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This article was first published in June 2019
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Editor
Barton Legum
ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following for their assistance throughout the preparation of this book:

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PREFACE

The past year has again confirmed *The Investment Treaty Arbitration Review*’s contribution to its field. The biggest challenge for practitioners and clients over the past year has been to keep up with the flow of new developments and jurisprudence in the field. There was a significant increase in the number of investment treaty arbitrations registered in the first years of this decade. These cases have come or are now coming to their conclusions. The result today is more and more awards and decisions being published, making it hard for practitioners to keep up.

Many useful treatises on investment treaty arbitration have been written. The relentless rate of change in the field rapidly leaves them out of date.

In this environment, therefore, *The Investment Treaty Arbitration Review* fulfils an essential function. Updated every year, it provides a current perspective on a quickly evolving topic. Organised by topic rather than by jurisdiction, it allows readers to access rapidly not only the most recent developments on a given subject, but also the debate that led to and the context behind those developments.

This fourth edition adds new topics to the *Review*, increasing its scope and utility to practitioners. It represents an important achievement in the field of investment treaty arbitration. I thank the contributors for their fine work in developing the content for this volume.

**Barton Legum**

Dentons
Paris
April 2019
Chapter 1

COVERED INVESTMENT

Can Yeğinsu and Ceyda Knoebel

I INTRODUCTION

The definition of a covered ‘investment’ is a key element in determining the applicability of protections under an investment treaty to a covered investor. It delineates the scope of a state’s consent to arbitrate expressed in the dispute settlement provisions of the international instrument containing that consent. Accordingly, the question of what constitutes an investment is often a critical threshold question of jurisdiction.

To date, much of the debate surrounding the definition of a covered investment has centred on whether the term has an objective meaning independent of the wording of the international instrument containing the state’s consent to arbitrate, or whether the meaning is derived purely from the text of the relevant instrument. That question remains unresolved.

There is no uniform definition of investment under customary international law or recognised by states in international instruments. Most investment treaties adopt an asset-based definition expressed with the formula ‘every kind of asset’ followed by an illustrative, non-exhaustive list comprising all types of properties and contractual rights, including, most commonly:

a movable and immovable property, and property rights such as mortgages, liens and pledges;
b equity and debt participation in a company, including shares, debentures and debt instruments;
c intellectual property rights, goodwill and know-how;
d claims to money and performance under a contract having an economic value; and
e concessions or licences granted under public law or contract.

This approach is reflected in a number of different permutations developed by specific treaty language, each of which has been the subject of arbitral jurisprudence that is considered in this chapter.

Any investment dispute submitted to the International Centre for Settlement of Investment Disputes (ICSID) for resolution under the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention), is subject to a determination of an autonomous notion of investment under Article 25 of the ICSID Convention, and must therefore meet the threshold requirements for a covered investment within the meaning of the ICSID Convention. These requirements are in addition

1 Can Yeğinsu is a barrister at 4 New Square Chambers and Ceyda Knoebel is a solicitor advocate at Gibson, Dunn & Crutcher LLP.
to the requirements under the investment treaty or agreement at issue containing a state's consent to arbitrate. This is often referred to as the 'double-barrel' test, and has given rise to significant controversy in arbitral jurisprudence, as discussed further below.

II DEVELOPMENT OF TREATY LANGUAGE

Historically, most definitions of investment in investment treaties (or agreements) were widely drafted and open-ended, allowing for evolving types of investments to be covered by the definition. For example, the Energy Charter Treaty (ECT), which is a sectoral multilateral treaty born from the European Energy Charter between the European Union and the former Soviet Union countries in the 1990s, includes one of the broadest definitions of investment. Other treaties refer extensively to ‘any kind of property invested . . . in the territory of [a Contracting Party].’

That said, not all earlier treaties adopted such wide language. Some define investment in a circular manner, referring to investment within the definition itself (i.e., ‘investment means any kind of asset or right related to an investment’ or ‘investment means every kind of investment’). Others embrace an exhaustive list. For example, the investment chapter in the 1994 North American Free Trade Agreement (NAFTA) between the United States, Canada and Mexico covers only interests in enterprises and property, other ‘interests arising from the commitment of capital or other resources in the territory of a Party to economic activity in such territory’ and ‘contracts where remuneration depends substantially on the production, revenues or profits of an enterprise’. The NAFTA list also refers to debt securities in, or loans to, a company (not state enterprises) but only if the maturity of the debt is at least three years and the enterprise is an affiliate of an investor. Certain claims to money are also expressly excluded from the definition.

The discrepancy between definitions has given rise to debate as to whether most favoured nation (MFN) treatment clauses in treaties with a narrow definition of investment could be deployed to import a broader definition from other treaties to which the defendant state is a party. However, consistent investment treaty jurisprudence has indicated that tribunals are not willing to widen the application of MFN clauses to import a more favourable definition of ‘investment’ from other treaties, on the basis that the definition is a crucial element of a state’s consent to arbitrate a particular dispute, which goes to the ratione materiae jurisdiction of an arbitral tribunal.

2 Malaysian Historical Salvors v. The Government of Malaysia, ICSID Case No. ARB/05/10, Award, 17 May 2007, para. 55.
3 See Article 1(6) of the ECT covering every kind of asset owned or controlled by a defined investor followed by a non-exhaustive, generous list of types of assets.
6 See, e.g., Article 1(a) of the Treaty between the United States of America and the Republic of Kazakhstan concerning the Reciprocal Encouragement and Protection of Investment, 19 May 1992. Such circular definitions have caused tribunals to seek to give a distinct and separate meaning to the word ‘investment’.
7 See Article 1139 of NAFTA.
8 See Metal-Tech Ltd v. Republic of Uzbekistan, ICSID Case No. ARB/10/3, Award, 4 October 2013, paras. 145–163; Rafat Ali Rizvi v. Republic of Indonesia, ICSID Case No. ARB/11/13, Award on
More recently, investment treaties and investment chapters within multinational trade agreements have departed from a purely asset-based definition, and additionally require the investment to display the ‘characteristics of an investment’. For example, the intended successor to NAFTA, the United States–Mexico–Canada Agreement (USMCA) defines investment as ‘every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk’. While providing a non-exhaustive list of assets, it also excludes certain claims to money, and orders and judgments entered in a judicial or administrative action from the definition of ‘investment’. Similarly, the investment chapter of the EU–Vietnam Free Trade Agreement (FTA) agreed in July 2018, the investment chapter of the EU–Canada Comprehensive Economic and Trade Agreement (CETA) and the EU–Singapore Investment Protection Agreement signed on 19 October 2018 all make reference to assets that have the characteristics of an investment, including ‘the commitment of capital or other resources, the expectation of gain or profit’, ‘the assumption of risk’ and ‘a certain duration’. The investment chapter of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (TPP11), which entered into force on 30 December 2018, adopts a similar construction, save for the reference to ‘a certain duration’. Before the political developments of 2016, it was expected that the investment chapter of the EU–US Transatlantic Trade and Investment Partnership agreement under negotiation would follow this trend. However, the negotiations remain suspended following the Trump administration’s voiced scepticism towards multilateral trading blocs. Regardless, we know the United States prefers a formulation similar to those in the recent multilateral trade agreements as reflected in

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Jurisdiction, 16 July 2013, para. 220; Vannessa Ventures Ltd. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/04/6, Award, 16 January 2013, para. 133.

9 For example, the 2015 India Model BIT defines investment as an ‘enterprise’, which the investor must have incorporated in the host state and that, together with its assets, must have the characteristics of an investment such as the commitment of capital or other resources, certain duration, the expectation of gain or profit, the assumption of risk and a significance for the development of the Party in whose territory the investment is made’. The Model BIT proceeds to list the assets that an enterprise must ‘possess’ to qualify as an ‘investment’.


11 See Article 14.1 of USMCA.


the 2012 US Model Bilateral Investment Treaty (BIT). It is clear that these new generation investment definitions seek to limit or clarify the scope of covered investments, in contrast with the broad, open-ended definitions found in earlier treaties encompassing ‘every kind of asset’.

This recent trend may be explained by states’ desire to exclude expressly one-off commercial transactions for the sale of goods or services, or purely contractual claims, from the scope of investments afforded treaty protections. These types of claims have previously been found by some tribunals to fall within a traditional definition of investment encompassing ‘claims to money and performance under a contract having an economic value’. Unfortunately, there is significant inconsistency in the jurisprudence on this issue, which is difficult to rationalise on the wording of the treaties.

For example, *Joy Mining v. Egypt* involved the non-performance of a contractual obligation by an Egyptian state entity as the counterparty under a contract for the provision of mining systems and supporting equipment. The definition of investment in the relevant UK–Egypt BIT includes the formulations ‘every kind of asset’ and ‘claims to money or to any other performance under contract having a financial value’. However, the tribunal refused to assume jurisdiction over the claim on the basis that it was necessary to draw a fundamental distinction between ‘ordinary sales contracts, even if complex, and an investment’, since otherwise ‘any sales or procurement contract involving a State agency would qualify as an investment’. The tribunal in *Nova Scotia Power v. Venezuela*, a case involving contractual rights under a coal supply agreement, reached a similar conclusion under the investment definition in the Canada–Venezuela BIT, which includes ‘money, claims to money, and claims to performance under contract having a financial value’. The tribunal commented that ‘[n]either the definition of investment, nor the BIT, should function as a Midas touch for every commercial operator doing business in a foreign state who finds himself in a dispute’.

In contrast, in *Deutsche Bank v. Sri Lanka*, the tribunal found that a hedging agreement (under which the Sri Lankan national petroleum corporation contractually failed to make a required payment to the claimant) fell within the investment definition in the Germany–Sri Lanka BIT, which covered ‘claims to money which have been used to create an economic value or claims to any performance having an economic value and associated with an investment’. Similarly, the annulment committee in *Malaysian Historical Salvors v. Malaysia* found that non-payment under a contract to find and salvage a shipwreck for the government

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16 See 2012 US Model BIT, Article 1: “‘investment’ means every asset . . . that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk’.

17 *Joy Mining Machinery Limited v. The Arab Republic of Egypt*, ICSID Case No. ARB/03/11, Award on Jurisdiction, 6 August 2004, para. 58. See also *Global Trading Resource Corp and Globex International Inc v. Ukraine*, ICSID Case No. ARB/09/11, Award, 1 December 2010, paras. 56 to 57.

18 *Nova Scotia Power Incorporated (Canada) v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)11/1, Award, 30 April 2014, paras. 75 to 78.

19 id., para. 82.

of Malaysia constituted an investment under the UK–Malaysia BIT definition of investment, even though the definition only included ‘claims to money or to any other performance under contract having a financial value’.21

Perhaps in reaction to the inconsistency of these decisions, the new generation FTAs and BITs tend to adopt more specific wording, indicating expressly when a sale of goods or a purely contractual claim is not included in the definition of investment. For example, the EU–Vietnam FTA, CETA. USMCA and the 2018 Dutch Model BIT categorically exclude sale of goods claims, clarifying that such transactions would not constitute a ‘claim to money’ referred to in the investment definition.22 The 2012 US Model BIT and the TPP11 text provide that ‘claims to payment that are immediately due and result from the sale of goods or services are less likely to have [the characteristics of an investment]’ without completely disqualifying them. By contrast, there are treaties such as the 2015 Australia–China and 2008 New Zealand–China FTAs, which adopt the wider ECT formula that merely requires any ‘claims to money or claims to any contractual performance’ to be ‘associated with an investment’.

III Covered Investment in ICSID Jurisprudence

Though consent of the parties to resolve their investment disputes before an ICSID tribunal ‘is an essential prerequisite for the jurisdiction of the Centre’,25 Article 25 of the ICSID Convention limits the Centre’s jurisdiction to disputes arising ‘directly out of an investment’:

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21 Malaysian Historical Salvors v. The Government of Malaysia, ICSID Case No. ARB/05/10, Decision on the Application for Annulment, 16 April 2009, paras. 61, 73 to 74.
22 See the EU–Vietnam FTA, Chapter 8 – Trade in Services, Investment and E-Commerce, General Provisions, Chapter 1, Article 1.4(p)(v): ‘For greater certainty, “claim to money” does not include claims to money that arise solely from commercial contracts for the sale of goods or services by a natural or juridical person in the territory of a Party to a natural or juridical person in the territory of the other Party; or financing of such contract other than a loan covered by subparagraph (iii), or any related order, judgment, or arbitral award’; CETA, Chapter 8 – Investment, Section A, Article 8.1: ‘For greater certainty, claims to money does not include: (i) claims to money that arise solely from commercial contracts for the sale of goods or services by a natural person or enterprise in the territory of a Party to a natural person or enterprise in the territory of the other Party. (ii) the domestic financing of such contracts; or (iii) any order, judgment, or arbitral award related to sub-subparagraph (i) or (ii)’; USMCA, Article 14.1: ‘investment does not mean . . . claims to money that arise solely from commercial contracts for the sale of goods or services by a natural person or enterprise in the territory of a Party to an enterprise in the territory of another Party; and Netherlands Model Investment Agreement, Article 1: “Claims to money” within the meaning of sub (iii) does not include claims to money that arise solely from commercial contracts for the sale of goods or services by a natural or legal in the territory of a Contracting Party to a natural or legal person in the territory of the other Contracting Party, the domestic financing of such contracts, or any related order, judgment, or arbitral award.’
23 TPP, Chapter 9 – Investment, Section A, Article 9.1, note 2.
The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.

The term ‘investment’ is not defined in the Convention. In this regard, the World Bank’s Report of the Executive Directors on the Convention states that:

No attempt was made to define the term “investment” given the essential requirement of consent by the parties, and the mechanism through which Contracting States can make known in advance, if they so desire, the classes of disputes which they would or would not consider submitting to the Centre (Article 25(4)).

Suggestions to include a contribution or a duration requirement or an emphasis on host state development in the Article 25 notion of investment were rejected by the negotiating states. It was agreed that the precise limitation on jurisdiction of an ICSID tribunal should be determined by the consent of the parties expressed by means of investment agreements, national legislation or investment treaties. This freedom, however, does not mean that parties can submit any dispute for resolution by the Centre. There are ‘outer limits’ to the jurisdiction of an ICSID tribunal, and arbitral tribunals interpreting the Article 25 reference to investment have developed various criteria to define and maintain those limits. It is fair to say that the task of defining those limits has proved to be complex.

With the intention of distinguishing treaty claims from ordinary commercial disputes, the idea that a covered investment must also constitute an investment under the ICSID Convention (independent of the definition of ‘investment’ in the treaty at issue) was first proposed by the Fedax v. Venezuela tribunal. This approach was embraced by the Salini v. Morocco tribunal, which devised the following criteria as the typical characteristics of an investment – later known as the Salini test: (1) contribution; (2) assumption of risk; (3) duration; and (4) contribution to the economic development of the host state. Subsequent ICSID tribunals have had differing opinions on the applicability of these criteria. Some have adopted them fully and applied the test rigidly as a jurisdictional requirement, whereas

26 id., para. 27.
28 Fedax NV v. The Republic of Venezuela, ICSID Case No. ARB/96/3, Decision of the Tribunal on Objections to Jurisdiction, 11 July 1997, paras. 18–20. The Fedax v. Venezuela tribunal also referred to the ‘basic features of an investment [that] have been described as involving a certain duration, a certain regularity of profit and return, assumption of risk, a substantial commitment and a significance for the host State’s development’ citing from an academic source at para. 43 of the award.
29 Salini Costruttori SPA and Italstrade SPA v. Kingdom of Morocco, ICSID Case No. ARB/00/4, Decision on Jurisdiction, 23 July 2001, paras. 50–52. The Salini tribunal omitted the fifth criteria of a ‘certain regularity of profit and return’ taken by the Fedax tribunal.
Covered Investment

others have taken a more flexible approach and preferred to apply only some elements of the test, finding that requirements on duration and contribution to economic development of the host state are too subjective to be consistently endorsed.\(^{31}\) A number of other tribunals have chosen to view the Salini criteria as guidance rather than strict jurisdictional requirements capable of depriving a tribunal of its jurisdiction if they are not fully satisfied.\(^{32}\) Some tribunals have even refused to apply the test altogether on the basis that, notwithstanding the reference to investment in Article 25 of the ICSID Convention, it is the investment treaty definition that should prevail as the ultimate expression of contracting parties’ consent.\(^{33}\) At the other end of the spectrum, one tribunal has added two further criteria to the Salini test, namely that assets be invested in good faith and in accordance with host state law\(^{34}\) – an expansion criticised by subsequent tribunals.\(^{35}\)

The Salini test has found little support outside the ICSID framework. Two notable exceptions are Romak v. Uzbekistan and Alps Finance v. Ukraine, in which tribunals constituted under the UNCITRAL Arbitration Rules applied the elements of the Salini test as the ‘objective characteristics of an investment’, declining jurisdiction on both occasions.\(^{36}\) However, the approach of these tribunals has been attributed to the specific facts of these cases\(^{37}\) since Romak v. Uzbekistan involved a mere sale of wheat as the alleged investment, and Alps Finance v. Ukraine an assignment of receivables. The definition of investment in both

\(^{31}\) See, e.g., Pantechniki SA Contractors & Engineers v. Republic of Albania, ICSID Case No. ARB/07/21, Award, 30 July 2009, paras. 36, 43; Saba Fakes v. Republic of Turkey, ICSID Case No. ARB/07/20, Award, 14 July 2010, paras. 110–112; Quiborax SA, Non Metallic Minerals SA and Allan Fok Kaplin v. Plurinational State of Bolivia, ICSID Case No. ARB/06/2, Decision on Jurisdiction, 27 September 2012, paras. 220, 235.

\(^{32}\) See, e.g., Ambiente Ufficio SPA and Others (Case formerly known as Giordano Alpi and Others) v. Argentine Republic, ICSID Case No. ARB/08/9, Decision on Jurisdiction and Admissibility, 8 February 2013, paras. 479, 481; MCI Power Group LC and New Turbine Inc v. Republic of Ecuador, ICSID Case No. ARB/03/6, Award, 31 July 2007, para. 165.

\(^{33}\) See, e.g., Malaysian Historical Salvors v. The Government of Malaysia, ICSID Case No. ARB/05/10, Decision on the Application for Annulment, 16 April 2009, paras. 73–79; Inmaris Perestroika Sailing Maritime Services GmbH and others v. Ukraine, ICSID Case No. ARB/08/8, Decision on Jurisdiction, 8 March 2010, para. 129; Alpha Projektholding GmbH v. Ukraine, ICSID Case No. ARB/07/16, Award, 8 November 2010, paras. 311–312; Philip Morris Brand Sàrl (Switzerland), Philip Morris Products SA (Switzerland) and Ahal Hermanos SA (Uruguay) v. Oriental Republic of Uruguay, ICSID Case No. ARB/10/7, Decision on Jurisdiction, 2 July 2013, paras. 204–206; Hassan Awidi, Enterprise Business Consultants Inc and Alfa El Corporation v. Romania, ICSID Case No. ARB/10/13, Award, 2 March 2015, paras. 197–199; SGS Société Générale de Surveillance SA v. Republic of Paraguay, ICSID Case No. ARB/07/29, Decision on Jurisdiction, 12 February 2010, para. 93.

\(^{34}\) Phoenix Action Ltd v. Czech Republic, ICSID Case No. ARB/06/5, Award, 15 April 2009, para. 114.

\(^{35}\) Saba Fakes v. Republic of Turkey, ICSID Case No. ARB/07/20, Award, 14 July 2010, para. 112.

\(^{36}\) Romak SA (Switzerland) v. The Republic of Uzbekistan, PCA Case No. AA280 (UNCITRAL Rules), Award, 26 November 2009, paras. 205–207; Alps Finance and Trade AG v. The Slovak Republic, UNCITRAL, Award, 5 March 2011, paras. 240 to 241.

\(^{37}\) See Guancachiri America Inc and Rarelec PLC v. Plurinational State of Bolivia, PCA Case No. 2011-17, Award, 31 January 2014, para. 364, noting that these two cases are ‘very fact-specific that can partially explain their reasoning’; see also White Industries Australia Limited v. The Republic of India, UNCITRAL, Final Award, 30 November 2011, para. 7.4.9.
BITs referred only to ‘claims to money or to any other performance having an economic value’ without linking such claims to an overarching economic activity; and a literal interpretation was found insufficient to determine the existence of a protected investment. In both tribunals’ conclusions, the perceived need to exclude one-off commercial transactions from the protection of a BIT was pivotal, while disregarding the four corners of the BITs in question.

IV EXTENT OF PROTECTION

Apart from traditional types of investments involving interests in infrastructure and public projects, tribunals have extended protection to different types of economic activities, including financial instruments (such as promissory notes, hedging agreements and sovereign bonds), contracts for the provision of services and arbitral awards crystallising a party’s rights and obligations. Some tribunals have preferred to look at the totality of the investment activity rather than individual elements of it to decide whether the entire

38 Romak SA (Switzerland) v. The Republic of Uzbekistan, PCA Case No. AA280 (UNCITRAL Rules), Award, 26 November 2009, paras. 182, 185; Alps Finance and Trade AG v. The Slovak Republic, UNCITRAL, Award, 5 March 2011, para. 230.
41 See the trio of Argentine government bond cases: Abacal and Others (Case formerly known as Giovanni a Beccara and Others) v. Argentine Republic, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility, 4 August 2011; Ambiente Ufficio SPA and Others (Case formerly known as Giordano Alpi and Others) v. Argentine Republic, ICSID Case No. ARB/08/9, Decision on Jurisdiction and Admissibility, 8 February 2013; Giovanni Alemanni and Others v. The Argentine Republic, ICSID Case No. ARB/07/8, Decision on Jurisdiction and Admissibility, 17 November 2014. The recent PoStová banka, a.s. and Istrokapital SE v. Hellenic Republic, ICSID Case No. ARB/13/8, Award, 9 April 2015 decision at paras. 318 to 324, concerning the Greek sovereign bonds in which the tribunal refused to assume jurisdiction because ‘sovereign debt, as indebtedness of a sovereign state has special features and characteristics’ and ‘cannot be equated to private indebtedness or corporate debt’ so that it ruled that the definition of investment referring to ‘loans, claims to money or to any performance under contract having a financial value’ in the relevant BIT could not be extended to sovereign debt.
42 See, e.g., SGS Société Générale de Surveillance SA v. Republic of Paraguay, ICSID Case No. ARB/07/29, Decision on Jurisdiction, 12 February 2010, where a contract for the pre-shipment inspection services with respect to goods to be exported from the host state were accorded protection; see also Malaysian Historical Salvors, SDN, BHD v. The Government of Malaysia, ICSID Case No. ARB/05/10, Decision for the Application for Annulment, 16 April 2009 in which the annulment committee held that a contract for the salvage of a shipwreck would qualify as a covered investment under the BIT, criticising the original tribunal in limiting itself to the analysis of the Salini criteria when rejecting jurisdiction.
43 In ATA Construction, Industrial and Trading Company v. The Hashemite Kingdom of Jordan, ICSID Case No. ARB/08/2, Award, 18 May 2010, para. 117, the tribunal held that the right to arbitration is a distinct investment based on the BIT definition, ‘claims to . . . any other rights to legitimate performance having financial value related to an investment’.

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operation constitutes an investment. To date, most tribunals have been reluctant to consider pre-investment activities and expenditures, which do not ultimately come to fruition, as covered investments.

V IRRELEVANCE OF ORIGIN OF CAPITAL

Unlike some treaties – such as the 1987 Association of Southeast Asian Nations Comprehensive Investment Agreement, which commands that investments are brought into, or derived from investments brought into, the host state territory – most treaties are silent on the origin of capital for the covered investment. In the absence of an express requirement in the treaty, investments made by foreign investors from local funds raised in the host state are treated in the same manner as investments funded with imported capital. Arbitral jurisprudence is settled: the origin of capital is irrelevant for the purposes of finding a covered investment and it is not a requirement that a foreign investor finances the investment from its own resources or that the assets or funds be imported from abroad.

44 See, e.g., Saipem SpA v. The People's Republic of Bangladesh, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007, para. 110, which considered that the entire operation including the underlying contract, the construction itself, the retention money, the warranty and the related ICC Arbitration was an investment under Article 25 of the ICSID Convention; see also White Industries Australia Limited v. The Republic of India, Final Award, para. 7.6.8, where the tribunal regarded the rights under an ICC award as 'a continuation or transformation of the original investment' after India inordinately delayed the enforcement of the arbitral award in India; see also Chevron Corp & Texaco Petroleum Co v. The Republic of Ecuador, Third Interim Award on Jurisdiction and Admissibility, PCA Case No, 2009-23, 27 February 2012, paras. 4.35–4.36; Mamidoil Jetoil Greek Petroleum Products Societe Anonyme SA v. Republic of Albania, ICSID Case No. ARB/11/24, Award, 30 March 2015, paras. 285 to 288.

45 See Mihaly International Corporation v. Democratic Socialist Republic of Sri Lanka, ICSID Case No. ARB/00/2, Award, 15 March 2002, paras. 48–51, where after extensive negotiations the parties never signed a contract for the construction and operation of a power plant. In PSEG Global Inc and Konya Ilgin Elektrik Üretim ve Ticaret Limited Şirketi v. Republic of Turkey, ICSID Case No. ARB/02/5, Decision on Jurisdiction, 4 June 2004, however, the tribunal found jurisdiction because a concession contract was actually signed for a power plant, and was valid and legally binding even though the project was never carried out.

46 See Yang Chi Oo Trading Pte Ltd v. Government of the Union of Myanmar, ASEAN I.D. Case No. ARB/01/1, Award, 31 March 2003, applying the relevant wording in Article II of the treaty providing that: 'This Agreement shall apply only to investments brought into, derived from or directly connected with investments brought into the territory of any Contracting Party by nationals or companies of any other Contracting Party and which are specifically approved in writing and registered by the host country and upon such conditions as it deems fit for the purposes of this Agreement.'

47 See Mera Investment Fund Limited v. Republic of Serbia, ICSID Case No. ARB/17/2, Decision on Jurisdiction, 30 November 2018, paras. 147 and 170.
In a well-known dissenting opinion in *Tokios Tokelés* 48 Professor Weil differed sharply from his co-arbitrators by taking the view that economic reality should prevail over formal legal structure when it comes to the interpretation of both the ICSID Convention and the specific provisions of BITs for the purposes of ascertaining an international investment. In his view, the ICSID system dictates a ‘transborder flux of capital’; for that reason, he disagreed with the majority in *Tokios Tokelés* who permitted claims against Ukraine by a Lithuanian entity wholly owned by Ukrainian nationals, while concluding that the origin of capital is irrelevant. Professor Weil’s opinion advocating the imposition of a jurisdictional requirement without a textual foundation as to the origin of capital is yet to find support in arbitral jurisprudence.

VI TERRITORIAL LIMITATIONS ON COVERED INVESTMENT

Most treaties place a territorial limit requiring that a covered investment be ‘made in the territory of the host state’. Some do not expressly refer to such territorial limits in the definition of ‘investment’ but instead refer to ‘investments in the territory of a Contracting Party’ within the context of the substantive obligations and protections under the treaty. Either way, arbitral tribunals examine the territorial nexus of an investment to the host state at the jurisdictional stage regardless of where this requirement is postulated. 49

Two examples from NAFTA cases illustrate the relevance of territorial connection. *Bayview v. Mexico* 50 was a claim brought by an American claimant in relation to its investment in farm and irrigation facilities in the United States involving alleged deleterious effects of Mexico’s use of the waters of the Rio Grande, on which the claimant’s enterprise was dependent. The NAFTA tribunal did not allow the claim under NAFTA Article 1101 on the basis that the investment in question was wholly confined to the territory of the United States. A similar issue arose in *Canadian Cattlemen for Fair Trade v. United States*, in which a group of Canadian cattle producers challenged a US prohibition on live-cattle imports from Canada after an outbreak of mad cow disease. The cattle businesses of the claimants were located entirely in Canada and therefore the tribunal dismissed the claim for lack of investment in the territory of the United States. 51

Contrary to traditional investments, such as acquisition of interests in immovable property or companies, tribunals draw a distinction for territorial nexus when it comes to investments of a financial nature. It is well established that, with regard to investments of a purely financial nature, the territorial determination should focus on where, or for the

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50 *Bayview Irrigation District et al v. United Mexican States*, ICSID Case No. ARB(AF)/05/1, Award, 19 June 2007, paras. 93 to 108.
benefit of whom, the funds are ultimately used, and not the place where the funds were paid out or transferred. Therefore, the relevant question is whether the benefit is enjoyed in the host state.\textsuperscript{52}

At times, respondent states have questioned whether a portfolio investment bought and paid for outside the host state with no flow of direct funds into the host state can be deemed to be invested ‘in the territory’ of the host state. For example, a trio of cases against Argentina involving bondholders who purchased Argentinian sovereign bonds in the secondary market turned on this question. Argentina argued that these transactions outside Argentina did not involve a direct flow of funds into the territory of Argentina and therefore the claims in relation to these bonds were not claims in relation to a covered investment. The dissenting opinion by Professor Abi-Saab in \textit{Abaclat v. Argentina} found that submission to be persuasive, stating that ‘such financial products with high velocity of circulation . . . traded within seconds at the touch of a button in capital markets, with no involvement or knowledge of the borrowing country, nor passage through the territory or the legal system of that State’, lacked the necessary territorial link to the host state.\textsuperscript{53} However, most tribunals considering financial investments (such as the Argentinian sovereign bonds or the hedging agreements as in \textit{Deutsche Bank v. Sri Lanka}) have not followed the approach of Professor Abi-Saab in his dissenting opinion.\textsuperscript{54} Rather, they have been satisfied that a sufficient territorial nexus exists as long as funds were made available to host states and served to finance their economy or needs. They all assigned weight to the fact that it was the state itself that ultimately benefited from the disbursement of funds even if these funds never entered their territory directly.\textsuperscript{55}

\textsuperscript{52} \textit{Fedax NV and The Republic of Venezuela}, ICSID Case No. ARB/96/3, Decision of the Tribunal on Objections to Jurisdiction, 11 July 1997, paras. 41–43; \textit{Abaclat and Others (Case formerly known as Giovanna a Beccara and Others) v. Argentine Republic}, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility, 4 August 2011, para. 374; \textit{Ambiente Ufficio SPA and Others (Case formerly known as Giordano Alpi and Others) v. Argentine Republic}, ICSID Case No. ARB/08/9, Decision on Jurisdiction and Admissibility, 8 February 2013, paras. 498–499, 508–510; \textit{British Caribbean Bank Ltd. v. Government of Belize}, PCA Case No. 2010-18/BCB-BZ, Award, 19 December 2014, paras. 206 and 207.

\textsuperscript{53} Dissenting Opinion of Abi-Saab in \textit{Abaclat and Others (Case formerly known as Giovanna a Beccara and Others) v. Argentine Republic}, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility, 4 August 2011, paras. 56 and 57, 78, 105. Argentina’s appointee in the sister case \textit{Ambiente v. Argentina}, Professor Santiago Torres Bernardez, held a similar opinion to Professor Abi-Saab; see Dissenting Opinion of Bernardez in \textit{Ambiente Ufficio SPA and Others (Case formerly known as Giordano Alpi and Others) v. Argentine Republic}, ICSID Case No. ARB/08/9, Decision on Jurisdiction and Admissibility, 8 February 2013, paras. 262 and 263.

\textsuperscript{54} \textit{Deutsche Bank AG v. Democratic Socialist Republic of Sri Lanka}, ICSID Case No. ARB/09/02, Award, 31 October 2012, paras. 288, 292. See also \textit{Ambiente Ufficio SPA and Others (Case formerly known as Giordano Alpi and Others) v. Argentine Republic}, ICSID Case No. ARB/08/9, Decision on Jurisdiction and Admissibility, 8 February 2013.

\textsuperscript{55} Contrast with \textit{Poštová banka, a.s. and ISTROKAPITAL SE v. Hellenic Republic}, ICSID Case No. ARB/13/8, Award, 9 April 2015, paras. 293–349, where the opposite conclusion was reached.
VII COMPLIANCE WITH HOST STATE LAW

Some treaties expressly require that an investment be made in accordance with host state law, while others are silent on the point.\(^{56}\) For treaties that include a form of conformity with host state law as part of the covered investment definition, tribunals have accepted that any illegality or breach of local law in the making of the investment would act as a jurisdictional bar.\(^{57}\) Where the treaty is silent on the issue, however, tribunals have reached different conclusions when addressing questions of non-conformity with local laws. A number of tribunals, such as the Phoenix tribunal, have suggested that conformity with host state law is an implied requirement for an investment to be a protected investment under an investment treaty and Article 25 of the ICSID Convention, even if the definition of investment in the treaty is silent on this issue.\(^{58}\) These tribunals have concluded that a state cannot be deemed to offer access to the ICSID dispute settlement mechanism to investments made in violation of its own law.\(^{59}\)

Other tribunals have, however, disagreed with this rationale, suggesting that states are at liberty (or not) to condition their consent to arbitrate, as well as the protections they offer, on compliance with host state law. If they have not done so, conformity with host state law cannot be part of the objective definition of ‘investment’ or relied upon to deprive the tribunal of its jurisdiction. It may give rise to an admissibility defence or a defence on the merits since recourse to treaty arbitration and substantive treaty protections may in certain circumstances breach the prohibition of abuse of rights that is an emanation of the principle of good faith. However, that does not mean that these elements are part of the definition of ‘investment’. An illegal or bad-faith investment remains an investment.\(^{60}\)

Tribunals have not always sought to draw a clear distinction between the different types of non-conformity with local law. In the face of an investor’s non-conformity, some tribunals have only penalised the investor for a breach of domestic regulation relating to the investment activity or admission of the investment.\(^{61}\) Other tribunals have interpreted non-conformity

\(^{56}\) Some treaties have a specific provision clarifying that the host state shall admit investments made in accordance with its laws from which tribunals have also inferred the same requirement, See, e.g., Saluka Investments BV v. Czech Republic, UNCITRAL, Partial Award, 17 March 2006, para. 204.

\(^{57}\) See, e.g., Incesa Vallisoletana SL v. Republic of El Salvador, ICSID Case No, ARB/03/26, Award, 2 August 2006, para. 335; Fraport AG Frankfurt Airport Services Worldwide v. Philippines, ICSID Case No. ARB/03/25, Award, 16 August 2007, para. 398; Alasdair Ross Anderson et al. v. Republic of Costa Rica, ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010, paras. 46, 55, 57 and 58.

\(^{58}\) Phoenix Action Ltd v. Czech Republic, ICSID Case No. ARB/06/5, Award, 15 April 2009, para. 101. The tribunal cited Plama Consortium Limited v. Republic of Bulgaria, ICSID Case No. ARB/05/24, Award, 27 August 2008, which held that the conformity requirement is implicit even when it is not expressly cited in the BIT (see Plama v. Bulgaria at paras. 138 to 143).


\(^{60}\) See, e.g., Quiborax SA, Non Metallic Minerals SA and Allan Fisk Kaplin v. Plurinational State of Bolivia, ICSID Case No. ARB/06/2, Decision on Jurisdiction, 27 September 2012, para. 226; Metal-Tech Ltd v. Republic of Uzbekistan, ICSID Case No. ARB/10/3, Award, 4 October 2013, para. 127; Liman Caspian Oil BV and NCL Dutch Investment BV v. Republic of Kazakhstan, ICSID Case No. ARB/07/14, Excerpts of Award, 22 June 2010, para. 187; Saba Fakes v. Republic of Turkey, ICSID Case No. ARB/07/20, Award, 14 July 2010, paras. 114, 119.

