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MAPPING THE FUTURE OF INVESTMENT TREATY ARBITRATION AS A SYSTEM OF LAW

This panel was convened at 1:00 p.m., Friday, March 27, by its chair, Lucy Reed of Freshfields Bruckhaus Deringer US LLP, who introduced the panelists: Gabriela Alvarez-Avila of Curtis, Mallet-Prevost, Colt & Mosle LLP; Yas Banifatemi of Shearman & Sterling LLP; James Crawford of the University of Cambridge and Matrix Chambers; and Toby Landau QC of Essex Court Chambers.*

INTRODUCTORY REMARKS BY LUCY REED†

Ms. Reed began the panel by noting the significant challenges to investment treaty arbitration's integrity as a system of law, including challenges to enforceability of awards, conflicting decisions, and certain states withdrawing from the International Centre for Settlement of Investment Disputes (''ICSID'') and bilateral investment treaties (''BITs''). She posed the following questions: Are these growing pains or a sign of fundamental flaws? Will the new generation of investment treaties help resolve these problems?

Ms. Reed introduced the panelists as ''card-carrying specialists'' in investment treaty arbitration and public international law. Gabriela Alvarez-Avila served as counsel at ICSID for several years. Yas Banifatemi has been involved in several investment treaty arbitration cases, including the *Yukos* shareholder cases brought under the Energy Charter Treaty, and she has also served as an arbitrator. James Crawford, the former head of the Lauterpacht Research Centre for International Law, has served as an advocate and arbitrator in numerous investment treaty arbitrations and has served on ICSID annulment committees. Toby Landau is an advocate and arbitrator in a number of investment arbitration cases. Makhdoom Ali Khan, former Attorney General of Pakistan and advocate on several investment treaty cases, was unable to join the panel, but the panel had the benefit of several questions and issues he raised.

Ms. Reed suggested that before looking at the future, the panel might examine the current state of investment treaty arbitration. On the positive side, there is a growing number of cases and final awards. There is also a growing diversity of participants—different states are being sued, different nationalities are represented as investors, occasionally nationals of developing countries are going up against developed countries, and there are more regional trade agreements containing international arbitration mechanisms. It is both negative and positive that there are rich, and sometimes inconsistent, awards. There is a growing number of withdrawals from ICSID—including Bolivia and Ecuador (with respect to hydrocarbons), and Venezuela's denunciation of the Dutch BIT. There is resistance to enforcement of final awards from Argentina.

REMARKS BY YAS BANIFATEMI‡

Ms. Banifatemi addressed the question of whether investment treaty arbitration is a ''system of law.'' If a ''system of law'' is defined as a body of rules and principles through which rights and obligations are established and justice is administered, then investment treaty arbitration is certainly a system of law.

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However, whether investment treaty arbitration is its own system of law, a system that is autonomous and distinct from other types of international arbitration, is another question. There is certainly a specific feature in investment treaty arbitration: because it is based on international treaties and raises questions that can be resolved through the application of treaty law or the rules governing the international responsibility of states, international law will, by definition, apply to a great number of issues. This feature, however, does not make the process itself any different from the arbitral process generally. Investment treaty arbitration can be properly defined as a "sub-system" of international arbitration, which also covers international commercial arbitration and investment contractual arbitration.

In investment arbitration, the challenges to the legitimacy, transparency, and efficiency of the system are specific to the public nature of one of the parties, namely the defendant state. Although adjustments may be warranted depending on which aspect of the process one attempts to improve, dismantling the entire system to account for the public nature of one party could undermine international arbitration—the broader system—as a whole, by introducing aspects that may be specific to adjudication before international courts but that are not specific to international arbitration as a system.

This can be shown be focusing on each of the three elements constituting "investment treaty arbitration."

I. *Investment* treaty arbitration. Does a distinction exist between *commercial* and *investment* arbitration?

There is a difference in scope between the two, in that arbitrators in commercial arbitration deal with the parties' contractual or legal rights and obligations, whereas in investment arbitration, arbitrators decide the international responsibility of a host state based on its contractual or treaty commitments relating to investments (because investment arbitration concerns "investments," arbitral tribunals must ensure that the jurisdictional requirements regarding the existence of an investment are met).

