits related thereto is exacted or interfered with to a similar extent, even where legal ownership over the assets in question is not affected, and so long as the deprivation is not temporary. The government’s intention is less important than the effects of the measure [i.e. the economic value of the use, enjoyment or disposition of the assets or rights affected by the administrative action or decision have been neutralized or destroyed] on the owner of the assets or on the benefits arising from such assets affected by the measures; and the form of the deprivation measure is less important than its actual effects.”48

The tribunal then stated that it was not for it to look at the legitimacy of a measure under the domestic law or regime, but solely under the applicable international law. The Tecmed award also considered that part of the analysis should be a proportionality test: there must be a reasonable relationship of proportionality between the charge or weight imposed upon the foreign investor and the aim sought to be realized by any expropriatory measure. A related question was whether the foreign investor was asked to carry too much of the burden for the protection of the local municipality, without compensation.49

A further limit on the availability of regulatory expropriation as a claim under IIA provisions was considered in the case of Olguin v. Republic of Paraguay.50 This case arose out of the bankruptcy of a bank in Paraguay. The claimant alleged that the actions of the host country had created this situation and led to his loss. The tribunal noted that the acts of the government accounting bodies charged with the oversight of banking services were negligent by omission in performing their duties.51 Nonetheless, it was held that the omission to act could not be an expropriation, which required positive acts by the Government, and a transfer of rights or the fruits of the investment, in the absence of the provisions of the BIT that related to “gross omissions”.52 Neither was the loss of funds due to a bankruptcy. Here, the premise that a BIT does
not act as an insurance policy for bad business decisions was applied. In addition, the tribunal noted that the claimant was an experienced businessman who was not unaware of the administrative situation in Paraguay and that he had made a risky and speculative investment. Thus, the actual knowledge of local circumstances, and the degree of risk voluntarily undertaken by the investor in the light of that knowledge, will be a factor to be considered in determining whether the actions of the host country Government and its agencies will be construed as regulatory takings or expropriations.

Other BIT cases have only tangentially addressed this issue. However, one of the more important of these is the Maffezini case. The tribunal considered the full enforcement of environmental impact assessment laws prior to the operation of an investment. It stated that such laws were consistent with common international practice, that they were important for environmental and social purposes, and that their full application could not qualify as an infringement of the fair and equitable treatment obligations.53

In sum, although the case law is still at an early stage, and the long-term development in this area is not clear, it may be said that tribunals are taking seriously the issue of regulatory expropriation and are trying to develop a balanced approach. Arguably, the emphasis on the effect, rather than purpose of the measure, tips the balance too much in favour of the investor. On the other hand, to establish the expropriatory effect of a regulatory measure, the cases suggest a rigorous standard of significant economic deprivation of the value of the investor’s assets, arising out of deliberate acts, not omissions. In any case, the regulatory intent behind the measure will be relevant in that a proportionality analysis would be impossible without taking this into account. Equally, the investor’s knowledge of the risks and rewards of the venture in question, given the actual business environment of the host country and the investor’s experience of it, will be significant factors.
F. Other legal claims by investors

In addition to the issues covered in previous subsections, IIAs contain other grounds for legal claims. Among these are provisions to ensure the repatriation of profits, prohibitions on the imposition of performance requirements on foreign investors, and provisions allowing movement of key personnel.

Of these various other possible grounds, only that concerning the prohibition of performance requirements has been raised in investment arbitration and this only in NAFTA, as most BITs do not contain performance requirements prohibitions.\(^{54}\)

G. Implications

There remains considerable uncertainty concerning the content of key substantive obligations stemming from the currently available awards. These areas of doubt include:

- In relation to national treatment, the criteria for comparing whether foreign and domestic investors are “in like circumstances” and the standard for determining less favourable treatment;
- The scope of the most-favoured-nation treatment provision;
- The meaning of the fair and equitable treatment standard, and the extent of the full protection and security provision; and
- The application of the rules on expropriation to regulatory measures designed to protect public welfare.

