Coherence and Consistency in International Investment Law

by Christoph Schreuer

The Role of Nationality

Coherence and consistency are desirable qualities in any legal system. A legal system is coherent if its elements are logically related to each other and if it shows no contradictions. A legal system is consistent if it treats identical or similar situations in the same way and if it gives equal treatment to the participants in the system. These properties are easiest achieved through rules of general application administered by decision-makers of general jurisdiction.

International investment law lacks coherence and consistency in several respects. In large measure this is a consequence of its legal foundations. There are a large number of bilateral treaties (notably bilateral investment treaties or BITs). There are regional treaties such as the North American Free Trade Agreement (NAFTA) and the Energy Charter Treaty (ECT). And there are some widely applicable multilateral treaties such as the ICSID Convention. These treaties afford various degrees of protection to the nationals of the States participating in them.

A closer look at this network shows that it does not offer a coherent system of protection. Rather, it is a fragmentary patchwork that favours some investors while ignoring others. The decisive criterion is usually the investor's nationality or, more precisely, the existence of favourable treaty relations between the host State and the investor's home State.

The investor's nationality is relevant for several purposes. The substantive standards guaranteed by a treaty will only apply to nationals of the States parties to the treaty (although permanent residents are sometimes included). In addition, the jurisdiction of an international tribunal is determined, *inter alia*,

by the claimant's nationality. In particular, if the host State's consent to jurisdiction is given through a treaty, the offer will only apply to nationals of a State that is a party to the treaty. Access to ICSID arbitration is limited to nationals of States that are parties to the ICSID Convention. In addition, the ICSID Convention contains negative nationality requirement: host State nationals are generally excluded.

Similar considerations apply with respect to regional treaties. Only nationals of Canada, Mexico and the United States may rely on the NAFTA against one of the other two States parties. Only nationals of States parties to the ECT benefit from that treaty vis-á-vis any of the other States parties to that treaty.

In the absence of the right treaty relations of their home States, investors will find themselves without protection. But even an investor who can rely on a BIT may find that he does not enjoy the same protection as its competitor who has a different nationality. BITs vary considerably. Some provide more comprehensive protection than others. On the one hand, these differences arise from variations in the level of substantive protection offered. A particular treaty may not include all the substantive standards offered by other treaties. On the other hand, the differences arise also from variations in the treaties' clauses on dispute settlement. Some cover any dispute arising from an investment. Others are restricted to claims arising from breaches of the treaty. Yet other clauses are restricted to disputes relating to expropriations. In addition, access to international arbitration is often subject to a variety of conditions and procedural requirements.

It follows that investors enjoy different levels of protection in relation to the same host State depending on their nationality. Identical or similar fact situations may lead to different outcomes depending on the investors' nationalities. The existence, absence or variation in contents of treaties for the protection of investments is an important cause of inconsistency in the system. But, as will be seen further below, it is not the only one.

This preoccupation with nationality in international investment law leads to a paradoxical situation. Nationality is extremely important for the purpose of gaining access to investment arbitration, or generally for protection under treaties. In actual cases, much time and effort is spent to prove or disprove a particular nationality.[1] But when a case reaches the merits, strangely enough, discrimination on the basis of nationality is prohibited: an expropriation that discriminates between investors of different nationalities is illegal.[2] There are rules against arbitrary and discriminatory treatment which includes discrimination on the basis of nationality. Also, discrimination on the basis of nationality would be a violation of the fair and equitable treatment standard.[3] In order to forestall differentiations on the basis of nationality, most treaties contain national treatment and most favoured nation (MFN) clauses. Discrimination on the basis of nationality constitutes a violation of these clauses.

Therefore, distinctions on the basis of nationality are illogical: they are mandated in some contexts and prohibited in other contexts. This leads to conflicting results and affects the system's coherence.

Apart from legal logic, distinctions on the basis of nationality are also unsavoury from an ethical standpoint. Why should individuals and corporations have widely differing rights depending on the accident of their nationality? Unequal treatment of investors that are in like circumstances offends our sense of justice. Yet we seem to be trapped in a paradigm of treaty law that appears to require discrimination based on the accidents of treaty relations.

A number of remedies have been devised to tackle this form of unevenness in the system. Some of these remedies are widely available but are of limited

[1] See e.g. *Soufraki* v. *United Arab Emirates*, Award, 7 July 2004; *Siag* v. *Egypt*, Decision on Juridiction, 11 April 2007.

[2] See e.g. *ADC* v. *Hungary*, Award, 2 October 2006, paras. 441-443.