On the other hand, a number of important similarities illustrate the identity of the mechanism and processes between international commercial arbitration and international investment arbitration. First, no matter what system or sub-system is chosen, consent to arbitration is always needed. An arbitral tribunal that decides without ensuring the existence of a consent by both parties is simply exceeding its powers. In addition, consent is always specific to the parties and to the dispute between those parties. Despite pressure from civil society and third parties to enter the system, such parties should not have systematic and unlimited access to arbitral proceedings. Each arbitration concerns a dispute between two specific parties—that is what a tribunal decides—be it commercial or investment treaty arbitration, and this fundamental feature should not be undermined by a systematic focus on *non*-parties. Second, the law applicable to the substance of the dispute is always determined based on the same method: party autonomy in the first place and, absent a choice by the parties, determination by the arbitrators. Third, the conduct of the proceedings is essentially the same. Notwithstanding minor differences, the various arbitration rules (in particular ICSID, UNCITRAL, and SCC) are similar in regard to the main aspects of the conduct of arbitral proceedings.

II. Investment *treaty* arbitration. Is there a difference between investment *treaty* arbitration and investment *contractual* arbitration?

There might be some arguments against a distinction based on the fact that what is protected is always an "investment;" in particular in ICSID arbitration, where the objective requirements of jurisdiction under Article 25 of the Washington Convention must be met in all cases.

There are also arguments in favor of a distinction based on the source of the obligation. First, in investment treaty arbitration, there is a set of treaty standards of protection against which the state's conduct is assessed, unlike in investment arbitrations where the tribunal is constituted on the basis of a contract. Second, in investment arbitrations based on contract, states can be claimants in the arbitration, whereas in treaty arbitration, the host state always has the procedural status of a defendant. Finally, in contractual investment arbitration, the applicable law will not always be international law; there are not necessarily treaty standards to interpret and apply. All this does not mean that the fundamental principle of the equality between the parties should be disregarded and that a state, as a party to the dispute, should enjoy preferred treatment based on its status as a state. As emphasized in the *Texaco* Award of 1977,[1] a state's consent to arbitrate its dispute with private parties—based on treaty or contract—is an attribute of its sovereignty.[2]

III. Investment treaty *arbitration*. What about the arbitral nature of investment treaty arbitration?

One challenge to investment treaty arbitration is that, unlike judges, arbitrators are private persons who do not hold a public office. Those who advocate this proposition, however, do not question the arbitrators' power to adjudicate. Indeed, such power is recognized by the majority of national legal systems, which acknowledge arbitration as a dispute resolution mechanism and accept the enforcement of the resulting arbitral award.

A related challenge to the power of the arbitrators to adjudicate is the so-called lack of a permanent body and the lack of an appeal system in arbitration. However, permanence and appeal are not defining features of arbitration; introducing them would undermine one of the main attractions of international arbitration as a dispute resolution process resulting in final and binding decisions.

Finally, there are difficulties arising from the lack of consistency in arbitral case law. This has been prevalent, for example, in cases relating to the effect of umbrella clauses. The system would benefit from greater consistency with regard to fundamental issues of international law. The difficulty, however, is that there is no rule of "precedent" in international arbitration, and a tribunal must decide on the basis of the text or the instrument on which it is constituted. It can, of course, find guidance in other tribunals' decisions, but it is not bound by those decisions.

With regard to transparency and confidentiality, a tendency is developing, as a result of the increasing publication of awards, where arbitrators engage in drafting longer and longer decisions containing *obiter dicta*, with the focus shifting away from the parties and moving to the public at large. Here, again, the general principle of *res inter alios acta* similarly applies: arbitrators, like judges, resolve individualized disputes between individual parties and *only* those parties. This is also true of the International Court of Justice. Article 59 of the Court's Statute states that "the decision of the Court has no binding force except as between the parties and in respect of that particular case."

In conclusion, while regard should be given, where relevant, to the specific features of investment treaty arbitration, this does not justify disassociating investment treaty arbitration from international arbitration in general with a view to, or with the consequence of, radically changing investment treaty arbitration as a dispute resolution mechanism. Ignoring the *arbitral*

[1] Texaco Overseas Petroleum v.Libyan Arab Republic, Int'l Arbitral Award, Jan. 19, 1977, 17 ILM 1 (1978).

[2] *See also* Case of the SS 'Wimbledon', 1923 PCIJ (ser. 1) No. 1, at 25 ("the right of entering into international engagements is an attribute of State sovereignty.").

nature of investment treaty arbitration—by introducing multiple layers of review, undermining the finality of the award, opening the proceedings to third parties, and making the process something for the public at large rather than, first and foremost, for the parties to the dispute—will inevitably result in undermining the international arbitration system as a whole.