Other issues are routinely raised in debates on the linkages between development and IIAs, in particular the role of performance requirements. As noted previously, the fact that the existing cases have not addressed these other issues in detail does not diminish the possibility of future disputes in these areas.
When combined, the above concerns raise additional issues for developing countries with regard to the scope of their national policy space and, in particular, the right to regulate foreign-owned assets and investments for the public policy purpose of economic and social development. Accordingly, the challenge arises for arbitrators, faced with claims based on IIA provisions, to interpret these in a manner that not only ensures the observance of investment protection obligations, but also sees such provisions as being responsive to legitimate claims by Governments to regulate in the public interest and in the furtherance of essential development policy objectives. In particular, arbitrators must guard against awards that may inadvertently contribute to the risk of “regulatory chill” as noted above (Cosbey et al., 2004). Given comparatively weaker regulatory regimes in many of the developing countries where BITs are a common instrument, a “regulatory chill” could have a profound impact on social and environmental conditions. In effect, policy space may be curtailed out of fear of arbitrations.

Finally, one may consider whether there is a broader political impact of the current arbitrations. The fact of the growing number of arbitrations increases the awareness of Governments and civil society of the potential consequences of entering into what might otherwise be seen as useful agreements. At the same time, there is no indication that these arbitrations have had an impact on the receptivity to FDI as a whole. What is more likely is that the interaction between national investment policies and IIAs will be the subject of a broader political debate. This would be a positive development, as more awareness and information about this issue could yield stronger and more coherent investment policies in the longer run. The same may hold true for the structure and content of future IIAs.
Notes

1. In the meantime there is more authority on this point, though not as basic as Mihaly. See Generation Ukraine, Inc. v. Ukraine, ICSID Case No. ARB/00/9. Award, 16 September 2003 (United States/Ukraine BIT), paragraphs 8.6, 18.5-18.9; and PSEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Uretim ve Ticaret Limited Sirketi v. Turkey, ICSID Case No. ARB/02/5, Decision on Jurisdiction, 4 June 2004 (United States/Turkey BIT), paragraphs 67-105.


3. NAFTA, Articles 1101-1102, Annex I, II, III, IV. Chapter 6 of NAFTA is also of relevance to the energy sector, and Chapter 14 is relevant for financial services.

4. S.D. Myers Inc. v. Canada, op. cit.; Marvin Roy Feldman v. The United Mexican States, ICSID Case No. ARB(AF)/99/1, Award on Merits, 16 December 2002 (NAFTA).

5. Marvin Roy Feldman v. The United Mexican States, op. cit., paragraph 12.3.


7. Ibid., paragraph 250.

8. Pope & Talbot, Inc. v. The Government of Canada, op. cit., Award on Merits, paragraphs 73-82. See also Occidental Exploration and Production Company v. The Republic of Ecuador, LCIA Case No. UN3467, Final Award, 1 July 2004 (United States/Ecuador BIT), here paragraphs 167-177.


10. Emilio Agustin Maffezini v. The Kingdom of Spain, ICSID Case No. ARB/97/7), Decision on Jurisdiction, 25 January 2000; Award, 13 November 2000; Rectification of Award, 31 January 2001 (Argentina/Spain BIT).

