

THE OXFORD HANDBOOK OF

INTERNATIONAL
ADJUDICATION

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OXFORD
UNIVERSITY PRESS



CHAPTER 14

INVESTMENT ARBITRATION

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1 THE FUNCTION OF INVESTMENT ARBITRATION IN INTERNATIONAL DISPUTE SETTLEMENT

ARBITRATION is the preferred method for the settlement of investment disputes between states and foreign investors. In its absence, investors would have to turn to domestic courts to seek a remedy against adverse action by the host state. From the investor's perspective, the host state's courts are not an attractive solution for several reasons. In many countries an independent judiciary cannot be taken for granted. Executive interventions in court proceedings or a sense of judicial loyalty to the forum state are likely to influence the outcome of proceedings. This is particularly so in cases involving large amounts of money. In addition, legislation is often the cause of complaints by investors. Domestic courts are typically bound to apply the local law even if it is at odds with international standards for the protection of investors. In fact, in some countries the relevant treaties containing these standards are not part of the domestic legal order. At times, domestic courts may be the perpetrators of the alleged violation of investor rights.

The courts of the investor's home country and of third states are usually not a viable alternative either. In most cases, they lack territorial jurisdiction over investments taking place in another state. An additional obstacle to the use of these courts is state immunity.

Under the traditional system of diplomatic protection the investor's state espouses the claim of its national and pursues it in its own name on the international plane against the host state. This system carries serious disadvantages for the protected investor. Diplomatic protection is discretionary: the investor has no right to it. The investor's state of nationality may refuse to pursue the claim or may abandon it at any stage. In addition, diplomatic protection requires the exhaustion of local remedies in the host state.

Diplomatic protection on behalf of investors also carries important disadvantages for the states concerned. It can constitute a serious strain on their relations. Developing countries, in particular, resent pressure from capital exporting countries, whether it is exercised bilaterally or in multilateral fora.

Arbitration provides a depoliticized international forum that is independent of the host state's judicial system. It may be initiated by the investor regardless of any decision of its home state. Investment arbitration carries advantages for both the investor and the host state. The advantage for the investor is obvious: it gains access to an effective international remedy. The advantage to the host state is two-fold: by offering an international procedure for dispute settlement it improves its

investment climate and is likely to attract more foreign investment. Also, by consenting to international arbitration the host state shields itself against other processes, notably diplomatic protection.

Investment arbitration uses a mechanism originally developed for the settlement of commercial disputes between private parties. But it has developed into an important branch of international adjudication. Investment arbitration involves two diverse parties, a sovereign state and a private investor. In the vast majority of cases the state is in the role of respondent and the investor is in the role of claimant.

The primary function of investment arbitration is an examination of the legality of state action vis-à-vis foreign investors. This may involve the scrutiny of the activity of all branches of the government: executive, judiciary, and legislature. In the exercise of this function, investment tribunals apply a variety of international law rules stemming from all fields of international law. Apart from specific treaties, the rules on treaty interpretation and questions of state responsibility are particularly prominent.

A distinctive feature of investment arbitration is its ad hoc nature: each tribunal is specifically constituted for the particular dispute. The parties to the dispute play a major role in the composition of tribunals. This goes considerably beyond the appointment of an ad hoc judge. A typical investment tribunal is composed of two party appointees and a president who is appointed by agreement of the parties. Alternatively, the president may be appointed by the two party appointed arbitrators or by an appointing authority. This method of appointment is designed to strengthen the confidence of the parties in the arbitral process. But the ad hoc nature of tribunals also has a serious effect on the coherence of the system and the consistency of decisions.¹

Investment arbitration has developed into a particularly active form of international adjudication. Hundreds of cases are pending and there is a constant stream of decisions by investment tribunals. These decisions play an important role in the practice of international law.

2 ARBITRATION INSTITUTIONS, RULES, AND REGIMES

Arbitration between a host state and a foreign investor may take place in the framework of a variety of institutions or rules. Exceptionally, arbitration may take place unsupported by a particular arbitration institution.

¹ On coherence and consistency, see section 14.1 of this chapter.

2.1 International Centre for Settlement of Investment Disputes (ICSID)

Nowadays the majority of investment arbitrations take place under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States.² The convention was drafted in the framework of the World Bank in Washington and entered into force on October 14, 1966. It created the International Centre for Settlement of Investment Disputes (ICSID, the Centre). This is why the convention is commonly referred to as the ICSID Convention or the Washington Convention. By mid-2012 the convention had 147 parties.³

ICSID provides a system of dispute settlement for investor–state disputes. It offers standard clauses for the use of the parties, detailed rules of procedure, and institutional support.⁴ The ICSID Convention offers a procedural framework for arbitration. It does not contain substantive rules on the protection of foreign investments. The Centre has its headquarters in Washington, D.C. It is a permanent administrative body but not a court. Arbitral tribunals are constituted separately for each case. The seat of a tribunal is to be fixed by agreement between the parties and the tribunal after consultation with the Secretary-General of ICSID.

The jurisdiction of ICSID requires an investment dispute of a legal nature between a state party to the convention and a national of another state party to the convention. In addition, both parties to the dispute (the host state and the investor) must have consented to ICSID's jurisdiction.⁵ Proceedings under the ICSID Convention are independent of the intervention of any outside bodies. In particular, domestic courts do not have the power to stay, to compel, or to otherwise influence ICSID proceedings. Also, domestic courts do not have the power to set aside or otherwise review ICSID awards.

ICSID had a slow start. The first case was not registered before 1972. The 1970s and 1980s saw steady but only intermittent action: one or two cases per year were typical for that period. Since the mid-1990s there has been a dramatic increase in activity. In 1995 there were four ICSID arbitrations pending. At the beginning of 2013 there were 166 cases pending. During 2012 the Secretary-General registered 40 new cases.

² 575 UNTS 159; 4 ILM 524 (1965). For detailed information, see <<https://icsid.worldbank.org/ICSID/Index.jsp>> accessed May 16, 2013.