\(^{61}\) See, e.g., Fraport AG Frankfurt Airport Services Worldwide v. Republic of the Philippines, ICSID Case No. ARB/03/25, Award, 16 August 2007, para. 398; Alasdair Ross Anderson et al. v. Republic of Costa Rica,
to condemn a wider illegality or iniquity in the investor’s behaviour; some have even extended the analysis of non-conformity beyond domestic law to encompass breaches of general principles of international law and international public policy.

Where arbitral tribunals have resorted to general principles of law or international public policy, they have mostly framed this as an emanation of the clean hands doctrine, on the basis that protection should be denied to investments that are made by way of fraud, corruption or deceitful conduct, and that denial is required to prevent the misuse of the international investment protection system by those who come with unclean hands. That means, regardless of whether the treaty includes an express requirement for compliance with domestic or international law, there is the possibility that a tribunal may deny treaty protection to a clearly abusive claim based on general principles of law on its own accord.

Unlawfulness is a difficult issue and one that is potentially open to abuse by states that have been complicit in the alleged wrongdoing on which they rely as a defence to an arbitration claim. There is also the question of degree; tribunals are reluctant to refuse a claim where the contravention of law in question is one of a technical or de minimis nature and it is uncertain as to where the line between fundamental versus trivial breaches should be drawn. Even where the contravention is more serious, there remains the issue of whether a state is released from an investment treaty claim if the state itself has required the investor to contravene the laws when making the investment.

ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010, para. 55; Rusoro Mining Ltd v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/12/5, Award, 22 August 2016, paras. 289–344.


See Inceysa Vallisoletana SL v. Republic of El Salvador, ICSID Case No. ARB/03/26, Award, 2 August 2006, paras. 224–227 and Plama Consortium Limited v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Award, 27 August 2008, paras. 144–146, where both tribunals directed themselves back to international law based on the reference to international law in the applicable substantive law.

See, e.g., Plama Consortium Limited v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Award, 27 August 2008, paras. 141, 143–144; Gustav F W Hamester GmbH & Co KG v. Republic of Ghana, ICSID Case No. ARB/07/24, Award, 18 June 2010, paras. 123–124 (an investment will not be protected if it has been created in violation of national or international principles of good faith; by way of corruption, fraud, or deceitful conduct; or if its creation itself constitutes a misuse of the system of international investment protection under the ICSID Convention[;] or . . . if it is made in violation of the host State's law . . . These are general principles that exist independently of specific language to this effect in the Treaty.); Churchill Mining Plc and Planet Mining Pty Ltd v. Republic of Indonesia, ICSID Case No. ARB/12/14 and 12/40, Award, 6 December 2016, paras. 488 to 508. See also World Duty Free Company Limited v. Republic of Kenya, ICSID Case No. ARB/00/7, Award 4 October 2006, paras. 137 to 157, where the question arose under an investment agreement governed by English law as opposed to a treaty under international law.

For e.g., the minor defect in company paperwork at issue in Alpha Projekt Holding GmbH v. Ukraine, ICSID Case No. ARB/07/16, Award, 8 November 2010, para. 297, did not prevent the tribunal from assuming jurisdiction. Similarly, in a recently released award, Peter A Allard v. The Government of Barbados, PCA Case No. 2012-06, Award on Jurisdiction, 13 June 2014 at paras. 92–94, the tribunal characterised non-compliance with exchange control legislation by the claimant as ‘inadvertent and technical’, and noted that there was nothing offensive to public policy or tainted with criminality. It further concluded that in the absence of the breach of fundamental legal principles of Barbados there is no reason to deny jurisdiction.
VIII CONCLUSION

The definition of a covered investment remains one of the most controversial topics in investment law and it is impossible to identify one agreed definition; the wording of international treaties is inconsistent and the arbitral jurisprudence is, in places, contradictory. The preponderance of generic definitions of investment within treaties means that a substantial degree of subjectivity cannot be excluded in their application to the specific facts of each case. The conflicting ways in which arbitral tribunals have construed similar wording do not make the task any more straightforward. Critics of investor–state arbitration find encouragement from the perceived lack of consistency and coherence in arbitral awards. For example, the paucity of tribunal agreement on the precise scope and application of the Salini criteria to the definition of investment within the ICSID framework (let alone in general) is cited as one of the principal reasons for questioning the legitimacy of the system and its participants.

That said, there does appear to be a trend emerging in the new generation FTAs and BITs in favour of an objective definition of ‘investment’ whereby states expressly import chosen aspects of the Salini criteria directly into their definitions of ‘investment’. It remains to be seen how tribunals interpreting these instruments will contribute to the current debate.66 Certainly, if states choose to make the Salini, or any other, criteria part of the ‘investment’ definition in the text of a treaty, tribunals would be expected to give weight to such express wording when interpreting the treaty’s terms ‘in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose’ as required under Article 31 of the Vienna Convention on the Law of Treaties.

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66 For example, the UNCITRAL claim filed in June 2016 by US hedge funds, Gramercy Funds Management LLC and Gramercy Peru Holdings LLC, against Peru under the US–Peru Trade Promotion Agreement of 2009 (TPA) is a case to watch. Similar to the new generation FTAs discussed in this chapter, the definition of investment in the TPA incorporates ‘characteristics of investment’ into the definition, including ‘the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk’. See the Statement of Claim as reported in IA Reporter, 9 June 2016: http://www.iareporter.com/articles/analysis-as-gramercy-fund-pursues-1-6-billion-bond-arbitration-against-peru-how-does-its-initial-case-stack-up-on-key-jurisdictional-fronts/ (accessed on 12 March 2019).
Chapter 2

COVERED INVESTORS

Patrick W Pearsall and David Manners-Weber

I INTRODUCTION

Who qualifies as a ‘covered investor’ under an international investment agreement? Whether an investor is covered by the state's offer to arbitrate certain claims is a critical question that often lies at the heart of jurisdictional disputes. If a state has not consented to arbitration with an investor, an arbitral tribunal has no jurisdiction to hear that investor’s claim.

As a general matter, covered investors are (1) persons (either natural or juridical) (2) with the requisite nationality who (3) have control over an investment that is entitled to protection under a given agreement. This chapter addresses common issues concerning such investors; it does not take a position on the proper way to approach or resolve these questions for any particular dispute. Whether an investor is covered in a specific case depends on the specific agreement at issue and the facts underlying the dispute.

II GENERAL PRINCIPLES RELATED TO NATIONALITY AND CONTROL

i Nationality

Under most international investment agreements (IIAs), to qualify for protection, an investor must be a national of a contracting state other than the host state in which they are investing. To claim protection, an investor must typically have the relevant nationality at the time of the events giving rise to the claim. Although the investor may be able to preemptively structure its investment to gain an IIA’s protection, tribunals may look unfavourably on an investor’s attempt to manufacture the requisite nationality after an alleged breach solely to bring a claim. Indeed, tribunals have largely rejected such post hoc attempts as ‘forum shopping’.

1 Patrick W Pearsall is a partner and chair of the public international law practice at Jenner & Block LLP, where David Manners-Weber is an associate.
3 Rudolf Dolzer & Christoph Schreuer, Principles of International Investment Law 54 (2d ed. 2012) (‘It appears from these cases that prospective planning within the framework of existing treaties will be accepted by tribunals. . . . What appears to be impossible is to create a remedy for existing grievances, in particular after a dispute has arisen, by arranging for a desirable nationality’).
4 Zachary Douglas, The International Law of Investment Claims 290 (2009) (‘There cannot . . . be a restructuring of the investment in order to resort to the dispute resolution provisions of an investment treaty once a dispute has arisen. Treaty shopping is acceptable; forum shopping is not’). See also Mobil Corp. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/07/27, Decision on Jurisdiction, 10 June 2010, para. 205; Phoenix Action, Ltd. v. Czech Republic, ICSID Case No. ARB/06/5, Award, 15 April 2009, para. 144 (finding ‘an abuse of the system of international ICSID investment arbitration’ where a Czech investor tried to bring a pre-existing claim against the Czech Republic under the Israel–
Tribunals have also confronted the question of how long an investor must retain the requisite nationality. That is, while the investor must be an appropriate national at the date giving rise to the claim, must they also have that nationality later in the proceedings? Must it be continuous?\(^5\) Under the traditional rules of diplomatic protection, whereby a state could bring a claim against another state based on an injury to one of its nationals, nationality must indeed be continuous.\(^6\) In the context of diplomatic protection, the continuous nationality requirement ‘ensures that the State seeking to protect a person has a proper interest in such protection.’\(^7\) The International Law Commission’s Draft Articles on Diplomatic Protection reflect this approach, requiring continuous nationality from the date of the events giving rise to the claim until the date of claim submission.\(^8\) Whether a continuous nationality requirement exists in the context of an IIA, however, will depend on that agreement’s language.

Article 25(2) of the ICSID Convention requires that a juridical person has the requisite nationality on the date of consent to arbitration; a natural person must have the requisite nationality on the date of consent and on the date the claim is registered by ICSID.\(^9\) One tribunal interpreted this language to mean that there is no requirement under the ICSID Convention that nationality be continuous from the time the claim arises.\(^10\)

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5. Compare *Loewen Group, Inc. v. United States of America*, ICSID Case No. ARB(AF)/98/3, Award, 26 June 2003, para. 225. (“In international law parlance, there must be continuous national identity from the date of the events giving rise to the claim, which date is known as the *dies a quo*, through the date of the resolution of the claim, which date is known as the *dies ad quem*’) with *Waguih Elie George Siag v. Arab Republic of Egypt*, Award, ICSID Case No. ARB/05/15, Award, 1 June 2009, paras. 497–99 (noting several critiques of *Loewen* and expressing the tribunal’s view that ‘the ICSID Convention does not require a party to hold constant nationality until the date of the award’).


8. See International Law Commission, note 6, at 31, 38–39 (commenting upon the text of Articles 5 and 10).

9. See also *Vladislav Kim v. Republic of Uzbekistan*, ICSID Case No. ARB/13/6, Decision on Jurisdiction, 8 March 2017, paras. 190–91 (stating that under the ICSID Convention and the Kazakhstan–Uzbekistan BIT, the natural investor needed to demonstrate nationality on the date of the alleged breach, the date of the claim’s submission to ICSID and the date the claim was registered by ICSID); *Waguih Elie George Siag v. Arab Republic of Egypt*, Decision on Jurisdiction, 11 April 2007 para. 206 (*Waguih Elie George Siag*) (“The Tribunal . . . finds that the relevant dates under the Convention are the date of consent and the date of registration’); *Ioan Micula v. Romania*, ICSID Case No. ARB/05/20, Decision on Jurisdiction and Admissibility, 24 September 2008, para. 111 (‘Pursuant to Article 25(2)(b) of the ICSID Convention, the relevant date for determining the nationality of the Corporate Claimants is the date of the consent to submit the dispute to ICSID arbitration, i.e., the date of the Request’).

10. See *Waguih Elie George Siag*, note 9, at paras. 205-06.
Control

To bring a dispute to arbitration, the investor typically must own or have control of the investment.\(^\text{11}\) Many IIAs, however, do not define what ‘control’ means.\(^\text{12}\) One ICSID decision defined it as legal control, rather than ‘actual day-to-day’ control.\(^\text{13}\) It found that, generally, ‘legal capacity is to be ascertained with reference to the percentage of shares held’, though minority shareholders could also demonstrate legal control ‘by reason of the percentage of shares held, legal rights conveyed in instruments or agreements such as articles of incorporation or shareholders’ agreements, or a combination of these’.\(^\text{14}\)

A number of treaties contain language protecting investors that exercise ‘direct or indirect’ control over an investment. The 2012 US Model BIT, for instance, refers to assets ‘that an investor owns or controls, directly or indirectly’.\(^\text{15}\) Similarly, the BIT between Canada and China protects investments ‘owned or controlled directly or indirectly by an investor’ of the contracting state.\(^\text{16}\) In such cases, it has been argued that nationals of a contracting state who hold their investments through intermediaries can nevertheless bring claims – even if those intermediaries do not have the same nationality.\(^\text{17}\)

Though it is possible that an investor might be required to continuously retain the requisite nationality, ‘there is no rule of continuous ownership of the investment’.\(^\text{18}\) As one tribunal said, ‘the issues addressed by [ICSID and BIT] instruments are precisely those of confiscation, expropriation and nationalisation of foreign investments. Once the taking has occurred, there is nothing left except the possibility of using the ICSID/BIT mechanism. That purpose would be defeated if continuous ownership were required.’\(^\text{19}\) Instead, the investor is generally required to control the investment only at the time of the events giving rise to the claim – not before or afterwards.\(^\text{20}\)

\(^{11}\) See Douglas, note 4, at 299-300.
\(^{12}\) See id., at 299–300.
\(^{13}\) Aguas del Tunari, S.A. v. Republic of Bolivia, ICSID Case No. ARB/02/3, Decision on Respondent’s Objections to Jurisdiction, 21 October 2005 (Aguas del Tunari), para. 264.
\(^{14}\) id.
\(^{15}\) Available at https://www.state.gov/documents/organization/188371.pdf.
\(^{16}\) Available at https://investmentpolicyhub.unctad.org/Download/TreatyFile/3476.
\(^{17}\) See Aguas del Tunari, note 13, at para. 236.
\(^{18}\) El Paso Energy International Company v. The Argentine Republic, ICSID Case No. ARB/03/15, Decision on Jurisdiction, 27 April 2006 (El Paso Energy International Company), para 135. See also Mondev International, Ltd. v. United States of America, ICSID Case No. ARB(AF)/99/2, Award, 11 October 2002, para. 91 (applying a similar logic in the context of the NAFTA: ‘To require the claimant to maintain a continuing status as an investor under the law of the host State at the time the arbitration is commenced would tend to frustrate the very purpose of Chapter 11, which is to provide protection to investors against wrongful conduct including uncompensated expropriation’).
\(^{20}\) See Daimler Financial Services AG v. Argentine Republic, ICSID Case No. ARB/05/1, Award, 22 August 2012, para. 145 (according standing to any qualifying investor under the relevant treaty texts who suffered damages as a result of the allegedly offending governmental measures at the time that those measures were taken’) (emphasis in original).
III  NATURAL PERSONS

Generally, a natural person is considered a national under an IIA if he or she is considered a national under the state party's own law.²¹ Tribunals have found, however, that although nationality may be defined by the state party’s own law, ‘where . . . the jurisdiction of an international tribunal turns on an issue of nationality, the international tribunal is empowered, indeed bound, to decide that issue’.²² Accordingly, in certain circumstances a tribunal may be empowered to determine whether an investor qualifies as a national even in contradiction of that nation’s own findings of fact.²³

Depending on the IIA, an investor may bring a claim if he or she has dual nationality with both a contracting state and a non-contracting state. Some have opined that there is no issue under the Energy Charter Treaty, for instance, given the ordinary meaning of the treaty’s language: Article 26(1) refers to ‘[d]isputes between a Contracting Party and an Investor of another Contracting Party’.²⁴ Likewise, several commentators and tribunals have found that dual nationality does not present a problem under the ICSID Convention.²⁵ Tribunals have rejected arguments that a claimant’s nationality must be ‘effective’²⁶ – that is, that the claimant must show a genuine link with the contracting state through which he or she brings his or her claim.²⁷ One tribunal said, ‘[A]s regards dual nationals who do not hold the nationality of the host State . . . the ICSID drafters did not subject their access to ICSID jurisdiction to the effective nationality test’.²⁸

Typically, however, a dual national cannot bring a claim if one of his or her nationalities is that of the host state.²⁹ Article 25(2)(a) of the ICSID Convention specifically excludes ‘any person who [on the relevant dates] also had the nationality of the Contracting State party to the dispute’. One ICSID tribunal found that such dual nationals are excluded even when his or her nationality with the host state is no longer effective.³⁰

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²¹ See, e.g., Hussein Nuaman Soufraki v. The United Arab Emirates, ICSID Case No. ARB/02/7, Award, 7 July 2004 (Hussein Nuaman Soufraki), para 55. (‘It is accepted in international law that nationality is within the domestic jurisdiction of the State, which settles, by its own legislation, the rules relating to the acquisition (and loss) of its nationality’).

²² id.

²³ In Hussein Nuaman Soufraki, note 21, the claimant asserted he was an Italian citizen protected by the BIT between Italy and the UAE. He provided the court with five Certificates of Nationality, copies of his Italian passports and a letter from the Italian Ministry of Foreign Affairs that explicitly declared Soufraki was entitled to invoke the ICSID/BIT forum on the basis of his Italian citizenship. Para. 14. The panel, however, stated that it ‘will in the end decide for itself whether, on the facts and law before it, the person whose nationality is at issue was or was not a national of the State in question’. Para. 55. It found that under Italian law, Soufraki – unbeknown to him – had forfeited his citizenship when he acquired Canadian nationality and residence, para. 52, and so the tribunal lacked jurisdiction to hear the dispute, para. 84.


²⁵ id., at 96–97. The Preliminary Draft of the ICSID Convention explicitly permitted investors who possessed the nationality of both a contracting and non-contracting state to be covered. id., at 97.

²⁶ Dolzer & Schreuer, note 3, at 46 (noting cases).

²⁷ For more on effective nationality, see Nottebohm (Liechtenstein v. Guatemala), 18 November 1953, [1955] ICJ Reports 111.

²⁸ Saba Fakes v. Republic of Turkey, ICSID Case No. ARB/07/20, Award, 14 July 2010, para. 63.

²⁹ Dolzer & Schreuer, note 3, at 46.

³⁰ Champion Trading Company v. Arab Republic of Egypt, ICSID Case No. ARB/02/9, Decision on Jurisdiction, 21 October 2003, section 3.4.1.
It is recommended to always consult the relevant IIA, however, because there is not necessarily a common approach to these questions. The US 2012 Model BIT, for instance, states that ‘a natural person who is a dual national shall be deemed to be exclusively a national of the State of his or her dominant and effective nationality’. Some understand this language to permit a dual national to bring a claim against the host state even if the claimant were also a national of that state, so long as it was not their ‘dominant and effective’ nationality.

IV  JURIDICAL PERSONS

Unincorporated entities will generally not enjoy legal protection unless specified by the IIA. Article 25(2)(b) of the ICSID Convention, which defines the nationality of juridical persons, requires legal personality – ‘a mere association of individuals or of juridical persons would not qualify.’ As a related point, entities that lack the capacity to sue under the law under which they were formed will not generally be able to sue under an IIA.

i  The nationality of juridical persons

Determining the nationality of a corporation can sometimes be more complicated than defining the nationality of a natural person. The ICSID Convention does not impose any particular test for the nationality of juridical persons not having the nationality of the host State, and there are several methods to determine corporate nationality. Sometimes the same IIA may incorporate multiple tests or adopt separate definitions of corporate nationality for each party. One of the more common tests to determine a company’s nationality is to look at the law under which the company was incorporated. The US Model BIT of 2012, for instance, describes an ‘enterprise of a Party’ as ‘an enterprise constituted or organized under the law of a Party’; the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) does the same. Some respondents have objected to this test, arguing that businesses must also show a bona fide connection to the state under which they claim nationality. ICSID tribunals have generally rejected such arguments, finding that contracting state parties

31 Available at https://www.state.gov/documents/organization/188371.pdf. The ‘dominant and effective’ test draws from the Iran–US Claims Tribunal Case No. A/18 (6 April 1984) 5 Iran-USCTR 251. For a discussion of this case, see McLauchlan et al., note 2, at 134-35.
32 Dolzer & Schreuer, note 3, at 47.
34 Douglas, note 4, at 312.
35 Dolzer & Schreuer, note 3, at 47.
37 Dolzer & Schreuer, note 3, at 47.
38 id.
39 Article 9.1. The CPTPP’s definition of ‘enterprise of a Party’ additionally includes ‘a branch [of an enterprise] located in the territory of a Party and carrying out business activities there’.
'should be given the widest possible latitude to agree on the meaning of “nationality”', and that ‘it is not open to the Tribunal to add other requirements which the parties themselves could have added but which they omitted to add.'

Other treaties’ definitions of nationality may include the corporate seat ‘siége social’. The particular meaning of siége social within a given agreement, however, may be the subject of contention: tribunals have found the phrase is not a “legal term of art,” with only one meaning. Instead, it can be ‘susceptible of either a formal or substantive meaning — it ‘can either be statutaire, referring to the seat appearing in the company’s bylaws or statutes, or réel, referring to the effective seat where the company is actually managed’. Recent tribunals have diverged when interpreting the term in the context of Belgium–Luxembourg Economic Union (BLEU) BITs.

Some IIAs require a bond of economic substance between the corporate investor and the state of its purported nationality. This bond might consist of ‘effective control’ over the corporation by nationals or the company having ‘genuine economic activity’ within the

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40 Tokios Tokelės v Ukraine, ICSID Case No. ARB/02/18, Decision on Jurisdiction, 29 April 2004 (Tokios Tokelės), para. 25.
41 Saluka Investments B.V. v. The Czech Republic, UNCITRAL, Decision on Jurisdiction, 7 May 2004, para. 240. See also Tokios Tokelės, note 40, at para. 36 (‘In our view, it is not for tribunals to impose limits on the scope of BITs not found in the text, much less limits nowhere evident from the negotiating history’).

In Tokios Tokelės, a Lithuanian company invoked the Lithuania–Ukraine BIT to bring ICSID arbitration proceedings against Ukraine. Ukraine objected, contending that the company was not a ‘genuine entity’ of Lithuania because, among other things, Ukrainian nationals owned 99 percent of the company’s shares and comprised two-thirds of its management. Para. 21. It argued that to allow a suit under these circumstances would thwart the object and purpose of the ICSID Convention by effectively ‘allowing Ukrainian nationals to pursue international arbitration against their own government’. Para. 22. The tribunal rejected Ukraine’s arguments. It noted that Article 1(2) of the BIT defined corporate nationality as ‘any entity established in the territory of the Republic of Lithuania in conformity with its laws and regulations’, and so found the company to be a Lithuanian national.

43 id., (emphasis in original).
44 Orascom TMT Investments S.à r.l. v. People’s Democratic Republic of Algeria, ICSID Case No. ARB/12/35, Final Award, 31 May 2017 (Orascom TMT Investments S.à r.l.), para. 273.

In Tenaris S.A. & Tallta-Trading, note 42, an ICSID tribunal was asked to interpret the term in the context of the BLEU–Venezuela BIT, which coupled a siége social requirement with a law of incorporation requirement. The tribunal found siége social to mean ‘the place of actual or effective management’, para. 154, because, were it to mean the ‘purely formal matter of the address of a registered office or statutory seat’, the term would be superfluous given that relevant laws of incorporation already encompassed a registered office requirement. Para. 150. In Capital Financial Holdings Luxembourg S.A. v. Republic of Cameroon, the tribunal followed the same approach. ICSID Case No. ARB/15/18, Award, 22 June 2017, para. 263. In Orascom TMT Investments S.à r.l., note 44, however, the tribunal rejected Tenaris S.A. & Tallta-Trading’s reasoning. Para. 287. Instead, when interpreting the BLEU–Algeria BIT, it found that siége social referred to a corporation’s ‘registered office’. It found this interpretation did not render the term superfluous under the BIT, even as the relevant law of incorporation already required a registered office; rather, it found that ‘the BIT simply spells out the place of incorporation text by specifying the two elements generally associated with it (constitution in accordance with local law and registered office).’ Para. 298.
Such a requirement can be designed to prevent ‘treaty shopping’, where investors with no real connection to a country structure their holdings so that they can claim protection under a favourable BIT.

ii Denial of benefits

Some IIAs contain ‘denial of benefits’ clauses to preclude certain investors – typically, those with no meaningful connection to a contracting state – from taking advantage of an IIA’s protections. Under such a clause, states reserve the right to deny a company of another party the benefits of the IIA in certain circumstances, such as if the company has no substantial business activities within the state party of its incorporation. For instance, Article 9.15 of the CPTPP reads, in part:

A Party may deny the benefits of this Chapter to an investor of another Party that is an enterprise of that other Party and to investments of that investor if the enterprise:
(a) is owned or controlled by a person of a non-Party or of the denying Party; and
(b) has no substantial business activities in the territory of any Party other than the denying Party.

The Comprehensive Economic and Trade Agreement between the European Union and Canada has a denial of benefits clause allowing contracting states to deny benefits to a corporate investor if the investor’s owners are nationals of a third-party state that is subject to sanctions. Article 8.16 states:

A Party may deny the benefits of this Chapter to an investor of the other Party that is an enterprise of that Party and to investments of that investor if:
(a) an investor of a third country owns or controls the enterprise; and
(b) the denying Party adopts or maintains a measure with respect to the third country that:
(i) relates to the maintenance of international peace and security; and
(ii) prohibits transactions with the enterprise or would be violated or circumvented if the benefits of this Chapter were accorded to the enterprise or to its investments.

Tribunals have differed as to whether a denial of benefits clause needs to be invoked before arbitration has been sought. Though a denial of benefits clause may be substantively similar to a restricted definition of ‘investor’ based on bonds of economic substance, the burden of

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46 Dolzer & Schreuer, note 3, at 49 (emphasis removed). See, e.g., the 2012 BIT between Egypt and Switzerland, protecting entities ‘which are constituted or otherwise duly organized under the law of that Contracting Party and have their statutory seat, together with real economic activities, in the territory of the same Contracting Party’. Available at https://investmentpolicyhub.unctad.org/Download/TreatyFile/1113.

47 Compare, e.g., Guaracachi America, Inc. v. The Plurinational State of Bolivia, UNCITRAL, Award, 31 January 2014 para. 376 (Guaracachi America, Inc.) (finding that “it is proper that the denial is “activated” when the benefits are being claimed’, and so the denial of benefits may be invoked at the time the claimant seeks arbitration) with Plama Consortium Ltd. v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 8 February 2005, para. 162 (finding the exercise of the Energy Charter Treaty’s ‘denial of benefits’ clause ‘should not have retrospective effect’).
proof can be different – while a claimant generally has the jurisdictional burden of proving that it falls within the definition of ‘investor’, tribunals diverge on who bears the burden of proof once a state invokes a denial of benefit clause.48

iii Foreign control of local companies

‘Host states often require that investments are made through locally incorporated companies.’49 While such local companies might not otherwise qualify as foreign investors, the ICSID Convention makes special allowance for them should a state agree to it. Under Article 25(2)(b) of the ICSID convention, a ‘National of another Contracting State’ includes:

Any juridical person which had the nationality of the Contracting State party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention.

In other words, some IIAs will treat a local company as a foreign investor – namely, as eligible to bring an international arbitration claim – if they are foreign-controlled and the state consents to it. States may consent in either a direct contract with the investor or by a blanket offer of consent via IIA. In the latter case, the IIA will usually state more broadly that local companies controlled by nationals of the other state will be treated as nationals of that state.50

Tribunals have noted that the ICSID Article 25(2)(b) ‘separately establishes a subjective test and an objective test’. Even where the parties agree ‘to treat the company as a national of another Contracting State for the purposes of this Convention’, ICSID jurisdiction is not satisfied unless the company is actually subject to foreign control – the ‘objective test is not satisfied by mere agreement by the Parties’.51

The CPTPP too provides a path to arbitration for local companies controlled by a foreign investor, albeit via a different mechanism. Article 9.19(1)(b) permits claimants to bring a claim ‘on behalf of an enterprise of the respondent that is a juridical person that the claimant owns or controls directly or indirectly’.

Notably, both the ICSID Convention and the CPTPP may require control, and thus the status of minority remains an open question that needs careful review under the specific facts.52 One tribunal confronted whether, through a shareholders’ agreement, a foreign investor might aggregate its ownership share of a local company with other investors to achieve the requisite degree of ‘foreign control’ under Article 25(2)(b) of the ICSID Convention. It found such aggregation permissible in some circumstances but not in others.53

48 Compare Ulysseas, Inc. v. The Republic of Ecuador, Interim Award, 28 September 2010, para. 166 (finding the burden with the state), with Guaracachi America, Inc., note 47, at para. 370 (finding the burden with the investor).
49 Dolzer & Schreuer, note 3, at 50.
50 id., at 51.
51 Natural Gas S.A.E. v. Arab Republic of Egypt, ICSID Case No. ARB/11/17, 3 April 2014, para. 133. See also Vacuum Salt Products Ltd. v. Republic of Ghana, ICSID Case No. ARB/92/1, 16 February 1994, para. 36 (finding that ‘the parties’ agreement to treat Claimant as a foreign national “because of foreign control” does not ipso facto confer jurisdiction’).
52 See Dolzer & Schreuer, note 3, at 57 (noting that neither the ICSID Convention nor the NAFTA, which has similar language to the CPTPP, offer comfort to minority shareholders’).
53 See Camuzzi International S.A. v. The Argentine Republic, ICSID Case No. ARB/03/2, Decision on Objection to Jurisdiction, 11 May 2005, paras. 38–41. For a critique of this tribunal’s reasoning, see
IIAs may also offer independent standing to shareholders – the shareholding itself becomes the investment. ‘Put differently, even if the local company is not endowed with investor status, the investor’s participation therein is seen as the investment.’\(^{54}\) Under this approach, the shareholder, as investor, bring claims in its own name ‘for adverse action by the host state against the company that affects its value and profitability’.\(^{55}\)

### iv State-owned enterprises

Some IIAs explicitly protect entities owned or controlled by a state.\(^{56}\) Even where IIAs do not, however, state-owned enterprises may in certain circumstances receive investor protection. In ICSID arbitrations, tribunals must decide whether a state enterprise is ‘a national of another Contracting State’ under Article 25. Several tribunals have applied the ‘Broches test’, named after the first ICSID Secretary-General Aron Broches, under which ‘a mixed economy company or government-owned corporation should not be disqualified . . . unless it is acting as an agent for the government or is discharging an essentially governmental function.’\(^{57}\)

### V CONCLUSION

It is axiomatic that if an investor is not covered by an IIA, that IIA generally does not provide the investor with substantive protections. An investor’s status, therefore, is often central to the resolution of the dispute itself. Determining this status requires careful analysis – it will turn both on the particular language of the applicable IIA and on the facts at hand, which can often involve complex corporate structures or searching inquiries into how a person has lived. Should a dispute arise between an investor and a state, both parties should develop a view on the issues early in the proceedings.

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\(^{54}\) Dolzer & Schreuer, note 3, at 57.

\(^{55}\) id.

\(^{56}\) See, e.g., Article 9.1 of the 2015 Australia–China free trade agreement, which expressly defines the term ‘enterprise’ to include ‘governmentally owned or controlled’ entities.

\(^{57}\) Beijing Urban Construction Group Co. Ltd. v. Republic of Yemen, ICSID Case No. ARB/14/30, Decision on Jurisdiction, 31 May 2017, para. 33. See also Ceskoslovenska Obchodni Banka A.S. v. The Slovak Republic, ICSID Case No. ARB/97/4, Decision on Objections to Jurisdiction, 24 May 1999; Emilio Agustín Maffezini v. Kingdom of Spain, ICSID Case No. ARB/97/7, Decision on Objections to Jurisdiction, 25 January 2000; Rumeli Telekom A.S. v. Republic of Kazakhstan, ICSID Case No. ARB/05/16, Award, 29 July 2008 (invoking and applying the Broches test).
Chapter 3

RATIONE TEMPORIS OR TEMPORAL SCOPE

Barton Legum, Obioma Ofoego and Catherine Gilfedder

I INTRODUCTION

The expression ratiōnem temporis denotes the effect of the passage of time on obligations or a tribunal’s power to decide a dispute. Numerous tribunals have dismissed claims on this basis. However, despite its potentially critical impact, this area has received relatively little attention in decisions or commentary. Tribunals frequently disagree on the basic principles or inconsistently apply the same principle.

The starting point in a specific case is the express wording of the treaty, which may determine its temporal scope. In the absence of express provisions, temporal issues are decided by reference to principles contained in the Vienna Convention on the Law of Treaties (VCLT), the International Law Commission’s Draft Articles on State Responsibility (the ILC Articles), and decisions of international courts and investment treaty tribunals.

This chapter deals with common issues regarding temporal jurisdiction. Section II addresses issues relating to the timing of an ‘investment’. Section III outlines the principle of non-retroactivity, and exceptions to the principle. Section IV examines issues relating to the timing of a ‘dispute’. Section V outlines temporal issues relating to termination of treaties, and Section VI addresses extinctive prescription.

II TIMING OF AN ‘INVESTMENT’

i What happens when the investment was made prior to the treaty coming into force?

This question does not feature significantly in cases. This is likely due in large part to the fact that an investment treaty will commonly state that it covers investments made prior to its entry into force.

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2 This chapter only examines investment treaties, although temporal issues may arise in relation to any consent document.


5 See, for example, the Canadian, Chinese, German, Malaysian and Turkish model bilateral investment treaties (BITs). For further examples, see Zachary Douglas, The International Law of Investment Claims (Cambridge University Press 2009) page 340; or, more recently, Cortec Mining v. Republic of Kenya, ICSID Case No. ARB/15/29, Award (22 October 2018) [284, 286].
If a treaty is silent on the matter, it has been suggested that investments made before the treaty’s entry into force are included within its scope.6

ii What happens if the investment occurred after the breach?

It is well-settled that a tribunal has no jurisdiction *ratione temporis* to consider allegations of a breach of a treaty in relation to acts that occur prior to the making of an investment. In *Mesa Power Group LLC v. Canada*, the tribunal affirmed that jurisdiction extends only to an investment that existed ‘at the time the challenged measure was adopted’.7 The same point was made in *Philip Morris v. Australia*.8 The tribunal found that the claimant had made its investment before the contested measure, albeit it ultimately held that the initiation of the arbitration constituted an abuse of rights, a different principle from *ratione temporis*.9

III NON-RETROACTIVITY OF TREATIES

Tribunals have repeatedly found that treaties, in the absence of clear language to the contrary, will not apply retroactively to acts or facts that occur before they enter into force.10 They have relied on Article 28 of the VCLT and Article 13 of the ILC Articles11 in doing so. However, facts occurring before the entry into force of a treaty can be taken into consideration in determining whether the treaty was subsequently breached.12

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6 Douglas (n 4) pages 340–341.
8 *Philip Morris Asia Limited v. The Commonwealth of Australia*, UNCITRAL, PCA Case No. 2012-12, Award on Jurisdiction and Admissibility (17 December 2015) (*Philip Morris v. Australia*).
9 ibid., [527].
11 Crawford (n 3) page 131.
12 Aaron C. Berkowitz et al (formerly Spence International Investments et al v. Republic of Costa Rica, ICSID Case No. UNCT/13/2, Interim Award (Corrected) (30 May 2017) [217–218] (*Spence v. Costa Rica*); holding that pre-entry into force facts cannot constitute a cause of action, but ‘may’ constitute circumstantial evidence that confirms or vitiates an apparent post-entry into force ‘breach’, and that pre-entry into force facts can be taken into account in assessing the damages. See also *Técnicas Medioambientales Tecmed SA v. United Mexican States*, ICSID Case No. ARB (AF)/00/2, Award (29 May 2003) [68] (*Tecmed v. Mexico*).
Some tribunals have found that it is necessary to ‘distinguish between (1) jurisdiction ratione temporis and (2) the applicability ratione temporis of the substantive obligations contained in a BIT’.13 The *Philip Morris* tribunal stated this distinction was ‘correct in theory’, but was unnecessary when the cause of action was founded upon a treaty breach.14

The principle of non-retroactivity is subject to qualifications where there are continuous and composite acts, and where a treaty is not yet in force, but a state has signed it.

### i Can continuous or composite acts occurring before the treaty enters into force be considered in assessing an alleged breach?