11. The first published case to address this is Asian Agricultural Products Ltd. v. Republic of Sri Lanka, op. cit.
12 Emilio Agustin Maffezini v. The Kingdom of Spain, op. cit., Decision on Jurisdiction, 25 January 2000, paragraphs 62, 63.
14 Siemens v. Argentina, ICSID Case No. ARB/02/8, Decision on Jurisdiction (English), 3 August 2004 (Germany/Argentina BIT).
15 Plama Consortium Limited v. Bulgaria, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 8 February 2005 (Energy Charter).
16 Tecnicas Medioambientales Tecmed S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, 29 May 2003 (Spain/Mexico BIT), paragraph 69. This is applied in practice in ADF Group Inc. v. United States of America, ICSID Case No. ARB(AF)/00/1, Final Award, 9 January 2003 (NAFTA).
17 MTD Equity Sdn. Bhd. & MTD Chile S.A. v. Chile, ICSID Case ARB/01/7, Award, 25 May 2004 (Malaysia/Chile BIT), paragraph 104.
18 Tecnicas Medioambientales Tecmed S.A. v. United Mexican States, op. cit.
19 Pope & Talbot, Inc. v. The Government of Canada, UNCITRAL, Award on Merits, 10 April 2001; Award on Damages, 31 May 2002; Award on Costs, 26 November 2002 (NAFTA).
20 Emilio Agustin Maffezini v. The Kingdom of Spain, op. cit.
21 Middle East Cement Shipping and Handling Co. S. A. v. Arab Republic of Egypt, ICSID Case No. ARB/99/6, Award, 12 April 2002 (Greece/Egypt BIT).
22 For example, Tecnicas Medioambientales Tecmed v. United Mexican States, op. cit.
23 S.D. Myers Inc. v. Canada, op. cit., paragraph 263.
24 Metalclad Corporation v. The United Mexican States, ICSID Case No. ARB(AF)/97/1, Award, 30 August 2000; Review by the British Columbia Supreme Court (2001 BCSC 664), 2 May 2001; Supplementary Reasons for BCSC Decision, 31 October 2001 (NAFTA), here Review (2001 BCSC 664), paragraphs 62-63.
26 See Tecnicas Medioambientales Tecmed v. United Mexican States, op. cit., paragraphs 152-174; and the NAFTA cases of Pope & Talbot, Inc. v. The Government of Canada, op. cit., Award on Damages, paragraph 57 et seq.; ADF Group Inc. v. United States of America, op. cit., paragraphs...
179-180; *Mondev International Ltd. v. United States of America*, ICSID Case No. ARB(AF)/99/2, Award, 11 October 2002 (NAFTA), here paragraphs 114-116.

27 *Pope & Talbot, Inc. v. The Government of Canada*, op. cit. Award on Damages, paragraph 64.

28 *Mondev International Inc v. United States of America*, op. cit., paragraph 119. In *ADF Group v. United States of America*, which concerned a statute on local procurement requirements, the tribunal reiterated the approach taken in the *Mondev* case, namely that a tribunal did not have carte blanche to arrive at its own idiosyncratic assessment, but must ground its determination on relevant sources of international law. *ADF Group v. United States of America*, op. cit., paragraphs 184-185.

29 *Mondev International Inc v. United States of America*, op. cit., paragraph 127.

30 Ibid., paragraph 116.

31 *Loewen Group, Inc. and Raymond Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Award on Jurisdiction, 5 January 2001; Award on Merits, 26 June 2003 (NAFTA), here Award on Merits, paragraph 132.

32 Ibid., paragraph 132.

33 *Tecnicas Medioambientales Tecmed v. United Mexican States*, op. cit., paragraph 154 et seq.

34 Ibid., paragraph 154.

35 *Waste Management, Inc. v. United Mexican States*, ICSID Case No. ARB(AF)/00/3, Final Award, 30 April 2004 (NAFTA), paragraph 98.


37 See, for example, *CME Czech Republic B.V. v. Czech Republic*, op. cit. paragraph 613; *Ronald S. Lauder v. The Czech Republic*, op. cit. paragraph 314; see also *Jack Rankin v. The Islamic Republic of Iran*, Iran-United States Claims Tribunal, Award, 3 November 1987 (17 Iran-United States Claims Tribunal Reports), paragraphs 135 and 147.

February 2002 (United Kingdom of Great Britain and Northern Ireland/Arab Republic of Egypt BIT).


On which see *Antoine Goetz v. Republic of Burundi*, ICSID Case No. ARB/95/3, Award, 10 February 1999 (Belgium-Luxembourg Economic Union/Burundi BIT).