³ Three states have terminated their participation by denouncing the ICSID Convention in accordance with its Art. 71: Bolivia on May 2, 2007, Ecuador on July 6, 2009, Venezuela on January 24, 2012.

⁴ For a concise overview see L Reed, J Paulsson, and N Blackaby, *Guide to ICSID Arbitration* (2nd edn, The Hague, London, New York: Kluwer 2011). For more detail see C Schreuer et al., *The ICSID Convention: A Commentary* (2nd edn, Cambridge University Press 2009).

⁵ ICSID Convention, Art. 25. For a more detailed treatment of consent to arbitration see section 5 of this chapter.

2.2 ICSID Additional Facility

In 1978 the Administrative Council of ICSID created the Additional Facility. It is open to parties that submit to its jurisdiction in certain cases that are outside ICSID's jurisdiction. The most important situation involves cases where either the host state or the investor's home state is not a party to the ICSID Convention. This has become especially important in the context of the North American Free Trade Agreement (NAFTA) since only the United States has ratified the ICSID Convention but Canada and Mexico have not.

Additional Facility proceedings receive institutional support from ICSID in a similar way as proceedings under the ICSID Convention. Arbitration under the Additional Facility is not governed by the ICSID Convention but by separate Additional Facility Rules. This means, in particular, that the ICSID Convention's provisions on the recognition and enforcement of awards are not applicable to awards rendered under the Additional Facility.

2.3 Other arbitration institutions

Institutions that deal primarily with commercial arbitration between private parties are also available, in principle, for investor–state arbitration. These include the International Chamber of Commerce; the London Court of International Arbitration (LCIA); the Arbitration Institute of the Stockholm Chamber of Commerce; Regional Arbitration Centres in Frankfurt, Vienna, Cairo, Kuala Lumpur, and Hong Kong; or the China International Economic and Trade Arbitration Commission (CIETAC). In current practice such arbitrations are often conducted under the UNCITRAL Arbitration Rules of 1976 (revised in 2010) and under the International Chamber of Commerce's Arbitration Rules of 1998 (revised in 2011). In addition, the Permanent Court of Arbitration (PCA) administers investment arbitrations.⁶

3 THE SUBJECT MATTER OF INVESTMENT DISPUTES

Under the ICSID Convention, jurisdiction is limited to legal disputes arising directly out of an investment. But the convention does not define the notion of investment. This has led to much debate and controversy. Most treaties providing

⁶ At the beginning of 2013 there were about 50 investment arbitrations pending in proceedings administered by the PCA.

for investment arbitration contain broad definitions of “investment.” These definitions include tangible and intangible property, participation in companies, claims to money, claims to performance, and intellectual property, as well as rights conferred by law or contract.

Tribunals have identified a number of typical elements for the concept of investment for purposes of the ICSID Convention. These include a substantial commitment, certain duration, risk, and, less clearly, a contribution to the host state’s development. The significance of these definitional elements is disputed among tribunals.⁷

Tribunals have emphasized the unity of the overall investment operation. What matters is not so much ownership of specific assets but rather the combination of rights that is necessary for the economic activity that constitutes the investment. An investment is typically a complex operation composed of a number of elements each of which on its own may not qualify as an investment.⁸

The classical issue in investment disputes is expropriation and the resulting duty to pay compensation. More recently, additional standards of treatment have gained in importance. These are mostly contained in treaties, especially in bilateral investment treaties (BITs) and some multilateral treaties such as the NAFTA and the Energy Charter Treaty (ECT). These standards include fair and equitable treatment, full protection and security, protection against arbitrary and discriminatory treatment, national treatment, and most favoured nation (MFN) treatment.

4 THE PARTIES TO THE INVESTMENT ARBITRATION

Investment arbitration involves a sovereign state (the host state) on one side and a private, foreign investor on the other. In many cases, it is not the state as such that deals with a foreign investor but a territorial subdivision such as a province or

⁷ *Salini v. Morocco* (Decision on Jurisdiction) [July 23, 2001] para. 56; *Malaysian Historical Salvors v. Malaysia* (Decision on Annulment) [April 16, 2009] paras 56–81; *Pantechniki v. Albania* (Award) [July 30, 2009] paras 42–4; *Inmaris v. Ukraine* (Decision on Jurisdiction) [March 8, 2010] paras 126–34; *Fakes v. Turkey* (Award) [July 14, 2010] paras 99–113; *Alpha v. Ukraine* (Award) [November 8, 2010] paras 310–32; *Abaclat v. Argentina* (Decision on Jurisdiction) [August 4, 2011] paras 362–71; *Quiborax v. Bolivia* (Decision on Jurisdiction) [September 27, 2012] paras 218–37.

⁸ *CSOB v. Slovakia* (Decision on Jurisdiction) [May 24, 1999] para. 72; *Enron v. Argentina* [January 14, 2004] para. 70; *Joy Mining v. Egypt* (Award) [August 6, 2004] para. 54; *Mitchell v. Congo* (Decision on Annulment) [November 1, 2006] para. 38; *Duke Energy v. Peru* (Decision on Jurisdiction) [February 1, 2006] para. 92; *Saipem v. Bangladesh* (Decision on Jurisdiction) [March 21, 2007] paras 110, 114.

municipality or a state entity. Under the rules of state responsibility, acts of territorial subdivisions will be attributed to the state. Where the state acts through a separate entity, attribution will depend on whether the entity exercises governmental authority or is directed or controlled by the state.⁹

In principle, only the state itself has party status in investment arbitration. But under Art. 25 of the ICSID Convention a state's constituent subdivision or agency may become a party to proceedings if so authorized by the state.¹⁰

Investment arbitration is designed for the protection of private investors. This would indicate that the investor must be a private individual or corporation. But state-owned corporations and state entities may be accepted as investors if they act in a private commercial capacity.¹¹

It has always been beyond doubt that arbitral proceedings are open to more than one claimant in one and the same case. The practice under the ICSID Convention shows numerous proceedings with more than one party on the claimants' side. More recently, this has led to mass claims involving thousands of claimants in connection with defaults under government bonds.¹²

The investor's nationality is relevant for several purposes. In order to gain access to dispute settlement under the ICSID Convention, the investor must not be a national of the host state but must be a national of another state party to the ICSID Convention.¹³ To rely on a clause in a treaty that offers consent to arbitration the investor must have the nationality of one of the states parties to that treaty.