[3] See e.g. *CMS* v. *Argentina*, Award, 12 May 2005, para. 290.

effectiveness. Other possible remedies would be highly effective but appear unattainable at least for the time being.

Most Favoured Nation Clauses

MFN clauses are widely available. An MFN clause in a treaty will extend the better treatment granted to a third State or its nationals to the beneficiary of the treaty.[4] Most BITs and some other treaties for the protection of investments contain some form of MFN clauses.[5] But there are considerable variations in detail. For instance, some MFN clauses specify whether they include or exclude dispute settlement.[6] But most MFN clauses are worded generally and just refer to the treatment of investments.

MFN clauses carry considerable potential for the achievement of coherence and consistency. If applied rigorously they could lead to the levelling of differences based on nationality.[7] Yet their effect is limited. Practice shows that they are often approached with trepidation and applied in a half-hearted manner. The applicability of MFN clauses is uncontested as far as the substantive standards of protection are concerned. If an applicable treaty does not contain a clause on fair and equitable treatment (FET), the treaty's MFN clause will usually close the gap. It will be possible to import the FET clause from a treaty between the host State and a third State.[8]

The situation is different when it comes to questions of dispute settlement. The usefulness of an MFN clause to amend the basic treaty's arbitration clause is hotly contested. Most tribunals have allowed the application of MFN clauses to overcome procedural obstacles. These would often require resort to

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[4] See also *R. Dolzer/T. Myers*, After *Tecmed:* Most-Favored-Nation Clauses in Investment Protection Agreements, 19 ICSID Review - FILJ 49 (2004).

[5] See Article 1103 NAFTA; Article 10(7) ECT.

[6] The BIT between Austria and Kazakhstan specifies in its Article 3(3) that MFN treatment extends to dispute settlement.

[7] See *S.W. Schill*, Multilateralizing Investment Treaties Through Most-Favored-Nation Clauses, 27 Berkeley Journal of International Law 496 (2009).

[8] *Bayindir* v. *Pakistan,* Award, 27 August 2009, paras. 148-167.

domestic courts for a certain period of time before arbitration became available.[9] By contrast, where claimants tried to import more generous offers of consent to arbitration from other treaties by invoking MFN clauses they usually failed.[10]

To make the situation even more confusing, tribunals have adopted broad statements either embracing or rejecting the use of MFN clauses in the context of dispute settlement.[11] Therefore, the distinction between procedural issues and questions of consent for purposes of MFN treatment is not supported by the reasoning of tribunals.

The usefulness of MFN clauses as instruments for achieving a more coherent system presupposes three elements:

1. There must be an applicable basic treaty upon which the investor may rely containing an MFN clause.
2. There must be another treaty of the host State providing for the better treatment that is desired.
3. The tribunal must be persuaded that the MFN clause should be applied to the issue in question. This is often not possible when it comes to dispute settlement.

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[9] *Maffezini* v. *Spain,* Decision on Jurisdiction, 25 January 2000, paras. 38-64; *Siemens* v. *Argentina*, Decision on Jurisdiction, 3 August 2004, at paras. 94-110; *Gas Natural SDG, S.A*. v. *Argentina*, Decision on Jurisdiction, 17 June 2005, at paras. 24-31, 41-49; *Suez, Sociedad General de Aguas de Barcelona S.A., and InterAguas Servicios Integrales del Agua S.A.* v. *Argentina*, Decision on Jurisdiction, 16 May 2006, at paras. 52-66; *National Grid PCL* v. *Argentina,* Decision on Jurisdiction, 20 June 2006, at paras. 53-94; *Suez, Sociedad General de Aguas de Barcelona S.A., and Vivendi Universal S.A*. v. *Argentina and AWG Group Ltd.* v. *Argentina*, Decision on Jurisdiction, 3 August 2006, at paras. 52-68; *Impregilo* v. *Argentina*, Award, 21 June 2011, paras. 51-109; *Hochtief* v. *Argentina*, Decision on Jurisdiction, 24 October 2011, paras. 12-111. But see *Wintershall* v. *Argentina*, Award, 8 December 2008, paras. 158-197.

[10] *Salini* v. *Jordan*, Decision on Jurisdiction, 29 November 2004, para. 119; *Plama* v. *Bulgaria*, Decision on Jurisdiction, 8 February 2005, paras. 183, 184, 227; *Berschader* v. *Russia*, Award, 21 April 2006, paras. 159-208; *Telenor* v. *Hungary*, Award, 13 September 2006, paras. 90-100; *Tza Yap Shum* v. *Peru*, Decision on Jurisdiction, 19 June 2009, paras. 189-220; *Austrian Airlines* v. *Slovakia*, Final Award, 9 October 2009, paras. 109-140. But see *RosInvest* v. *Russia*, Award on Jurisdiction, October 2007, paras. 124-139.