Remarks by Toby Landau QC*

Mr. Landau QC discussed current pressures on investment treaty arbitration. A key problem facing this field is the fundamental misconception that investment treaty arbitration is simply a subset of ordinary commercial arbitration. While there might be a passing resemblance between the two systems, there are dangers in characterizing investment treaty arbitration in this way. Properly analyzed, the two systems are fundamentally different, and the difference runs far deeper than the few procedural issues that are often focused upon (such as the approach to transparency or precedent).

At its core, investment treaty arbitration is a different dispute resolution mechanism to commercial arbitration by virtue of the nature of the rights and obligations at stake, and the mandate of the tribunal. As others have commented (*e.g.*, Van Harten), unlike commercial arbitration, it is in essence a form of public law, or administrative adjudication, in which a vertical relationship between sovereign and citizen is at stake, rather than a horizontal, and private relationship between equal transacting parties. As such, its effects flow far wider than the immediate disputing entities. These fundamental differences each require their own procedural response in terms of the arbitral process itself. And yet dispute resolution in this field has, in effect, been "shoe-horned" into the private, commercial arbitration procedural model, which was not designed for it, and for which, in many ways, it is ill-suited. The position is further compounded by the fact that many investment treaty arbitrations are staffed, both in terms of counsel and arbitrators, by professionals who have grown up in (as some might say the "murky") world of commercial dispute resolution, with little or no expertise in the more specialized (and as some might say more "refined") fields of public, and public international, law. The results of this mismatch are identifiable tensions within the system, and (whether right or wrong) a growing groundswell of criticisms and pressures from without.

In the course of any such analysis, however, one must "drop" a very important footnote at the outset: the pressures and criticisms that the process has engendered may well be, in actual fact, without any foundation at all. This, however, is beside the point. What matters, ultimately, is perception—and as long as there remain perceptions that this field is problematic, or potentially unfair, the integrity and legitimacy of the system remains endangered.

In terms of specific pressures on the investment treaty arbitration process, two categories of case merit attention.

First, there is the category of case that involves pure treaty disputes, where there is an argument as to the application of a treaty, and an investor who pursues rights and obligations that are wholly dependent upon that instrument, and where the dispute would not have arisen but for the treaty—a pure BIT claim.

Second, there are a large number of cases that turn up as BIT claims, but could also have been contract claims. Much foreign investment happens pursuant to investment contracts, and many of those contracts will have their own dispute resolution system. Contractual

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mechanisms are now frequently supplanted with what is perceived as an elevated form of arbitration under a BIT, where a dispute may be resolved at a political level, and where a claimant may be able to assert more pressure. In this way, commercial cases that are handled by commercial practitioners are now repackaged as treaty claims.

Each of these two categories gives rise to different types of pressures. In the pure BIT claim, the difference in the types of issues at stake and the role of tribunals, as compared to commercial arbitrations, is most pronounced. Unlike any other system of national administrative law, arbitrators in a BIT setting are placed in a position of singular, extraordinary power. Tribunals can review, question, and sanction regulatory action by governments, by legislatures, and by national judicial bodies in a way that no national judge could ever do. Cases frequently involve regulatory issues concerned with how governments govern, entailing issues far beyond the immediate parties to the dispute (*e.g.*, access to water; black empowerment policies; indigenous populations rights; etc.). In reviewing regulatory activity, treaty tribunals apply broad principles as set out in BITs, which invariably provide little guidance or detail. The broad and often anodyne wording of a treaty reflects the old adage—that the definition of a treaty is a disagreement reduced to writing. Contracting states often agree to broad and unspecific language because that is all upon which they can agree. Treaty tribunals have no doctrine of precedent to guide or bind them. Their decisions are not subject to appeal, and their procedures are frequently the subject of only very limited (if any) review by any national judicial system. Treaty tribunals can effect huge allocations of public funds, by way of damages awards, and such allocations, unlike other distributions of public funds, are beyond outside scrutiny. It is the nature of this process that renders investment treaty arbitration so different from commercial arbitration and has generated fears and criticisms. Specific procedural safeguards are required, and there is a different notion of the arbitral mandate—in a way that is simply not relevant in commercial arbitration. As long as these differences are ignored, and the process is viewed as no different to any other kind of arbitration, the system remains vulnerable.