An individual's nationality is determined by the law of the state whose nationality is claimed. An investment tribunal need not unquestioningly accept a passport or certificate of nationality as proof of nationality.¹⁴

For juridical persons the decisive criterion to determine nationality is the place of incorporation or registration.¹⁵ The place of the *siège social* (corporation's seat) may also be relevant to determine its nationality. Control of the company, for instance

⁹ See Arts 4, 5, 8 of the International Law Commission's Articles on State Responsibility.

¹⁰ The Convention requires that the constituent subdivision or agency be designated to ICSID. ICSID maintains a public register of designated subdivisions and agencies of states, but relatively few countries have made designations under this provision. Constituent subdivisions or agencies have played a limited role in ICSID practice. See *Cable Television v. St Kitts and Nevis* (Award) [January 13, 1997]; *Tanzania Electric v. Independent Power Tanzania* (Award) [July 12, 2001] para. 13; *Repsol v. Petroecuador* (Decision on Annulment) [January 8, 2007]; *Noble Energy v. Ecuador* (Decision on Jurisdiction) [March 5, 2008] para. 6.

¹¹ *CSOB v. Slovakia* (Decision on Jurisdiction) [May 24, 1999] paras 15–27; *Telenor v. Hungary* (Award) [September 13, 2006] para. 16; *Rumeli Telekom v. Kazakhstan* (Award) [July 29, 2008] paras 325–8.

¹² *Abaclat et al v. Argentina* (Decision on Jurisdiction) [August 4, 2011] paras 216, 294–8, 480–92, 506–51.

¹³ Exceptionally, under Art. 25.2.b of the ICSID Convention a corporation registered in the host state may be treated as a foreign company for the purposes of the ICSID Convention if, because of its foreign control, the parties to the dispute have so agreed.

¹⁴ *Soufraki v. United Arab Emirates* (Award) [July 7, 2004].

¹⁵ *Tokios Tokelès v. Ukraine* (Decision on Jurisdiction) [April 29, 2004] paras 21–71; *Saluka v. Czech Republic* (Partial Award) [March 17, 2006] paras 1, 73, 183–6, 197, 240, 241.

through majority ownership, is relevant only in exceptional circumstances. This would be the case if the relevant treaty requires effective control over the corporation by nationals of the state whose nationality is claimed or a genuine economic activity in that state.¹⁶

Nationality planning through the establishment of a corporation in a state that has favourable treaty relations with the host state is possible and accepted, in principle.¹⁷ But it will work only if it is undertaken before the outbreak of a dispute with the host state.¹⁸ Some states counteract practices of this kind through so-called denial of benefits clauses such as Art. 17.1 of the Energy Charter Treaty. Under such a clause, the states reserve the right to deny the benefits of the treaty to a company that does not have an economic connection to the state whose nationality it claims.¹⁹

The nationality of corporate investors has somewhat lost importance through the generous granting of standing to shareholders. Most investment treaties include shareholding or participation in companies in their definitions of investment. In this way, it is not the company that is seen as the investor but the shareholder whose participation in the company becomes the investment. The foreign shareholder may then pursue claims for unlawful action by the host state that affects the company's value and profitability. This practice is particularly relevant where the company is incorporated in the host state.²⁰

5 CONSENT TO ARBITRATION

5.1 Different forms of consent: contracts, legislation, and treaties

Arbitration is always based on an agreement between the disputing parties. In practice, consent to investment arbitration is given in one of three ways: (i) a consent clause may be included in a direct agreement between the investor and the host

¹⁶ *Champion Trading v. Egypt* (Decision on Jurisdiction) [October 21, 2003] sec 3.4.2.

¹⁷ *Aguas del Tunari v. Bolivia* (Decision on Jurisdiction) [October 21, 2005] paras 330–2.

¹⁸ *Mobil v. Venezuela* (Decision on Jurisdiction) [June 10, 2010] paras 200, 201.

¹⁹ *Plama v. Bulgaria* (Award) [August 27, 2008] paras 77–95; *Petrobart v. Kyrgyz Republic* (Award) [March 29, 2005], (2005) 3 Stockholm Intl Arb Rev 45, 64; *AMTO v. Ukraine* (Award) [March 26, 2008] paras 59–69; *Libananco v. Turkey* (Award) [September 2, 2011] paras 549–56.

²⁰ See e.g.: *Genin v. Estonia* (Award) [June 25, 2001] para. 324; *CMS v. Argentina* (Decision on Jurisdiction) [July 17, 2003] paras 36–48; *LG&E Energy v. Argentina* (Decision on Jurisdiction) [April 30, 2004] paras 50–63; *GAMI v. Mexico* (Award) [November 15, 2004] paras 33–5; *Sempre Energy v. Argentina* (Decision on Jurisdiction) [May 11, 2005] paras 92–4; *El Paso Energy v. Argentina* (Decision

state; (ii) a provision in the host state's national legislation may offer arbitration to foreign investors in general terms; (iii) a treaty between the host state and the investor's state of nationality may offer arbitration to the nationals of the respective states.

An agreement between the parties recording consent to arbitration may be achieved through a compromissory clause in an investment agreement between the host state and the investor submitting future disputes arising from the investment operation to arbitration. Consent may be given with respect to existing or future disputes.²¹

The host state may offer consent to arbitration to foreign investors in its legislation in general terms. Not every reference to investment arbitration in national legislation, however, amounts to consent to jurisdiction. Some provisions are unclear and have led to disputes as to whether the host state had given its consent.²²

A legislative provision containing consent to arbitration is merely an offer by the state to investors. In order to perfect an arbitration agreement that offer must be accepted by the investor. The investor may accept the offer simply by instituting arbitration.²³ The host state may repeal its offer at any time before it is accepted.²⁴

By far the largest number of investment arbitrations is based on clauses in BITs offering arbitration. Through these clauses the states parties to the BIT offer consent to arbitration to investors who are nationals of the other contracting party. The arbitration agreement is perfected through the acceptance of that offer by an eligible investor. Most investor–state dispute settlement clauses in BITs offer unequivocal consent to arbitration.²⁵ But some clauses in BITs referring to arbitration merely hold out a promise or a prospect of future consent.