The principle of non-retroactivity may not apply to state action that is deemed to be a continuous or composite act. In such cases, a tribunal assessing an alleged breach may consider conduct that occurred before the treaty's entry into force.15 However, a number of tribunals have been cautious in attributing significant weight to such acts, so as to avoid an overreaching retroactive application of the substantive provisions of a treaty. Some tribunals have stated that continuous or composite acts prior to the treaty's entry into force are relevant only as factual background.16 Others have appeared to give them more weight.17 Acts constituting a breach, along with damages, may be limited to those that post-date the treaty’s entry into force.18

A continuous act is defined as a single act that extends over time and breaches an international obligation throughout.19 Article 28 of the VCLT supports the relevance of continuous acts despite the principle of non-retroactivity.20 The same is true of Article 14(2)

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14 Philip Morris v. Australia (n 7) [528].

15 Douglas (n 4) pages 341–342; Société Générale (n 9) [94]; Walter Bau v. Thailand (n 9) [9.84]; *ABCI Investments NV v. Republic of Tunisia*, ICSID Case No. ARB/04/12, Decision on Jurisdiction (18 February 2011) [178]; Paushok v. Mongolia (n 13) [491].


17 Chevron Corporation (USA) and Texaco Petroleum Corporation (USA) v. The Republic of Ecuador [I], PCA Case No. 34877, Interim Award (1 December 2008) [282–284] (Chevron v. Ecuador); Walter Bau v. Thailand (n 9) [12.26, 12.36–12.37, 13.1(f)].


of the ILC Articles. A number of tribunals have taken a similar approach. Acts found to be continuous include the non-payment of a contractually specified amount, the continued withholding of permits and concessions, and a continuing delay by national courts. A composite act is an act composed of a ‘series of actions or omissions defined in aggregate as wrongful’. A composite act does not ‘occur’ until the completion of the series. Tribunals have found it sufficient that the point of completion takes place after the effective date of the treaty. Tribunals have, however, been reluctant to accept claims of a composite breach whose purpose is to circumvent a limitation period stated to run from the investor’s first knowledge of breach or loss.

ii What happens if a treaty has not come into force, but a state has signed it?

Arguments that a state is bound by a treaty before it enters into force have been made in two contexts. First, where the treaty is provisionally applicable; and second, on the basis that states should refrain from committing acts that defeat the object and purpose of the signed treaty.

First, as specified in the VCLT, the contracting parties may agree to provisionally apply a treaty, or part of a treaty, before it enters into force. In those cases, the treaty will be binding, unless the treaty provides otherwise or it is otherwise agreed.

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21 Crawford (n 19) page 259; see also ILC Article 14(2) in Crawford (n 3) page 135.
23 SGS v. Philippines (n 22) [43, 167].
24 Pacific Rim v. El Salvador (n 16) [3.43].
25 Chevron v. Ecuador (n 17) [298]; see also Rubins and Love (n 13) page 484.
26 ILC Article 15, in Crawford (n 3) page 141. See also El Paso Energy International Company v. The Argentine Republic, ICSID Case No. ARB/03/15, Award (31 October 2011) [518].
28 Spence v. Costa Rica (n 12) [208], holding that composite acts ‘cannot without more renew the limitation period as this would effectively denude the limitation clause of its essential purpose, namely, to draw a line under the prosecution of historic claims’. See also Ansun Housing Co., Ltd v. People’s Republic of China, ICSID Case No. ARB/14/25, Award (9 March 2017) [113]; Rusoro Mining Ltd v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/12/5, Award (22 August 2016) [207-208], See contra United Parcel Service of America Inc v. Government of Canada, UNCITRAL, Award on the Merits (24 May 2007) [28].
Ratione Temporis or Temporal Scope

Provisional application has been addressed in cases concerning Article 45 of the Energy Charter Treaty (ECT). Tribunals have repeatedly retained jurisdiction on the basis of Article 45, including in the Yukos cases, where the tribunal found the ECT was provisionally applicable to Russia even though Russia had not ratified the treaty. Ultimately, Russia was held to be liable for breach of the expropriation provision. The tribunals in Petrobart v. Kyrgyzstan and Kardassopoulos v. Georgia took a similar approach.

Second, Article 18 of the VCLT requires a state to refrain from acts that would defeat the object and purpose of a treaty. Legal security and transparency are the aims behind this principle. The tribunal in Tecmed v. Mexico made explicit reference to Article 18, and stated that it would take the principle into consideration in assessing acts enacted by Mexico between the signature and the entry into force of the relevant treaty. However, a more restrictive


32 Hulley Enterprises Limited (Cyprus) v. The Russian Federation, PCA Case No. AA 226, Interim Award on Jurisdiction and Admissibility (30 November 2009) [338, 395]; Yukos Universal Limited (Isle of Man) v. The Russian Federation, PCA Case No. AA 226, Interim Award on Jurisdiction and Admissibility (30 November 2009) [338, 395]; Veteran Petroleum Limited (Cyprus) v. The Russian Federation, PCA Case No. AA 226, Award (18 July 2014) [1585]; Yukos Universal Limited (Isle of Man) v. The Russian Federation, PCA Case No. AA 226, Award (18 July 2014) [1585]; Veteran Petroleum Limited (Cyprus) v. The Russian Federation, PCA Case No. AA 226, Award (18 July 2014) [1585]. The awards referred to in this and in the previous footnote were set aside by The Hague District Court, in its judgment of 20 April 2016 (The Russian Federation v. Yukos Universal Limited et al, joined cases, Case No. C/09/477160 / HA ZA 15-1, available at http://deeplink.rechtspraak.nl/uitspraak?id=ECLI:NL:RBDHA:2016:4230). The Court held that the tribunal of the Yukos cases lacked jurisdiction because the Russian Federation had only signed, but never ratified, the ECT. In particular, the Court maintained that Article 45 ECT limits provisional application to only those ECT provisions that are compatible with Russian law. The Court held that this was a public law dispute, which Russian law did not allow to be resolved by arbitration, so Article 26 ECT was not compatible with Russian law. Because, under Russian law, treaties modifying domestic laws can bind the Russian Federation only if ratified (not just signed), the Court concluded that the Russian Federation was not bound by the ECT jurisdictional provisions, thereby depriving the tribunal of its jurisdiction to hear the cases.

33 Petrobart Limited v. The Kyrgyz Republic, SCC Arbitration No. 126/2003, Award (29 March 2005) [Section VIII.2]. The United Kingdom’s signature of the ECT bound Gibraltar, as a British overseas territory, and the provisional application of the treaty was engaged, despite the fact that the United Kingdom’s later ratification of the ECT excluded Gibraltar.

34 Ioannis Kardassopoulos v. Republic of Georgia, ICSID Case No. ARB/05/18, Decision on Jurisdiction (6 July 2007) [198–204, 247–248]. The ECT’s provisional application applied to both Georgia and Greece, even though the dispute concerned measures before the entry into force of the ECT. The tribunal found that Georgia directly expropriated the claimant’s investment by means of a decree that was dated more than two years before the ECT entered into force.


36 Tecmed v. Mexico (n 12) [70–71].
approach was adopted in *MCI v. Ecuador*, where the tribunal pointed out that Article 18 is an application of the principle of good faith and does not amount to the retroactive application of a treaty’s clauses.38

**IV ‘DISPUTES’ ARISING BEFORE THE ENTRY INTO FORCE OF THE TREATY**

Numerous decisions address the meaning of a ‘dispute’ in treaties’ arbitration provisions. Cases in this area have broadly fallen into two categories.

The first category concerns cases where the treaty makes provision, explicitly39 or implicitly,40 for the exclusion of disputes that arose prior to the treaty coming into force.

The second comprises cases where the treaty provides no guidance and tribunals have applied general international law principles to determine whether the treaty covers disputes arising before its entry into force. *Ping An v. Belgium* highlighted the divergent views in such cases, noting that some tribunals have applied a presumption of non-retroactivity (with or without reference to VCLT Article 28) to deny jurisdiction,41 while others have rejected the existence of any such presumption.42 The *Ping An* tribunal expressed doubt as to whether *Mavrommatis Palestine Concessions*43 stood for ‘a principle that there is a presumption that the jurisdiction of a tribunal extends to disputes which arose prior to its establishment’.44

Common to both categories is the importance of determining when the dispute ‘arises’. Some tribunals have asserted that the key factor in determining the existence of a dispute is the expression of a disagreement, which in time acquires a precise legal meaning, or the establishment of a ‘conflict of legal views and interests’.45 The identification of when this

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39 See the Agreement between the Government of the Republic of Chile and the Government of the Republic of Peru for the Promotion and Reciprocal Protection of Investments (entered into force 11 August 2001) Article 2, which provides that the treaty ‘shall not, however, apply to differences or disputes that arose prior to its entry into force’.

40 In *Salini v. Jordan* (n 9), the tribunal interpreted the phrase ‘any dispute which may arise between one of the contracting parties and the investor of the other contracting Party on investments’, holding (at [170]) that ‘[s]uch language does not cover disputes which may have arisen before the entry into force of the BIT’.

41 *Ping An v. Belgium* (n 9) [189–191].

42 *Ping An v. Belgium* (n 9) [191], considering *Tradex Hellas SA v. Republic of Albania*, ICSID Case No. ARB/94/2, Decision on Jurisdiction (24 December 1996), page 194, where the tribunal was ‘not convinced’ that there was such a presumption. For further discussion, see Nick Gallus, *The Temporal Scope of Investment Protection Treaties* (BIICL 2009) pages 132–137.

43 *Mavrommatis Palestine Concessions*, (30 August 1924) [90], PCIJ Series A, No. 2, 35 (*Mavrommatis Palestine Concessions*). Commentators have interpreted this case as supporting the view that unless a treaty specifically prevents it, an international tribunal can take jurisdiction over a dispute arising before its entry into force. See Gallus (n 42) page 139; Rubins and Love (n 13) page 490.

44 *Ping An v. Belgium* (n 9) [174 et seq.].

45 *Mavrommatis Palestine Concessions* (n 43) [19]. This formulation has been adopted by investment treaty tribunals; see, for example, *Emilio Agustín Maffezini v. The Kingdom of Spain*, ICSID Case No. ARB/97/7, Decision of the Tribunal on Objections to Jurisdiction (25 January 2000) [96].
occurs can give rise to opposing results in apparently similar circumstances. In *Lucchetti v. Peru*, the tribunal outlined what has been coined the ‘subject matter’ test, asking if ‘the facts or considerations that gave rise to the earlier dispute continued to be central to the later dispute’\(^{46}\) or if the disputes had the same ‘origin or source’.\(^{47}\) It considered the subject matter, origin and source of both disputes to be insufficiently different for it to accept jurisdiction.\(^{48}\)

By contrast, in *Jan de Nul v. Egypt*,\(^{49}\) the tribunal held that the dispute before it, which dealt with treaty violations, was a ‘new dispute’, which crystallised after the treaty came into force.\(^{50}\)

This question sharply divided the tribunal regarding the second claimant in *Eurogas*, where the BIT at issue applied only to disputes ‘which [have] arisen not more than three years prior to its entry into force’.\(^{51}\)

The majority considered what mattered were ‘the real causes of the dispute’,\(^{52}\) holding that the transgression complained of was the original reassignment of the claimant’s mining rights four years before the BIT took effect, and subsequent actions of the Slovak authorities merely maintained the effects of this. Professor Gaillard’s dissent advocated a broader view, concluding that an analysis of ‘all the factual and legal circumstances leading to the disagreement brought before the tribunal’ revealed that later conduct of the authorities (which included ignoring court decisions quashing the reassignment) in fact constituted the ‘definitive reassignment’ and thus formed part of the dispute between the parties, meaning the tribunal should accept jurisdiction.\(^{53}\)

**V IMPACT OF THE TERMINATION OF TREATIES**

i  **Can a claim be initiated after the treaty has been terminated?**

Of increasing prominence are temporal issues surrounding termination of BITs. Such terminations have historically been rare,\(^{54}\) but a growing number of states have served notices to terminate or threatened to do so, often due to the existence of or preference for multilateral investment protection arrangements.\(^{55}\) EU Member States have moved or undertaken to terminate their intra-EU BITs in line with the European Commission’s position, and

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\(^{46}\) Empresas Lucchetti SA and Lucchetti Peru SA v. The Republic of Peru, ICSID Case No. ARB/03/4, Award (7 February 2005) [50].

\(^{47}\) ibid., [53].

\(^{48}\) ibid.


\(^{50}\) Jan de Nul v. Egypt (n 47) [59, 128]. See also, for example, Renée Rose Levy and Gremcitel SA v. Republic of Peru, ICSID Case No. ARB/11/17, Award (9 January 2015) [167], *Philip Morris v. Australia* (n 6) [532] and *Lao Holdings NV v. The Lao People’s Democratic Republic*, ICSID Case No. ARB(AF)/12/6, Decision on Jurisdiction (21 February 2014) [124].

\(^{51}\) *EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic* (ICSID Case No ARB/14/14), Award (18 August 2017) (EuroGas v. Slovakia).

\(^{52}\) ibid., [453].

\(^{53}\) *EuroGas v. Slovakia* (n 51) Dissenting Opinion of Professor Emmanuel Gaillard.

\(^{54}\) As at September 2014, only 19 treaties had reportedly been terminated unilaterally, and two consensually (all but three since 2012); see Kathryn Gordon and Joachim Pohl, ‘Investment Treaties over Time – Treaty Practice and Interpretation in a Changing World’, *OECD Working Papers on International Investment*, 2015/02, OECD Publishing, pages 18–19.

\(^{55}\) For instance, reports suggest that in the past five years states, including Ecuador, India, Indonesia and South Africa, have served notices to terminate large proportions of their BITs.
consequent upon the CJEU’s decision in the Achmea case, which held that the Treaty on the Functioning of the European Union precluded the investor–state arbitration provision of the Netherlands–Slovakia BIT.

BITs tend to contain provisions regulating how they are terminated. Many specify an initial period during which they cannot be terminated except in exceptional circumstances, following which termination is permissible upon a period of written notice. In most BITs, a specific clause (a survival clause) provides for treaty protections to continue after termination for existing investments, usually for between 10 and 15 years. There are examples of states purporting to disapply survival clauses in cases of termination by mutual consent, albeit the effectiveness of this appears not to have been tested before any tribunal.

**ii What is the impact of a state’s denunciation of the ICSID Convention?**

The withdrawals from the ICSID Convention of Bolivia, Ecuador and Venezuela in 2007, 2009 and 2012, respectively, spurred debate around the effects of withdrawal on consent to jurisdiction given while the treaty was in force. Commentators and tribunals disagree on the effect of Articles 71 and 72, and more specifically, the meaning of ‘consent’ in Article 72, which provides that denunciation does not affect ‘rights or obligations under this Convention . . . arising out of consent to the jurisdiction of the Centre given by [a State or investor] before such notice was received by the depositary’. In Venoklim v. Venezuela, the tribunal found that during the six-month period after denunciation the state was still a contracting state, whose consent to arbitration subsisted, and that consent could still be accepted and ‘perfected’ by

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56 Case C-284/16 Slowakische Republik v. Achmea BV, Judgment, 6 March 2018.
57 See Declaration of the Representatives of the Governments of the Member States of 15 January 2019 on the Legal Consequences of the Judgment of the Court of Justice in Achmea and on Investment Protection in the European Union (signed by 22 Member States); separate declarations were signed by the remaining Member States who disagreed as to the effect of Achmea on the ECT (the January 2019 Declarations).
58 Rudolf Dolzer and Margrete Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff 1995) page 47. Of the sample of 2,061 treaties reviewed by Gordon and Pohl (n 54), 97 per cent contain provisions extending some or all effects of the treaty beyond termination for a fixed ‘survival’ period, with the average period being 12.5 years. Under the United States–Mexico–Canada Agreement (USMCA), investors will remain able to bring claims relating to investments made under NAFTA for three years following NAFTA’s termination: see USMCA, Annex 14-C, paragraph 3.
59 The Czech Republic, Indonesia and Peru have purported to terminate treaties in this way, sometimes first amending the BIT to remove the survival clause before terminating.
60 In one of a number of ICSID awards that have held that Achmea does not affect jurisdiction under the ICSID Convention, a tribunal has recently observed that even if Hungary as the respondent state could be said to have implicitly terminated the underlying BIT by acceding to the European Union, the tribunal would still have jurisdiction owing to the survival clause, which neither of the parties had attempted to modify or renegotiate; see UP (formerly Le Chèque Déjeuner) and C.D Holding Internationale v. Hungary, ICSID Case No. ARB/13/35, Award (9 October 2018) [265]. EU Member States have, in the January 2019 Declarations, adopted the position that agreements to arbitrate in intra-EU BITs are inapplicable *ab initio* and thus sunset provisions do not operate to extend them. For further discussion, see Chrispas Nyombi and Tom Mortimer, ‘The turf war between the European Commission and intra-EU BITs: is an end in sight?’, *Int. A.L.R.* 2018, 21(3), 66–79.
an investor. The Blue Bank v. Venezuela tribunal had no hesitation in agreeing. By contrast, the tribunal in Fábrica de Vidrios Los Andes CA and Owens-Illinois de Venezuela CA v. Venezuela (Favianca) considered ‘consent’ in Article 72 to mean consent already perfected – Venezuela’s offer to arbitrate in the treaty could not therefore be ‘accepted’ after its denunciation. The tribunal remarked that the ordinary meaning of ‘consent to the jurisdiction’ could encompass either interpretation, but in the context of the Article and Convention as a whole (including the travaux) it was ‘quite obvious’ that perfected consent was required. It therefore declined jurisdiction over the dispute.

The Favianca tribunal’s reasoning would logically imply that consent could not be perfected after the six-month period in Article 71. While the Venoklim or Blue Bank tribunals did not address this broader issue, in his separate opinion in Blue Bank, Christer Söderlund opined that consent in a treaty remained effective even beyond the six months following denunciation, so ICSID arbitration was in principle available at any time until the treaty’s termination. Some commentators have concurred with Söderlund’s view on this question.

VI EXTINCTIVE PRESCRIPTION

The principle of extinctive prescription is that a right can be lost, or a claim barred, when not exercised within a certain amount of time. For extinctive prescription to operate, the delay must be unreasonable and attributable to the claimant. Prejudice to the respondent

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62 Venoklim Holding BV v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/12/22, Award (3 April 2015), [63]. The majority of the tribunal declined jurisdiction on the grounds that the Venezuelan Investment Law (VIL), under which Venoklim’s claims were originally brought, could not alone constitute Venezuela’s consent to arbitration and Venoklim was not an international investor under the VIL. Venoklim has since filed a separate claim against Venezuela relating to the same expropriation, this time under the Netherlands–Venezuela BIT (ICSID Case No. ARB(AF)/17/4), in which the tribunal was constituted in March 2018.


65 ibid., [273].

66 The Favianca claimants have applied for annulment of the award, ICSID Case No. ARB/12/21, Application for Annulment, 9 March 2018.

67 Blue Bank v. Venezuela (n 64) Separate Opinion of Christer Söderlund [45].


may also be a relevant consideration. Although this principle is recognised in customary international law, cases applying it are rare and claims are typically time-barred via a specific provision in a treaty.

Some treaties provide express time limitations on claims. For example, the NAFTA provides a three-year limitation from 'the date on which the investor first acquired, or should have first acquired, knowledge of the alleged breach and knowledge that the investor has incurred loss or damage'. In *Ansung Housing v. China*, the tribunal summarily dismissed a claim under a similar provision in a China–Korea BIT as the claim was manifestly time-barred given the facts stated in the Request for Arbitration. Tribunals can, however, refer to facts occurring outside the limitation period, where relevant.

Where a treaty does not provide specific time bars, tribunals have generally allowed claims, without rejecting the possibility of time-barring them. In *Wena Hotels v. Egypt*, a lapse of seven years after the expropriation was insufficient to bar the claim because the claimant had diligently pursued its claim and provided sufficient notice. Similarly, in *Kardassopoulos v. Georgia*, a delay of 10 years did not prevent the claim from being brought as the claimant had reasonably believed an amicable settlement was possible and Georgia had been given timely notice of the dispute.
Part II

ADMISSIBILITY AND PROCEDURAL ISSUES
Chapter 4

ADMISSIBILITY

Michael D Nolan

I

INTRODUCTION

Tribunals seized to resolve disputes pursuant to bilateral investment treaties (BITs) under either the ICSID Convention or the UNCITRAL Arbitration Rules draw distinctions between the concepts of ‘jurisdiction’ and ‘admissibility’. The term ‘admissibility’ is not addressed in the ICSID Convention, the UNCITRAL Arbitration Rules or BITs. It has been observed that the concept of admissibility ‘partakes of its generic meaning in the general theory of law’.2 This chapter explores the genesis of the concept of admissibility and the various contexts in which the concept has been applied by ICSID tribunals.

Even though the concept of admissibility is discussed and has served as a basis for dismissal of BIT claims, at least one tribunal has questioned its power to dismiss the claim based on admissibility. In Methanex v. United States, the tribunal found that it had no power to dismiss a claim based on admissibility, noting the following:

There is here no express power to dismiss a claim on the grounds of “inadmissibility”, as invoked by the USA; and where the UNCITRAL Arbitration Rules are silent, it would be still more inappropriate to imply any such power from Chapter 11 . . . It is unnecessary to develop these materials further.3

The Methanex tribunal specifically referred to Article 79(1) of the Rules of Court of the International Court of Justice (ICJ) concerning preliminary objections and referring to ‘admissibility of the application’ before the court,4 and concluded that it had ‘no express or implied power to reject claims based on inadmissibility’.5 In Methanex, the respondent argued that the claims were inadmissible on two grounds. First, because under customary international law creditors’ claims are inadmissible if they stem solely from a measure’s effect on the debtor, there must be an action that directly affects the creditor’s right.6 Second, the

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1 Michael D Nolan is a partner at Milbank LLP. The original edition of this chapter was co-authored by Elitza Popova-Talty, a former associate at the firm.
2 Abaclat v. Argentine Rep, ICSID Case No. ARB/07/5, Dissenting Opinion to Decision on Jurisdiction and Admissibility, paragraph 17 (4 August 2011) (‘As with jurisdiction, the concept of admissibility in international law partakes of its generic meaning in the general theory of law, but is further particularized in function of the specificities of international adjudication, including its consensual basis’).
3 Methanex Corp v. US, First Partial Award, paragraphs 124 and 126 (7 August 2002).
4 id. at paragraph 125.
5 id. at paragraph 126.
6 Methanex Corp v. US, Respondent’s Memorial on Jurisdiction and Admissibility, page 26 (13 November 2000). The respondent relied on international customary law authorities for the proposition
respondent argued that the claimants failed to identify an international legal obligation owed to it that was violated. In this regard, the respondent relied on *Barcelona Traction, Light and Power (Belgium v. Spain)* holding that:

> [i]n order to bring a claim in respect of the breach of such an obligation, a State must first establish its right to do so, for the rules on the subject rest on two suppositions: The first is that the defendant State has broken an obligation towards the national State in respect of its nationals. The second is that only the party to whom an international obligation is due can bring a claim in respect of its breach.7

Nonetheless, the concept of admissibility has been applied by a number of tribunals in the context of procedural irregularities, which have been held to prevent the hearing of the case or to be a basis for dismissing claims because of conduct on the part of the claimant. Indeed, it has been observed that the concept of admissibility has become so important that many awards focus more on admissibility than on jurisdiction.8

II THE TERM ‘ADMISSIBILITY’ IN THE PRACTICE OF NON-INVESTMENT TRIBUNALS

The term ‘admissibility’ appears in the rules or procedures of several courts of international law. For example, the Rules of Court of the ICJ9 Article 79 defines admissibility as follows:

*Any objection by the respondent to the jurisdiction of the Court or to the admissibility of the application, or other objection the decision upon which is requested before any further proceedings on the merits, shall be made in writing as soon as possible, and not later than three months after the delivery of the Memorial. Any such objection made by a party other than the respondent shall be filed within the time limit fixed for the delivery of that party’s first pleading.*

Before deciding the case, the court must determine as a preliminary matter both the issue of jurisdiction and admissibility. Jurisdictional issues in the ICJ practice ‘are those which ultimately derive from whether the Court has the right and power to consider the case brought by a state’, while issues of admissibility determine whether the case itself is one proper for determination when brought before the court.10 In ICJ practice, the respondent’s
objections to admissibility may be grounded in one or more of the following: (1) lack of *locus standi* by the applicant, (2) the necessity to join a third party, (3) the mootness of the dispute or (4) the existence of local remedies that have not been exhausted.¹¹

The Articles on Responsibility of States for Internationally Wrongful Acts similarly provide that a claim is inadmissible if (1) the claim is not brought in accordance with any applicable rule relating to the nationality of claims; or (2) the claim is one to which the rule of exhaustion of local remedies applies and any available and effective local remedy has not been exhausted.¹² Another example of definition of the concept of admissibility is contained in Article 35 of the European Convention on Human Rights. Under that provision, the court can reject applications as inadmissible if (1) domestic remedies have not been exhausted; (2) application is anonymous or substantially the same as a matter already examined by the court; (3) the application is incompatible with the provisions of the Convention, manifestly ill-founded or constitutes an abuse of right; or (4) the applicant has not suffered significant disadvantage.¹³ The obligation to exhaust domestic remedies is based on customary international law and is intended to allow national courts to remedy the violation. The concept of ‘abuse of right’ is understood according to general legal theory, namely the harmful exercise of a right for purposes other than those for which it is designed.¹⁴ The European Court of Human Rights has issued a detailed *Practical Guide on Admissibility Criteria* with explanations and examples of each ground for rejection of an application based on admissibility.¹⁵

### III ADMISSIBILITY AND JURISDICTION IN THE PRACTICE OF ICSID TRIBUNALS

Admissibility has been distinguished from jurisdiction by investment tribunals. It has been accepted by a number of tribunals that, although jurisdictional objections are aimed at the tribunal authority to decide the case, challenges of admissibility are rooted in a defect of the claim.

In *Waste Management Inc v. United Mexican States*, the dissent summarised the practice as follows:

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¹⁴ Cases in which the Court has found an abuse of the right include: provision of misleading information; use of offensive language; violation of the obligation to keep friendly settlement proceedings confidential; application manifestly vexatious or devoid of any real purpose. European Court of Human Rights, *Practical Guide on Admissibility Criteria* 37–39 (2014), available at www.echr.coe.int/Documents/Admissibility_guide_ENG.pdf.

¹⁵ id.
International decisions are replete with fine distinctions between jurisdiction and admissibility. For the purpose of the present proceedings it will suffice to observe that lack of jurisdiction refers to the jurisdiction of the Tribunal and inadmissibility refers to the admissibility of the case. Jurisdiction is the power of the tribunal to hear the case; admissibility is whether the case itself is defective – whether it is appropriate for the tribunal to hear it. If there is no title of jurisdiction, then the tribunal cannot act.\footnote{ICSID Case No. ARB(AF)/98/2, Dissenting Opinion to Award, paragraphs 57–58 (8 May 2000), 15 ICSID Rev 241, 265 (2000). The distinction was emphasised by Professor Abi-Saab as follows: ‘Generically, the admissibility conditions relate to the claim, and whether it is ripe and capable of being examined judicially, as well as to the claimant, and whether he or she is legally empowered to bring the claim to court.’ \textit{Abachat v. Argentine Rep}, ICSID Case No. ARB/07/5, Dissenting Opinion to Decision on Jurisdiction and Admissibility, paragraph 18 (4 August 2011).}

This definition is reminiscent of Professor Brownlie’s distinction between the two concepts. Professor Brownlie observes that ‘[a]n objection to the admissibility of a claim invites the tribunal to dismiss (or perhaps postpone) the claim on ground which, while it does not exclude its authority in principle, affects the possibility or propriety of its deciding the particular case at the particular time.’\footnote{James Crawford, \textit{Brownlie’s Principles of Public International Law} 693 (8th edition 2012).} Under this approach, the tribunal should first determine whether it has jurisdiction over the dispute and, once that jurisdiction has been confirmed, address the admissibility of the claims. But some tribunals have been less willing to draw a clear distinction between jurisdiction and admissibility. In \textit{Consorzio Groupement LESI-DIPENTA v. Algeria}, the tribunal acknowledged at the outset that objections of jurisdiction and admissibility ‘must be dealt with separately and successively, because they deal with different questions’.\footnote{ICSID Case No. ARB/03/08, Award, paragraph 2 (10 January 2005).} Nonetheless, because the claimant was not the holder of the rights under the contract, the tribunal found both that its claims were inadmissible and that the tribunal did not have jurisdiction over the claims.\footnote{id. at paragraph 40 (‘In the end, because the Claimant was not the holder of the rights and obligations of the Contract under which the investment was made, it follows that its Request for Arbitration is inadmissible and that it cannot claim to be an investor within the meaning of Article 25(1) of the Convention. For this reason, not only is the Request for Arbitration inadmissible but, applying the provisions of the Convention, the Arbitral Tribunal has no jurisdiction, since it can consider the matter only at the request of an investor within the meaning of the Convention.’)} In \textit{Pan American Energy LLC and BP Argentina Exploration Company v. Argentine Republic} the tribunal held: ‘there is no need to go into the possible – and somewhat controversial – distinction between jurisdiction and admissibility. Whatever the labelling, the parties have presented their case on the basis of the six objections raised by the Respondent.’\footnote{ICSID Case No. ARB/03/13, Decision on Preliminary Objections, paragraph 54 (7 July 2006).}

The recent decision in \textit{Abaclat v. Argentina} demonstrates the challenges associated with determining the nature of the objection. In \textit{Abaclat v. Argentina}, the first investment dispute dealing with mass claims, the tribunal decided that it had jurisdiction to hear the claims of over 60,000 Italian investors against Argentina under the ICSID Convention and the Argentina–Italy BIT.

Noting that the differences between jurisdiction and admissibility are ‘not always clear’, the majority (Professor Tercier and Professor van den Berg) applied the following criteria in distinguishing the two kinds of objections:
If there was only one Claimant, what would be the requirements for ICSID’s jurisdiction over its claim? . . . If the issue raised relates to another aspect of the proceedings, which would not apply if there was just one Claimant, then it must be considered a matter of admissibility and not of jurisdiction.21

In a dissent, Professor Abi-Saab disagreed with the majority conclusion that the number of the claimants was an issue of admissibility and not of jurisdiction. Professor Abi-Saab criticised the majority for adopting an ‘extremely narrow, in fact partial, concept of jurisdiction’.22 Professor Abi-Saab viewed the number of claimants as bearing on the ‘consent to arbitrate’ thus being an issue of jurisdiction. The dissent quoted from the US Supreme Court decision in Stolt-Nielsen SA v. Animal Feeds International Corp holding that ‘class action arbitration changes the nature of arbitration to such degree that it cannot be presumed the parties consented to it by simply agreeing to submit their disputes to an arbitrator’ and that ‘changes brought about by the shift from bilateral arbitration to class action arbitration [are] fundamental’.23

Whether the objection is based on jurisdiction or admissibility has significant practical implications. In bifurcated cases where issues of jurisdiction are separate from issues of liability, tribunals will deal with admissibility issues in the merits rather than the jurisdictional phase. In some cases, issues of jurisdiction are decided at the same time as issues of admissibility as tribunals have broad discretion when to decide on admissibility.24

IV DISMISSAL ON THE BASIS THAT THE CLAIMS ARE ‘PREMATURE’

In SGS Société Générale de Surveillance SA v. Philippines the dispute arose out of a service contract stipulating that disputes should be referred for resolution to the courts of the Philippines. Nonetheless, when the investor sought protection under the BIT between Switzerland and the Philippines, the Philippines objected on the basis that the investor’s claim was for breach of contract and as such should be brought before a Philippines court. The tribunal determined that it had jurisdiction over the dispute because the treaty extended to contractual claims and the investor had expressly asserted breaches of the treaty. The tribunal, nevertheless, found that it was impeded from hearing the dispute, and the claims were inadmissible:

The question is whether a party should be allowed to rely on a contract as the basis of its claim when the contract itself refers that claim exclusively to another forum. In the Tribunal’s view the answer is that it should not be allowed to do so, unless there are good reasons, such as force majeure, preventing

21 Abaclat v. Argentine Rep, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility, paragraph 249 (4 August 2011). The tribunal found that the issue was one of admissibility: ‘Assuming the Tribunal has jurisdiction over claims of several individual claimants, it is difficult to conceive why and how the Tribunal could lose jurisdiction where the number of claimants outgrows a certain threshold . . . what is the relevant threshold? . . . and can the Tribunal really “lose” jurisdiction it has when looking at Claimants individually?’ id. at paragraphs 484–490.

22 Abaclat v. Argentine Rep, ICSID Case No. ARB/07/5, Dissenting Opinion to Decision on Jurisdiction and Admissibility, paragraph 126 (4 August 2011).

23 id. at paragraphs 150–51 (quoting 130 S Ct 1758, 1774 (2010)).

24 In Abaclat, the tribunal issued a decision on jurisdiction and admissibility. Abaclat v. Argentine Rep, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility (4 August 2011).
Admissibility

the claimant from complying with its contract. This impediment, based as it is on the principle that a party to a contract cannot claim on that contract without itself complying with it, is more naturally considered as a matter of admissibility than jurisdiction.  

The tribunal thus found that until the question of the scope of the respondent’s obligation was clarified by agreement between the parties or by Philippine courts, a decision by an ICSID tribunal would be ‘premature’. Citing to Brownlie, the tribunal also observed that ‘the analogous rule of exhaustion of local remedies is normally a matter concerning admissibility rather than jurisdiction in the strict sense.’

V DISMISSAL ON ADMISSIBILITY BASED ON ALLEGED WRONGDOING BY THE INVESTOR

Perhaps uniquely in the investment treaty context, tribunals have applied the concept of admissibility to dismiss claims on the basis of the alleged wrongdoing by the investor. For example, in Plama v. Bulgaria28 the tribunal found that the effect of the claimant’s fraud and illegal conduct was to ‘preclude the application of the protections of the ECT’. The respondent had argued that the claimant had obtained the investment through unlawful means rendering the claim inadmissible. The tribunal bifurcated the proceeding in jurisdiction and merits phase. In the decision on jurisdiction, the tribunal concluded that the respondent’s allegations on misrepresentation did not deprive it of jurisdiction in this case and decided to examine these allegations during the merits phase. The analysis section of the Plama award on the merits did not use the term ‘admissibility’. But in substance, the tribunal adopted the respondent’s arguments finding that ‘the substantive protections of the ECT cannot apply to investments that are made contrary to law’. In its reasons, the tribunal stated that granting the protection of the Energy Charter Treaty (ECT) would be contrary to the principle of nemo auditur propriam turpitudinem allegans – no one is heard when alleging one’s own wrong. The tribunal referred to the decisions in Inceysa v. El Salvador and World Duty Free v. Kenya invoking the principle of good faith, respect for the law and international public policy. The tribunal thus dismissed the claims because of the conduct on the part of the investor, not because of lack of jurisdiction.