The second category of case tends to involve contractual disputes that are sufficiently significant and sensitive as to warrant the added protection of a BIT claim, and where a simple contract arbitration risks obstruction or interference (often by way of wrongful resort by a party to a national court). This type of case—even when re-packaged as a treaty claim—brings with it all the difficulties which are already inherent in this type of commercial arbitration, where the process is viewed with suspicion by a party, and a process best avoided if possible.[1] The same pressures have now reappeared as an issue for treaty arbitration.[2]

If any blame for these pressures is to be placed upon arbitrators, it is the tendency of some to come to a treaty dispute wearing a ''commercial arbitration hat,'' and to address any manifest pressures by way of limited—and often cosmetic—procedural gestures (such as the grant of a little publicity in order to quell the concerns of NGOs). What is needed is the adoption of an entirely different mindset, and conception of the process as a whole. The starting point should not be commercial arbitration, but rather inter-state arbitration, which provides a more appropriate initial model from which to develop an appropriate procedure.

[1] For example, notorious and problematic commercial arbitrations such as The Hub Power Company Ltd v. (1) WAPDA & (2) The Federation of Pakistan, Supreme Court of Pak., [2000] 16 Arb. Int'l 431; Himpurna v. Indonesia, 15 Mealey's Int'l Arb. Rep.,9 (2000).

[2] For example, the injunctions issued by national courts to restrain the ICSID arbitrations in SGS v. Pakistan, Case No ARB / 01 / 13 and Chevron v Bangladesh, Case No ARB / 06 / 10.

Remarks by James Crawford*

Professor Crawford addressed the causes and prognosis for states dropping out of ICSID and other investment treaties. The question is whether we have a perception of a crisis based on a few incidents, or whether a real crisis threatens the system. At one level the answer to complaints about unfairness against host states is simple. The basis for international investment arbitration is a treaty governed by international law. Since a treaty deals with the exercise of public power, if governments do not want arbitrators deciding issues of public power, they should not enter into investment arbitration treaties.

While there have been some withdrawals, there have not yet been very many, and those withdrawals have been selective. States that have withdrawn from particular BITs have not withdrawn from all of their BITs. There have only been a few withdrawals from ICSID, and whatever the effect (or lack thereof) on jurisdiction in pending cases, this does not necessarily influence other investment treaties to which those states are parties. The way BITs are constructed arguably preserves treaty coverage for a period of time notwithstanding termination. But perceptions are extremely important in the field. The BIT system came into existence relatively quickly, and states could abandon BITs relatively quickly if there were a widespread perception of a systemic crisis.

The BIT system is a sub-system of international law that has its own long-term balances. Looking back at the Venezuela arbitrations of the early part of the twentieth century, one could find arbitrators doing a good job, broadly speaking, with the same situations—treaty/contract, factual disputes, regulatory autonomy—that occur now. As such, the withdrawals so far do not present a systemic crisis. They are simply exercises of the authority that states have under all the BITs to give notice and withdraw, to whatever effect that may have on pending disputes.

The European Union creates another sub-system presenting a problem that may have a fortuitous interaction with the current debate about BITs. The European Court of Justice has just handed down a decision in the case, *European Commission v. Austria*, in which it said that certain aspects of the BITs of those states needed adjustment.[1] Reminiscent of the *MOX* case, the ECJ continued its trend of treating European law as superior to international law when it matters and also as superior to national law when it matters.[2]

There could be consequences of the unsettling of the BIT system within Europe. There is no doubt that the system is presently fragile. One of the frailties results from the Argentina cases and the failure of Argentina to comply with final awards against it. We now have quite widespread expropriations elsewhere, and we will see if the advice given to governments around the world is that they are better overall to take the risk of BIT exposure and the possibility of defending the state in the arbitrations or to do away with the system altogether.

Remarks by Gabriela Alvarez†

Ms. Alvarez focused on the question of whether the new generation of BITs addresses or is capable of addressing some of the problems described by the panel.

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[1] Case C-211/9, Comm'n v. Austria (2007).

[2] Case C-459/3, Comm'n v. Ireland (2006).

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One of the main concerns for users of investor-state arbitration proceedings is the lack of reasons or thin reasoning given in some awards. The new model BITs try to address this problem. They provide for a procedure by which either party can request a tribunal to transmit its proposed decision or award to the parties in the proceeding as well as to the BIT state that is not a party to the proceeding. The parties and states would then provide comments to the tribunal concerning any aspect of its proposed decision or award within sixty days. The tribunal is bound to consider any comment and to issue its decision or award no later than forty-five days after the expiration of the sixty-day comment period. This procedure shall apply as long as an appeal mechanism is not in place. Indeed, the new models provide for the state parties to negotiate and set up an appellate mechanism that would review the awards rendered by tribunals. This mechanism is aimed at ensuring not only that the decisions will be reasoned, but also that they will be correct and consistent. The problem was highlighted in the *CMS* Annulment decision in which the tribunal stated that the *CMS* tribunal had made mistakes that ultimately could not be addressed by the Annulment Committee.[1]