*Metalclad Corporation v. The United Mexican States*, op. cit.


This was stated quite clearly in *S.D. Myers v. Canada*, op. cit., paragraphs 281, and 280-285 more generally. However, these paragraphs also stated that regulatory measures could be subject to claims for compensation as an expropriation. See also *Pope & Talbot, Inc. v. The Government of Canada*, op. cit., Interim Award on Merits, paragraphs 96-99.

Marvin Roy Feldman v. The United Mexican States, op. cit., paragraph 98.

Ibid., paragraph 103.

*Tecnicas Medioambientales Tecmed S.A. v. United Mexican States*, op. cit., paragraphs 121 et seq.

Ibid., paragraph 116.

Ibid., paragraph 122.


Ibid., paragraph 70.

Ibid., paragraph 73.

*Emilio Agustin Maffezini v. The Kingdom of Spain*, op. cit., Award, paragraph 67.

It was a primary issue in *ADF Group Inc. v. United States of America*, op. cit. It has been raised but addressed only briefly in other cases, including *Pope & Talbot, Inc. v. The Government of Canada*, op. cit., Interim Award on Merits, and in *S.D. Myers Inc. v. Canada*, op. cit.
CONCLUSIONS

The foregoing analysis has tried to identify some of the current issues concerning the investor-State dispute settlement procedures. At the end of 2005, the universe of IIAs exceeded 5,000 agreements (i.e. BITs, DTTs and other agreements with investment provisions), with the majority of all these treaties containing investor-State dispute settlement mechanisms. Arbitral awards will undoubtedly influence the interpretation of this vast network of agreements, not only with regard to the negotiation of the terms of future agreements, but also concerning the settling of disputes. In addition, as noted in the previous section, the risk of a “regulatory chill” in developing countries, as a result of arbitral decisions that may go too far in protecting the rights of investors and their investments, is a matter of concern of which arbitrators need to take heed in order to develop balanced case law.

In this regard, the preceding discussion suggests some potentially significant risks of financial, administrative, institutional and policy costs. The mitigation of these risks is appropriate and, in some cases, essential if the benefits of IIAs are not to be diminished by them. In the light of these considerations, a number of observations can be made concerning both procedural and substantive issues.

A. Procedural issues

From a procedural perspective, it appears that the concerns identified in this paper could be addressed by improving the dispute settlement procedures, in particular by increasing transparency, addressing issues arising out of the multiplicity of proceedings and consistency of awards, and encouraging the development of effective domestic institutions for dispute settlement and their increased use.

1. Improving the procedures in general

A primary concern in this context is to focus more attention on the means of avoiding or reducing arbitral proceedings in the first place – for example, emphasizing the pre-arbitration means of settling a dispute, and increasing the thresholds applied with regard to initiating
an arbitral proceeding. This is especially important where the parties wish to maintain a good investment relationship, a relationship that is often put at risk through recourse to litigation. To address this point, a number of approaches can be considered:

- Greater recourse to conciliation along the lines of Article 28 of the ICSID Convention. Indeed, ICSID has a policy of drawing the attention of parties to a dispute to the conciliation alternative. On the other hand, mediation may be a more useful means of reaching an amicable settlement than the use of comparatively formal conciliation proceedings. Indeed, ICSID has suggested the establishment of a mediation facility for investor-State disputes.¹

- Limiting exposure to frivolous claims, as provided for in the Chile-United States Free Trade Agreement, Article 10.19.6, and the United States-Uruguay BIT, Article 28.6. In this regard, it should be noted that ICSID has a rigorous registration process under which the Secretary-General of ICSID will refuse to register a case where it is manifestly outside the jurisdiction of the Centre. However, this jurisdiction does not extend to the merits of the dispute that remain within the power of the tribunal. In relation to this power, ICSID has proposed that the Arbitration and Additional Facility Rules be amended to allow for the expedited dismissal of a claim, or part of it, at an early stage of the proceedings.²