Brownlie lists five grounds for inadmissibility of interstate claims: (1) the existence of legal interest on part of the claimant; (2) necessary third parties; (3) mootness of the dispute as a result of events arising after the complaint was filed; (4) extinctive prescription (i.e.,

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25 ICSID Case No. ARB/02/6, Decision of the Tribunal on Objections to Jurisdiction, paragraph 154 (29 January 2004).
26 id. at paragraph 155.
27 id. at paragraph 154 (citing Brownlie, Principles of Public International Law 681 (6th edition 2003)).
28 Plama Consortium Ltd v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Award (27 August 2008). The tribunal composed of Carl F Salans (president), Albert Jan van den Berg (appointed by claimant) and V V Veeder (appointed by Bulgaria).
29 id. at paragraph 135.
30 id. at paragraph 96.
31 id. at paragraph 97.
32 id. at paragraph 139.
33 id. at paragraph 141.
unreasonable lapse of time in presentation of international claim; and (5) waiver. Under separate ‘other grounds’, Brownlie observes that ‘[t]here may be a residue of instances in which questions of inadmissibility and “substantive” issues are difficult to distinguish. This is the case of the so-called “clean hands” doctrine, according to which a claimant’s involvement in activity unlawful either under municipal law or international law may bar the claim.’ Interestingly, Brownlie observed that the ICJ has never applied the doctrine even in cases where it could have done so. Crawford’s Second Report on State Responsibility includes chapter V, entitled ‘Circumstances precluding wrongfulness’. A section of chapter V entitled ‘Possible justifications or excuses not included in chapter V’ contains a subsection entitled ‘The so-called “clean hands” doctrine’. The report notes that the doctrine of unclean hands has hardly been referred to in the International Law Commission’s previous work on state responsibility. Citing Salmon, the report notes that the doctrine has been applied in a series of decisions of the United States–Great Britain Mixed Commission set up under a Convention of 8 February 1853 for the settlement of shipowners’ compensation claims. These cases were ‘all characterized by the fact that the breach of international law by the victim was the sole cause of the damage claimed, [and] that the cause-and-effect relationship between the damage and the victim’s conduct was pure, involving no wrongful act by the respondent State’. Considering that chapter V was not concerned with procedural issues or admissibility of claims, the report explained the Special Rapporteur’s view that there was thus no basis to include the clean hands doctrine as a ‘new circumstance precluding wrongfulness’. The Special Rapporteur concluded that ‘it is not possible to consider the “clean hands” theory as an institution of general customary law’.

The doctrine of nemo auditur propriam turpitudinem allegans has been discussed not only by investment tribunals, but also by national courts. By way of comparison, in French tort law, for example, illegality has for a long time played a major role in discarding the protection of interests held to be illegitimate. The discussion turned mainly around the admissibility of claims brought by concubines who suffered material and non-material damage as a result of their partner’s death in fatal accidents. The interest of such secondary victims was long regarded as being illegitimate. Since the 1970s, however, there has been strong support for the opinion that the maxim nemo auditur propriam turpitudinem allegans could not be invoked to dismiss an action in tort, and that the participation of the victim in the wrongful act was to be treated as an instance of contributory negligence that could lead...
to partial, or even total, exoneration of the defendant. Whether the doctrine of clean hands should be considered as a basis of erasing the wrongfulness of the state’s conduct, or to what extent the wrongfulness of the investor conduct has contributed to the injury suffered by it, are not issues that have so far received attention in the decisions of investment tribunals.

VI ADMISSION OF EVIDENCE

In the US federal legal system, the term ‘admissibility’ is used in the context of evidence. For evidence to be presented in legal proceedings, in addition to being relevant to factual proposition in the case, it also must be admissible. The concept of admissibility allows the court to exclude evidence that may otherwise be relevant or material. Two prominent examples of such rules of admissibility or rules of exclusion are the rule against hearsay evidence and the rule against character evidence. In the United States, Federal Rule of Evidence 404(a)(1) bars the use of evidence of a person’s character ‘to prove that on a particular occasion the person acted in accordance with the character’ and Federal Rule of Evidence 404(b)(1) provides that evidence of a crime or wrong is not admissible ‘to prove a person’s character in order to show that on a particular occasion the person acted in accordance with the character’.44

In the context of ICSID proceedings, parties also have objected to the use of documents in evidentiary hearings on the basis of their admissibility; although it is not always clear whether the parties refer to inadmissible documents as documents that are otherwise relevant or have used the term ‘admissibility’ as synonymous with ‘relevancy’. In Methanex Corporation v. United States, the tribunal held certain documents illegally obtained by Methanex to be inadmissible. The documents were found to be obtained by Methanex ‘by deliberately trespassing onto private property and rummaging through dumpsters inside the office-building for other persons’ documentation’.45

In Abaclat v. Argentina, the tribunal was seized to decide on the admissibility of documents for witness and expert examination at the hearing. The claimants had objected to the respondent’s proposed use of documents during the hearing, because the documents were not ‘within the scope of admissible examination, i.e. to documents relevant to the direct testimony by Claimants’ experts and witnesses’. The claimants had also objected on the asserted basis that the documents violated the tribunal’s confidentiality order and the respondent acted in bad faith in not disclosing those documents earlier.46 The tribunal issued a detailed procedural order addressing whether certain categories of documents were admissible or not, but the order did not set forth a standard or definition of admissible evidence. The tribunal ruled that ‘the use of these documents may not serve to unduly extend the scope of admissible examination for the jurisdictional hearing’.47 Claimants had also objected to the use of a DVD and its transcript of an Italian television show broadcast discussing Italian court decisions concerning proceedings initiated by the claimants, and intended to be used for

44 Fed R Evid 404(a)–(b).
45 Methanex Corporation v. United States of America, UNCITRAL, Final Award of the Tribunal on Jurisdiction and Merits (3 August 2005) Pt II, chapter I, paragraph 55.
47 id. at paragraph 50.
Admissibility

cross-examination by the respondent of the claimants’ expert because of (1) the fact that the statements made in this television show are not witness testimony, (2) the alleged unreliability of the source and (3) the late filing of this material. After expressing concern about the time the respondent intended to use with the particular witness, the tribunal allowed the use of the material requested by the respondent subject to ‘the Tribunal reserv[ing] the right to interrupt the examination of [the claimants’ expert] in case it deems that Respondent’s examination is beyond the scope of what is necessary and appropriate’. Thus, in this case, even though the claimants’ objections were on the basis of admissibility and what the claimant was alluding to were concerns about the quality of the evidence, the tribunal generally found the material to be admissible (even though it did not formulate what it viewed as admissible evidence) but reserved for itself the right to exclude it on the basis of judicial economy.

In the recent decision of the ad hoc committee in Ioan Micula, Viorel Micula, SC European Food SA, SC Starmill SRL and SC Multipack SRL v. Romania, the respondent sought to introduce into the record eight factual exhibits concerning various enforcement proceedings. Following the claimants’ objection on admissibility grounds, the committee denied the request on the basis that ‘the new evidence was not directly relevant to the grounds for annulment.’

VII CONCLUSION

The concept of admissibility has played and will continue to play an important role in investment treaty arbitration. With the increase in investment treaty disputes, it can be expected that respondent states will continue to rely on admissibility as a basis for dismissal of investor claims. Future investment tribunals will have the opportunity to develop the concept in a way that fits the unique nature of the claims they are called on to adjudicate.

48 Abacalt v. Argentine Rep, ICSID Case No. ARB/07/5, Procedural Order No. 5, paragraph 18 (2 April 2010).
49 id. at paragraph 20(ii).
50 ICSID Case No. ARB/05/20, Decision on Annulment (26 February 2016).
51 id. at paragraph 79.
Chapter 5

BIFURCATION IN INVESTMENT TREATY ARBITRATION

Marinn Carlson and Patrick Childress

I INTRODUCTION

Bifurcation refers to splitting an arbitration into two separate phases, and most often involves splitting jurisdictional issues from the merits. A tribunal’s decision on whether to bifurcate is one of the most critical procedural inflection points in an investment treaty arbitration. If a tribunal bifurcates and dismisses the claims on jurisdiction, the parties avoid briefing the merits, which can save many months (if not years) of time and millions of dollars in legal fees. But, if the tribunal bifurcates and finds jurisdiction, the parties must then embark on a new, separate merits procedure, extending the overall arbitral calendar and increasing costs substantially. It follows that a tribunal’s bifurcation decision is a pivotal moment in an investment treaty arbitration.

This chapter focuses on the legal framework that tribunals apply when considering whether to bifurcate jurisdictional objections from the merits (Section II), and the strategic issues parties consider when deciding to seek or to resist jurisdictional bifurcation (Section III). Lastly, we briefly explore the less common practice of bifurcating proceedings to separate the analysis of damages from the merits phase (Section IV).

II LEGAL FRAMEWORK FOR CONSIDERING APPLICATIONS TO BIFURCATE JURISDICTION

i The rules governing bifurcation

The two primary sets of procedural rules for investment treaty arbitration – the International Centre for Settlement of Investment Disputes (ICSID) Arbitration Rules and the United Nations Commission on International Trade Law (UNCITRAL) Rules – expressly provide for bifurcation of jurisdictional objections. Article 41(2) of the ICSID Convention states that:

Any objection by a party to the dispute that that dispute is not within the jurisdiction of the Centre, or for other reasons is not within the competence of the Tribunal, shall be considered by the Tribunal which shall determine whether to deal with it as a preliminary question or to join it to the merits of the dispute.

ICSID Arbitration Rule 41 uses similar language, stating in the pertinent part that:

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The Tribunal may on its own initiative consider, at any stage of the proceeding, whether the dispute or any ancillary claim before it is within the jurisdiction of the Centre and within its own competence.

The Tribunal . . . may deal with the objection [that a dispute or any ancillary claim is not within the jurisdiction of the Centre or, for other reasons, is not within the competence of the Tribunal] as a preliminary question or join it to the merits of the dispute.2

The UNCITRAL Rules also permit bifurcation; however, the approach to bifurcation shifted between the 1976 and 2010 versions of the UNCITRAL Rules. Article 24(4) of the 1976 UNCITRAL Rules states that:

In general, the arbitral tribunal should rule on a plea concerning its jurisdiction as a preliminary question. However, the arbitral tribunal may proceed with the arbitration and rule on such a plea in their final award.

Tribunals have held that this language – namely that a tribunal ‘should rule’ on its jurisdiction ‘as a preliminary question’ – suggests that the 1976 UNCITRAL Rules create a presumption in favour of bifurcation.3

The approach to bifurcation changed in the 2010 revision to the UNCITRAL Rules. Article 23(3)4 states that:

The arbitral tribunal may rule on a [jurisdictional objection] either as a preliminary question or in an award on the merits.

Tribunals have held that this new formulation – namely that a tribunal ‘may rule’ on its jurisdiction as a preliminary question – eliminated the presumption in favour of bifurcation that existed in the 1976 UNCITRAL Rules.5 This change brought the UNCITRAL Rules in line with ICSID Arbitration Rules, which likewise include no stated presumption in favour of jurisdictional bifurcation.

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2 The ICSID Arbitration Rules also provide that ‘[u]pon the formal raising of an objection relating to the dispute, the Tribunal may decide to suspend the proceeding on the merits.’ ICSID Arbitration Rules, Rule 41(3). However, the ICSID Secretariat recently proposed amendments to the ICSID Arbitration Rules that would remove tribunals’ power to suspend the proceedings during the pendency of a bifurcation application. See Proposals for Amendment of the ICSID Rules, Consolidated Draft Rules, Volume II, August 2, 2018, Rule 36.


4 This provision is unaffected by the 2013 revisions to the UNCITRAL Rules (incorporating rules on transparency in investment treaty arbitration).

The legal test for bifurcation

Neither the ICSID Arbitration Rules nor the UNCITRAL Rules provide guidance on the factors that a tribunal should consider when deciding whether to bifurcate proceedings.6 However, investment treaty tribunals have developed and followed a fairly consistent approach to the analysis. Procedural efficiency – whether bifurcation is more likely to increase or decrease the time and costs associated with the arbitration – is the overarching factor that tribunals consider when deciding bifurcation applications. In his seminal treatise on the ICSID Convention, Professor Schreuer explains that the question of whether to bifurcate proceedings is:

>a matter of procedural economy. It does not make sense to go through lengthy and costly proceedings dealing with the merits of the case unless the tribunal’s jurisdiction has been determined authoritatively. On the other hand, some jurisdictional questions are so intimately linked to the merits of the case that it is impossible to dispose of them in preliminary form.7

Tribunals generally agree with Professor Schreuer’s analysis.8 For instance, the Clayton v. Canada tribunal held that ‘its purpose in directing bifurcation . . . was to facilitate the efficient litigation of the claim within the arbitration process’.9 In the recent Eco Oro v. Colombia decision on bifurcation, the tribunal held similarly, noting that, in addressing a bifurcation application, ‘it should seek to determine what will best serve the Parties and the sound administration of justice, in particular with respect to procedural efficiency’.10 The ICSID Secretariat appears to have embraced this emphasis on efficiency. A new provision appears in the ICSID Secretariat’s recently proposed revisions to the ICSID Arbitration Rules, specifying that:

[i]n determining whether to bifurcate, the Tribunal shall consider all relevant circumstances, including whether bifurcation would materially reduce the time and cost of the proceeding.11

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6 See, e.g., Global Telecom Holding S.A.E. v. Canada, ICSID Case No. ARB/16/16, Procedural Order No. 2 Decision on Respondent Request for Bifurcation, December 14, 2017 (holding that ‘[n]either the ICSID Convention nor the Arbitration Rules sets forth a legal standard applicable to the decision of whether to join preliminary objections to the merits or instead to hear them in a preliminary phase. The ICSID Convention and the Arbitration Rules leave this decision entirely to the discretion of tribunals’).


10 Eco Oro Minerals Corp. v. Republic of Colombia, ICSID Case No. ARB/16/41, Procedural Order No. 2, June 28, 2018, para. 50.

To determine whether bifurcation would be efficient, investment treaty tribunals focus their analyses on three questions: 12

a Is the jurisdictional objection serious and substantial (i.e., does the objection have a reasonable chance of success)?
b Will the jurisdictional objection, if sustained, result in a material reduction (or complete elimination) of the merits phase of the proceedings?
c Is the jurisdictional objection so intertwined with the merits that bifurcation is impractical?

Each prong of the test is taken up in the sections that follow.

**Prong 1: Is the jurisdictional objection serious and substantial?**

The first question that tribunals ask when addressing an application to bifurcate is whether the jurisdictional objection is ‘serious and substantial’. 13 If it is not, the objection is unlikely to succeed, and will not dispense with (or reduce the scope of) the arbitration. It follows that absent one or more serious and substantial objections, a separate jurisdictional phase is needless and wasteful. When addressing whether a jurisdictional objection is serious and substantial at the bifurcation request stage, tribunals do not undertake a full analysis of the objections. Instead, tribunals typically limit their assessment to whether, on its face, the objection is frivolous or clearly without merit. The *Resolute Forest* tribunal explained the limited nature of the Prong 1 inquiry, noting that:

> [t]he determination of the first part of the test, namely whether an objection is prima facie serious and substantial[,] should not, in the Tribunal's view, entail a preview of the jurisdictional arguments themselves. Rather, at this stage the Tribunal is only required to be satisfied that the objections are not frivolous or vexatious. 14

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13 See, e.g., *Lighthouse Corporation Pty Ltd and Lighthouse Corporation Ltd, IBC v. Democratic Republic of Timor-Leste*, ICSID Case No. ARB/15/2, Procedural Order No. 3 on Bifurcation and Related Requests, July 8, 2016, para. 23 (holding that Timor Leste’s objections regarding consent to ICSID arbitration, the existence of a cognizable investment, and the alleged foreign investor’s nationality ‘do not appear frivolous’, and thus, satisfy Prong 1 of the test).

This approach creates practical challenges for counsel when crafting Prong 1-related arguments. On the one hand, a respondent must set out its arguments in some detail to satisfy the tribunal that its objection is not frivolous. And of course, a claimant will need to assert its counterarguments with some granularity to persuade the tribunal that the respondent’s objection is not, in fact, serious and substantial. On the other hand, it is not appropriate for the parties to submit a lengthy, fully formed jurisdictional briefing (backed by extensive jurisprudence, copious factual evidence, etc.) at this stage. For counsel, finding the right balance with respect to Prong 1 can be a challenge.

**Prong 2: Will a successful objection materially reduce the scope of the proceedings?**

The second question that investment treaty tribunals generally ask when considering a bifurcation application relates to the impact that the jurisdictional objection, if successful, will have on the proceedings. If the objection will not ‘materially reduce’ the scope of the arbitration, bifurcation will be a wasteful exercise. This of course raises the question: what does ‘materially’ mean in this context? On one extreme, if a successful jurisdictional objection would end the arbitration, that objection would certainly satisfy Prong 2. This was the situation in the recent *Glencore v. Bolivia* decision on bifurcation, where the tribunal noted that:

> Respondent alleges that the Tribunal lacks jurisdiction because Glencore Bermuda committed an abuse of process by structuring an investment in order to obtain standing. . . . as to [this objection] it is clear that, if successful, these proceeding [sic] would be brought to an end.16

However, if a successful objection would only narrow, but not eliminate, a future merits phase, this may not be sufficient to warrant bifurcation. The *Gavrilovic v. Croatia* tribunal held that a bifurcation application failed Prong 2 of the analysis because:

> even if the Respondent were successful in its [jurisdictional argument], it would not appear to obviate the need for a merits phase. . . . Indeed, the scope of the dispute, although perhaps narrower, may not be so narrowed as to warrant the cost, expense and inconvenience of dividing the proceeding into two phases. Put simply, as the Claimants contend, it appears not to be a substantial enough objection, in and of itself, to justify bifurcation.17

As this analysis illustrates, the requirement that a jurisdictional objection can materially reduce the scope of the arbitration is a sensible one. It would be inefficient to hear a jurisdictional objection in a separate phase if, regardless of the outcome, the parties will nonetheless proceed to a complex and costly merits phase of the proceedings.

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15 Of course, a jurisdictional objection may also be raised by a claimant against a respondent state’s ancillary claim (such as a counterclaim) – and thus, at least in theory, bifurcation could equally be sought by a claimant looking to dispose of a respondent state’s claim. For convenience, however, the discussion here will use terminology associated with the far more common scenario of a respondent state proposing bifurcation and the claimant investor resisting it.


17 *Gavrilovic and Gavrilovic d.o.o. v. Republic of Croatia*, ICSID Case No. ARB/12/39, Decision on Bifurcation, January 21, 2015, para. 82.
Prong 3: Is the jurisdictional objection intertwined with the merits?

The third question that investment treaty tribunals typically ask when considering bifurcation is whether reaching a decision on the jurisdictional objection will require an examination of the merits of the case. If the jurisdictional arguments are too intertwined with merits-related issues, tribunals generally refuse to bifurcate.18 Professor Schreuer confirms that bifurcation is not appropriate 'where the answer to the jurisdictional questions depends on testimony and other evidence that can only be obtained through a full hearing of the case'.19

The Gavrilovic v. Croatia tribunal explored Prong 3 in detail, ultimately concluding that the jurisdictional objections in that case were not sufficiently separated from the merits.20 The Gavrilovic tribunal held that:

a ruling on at least three of the four preliminary objections would in all likelihood require a detailed examination of the same evidence that will ultimately need to be examined at the stage of determining the merits. There is no procedural or other advantage with bifurcating the proceeding, so as to require not only the Tribunal to consider the same, or similar, evidence on two occasions, but so as to require witnesses to appear on two occasions, submissions to be prepared which canvass the same, or similar, matters, and the consequential cost and expense. . . . Once a considerable factual overlap is accepted, which the Tribunal considers to be the case, little can be said in support of the division of the case.21

As the Gavrilovic tribunal explained clearly, there is little sense in bifurcating a jurisdictional objection if, to decide that objection, a tribunal would need to examine anyway the merits of the claimant’s claims. Furthermore, tribunals have held that addressing merits-related issues at the jurisdictional stage – before the tribunal can review all of the evidence and arguments on the merits – could raise due process issues related to ‘prejudging’ the merits.22

The three-part analysis described above is a conjunctive test. Tribunals typically only favour bifurcation when a preliminary objection meets all three criteria. It would seem ill-advised, for example, to bifurcate an objection that was not serious and substantial (Prong 1), even if the objection would dispose of the case if successful and was distinct from the merits (Prongs 2 and 3). Likewise, it would appear unwise to bifurcate an objection that would not

18 See, e.g., Gavrilovic and Gavrilovic d.o.o. v. Republic of Croatia, ICSID Case No. ARB/12/39, Decision on Bifurcation, January 21, 2015, para. 93. See also Lighthouse Corporation Pty Ltd and Lighthouse Corporation Ltd, IBC v. Democratic Republic of Timor-Leste, ICSID Case No. ARB/15/2, Procedural Order No. 3 on Bifurcation and Related Requests, July 8, 2016, para. 25.
20 Gavrilovic and Gavrilovic d.o.o. v. Republic of Croatia, ICSID Case No. ARB/12/39, Decision on Bifurcation, January 21, 2015, para. 93.
21 ibid.
dispose of ‘all or an essential part of’ the claims (Prong 2), even if the objection were serious and substantial and distinct from the merits (Prongs 1 and 3). For these reasons, tribunals typically deny bifurcation if an objection fails even one of the three prongs of the test.

III  STRATEGIC CONSIDERATIONS REGARDING BIFURCATION APPLICATIONS

In light of the significant impact that bifurcation can have on the arbitral process, parties should consider carefully whether to request or to resist bifurcation. Unsurprisingly, the strategic considerations for claimant investors and respondent states differ, as are described below.

i  Strategic considerations for respondents

The conventional wisdom is that if a respondent state has reasonably sound jurisdictional objections, the respondent should seek to bifurcate the proceedings. There is logic to this approach: if a respondent prevails on one or more of its jurisdictional objections, this could dispense with, or at least lessen the complexity of, the merits phase of the arbitration. In addition to this clear upside, there are at least three other potential benefits to a respondent seeking bifurcation.

First, bifurcated proceedings often focus the tribunal’s attention (at least initially) on facts favourable to the respondent. In many cases, the factual story related to a jurisdictional objection (be it corruption, illegality, abuse of process, etc.) does not present a claimant in a positive light. However, the facts related to the merits (e.g., alleged expropriation or unfair and inequitable government treatment) may well paint a less-than-ideal picture of the respondent state. In that scenario, by isolating jurisdictional issues from the rest of the case, a respondent can focus the tribunal’s attention on factual issues that are unfavourable to the claimant, while keeping its own alleged misdeeds largely out of the spotlight. By shaping and narrowing the story in this way, the respondent gains a strategic advantage.

Second, respondents might seek to use bifurcation to extend arbitral proceedings to delay any possible adverse consequences of their actions. Although this is an approach the authors do not endorse, commentators have observed that ‘[a] party may be advocating bifurcation to delay and obstruct the arbitration, rather than to make it more efficient.’23 The appeal of this strategy is not difficult to discern: in a bifurcated proceeding, even if the jurisdictional claim fails, the respondent succeeds in extending the arbitral calendar, and thus, delaying its receipt of a potential adverse award. (Though a tribunal’s eventual award of interest could in theory nullify any financial advantage of such a delay, financial motives may not be the only ones in play.)

Third, if a respondent state presents a jurisdictional objection, but does not seek bifurcation, a tribunal might (rightly or wrongly) perceive this as an indication that the respondent believes its jurisdictional objection is weak. It could be argued that if a respondent truly believes its jurisdictional objection will succeed, it will seek to have that objection heard before arguing the merits.

There are, however, perfectly valid reasons why a respondent state might not want to seek bifurcation. For example, if a respondent believes that the overall equities favour the state – imagine, for example, that the respondent has evidence that the investor caused serious

environmental damage that it wants the tribunal to see – it might behoove that respondent to tell its whole story (jurisdiction and merits) all at once for maximum impact. Or, if a respondent’s jurisdictional objection will not significantly streamline the case if successful, the respondent might be best served by not seeking bifurcation, thereby avoiding additional costs. More often, however, if a respondent has strong jurisdictional objections that will have a material impact on the scope of the case, seeking bifurcation is a prudent course.

ii Strategic considerations for claimants

Claimants typically oppose bifurcation, and do so for reasons that are often the converse of the factors that lead respondents to lodge bifurcation requests. First, claimants generally prefer to avoid stand-alone jurisdictional phases if they will focus on the claimants’ own misconduct (e.g., corruption or abuse of rights), while deferring consideration of the compelling facts that claimants want to highlight (e.g., facts related to expropriation or unfair treatment). In those cases, claimants will perceive a benefit in presenting their merits-related story at the same time that they argue jurisdiction.

Second, unlike a respondent (which might prefer for various reasons to extend the proceedings), a claimant’s incentive is to conclude the arbitration and receive a favourable award as quickly as possible. The most direct path to that outcome is an arbitral process in which the tribunal hears jurisdiction and merits together.

Third, Prong 1 of the bifurcation analysis relates to whether the jurisdictional objection is serious and substantial. Thus, an application for bifurcation necessarily involves an argument from the respondent that it is asserting a serious and substantial objection. If a claimant does not challenge that characterisation, a tribunal might interpret this as a sign that the respondent’s objections have traction. At the very least, by not opposing bifurcation, a claimant forgoes an early opportunity to explain to the tribunal why the respondent’s jurisdictional objection is not, in fact, serious and substantial.

For these reasons, it is typically advisable for claimants to oppose bifurcation. As always, however, there are exceptions to the rule. For instance, if a respondent raises a jurisdictional objection that is indeed distinct from the merits and has the potential to dispose of the case, it might make sense for a claimant to agree to bifurcate that issue to save its own resources as well. The case for doing so may be even stronger if, in exchange for agreeing not to oppose bifurcation, the claimant can secure the respondent’s agreement to an accelerated procedural calendar for the jurisdictional phase. Imagine, for example, a hypothetical case where a respondent state objects to ICSID jurisdiction based on its withdrawal from the ICSID Convention. This is a purely legal issue that is wholly separate from the substance of the hypothetical investor’s claim, and may be amenable to a relatively speedy resolution. In this scenario, it might be wise for a claimant to agree to obtain the tribunal’s verdict on the threshold issue before expending the resources to fully develop and argue its case on the merits.

IV BIFURCATION OF DAMAGES

Historically, the vast majority of bifurcated proceedings have involved the separation of the jurisdictional and merits phases of an arbitration. This section, however, briefly discusses a different category of bifurcation: separating the damages phase of the proceedings from
the merits.24 The rules of the major arbitral institutions do not specifically provide for the bifurcation of damages or quantum issues. However, tribunals typically cite procedural rules granting them general authority to control the arbitration procedure as a basis for bifurcating damages.25

Although bifurcating damages is not common, it also not unheard of – tribunals do, on occasion, decide damages-related issues separately from the merits, and considerations of efficiency appear to predominate in their analysis of the decision to do so, just as in the bifurcation of jurisdiction and merits.26 For instance, in Suez v. Argentina, the tribunal decided that the most efficient approach would be to separate its damages analysis from its decision on the liability of the respondent. The Suez tribunal stated that it:

*has decided to render a decision on liability before arriving at an award on damages. It has chosen to adopt this procedure for reasons of judicial economy. Given the complexity of this case and the extraordinarily voluminous nature of the record, the Tribunal by rendering a decision on liability now and thereby defining the scope of its investigation with respect to a determination of damages will be able more efficiently to define the mission of the independent expert that will assist the Tribunal in this determination.*27

The tribunal in Glencore v. Bolivia took a similar approach. In that case, the tribunal rejected an application to hear jurisdictional challenges in a separate phase, but chose to bifurcate damages, noting that ‘[t]his approach seems to the Tribunal more efficient in terms of time and costs than the alternative’.28

Bifurcating the damages phase is more likely to produce efficiencies in particular situations. For instance, where a claimant plans to assert particularly complex, novel or fact-intensive damages arguments, bifurcation of damages may be warranted for at least two reasons. First, if the claims fail at the jurisdictional or merits stage, both parties would avoid the time and expense associated with developing their complicated damages-related theories. Second, a separate damages phase would ensure that parties have sufficient opportunity to focus on, and fully develop, their damages theories and counterarguments. Another scenario that might warrant bifurcation of damages would be a case involving jurisdictional objections with the potential to eliminate some claims, particularly if the damages are expected to differ

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24 We use ‘the merits’ here to encompass all stages of the case leading to a finding of liability, whether or not those prior stages include jurisdictional objections (or indeed, even bifurcation of jurisdictional issues, which can potentially lead to ‘trifurcation’ of the case into jurisdiction, merits, and damages phases).

25 For instance, in Suez v. Argentina, the tribunal based its authority to bifurcate damages on Article 44 of the ICSID Convention, which states that: ‘[i]f any question of procedure arises which is not covered by this Section or the Arbitration Rules or any rules agreed by the parties, the Tribunal shall decide the question’. See Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal S.A v. Argentine Republic, ICSID Case No. ARB/03/19, Decision on Liability, July 30, 2010, para. 272.


from claim to claim or overlap in complex ways across claims. In that situation, where the jurisdictional outcome may significantly reduce the scope or complexity of the damages analysis, it may make sense to bifurcate and address damages only after it is clear which claims are left standing.

V CONCLUSION

As this chapter highlights, a decision on bifurcation is a critical procedural moment in an arbitration. Though bifurcation can accelerate the resolution of a dispute, it can also significantly prolong the arbitral process. For this reason, tribunals have developed – and have applied with commendable consistency – the detailed, tripartite test described above. The parties also play an important role. Their strategic decisions regarding whether to request or to oppose bifurcation will shape the arbitration in important ways, impacting the length and cost of the arbitral proceedings.
INTRODUCTION

The promulgation of Rule 41(5) in the ICSID Rules of Procedure for Arbitration Proceedings (the ICSID Arbitration Rules) on 10 April 2006 was a bold and innovative step in international arbitration, and remained a unique feature of the ICSID Arbitration Rules for the first 10 years of its promulgation. Rule 41(5) reads:

Unless the parties have agreed to another expedited procedure for making preliminary objections, a party may, no later than 30 days after the constitution of the Tribunal, and in any event before the first session of the Tribunal, file an objection that a claim is manifestly without legal merit. The party shall specify as precisely as possible the basis for the objection. The Tribunal, after giving the parties the opportunity to present their observations on the objections, shall, at its first session or promptly thereafter, notify the parties of its decision on the objection. The decision of the Tribunal shall be without prejudice to the right of a party to file an objection pursuant to [Rule 41(1)] or to object, in the course of the proceeding, that a claim lacks legal merit.

The governing rules of most arbitral institutions did not stipulate in express terms the arbitral tribunal’s authority to dismiss claims in an expedited fashion, other than to make a general...
provision for the tribunal to ‘conduct the proceedings so as to avoid unnecessary delay and expense and to provide a fair and efficient process for resolving the parties’ disputes’. Over the past few years, major arbitral institutions have departed from this trend, and there is an increasing number of institutional rules that now expressly provide for powers of summary dismissal of claims. Although some commentators have suggested that it is possible for such authority to be read into the general provision, tribunals no doubt take different views on this. It is reasonable to imagine that an arbitral tribunal would be slow to terminate the proceedings at the outset, without an explicit power to do so, for fear of (unwittingly) affecting the claimant’s right to be heard.

II GENESIS OF RULE 41(5)

The inclusion of such a summary dismissal mechanism in the ICSID Arbitration Rules was first raised in an ICSID Secretariat Discussion Paper circulated to the members of the ICSID

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Objections of Manifest Lack of Legal Merit of Claims: Arbitration Rule 41(5)

Administrative Council on 22 October 2004, some 36 years after the ICSID Arbitration Rules came into force on 1 January 1968. It proposed the creation of ‘a special procedure’, pursuant to which ‘the tribunal may at an early stage of the case be asked on an expedited basis to dismiss all or part of the claim . . . without prejudice to the further objections a party might make, if the request were denied’. This was intended to address calls for greater efficiency in ICSID proceedings, as well as recurring complaints by state parties that the ICSID Secretariat’s limited screening power under Article 36(3) of the ICSID Convention was inadequate to weed out claims that were manifestly unmeritorious. These complaints grew louder with the increase in number of investment claims lodged, and were fuelled by concerns that state parties were being exposed to abusive tactics of investors seeking to game the system:

The significant increase in investment disputes over the last decade has given rise to the concern that investors may abuse the system. Investors may be eager to claim as many violations of the applicable IIA as possible in order to increase their chances of success. This may take a heavy toll in terms of time, effort, fees and other costs, not only for the parties to the dispute, but also for the arbitral tribunal. It is within this context that several countries have advocated a procedure to avoid “frivolous claims” in investment-related disputes, namely claims that evidently lack a sound legal basis.

Following consultations with various stakeholders and interest groups, the first draft of what would become the current Rule 41(5) was published in a 12 May 2005 ICSID Secretariat Working Paper. The main differences between the draft and final versions of the text of Rule 41(5) were the addition in the final version of ‘legal’ in the phrase ‘manifestly without legal merit’; the inclusion in the final version that parties can agree ‘to another expedited

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11 ICSID Discussion Paper-2004 at [10].
12 The exercise of the Article 36(3) screening power is confined to cases where the request discloses a manifest lack of jurisdiction, and does not extend to the merits of the dispute or to cases where jurisdiction is merely doubtful but not manifestly lacking. A decision by the ICSID Secretariat pursuant to Article 36(3) is, furthermore, given only on the basis of information supplied by the requesting party and therefore does not typically follow an adversarial process. See ICSID Discussion Paper-2004 at [6], [9], [10]; Antonio Parra, ‘The Development of the Regulations and Rules of the International Centre for Settlement of Investment Disputes’ (2007) 22(1) ICSID Review 55, page 65; Puig and Brown, ‘The Secretary-General’s Power To Refuse To Register a Request for Arbitration under the ICSID Convention’ (2012) 27(1) ICSID Review 172, page 190; Carlevaris, ‘Preliminary Matters: Objections, Bi-furcation, Request for Provisional Measures’ in Litigating International Investment Disputes: A Practitioner’s Guide (Giorgetti ed., Brill, 2014) page 173 (Carlevaris-2014), pages 175–180; Michele Potestà, ‘Preliminary Objections to Dismiss Claims that are Manifestly Without Legal Merit under Rule 41(5) of the ICSID Arbitration Rules’ in Crina Baltag (ed.), ICSID Convention after 50 Years: Unsettled Issues (Kluwer Law International, 2017) (Potestà-2017), page 252.
procedure for making preliminary objections; and the addition of the rule that the objection needs to be filed ‘in any event before the first session of the Tribunal’ (these aspects of the Rule are discussed further in Section IV).

III  THE EARLY CASES

Rule 41(5) got off to a relatively muted beginning. In the first three years of its existence, it was invoked only twice in the 72 cases registered under the ICSID Convention15 (in Trans-Global Petroleum Inc v. Jordan16 (Trans-Global) in February 2008 and Brandes Investment v. Venezuela17 (Brandes) in December 2008), and with only partial success in Trans-Global.