A number of regional multilateral treaties also offer consent to investment arbitration. These offers are also subject to an acceptance on the part of the investor. Article 1122 of the NAFTA contains such an offer. Article 1120 of the NAFTA specifies that an investor may submit a claim to arbitration under the ICSID Convention, under the ICSID Additional Facility Rules, or under the UNCITRAL Arbitration Rules. Of the three NAFTA States, only the United States has ratified the ICSID Convention while Canada and Mexico have not. Therefore, at present ICSID arbitration under the NAFTA is impossible.

on Jurisdiction) [April 27, 2006] para. 138; *Phoenix v. Czech Republic* (Award) [April 15, 2009] paras 121–3; *Hochtief v. Argentina* (Decision on Jurisdiction) [October 24, 2011] paras 112–19.

²¹ Agreements to submit existing disputes to arbitration are rare. But see *MINE v. Guinea* (Award) [January 6, 1988] 4 ICSID Rep 61, 67; *Compania del Desarrollo de Santa Elena SA v. Costa Rica* (Award) [February 17, 2000] para. 26.

²² *Mobil v. Venezuela* (Decision on Jurisdiction) [June 10, 2010] paras 67–140; *CEMEX v. Venezuela* (Decision on Jurisdiction) [December 30, 2010] paras 63–139; *Brandes v. Venezuela* (Award) [August 2, 2011] paras 79–118.

²³ *Tradex v. Albania* (Decision on Jurisdiction) [December 24, 1996] 5 ICSID Rep 47, 63; *Zhinvali v. Georgia* (Award) [January 24, 2003] para. 342.

²⁴ *SPP v. Egypt* (Decision on Jurisdiction) (I) [November 27, 1985] para. 40.

²⁵ *RosInvest v. Russia* (Award on Jurisdiction) [October 1, 2007] paras 56–75.

Similarly, the ECT in Art. 26 provides consent to investment arbitration. Under the ECT the investor may submit the dispute to arbitration under the ICSID Convention, the ICSID Additional Facility Rules, the UNCITRAL Arbitration Rules, or under the Arbitration Institute of the Stockholm Chamber of Commerce.

A provision of consent to arbitration in a treaty is merely an offer by the respective states that requires acceptance by the other party. That offer may be accepted by a national of the other state party to the BIT. An investor may accept an offer of consent contained in a treaty simply by instituting ICSID proceedings.²⁶

In the case of arbitration clauses contained in treaties, a withdrawal of an offer of consent before its acceptance would be more difficult than in the case of national legislation. Once the arbitration agreement is perfected through the acceptance of the offer contained in the treaty, it remains in existence even if the states parties to the BIT agree to amend or terminate the treaty.

5.2 The scope of consent

The scope of consent to arbitration offered in treaties varies. Many BITs refer to “disputes concerning investments” or “any legal dispute concerning an investment.” These provisions do not restrict a tribunal’s jurisdiction to claims arising from the BIT’s substantive standards. By their own terms, these consent clauses encompass disputes that go beyond the interpretation and application of the BIT itself and would include disputes that arise from a contract in connection with the investment.²⁷

Other BITs contain a more limited offer of consent to arbitration covering only violations of the BIT’s substantive standards. Similarly, under Art. 1116 of the NAFTA, the scope of the consent to arbitration is limited to claims arising from alleged breaches of the NAFTA itself. Also, under Art. 26.1 of the ECT the scope of the consent is limited to claims arising from alleged breaches of the ECT.²⁸

Some expressions of consent to arbitration are narrowly confined as to their subject matter. Typical examples for narrow clauses of this kind are expressions of consent that are limited to disputes relating to expropriations or to the amount of compensation for expropriations.²⁹

²⁶ *Toto v. Lebanon* (Decision on Jurisdiction) [September 11, 2009] para. 94; *Generation Ukraine v. Ukraine* (Award) [September 16, 2003] paras 12.2, 12.3.

²⁷ *Salini v. Morocco* (Decision on Jurisdiction) [July 23, 2001] para. 61; *Compañía de Aguas del Aconquija, SA & Vivendi Universal v. Argentina* (Decision on Annulment) [July 3, 2002] para. 55; *SGS v. Philippines* (Decision on Jurisdiction) [January 29, 2004] paras 131–5; *Chevron & Texaco v. Ecuador* (Interim Award) [December 1, 2008] paras 203, 209–211; *SGS v. Paraguay* (Decision on Jurisdiction) [February 12, 2010] paras 129, 183; *Alpha v. Ukraine* (Award) [November 8, 2010] para. 243.

²⁸ *Kardassopoulos v. Georgia* (Decision on Jurisdiction) [July 6, 2007] paras 249–51.

²⁹ *Telenor v. Hungary* (Award) [September 13, 2006] paras 18.2, 25, 57, 81–3; *ADC v. Hungary* (Award) [October 2, 2006] paras 12, 445; *Tza Yap Shum v. Peru* (Decision on Jurisdiction) [June 19, 2009] paras 129–88; *Saipem v. Bangladesh* (Award) [June 30, 2009] paras 120–32.

6 PROCEDURAL REQUIREMENTS FOR THE INSTITUTION OF PROCEEDINGS

6.1 Attempt at amicable settlement

A common condition in treaties providing for investor–state arbitration is a prior attempt at amicable settlement through negotiations within a certain period of time. A typical waiting period under BITs would be six months. The NAFTA (Arts 1118 to 1120) also prescribes a waiting period of six months since the events giving rise to the claim. Article 26.2 of the ECT offers consent to arbitration if the dispute cannot be settled within three months from the date on which either party requested amicable settlement.