[11] Contrast *Gas Natural SDG, S.A*. v. *Argentina,* Decision on Jurisdiction, 17 June 2005, at para. 49 and *Plama* v. *Bulgaria*, Decision on Jurisdiction, 8 February 2005, para. 223.

Nationality Planning

A more radical approach is nationality planning. In relation to a particular host State nationals of some countries may be unable to benefit from a BIT or other treaty. Others may find that an available BIT does not offer the desired protection. Yet other nationals may be able to rely on a treaty that offers the required level of security. Nationality planning consists in the deliberate acquisition of a nationality that gives access to the desired protection. Most often this will be done through the creation of a corporate structure that allows the investor to rely on a favourable treaty.

If the treaty in question accepts incorporation as a sufficient basis for corporate nationality all that is required is the establishment of a corporation in the State that has the favourable treaty with the host State. That corporation may serve as a conduit for a new investment or as a holding company for an existing investment.

Nationality planning or treaty shopping is not illegal or unethical as such. But States may regard such practices as undesirable and take appropriate measures against them.

A strategy employed in some treaties to counteract nationality planning is to require a bond of economic substance between the investor and the State whose nationality is claimed. Such an economic bond may consist of effective control over the corporation by national of that State. Alternatively, it may consist of genuine economic activity of the company in that State. Another strategy is the insertion of a so-called denial of benefits clause into the treaty that provides for jurisdiction. Under such a clause the States reserve the right to deny the benefits of the treaty to a company that does not have a genuine economic connection to the State whose nationality it claims.[12]

[12] Article 17(1) ECT.

In the absence of treaty clauses designed to block nationality planning, tribunals have accepted deliberately structured nationalities in some situations[13] but have dismissed them in others. They have accepted provident nationality planning that was designed to put investments under the protective umbrella of investment treaties.[14] But they have limited this acceptance to prospective planning. Prospective means that the corporate arrangements must have been in place before the facts that led to the dispute occurred or at any rate before the dispute arose. They have rejected *ex post facto* corporate restructuring to create a remedy after a dispute had broken out.[15]

Therefore, the success of nationality planning depends primarily on the time of the corporate structure's creation in relation to the relevant facts. If the restructuring is undertaken early i.e. before the adverse acts or at any rate before the outbreak of the dispute, the newly acquired nationality will be honoured. But a last minute change of nationality in the face of an existing dispute will be rejected.

It follows from the above that nationality planning as an instrument for achieving coherence and consistency has serious limitations:

1. It requires careful forward planning.
2. The administrative effort involved is typically realistic only for major investors.
3. It requires the existence of a favourable treaty that accepts incorporation as a sufficient connecting point for nationality.

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[13] *Autopista* v. *Venezuela,* Decision on Jurisdiction, 27 September 2001, paras. 83, 89-91, 110-134, 142; *Tokios Tokelės* v. *Ukraine*, Decision on Jurisdiction, 29 April 2004, paras. 18-71; *Aguas del Tunari* v. *Bolivia*, Decision on Jurisdiction, 21 October 2005, paras. 206-323, 329-332; *Saluka* v. C*zech Republic*, Partial Award, 17 March 2006, paras. 229, 241; *ADC* v. *Hungary,* Award, 2 October 2006, paras. 334-341, 350, 357-359; *Rompetrol* v. *Romania,* Decision on Jurisdiction and Admissibility, 18 April 2008, paras. 71-110.

[14] *Mobil* v. *Venezuela*, Decision on Jurisdiction, 10 June 2010, paras. 142-206.

[15] *Banro* v. *DR Congo*, Award, 1 September 2000; *Phoenix* v. *Czech Republic,* Award, 15 April 2009, 135-145; *Cementownia* v. *Turkey,* Award, 17 September 2009, paras. 116-117, 122-123, 136, 153-157.

4. It is subject to preventive measures embedded in the treaty such as the requirement of a real economic activity or a denial of benefits clause.

A Multilateral Agreement on Investment

An effective method to achieve coherence and consistency would be the creation of a multilateral treaty to replace the multitude of diverse bilateral and regional treaties. Such a treaty could grant identical substantive and procedural rights to investors from all participating countries. A treaty of this nature that is widely ratified would make nationality largely irrelevant. It would offer the same level of substantive and procedural protection to all investors.