Trans-Global concerned allegations that Jordan had engaged in a systematic campaign to destroy the claimant’s investments in a petroleum exploration venture after the claimant confirmed its discovery of oil pay zones in the designated area of exploration. Specifically, Jordan was alleged to have breached (1) the fair and equitable treatment standard in Article II(3)(a) of the US–Jordan bilateral investment treaty (BIT), (2) the non-discrimination provision in Article II(3)(b) of the US–Jordan BIT and (3) an obligation to consult the claimant in Article VIII of the US–Jordan BIT. Jordan filed Rule 41(5) objections, asserting that the claims were manifestly without legal merit as they alleged ‘infringements of non-existent legal rights of the Claimant or non-existent legal obligations of [Jordan]’.18 The application failed in relation to the first two claims under Articles II(3)(a) and II(3)(b), but succeeded in relation to the third claim as Article VIII was found to contain only an obligation of consultation between the two contracting states and not between the investor and the host state; ‘the essential legal basis’ in respect of the third claim was therefore ‘entirely missing under the BIT’.19

It was not until December 2010 that Rule 41(5) came to life.20 Within a span of 10 days, two separate tribunals in Global Trading Resource Corp and anor v. Ukraine21 (Global Trading) and RSM Production Corp v. Grenada22 (RSM Production) issued orders dismissing claims pursuant to Rule 41(5). The tribunal in Global Trading did so on jurisdictional grounds (holding that the sale and purchase contracts on which the claims were based were ‘pure commercial transactions that cannot on any interpretation be considered to constitute “investments” within the meaning of Article 25 of the ICSID Convention’),23 while the

17 Brandes Investment v. Venezuela, ICSID Case No. ARB/08/3 (Decision on the Respondent’s Objection under Rule 41(5) of the ICSID Arbitration Rules, 2 February 2009).
18 Trans-Global at [95].
19 Trans-Global at [118]–[119].
21 Global Trading Resource Corp and Globex International Inc v. Ukraine, ICSID Case No. ARB/09/11 (Award, 1 December 2010).
22 RSM Production Corporation and ors v. Grenada, ICSID Case No. ARB/10/6 (Award, 10 December 2010).
23 Global Trading at [57].
tribunal in *RSM Production* dismissed all of the claimant’s claims on preclusion grounds (as the claims were ‘no more than an attempt to relitigate and overturn the findings of another ICSID tribunal’). Since then, decisions on Rule 41(5) have been rendered (albeit mostly finding against the applicant) a further 23 times (thrice in annulment proceedings), bringing the total number of Rule 41(5) applications filed to date to 27. A review of the available decisions rendered to date reveals a fairly consistent application and interpretation of Rule 41(5) by ICSID tribunals (see Section IV).

### IV RULE 41(5) IN PRACTICE

#### i A residual rule

Rule 41(5) begins with ‘Unless the parties have agreed to another expedited procedure for making preliminary objections’. This accords ‘proper prominence’ to agreements on other forms of expedited procedures that may already be contained in some investment treaties and

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24 *RSM Production* at [9.1].
25 *RSM Production* at [7.3.6].
26 Although China in *Ansung Housing Co Ltd v. People’s Republic of China*, ICSID Case No. ARB/14/25 (Award, 9 March 2017) (*Ansung Housing*) (the second ever ICSID claim to be brought against China, and the first such claim to proceed past the stage of tribunal constitution) succeeded in its Rule 41(5) application (filed on 15 September 2016), on the grounds that the claim was time-barred under Article 9(7) of the 2007 China–Korea BIT and thus ‘manifestly without legal merit’ (*see* *Ansung Housing* at [105]–[122]), and that the MFN clause in Article 3(3) of the 2007 PRC–Korea BIT could not be invoked to sidestep the temporal limitation prescribed in Article 9(7) (*see* *Ansung Housing* at [136]–[141]). The tribunal issued an oral ruling in China’s favour at the close of the Rule 41(5) hearing (conducted during the first session in Singapore) on 14 December 2016, declared the proceedings closed on 15 February 2017 (following the submission of costs statements and observations on costs) (*see* *Ansung Housing* at [4], [24]–[27]), before issuing its Award on 9 March 2017.

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agreements. Where that is the case, the procedure proposed in Rule 41(5) would only apply to the extent not otherwise agreed by the parties under the relevant treaties. See, for example, Pac Rim Cayman LLC v. El Salvador (Pac Rim), where El Salvador submitted that, given the opening line in Rule 41(5), it was the expedited procedure under Articles 10.20.4 and 10.20.5 of CAFTA, and not that under Rule 41(5), that was applicable. That submission was not materially disputed by the claimant and was accepted by the ICSID tribunal as correct.

ii Scope – merits, jurisdiction and procedure

In terms of the scope of objections that can be raised by respondent states, it is by now accepted that Rule 41(5) permits not just objections as to merits, but also jurisdictional objections. As was first noted in Brandes:

Rule 41(5) does not mention “jurisdiction”. The terms employed are “legal merit”. This wording, by itself, does not provide a reason why the question whether or not a tribunal has jurisdiction and is competent to hear and decide a claim could not be included in the very general notion that the claim filed is “without legal merit”. . . . [But] [s]till there exist no objective reasons why the intent not to burden the parties with a possibly long and costly proceeding when dealing with such unmeritorious claims should be limited to an evaluation of the merits of the case and should not also englobe an examination of the jurisdictional basis on which the tribunal’s powers to decide the case rest. . . . The Arbitral Tribunal therefore interprets Rule 41(5) in the sense that the term “legal merit” covers all objections to the effect that the proceedings should be discontinued at an early stage because, for whatever reason, the claim can manifestly not be granted by the Tribunal.

30 For example, Article 9.22(4) of the Trans-Pacific Partnership Agreement (read with Article 9, 22(4) of the Trans-Pacific Partnership Agreement), which permits the raising of preliminary objections on the ground that a claim is manifestly without legal merit; Articles 28(4) and 28(5) of the 2012 US Model BIT, which provides that a tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favour of the claimant may be made; Articles 10.19(4) and 10.19(5) of the 2003 Chile–US Free Trade Agreement; Articles 28(4) and 28(5) of the 2008 Rwanda–US BIT; Articles 10.20.4 and 10.20.5 of the Central America Free Trade Agreement (CAFTA).

31 Antonietti, ‘The 2006 Amendments to the ICSID Rules and Regulations and the Additional Facility Rules’ (2007) 41 International Lawyer 427 (Antonietti-2007), page 441. In the absence of such a treaty provision, disputing parties may also mutually agree on the use of an alternative procedure (e.g., in an investment contract), though one would expect such a scenario to be uncommon: Potestà and Sobat-2012, page 12; Potestà-2017, page 253.

32 Pac Rim Cayman LLC v. El Salvador, ICSID Case No. ARB/09/12 (Decision on the Respondent’s Preliminary Objections under CAFTA Articles 10.20.4 and 10.20.5, 2 August 2010).

33 Pac Rim at [81].

34 Pac Rim at [85].

35 Though ‘a party may’ in Rule 41(5) would seem to encompass both the claimant and respondent, the procedure is hardly likely to hold much interest for a claimant (except for the case where a claimant is seeking the dismissal of a respondent’s unmeritorious counterclaim): Potestà-2017, page 254.


37 Brandes at [50], [52], [55].

38 See, further, Diop-2010, pages 322–323.
This position accords with the drafting history of Rule 41(5) and discussions at the ICSID Secretariat during the 2006 amendment process, and has been consistently endorsed by subsequent ICSID tribunals confronted with Rule 41(5) applications raising objections based on jurisdiction.

In *RSM Production*, Rule 41(5) was further extended to cover objections premised on ‘equitable considerations and procedural impediments’. The dispute concerned an agreement between the claimant and Grenada, under which the claimant was to be granted a licence for petroleum exploration if this was requested within a certain period. After Grenada denied the claimant’s untimely licence request, the claimant initiated ICSID arbitration proceedings, which were disposed of in Grenada’s favour. The claimant was dissatisfied, and commenced a second ICSID arbitration on the basis of the US–Grenada BIT, although all of the legal and factual predicates of the claims were the same as those that arose in the first arbitration and had been determined conclusively against the claimants. In the circumstances, the tribunal in the second arbitration dismissed all of the claims pursuant to Rule 41(5), reasoning that:

> [A]: pleaded and argued, the present case is no more than an attempt to relitigate and overturn the findings of another ICSID tribunal, based on allegations of corruption that were either known at the time or which ought to have been raised by way of a revision application and over which the Prior Tribunal had jurisdiction. Claimant’s present case is thus no more than a contractual claim (previously decided by an ICSID tribunal which had the jurisdiction to deal with Treaty and contractual issues), dressed up as a Treaty case. . . . [T]he Tribunal finds that the initiation of the present arbitration is thus an improper attempt to circumvent the basic principles set out in Convention Article 53 [finality of awards] and the procedures available for revision and rectification of awards provided for in Article 51.

The ‘abuse of process’ overtones in *RSM Production* highlight an additional functionality of Rule 41(5) in preventing abuse of international arbitral procedures. As Brabandere suggests, ‘[a]lthough the objective of Rule 41(5) is not explicitly aimed at targeting claims that constitute an “abuse of process”, it is likely that the rule will prevent, or at least offer an adequate procedure to assess the submission of such claims, since it provides arbitral tribunals operating under the ICSID Convention with a procedure to assess the claims, *inter alia* on these grounds in an early stage in the proceedings.’ It remains to be seen whether Rule 41(5) will be more often utilised in this capacity.

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39 Diop-2010, page 322.
40 See Global Trading at [30]; PNG Sustainable Development Program Ltd v. Papua New Guinea, ICSID Case No. ARB/13/33 (Decision on the Respondent’s Objections under Rule 41(5) of the ICSID Arbitration Rules, 28 October 2015) at [91]; Emmis International Holdings BV and ors v. Hungary, ICSID Case No. ARB/12/2 (Decision on Respondent’s Objection under ICSID Arbitration Rule 41(5), 11 March 2013) (Emmis International) at [64]–[72]; Lion Mexico at [71]–[75] (in the context of an application brought pursuant to Rule 45(6) of the ICSID Arbitration (Additional Facility) Rule).
41 Diop-2010, page 324.
42 *RSM Production* at [4.1.1]–[4.1.2].
43 *RSM Production* at [7.3.6]–[7.3.7].
44 Brabandere-2012, pages 30 and 44.
45 Brabandere-2012, page 44.
Objections of Manifest Lack of Legal Merit of Claims: Arbitration Rule 41(5)

iii Procedure

The procedure under Rule 41(5) is significantly expedited. The respondent has just 30 days after the constitution of the tribunal, and ‘in any event before the first session of the Tribunal’, to raise any objection under Rule 41(5). This 30-day period was designed to fit within the default 60-day period post the constitution of the tribunal (stipulated in ICSID Arbitration Rule 13(1)) within which the tribunal must hold its first session, and after which the tribunal must decide ‘promptly’.

Though it was suggested that ‘promptly’ should be understood in terms of ‘days or weeks, [and] not months’, the concept has generally been applied in terms of weeks and, at times, months; for example, the tribunals in *Trans-Global, Brandes and PNG Sustainable Development Program Ltd v. Papua New Guinea (PNGSDP)* took roughly three weeks following oral arguments to issue their decisions, whereas the process took more than three months in *Lion Mexico* and almost five months in *Global Trading*.

In any case, the Rule specifically requires parties to be given ‘the opportunity to present their observations on the objections’ before the tribunal ‘promptly’ decides, and failure to accord parties with a full opportunity to be heard could potentially lead to a charge of serious departure from a fundamental rule of procedure, with the consequence of a possible annulment under Article 52(1)(d) of the ICSID Convention. How the balance between the desire for an expedited decision and the requirements of a properly reasoned determination is to be struck would depend on the requirements of each individual case. As noted in *Global Trading*:

Rule 41(5) is sparse in its indications to a tribunal as to the procedure to be followed when an objection is lodged. It says no more than that “the parties” (in the plural) must have ‘the opportunity to present their observations on the objection”, and that the Tribunal is required to notify the parties of its decision “at its first session or shortly thereafter”. To the extent that the Rule leaves the question of procedure there, it is no doubt for each individual Tribunal to fill in the gaps by exercising the general procedural powers given to it by Rule 19. On the other hand, it should be noted that – if a Tribunal does in the event decide that all claims are manifestly without legal merit – it is then required by Rule 41(6) to render “an award” to that effect, thus attracting those elements of the Rules and the ICSID Convention that relate to the rendering of an award. . . . There may be cases in which a tribunal can come to a clear conclusion on a Rule 41(5) objection, simply on the written submissions, but they will be rare, and the assumption must be that, even then, the decision will

46 The 2016 SIAC Rules and 2017 SIAC Investment Arbitration Rules do not specify any time limit to raise an objection that the claim is manifestly without legal merit.
49 ICSID Case No. ARB/13/33 (Decision on the Respondent’s Objections under Rule 41(5) of the ICSID Arbitration Rules, 28 October 2014).
50 There must be some limit to this – if it is too difficult to decide, the case is probably not one that is suitable for summary dismissal under Rule 41(5). The drafters of Rule 41(5) ‘can only have had in mind an objection that was so clear-cut that it could be decided virtually on the papers or with a minimum of supplementary argument’ (*MOL Hungarian Oil and Gas Company plc v. Croatia*, ICSID Case No. ARB/13/32 (Decision on Respondent’s Application under ICSID Arbitration Rule 41(5), 2 December 2014) (*MOL*) at [44].

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be one not to uphold the objection, rather than the converse. That is because, if an objection is not upheld at the Rule 41(5) stage, the rights of the objecting party remain intact, as the last sentence of the Rule makes plain.\textsuperscript{52}

It appears to be the norm for parties to be permitted one to two rounds of written submissions, followed by a round of oral arguments, before the tribunal issues a decision or award under Rule 41(5). With the exception of a handful of cases,\textsuperscript{53} this has been the typical manner in which Rule 41(5) proceedings have been conducted to date.\textsuperscript{54}

Finally, the last sentence of Rule 41(5) makes clear that the dismissal of a Rule 41(5) objection will not affect a party’s right to thereafter file jurisdictional objections according to the normal procedure under Rule 41(1). In this manner, Rule 41(5) forms part of a ‘harmonious continuum’\textsuperscript{55} of jurisdictional review of claims with a progressively higher standard of review at each stage, beginning from the Secretary General’s screening power under Article 36(3) of the ICSID Convention, and ending with the tribunal’s determination of objections raised under the Rule 41(1) procedure.\textsuperscript{56}

\textsuperscript{52} Global Trading at [32]–[33].

\textsuperscript{53} Emnis International; Accession Mezzanine Capital LP and anor v. Hungary, ICSID Case No. ARB/12/3 (Decision on Respondent’s Objection under Arbitration Rule 41(5), 16 January 2013); Edenred SA v. Hungary, ICSID Case No. ARB/13/21 (Decision on Preliminary Objections Pursuant to ICSID Arbitration Rule 41(5), 6 June 2014); Transglobal Green Energy LLC and Transtglobal Green Panama SA v. Republic of Panama, ICSID Case No. ARB/13/28 (Decision on the Admissibility of Respondent’s Preliminary Objection to Jurisdiction of the Tribunal under Rule 41(5) of the Arbitration Rules, 17 March 2015); Álvarez y Marisc Corporation SA and others v. Republic of Panama (Álvarez), ICSID Case No. ARB/15/14 (Decision on Respondent’s Preliminary Objections Pursuant to ICSID Arbitration Rule 41(5), 27 January 2016); Matthias Kruck and others v. Spain, ICSID Case No. ARB/15/23 (Decision on the Respondent’s Preliminary Objections Pursuant to ICSID Arbitration Rule 41(5), 14 March 2016); Lion Mexico (where the tribunals appeared to have dispensed with oral arguments on the Rule 41(5) applications).

\textsuperscript{54} Trans-Global; Brandes; Global Trading; RSM Production; Rafat Ali Rizvi v. Indonesia, ICSID Case No. ARB/11/13 (Award on Jurisdiction, 16 July 2013); PNGSDP; MOL; Pan American Energy LLC v. Plurinational State of Bolivia, ICSID Case No. ARB/10/8 (Decision on the Respondent’s Objection Pursuant to Rule 41(5) of the ICSID Arbitration Rules, 26 April 2013); CEAC Holdings Limited v. Montenegro, ICSID Case No. ARB/14/8 (Decision on the Respondent’s Preliminary Objections Pursuant to ICSID Arbitration Rule 41(5), 27 January 2015); Elektrogospodarstvo Slovenije – razvoj in inzenirving d.o.o. v. Bosnia and Herzegovina, ICSID Case No. ARB/14/13 (Decision on the Respondent’s Preliminary Objections Pursuant to ICSID Arbitration Rule 41(5), 3 November 2015); Elsamex SA v. Honduras, ICSID Case No. ARB/09/4 (Decision on Elsamex SA’s Preliminary Objections, 7 January 2014); Vattenfall AB and others v. Federal Republic of Germany, ICSID Case No. ARB/12/12 (Decision on the Respondent’s Objection Pursuant to Rule 41(5) of the ICSID Arbitration Rules, 2 July 2013); Lundin Tunisia BV v. Tunisia, ICSID Case No. ARB/12/30 (Decision on the Respondent’s Objection Pursuant to Rule 41(5) of the ICSID Arbitration Rules, 6 January 2014); Ansung Housing. Similarly for Mobile TeleSystems, in respect of proceedings under Arbitration (Additional Facility) Rule 45(6).

\textsuperscript{55} Diop-2010, page 318. See also Brandes at [53], where the tribunal noted that ‘there are actually three levels at which jurisdictional objections could be examined. First by the Secretariat, and if the case passes that level, it would then be under Rule 41(5), and if it passes that level, it might still be under Rule 41(1).’

\textsuperscript{56} Diop-2010, page 319–321.
Test for ‘manifest lack of legal merits’

There is a high level of uniformity in the manner in which ICSID tribunals have applied the test of ‘manifest’ lack of merit. ‘Manifest’ in this regard has consistently been equated with ‘evident’, ‘obvious’ or ‘clearly revealed to the eye, mind or judgement’. The threshold is very high, and a respondent must establish its Rule 41(5) objection ‘clearly and obviously, with relative ease and dispatch’. Put another way, it must be shown that the claim is ‘clearly and unequivocally unmeritorious’ and thus ‘untenable in a way that is evident and easily proved’. This will not be the case where the claimant has ‘a tenable arguable case’, or where the objections throw up novel, difficult or disputed legal issues (since Rule 41(5) was intended ‘only to apply undisputed or genuinely indisputable rules of law to uncontested facts’).

Unsurprisingly, the high threshold under Rule 41(5) has rarely been crossed. For example, in Trans-Global, where it was ‘obvious’ that the claims under Article VIII of the US–Jordan BIT were based on ‘non-existent legal rights of the Claimant’ and ‘non-existent legal obligations of [Jordan]’ (a conclusion that the tribunal was able to reach with ‘little difficulty of interpretation’); in Global Trading, where neither of the relevant contracts could ‘by any reasonable process of interpretation be construed to be “investments” for the purposes of the ICSID Convention’; in Emmis International, where it was ‘manifest’ from the ‘plain text of the Treaties’ that the claimants were not covered by the consent of the host state; and in Ansung Housing, where there were ‘multiple and clear pleadings’ by the claimants confirming that they ‘first knew’ that they incurred loss and damage more than three years before the commencement of proceedings (thus offending the three-year limitation period under Article 9(7) of the 2007 China–Korea BIT) and where it was ‘clear’ from a ‘plain reading’ of the most favoured nation (MFN) clause in Article 3(3) of the 2007 China–Korea BIT that MFN treatment did not extend to the temporal limitation period for investor–state arbitration in Article 9(7).

More often than not, the threshold is fallen short of. In PNGSDP, the state raised Rule 41(5) objections in relation to both the tribunal’s jurisdiction and the substantive merits of the claimant’s claims. On jurisdiction, the state argued that the mandatory jurisdictional requirements under Article 25(1) of the ICSID Convention were not satisfied as the state

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57 Trans-Global at [83]; PNGSDP at [88]; Lion Mexico at [62]–[67] (in the content of an application brought pursuant to Rule 45(6) of the ICSID Arbitration (Additional Facility) Rules).
58 Trans-Global at [88]; Global Trading at [35]; Brandes at [63]; PNGSDP at [88]; MOL at [25], [45]; Ansung Housing at [70], [142].
59 Lion Mexico at [66].
60 Diop-2010, page 336.
61 PNGSDP at [88].
62 PNGSDP at [89]. In Ansung Housing (see [32], [71]), the tribunal ‘assume[d] the truth of the facts alleged by Claimant’ for purposes of ruling on China’s Rule 41(5) application.
63 Trans-Global at [118].
64 Trans-Global at [95].
65 ibid.
66 Global Trading at [56].
67 Emmis International at [70].
68 Ansung Housing at [107]–[108].
69 Article 9(7) of the 2007 China–Korea BIT provided: ‘an investor may not make a claim pursuant to paragraph 3 of this Article if more than 3 years have elapsed from the date on which the investor first acquired, or should have first acquired, the knowledge that the investor had incurred loss or damage’.
70 Ansung Housing at [136]–[141].
did not provide a standing offer to arbitrate investment disputes by its domestic legislation, Section 39 of the Investment Protection Act 1992 (IPA), and the claimant was not a ‘foreign investor’ with a ‘private foreign investment’, because it existed to fulfill the sole public purposes of promoting sustainable development and advancing the general welfare of the people of Papua New Guinea (PNG). The state also argued that the claims that were based upon the alleged MFN clause in Section 37(1) of the IPA were manifestly without legal merit, as Section 37(1) was not an MFN clause but simply a clause that entitled a foreign investor to the protections under the IPA, unless the investor is entitled to more favourable treatment under any other treaty to which PNG is also a party.

Although the MFN clause argument essentially required the tribunal to construe Section 37(1) of the IPA – which could arguably be carried out under a summary Rule 41(5) procedure – after three rounds of written submissions (two by the state and one by the claimant) and an oral hearing, the tribunal found that all of the state’s objections gave rise to novel and complex issues of laws that also required analysis of ‘relatively unusual’ facts:

[T]he interpretation of the IPA and IDCA [Investment Disputes Convention Act] is central to the Respondent’s objections with respect to written consent and the alleged MFN clause in the IPA. The Tribunal considers that these interpretations cannot be satisfactorily made in the context of a Rule 41(5) application, which necessarily involves an expedited and summary procedure. The Tribunal notes that there are disputed questions regarding which system (or systems) of law should apply to the interpretation of the IPA and IDCA (in particular, international or domestic rules of interpretation), and in addition, which specific interpretive principles should apply (e.g., the effet utile principle and the rule of contra proferentem). Further, the Tribunal notes that the IPA and the IDCA have not yet been the subject of interpretation by an ICSID tribunal, and it will therefore be required to decide issues of first impressions. Doing so in a summary Rule 41(5) procedure would be inappropriate.

[T]he Respondent’s objection with respect to “private foreign investment” cannot be satisfactorily dealt with at this stage of the proceeding. The Respondent’s objection does not appear to be based upon an explicit jurisdictional criterion set out in either the ICSID Convention or the relevant PNG legislation. Rather, the Respondent’s objection appears to be based on the Respondent’s interpretation of the ICSID Convention’s jurisdictional requirements in light of materials extraneous to the terms of Article 25(1) (in particular, the Convention Preamble and the Report of the Executive Directors on the [ICSID Convention]) and a distinction drawn by the Respondent between the Claimant and what the Respondent refers to as “typical foreign investors” considered in other ICSID Convention cases.

71 Section 39 of the IPA provided: ‘The Investment Disputes Convention Act 1978, implementing the [ICSID Convention], applies, according to its terms, to disputes arising out of foreign investment.’ The Investment Disputes Convention Act 1978 in turn provided, in Section 2: ‘A dispute shall not be referred to [ICSID] unless the dispute is fundamental to the investment itself.’ Papua New Guinea (PNG) eventually succeeded on this ground in the subsequent Rule 41(1) proceedings (PNG Sustainable Development Program Ltd v. Papua New Guinea, ICSID Case No. ARB/13/33 (Award, 5 May 2015)).

72 Section 37(1) of the IPA provided: ‘The provisions of this section shall apply to a foreign investor except where treatment more favourable to the foreign investor is accorded under any bilateral or multilateral agreement to which the State is a party.’
As such, the Respondent’s objection is unsuited for a Rule 41(5) application. It does not involve application of undisputed or indisputable legal rules, but rather involves novel issues of interpretation and analysis.73

The tribunal in Lion Mexico (the first publicised decision concerning an application brought pursuant to Rule 45(6) of the ICSID Arbitration (Additional Facility) Rules) also dismissed the respondent state’s preliminary objections in very similar terms:

The amount of evidence and the length and detail of the arguments show the complexity of the underlying legal question.

The Tribunal further notes that the issue of whether pagarés [i.e., promissory notes] and hipotecas [i.e., mortgages] that formalize and secure loans with a maturity of less than three years can be considered as investments under Art. 1139(g) and (b) NAFTA – separately from contemporaneous loan transactions – seems to be a novel issue, which has never been addressed in previous decisions.

. . . [T]he question whether the pagarés and hipotecas constitutes an investment pursuant to Art. 1139(g) and (b) NAFTA, or whether their status must be considered exclusively pursuant to Art. 1139(d) NAFTA, raises complex interpretative issues and requires a greater degree of consideration and a more thorough analysis of Mexican law and international legal principles. The Tribunal requires further legal argument on these issues within the context of the full development of the Parties’ cases.74

In a relatively recent decision of Eskosol SpA in liquidazione v. Italian Republic75 (Eskosol), the tribunal rejected the respondent’s (Italy’s) application under Rule 41(5). Italy presented four separate grounds for its application76 and the claimant, Eskosol SpA, argued that none of Italy’s objections satisfied the requirements of Rule 41(5), as they demanded ‘a significant factual enquiry’ and raised ‘novel and complex legal issues’.77 While the parties agreed that ‘in order to be manifestly without legal merit, the claims must be plainly without merit as a matter of law’, Italy used the additional formulation of ‘clearly and obviously’ to construe the word ‘manifest’, and Eskosol SpA referred to tribunal decisions to contend that the defect must be ‘obvious and plain’.78 The tribunal opined that ‘for the purposes of this case, there was no need to distinguish among the formulations of plain, clear and obvious, which all recognize that the manifest standard requires a very high degree of clarity, [such that], in the

73 PNGSDP at [94]–[98].
74 Lion Mexico at [79]–[81].
76 ‘(i) Eskosol cannot be considered a “national of another Contracting State” under Article 25(2)(b) of the ICSID Convention . . . (ii) Eskosol does not qualify as an “investor” either under the Energy Charter Treaty or the ICSID Convention . . . (iii) Under Article 26(3)(b)(i) of Annex 1D of the Energy Charter Treaty, Italy declined to consent to arbitration of a dispute previously submitted to another forum; (iv) The claim is barred by the principles of lis pendens and res judicata or collateral estoppel.’ Eskosol at [43].
77 Eskosol at [42].
78 The claimant inter alia relied on Trans-Global, Global Trading, Brandes, Elsamex, RSM Production, Álvarez and PNGSDP, Eskosol at [37].
view of the tribunal, the claims presented cannot succeed as a matter of law. The tribunal concluded that as the issues involved were not ‘manifest’, but ‘novel and complex’, they were unsuitable for a resolution in Rule 41(5) application.

These explications of the test of manifest lack of legal merit should not be confused with the *prima facie* test that is used for preliminary objections to jurisdiction under Arbitration Rule 41(1), which is less strict:

> The *prima facie* test . . . requires the arbitral tribunal to undertake a full evidentiary inquiry into genuine jurisdictional matters but allows a *prima facie* assessment not only of the alleged facts but also of the legal standards applicable to determine a violation of the BIT on the merits. Contrary to this, a preliminary objection under Arbitration Rule 41(5) must be directed either at jurisdiction or at the merits and allows neither for an evidentiary inquiry nor for the arbitral tribunal to undertake a *prima facie* assessment of legal standards. Instead, the arbitral tribunal has to be absolutely certain about the applicable legal standard in order to find that a claim is manifestly without legal merit. If the tribunal is in doubt, the preliminary objection will be rejected and the proceeding will continue.

> **v Addressing disputed facts**

The applicable standard of review for making a finding that a claim is ‘manifestly’ without legal merit must also be distinguished from the question of what standard an ICSID tribunal should apply in addressing facts asserted by a claimant. As seen above, the threshold for the former inquiry is necessarily very high (manifest). Conversely, a very low bar is set for the latter inquiry:

> At the first level of inquiry, the Tribunal should accept pro tem the facts as alleged by the claimant, to assess whether, on the basis of the claimed set of facts . . . there might be a violation of the relevant obligation. At the second level of inquiry, the Tribunal must make a definitive finding that the claims are “manifestly without legal merit”. It is on this second question that the four Tribunals are in complete agreement that the bar is “high”.

The word ‘legal’ (in ‘without legal merit’) was specifically introduced into the final text of Rule 41(5) to avoid improper discussions on the facts of the case at the Rule 41(5) stage, and ICSID tribunals have therefore been careful to emphasise that objections should be based on legal impediments to claims (and not factual ones, which a tribunal may not be in a position to decide in a preliminary manner). Tribunals would therefore refuse to entertain factual evidence or weigh the credibility or plausibility of a disputed factual allegation at the

79 Eskoöl at [37].
80 Eskoöl at [98].
81 Eskoöl at [120]; [169]; [171].
85 Antonietti-2007, page 440; Diop-2010, pages 325–326; Lion Mexico at [68]–[70].
86 Trans-Global at [97]; Brandes at [59]; PNGSDP at [90].
87 Schreuer, page 543; Trans-Global at [91].

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Objections of Manifest Lack of Legal Merit of Claims: Arbitration Rule 41(5)

Rule 41(5) stage; 88 ‘basically the factual premise has to be taken as alleged by the Claimant. Only if on the best approach for the Claimant, its case is manifestly without legal merit, it should be summarily dismissed.’ 89

Notwithstanding this, tribunals (e.g., those in Trans-Global and RSM Production) seem prepared to make a ‘plausibility exception’ 90 to the rule that the facts alleged by the claimant should be taken at face value if disputed facts that are relevant to the legal merits of the claim are regarded as manifestly incredible, frivolous, vexatious or inaccurate, or made in bad faith. 91

V CONCLUSION

After more than 10 years of Rule 41(5), one looks back and notes with some relief that initial concerns that the Rule would be prone to abuse by respondent states – who can delay proceedings and increase costs by invoking without basis an ‘additional procedural layer’ 92 – have not eventuated. To date, only 27 Rule 41(5) applications have been filed, representing a fraction of ICSID’s caseload. 93 The high threshold set and consistent approach to such applications, as well as potential costs consequences for unmeritorious invocations of Rule 41(5) 94 has likely served as an important deterrent against trigger-happy behaviour in this respect. The built-in short timelines in Rule 41(5) have also ensured that applications have generally been swiftly disposed of, and guard against any abuse of the process as a delay tactic. Given the positive experience with Rule 41(5) thus far, this is certainly a feature of

88 Trans-Global at [105].
89 Brandes at [61].
90 Markert-2011, page 147.
91 Trans-Global at [105]; RSM Production at [6.1.2]; Emnis International at [26].
92 Schreuer, page 544.
93 Based on information obtained from the ICSID website https://icsid.worldbank.org/en/Pages/Process/Decisions-on-Manifest-Lack-of-Legal-Merit.aspx (last visited on 11 February 2019) and the unreported decision in African Petroleum Gambia Limited and APLC Gambia B.V. v. Republic of The Gambia, ICSID Case No. ARB/17/38, which has yet to be reflected on the former page but is reflected in the ICSID website’s Case Details page https://icsid.worldbank.org/en/Pages/cases/casedetail.aspx?CaseNo=ARB%2f17%2f38 (last visited 11 February 2019). See also Le Cannu, ‘Foundation and Innovation: The Participation of African States in the ICSID Dispute Resolution System’ (2018) 33(2) ICSID Review 456, page 486, where it is estimated that around 1 per cent of all arbitration proceedings under the ICSID Convention and Additional Facility Rules have resulted in an award deciding claims are manifestly without legal merit.
94 Although tribunals in the earlier cases had exercised caution in the allocation of costs (given the newness of Rule 41(5)), a more robust approach to costs may be expected by tribunals moving forward as parties gain familiarity with the scope and aims of the Rule 41(5) procedure. This was so in Ansung Housing, where the tribunal noted (at [162]) that ‘the Rule 41(5) procedure is no longer new and . . . the Claimant’s limitations arguments were not reasonable’, and awarded the successful Rule 41(5) applicant (China), inter alia, 75 per cent of its legal fees and expenses. Going forward, one can also expect the same robust approach to be adopted against parties mounting unmeritorious applications. In the recent Eskosol case, the tribunal, vide Procedural Order No. 3, Decision on Respondent’s Request for Provisional Measures, dated 12 April 2017, denied Italy’s request for provisional measures, which included an order for security for costs for the Rule 41(5) application. Noting that requests for measures regarding security for costs are not ipso facto beyond the scope of a tribunal’s powers at [31], the tribunal undertook a proportionality analysis, and held that ‘Italy had not demonstrated that it was either necessary or urgent that Eskosol S.p.A. post security of $250,000 for a potential costs award in Italy’s favour’ at [36]–[39].
the ICSID Arbitration Rules that is worth retaining. The success of Rule 41(5) is evident from the move by the Singapore International Arbitration Centre to include a similar explicit provision in their rules,95 and it will be interesting to see whether other arbitral institutions follow suit. That has since materialised, as demonstrated by the growing trend among other major arbitral institutions to do the same.96 In the Working Paper published by ICSID on 3 August 2018 on the proposed amendments to the ICSID Arbitration Rules, ICSID has proposed the retention of Rule 41(5) (in the form of proposed Rule 35 which expressly recognises that this covers objections to jurisdiction as well as merits),97 which is yet another affirmation of the success of the rule.

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96 See footnote 6.

Chapter 7

INVESTMENT ARBITRATION AND PARALLEL PROCEEDINGS

Sae Youn Kim and Tae Joon Ahn

I INTRODUCTION

The rapid increase in cross-border transactions in recent decades has naturally given rise to a spike in various types of international disputes involving numerous subjects and parties of different nationalities all over the world. Consequently, when facing such international disputes, the concerned parties are no longer limited to seeking to resolve them via a traditional litigation at a domestic court. Rather, now disputing parties usually have the luxury of choosing one of several options at their disposal. The rise in prominence of international arbitration, both commercial and investment, as well as international organisations such as the World Trade Organization (WTO) have certainly contributed to this development. Complications arise, however, where the parties have a disagreement over where to take the dispute to begin with.

For instance, in an investment arbitration case under a bilateral investment treaty (BIT), one party might opt to go ahead and initiate a litigation in front of a national court even though an arbitration case is already in progress. This would be a classic example of a parallel proceeding in international arbitration. In this example, it is entirely possible that the national court hearing the second proceeding might decline to exercise jurisdiction based on the specific wording of the arbitration clause between the parties. That may not always happen, however, and if so the end result would be that the parties would suddenly be facing parallel proceedings. To further complicate matters, a domestic court is not the only forum with which an arbitral tribunal might find overlapping jurisdiction. Instead, a tribunal could easily find overlapping jurisdiction with another arbitral tribunal or even international courts.

While it always has been and remains quite common to see issues arising from overlapping jurisdiction in domestic settings, in international law this is an emerging and new issue. Nevertheless, it seems obvious that its importance will only increase and indeed, parallel proceedings are becoming more and more common in practice. Parallel proceedings are naturally problematic as well as burdensome to the concerned parties for a number of reasons. Even besides the fact that they require additional costs and time, the existence

1 Sae Youn Kim and Tae Joon Ahn are partners at Yulchon LLC.
2 David W Rivkin, ‘The Impact of Parallel and Successive Proceedings on the Enforcement of Arbitral Awards’ in Julian D M Lew and Bernardo M Cremades Roman (eds), Parallel State and Arbitral Procedures in International Arbitration (International Chamber of Commerce 2005) 269 (‘supranational institutions, treaty-based tribunals, arbitral institutions and commissions, and ad hoc tribunals’).
4 Rivkin (n 2) 269.
of conflicting awards could cause serious issues at the enforcement stage and encourage forum-shopping. For that reason, as we will see, critics and arbitrators have crafted a number of sophisticated – albeit insufficient – mechanisms to deal with them.

In the following, we will delve into some of the basics surrounding parallel proceedings in international arbitration such as the concept, some of the problems they pose and solutions that arbitral tribunals have adopted to address such problems.