The reaction of tribunals to non-compliance with these waiting periods has varied. In some cases the tribunals found that non-compliance with the waiting periods did not affect their jurisdiction.³⁰ Other tribunals have found the claims inadmissible under these circumstances.³¹ A compromise solution is to suspend proceedings to allow additional time for negotiations if these appear promising.

6.2 Requirement to resort to domestic courts

Where consent has been given to investor–state arbitration, there is generally no need to exhaust local remedies.³² One of the purposes of investor–state arbitration is to avoid the vagaries of proceedings in the host state’s courts. Article 26 of the ICSID Convention specifically excludes the requirement to exhaust remedies “unless otherwise stated.”

Some BITs provide that before an investor may bring a dispute before an international tribunal he or she must seek its resolution before the host state’s domestic courts for a certain period of time, often 18 months. In practice, investors are often able to avoid the application of such a rule by invoking an MFN clause in the BIT.

³⁰ *Ethyl Corp v. Canada* (Decision on Jurisdiction) [June 24, 1998] paras 76–88; *Lauder v. Czech Republic* (Final Award) [September 3, 2001] para. 187; *SGS v. Pakistan* (Decision on Jurisdiction) [August 6, 2003] para. 184; *Bayindir v. Pakistan* (Decision on Jurisdiction) [November 14, 2005] paras 88–103; *Biwater Gauff v. Tanzania*, (Award) [July 24, 2008] paras 338–50.

³¹ *Goetz v. Burundi* (Award) [February 10, 1999] paras 90–3; *Enron v. Argentina* (Decision on Jurisdiction) [January 14, 2004] para. 88; *Wintershall v. Argentina* (Award) [December 8, 2008] paras 133–57; *Burlington Resources v. Ecuador* (Decision on Jurisdiction) [June 2, 2010] paras 312–18, 332–40; *Murphy v. Ecuador* (Award) [December 15, 2010] paras 90–157.

³² *Amco v. Indonesia* (Decision on Annulment) [May 16, 1986] para. 63; *Lanco v. Argentina* (Decision on Jurisdiction) [December 8, 1998] para. 39; *IBM v. Ecuador* (Decision on Jurisdiction) [December 22, 2003] paras 77–84; *AES v. Argentina* (Decision on Jurisdiction) [April 26, 2005] paras 69, 70; *Saipem v. Bangladesh* (Award) [June 30, 2009] paras 174–84.

This allows them to rely on other BITs of the host state that do not contain that requirement.³³ In some cases tribunals have discarded the treaty requirement to first go to domestic courts because such an attempt would have been evidently futile.³⁴

6.3 Fork in the road

Fork in the road clauses provide that the investor must choose between the litigation of its claims in the host state's domestic courts or through international arbitration and that the choice, once made, is final.

Not every appearance before a court or tribunal of the host state will constitute a choice under a fork in the road provision. Tribunals have held that the loss of access to international arbitration under a fork in the road clause applies only if the same dispute involving the same cause of action between the same parties has been submitted to the domestic courts of the host state.³⁵

7 THE APPLICABILITY OF MFN CLAUSES TO DISPUTE SETTLEMENT

Most BITs and some other treaties for the protection of investment, including the NAFTA and the ECT, contain MFN clauses. An MFN clause contained in a treaty will extend the better treatment granted to a third state or its nationals to a

³³ *Maffezini v. Spain* (Decision on Jurisdiction) [January 25, 2000] paras 54–64; *Siemens v. Argentina* (Decision on Jurisdiction) [August 3, 2004] paras 32–110; *Gas Natural SDG, SA v. Argentina* (Decision on Jurisdiction) [June 17, 2005] paras 24–49; *Suez, Sociedad General de Aguas de Barcelona SA, and InterAguas Servicios Integrales del Agua SA v. Argentina* (Decision on Jurisdiction) [May 16, 2006] paras 52–66; *National Grid plc v. Argentina* (Decision on Jurisdiction) [June 20, 2006] paras 80–93; *Suez, Sociedad General de Aguas de Barcelona SA, and Vivendi Universal SA v. Argentina and AWG Group Ltd v. Argentina* (Decision on Jurisdiction) [August 3, 2006] paras 52–68; *Impregilo v. Argentina* (Award) [June 21, 2011] paras 51–109; *Hochtief v. Argentina* (Decision on Jurisdiction) [October 24, 2011]; *Teinver v. Argentina* (Decision on Jurisdiction) [December 21, 2012] paras 137–86. But see *Wintershall v. Argentina* (Award) [December 8, 2008] paras 158–97; *ICS Inspection v. Argentina* (Award) [February 10, 2012] paras 243–327; *Daimler v. Argentina* (Award) [August 22, 2012] paras 160–281.

³⁴ *Abuclat v. Argentina* (Decision on Jurisdiction and Admissibility) [August 4, 2011] paras 585–90; *Urbaser v. Argentina* (Decision on Jurisdiction) [December 19, 2012] paras 196–200; *Ambiente Ufficio v. Argentina* (Decision on Jurisdiction and Admissibility) [February 8, 2013] paras 589–628.

³⁵ *CMS v. Argentina*, note 20 at paras 77–82; *LG&E v. Argentina*, note 20, at paras 75, 76; *Champion Trading v. Egypt*, note 16, at sec. 3.4.3; *Pan American v. Argentina* (Decision on Preliminary Objections) [July 27, 2006] paras 155–7; *Toto v. Lebanon* (Decision on Jurisdiction) [September 11, 2009] paras

beneficiary of the treaty. This has led to the question whether the effect of a generally worded MFN clause extends to the arbitration clauses in these treaties.

This issue has led to much controversy and to conflicting decisions. One school of thought regards dispute settlement as an essential aspect of the treatment that is covered by an MFN clause. A different approach distinguishes between substantive and procedural questions restricting the effect of MFN treatment to substance.

Most of the cases in which the tribunals have accepted the applicability of the MFN clauses to dispute settlement concerned procedural obstacles, such as the requirement first to resort to the domestic courts for 18 months.³⁶ Most of the cases in which the effect of the MFN clauses was denied concerned attempts to extend the scope of jurisdiction substantively to issues not covered by the arbitration clauses in the basic treaties.³⁷ Nevertheless, there is substantial contradiction in the reasoning of the tribunals. In particular, both groups of tribunals made broad statements as to the applicability, or otherwise, of MFN clauses to dispute settlement that are impossible to reconcile.