- Excluding, a priori, certain substantive matters from investor-State dispute settlement (see, for example, Article 22 of the Canadian model Foreign Investment Promotion and Protection Agreement with reference to transparency and Annex IV of the 2004 Canadian model BIT with reference to certain pre-establishment rights) or creating additional mechanisms to preclude the claim from proceeding (under the 2004 Canadian model BIT, the investor's claim relating to a party's tax measure
cannot proceed if the taxation authorities of both parties jointly determine that there is no violation of the BIT).³

- Providing for extended cooling-off periods, such as Annex 10-C (“Special Dispute Settlement Provisions”) of the Chile-United States Free Trade Agreement, which imposes a minimum period of one year before the investor can submit a claim against Chile in the event of the imposition of restrictive measures with regard to payments and transfers. On the other hand, insisting on long waiting periods may not be very useful in cases where there is no chance of an amicable settlement. In such cases, it may be better for the terms of the IIA to allow for the parties to proceed to the arbitration proceedings at the earliest possible date.

- Time limits on claims, such as the United States model BIT, Article 26, under which no claim may be submitted to arbitration if more than three years have elapsed from the date on which the claimant first acquired knowledge of the alleged violation of the agreement.

In addition, providing for more detailed dispute settlement rules in new IIAs could be considered, as is done in the revised United States and Canada model BITs, so as to avoid leaving too much discretion in the hands of the arbitral tribunal to establish its own rules. This would give the process greater certainty. On the other hand, where an IIA refers to existing institutional procedures, such as ICSID, the dispute settlement process will already be subject to quite detailed procedural rules. In such cases the addition of further detail in the IIA may not be particularly useful, unless very specific problems are to be addressed, as is the case with the United States and Canadian models.⁴
2. Improving specific procedural issues

A number of specific procedural issues highlighted in the preceding chapters may also benefit from further refinement, some of which are set out below.

Transparency

The issue of transparency remains critical in investor-State dispute settlement procedures. Since the disputes often concern public policy issues, calls for the participation of interested or affected non-disputing parties have increased. Despite the above-mentioned developments in the NAFTA context in this regard, as well as other efforts on the part of the United States and Canada in conjunction with more recent bilateral treaty partners, the issue subsists in the broader BIT context. While it would be impracticable to renegotiate each and every BIT, increased transparency could be achieved if it was possible to introduce relevant modifications to the international arbitration rules that are relied upon by reference in these BITs (first of all, UNCITRAL and ICSID rules). Indeed, the proposed reforms of the ICSID procedure include the amendment of the Arbitration Rules (AR No. 37 and AFR No. 41) to make clear that the tribunals would have the authority to accept and consider submissions from third parties and to allow third parties to attend hearings, or even open them to the public, without the need for the tribunal to obtain the consent of both parties, as is currently the case.

In addition, transparency could be enhanced by a requirement for the publication of all notices of arbitration under any investor-State dispute settlement in a single registry. This is done in NAFTA and in more recent United States bilateral agreements, and is now partially done at ICSID with the listing of the names and a one-line description of the subject of the case, together with its procedural stages. However, the establishment of a single registry on a global level would be much more difficult to achieve, since it would require worldwide cooperation.
Multiplicity of proceedings and consistency of awards

The issues surrounding possible multiple proceedings and potential contradictory awards, and the risks associated with them, also need to be addressed. Some procedural or institutional measures in this regard could include:

- A requirement that cases based on the same facts be consolidated, irrespective of the relationship or different legal personality of the claimants. NAFTA has a model for this, as have the latest BIT and FTAs by the United States and the Canadian BIT model.

- The use of a general appellate body that would ensure consistency in similar cases, as well as the possible establishment of a permanent tribunal to adjudicate investment disputes. As noted above, this is contemplated in several recent treaties involving the United States, and is the subject of increasing attention from Governments and academics. According to ICSID, by mid-2005 as many as 20 countries may have signed treaties with provisions on an appeals mechanism in investor-State disputes. However, such a body would have many challenges to overcome. Given the current caseload in investment arbitration, it would probably be a busy tribunal that would require a large capacity. It would also require the amendment of many IIAs for the authority of this new body to be recognized. Last, not least, it is uncertain whether a critical mass of countries would support this idea.