II WHAT ARE PARALLEL PROCEEDINGS?

i Definition and types of parallel proceedings

Before delving any further, it would first be necessary to define the term ‘parallel proceedings’. There is no general definition of parallel proceedings, but as a guideline, the International Law Association defines the term ‘concurrent proceedings’ as ‘proceedings pending before a domestic court or another arbitral tribunal, in which the parties and one or more of the issues are the same or substantially the same as the ones before the arbitral tribunal in the Current Arbitration.’ This is a noticeably broad definition and to somewhat narrow it down, the proceedings must ‘address the same claims, demand or cause of action between the same parties.’ Needless to say, two proceedings are not deemed parallel or concurrent just because the involved parties are identical or they originate from the same transaction. In contrast, the proceedings must be essentially identical but simply filed in front of two separate courts, tribunals or some other institutions with adjudicative authority.

Parallel proceedings are most common between an arbitral tribunal and a domestic court, as one might expect. However, they can easily take other forms as well. For example, an investor might file a claim under a relevant BIT or in front of a domestic court while simultaneously encouraging the state of its nationality to file a WTO claim against the respondent state. While this example does not technically fit into the definition stated above since the involved parties are not identical, there is no denying that international court proceedings such as WTO proceedings can also be pursued in parallel with arbitral proceedings. In this context, parallel proceedings can arise between courts and arbitral tribunals, regardless of whether the courts are international or domestic.

As the number of channels that parties may take in resolving international disputes has risen, it is only logical that potential areas where different forums might clash over their respective jurisdiction have increased as well. For the purposes of this paper, however, we

7 Erk-Kubat (n 5) 25.
11 ibid., 44–50.
will briefly touch upon and discuss issues arising from the following two types of parallel proceedings: (1) those between a domestic court and an arbitral tribunal; and (2) those between two different arbitral tribunals.

ii What are some of the causes of parallel proceedings?

One of the causes of parallel proceedings in international arbitration is the doctrine of competence-competence, as it empowers the arbitral tribunal with the authority to decide its own jurisdiction.13 In that sense, while an arbitral tribunal’s decision on jurisdiction is not final and may be reviewed by domestic courts, the arbitral tribunal nonetheless has priority over other adjudicative bodies on whether or not it has the requisite jurisdiction over a claim.14 This in particular creates room for conflict with local courts, as the scope of the competence-competence rule and the involvement of domestic courts can vary depending on the jurisdiction.15 Under the competence-competence doctrine, both domestic courts and arbitral tribunals could independently decide to exercise jurisdiction over the same case without being affected by one another in any way.16 This problem is further exacerbated by the fact that arbitrators are more likely to find jurisdiction than local court judges since they receive monetary compensation for hearing a dispute.17 Given that tendency, it seems perfectly reasonable that whereas a judge might decline to exercise jurisdiction over a certain case owing to potentially overlapping jurisdictions, an arbitrator might very likely find otherwise.

Specifically for investment arbitrations, another possible cause of parallel proceedings is the inclusion of an umbrella clause in the relevant BIT. Umbrella clauses can be phrased in a number of ways in a BIT,18 but regardless of the specific wording, they attempt to extend the scope of the BIT beyond disputes under the BIT itself. These unique provisions are called umbrella clauses because ‘they put contractual commitments under the BIT’s protective umbrella’.19 Thus, by utilising an umbrella clause, an investor might initiate an investment arbitration while simultaneously carrying out a contractual claim in a different forum. To put it differently, where applicable, an investor could bring an investment treaty claim against the state as well as a breach of contract claim in front of a domestic court at the same time. Consequently, there would be two proceedings involving the same parties and the same set of facts pending at two different forums. Umbrella clauses are expectedly controversial and the source of much confusion and uncertainty. For their part, ICSID tribunals have rendered inconsistent rulings on the line dividing contract and treaty claims.20

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13 Forsten (n 9) 36.
15 ibid., 218–230.
16 Erk-Kubat (n 5) 2 (‘competence-competence may, by authorising the arbitral tribunal to decide on its own jurisdiction, lead to jurisdictional conflicts of competence where national courts and arbitral tribunals both declare themselves competent to hear a case’).
18 Yannaca-Small (n 8) 1032.
Finally, parallel proceedings can be intentionally initiated by the actual parties to the dispute themselves.\textsuperscript{21} For example, a party might commence a parallel proceeding as a tactical decision to delay the proceedings, or a party might do so as a precautionary measure.\textsuperscript{22} This is because, depending on the applicable national legislations, ‘there is room for playing with parallel proceedings that can really make a difference on the outcome of the case.’\textsuperscript{23} In the worst case, parties can take advantage of parallel proceedings to take the fight to a forum more favourable to it or even just to cause annoyance and worsen the burden on the opposing party.\textsuperscript{24} Whether such behaviour is ethical is an entirely different issue, but at the very least most would agree that it cannot be encouraged.

\section*{III ISSUES WITH PARALLEL PROCEEDINGS}

\subsection*{i General issues}
Parallel proceedings are the source of a number of complications in international arbitration. For instance, they may cause delays, increase costs, potentially be an abuse of process, encourage forum shopping or lead to conflicting results.\textsuperscript{25} Among these, the biggest concern might very well be the last one.\textsuperscript{26} On first thought, it is natural that parties would prefer to avoid parallel proceedings since they would be forced to spend additional time and effort over the same dispute and set of facts. Having to litigate the same cause of action twice would undermine some of the notable advantages of international arbitration, such as the speed of the proceedings and relatively lower expenses, after all. Parallel proceedings also run the risk of being characterised as an abuse of process, depending on the facts and circumstances of the particular dispute. Interestingly, another potential issue is that an ongoing domestic proceeding, as court proceedings are generally open and public, could result in the loss of confidentiality, thereby stripping the arbitration of another one of its principal advantages.\textsuperscript{27}

These particular problems are complications that arise from the existence of a parallel proceeding in a different forum. This means that they are unnecessary and should be avoided if possible. As we will see below, however, these issues are at most a procedural inconvenience compared with the grave implications and potential impact of forum shopping and conflicting results.

\subsection*{ii Conflicting results and forum shopping}
Conflicting results and forum shopping are undoubtedly two of the most significant drawbacks to parallel proceedings that strike at the heart of both commercial and investment international arbitrations. Starting with the former, for one thing the mere existence of a conflicting arbitration award can raise questions about its enforceability under the New York

\begin{itemize}
\item \textsuperscript{21} Erk-Kubat (n 5) 11–13.
\item \textsuperscript{22} ibid., 12.
\item \textsuperscript{23} Emmanuel Gaillard and Philippe Pinsolle, ‘Advocacy in Practice: The Use of Parallel Proceedings’ in R. Doak Bishop and others (eds), \textit{The Art of Advocacy in International Arbitration} (Juris Net 2010) 174.
\item \textsuperscript{25} Rivkin (n 2) 271.
\item \textsuperscript{26} Pauwelyn and Salles (n 3) 83.
\item \textsuperscript{27} Forsten (n 9) 37–38.
\end{itemize}
This is especially the case since domestic courts and arbitral tribunals may very well apply different substantive laws. Even worse, where there are two conflicting decisions, the enforcement of one might result in a violation of the other, which would put the party seeking enforcement in a difficult position. Most importantly, however, inconsistent rulings might leave the dispute unresolved while simultaneously threatening the stability and legitimacy of the system of the tribunal itself.

One notable set of proceedings in which this became an issue was the conflicting results between *Lauder v. Czech Republic* and *CME v. Czech Republic*. A total of four principal proceedings ensued from a series of events, including the above-mentioned two investment arbitrations under the US–Czech Republic BIT and the Netherlands–Czech Republic BIT, respectively. The tribunals in these two investment arbitration cases rendered conflicting decisions, and needless to say, the reaction to these conflicting awards was largely negative. For example, some have even gone as far as labelling the outcome of these parallel proceedings a 'debacle'.

Furthermore, the fact that different tribunals or courts could render conflicting results creates an incentive for parties to entertain the idea of forum shopping, which is a new phenomenon among international tribunals. Even though there may be no clear answer as to whether forum shopping in international arbitration is clearly negative, there can be little doubt that greater stability and predictability would be beneficial for the investment arbitration system in general. Forum shopping hurts the investment arbitration system in that respect since it is based on the premise that different forums could very well lead to different outcomes regarding the same dispute. There are a number of other reasons why parties might use parallel proceedings for forum shopping among tribunals or courts, much like how they might do so under domestic law. Among other things, they might do so to take advantage of favourable procedural issues, such as interim measures or different discovery rules, or because of practical considerations such as geographical convenience. In essence, parties seek ‘home advantage’ by engaging in forum shopping. Ultimately, their intent would be to take their claim to the forum that would be most favourable for their interests.

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28 Rivkin (n 2) 271.
29 Forsten (n 9) 38.
30 ibid., 40.
31 Pauwelyn and Salles (n 3) 83.
33 For additional details on these cases, see Rivkin (n 2).
36 Pauwelyn and Salles (n 3) 78.
38 Erk-Kubat (n 5) 13-14.
39 Kreindler (n 37) 138.
iii Abuse of process and parallel proceedings

As Professor Gaillard once recognised, filing multiple arbitral proceedings can be characterised as a potential type of abuse of process. Indeed, respondent states in investment arbitration proceedings often raise the abuse of process challenge (or a similar good faith argument) when faced with the threat of having to defend the same interest against de facto same investors in more than one proceeding. This resistance by respondent states to the multiplication of arbitral proceedings inevitably leads to fierce controversy in the jurisdictional phase of investment arbitration proceedings. On this issue, an ICSID tribunal recently rendered a noteworthy award. In that case, the tribunal noted that ‘the four parallel arbitration[s] with, essentially, the same factual matrix, the same witnesses and many identical claims’ had been pursued. In spite of the ostensible multiple proceedings arising out of virtually ‘the same factual matrix’, however, the tribunal held that ‘none of the four arbitrations at issue here is, per se, an abuse.’ The tribunal nonetheless warned against double recovery of the same sum by a duplicative (overlapping) claimant. Furthermore, the tribunal noted that, in situations where claimants have pursued multiple proceedings because of their lack of confidence in the jurisdiction of the tribunals, it would be in the best interest of the claimants to withdraw the duplicative claims once a jurisdiction is confirmed so as to avoid the finding of an abuse of process. While this award did not squarely sever the correlation between parallel proceedings and abuse of process, it did make clear that the pursuit of multiple proceedings in itself would not automatically be deemed abusive, as long as the claimant has good reasons to pursue them on the basis of its right of recourse to treaty protection or arbitration clauses.

iv Conclusion

Given such convoluted issues and potentially negative implications of parallel proceedings, it seems obvious that judges and arbitrators have to be well versed in possible means of dealing with them. Despite the obvious need to develop mechanisms designed to prevent parallel proceedings, as we will see in the subsequent section, they have rather limited measures in terms of effectiveness at their disposal.

Now that we have identified the problems and issues caused by parallel proceedings, logically the next step will be discussing ways for arbitral tribunals to rectify them. The American Law Institute and the European Court of Justice have each attempted to address parallel proceedings, but it is apparent that there is no clear-cut answer available at this point. Still, arbitral tribunals can and have sought to resolve issues arising from parallel proceedings by adopting certain legal principles from domestic law and local courts. In the following, we will discuss some of the possible means through which arbitral tribunals could limit or prevent parallel proceedings from taking place or proceeding any further.

42 Ampal-American Israel Corporation and others v. Arab Republic of Egypt, ICSID Case No. ARB/12/11, Decision on Jurisdiction, 1 February 2016, para. 328.
43 ibid., para. 329.
44 ibid., para. 330.
45 ibid., 95.
46 Teitz (n 24) 4.
Investment Arbitration and Parallel Proceedings

IV POSIBLE SOLUTIONS

i Res judicata and lis pendens

First of all, arbitral tribunals can utilise the principles of res judicata and lis pendens, both of which are of course borrowed concepts from domestic law principles. Needless to say, res judicata and lis pendens are hardly the only means or legal principles applicable for addressing the matter of parallel proceedings. For example, as a general principle of international law, courts and tribunals may decline jurisdiction as a matter of comity. Nevertheless, res judicata and lis pendens are effective as ‘preclusion doctrines’ in that they ‘bar either the jurisdiction of a court or the plaintiff’s right to have her substantive claims examined’. In other words, where applicable, res judicata and lis pendens would require the court or tribunal in the second proceeding to decline jurisdiction.

Starting first with the principle of res judicata, it is applicable where another court or tribunal has already rendered a decision on the dispute, whereas lis pendens is applicable if the dispute is still pending. Widely known as ‘claim-preclusion’, res judicata blocks a party from seeking to relitigate a claim that has already been resolved in a final and conclusive manner. While not perfectly interchangeable with its domestic law counterpart, res judicata is a principle of international commercial arbitration. In the context of international arbitration, res judicata can be applied in a similar manner as in domestic law.

However, the utilisation of res judicata in parallel proceedings is bound to be limited, as it only applies to proceedings where the parties, the object or subject matter, and the cause of action are identical. More importantly, res judicata necessarily presupposes a final and conclusive judgment. Thus it would apply to subsequent proceedings but not to the situation where two or more proceedings are currently in progress. Even if there is a final judgment, it must be binding on the subsequent proceeding. Where a final judgment is deemed to be non-binding, tribunals have merely ‘acknowledged the “persuasiveness” of non-binding awards’. To make matters even more challenging, res judicata is only applicable to two proceedings in the same legal system. As such, it follows that res judicata cannot be applied to proceedings between different international tribunals. Logically, it cannot be applied to an international tribunal and a domestic court either for the same reason.

As for lis pendens, which is the method adopted by signatories to the Brussels I Regulation, in domestic law this particular doctrine bars a court from hearing a case that is

47 Rivkin (n 2) 292–295.
48 Forsten (n 9) 43 (‘[o]ther measures include, inter alia, anti-suit injunctions, consolidation of proceedings, and the application of the doctrine of forum non conveniens’).
49 Rivkin (n 2) 291.
50 Pauwelyn and Salles (n 3) 86.
51 ibid.
53 ibid., 103.
54 ibid., 90.
55 Pauwelyn and Salles (n 3) 104.
Investment Arbitration and Parallel Proceedings

‘already pending before another court in the same legal system’.\(^{57}\) In an investment arbitration setting, however, there is no indication that *lis pendens* must be limited to proceedings within the same legal system as well. Instead, it could be applied so that ‘the subject matter of the dispute may not be negotiated simultaneously before more than one tribunal.’\(^{58}\) Unlike *res judicata*, *lis pendens* is built to deal with proceedings that are occurring concurrently.\(^{59}\) Nevertheless, much like the case with *res judicata*, there is an ongoing debate over whether *lis pendens* is a principle of international law.\(^{60}\)

In addition, *lis pendens* is only applicable under extremely limited circumstances.\(^{61}\) Since it requires parallel proceedings to be taking place in the same legal system, it would not be applicable to overlapping jurisdictions between a domestic court and an arbitral tribunal.

Given the uncertainty over the role that *res judicata* and *lis pendens* might have in the domain of international law, it becomes clear that they are not fit or sufficient for dealing with the problems accompanying parallel provisions on their own. At most they could be expected to play a supplementary role where applicable.

### ii Consolidation of arbitrations/claims

Another possible solution to parallel proceedings is consolidating the arbitrations/claims, as a domestic court might do. By doing so, parallel proceedings can be consolidated into a single proceeding. In fact, consolidation of claims have been used in commercial arbitrations to deal with parallel proceedings.\(^{62}\) The International Chamber of Commerce (ICC), for example, prescribes in Article 10 of its Rules of Arbitration that the International Court of Arbitration of the ICC may consolidate two or more arbitrations in instances such as ‘where the claims in the arbitrations are made under more than one arbitration agreement, the arbitrations are between the same parties, the disputes in the arbitrations arise in connection with the same legal relationship, and the Court finds the arbitration agreements to be compatible.’\(^{63}\) For parallel proceedings, the prerequisite that the parties must be the same would be immediately satisfied, but one problem with this approach, at least in the case of the ICC, is that the concerned parallel proceedings must be taking place in the same legal system,\(^{64}\) which seems to be a recurring issue for mechanisms to deal with parallel proceedings. Thus, generally there are no means for a domestic court to consolidate claims made in an arbitral proceeding, and vice versa.

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\(^{57}\) Yannaca-Small (n 8) 1022.

\(^{58}\) Dimsey (n 52) 87.

\(^{59}\) Pauwelyn and Salles (n 2) 106.

\(^{60}\) ibid.

\(^{61}\) ibid., 110.


\(^{63}\) International Chamber of Commerce, Rules of Arbitration, Article 10(c); The Korean Commercial Arbitration Board also has a similar provision, Korean Commercial Arbitration Board, International Arbitration Rules, Article 23.

\(^{64}\) Article 10 specifies that the arbitrations must be pending under the ICC Rules of Arbitration, International Chamber of Commerce, Rules of Arbitration Article 10. As only the International Court of Arbitration may administer arbitrations under the ICC Rules of Arbitration as per Article 1, this means that the International Court of Arbitration can consolidate only ICC arbitrations, International Chamber of Commerce, Rules of Arbitration, Article 1.
Moreover, whereas domestic courts generally have broad jurisdiction, arbitral tribunals can only hear a claim upon agreement by the parties. As obvious as it may seem, a court must have the jurisdiction to do so in the first place to consolidate two or more proceedings into one. That being the case, since the boundaries of the jurisdiction of an arbitral tribunal are entirely set by the scope of the consent of the involved parties, the power of the tribunal to consolidate claims is naturally far more limited than that of a domestic court. It follows that consolidating claims between two or more parallel proceedings would be a viable option for arbitral tribunals only in limited circumstances.

iii Waiver provisions

Perhaps a more effective solution would be preventing parallel proceedings from arising in the first place. There are two simple ways of preventing parallel proceedings from arising at all, one of which is via a waiver provision. In fact, the simplest way of dealing with parallel proceedings might be including a waiver provision as part of a BIT. In order to comply with a waiver provision, the investor would have to submit a written waiver foregoing any other dispute settlement procedure prior to filing an arbitration. That way, the investor is precluded from seeking an alternative dispute settlement procedure for the same claim under the BIT. Indeed, investment treaties can explicitly include provisions requiring claimants to refrain from initiating parallel proceedings, and many recent investment treaties in fact do include such provisions. For example, Article 8(6) of the Mexico–Korea BIT provides as follows:

*A disputing investor may submit a claim to arbitration only if he consents to arbitration in accordance with the procedures set out in the Agreement and waives his right to initiate before any administrative tribunal or court under the law of the Contracting Party, or other dispute settlement procedures, and any proceedings with respect to the measure of the disputing Contracting Party that is alleged to be a breach of this Agreement.*

A waiver can be explicit or implicit, and by submitting a written waiver the investor relinquishes its right, claim, or privilege. When there is a waiver clause, by choosing to arbitrate, the investor foregoes its right to take the dispute to another forum. It seeks to directly prevent the negative effects of parallel proceedings such as the respondent state being forced to litigate multiple proceedings as well as the risk of double recovery and inconsistent findings of fact and law. Any attempt to initiate a parallel proceeding in spite of a valid waiver provision would by definition violate it and lead to the relevant arbitral tribunal declining jurisdiction.

However, there are shortcomings with this approach as well. Most notably, in order to be effective, the waiver provision must be worded carefully and precisely. Thus the drafters

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65 Pauwelyn and Salles (n 3) 87 (‘[b]oth consolidation and joinder presume that the court deciding the case has jurisdiction to do so in respect to all aspects and parties to the dispute’).


68 *The Renco Group Inc v. The Republic of Peru*, ICSID Case No. UNCT/13/1, Partial Award on Jurisdiction, 15 July 2016, para. 84.
of a BIT must exercise caution to increase the likelihood that an arbitral tribunal would find a waiver provision valid. This is more difficult than it may seem because a waiver provision has a formal as well as a material component.\(^69\) The formal requirement is that the investor must submit a written waiver that complies with the terms of the treaty.\(^70\) As for the material component, however, the investor must refrain from ‘initiating or continuing proceedings in a domestic court’.\(^71\) Even if the investor satisfies the formal component, a tribunal will decline to exercise jurisdiction if the second prong is not met. This can be seen in the first proceeding of Waste Management Inc v. United Mexican States and the partial award on jurisdiction in Renco Group v. Peru.\(^72\)

Starting with Waste Management, the claimant submitted a written waiver as required by Article 1121, but simultaneously pursued two domestic proceedings against a Mexican state bank along with another arbitration against a municipal government.\(^73\) Based on these facts, the arbitral tribunal held that as the claimant was not planning to terminate the domestic proceedings, its actions contradicted the intent behind Article 1121.\(^74\) For that reason, the arbitral tribunal could not exercise jurisdiction. This was even though the claimant’s waiver had satisfied the formal requirement.\(^75\)

Turning to Renco Group v. Peru, which was an ICSID case under the Peru–United States Trade Promotion Agreement (the Treaty), the tribunal had to determine whether it had jurisdiction in light of the claimant’s notice of arbitration that was accompanied by a waiver. Article 10.18(2)(b) of the Treaty required an investor to first submit a written waiver prior to initiating a claim under the Treaty before an administrative tribunal, court or some other dispute settlement body. However, in its waiver the claimant had stated that it reserved the right to bring claims in another forum if the tribunal declined to hear it on jurisdictional and admissibility ground.\(^76\) In the partial award decision on jurisdiction, a split tribunal held that the reservation of rights was in breach of Article 10.18(2)(b) of the Treaty.\(^77\)

As a second line of defence, the claimant in this case argued that it would still be able to ‘cure’ the defective waiver. The tribunal disagreed, however, by holding that ‘[c]ompliance with both elements is a precondition to Peru’s consent to arbitrate and to the existence of a valid arbitration agreement’.\(^78\) Since there was no arbitration agreement in the first place, the tribunal could not exercise jurisdiction to hear the claim.

Therefore, it is evident that a waiver provision does not invariably prevent parallel proceedings from arising. As discussed above, there are several hurdles one party must overcome in order to prevent parallel proceedings through the use of a waiver provision.

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\(^{69}\) ibid., para. 73.

\(^{70}\) ibid., para. 60.

\(^{71}\) ibid., para. 142.

\(^{72}\) ICSID Case No. ARB(AF)/98/2, Arbitral Award, 2 June 2000, 236–238; Renco (n 68).


\(^{74}\) Waste Management (n 66) 236–238; Renco (n 68).

\(^{75}\) Dodge (n 73) 63.

\(^{76}\) Renco (n 68) para. 58.

\(^{77}\) ibid., para. 119.

\(^{78}\) ibid., para. 135.
iv  Fork-in-the-road clauses

A similar but perhaps more effective recourse for dealing with parallel proceedings is by inserting a fork-in-the-road clause in BITs or commercial contracts. Generally, a fork-in-the-road clause requires the investor to ‘choose between the litigation of its claims in the host State’s domestic courts or international arbitration and that, once made, the choice is final’. That is, once an investor has made its choice, it is irrevocable. The choice does not necessarily only have to be between two options, as a fork-in-the-road clause may offer the investor several different options instead. Although they may seem eerily similar at first thought, a fork-in-the-road clause can be distinguished from a waiver provision in that the latter requires the investor to refrain from turning to a domestic court prior to filing an arbitration by submitting a written waiver, whereas the former allows the investor to choose between a domestic proceeding and an investment arbitration.

To reiterate, the difference is that a waiver requirement in a BIT, on one hand, forces the investor to choose arbitration as the only dispute settlement procedure. A fork-in-the-road clause, on the other hand, allows the investor to choose arbitration among two or more options. In that sense, it offers greater freedom and flexibility to the investor. Some have also suggested that a waiver provision, unlike a fork-in-the-road clause, encourages the investor to consider the option of utilising domestic remedies before filing an arbitration claim. Ideally, however, the end result would be identical in that either method would lead to the preclusion of parallel proceedings. Moreover, regarding the investor’s choice between a domestic court or international arbitration, the tribunal in *OEPC v. Republic of Ecuador*, which was an investment arbitration under the US–Ecuador BIT, has held that the choice must have been free and not under any duress. Another caveat to this approach is that the tribunal must still determine whether the claimant’s appearance in front of a domestic court suffices as its choice under the fork-in-the-road clause.

Overall, a tribunal relies on the following three-prong test to determine whether an investor has exercised its right under the fork-in-the-road clause: (1) whether the domestic proceeding was instituted before the arbitration was chosen, (2) whether the dispute between the parties is identical in both proceedings and (3) whether the parties are also identical. Despite this general framework, ultimately a tribunal evaluates each fork-in-the-road clause on a case-by-case basis. As a result, there is no consistent jurisprudence on how to interpret a fork-in-the-road clause.

Therefore, much like the situation with waiver provisions, the mere inclusion of a fork-in-the-road clause does not automatically give effect to it. Rather, the parties must exercise in drafting it and also in their attempts to utilise it.

79 Schreuer (n 19) 239.
81 Kreindler (n 37) 148.
82 Rivkin (n 2) 286.
84 *Occidental Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467, 1 July 2004.
85 Rivkin (n 2) 289.
86 Schreuer (n 19) 241.
87 ibid., 248.
88 Rivkin (n 2) 288.
v Conclusion

As a whole, the analysis above proves that each of the techniques currently available has its own drawbacks and, if invoked alone, is not sufficient to address the problems caused by parallel proceedings. Instead, arbitral tribunals must have regard to some or a combination of these options where applicable. What is more, with regard to waiver or fork-in-the-road clauses in BITs, parties should elaborate on drafting treaty language and structure to preclude parallel proceedings, which is expected to result in predictability for parties and clarity for arbitral tribunals.

V CONCLUSION

Cross-border transactions and investments have become an essential and inevitable component of today's world economy. For example, the number of arbitration cases administered by the world’s major commercial arbitration institutions continues to increase each year. At the same time, investment arbitrations are becoming more and more common as well. Invariably, this means that the potential room for conflict resulting from parallel proceedings in the realm of international arbitration is growing as well. Therefore, any actor in the world of international arbitration – both commercial and investment – must keep an eye out on the issue of parallel proceedings. While there are a number ways to alleviate some of the problems arising from parallel proceedings, as discussed above, there are still inherent limitations and glaring weaknesses with each of those methods. Furthermore, despite the danger they pose, discussions regarding parallel proceedings in international arbitration are somewhat scarce and inadequate.

Ultimately, given the magnitude of the problems they pose and the lack of clear solutions or in-depth discussions, there can be little doubt that the issue of parallel proceedings warrant greater attention by the international arbitration community in the future. Left alone, parallel proceedings can eventually lead to ‘fragmentation and unpredictability’. After all, by increasing the burden on the parties and frustrating their attempts to enforce arbitral awards, parallel proceedings are bound to have a negative impact on the role of international arbitration as a dispute settlement mechanism. While our recommendation is that careful drafting of waivers and fork-in-the-road clauses are relatively superior to the other solutions, in order to appropriately remedy such problems caused by parallel proceedings, a consistent jurisprudence will be necessary. To achieve this objective, as a start arbitral tribunals will have to accept the gravity of the issues originating from parallel proceedings.

91 Erk-Kubat (n 5) 1.
92 Teitz (n 24) 70.
I  INTRODUCTION
Remarkably little has been written on evidence and proof in the specific context of investment arbitration. This is not because evidence plays a different or even smaller role in investment arbitration than in commercial arbitration, but rather because there are no major differences in the collection of evidence in investment arbitration. In fact, when the IBA Rules on the Taking of Evidence in International Commercial Arbitration of 1999 were revised in 2008, their title was changed to the IBA Rules on the Taking of Evidence in International Arbitration.2

The same applies with regard to the burden of proof. However, the specificities of investment arbitration, with claimants asking for compensation for expropriation and – given the involvement of state parties – a higher incidence of allegations of corruption, have led several tribunals to specifically address the degree of burden of proof in such circumstances.

II  EVIDENCE
i  Statutory provisions and institutional rules
It is generally accepted that, in international arbitrations, tribunals enjoy broad discretion as to evidentiary matters. Strict evidentiary rules typical for domestic evidential systems apply just as little to international arbitrations as domestic procedural rules.

The discretion of arbitrators is expressly provided for in the various national arbitration laws (lex arbitri) and many institutional arbitration rules. Article 19 of the UNCITRAL Model Law on International Commercial Arbitration provides for the ‘Determination of rules of procedure’ as follows:

(1) Subject to the provisions of this Law, the Parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.
(2) Failing such agreement, the arbitral tribunal may, subject to the provision of this Law, conduct the arbitration in such manner as it considers appropriate. The power conferred upon the arbitral tribunal includes the power to determine the admissibility, relevance, materiality, and weight of any evidence.

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1 Martin Wiebecke is an attorney-at-law at Anwaltsbüro Wiebecke.
2 IBA Rules on the Taking of Evidence in International Arbitration of 29 May 2010.
However, many national legislators that do not follow the UNCITRAL Model Law have also made similar provisions, such as Sections 34(1) and (2)(f) of the English Arbitration Act of 1996:

Procedural and evidential matters.

(1) It shall be for the tribunal to decide all procedural and evidential matters, subject to the right of the parties to agree any matter.

(2) Procedural and evidential matters include—

(f) whether to apply strict rules of evidence (or any other rules) as to the admissibility, relevance or weight of any material (oral, written or other) sought to be tendered on any matters of fact or opinion, and the time, manner and form in which such material should be exchanged and presented.

This view is also confirmed by court decisions, in particular in the United States, where courts have repeatedly emphasised the broad discretion of arbitrators in matters of evidence, even in contradiction to domestic evidential rules such as the exclusion of hearsay evidence.3

Subject to the provisions on evidence in the lex arbitri, the parties may, of course, agree on the evidentiary rules to be applied in their arbitration. This is mostly done with reference to the arbitration rules of an arbitration institution, but it is also possible to agree evidentiary rules in the arbitration clause or, once the dispute has arisen, in the context of establishing procedural orders or terms of reference.

Article 27 of the UNCITRAL Arbitration Rules 2013 on ‘Evidence’ provides, inter alia, as follows:

1. Each party shall have the burden of proving the facts relied on to support its claim or defence.

2. Witnesses, including expert witnesses, who are presented by the parties to testify to the arbitral tribunal on any issue of fact or expertise may be any individual, notwithstanding that the individual is a party to the arbitration or in any way related to a party.

4. The arbitral tribunal shall determine the admissibility, relevance, materiality and weight of the evidence offered.

The provisions in Article 25 of the International Chamber of Commerce Rules are more extensive in describing the collection of evidence, but do not mention issues related to its valuation:

Article 25: Establishing the Facts of the Case

1. The arbitral tribunal shall proceed within as short a time as possible to establish the facts of the case by all appropriate means.

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2 After studying the written submissions of the parties and all documents relied upon, the arbitral tribunal shall hear the parties together in person if any of them so requests or, failing such a request, it may of its own motion decide to hear them.

3 The arbitral tribunal may decide to hear witnesses, experts appointed by the parties or any other person, in the presence of the parties, or in their absence provided they have been duly summoned.

4 The arbitral tribunal, after having consulted the parties, may appoint one or more experts, define their terms of reference and receive their reports. At the request of a party, the parties shall be given the opportunity to question at a hearing any such expert.

5 At any time during the proceedings, the arbitral tribunal may summon any party to provide additional evidence.

6 The arbitral tribunal may decide the case solely on the documents submitted by the parties unless any of the parties requests a hearing.

The ICSID Rules of Procedure for Arbitration Proceedings contain more detailed provisions on evidence. After Rule 33 on Marshalling of Evidence, Rule 34 provides for General Principles. Its first paragraph states: ‘The Tribunal shall be the judge of the admissibility of any evidence adduced and of its probative value.’

The provisions in Rule 34(2) give tribunals the power to call upon the parties to produce documents, witnesses and experts, and to visit any place connected with the dispute or conduct inquiries there, at any stage of the proceedings.4 Rule 34(3) obliges the parties to cooperate with the tribunal. Rule 35 addresses the examination of witnesses and experts, with some special rules related thereto in Rule 36. Finally, Rule 37 provides, inter alia, details for visits and inquiries.

Although specific evidentiary rules in arbitration clauses are rare, agreeing to evidentiary or procedural rules with a substantial impact on evidentiary matters and questions is very common when tribunals submit to the parties drafts of specific procedural rules, constitution orders and terms of reference. These documents often contain a reference – of higher or lower obligation on the part of the tribunal – to adhere to the IBA Rules on the Taking of Evidence in International Arbitration (the IBA Rules of Evidence).

ii Admissibility of evidence

Whether with an explicit reference, for example, in an arbitration clause (rare), or within specific procedural rules or terms of reference (more common), the parties are often (indirectly) agreeing on the application of the evidentiary rules contained in the IBA Rules of Evidence. Article 9(1) thereof on ‘Admissibility and Assessment of Evidence’ is worded almost identically to Article 27(4) of the UNCITRAL Arbitration Rules: ‘The Arbitral Tribunal shall determine the admissibility, relevance, materiality and weight of evidence.’

However, it is generally accepted that, even without any statutory provision or private agreement by the parties, be it on the application of arbitration rules, the IBA Rules of Evidence, or in an arbitration clause or subsequent procedural agreement, tribunals have the implied authority to resolve issues of admissibility, relevance and evaluation of evidence.5

Again, national rules on the admissibility of evidence, such as the exclusion of hearsay or the rule that corporate officers may not testify for their company, are not applicable in

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4 Rule 34(2) has largely the same content as Article 43 of the ICSID Convention.
Evidence and Proof

international arbitration. Nevertheless, arbitral tribunals may limit the evidence, though they are rather reluctant to do so in practice. They sometimes do so with regard to the testimony of witnesses and experts at evidentiary hearings. In this respect, Article 8(2) of the IBA Rules of Evidence provides as follows:

The Arbitral Tribunal may limit or exclude any question to, answer by or appearance of a witness, if it considers such question, answer or appearance to be irrelevant, immaterial, unreasonably burdensome, duplicative or otherwise covered by a reason for objection set forth in Article 9.2.

Article 9(2) of the IBA Rules of Evidence gives tribunals, not only at the request of a party, but also on their own motion, the power to exclude from evidence or production documents statements, oral testimony or inspection for reasons such as the lack of sufficient relevance to the case or materiality to its outcome; legal impediment or privilege; unreasonable burden to produce; compelling commercial or technical confidentiality; or even for compelling grounds of special political or institutional sensitivity.

However, even if arbitral tribunals have the right to exclude evidence under these circumstances, they are hesitant to do so in practice – and even more so in investment treaty arbitration. Reasons for this include avoiding the need to exclude evidence that could possibly prejudice a party’s right to present its case, with no possibility of appeal on substantive grounds, but also to avoid the impression that the tribunal is escaping difficult decisions, in particular in highly political matters.6 For these reasons, arbitral tribunals generally admit evidence rather freely, disregard technical rules of admissibility of evidence – in particular, those known in common law – and focus on assessing the weight of the evidence (i.e., its probative value).

iii Probative value

Given that admissibility criteria are not often used to exclude evidence, the weighing of evidence by tribunals becomes more important. Most arbitrators consider contemporaneous documents to be the best form of evidence. Witness testimony, unless it has been tested in cross-examination or by an examination of the arbitrators themselves, is usually given less weight. Direct (primary) evidence is usually considered to be more reliable and thus to have more weight than indirect (secondary) or circumstantial evidence. However, a tribunal will look at the reasons why it is impossible for a party to produce direct evidence. Documents may have been lost or destroyed due to armed conflicts or civil unrest.7 In such cases, tribunals will rely on presumptions or inferences, and consider facts proven on the basis of other proven facts or factual knowledge, a series of facts linked together or accepted factual knowledge, such as in the Corfu Channel case of the International Court of Justice.8 However, a presumption or inference may shift the burden of proof to the other party.

Tribunals may also draw negative inferences from a party’s procedural conduct, such as not producing documents that should be in its possession or witnesses under its control.