8 SELECTION OF DOMESTIC COURTS IN CONTRACTS

Contracts between host states and foreign investors often contain forum selection clauses referring disputes arising from the application of these contracts to the host states' domestic courts. When disputes in connection with the investments arose, investors would invoke the provisions of treaties, usually BITs, granting them access to international arbitration. In turn, the host states would rely on the forum selection clauses in the contracts, arguing that the investors had waived their right to international arbitration.

The tribunals have adopted a distinction between contract claims, which are subject to contractual forum selection clauses, and treaty claims, which are unaffected

203–17; *Victor Pey Casado v. Chile* (Award) [May 8, 2008] paras 467–98; *Total v. Argentina* (Decision on Liability) [December 27, 2010] paras 442–3.

³⁶ See note 33.

³⁷ *Salini v. Jordan* (Decision on Jurisdiction) [November 29, 2004] para. 119; *Plama v. Bulgaria* (Decision on Jurisdiction) [February 8, 2005] paras 183–227; *Berschader v. Russia* (Award) [April 21, 2006] paras 159–208; *Telenor v. Hungary* (Award) [September 13, 2006] paras 83–100; *Tza Yap Shum v. Peru* (Decision on Jurisdiction) [June 19, 2009] paras 189–220; *Austrian Airlines v. Slovakia* (Final Award) [October 9, 2009] paras 109–40. But see *RosInvest v. Russia* (Award on Jurisdiction) [October 2007] paras 124–39.

by such clauses. Under this consistent practice the treaty-based jurisdiction of international arbitral tribunals to decide on violations of these treaties is not affected by domestic forum selection clauses in contracts. The contractual selection of domestic courts is restricted to violations of the respective contracts.³⁸

A particular course of action by the host state may well constitute a breach of contract and a violation of international law. The two categories are not mutually exclusive. Rather, two different standards must be applied to determine whether one or the other or both have been violated.

The situation is made even more complex by the fact that some treaties offer jurisdiction for investment disputes in general terms, which includes contract claims. Therefore the jurisdiction of treaty-based tribunals is not necessarily restricted to violations of the treaty's substantive provisions.

The separate treatment of contract claims and treaty claims leads to situations where the claimant may be compelled to pursue part of its claim through national and another part through international procedures. This has undesirable consequences. The need to dissect cases into contract claims and treaty claims to be dealt with by separate fora requires claim-splitting and has the potential of leading to parallel proceedings. This is uneconomical and contrary to the goal of reaching final and comprehensive resolutions of disputes.

9 APPLICABLE LAW

Investments typically are complex operations involving numerous transactions under the host state's local law. These transactions will have their closest connection to the host state's legal system. At the same time, there is a considerable body of substantive international law protecting foreign investors. It consists of treaty law, contained mostly in BITs, but also in multilateral treaties such as the NAFTA and the ECT. In addition, other treaties and customary international law remains

³⁸ *Compañía de Aguas del Aconquija, SA & Vivendi Universal v. Argentina*, note 27, at paras 60, 72, 76, 95, 96, 101, 103; *National Grid plc v. Argentina* (Decision on Jurisdiction) [June 20, 2006] paras 167–70; *Inceysa v. El Salvador* (Award) [August 2, 2006] paras 43, 212–17; *Total v. Argentina* (Decision on Jurisdiction) [August 25, 2006] paras 82–5; *Fraport v. Philippines* (Award) [August 16, 2007] paras 388–91; *Vivendi v. Argentina* (Resubmitted Case: Award) [August 20, 2007] paras 73.–73.11; *Helnan v. Egypt* (Award) [July 3, 2008] paras 102–3; *TSA Spectrum v. Argentina* (Award) [December 19, 2008] paras 42–66; *Enron v. Argentina* (Decision on Annulment) [July 30, 2010] paras 128–50; *Impregilo v. Argentina* (Award) [June 21, 2011] paras 141–89; *SGS v. Paraguay* (Award) [February 10, 2012] paras 75, 96–109.

relevant to various questions, including state responsibility, nationality, or the international minimum standard.

Some treaties providing for investment arbitration refer to the parties' agreement on choice of law. Some of the relevant treaties contain their own choice of law clauses in case there is no agreement on applicable law between the parties. For instance, Art. 42 of the ICSID Convention refers primarily to any agreement on choice of law that the parties may have reached. In the absence of such an agreement, it provides for the application of the host state's law and international law.³⁹

In non-ICSID arbitration between investors and host states, tribunals also apply a combination of international law and host state law. The UNCITRAL Arbitration Rules refer the tribunal to the law designated by the parties. In the absence of a choice of law, the tribunal is to apply the law that it determines to be appropriate.⁴⁰

Many of the treaties that offer investor–state arbitration, such as the NAFTA, the ECT, and some BITs, also contain provisions on applicable law. Some of these provisions, including Art. 1131 of the NAFTA and Art. 26 of the ECT, refer exclusively to international law. Some BIT provisions dealing with applicable law, combine the host state's domestic law with international law.⁴¹ Where jurisdiction is based on a BIT that does not contain a provision on governing law, tribunals have sometimes construed such a choice from the parties' reliance on the BIT.⁴²

In most cases the applicable substantive law in investment arbitration combines international law and host state law. This is so whether or not the parties have made a choice of law that combines international law with host state law. In the majority of cases tribunals have, in fact, applied both systems of law.⁴³ Host state law is particularly important to determine the existence and the legality of investments. Where there was a contradiction between the two, international law had to prevail.⁴⁴ It is

³⁹ See also Art. 54 of the ICSID Additional Facility Rules.

⁴⁰ UNCITRAL Arbitration Rules 2010, Art. 35.1.