A multilateral agreement on investment, while technically possible, is not a realistic possibility under present circumstances. Repeated efforts to draft such a treaty have all failed for a variety of reasons. At present, chances for the success of such a project are slimmer than ever. Negotiations for the drafting of such an agreement would open a veritable Pandora's Box of disagreements. In the unlikely event that agreement on a text were to be achieved, universal or near universal acceptance is unlikely.

Rights for Nationals of Non-Contracting States

The limitation of benefits arising from treaties to nationals of participating States is not a necessary consequence of the law of treaties. It is entirely possible to extend rights arising from treaties to nationals of non-contracting States. Treaties for the protection of human rights are a case in point. For instance, the European Convention of Human Rights guarantees rights and freedoms to everyone within the jurisdiction of the participating States regardless of nationality.[16] Similarly, applications to the European Court of

[16] [European] Convention for the Protection of Human Rights and Fundamental Freedoms, Article 1.

Human Rights claiming violations of rights set forth in the Convention may be submitted by "any person".[17]

The limitation of rights under investment treaties to nationals of participating States is based on a conscious decision. Human rights are accepted as having universal application. Their observance is accepted as an indispensable guarantee of human dignity. By contrast, economic rights of foreigners are regarded as a matter of economic policy. States are only willing to offer treaty guarantees to investors on the basis of reciprocity.

Conflicting Interpretations

Gaps and discrepancies in treaty relations are not the only cause of problems with the coherence and consistency of international investment law. At times similar or identical treaty provisions in BITs are interpreted in different ways. Sometimes one and the same treaty provision is interpreted differently by different tribunals. For instance, in the application of the clause on emergency in the BIT between Argentina and the United States, tribunals have reached widely divergent results even in relation to the same facts.[18]

Discordant interpretations of this kind are a consequence of the nature of investment arbitration. Each tribunal is put together on an *ad hoc* basis. Differently composed tribunals will inevitably not always agree on all points. Even competent and impartial arbitrators may reach conflicting results. In addition, arbitration, more than other forms of litigation, is driven by the arguments presented by the parties which may differ from case to case.

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[17] Article 34.

[18] *CMS* v. *Argentina*, Award, 12 May 2005, paras. 332-378; *CMS* v. *Argentina,* Decision on Annulment, 25 September 2007, paras. 101-150; *LG&E* v. *Argentina*, Decision on Liability, 3 October 2006, paras. 201-266; *Enron* v. *Argentina*, Award, 22 May 2007, paras. 322-342; *Enron* v. *Argentina*, Decision on Annulment, 30 July 2010, paras. 347-405; *Sempra* v. *Argentina*, Award, 28 September 2007, paras. 364-391; *Sempra* v. *Argentina*, Decision on Annulment, 29 June 2010, paras. 106-221; *Continental Casualty* v. *Argentina*, Award, 5 September 2008, paras. 160-236; *Continental Casualty* v. *Argentina*, Decision on Annulment, 16 September 2011, paras. 104-143.

In commercial arbitration such diversity of outcomes is usually not perceived as a major problem. Most awards are not published and the settlement of the dispute at hand is seen as more important than the development of a *jurisprudence constante*. By contrast, investment arbitration attracts much attention and discrepancies in the application of the law are widely discussed.

Several solutions are feasible for the promotion of a more harmonious case law. One such solution would be a faithful adherence to precedent.[19] Tribunals have emphasized on many occasions that they are not bound by previous decisions. At the same time they have also stated that they will take due account of previous cases when making their own decisions.[20] Tribunals frequently refer to and rely on earlier decisions but this has not always secured consistency.

An institutionalised solution carrying a high probability of uniformity of interpretation would be the creation of a centralised international investment court. At present, there is no indication that such a dramatic step is under serious discussion. Even in the unlikely event of agreement on a comprehensive multilateral agreement on investment, it is unclear whether his would involve the creation of a centralized form of adjudication.

Another idea that has been canvassed repeatedly is the creation of an appeals procedure.[21] Although the idea has appeared in a number of documents, it has not been implemented in practice. Any harmonizing effect would require an appeals body with wide competence that transcends individual treaties and covers proceedings under the ICSID, UNCITRAL, ICC and Stockholm Rules.

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[19] See *A. Rigo Sureda*, Precedent in Investment Treaty Arbitration, in: International Investment Law for the 21st Century, p. 830 (*C. Binder, U. Kriebaum, A. Reinisch, S. Wittich* eds., 2009).