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6 Born, op. cit., page 2,311.
7 See also Article 9(2)(d) of the IBA Rules of Evidence.
However, it is difficult to draw negative inferences in practice, mostly because it is not clear what the inference must actually be. Arbitrators, therefore, usually avoid such situations, particularly in view of the fact that *non liquet* decisions are not customary in arbitration.9

**III PROOF**

i Burden of proof

Unlike for the taking of evidence, few provisions on the burden of proof in arbitration exist. Usually, the *lex arbitri* does not contain any, and only a few arbitral rules mention it, such as Section 27(1) of the UNCITRAL Arbitration Rules, which states that each party shall have the burden of proving the facts relied on to support its claim or defence. This is the general rule in international arbitration, in addition to the burden of proving factual assertions and assertions that have been contested by the other side.

In civil law systems, the burden of proof is considered to be a question of the applicable substantive law. Not only are many burden of proof rules contained in substantive law provisions, but they may be inextricably connected to substantive legal rules: for example, a provision for the reversal of the burden of proof.10

In common law jurisdictions, however, it is an issue of procedural law. The common law distinction that the applicable foreign law must be proven like facts has become less important in arbitration as it is now customary for lawyers from civil law systems to provide extensive arguments on the legal points of their case.

This difference raises conflict of law questions – although these are alleviated in international arbitrations by a more pragmatic approach. Even though the inherent connection between the burden of proof rules and the substantive law may favour the civil law system view, in international arbitral practice, additional considerations come into play, such as the availability or unavailability of discovery, which does not exist in civil law systems but gives burden of proof rules a strong procedural aspect as well.11 Therefore, tribunals tend to be flexible when applying the burden of proof rules to a specific case. Generally, international arbitral decisions hinge much less on burden of proof issues than in domestic cases, not least because tribunals try to collect more evidence to have a more complete picture of the case.

In investment treaty arbitrations, questions of burden of proof typically further arise in respect of certain issues specific to investor–state arbitration: nationality, *ratione persona* scope, expropriation and compensation.

As regards nationality, including dual nationality and foreign control issues, and the *ratione persona* scope, tribunals traditionally followed the general rule that a party asserting a fact has the burden to prove it.12 More recently, however, as regards nationality issues at the jurisdictional phase of the proceedings, tribunals have begun to differentiate.13 However, so far a general trend to shift the burden of proof for certain nationality issues from the claimant to the respondent cannot be ascertained.

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9 cf. Article 42(2) of the ICSID Convention.
10 Such as in Article 97 of the Swiss Code of Obligations.
11 Born, op. cit., page 2,315.
13 *Siag v. Egypt* (Award) ICSID Case No. ARB/05/15, IIC 374 (2009) paras 138–141; *Tulip Real Estate Investment and Development Netherlands BV v. Turkey* (Decision on Bifurcated Jurisdictional Issue) ICSID
ii  Standard of proof

The standard of proof indicates the required degree of proof necessary to show that an assertion of fact has been proven. National laws provide many different definitions of what degree of proof must be met. However, most arbitration laws and institutional arbitration rules do not contain any provisions regarding the standard of proof that must be met. The most common standard in current international arbitration practice is the test of a ‘balance of probabilities’ — namely, a fact will be considered as proven if it is more probable than not that it is true. As with the burden of proof, tribunals should address the standard they apply in their awards.

A question intensely debated is whether criminal acts such as fraud, bribery and corruption require a higher standard of proof than the generally accepted standard of balance of probabilities (e.g., ‘clear and convincing evidence’). There is no uniform approach. Some argue that, in cases of corruption, a party only needs to establish a\textit{prima facie} case of corruption and that the burden of proof then shifts to the other party to prove the absence of corruption. However, this would result in the other party having to prove the negative, which it will not be able to do, particularly in corruption cases.\footnote{cf. Metal-Tech v. Uzbekistan, ICSID Case No. Arb/10/3, Award of 4 October 2013, paras. 236 et seq.}

It is sometimes argued that, for the quantum of damages, a different, mostly lower, standard of proof applies, not least because this may be the case under certain civil law provisions. This does not apply generally in arbitration. However, there are other, contractual, situations where the burden of proof or the standard of proof to be applied for the calculation of damages may change. Contractual provisions (e.g., liquidated damages clauses or penalty clauses) may lead impliedly to a different allocation of the burden of proof. With liquidated damages clauses, the claimant only needs to prove the breach by the other party and the existence of the damage, and not the quantum of the damage. This is different from penalty clauses, where the claimant only needs to prove the breach, but the respondent then has the burden of proof to show that the penalty is excessive.

Finally, in cases of a limitation of liability for wilful misconduct or gross negligence, the claimant needs to prove not only the existence and quantum of damages resulting from the breach, but also that these were the result of a wilful misconduct or gross negligence of the respondent.

Quantifications of damages are always discretionary. Tribunals may not apply rules of burden of proof and standard of proof in such a way to either award damages or not. Rather, with the assistance of the parties and their experts, tribunals have to assess the damages on their own, and thus the compensation to be paid.

This chapter explores investor–state dispute settlement (ISDS) to reveal the origins of that now ubiquitous feature of investment treaty arbitration – the third-party funder. Where does it come from? How did it get here? And how did it spread so quickly? To some, a headache to others, a cure. In examining the past we may even get a glimpse of the future of this unusual and resilient facet of ISDS.

As with all good investigations that seek to identify what was to explain what has come to be, it is proposed that there are categories with specific characteristics of their age that reveal different stages of development. Each of these categories are designated ages specific to the evolution of the third-party funder, summarised in the following table:

<table>
<thead>
<tr>
<th>Age</th>
<th>Time</th>
<th>Number of third-party funders</th>
<th>Available investment (US$)</th>
<th>Type</th>
<th>Expansion</th>
<th>Nature</th>
<th>Third-party funding terms*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pre-industry</td>
<td>Pre-2005</td>
<td>&lt;10**</td>
<td>&lt;30 million†</td>
<td>Opportunity</td>
<td>Litigation</td>
<td>Ad hoc</td>
<td>+50%</td>
</tr>
<tr>
<td>Industry</td>
<td>2005–2010</td>
<td>&lt;30***</td>
<td>&gt;100 million</td>
<td>Industry</td>
<td>Commercial arbitration</td>
<td>Standardisation</td>
<td>30%</td>
</tr>
<tr>
<td>Post-industry</td>
<td>2010–2017</td>
<td>&lt;40‡</td>
<td>&gt;1 billion</td>
<td>Profession</td>
<td>Investment treaty arbitration</td>
<td>Risk pricing</td>
<td>30%–70%</td>
</tr>
<tr>
<td>Modern</td>
<td>2017 onwards</td>
<td>&gt;60§</td>
<td>&gt;10 billion§</td>
<td>Specialist</td>
<td>Sector-specific</td>
<td>Merits-driven</td>
<td>1–2x +%</td>
</tr>
</tbody>
</table>

* These are aggregated terms as funders typically use a combination of multiple investments or a percentage of damages return on investment, either in combination or whichever results in a greater return on investment.

** Hillcrest Litigation Services Limited was established in Australia in 1993; IMF Bentham was publicly listed in the Australian stock exchange in 2001, but was established in 1994; Foris AG was established in Germany in 1996; and Litigation Lending Services was established in Australia in 1999. Harbour Litigation alludes to the origins of its business in 2002. It is estimated that there would have been fewer than 10 known litigation funders prior to 2005 operating globally, most of which would have been in Australia and Germany.

*** Of the 40 listed third-party funders on the Third Party Funding Observatory, around 20 appear to have been established between 2005 and 2010. Most growth coming from the United States and the United Kingdom. The list is likely incomplete and it is estimated that there was a three-fold increase in third-party funders between 2005 and 2010 in line with the increase in reported investment capital.

† Between 2000 and 2005, IMF’s trading volume increased from A$500,000 to nearly A$4 million (https://markets.ft.com/data/equities/tearsheet/summary?s=IMF:ASX). Extrapolating this type of growth to around 10 third-party funders and discounting for variants in performance, it seems likely that the equivalent of less than US$30 million was being invested in third-party funding per annum globally prior to 2005, and likely significantly less.

‡ An additional 20 third-party funders have been identified by the Third Party Funding Observatory after 2010. The list is likely incomplete but provides strong evidence of the continued surge in third-party funding in the United States, the United Kingdom and Germany.

³ With the opening of markets for third-party funding in the United Arab Emirates, Singapore, Hong Kong and mainland China, there is strong evidence from local and international law firms that the number of third-party funders is on the rise. It is likely that as each jurisdiction continues to define its relationship with third-party funding, there will be an increase not only in the number but the types of third-party funders and associated third-party funding services from insurers and brokers.

⁴ Of the estimated US$10 billion invested annually by third-party funders in disputes, US$5 billion appears to be invested in the United States (https://www.ft.com/content/926355de-c941-11e7-ab18-7a91b7d163ce; https://www.law360.com/in-depth/articles/992299).

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I THE PRE-INDUSTRY AGE

Third-party funding as a concept has existed for hundreds of years, and likely more. Despite what critics of third-party funding may say, it has its origins in access to justice. Jeremy Bentham wrote exhaustively on the topic of access to justice in the 1700s in the furtherance of ideas such as utilitarianism and distributive justice, and worked tirelessly for the repeal of champerty and maintenance laws in place since medieval times. The cost of access to justice has long been high in most legal jurisdictions, and without third-party funding good claims were often defeated by deep pockets. The fear that vulnerable people could be used as puppets in staged legal battles between wealthy land owners was not sufficient to deny access to justice for the majority of the population. It was inconsistent with what Bentham defined as the ‘fundamental axiom’ of his philosophy: the principle that ‘it is the greatest happiness of the greatest number that is the measure of right and wrong’.

Since then, very slowly, champerty and maintenance laws or their equivalents in most legal jurisdictions have been diluted or repealed in whole or in part. However, this is, in short, the philosophical origins of access to justice and third-party funding, not third-party funders. Third-party funders with a specific mandate to invest in disputes are a relatively recent phenomenon. Research suggests that prior to 2005, there were few types of third-party funders with the dedicated purpose of investing in claims, let alone a third-party funding industry. Although third-party funding as an investment opportunity existed, it was relatively low-profile and characterised by an infrequent ad hoc nature. There is debate as to whether it evolved in Australia (long considered the birth place of third-party funding in the common law world) or Germany as an offshoot from a highly developed form of legal insurance. There is little doubt that, during this pre-industry age, types of third-party funders existed in both these jurisdictions. However, the type of third-party funder unconnected with a claimant prior to the beginning of a dispute (i.e., not premium-based legal cost insurance) with the ability to allow for complete, or near complete, cost-risk transfer in exchange for sharing damages to advance a claim, the essence of the modern day third-party funder is likely to have arisen in common law jurisdictions. Why? Cost. The cost of third-party funding in most common law jurisdictions, owing to the nature of their litigation proceedings, is generally higher than civil law jurisdictions. In common law jurisdictions, it was and is for many as the former Irish Judge Sir James Mathew has said, that ‘justice is open to all, like the Ritz Hotel’.

A third-party funder during this pre-industry age, from the early 1990s to the early 2000s, was unlikely to have many disputes specialist lawyers working for it let alone ISDS specialists. They would have likely been characterised by insurance and investment experience; it would have undoubtedly required a high appetite for risk. Financial markets at this time were running hot and cold. Surplus funds designated for high-risk investment turned to third-party funding as an uncorrelated asset class. As a consequence, and from mostly anecdotal evidence, commercial terms ran high. Terms as high as 80 per cent of the damages have been seen and were likely common, embedded in questionably enforceable contracts.

In parallel to this development, the notion of beneficial ownership of proceeds and control was being revisited at the ISDS level as exemplified by CSOB Bank v. Slovak Republic, where the tribunal found that:

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2 See first table footnote.
The issue at stake in this dispute was nationality and control from financing parties. Such cases involving beneficial ownership of the proceeds of a claim and control set the scene for revisiting this issue with third-party funders at a subsequent stage.

II THE INDUSTRY AGE

In this period, the viability of third-party funding as not just an *ad hoc* investment opportunity but as an industry started to take shape. The evolution was not, of course, uniform; some jurisdictions advanced faster than others. In Europe, the United Kingdom was where many third-party funders began to most resemble modern day third-party funders. Third-party funding contracts were mostly imported and worked on from non-recourse financing practices, and a small body of law began to develop. However, from the decision in *Arkin v. Borchard Lines Ltd* (2005), a shift occurred in the United Kingdom. It is a decision that gave rise to what has since been interpreted as the principle that a funder could be held liable in adverse costs for a failed claim up to the amount that it invested into that claim: the ‘*Arkin* cap’, which has more recently come under review from the 2017 decision in *Bailey v. GlaxoSmithKline UK Ltd*. For some, *Arkin* exposed a potential liability that would deter investors in third-party funding. For others, *Arkin* provided reassuring clarity. A known unknown became clearer, and from it contractual risk sharing mechanisms could be forged and business models engineered. *Arkin* provided the bedrock on which a new industry could be founded. It heralded the first paradigm shift of third-party funding from isolated investment opportunity to the creation of third-party funding as a viable business model that would give rise to the burgeoning industry that it is today.

During this time, third-party funding was still mostly concentrated on litigation but, as with all developing industries, satellite opportunities spiralled from it to create third-party funding brokers. A satellite industry was formed by those who had worked on raising financing on an *ad hoc* basis for claims during the pre-industry age – those individuals with ability and foresight but who had neither the means nor arguably the appetite for third-party funding of disputes. Brokers accounted for the majority of third-party funding opportunities for the nascent third-party funder during the industry age. They paved the way through competition and legitimisation for not only a standardisation of terms but the expansion of third-party funding into commercial arbitration. As more funders came on to the market, the need for more investment opportunities expanded. In exchange for a tempering of industry terms to what is still often seen today – the greater of three times the investment or 30 per cent of the damages – brokers sought to increase the number of investment opportunities for these hungry third-party funders. International commercial arbitration was a natural choice. Rooted in practices not too dissimilar to what the third-party funding industry were used to, the leap was not one of faith but of logic.

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5 Ceskoslovenska obchodni banka, a.s. (CSOB) v. Slovak Republic, ICSID Case No. ARB/97/4, Decision of the Tribunal on Objections to Jurisdiction (24 May 1999).
6 This is not to suggest that third-party funding brokers did not exist prior to this time but merely that by this time there were established third-party funders, and therefore brokers who catered for them.
The nature of international commercial arbitration is more private than either litigation or ISDS. The confidentiality of the proceedings and the privacy of the parties allowed third-party funders to revert to a more creative financial space. How a private party to private proceedings financed its dispute was not the purview of the tribunal in commercial arbitration. This allowed funders to focus more on creative financial solutions than legal issues in respect of access to justice and any form of associated liability for costs. As third-party funders were not considered party to the arbitration agreement, they were not exposed to the same liability as they might be during domestic litigation as with Arkin in the United Kingdom. Third-party funders during this time adopted vocabulary from the banking world and started to identify themselves more with providers of non-recourse financing and, accordingly, started adapting third-party funding models on that basis. This allowed them to focus on wealthier claimants rather than access to justice or impecunious claimants. They sought to infiltrate corporate culture by promoting the advantages of financial risk transfer to commercial entities that did not need investment but that may choose it if the advantages in doing so could be justified not in terms of access to justice but in terms of bottom-line profitability. This period gave rise to financing solutions such as portfolio financing: the notion that a financial facility can be put in place across a claimant’s portfolio of disputes or indeed a facility for a law firm to be used across multiple disputes. Third-party funders explained the benefits of their financing to corporate clients as one in which a legal department could be converted from a cost centre into a profit centre, and notions of shifting the costs of a dispute off the balance sheet sought to win over chief financial officers. For many, this was a rebalancing of what third-party funders should be – a financial device, not a legal one. Disputes for funders could be seen as purely about compensation of loss without having to concern themselves with issues such as the dispensation of justice and the role funders play in either supporting, or in some jurisdictions running, claims. It was, like the commercial arbitration agreement, a private matter between commercial entities only.

This view of third-party funding as one chiefly about finance was born in the industry age as it pertains to international commercial arbitration and remains so today. It is perhaps best exemplified in the Essar Oilfield Services limited v. Norscot Rig Management Pvt Limited case (Essar v. Norscot). This was an International Chamber of Commerce (ICC) arbitration seated in London where Sir Philip Otto, sitting as sole arbitrator, allowed the victorious party to claim its third-party funding costs (including the funders’ uplift) from the losing party. The award was challenged on this basis but upheld by the High Court of Justice by J Waksman QC on the basis that recoverable costs were broadly enough defined under the ICC 2012 Rules and the 1996 Arbitration Act that the arbitrator was permitted to do so. There are multiple procedural issues that relate to Essar v. Norscot, but from the perspective of third-party funder responsibility, the case is significant for two main reasons: (1) it reinforces the view that third-party funding is purely a financial device and, under the right conditions, recoverable on success; and (2) it raises issues of transparency and the effect of the presence of a third-party funder on all the parties to a dispute. The latter is of particular importance as it pertains to the third-party funder of investment treaty disputes, which dramatically increased in the post-industry age.

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The second paradigm shift in third-party funding occurred nearly 10 years after Arkin with the now infamous Excalibur Ventures LLC v. Texas Keystone Inc and Ors, which was revisited more recently by the court of appeal in 2016. In this seminal case, Lord Justice Clarke drew a clear line between professional and ad hoc third-party funders. Weighing the benefits of access to justice against the potential for profiteering, his judgment was reassuring to some and a stern warning to others. In addition to confirming the Arkin cap, Clarke LJ inferred that if a third-party funder undertook proper due diligence to meet the claimant and to undertake the requisite assessment of the merits of a claim, it may be treated differently to those third-party funders that had abdicated responsibility and sought to treat a claim purely as an investment opportunity. The latter could be subject to costs orders on an indemnity basis. It imparted a sense of responsibility on third-party funders to be accountable for their investments. For some, Excalibur would discourage further investment in third-party funding and for others, as with Arkin, it provided additional clarity.

As a result, third-party funders began to distinguish themselves by those that had invested in the requisite skills and abilities to assess the merits of a claim, and those that were derided as being akin to gamblers, or ad hocs in the parlance of the growing third-party funding industry. Excalibur was the catalyst for the second paradigm shift that gave rise to the self-proclaimed professional third-party funder. Distinguishing between ad hoc and professional third-party funders, however, was unclear. At best, it seemed to be a distinction based on how many lawyers the third-party funder recruited. But, the focus on bringing on more disputes lawyers and the professionalisation of the industry brought disputes lawyers with ISDS experience – another disputes market for third-party funders to expand into. During this age, third-party funders began more aggressively focusing on ISDS disputes.

Third-party funding of disputes did not start with ISDS but it has become the fastest growing dispute forum for third-party funders. The reasons for this are both qualitative and quantitative: ISDS is expensive (US$6.1 million per side in claimants’ costs) and long (an average of 3.86 years to obtain an award, and an additional one to two years for post-award processes and enforcement). The ability to transfer the cost risk to a third party by sharing the upside in a potential award is obviously very attractive, but it was not obvious what the commercial terms of the funding agreement should be. ISDS was relatively untested at early stages of this post-industry age. As a result, what was typically seen in the industry was a reversion to pre-industry pricing revamped and referred to as risk pricing: this was merely a means by which a third-party funder could account for uncertainty by increasing profitability. But the nature of ISDS disputes are qualitatively different to commercial arbitration. Where investors seek recourse for either the partial or wholesale destruction or expropriation
without fair, prompt or adequate compensation of their investment, the loss suffered is often near complete. Third-party funding has its origins in access to justice for the impecunious, as explained above. When the wealthy ruling classes had such disproportionate influence that by their dealings they could destroy not just the transaction but the livelihood, the wealthy were practically above the rule of law, not least of which because of the high cost of access to justice. Investors and states have a similar inequality of arms inherent in the system (notwithstanding certain wealthy multinational companies), and as third-party funding was originally sought to balance the playing field in domestic litigation, it has readily been taken up by investor claimants in ISDS for the same reason.

Suddenly, at the ISDS level during this time, there were a plethora of task forces, white papers, practice directions and salient cases about or concerning third-party funders. For some, the issues relevant to domestic litigation where the nation state was involved in administering disputes pertaining to transparency and accountability became even more relevant when dealing with the nation state as a party to the dispute. From cases and developments, the dominant issues were those of provisional measures such as security for costs and confidentiality and transparency of the agreement with the third-party funder, as summarised below.

ii Security for costs

The ICSID Convention does not contain an express provision on security for costs and tribunals have tended to be reluctant on granting such orders. This restrictive approach has been maintained in various ICSID proceedings where third-party funders were involved. For instance, the arbitral tribunal in *Commerce Group Corp and San Sebastian Gold Mines, Inc v. El Salvador* maintained a restrictive approach to security for costs even when the proceedings were stayed while the applicants sought third-party funding. In the Order of the

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10 The ICCA-Queen Mary Task Force on Third-Party Funding is a joint task force established by ICCA and Queen Mary, University of London in 2013. https://www.arbitration-icca.org/media/10/40280243154551/icca_reports_4_tpf_final_for_print_5_april.pdf.

11 In Hong Kong, the Commission issued two reports after consultations, in October 2015 and October 2016, which culminated in proposed legislative amendments to Hong Kong’s Arbitration Ordinance, as well as proposed amendments to associated regulations. In Singapore, the consultations carried out by the Ministry culminated in two proposed draft instruments: the Civil Law (Amendment) Bill 2016 and the Civil Law (Third Party Funding) Regulations 2016.


13 There are several examples of investor–state arbitration cases where third-party funders have been involved. Among the more high-profile is the Canadian mining company, Crystalex, which was awarded over US$1.38 billion in a claim against Venezuela in which Crystalex was supported by third-party funders. More recently, Eco Oro, having filed an ICSID arbitration under the Canada–Colombia Free Trade Agreement relating to the Angosutra gold and silver deposit in the country’s Andean region, has the backing of third-party funders.


Committee Discontinuing the Proceeding and Decision on Costs, dated 28 August 2013, the tribunal ordered the claimants to pay the full administrative costs of the proceedings, but maintained its denial of security for costs.

The first known instance where an ISDS tribunal ordered security for costs where third-party funding was involved was the RSM Production Corporation v. Saint Lucia case, 13 August 2014, in which the tribunal ordered the claimant to pay security for costs in the amount of US$750,000 in the form of an irrevocable bank guarantee. However, that the claimant had obtained third-party funding was only used as a supportive argument not withstanding the separate ‘assent’ by Gavin Griffith who saw the ruling as confirmation that there should be automatic or near automatic security for costs where third-party funders are involved in ISDS cases. In contrast, the tribunal’s reasoning did not show any such contempt for third-party funders, as the main and decisive reason for ordering security for costs was the claimant’s proven history of defaulting on costs orders.

There have been subsequent decisions since RSM that have retained the same position in terms of a third-party funder’s involvement and an applicant’s request for security for costs. These early cases in the post industry age at the ISDS level as they relate to third-party funders suggest that tribunals are thus far inclined to maintain the status quo and to treat the advent of third-party funders in ISDS as nothing that would give rise to deviating from the long held view that security for costs applications should be allowed only in exceptional circumstances. However, there is a growing number of cases that suggest that future tribunals are prepared to investigate third-party funding arrangements more closely.

iii Confidentiality

ICSID tribunals have held that the parties themselves are not under a general duty of confidentiality, absent agreement to the contrary. In contrast, certain tribunals have highlighted the importance of limiting public discussion of the case to not disturb the proceedings. However, as non-parties to the arbitration agreement, third-party funders are not bound by any confidentiality duties flowing from that agreement. This was notably the

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18 See, for instance, in Amco Asia Corp. & Others v. Republic of Indonesia, ICSID Case No. ARB/81/1, Decision on Request for Provisional Measures of 9 December 1983: ‘as to the “spirit of confidentiality” of the arbitral procedure, it is right to say that the Convention and the Rules do not prevent the parties from revealing their case’; and Biwoner Gauff (Tanzania) Ltd. v. United Republic of Tanzania, ICSID Case No. ARB/05/22, Procedural Order No. 3 of 29 September 2006 (paras. 114-121).
19 The Loewen Group Inc. and Raymond L. Loewen v. United States of America, ICSID Case No. ARB(AF)/98/3, Decision on hearing of Respondent’s objection to competence and jurisdiction of 5 January 2001.
case during the *EuroGas Inc and Belmont Resources Inc v. The Slovak Republic* case in which the respondent's request for a confidentiality order against the claimants' funder was reportedly rejected by an ICSID tribunal.

**iv Conflicts of interest**

Arbitral tribunals tend to set aside requests for disclosure of third-party funding agreements raised by respondents at the ISDS level. In *Guaracachi America, Inc and Rurelec PLC v. The Plurinational State of Bolivia* (2013), the tribunal decided not to order the production of the agreement or 'further documentation' because the applicable provisions governing conflicts of interest in the present proceedings do not foresee the production of document by the Parties but rather disclosure by the arbitrators upon becoming aware of circumstances that could create a conflict of interest.\(^{20}\)

Concerns for conflicts of interest where third-party funding is involved are usually raised by the non-funded party and often relate to potential funder–arbitrator relationships. This issue is closely related to confidentiality, disclosure and transparency. For instance, in *South American Silver Ltd (Bermudas) v. Plurinational State of Bolivia*\(^{21}\) with respect to Bolivia's request to order South American Silver to disclose the identity of its third-party funder and to disclose the terms of the funding agreement, the claimant readily conceded on the former and the tribunal rejected the latter.\(^{22}\)

During the *Muhammet Çap and Sehil İnşaat Endustri ve Ticaret Ltd Sti v. Turkmenistan* case,\(^{23}\) on 23 June 2014, the tribunal issued its Procedural Order No. 2 recording its decision on the respondent's request of 11 April 2014 for disclosure of the third-party funding agreement. The tribunal ruled as follows:

> It seems to the Tribunal that the following factors may be relevant to justify an order for disclosure, and also depending upon the circumstances of the case:
> a To avoid a conflict of interest for the arbitrator as a result of the third-party funder;
> b For transparency and to identify the true party to the case;
> c For the Tribunal to fairly decide how costs should be allocated at the end of any arbitration;
> d If there is an application for security for costs if requested, and
> e To ensure that confidential information which may come out during the arbitral proceedings is not disclosed to parties with ulterior motives.


\(^{22}\) 'The Tribunal considers that while the existence of a third-party funder may be an element to be taken into consideration in deciding on a measure as the one requested by Bolivia, this element alone may not lead to the adoption of the measure . . . the disclosure of the name of the funder, the Tribunal considers that, for purposes of transparency, and given the position of the Parties, it must accept Bolivia’s request of disclosure of the name of SAS’ funder. Finally, concerning the disclosure of the terms of the financing agreement entered into with the third-party funder, the Tribunal will reject such request. In the Tribunal’s opinion, there is basis to order the disclosure of the name of the third-party funder, but not to order the disclosure of the agreement entered into with the third-party funder.' (Paras. 75-84).

\(^{23}\) *Muhammet Çap and Sehil İnşaat Endustri ve Ticaret Ltd Sti. v. Turkmenistan* (Decision on Respondent’s Objection to Jurisdiction under Article VII(2) of the Turkey-Turkmenistan BIT).

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Applying these factors, the tribunal was not persuaded that there was any reason to make an order requiring the claimants to disclose how they were funding the arbitration, but the factors listed do open the door to future rulings where such a disclosure can be made, and specifically the tribunal held that ‘this decision does not preclude the respondent from making a further request for disclosure at a later stage in this arbitration if it has additional information to justify the application.’

Taken as a whole, these cases and developments as they pertain to security for costs, confidentiality and conflicts of interest at the ISDS level are strong evidence that the role of third-party funders is unlikely to be relegated to that of mere financial services providers. Questions of transparency and legitimacy will continue to be probed, and, as a consequence, the type of third-party funder, how they conduct themselves, and from where and how they have raised their money are likely to be of greater relevance in the modern age.

IV THE MODERN AGE

We are currently in what appears to be the third paradigm shift of third-party funding – the modern age. There are today two prevailing and competing models of ‘professional’ third-party funders: risk pricing versus merits-based models. The former dictates that most claims can be funded if the terms are right and adheres to the view that third-party funders are mere providers of bespoke financial products. By this logic, even Excalibur could have been funded providing the commercial terms of the investment were sufficiently high to justify the risk. The reason for this is that the risk pricing model considers awards and judgments only in terms of compensation of loss and thus there is nothing wrong in funding an unmeritorious claim if the potential for a windfall is possible. This is the same mentality that characterises many financial markets where higher risks equate to higher rewards.

In contrast, the merits-based model requires the funder to treat a judgment or award as more than just an investment opportunity and a commodity to be invested in. It dictates that an award is first and foremost a judicial instrument for the dispensation of justice. The compensation of loss is as a result of the dispensation of justice, and thus knowingly funding an unmeritorious case or not accepting responsibility to assess the merits can and arguably should expose the funder to a costs liability.

If the battle between these two competing models continues unchecked, it is likely that the risk pricing model will prevail. The reasons for this are particular to our times as third-party funding presents, for many potential investors in third-party funding, an uncorrelated asset class and thereby an attractive investment during times of financial market instability. As a consequence, a new crop of would-be funders have come to the market having raised funds with promises of windfall returns to their investors. They were able to do so because despite the first two paradigm shifts, the third-party funding industry standard terms have barely changed in nearly 15 years. They continue to equate to three times or 30 per cent, whichever is the greater. This is surprising because the greater of three times or 30 per cent of the total value of the asset in private equity or asset management terms represents a windfall return unheard of in most markets, except in very high-risk categories. However, most self-proclaimed professional third-party funders report win rates that are between 80 and 90 per cent, or more. If terms such as three times the investment or 30 per cent of the value of the dispute have been historically justified to claimants and law firms on the basis that investment in disputes is high-risk, it is a statement at odds with the reported reality by mainstream third-party funders. Consequently, in the absence of defining cases for this third
paradigm shift, the risk pricing model is likely to prevail because funders are readily able to raise new, albeit expensive, money on the basis of an industry standard of three times or 30 per cent return on investment, which could arguably allow funders to lose 70–80 per cent of the claims they invest in and still generate profits for their investors.

However, this current paradigm shift, characterised by the battle between the risk pricing and merits-based models of third-party funding, is not devoid of indicators as to how it may develop. Consistent with the previous two paradigm shifts, in 2016 the UK Court of Appeal upheld Clarke LJ’s judgment on *Excalibur* and, therefore, the merits-based model that encourages thorough due diligence prior to funding a claim, and ongoing and effective monitoring during the life of the dispute. Furthermore, in *Bailey v. GlaxoSmithKline UK Ltd* [2017] Justice Foskett effectively considered the nature of the funder involved and decided that the *Arkin* cap could be lifted if not doing so would lead to an injustice. These advancements in case law at the domestic litigation level in countries such as the United Kingdom are likely to help shape the development of the role of the third-party funder at the ISDS level because of the one common denominator – the nation state. Where public money is involved, whether by administering a dispute or participating in it, questions will be asked about whether third-party funders are adopting a risk pricing model that may well give rise to more and greater disputes of questionable merit in search of windfall returns regardless of the cost to the public, or whether funders will be compelled to adopt a merits-based model where funders scrutinise more and temper returns on investment.

The differences between funders is greater today than their similarities. Some funders are publicly listed, some have front offices regulated by financial authorities and at least one has set up regulated asset management funding vehicles for the specific purpose of funding disputes. However, the vast majority and some well-known third-party funders appear to opt for a form of self-regulation with no oversight or transparency on conduct, how money is raised or from where. Tribunals in ISDS cases are likely to be put under more pressure to probe further not only into who the third-party funder to an ISDS dispute is, but also how much control it is exerting over the dispute. So far, tribunals have mostly been reluctant to inspect the workings of the funding agreement. Instead, they tend to prefer to focus on who the funder is for the purpose of conflicts of interests with the tribunal. However, it is not inconceivable that at some point during the modern age, if third-party funding remains an unregulated activity, tribunals will more frequently seek to inspect funding agreements to determine whether the funder has subrogated any of the rights typically reserved for the claimant. In the absence of an ability to develop an equivalent to the *Arkin* cap principle, ISDS tribunals may more frequently render orders for provisional measures such as security for costs. As a counterbalance, such a development may lend greater weight to arguments that the costs of such security should be recoverable from the respondent if the claim ultimately prevails.

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24 e.g., IMF Bentham, Burford Capital.
25 e.g., Augusta Ventures, Harbour Litigation Funding and, until the recent decision to cease trading, Calunius.
27 The Association of Litigation Funders is the most well-known example of a self-regulating body owned and controlled by the members it regulates.
28 In 2017, Burford Capital’s role as funder of a pair of treaty claims against Pakistan worth US$640 million ended with the claimants being ordered to pay around £11 million in costs; Vannin Capital’s role in
Some jurisdictions have already taken the view that third-party funding needs greater oversight and control. In the United Arab Emirates, the Dubai International Financial Centre has created a practice direction specifically for third-party funding. Regulation is currently being considered in Abu Dhabi. In Singapore and Hong Kong, third-party funding regulations have now been enacted. In Australia, there has more recently been a call for the licensing of third-party funders. These steps all precede what is widely expected to be a change in the ICSID rules in respect of third-party funding. The evolution of the third-party funder from litigation through commercial arbitration to ISDS has brought with it a desire for greater oversight and control of third-party funding. The question is what type of regulation – negative (responding to a problem) or positive (ensuring access to third-party funding) – will prevail? It is submitted that the answer lies in the type of third-party funder and the third-party funding model that prevails between risk pricing or merits-driven models as it pertains to ISDS.

financing a US$100 million DR-CAFTA claim against Costa Rica ended in a victory for the state and a US$1 million costs award against the claimant. At the time of writing, in Italba Corporation v Oriental Republic of Uruguay (ICSID Case No. ARB/16/9), the state prevailed leaving a cost awards against the claimant who was funded by IMF Bentham for US$5.9 million.
I INTRODUCTION

In the majority of investment treaty arbitrations, investors are entitled to submit an investment dispute to arbitration under the rules designated in the bilateral investment treaties (BITs). BITs usually specifically provide the foundation of the jurisdiction of the International Centre for Settlement of Investment Disputes (ICSID) as well as arbitration under the United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules, for example:

[i] the investment dispute shall at the request of the disputing investor be submitted to either:
(b) arbitration in accordance with the ICSID Convention, if the ICSID Convention is available;
(c) arbitration under the ICSID Additional Facility Rules, if the ICSID Additional Facility Rules are available; (d) arbitration under the UNCITRAL Arbitration Rules, or (e) if agreed with the disputing Contracting Party, any arbitration in accordance with other arbitration rules.2

A smaller number of investment treaty arbitrations are based on investment agreements instead of BITs. If the country of the investor and the host state have not entered into a BIT, the investor needs to specifically agree with the host state to submit the investment dispute to arbitration under specific rules, such as the ICSID Convention and the ICSID Rules of Procedure for Arbitration Proceedings (the ICSID Rules), which require that disputing parties must have consented in writing to the submission of their dispute to ICSID arbitration.

II THE ICSID CONVENTION AND THE ICSID RULES

i The ICSID Convention

History and Member States

As at 1 January 2018, 153 countries had ratified the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention). The ICSID Convention was signed by the first contracting states in 1965. The ICSID Convention established the International Centre for Settlement of Investment Dispute (ICSID) in Washington, DC in the United States. ICSID is funded by the World Bank.