⁴¹ *Antoine Goetz v. Burundi* (Award) [February 10, 1999] paras 95–133; *Maffezini v. Spain* (Award) [November 13, 2000] paras 47–50, 52, 57, 67–69, 71, 77, 83, 89–93; *Occidental v. Ecuador* (Final Award) [July 1, 2004] para. 93; *Eastern Sugar v. Czech Republic* (Partial Award) [March 27, 2007] paras 191–7. *BG Group v. Argentina* (Final Award) [December 24, 2007] paras 89–103; *National Grid v. Argentina* (Award) [November 3, 2008] paras 81–90.

⁴² *AAPL v. Sri Lanka* (Award) [June 27, 1990] paras 18–24; *Wena Hotels v. Egypt* (Award) [December 8, 2000] paras 78, 79; *ADC v. Hungary* (Award) [October 2, 2006] paras 288–91; *LG&E v. Argentina* (Decision on Liability) [October 3, 2006] paras 85, 97–8; *Saipem v. Bangladesh* (Award) [June 30, 2009] para. 99; *Bayindir v. Pakistan* (Award) [August 27, 2009] paras 109, 110.

⁴³ *CMS v. Argentina* (Award) [May 12, 2005] para. 117. See also, *Wena v. Egypt* (Decision on Annulment) [February 5, 2002] paras 37–40; *Azurix v. Argentina* (Award) [July 14, 2006] para. 67; *LG&E v. Argentina*, note 42, at paras 82–99; *Enron v. Argentina* (Award) [May 22, 2007] paras 203–9; *Tokios Tokelès v. Ukraine* (Award) [July 26, 2007] paras 138–45; *Sempra v. Argentina* (Award) [September 28, 2007] paras 231–40.

⁴⁴ *LG&E v. Argentina*, note 42, at para. 94; *CDSE v. Costa Rica* (Award) [February 17, 2000] paras 64, 65; *Duke Energy v. Peru* (Decision on Jurisdiction) [February 1, 2006] para. 162.

left to the tribunals to classify the various issues before them as to which international law or host state law is to apply.

10 REMEDIES

Under the international law of state responsibility, reparation for a wrongful act takes the form of restitution, compensation, and satisfaction.⁴⁵ In investment arbitration the remedy nearly always consists of monetary compensation. Restitution in kind or specific performance is ordered infrequently.⁴⁶ Satisfaction also plays a subordinate role in investment arbitration.⁴⁷

If an illegal act has been committed the guiding principle is that reparation must, as far as possible, restore the situation that would have existed had the illegal act not been committed. Under this principle, damages for a violation of international law have to reflect the damage actually suffered by the victim. Therefore, punitive or moral damages will not usually be granted.⁴⁸ Lost profits will be awarded only if they are not speculative, that is, in cases where the investment has a record of profitability or there are other clear indicators of future profits.

The calculation of compensation for a lawful expropriation follows different standards. Many of the treaties dealing with compensation for expropriation refer to the expropriated investment's fair market value immediately before the expropriation became publicly known.

An award of damages or compensation normally includes interest. Interest is due from the date at which the principal amount was due. In the case of damages, this is normally the date of the wrongful act. In the case of compensation, interest is due normally from the date of the expropriation. The rate of interest is usually

⁴⁵ Art. 34 of the International Law Commission's Articles on State Responsibility.

⁴⁶ *Texaco v. Libya* (Award on the Merits) [January 19, 1977] 53 ILR 389, 497–511; *Goetz v. Burundi* (Award) [September 2, 1998 and February 10, 1999] paras 132–3; *Semos v. Mali* (Award) [February 25, 2003]; *Enron v. Argentina* (Decision on Jurisdiction) [January 14, 2004] paras 76–9; *ADC v. Hungary* (Award) [October 2, 2006] para. 523; *Siemens v. Argentina* (Award) [February 6, 2007] para. 403.5; *Micula v. Romania* (Decision on Jurisdiction and Admissibility) [September 24, 2008] paras 158–68; *ATA v. Jordan* (Award) [May 18, 2010] paras 129–32.

⁴⁷ *Biwater Gauff v. Tanzania* (Award) [July 24, 2008] paras 465–67, 807; *Europe Cement v. Turkey* (Award) [August 13, 2009] paras 146–8, 176, 181; *Quiborax v. Bolivia* (Decision on Jurisdiction) [September 27, 2012] paras 37, 299–308.

⁴⁸ *Siag v. Egypt* (Award) [June 1, 2009] paras 544–8; *Europe Cement v. Turkey*, note 47, at paras 177–81; *Cementownia v. Turkey* (Award) [September 17, 2009] paras 164–72; *Lemire v. Ukraine* (Decision on Jurisdiction and Liability) [January 14, 2010] paras 426–86. But see *Desert Line v. Yemen* (Award) [February 6, 2008] paras 284–91.

calculated on the basis of the legal interest rate in an applicable legal system or some inter-bank rate such as the London Interbank Offered Rate (LIBOR). The practice of tribunals shows a trend toward compounding interest.

11 COSTS

The costs of major investment arbitrations can be considerable and may run into millions of US dollars for complex cases. The costs consist of three elements: the charges for the use of the facilities and expenses of ICSID or any other arbitration institution, the fees and expenses of the arbitrators, and the expenses incurred by the parties in connection with the proceedings. Of these three categories, the third, consisting mainly of the costs for legal representation, is typically by far the largest.

The ICSID Convention leaves it to the tribunal's discretion as to who will pay these costs, unless the parties agree otherwise.⁴⁹ The UNCITRAL Arbitration Rules state that, in principle, the unsuccessful party shall bear the costs of the arbitration.⁵⁰ But in a particular case, both parties may be partly successful. This is the case if the claimant wins on jurisdiction but the respondent state wins on the merits, or if only part of the claims and arguments of one party is accepted.

In many cases tribunals have found that the fees and expenses of ICSID and of the arbitrators were to be shared equally and that each party had to bear its own expenses. In some cases the tribunals awarded costs as a sanction for improper conduct of one of the parties. More recently, tribunals have shown a growing tendency to adopt the principle that costs follow the event. An award of costs against the losing party may be total or, more frequently, may cover a certain proportion of the overall costs.