Appeal mechanisms also provide the opportunity to discuss another feature of the new model BITs: the suspension of the enforcement of an award while the award is subject to annulment proceedings. The discussion is whether suspension of the enforcement should be granted, and if so, under what conditions. The new U.S. and Canada Model BITs make clear that enforcement cannot be sought until post-award remedies are exhausted, or the deadline for them has expired. These post-award remedies are interpretation, revision, or annulment of an award under the ICSID system and the procedure to revise, set aside, or annul an award under the UNCITRAL or the ICSID Additional Facility Rules.

Another concern is treaty shopping by investors for the sole purpose of obtaining protection of BITs. Some of the new provisions included in the new model BITs address this problem directly. For instance, the new models include a Denial of Benefits Clause that allows a state to deny benefits of the treaty to an investor of the other party if 1) the enterprise has no substantial business activities in the territory of the other party, and 2) if persons of a non-party, or of the denying party, own or control the enterprise (i.e., shell companies). The extent to which these provisions will avoid treaty shopping still remains to be seen. The application of this type of clause has already caused a number of treaty interpretation problems. In the Norway Model BIT, the requirement of substantial business activities is directly contained in the definition of investor, which leaves it to tribunals to delineate the concept of substantial business activities. Also, the new Canada Model BIT provides that Most Favored Nation (''MFN'') treatment does not extend to treatment accorded under existing treaties, and thus the MFN guarantees are applicable only to future treaty provisions.

There have been a number of changes in the model BITs that limit the scope of the treaties and seem to be a response to expansive interpretations by some tribunals of particular provisions. The concept of investment in the new model BITs includes the typical enumerative list of what could be considered an investment, but it now adds that for an investment to qualify as such under the agreement, the asset must have the characteristics of an investment, such as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk. These limitations on the concept seem to be inspired by some findings of ICSID tribunals regarding the concept of investment under the ICSID Convention; they might be in response to concerns over an expansion of the concept of investment under other arbitration rules. These changes will help harmonize the concept of investment under BITs

[1] CMS v. Argentina, ICSID Case No. ARB/01/8, Annulment Committee Decision, ¶¶ 136, 158-59 (Sept. 25, 2007).

and the ICSID Convention. In the past, some ICSID tribunals have found that when a business transaction fits within the definition of investment under the treaty, this meant that it also fell within the definition of investment under the ICSID Convention, without taking into account any ''objective requirements'' under the ICSID Convention. The above-mentioned changes regarding the definition of investment in the new model BITs help to bridge the gap between the concept of investment under an investment treaty and that under ICSID.

Another substantive change relates to the concept of fair and equitable treatment and the standard of full protection and security. Both are included in the minimum standard of treatment, which must be applied in accordance with customary international law. In the new U.S. Model BIT, this provision is accompanied by a clarification that addresses some concerns of states that had perceived unjustified expansion of the above-mentioned standard. This clarification states that the ''fair and equitable treatment and full protection and security do not require treatment in addition or beyond that which is required by the minimum standard of treatment, and do not create additional substantive rights.''

In regard to expropriation, the text of the new U.S. Model BIT provides for a number of clarifications regarding the concept of indirect expropriation, and it directs tribunals to consider a number of conditions before reaching a finding of direct expropriation. The most important limitation refers to situations that cannot constitute indirect expropriations. It states that ''non-discriminatory regulatory actions by a party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment'' could not be considered an indirect expropriation. This limitation addresses concerns by states over their ability to regulate key aspects of public welfare. However, this provision is qualified by an initial sentence that states ''except in rare circumstances.'' This rather obscure exception to the exception certainly does not help to strengthen legal certainty.

In some areas, the provisions of the new model BITs give rather precise directions to tribunals—for example, with regard to the tribunal's preliminary objections. In other respects, the new provisions will certainly represent a bigger challenge for both parties and, in particular, for tribunals that would need to identify customary international law rules (for example, with regard to fair and equitable treatment). It has never been an easy task to define the rules in international law that come from custom, since this entails identifying a consistent practice and an *opinio juris*. Parties and tribunals will need to address in a rigorous way some of the substantive provisions of these BITs to crystallize the contents of the standards and to arrive at generally accepted principles. All parties interested in making this field evolve and progress in the right direction will have to put the extra time and effort into making that happen.