- The use of a standing body of arbitrators from which all arbitrators must be chosen (a roster). This could improve consistency in the arbitration process, and restrain the arbitrating parties' possible temptation to appoint persons sympathetic to their positions. Lists of arbitrators do exist, for
example with ICSID. However, any list would need to be quite large to ensure sufficient variety and choice of individual arbitrators.

In addition, improvements in the wording of procedural provisions could be considered, including a review of the operation of “fork-in-the road” (“choice-of-forum”) provisions, or the intentions for, and operation of, umbrella clauses, and of the definition of “investor” and “investments” to ensure that these are commensurate with the goals of IIAs today.

Enhancing the capacity of domestic institutions

A further possible approach to balance national policy space and developmental goals against investment protection is to enhance the role of domestic dispute settlement bodies. If transparent, reliable and objective local dispute settlement mechanisms are available, the need for international dispute settlement might be less urgent. This may help to reduce the overall costs of dispute settlement by providing local solutions to local problems. To that end, it seems necessary to develop and improve local capacity for legislative, administrative and judicial institutions and practices.

On the other hand, the introduction of a requirement that the foreign investor exhaust local remedies before having recourse to international methods of dispute settlement could create difficulties. This is not an approach found in recent IIA practice. A possible disadvantage of such a requirement is that the investor, after an unsatisfactory outcome, may have recourse to international arbitration, subjecting the host country’s national court system to a possible review by an international tribunal (UNCTAD, 2003c, p. 117).
B. Substantive issues

As already indicated, the analysis in this paper points to the need to review substantive provisions in IIAs, particularly provisions on national treatment, MFN treatment, fair and equitable treatment, and expropriation.

- Careful consideration needs to be given to national treatment provisions regarding their de jure and de facto application, and the scope of “like circumstances”. As explained above, arbitration tribunals have interpreted the latter term in different ways. In the case of developing countries, an important issue can be whether domestic enterprises, operating in the same local market as a foreign investor, which may be a large TNC, should be regarded as being in “like circumstances”. Moreover, care should be taken concerning the possible application of investor-State dispute settlement provisions to pre-establishment rights.

- Similarly, MFN provisions in future treaties ought to be carefully drafted so as to avoid unintended results arising out of the interpretations of MFN clauses by arbitral tribunals in the light of the diverging decisions in the Maffezini, Tecmed, Salini and Plama cases. A limited example of how this issue could be addressed is provided by Annex III of the Canadian model BIT, which excludes treatment accorded under all bilateral or multilateral international agreements in force or signed prior to the date of entry into force of the treaty from its application.

- Attempts could be made to give greater clarity to the provision on fair and equitable treatment. For example, both the United States' and Canada's new model BITs make it clear that the concepts of “fair and equitable treatment” and “full protection and security” do not require treatment in addition to or beyond what is required by the customary international law minimum
standard for the treatment of aliens. The United States model BIT further spells out the meaning of respective standards, stating that “fair and equitable treatment” includes the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings and that “full protection and security” require each party to provide the level of police protection required under customary international law.

- Clarification could be sought concerning the scope of regulatory expropriations. It is important to strike a balance between a country's right to regulate and the reasonable commercial interests of the investor. Again, both the United States' and Canada's new model BITs provide an example of how this could be approached. In both, a separate annex is added to clarify the issue. Specifically, respective annexes provide for a fact-based, case-by-case inquiry into alleged regulatory expropriations, an inquiry that considers various factors, including the economic impact of a measure, the extent of interference with reasonable investment-backed expectations and the character of the impugned measure. Additionally, these annexes have a caveat to the effect that only in “rare circumstances” are non-discriminatory measures designed to protect legitimate public welfare objectives, such as health or environment, deemed to be indirect expropriations. Canada's model text is conceptually different and goes further than that of the United States by offering an example of such “rare circumstances”: “when a measure or series of measures are so severe in the light of their purpose that they cannot be reasonably viewed as having been adopted and applied in good faith” (see Annex B.13 (1) of Canada's model BIT).