12 CHALLENGE AND REVIEW OF DECISIONS

Awards are final and not subject to any appeals procedures.⁵¹ It is only under very limited circumstances that a review of awards is possible. In non-ICSID arbitration, including arbitration under the Additional Facility, the normal way to

⁴⁹ Art. 61.2.

⁵⁰ Art. 42.1.

⁵¹ ICSID Convention, Art. 53.

challenge an award is through national courts. This is done in the courts of the country in which the tribunal had its seat or by the courts charged with the task of enforcing the award. In many countries, this process is subject to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958.⁵²

ICSID awards are not subject to annulment or any other form of scrutiny by domestic courts. Rather, the ICSID Convention offers its own self-contained system for review. Under this procedure, an ad hoc committee appointed by ICSID may annul the award upon the request of a party on the basis of five narrowly defined grounds.⁵³ Annulment is concerned only with the legitimacy of the process of decision but not with its substantive correctness. An annulment merely removes the original decision without replacing it. Therefore, an ad hoc committee acting under the ICSID Convention does not have the power to render its own decision on the merits. After an annulment, the dispute may be resubmitted to a new tribunal.

13 ENFORCEMENT OF AWARDS

Arbitral awards are binding upon the parties and carry an obligation to comply. Non-compliance with an award by a state would be a breach of the ICSID Convention and would lead to a revival of the right to diplomatic protection by the investor's state of nationality.

The enforcement of non-ICSID awards, including Additional Facility awards, is subject to the national law of the place of enforcement and to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

ICSID awards are to be recognized as binding, and their pecuniary obligations are to be enforced like final domestic judgments in all states parties to the convention. The obligation to enforce the pecuniary obligations arising from ICSID awards is limited by any immunity from execution of states.⁵⁴

⁵² 330 UNTS 38 (1959). ⁵³ ICSID Convention, Art. 52.

⁵⁴ ICSID Convention, Arts 54, 55.

14 PROBLEMS AND CHALLENGES

14.1 Coherence and consistency

Tribunals frequently refer to and rely on earlier decisions. Despite that practice, the lack of consistency of case law has become a matter of concern. A system that operates with a large number of differently composed tribunals is more vulnerable to discrepancies than courts with a permanent composition and courts embedded in a hierarchical judicial system.

A permanent court for investment disputes is not a realistic goal in the foreseeable future. The idea of appeals procedures has been widely discussed and has found entry into some US BITs. If applied separately for each treaty, appeals procedures are unlikely to lead to more coherence. Also, Art. 53 of the ICSID Convention explicitly states that awards “shall not be subject to any appeal.” A possible alternative would be the creation of a central facility that gives preliminary rulings in pending proceedings.

14.2 Transparency

Confidentiality is traditionally considered one of the major advantages of arbitration. But in investment arbitration the presence of issues of public interest has increasingly led to demands for more openness and transparency. Two issues are typically discussed under the heading of transparency: access to information and third party participation.

Awards are not published automatically. ICSID publishes awards only with the consent of both parties.⁵⁵ Since 2006 the Centre has been under an obligation to publish excerpts of the legal reasoning of each award.⁵⁶ The parties are free to release awards and other decisions for publication unless it is otherwise agreed. Most ICSID awards have been published in one way or another, but there are some awards and other decisions that have remained unpublished. Non-ICSID awards are published sporadically.

Most hearings are closed to the public. Under a rule introduced in 2006, ICSID tribunals may, under certain circumstances, allow other persons to attend all or part of the hearings.⁵⁷ Some investment treaties provide that investor–state arbitration hearings shall be open to the public.

⁵⁵ ICSID Convention, Art. 48.5.

⁵⁶ ICSID, Arbitration Rule 48.4.

⁵⁷ ICSID, Arbitration Rule 32.

In some cases ICSID tribunals have permitted the submission of *amicus curiae* briefs by non-disputing parties. Under a procedure introduced in 2006, the tribunal may, after consulting the parties, allow an entity that is not a party to file a written submission regarding a matter within the scope of the dispute.⁵⁸

Non-ICSID tribunals operating in the framework of NAFTA under the UNCITRAL Rules have allowed third parties to make written submissions. In October 2003 the NAFTA Free Trade Commission issued a statement regarding the participation of non-disputing parties.⁵⁹

14.3 Regulatory chill

Concerns about the impact of investment arbitration on the states' ability to exercise their regulatory functions have been voiced for some time. These concerns appear to be mostly theoretical. An examination of tribunal practice shows a high degree of sensitivity towards public order concerns. This is particularly manifest in cases involving environmental issues. Tribunals have generally respected *bona fide* environmental measures and other measures serving a genuine public interest taken by host states.

14.4 Pro-investor bias

Accusations of pro-investor bias in investment tribunals are highly subjective and difficult to verify. Statistics do not support these concerns. A large proportion of cases are dismissed as early as the jurisdictional stage. Of the remaining cases, roughly half are dismissed on the merits. Even in cases in which the investor prevails, typically only a fraction of the relief demanded is awarded.

Tribunals react rigorously when they find illegal or improper action by investors. This concerns corruption, misleading information, illegality under host state law, and abuse of process. Practices of this kind lead to the dismissal of claims.

RESEARCH QUESTIONS

1. How do tribunals deal with evidence and proof of facts, including production of documents, witnesses and experts, standard of proof, and burden of proof, in international investment arbitration?

⁵⁸ ICSID, Arbitration Rule 37.2.

⁵⁹ NAFTA Free Trade Commission Statement on Non-Disputing Party Participation (October 7, 2003) 44 LM 796 (2005).

2. What is the role of provisional measures in international investment arbitration? How do tribunals deal with issues of urgency and necessity, the legal nature and the circumstances requiring provisional measures?
3. Is there room for non-pecuniary remedies in international investment arbitration? Are Arts 34–37 of the ILC Articles on state responsibility, dealing with restitution, satisfaction, and declaratory relief applicable?
4. To what extent do third parties, i.e. non-participating states and *amici curiae*, have access to investment arbitration?

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