[20] See e.g.: *Saipem* v. *Bangladesh,* Decision on Jurisdiction, 21 March 2007, para. 67; *RosInvest* v. *Russia*, Final Award, 12 September 2010, paras. 281-286.

[21] See *A. Reinisch*, The Future of Investment Arbitration, in: International Investment Law for the 21st Century, p. 910 (*C. Binder, U. Kriebaum, A. Reinisch, S. Wittich* eds., 2009).

An obvious obstacle to the establishment of an appeals procedure is Article 53(1) of the ICSID Convention which specifically excludes any form of appeal against an award.[22] An amendment of the ICSID Convention would require the acceptance by all States parties to the Convention which is close to impossible.[23] Also, appeal presupposes a decision that has been made already, that will be attacked for a perceived flaw and that may be revised and repaired.

Preliminary Rulings

The most effective way to achieve judicial coherence and consistency is not submitting decisions to review and reversal. An alternative to an appeals procedure would be the introduction of a system of preliminary rulings.[24] Rather than repair the damage after it has occurred, it is more sensible to address the problem of inconsistency through preventive action. The coherence of case law may be achieved more effectively and economically through an interim procedure while the original proceedings are still pending. Under such a system a tribunal would suspend proceedings and request a ruling on a question of law from a body established for that purpose.[25]

A mechanism of this kind would require the establishment of a central and permanent body that would be authorised to give preliminary rulings. A permanent body of this kind would be less ambitious than a permanent court for the adjudication of investment disputes. It would not do away with the basic structure of current investment arbitration consisting of a multitude of individual tribunals. But, if successfully used, it could guarantee a large

[22] Article 53(1) of the ICSID Convention provides in relevant part: "The award shall be binding on the parties and shall not be subject to any appeal or to any other remedy except those provided for in this Convention."

[23] Article 66 ICSID Convention.

[24] The idea has been put forward by *G. Kaufmann-Kohler*, Annulment of ICSID Awards in Contract and Treaty Arbitrations: Are there Differences?, in *E. Gaillard/Y. Banifatemi* (eds.), Annulment of ICSID Awards 289 (2004). See also *G. Kaufmann-Kohler,* In search of Transparency and Consistency: ICSID Reform Proposal, TDM, vol. 2, No. 5, p.8 (2005).

[25] For more detailed discussion see *C. Schreuer*, Preliminary Rulings in Investment Arbitration, *in*: Appeals Mechanism in International Investment Disputes (*K. Sauvant* ed.) 207 (2008).

measure of harmonization without depriving the tribunals of their basic competence to adjudicate the cases submitted to them.

Preliminary rulings would not affect the principle of finality. They would leave Article 53 of the ICSID Convention untouched.

Summary and Conclusions

International investment law suffers from a deficit of coherence and consistency. To a large extent this is caused by differences in treaties applicable to the relationships between host States and investors of different nationalities. This leads to different treatment of investors depending on their nationality. This *de facto* discrimination on the basis of nationality stands in marked contrast to the prohibition of discrimination reflected by substantive standards of protection.

MFN clauses may offer relief in some situations. But they require the existence of a third party treaty that offers better treatment. Also, many tribunals have approached MFN clauses with some trepidation. In particular, they have refused to apply them to provisions on the settlement of disputes.

Some investors have tried to avoid disadvantages based on nationality through appropriate corporate structuring. This technique requires foresight and advance planning. Also, it will only work in the presence of treaties that accept incorporation in a contracting State as a sufficient basis for protection.

An extension of investors' rights beyond the current system of mostly bilateral treaties is possible, at least theoretically. This could be achieved through the creation of a widely accepted multilateral treaty. Alternatively, States could follow the example of human rights treaties and grant substantive and procedural rights to investors regardless of nationality. Both solutions, while technically feasible, are not a realistic possibility in the near future.

Even without divergent treaty provisions tribunals have at times reached conflicting outcomes. Reliance on precedents, while useful, has not always been able to achieve uniformity of interpretation. The creation of a centralized investment court would be conducive to consistency. But under present circumstances this is not a realistic possibility. Appeals procedures have been discussed but never implemented. One of the reasons is a provision in the ICSID Convention that rules out appeals against awards.

The most realistic way to achieve consistency of interpretation would be the introduction of a preliminary rulings procedure while proceedings are still under way before the original tribunal. This would require the creation of a permanent institution to which tribunals would turn for guidance when confronted with contentious question.

There are several techniques to overcome inconsistencies in current international investment law. Some are more promising than others. All of them require a political will to do away with current inequalities. As it happens, the techniques with the highest potential for harmonization are also those that carry the least likelihood for their implementation.