- Finally, consideration could be given to the use of interpretative notes (as is often done in trade agreements), which are consistent with the Vienna Convention on the Law of
Treaties. The NAFTA Free Trade Commission's interpretative statements can serve as an example of parties developing more specificity in agreements, although this could be problematic if States parties to pending proceedings tried to use such means to improve their position as litigants.

C. The role of the international community

As already noted, the burden of addressing the challenges arising out of the current investor-State dispute settlement system is likely to weigh disproportionately on developing countries, especially the least developed ones, because they often lack the human and financial resources needed to adequately “navigate” within this system. This underlines the importance of capacity-building technical cooperation in this regard. Several issues could be considered, for example:

- Increasing capacity building for developing countries. This is essential for developing countries' effective and informed participation in the negotiation of future IIAs and in the prevention and management of investor-State disputes.8 (The UNCTAD secretariat has recently developed a training course with a view to equipping developing country Governments with the necessary capacity to manage investor-to-State disputes and to be able to mobilize the necessary expertise to assist them in the proper conduct of such procedures.9)

- Strengthening international institutional capacities to help developing countries manage better investor-State disputes could provide an additional, and probably cost-effective, option in this area.10
The implications of the investor-State dispute settlement procedures are gaining more attention as foreign investors are increasingly making use of the relevant IIA provisions to challenge measures taken by host countries that adversely affect their investments. In view of the difficulties experienced with current dispute settlement procedures, the above analysis points to several possible improvements of the present investor-State arbitration system. These may involve various procedural, substantive and capacity-enhancing matters. The basic purpose of these revisions would be to ensure the transparency, consistency and reliability of the system and the coherence of outcomes, it being borne in mind that the investor-State dispute settlement procedures are likely to continue to play a significant role in the evolution of international investment rules.

Given the vulnerability of developing countries and their inherent difficulties in addressing some of the issues discussed here, technical assistance and institution building for these countries should be an essential element of whatever package of improvements is designed.
Notes


3  Canada’s new model BIT includes a number of procedural innovations with regard to the ISDS process, namely full disclosure of investor-State disputes, open arbitral proceedings and publication of all documents related to disputes. See www.dfait-maeci.gc.ca/tna-nac/documents/2004-FIPA-model-en.pdf.

4  On the United States model see further Kantor (2004).

5  ICSID (2004, para. 20).

6  See chapter II.B.

7  See footnotes 40, 46, 11 and 45.

8  ICSID (2004, para. 19) suggests an intensification and further systematization of training efforts in this area.

9  The course on Managing Investment Disputes was designed as a follow-up to an expert meeting in November 2004 and the Commission on Investment's session in March 2005, which identified developing countries' needs for technical assistance and capacity building to deal with disputes arising out of investment treaties and involving private investors and the State. It was based mainly on sharing of experience and studying actual cases (case studies provided by UNCTAD), and touched on both the substantive and the institutional aspects involved.

10 This issue was discussed at a joint UNCTAD-OECD-ICSID high-level symposium in Paris on 12 December 2005.
REFERENCES


Annexes

Annex 1: Known investment treaty claims
(November 2005)

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**Total** 219

*Source*: UNCTAD.

*Note*: Notices of intent not included.
Annex 2: List of cases reviewed

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CME Czech Republic B.V. v. Czech Republic, UNCITRAL, Partial Award, 13 September 2001 (The Netherlands/Czech Republic BIT). Also The Czech Republic v. CME Czech Republic B.V, Court of Appeal, Stockholm, Sweden, Case No. T-8735-01 (42 ILM 919 (2003)).

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