1 Hiroki Aoki and Naoki Iguchi are partners at Nagashima Ohno & Tsunematsu.
2 Article 15(2) of the 2012 Japan/Korea/China Triparty Agreement for the Promotion, Facilitation and Protection of Investment (the 2012 Japan/Korea/China Investment Treaty).
Belize, the Dominican Republic, Ethiopia, Guinea-Bissau, Kyrgyzstan, Russia and Thailand have signed the ICSID Convention but have not yet ratified it (List of Contracting States and Other Signatories of the Convention (ICSID/3)). Brazil, India, Vietnam and South Africa are large economies that have not signed.

**Overview**

The ICSID Convention contains various provisions in addition to the procedural rules for arbitration. Since the ICSID Convention creates a fundamental basis for ICSID’s dispute resolution function and mechanism, it has also provided a basis for other subordinate rules and regulations, which include the Administrative and Financial Regulations; the Rules of Procedure for the Institution of Conciliation and Arbitration Proceedings; the Rules of Procedure for Conciliation Proceedings; and the Rules. For the purpose of practical use, this chapter focuses on the ICSID Convention and the Rules.

The ICSID Convention also sets out procedural provisions that directly impact arbitration procedures. Among them, there are some provisions that are unique compared with popular rules of arbitration for conventional commercial arbitration, including those detailed in the following subsections.

**Jurisdiction (Article 25)**

Jurisdictional conditions for access to arbitration under the ICSID Convention are: (1) the dispute must be between an ICSID member state and an individual or company that qualifies as a national of another ICSID member state; (2) the dispute must be a legal dispute arising directly out of an investment; and (3) the disputing parties must have consented in writing to the submission of their dispute to ICSID arbitration (Article 25). Those are considered to be mandatory requirements to resolve the dispute by ICSID arbitration.

Requirement (3) may be satisfied by a specific submission clause in investment agreements entered into between investors and host states. In the great majority of investment treaty arbitrations, this requirement has been satisfied by the state’s prior agreement in BITs, for example, ‘[e]ach Contracting Party hereby gives its consent to the submission of an investment dispute by a disputing investor to the arbitration set out in paragraph 3 in accordance with the provisions of this Article’.\(^3\)

Most BITs, as well as Article 25(1) of the ICSID Convention, adopt a concept of ‘investment’, which has been argued in many cases in connection with the jurisdiction. One of the leading cases in this regard is *Salini Construttori SpA and Italtrade SpA v. Kingdom of Morocco*, ICSID Case No. ARB/00/4, Decision on Jurisdiction (23 July 2001), which stated:

\[i\]he Tribunal notes that there have been almost no cases where the notion of investment within the meaning of Article 25 of the ICSID Convention was raised. However, it would be inaccurate to consider that the requirement that a dispute be “in direct relation to an investment” is diluted by the consent of the Contracting Parties. To the contrary, ICSID case law and legal authors agree that the investment requirement must be respected as an objective condition of the jurisdiction of the Centre.

The *Salini* tribunal further held that ‘[t]he doctrine generally considers that investment infers: contributions, a certain duration of performance of the contract and a participation

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3 Article 15(4) of the 2012 Japan/Korea/China Investment Treaty.
in the risks of the transaction [citation omitted]. In reading the Convention's preamble, one may add the contribution to the economic development of the host State of the investment as an additional condition.’

Since each of the ICSID tribunal’s awards are not treated as binding precedents for subsequent tribunals, tribunals have taken different approaches in determining and applying the criteria for investment.

**An award and its recognition and enforcement (Articles 53 to 55)**

An award is final and binding. Each party must comply with it pursuant to its terms. An award may not be set aside by the courts of any member state (Article 53). If a party fails to comply with the award, the other party can seek to have the pecuniary obligations recognised and enforced in the courts of any ICSID member state as though it were a final judgment of that state’s courts (Article 54(1)). In summary, awards rendered in the ICSID arbitration are preferred.

A party seeking recognition or enforcement in a member state must provide a copy of the award certified by the ICSID Secretary-General to a competent court (Article 54(2)). Certified copies are sent to the parties on the date of dispatch of the award, and the parties may request additional copies at any time.

However, although member states must recognise and enforce the award, each state’s laws relating to ‘sovereign immunity’ from execution continue to apply (Article 55). Accordingly, investors are sometimes confronted with the problem of execution, even after obtaining a winning award. ICSID does not formally assist a winning party’s enforcement procedure in state courts.

Accordingly, an unsatisfied party must consider various measures to press the state to accept the award. For example, if a party finds difficulty in enforcing the award and informs ICSID of such a situation, ICSID may contact the non-complying party to request further information on how to comply with the award, which may be helpful for the performance by the state. Another de facto enforcement measure would be publication (see below).

**Annulment (Articles 50 and 52)**

ICSID provides annulment as a post-award remedy. It is intended to be a safeguard against the violation of fundamental legal principles relating to the process (Article 52 and Rules 50 and 52–55). A party may apply for full or partial annulment of an award on the basis of one or more of the following five grounds:

a. the tribunal was not properly constituted;

b. the tribunal has manifestly exceeded its powers;

c. there was corruption on the part of a member of the tribunal;

d. there has been a serious departure from a fundamental rule of procedure; or

e. the award has failed to state the reasons on which it is based.

The application for annulment has to be submitted within 120 days after the award is rendered (Article 52(2)).

An ad hoc committee will decide the application. The ad hoc committee comprises three members appointed from the panel of arbitrators by the Administrative Council. The Rules apply, mutatis mutandis, to an annulment proceeding (Rule 53). A party may request stay of enforcement of the award pending the committee’s annulment decision (Article 52(5) and Rule 54).
The committee’s decision on annulment is not an award and may not be annulled through an ICSID annulment procedure. However, the decision is equated to an award for purposes of its binding force, recognition and enforcement (Article 53(2)).

If an award is annulled in whole or in part, a party is entitled to submit a request for resubmission, identifying the original award and explaining in detail (Rule 55(1)). The resubmission request will be examined by a new tribunal.

**Publication (Article 48)**

The ICSID Convention provides that ICSID shall not publish the award without the consent of the parties; in other words, ICSID can publish the award if the parties agree to it. The parties may agree to publish the award or annulment decision on ICSID’s website. If the parties do not agree, ICSID will publish excerpts of the decision’s legal reasoning (Rules 48(4) and 53). Arbitrators owe confidentiality obligations (Rule 6).

However, the ICSID Convention and Rules do not have any provision to prohibit the parties from publishing the award. In practice, most commercial agreements have a confidentiality clause that requests parties to arbitration to keep the procedure and award confidential, unless otherwise required under the applicable law (e.g., mandatory disclosure to investors). Unlike commercial arbitration, parties to investment treaty arbitration are not necessarily parties to commercial agreements and, in such a case, are not bound by contractual confidentiality obligations. Accordingly, unless otherwise agreed during the arbitration procedure, the parties may unilaterally publish the awards and decisions. In many situations, the purpose of publishing is to make the outcome transparent and urge the losing party to perform the award.

**The ICSID Rules**

**Overview**

The ICSID Arbitration Rules apply as a basic set of rules for ICSID arbitration, together with the ICSID Convention.

**Appointment of arbitrators (Rule 3)**

Absent a prior agreement between the parties or specified rules in the investment treaty, ICSID invites the parties to agree on the number of arbitrators and the method of their appointment (Rule 2).

The number of arbitrators is one or any uneven number. The parties are otherwise free to adopt any workable method of appointment that suits their needs, including provisions on time limits and special procedures. The parties are free to appoint arbitrators from the ICSID Panel of Arbitrators.

The Rules provide a method and timeline for appointing arbitrators. In a three-arbitrator tribunal, the Rules assume that the president of the tribunal is appointed by agreement of the parties (Article 37 and Rule 3). If the tribunal is not constituted within 90 days of the registration of the case, either party may request the chair of the Administrative Counsel of ICSID to appoint the arbitrator not yet appointed and designate the president of the tribunal (Rule 5). Certainly, the ICSID Convention and Rules allow parties to agree on the method of appointment and will follow such agreed method, including exchange of a list of candidates between the parties. If the parties cannot appoint all the arbitrators, including the chair of the tribunal, the ICSID default mechanism will operate.
Sessions of the tribunal (Rule 13)

The first session should be held within 60 days of the constitution of the tribunal, unless the parties agree otherwise (Rule 13(1)). The dates of that session shall be fixed by the president of the tribunal after consultation with its members and the Secretary-General of ICSID. The secretary of the tribunal will assist the tribunal to fix the date by contacting the parties to enquire about their availability for the session.

The parties may agree on any location for the first session, provided that the tribunal approves the venue and there are suitable facilities. The tribunal often proposes a venue for the parties’ consideration. If there is no agreement, an in-person meeting will take place by default at the seat of ICSID in Washington, DC (Article 63 of the ICSID Convention and Rule 13(3)). The World Bank’s facilities in Washington, DC or Paris, France, are the most popular places for the first session. ICSID can also provide other premises of the World Bank. ICSID has also entered into collaboration agreements with some popular arbitration institutions. The first session can be held in person, by telephone or by videoconference. In fact, increasing numbers of first sessions have been held by telephone or videoconference, to save time and costs.

The purpose of the first session of the tribunal is to ascertain the parties’ agreements or separate views on procedural questions such as the applicable arbitration rules, languages to be used, place of proceedings and the procedural calendar. The session enables the tribunal to set a schedule and establish specific rules for each case in a procedural order.

Unlike traditional commercial arbitration, the secretary of the tribunal, who is appointed by the Secretary-General (Administrative and Financial Regulation 25) will have an active function in the procedures. The secretary of the tribunal circulates a draft agenda approved by the tribunal to the parties for their comments well in advance of a first session. The draft agenda has been developed by ICSID taking into account standard procedural items, such as the procedural calendar (Rule 20). The agenda is often accompanied by a draft procedural order to guide the parties in reaching agreements on specific issues.

At the first session, the tribunal sometimes allows oral submissions of either party, if such a party submits a request for bifurcation of the proceeding, a request for provisional measures or a request to dispose of the matter because the claim is manifestly without legal merit.

The president of the tribunal will issue a procedural order based on the agreements reached and the procedural decisions taken by the tribunal. The procedural order will be circulated to the parties by the secretary of the tribunal promptly after the first session.

Evidence (Rules 33, 34, 35 and 36)

The parties should file evidence in support of their claim or defence with their written pleadings or instruments (Rules 24 and 33).

The ICSID Convention and Rules allow various types of evidence to be filed in the written procedure; namely, documentary evidence (e.g., exhibits, witness statements and expert reports) or non-documentary evidence (e.g., audio and video files) (Rule 34(2)(b)). Demonstrative exhibits (e.g., PowerPoint presentations, charts and graphs) may be used at a hearing provided they contain no new evidence and identify the evidence on record relied on. Site visits may be allowed by the tribunal upon a party’s request (Rule 37(1)). If the evidence is in a language other than the procedural language, it must be submitted in the original language together with a translation (Administrative and Financial Regulation 30(3) and (4)).
The tribunal decides any disagreement about the admissibility of the evidence (Rule 34(1)). The parties and the tribunal often agree that the tribunal may be guided by the International Bar Association Rules on the Taking of Evidence in International Arbitration (the IBA Rules of Evidence) when considering the admissibility of evidence and other evidentiary issues. The tribunal has the discretion to consider the relevance, weight and credibility of the evidence submitted by the parties (Rule 34(1)).

Like commercial arbitration, each party produces its own witnesses and appoints its own experts. The tribunal may call upon the parties to produce further witnesses and experts if it deems it necessary (Article 43 of the ICSID Convention and Rule 34).

Oral procedure – hearings and procedural sessions (Rule 29)
The oral procedure follows parties’ written submissions (Rule 29). The oral procedure consists of ‘hearings’ and ‘procedural sessions’. Most hearings are held in person, while procedural sessions (such as the first session of the tribunal) are often held by telephone or videoconference.

Usually, hearings will take place in the following order: (1) opening statements, (2) witness examination, (3) expert examination and (4) closing arguments. A tribunal may put questions to counsel, witnesses and experts (Rule 32). The parties may agree that there should be no opening or closing statement, or that the closing statement should be replaced by post-hearing briefs.

While the Rules refer to general principles on ‘Marshalling of Evidence’ (Rule 33), ‘Evidence: General Principle’ (Rule 34), ‘Examination of Witnesses and Experts’ (Rule 35) and ‘Witnesses and Experts: Special Rules’ (Rule 36), the ICSID Convention and Rules do not have detailed rules on how witnesses and experts are examined. In practice, a party that intends to cross-examine a witness or expert calls that witness. Fact witnesses and experts are required to make a declaration before testifying (Rules 35(2) and (3)). Fact witnesses are often not allowed to attend the hearing until after their testimony.

After seeking the views of the parties, the tribunal will decide the manner in which the record of the hearings shall be kept (Rule 20(g)). In practice, ICSID usually keeps audio recordings and written transcripts of hearings. In many cases, the parties ask the court reporter to prepare a verbatim transcript of the entire hearing in electronic format.

Public access to the hearings
Unlike Conciliation Rule 27(1), which requires that the conciliation hearing should be held in private, the ICSID Convention and Rules applicable to investment treaty arbitration do not set out default rules on the privacy of the hearings. If the hearing is open to the public, ICSID provides a video link from the hearing room that is broadcast to a separate room in the premises of the hearing that is open to the public.

Decision-making of the tribunal (Rules 15 and 16)
The deliberations of the tribunal shall take place in private and remain secret (Rule 15), usually immediately after a hearing or procedural session. Deliberations can also be held by telephone, videoconference or correspondence (Rule 16(2)).

Decisions of the tribunal shall be taken by a majority of the votes of all its members. The tribunal is generally allowed to have a deliberation by correspondence, but in this case all members must be consulted. The parties may agree that the president of the tribunal
decides without consulting the other members in urgent situations, subject to possible reconsideration of the decision by the full tribunal. Such decisions typically relate to the extension of time limits and other urgent procedural questions (Rule 26(1)).

iii The Additional Facility Rules
ICSID stipulated the 1978 Additional Facility Rules for investment disputes that fall outside the scope of the ICSID Convention. The ICSID Additional Facility Rules are widely referred to in investment treaties of which either party is not a member state of the ICSID Convention.

iv Recent developments
ICSID initiated the amendment process in October 2016 and invited member states to suggest topics that merited consideration. In January 2017, ICSID also invited suggestions from the public in early 2018. The Secretariat has recently published those suggested comments on its website. It is expected that ICSID will consider and incorporate the lessons learned from the development of investment treaty arbitration practice.

III THE UNCITRAL RULES
i Overview
The UNCITRAL Arbitration Rules introduced in 1976, or as revised in 2010 (the UNCITRAL Rules), have also been extensively used in investment arbitrations under various BIT and free trade agreement investment chapters. The UNCITRAL Rules were tailored mainly for ad hoc arbitration, but a number of arbitration institutions accept the administration of the arbitration under the UNCITRAL Rules.

ii Key features of the UNCITRAL Rules

Commencement of arbitration
Arbitration may be commenced by communicating to the respondents a notice of arbitration (Article 3.1). Within 30 days of the receipt of the notice of arbitration, the respondent shall communicate to the claimant the response (Article 4.1).

Selection of arbitrators
If parties have not agreed on the number of arbitrators previously or within 30 days of the respondents’ receipt of the notice of arbitration, three arbitrators shall be appointed (Article 7.1).

If the parties have not reached agreement within 30 days (1) of receipt by other parties of a proposal for the appointment of a sole arbitrator, or (2) of the appointment of the second arbitrator (if three arbitrators are to be appointed), the appointing authority shall use the ‘list procedure’ for selecting the arbitrator, as set forth in Article 8.2.

Challenge to arbitrators
Any arbitrator may be challenged if ‘circumstances exist that give rise to justifiable doubts as to the arbitrator’s impartiality or independence’ (Article 12.1). A party that intends to challenge an arbitrator shall send notice of its challenge within 15 days after either it has been notified of the appointment of the challenged arbitrator or after the circumstances mentioned above became known to that party (Article 13.1).
Seat of arbitration
If the parties have not previously agreed on the place of arbitration, it shall be determined by the arbitral tribunal with regard to the circumstances of the case (Article 18.1).

The arbitral proceedings and the award will be subject to the national legislation applicable in the jurisdiction where the seat is situated. This is the notable difference from the ICSID Rules.

Arbitral procedure
Subject to the Rules, the arbitral tribunal may conduct the arbitration in such manner as it considers appropriate, provided that the parties are treated equally and that each party is given a reasonable opportunity of presenting its case (Article 17.1). As soon as practicable after its constitution and after inviting the parties to express their views, the arbitral tribunal shall establish the provisional timetable of the arbitration (Article 17.2).

Preliminary measures
Article 26.2 lists examples of the interim measures available to the party as follows:

- maintain or restore the status quo pending determination of the dispute;
- take action that would prevent, or refrain from taking action that is likely to cause:
  - current or imminent harm; or
  - prejudice to the arbitral process itself;
- provide a means of preserving assets out of which a subsequent award may be satisfied; or
- preserve evidence that may be relevant and material to the resolution of the dispute.

The party requesting an interim measure is required to satisfy the arbitral tribunal for the following requirements (Article 26.3):

- harm not adequately reparable by an award of damages is likely to result if the measure is not ordered, and such harm substantially outweighs the harm that is likely to result to the party against whom the measure is directed if the measure is granted; and
- there is a reasonable possibility that the requesting party will succeed on the merits of the claim.

These are the characteristic provisions of the UNCITRAL Rules since some other institutional rules do not provide such a detailed list of examples and the requirements, but just leave it to the tribunal’s discretion.

Costs
The arbitral tribunal shall fix the costs of arbitration in the final award or in another decision (Article 17.2). Within 15 days of receiving the arbitral tribunal’s determination of fees and expenses, any party may refer for review such determination to the appointing authority. The appointing authority may make adjustments to the tribunal’s determination and such adjustment shall be binding upon the arbitral tribunal (Article 41.4(b) and (c)).
Confidentiality and transparency – the UNCITRAL Transparency Rules

In 2013, the UNCITRAL Rules were amended and the UNCITRAL Rules on Transparency in Treaty-based Investor–State Arbitration (the UNCITRAL Transparency Rules) were introduced.

The UNCITRAL Transparency Rules are applicable to arbitration initiated pursuant to a treaty concluded on or after 1 April 2014, unless the parties to the treaty have agreed otherwise (Article 1 of the UNCITRAL Transparency Rules). It can be applied to arbitration based on a treaty concluded prior to 1 April 2014 when the parties to the relevant treaty, or disputing parties, agree to their application.

The UNCITRAL Transparency Rules went further than the other arbitration rules such as the ICSID Rules with regard to the transparency. The key elements are as follows.

Possible ISDS reform

At UNCITRAL, states have begun debates about the possible reform of investor–state dispute settlement (ISDS). UNCITRAL mandates a working group to proceed to: (1) first identify and consider concerns regarding ISDS; (2) consider whether reform was desirable in light of any identified concerns; and (3) if the working group were to conclude that reform was desirable, develop any relevant solutions to be recommended to the UNCITRAL Commission.

Publication of information and documents

Upon the filing of notice of arbitration, (1) the name of the disputing parties, (2) the economic sector involved and (3) the treaty under which the claim is being made shall be published (Article 2). Further, the following documents shall be published:

a. a notice of arbitration and response thereto;
b. subsequent written statements or submissions, including a statement of claim and a statement of defence;
c. a table listing all exhibits to the written submission, and to expert reports and witness statements (but not the exhibits themselves), if the table has been prepared in the proceedings;
d. expert reports and witness statements, upon request by any person to the tribunal;
e. any written submissions by a non-party to the arbitration;
f. transcript of hearings (where available); and

g. tribunals orders, decisions and awards.

Third-party submissions

Non-disputing parties to the treaty and any other third party may make a submission with the tribunal's permission (Articles 4 and 5). In determining whether to allow such submission by the third party (other than the non-disputing party), the tribunal shall consider:

a. whether the third party has a significant interest in the proceedings; and
b. the extent to which the submission would assist the tribunal by bringing a perspective, particular knowledge or insight that is different from that of the disputing parties.

Hearings

Hearings shall be public and the tribunal shall make the logistical arrangements to facilitate public access to hearings (Article 6).
Information to be made available to the public under the UNCITRAL Transparency Rules shall be through the central repository, the function undertaken by the Secretary-General of the United Nations.

IV THE PCA RULES

The PCA Arbitration Rules 2012 (the PCA Rules) were introduced by the Administrative Council of the Permanent Court of Arbitration (PCA) on 17 December 2017. The PCA Rules are a consolidation of four prior sets of procedural rules that the PCA established in the 1990s. The PCA Rules can be applied to a disputes involving at least one state, state-controlled entity or intergovernmental organisation (collectively, ‘the states’).

The PCA Rules basically follow the UNCITRAL Rules, but have some characteristic features, such as:

a. the PCA Rules confirm that agreement by the states to arbitrate under the PCA Rules constitutes a waiver of any right of immunity from jurisdiction, although immunity relating to enforcement must be expressed explicitly (Article 1.2);

b. the International Bureau of the PCA at The Hague shall serve as registry for the proceedings (Article 1.3). The parties to the arbitration must communicate their submissions and all communications to the arbitral tribunal to the International Bureau of the PCA (Articles 3.1, 4.1, 17.4, 20.1 and 21.1);

c. the Secretary-General of the PCA is the mandatory appointing authority (Article 6.1);

d. the PCA Rules clearly provide an option to appoint five arbitrators (Articles 9.1 and 10.1). Arbitrators do not need to be members of the PCA (Article 10.4);

e. notice of challenge to an arbitrator needs to be sent within 30 days (as opposed to 15 days under the UNCITRAL Rules) after the basis for the challenge became known to the party (Article 13.1). In rendering the decision on a challenge, the PCA may indicate reasons for the decision, unless the parties agree that no reasons shall be given (Article 13.5);

f. the PCA Rules set out a clear provision that the arbitrator may perform a site visit after consultation with the parties (Article 27.3);

g. the PCA Rules clarify the applicable laws in cases involving only states, only states and intergovernmental organisations, or intergovernmental organisations and private parties (Article 35.1);

h. before fixing the costs of arbitration, the arbitral tribunal is required to submit its determination to the PCA for review (Article 41.3); and

i. the deposit shall be directed to the PCA instead of the arbitral tribunal (Article 43.1).

V THE SCC RULES 2017

The Arbitration Institute of the Stockholm Chamber of Commerce (SCC) is a major arbitration institution for investment arbitration, particularly for energy disputes. The SCC announced that the SCC Arbitration Rules are the third most commonly used arbitration rules in investment disputes, and the SCC is the second-largest investment arbitration institute after ICSID. Between 1993 and 2016, 92 investor–state disputes were registered at the SCC.
The latest SCC Rules are the SCC Rules 2017, entering into force on 1 January 2017. Key features of SCC Rules 2017 include:

a the introduction of Appendix III, which is specifically applied to investment treaty disputes. Under Appendix III, third persons and non-disputing treaty parties may request or be invited to make written submissions;

b there is no special rule for investment arbitrations of the confidentiality and transparency. Therefore, unless otherwise agreed by the parties, the confidentiality of the arbitration and the award shall be maintained (Article 3);

c the default number of arbitrators is three for the investment arbitration (Article 2 of Appendix III);

d a request for arbitration needs to be filed to the SCC, and the Secretariat of the SCC shall send a copy to the respondent. The Secretariat sets a time limit on the answer (Article 9);

e the board of the SCC may request further details from either party on any of their written submission. If the party fails to comply with the board’s request, the board may dismiss the case, or the counterclaim or set-off (Article 10);

f the board of the SCC shall dismiss a case, in whole or in part, if the SCC manifestly lacks jurisdiction over the dispute (Article 12);

g the proposal of appointment of an administrative secretary needs to be submitted to the SCC, and is subject to the parties’ approval. The administrative secretary’s fees shall be paid from the fees of the arbitral tribunal (Article 24);

h a party may request a summary procedure determining any issues where:

• an allegation of fact or law material to the outcome of the case is manifestly unsustainable;

• even if the facts alleged by the other party are assumed to be true, no award could be rendered in favour of that party under the applicable law; or

• any issue of fact or law material to the outcome is suitable for the summary procedure for any other reason (Article 39);

i the final award shall be made no later than six months from the date the case was referred to the arbitral tribunal, unless the board of the SCC extends the time limit (Article 43); and

j a party may apply for the appointment of an emergency arbitrator until the case has been referred to an arbitral tribunal. The SCC board shall seek to appoint an emergency arbitrator within 24 hours of receipt of application. Any emergency decision on interim measures shall be made no later than five days from the date the application was referred to the emergency arbitrator (Appendix II).

VI THE SIAC IA RULES 2017

In 2016, Singapore International Arbitration Centre (SIAC) introduced a new set of rules for the investment arbitrations, which came into effect on 1 January 2017 (the SIAC IA Rules 2017). The SIAC IA Rules 2017 can be applied in any dispute involving states (no qualification of ‘investor’ or ‘investment’ is required under the Rules, without prejudice to any requirements under the underlying instruments). The SIAC IA Rules 2017 are largely based on the SIAC Arbitration Rules 2016, which are mostly used for commercial arbitration, but include some unique provisions:
they provide for a state immunity clause similar to the PCA Rules (Article 1.3);

b the parties may agree that the arbitral tribunal shall be composed of one, three or any other odd number of arbitrators (Articles 5.1 and 5.2);

c a default list procedure shall be adopted if party fails to agree on:
• a sole arbitrator within 42 days; or
• a presiding arbitrator if there are multiple arbitrators. The list procedure is similar to the one in the UNCITRAL Rules, but the SIAC Court shall communicate at least five names (as opposed to three names in the UNCITRAL Rules) (Article 8);

d the Rules clearly provide that where the parties are of different nationalities, the SIAC Court shall appoint a different nationality than the parties in principle (Article 5.7);

e ‘Statement of Claim’ and ‘Statement of Defence’ in the SIAC Rules 2016 are replaced by ‘Memorial’ and ‘Counter-Memorial’, and the witness statement or expert report supporting the claim needs to be accompanied with the factual and legal submissions (Articles 17.2 and 17.3). Reply and rejoinder shall be filed by agreement of the parties, or if deemed necessary by the tribunal (Article 17.4);

f a third party or non-disputing contracting state may make written submissions subject to the terms and conditions under the Rules (Article 29);

g by agreeing to use the IA Rules, the parties shall be deemed to have allowed SIAC to publish limited information as follows (Article 38):
• the nationality of the parties;
• the identity and nationality of the tribunal;
• the treaty, statute or other instrument under which the arbitration has been commenced;
• the date of commencement;
• whether the proceedings are ongoing or have been terminated; and
• redacted excerpts of the reasoning of the tribunal and redacted decisions by the SIAC Court on challenges to arbitrators;

h third-party funding: the tribunal may order the disclosure of (Article 24(l)):
• the existence of a party’s third-party funding arrangement;
• the identity of the third-party funder and, where appropriate, details of the third party;
• the funder’s interest in the outcome of the proceedings; and
• whether the third-party funder has committed to undertake adverse costs liability. The tribunal may take into account any third-party funding arrangements in apportioning the costs of the arbitration (Article 33.1);

i early dismissal may be applied by a party if a claim or defence is manifestly without legal merit; manifestly outside the jurisdiction of the tribunal; or manifestly inadmissible (Article 26). This rule was the same in the SIAC Rules 2016;

j application for an emergency arbitrator may be available only when the parties expressly agree on the application of the emergency arbitrator provisions (Article 27.4); and

k within 90 days from the date on which the tribunal declares the proceedings closed, the tribunal shall submit the draft award to the SIAC Registrar (Article 30.3).
VII THE CIETAC IA RULES 2017

On 19 September 2017, CIETAC released its Investment Arbitration Rules (CIETAC IA Rules 2017), which became effective on 1 October 2017. It was announced on their implementation that the purpose of the CIETAC IA Rules 2017 is to support Chinese enterprises throughout the implementation of the ‘Belt and Road Initiative’.

The CIETAC IA Rules 2017 provide transparency rules, including public access to hearings and documents submitted in the arbitration. They also provide the rules pertaining to third-party submissions following the recent trend implemented in other rules, as we have seen above.

As for third-party funding, Article 27 requires that parties receiving third-party funding disclose, without any delay, the existence and nature of the arrangement and the identity of the funder.

One of the unique features of the CIETAC IA Rules is Article 43, which allows the arbitral tribunal to mediate the case during the pendency of the arbitration by itself.
Chapter 11

CORRUPTION, FRAUD AND ABUSE OF PROCESS IN INVESTMENT TREATY ARBITRATION

Carmen Martinez Lopez and Lucy Martinez

I  INTRODUCTION AND OVERVIEW

This chapter addresses the issue of misconduct and impropriety by claimants and investors in investor–state arbitration, including corruption, bribery, fraud, illegality and abuse of process. Investor–state tribunals consistently deny such claims, at either the jurisdiction and admissibility, or merits phase, often awarding costs to the state. However, tribunals have not clearly articulated the burden and standard of proof for such allegations, and greater consistency and clarity is needed in this important area.

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Section II of this chapter summarises cases in which tribunals have dismissed claims on the basis of misconduct by the claimant or investor, across three broad categories: (1) corruption and bribery; (2) fraud, illegality, misrepresentation or lack of good faith; and (3) abuse of process. Section III discusses the timing of challenges by states based on investor misconduct, and Section IV examines the burden and standard of proof for such allegations. Section V summarises remedies available to tribunals and states when faced with investor misconduct (or allegations or suspicions thereof), and Section VI sets out our conclusions.

II CASES INVOLVING INVESTOR MISCONDUCT

This section summarises cases where the investor misconduct has been 'outcome-determinative', leading to dismissal of the case, and does not address cases where tribunals have rejected such allegations, or where the claim has been dismissed on other bases, such as lack of *ratiōne temporis* jurisdiction. Cases are presented in chronological order, to illustrate the jurisprudential evolution.

i Corruption and bribery in relation to the investment

Corruption is widely condemned under international and national law for its far-reaching economic, social and political impact. As noted by former UN Secretary-General Kofi Annan:

*Corruption is an insidious plague that has a wide range of corrosive effects on societies. It undermines democracy and the rule of law, leads to violations of human rights, distorts markets, erodes the quality of life and allows organized crime, terrorism and other threats to human security to flourish.*

To date, only three tribunals have dismissed investor–state claims on the basis of corruption or bribery; two are discussed herein.  

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4 UN Convention, foreword, page iii.

5 (1) World Duty Free Company Limited v. The Republic of Kenya, ICSID Case No. ARB/00/7, Award, 4 October 2006 (World Duty Free v. Kenya); (2) Metal-Tech Ltd. v. The Republic of Uzbekistan, ICSID Case No. ARB/10/3, Award, 4 October 2013 (Metal-Tech v. Uzbekistan); (3) Spentex Netherlands B.V. v. Republic of Uzbekistan, ICSID Case No. ARB/13/26, Award, 27 December 2016 (Spentex v. Uzbekistan) (award not publicly available, but discussed in V Djanic. In newly unearthed Uzbekistan ruling, exorbitant fees promised to consultants on eve of tender of process are viewed by tribunal as evidence of corruption, leading to dismissal of all claims under Dutch BIT, IAREporter, 22 June 2017, available at https://www.iareporter.com/articles/in-newly-unearthed-uzbekistan-ruling-exorbitant-fees-promised-to-consultants-on-eve-of-tender-process-are-viewed-by-tribunal-as-evidence-of-corruption-leading-to-dismissal-of-all-claims-under-dutch/ (accessed 9 January 2018), reporting that the case was dismissed as inadmissible due to the investment having been obtained through corruption). In two other investor–state cases, allegations of corruption apparently led to settlement of the dispute: (1) Siemens AG v. The Argentine Republic, ICSID Case No. ARB/02/8, Award, 6 February 2007 (Siemens v. Argentina); US Federal Bureau of Investigation, Dept of Justice Press Release, ‘Siemens AG and Three Subsidiaries

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The first investor–state tribunal to dismiss a claim on the basis of corruption was in World Duty Free v. Kenya. The claimant alleged expropriation of its contractual rights regarding duty-free concessions in airports. Remarkably, the claimant’s CEO admitted in his witness statement to making a ‘personal donation’ of US$2 million to the Kenyan President. The CEO testified that he felt ‘uncomfortable’ about this ‘donation’, but ‘was given to understand that it was lawful and that [he] didn’t have a choice if [he] wanted [his] investment contract’. Perhaps unsurprisingly, in light of this direct admission by the claimant, the tribunal dismissed the claims on the basis of ‘international public policy common to the community of nations’, as the original investment was procured through bribery. The tribunal found that the claimant ‘is not legally entitled to maintain any of its pleaded claims in these proceedings’, denouncing corruption in the following terms:

Such corruption is more odious than theft; but it does not depend upon any financial loss and it requires no immediate victim. Corruption of a state officer by bribery is synonymous with the most heinous crimes because it can cause huge economic damage, and its long-term victims can be legion. The offence lies in bribing a person to exercise his public duty corruptly and not in accordance with what is right and proper for the state and its citizens. Like any other contract, a state contract procured by bribing a state officer is legally unenforceable, as an affront to the public conscience.

The tribunal found that ‘there can be no successful party on the merits in the traditional sense’ and directed each party to bear its own costs and fees.

Metal-Tech v. Uzbekistan (2013)

The claimant alleged expropriation of its investment in a plant for the production of molybdenum. The state objected to jurisdiction on the basis of, inter alia, alleged corruption in the making and operation of the investment. The chair and CEO of the claimant testified that he paid US$4 million to consultants with connections to state officials, including the brother of the Prime Minister, but maintained that these payments were for lobbying services. The tribunal dismissed the claim on the basis of lack of jurisdiction, because the investment had not been ‘implemented in accordance with the laws and regulations of the
Corruption, Fraud and Abuse of Process in Investment Treaty Arbitration

Contracting Party in whose territory the investment is made’, as required by Article 1(1) of the relevant BIT.13 The tribunal found that the claimant had failed to substantiate the services provided by the consultant. In reaching this conclusion, the tribunal emphasised the need to promote the rule of law:

While reaching the conclusion that the claims are barred as a result of corruption, the Tribunal is sensitive to the ongoing debate that findings on corruption often come down heavily on claimants, while possibly exonerating defendants that may have themselves been involved in the corrupt acts. It is true that the outcome in cases of corruption often appears unsatisfactory because, at first sight at least, it seems to give an unfair advantage to the defendant party. The idea, however, is not to punish one party at the cost of the other, but rather to ensure the promotion of the rule of law, which entails that a court or tribunal cannot grant assistance to a party that has engaged in a corrupt act.14

The tribunal ordered the parties to bear their own costs, on the basis that the state had participated in ‘creating the situation that leads to the dismissal of the claims’ (i.e., the corruption).15

Commentary

a To date, only three tribunals have dismissed claims on the basis of bribery or corruption (World Duty Free v. Kenya, Metal-Tech v. Uzbekistan and Spentex v. Uzbekistan).
b The claims were dismissed on the basis of ‘international public policy’, and lack of jurisdiction or inadmissibility, namely lack of a protected ‘investment’.
c In relation to costs, in World Duty Free v. Kenya and Metal-Tech v. Uzbekistan, the tribunals directed the parties to bear their own costs. However, in Spentex v. Uzbekistan, the tribunal apparently directed the state to donate to a United Nations anti-corruption initiative, and then ordered the costs of the arbitration to be split equally between the parties.
d Some commentators have criticised these awards for permitting a state to rely on its own wrongful conduct to escape liability.16
e Some commentators suggest that allegations of corruption are likely to increase in investor–state disputes, and tribunals have a duty to investigate a potential issue of corruption *sua sponte*, to ensure the enforceability of the award.17
f Allegations of corruption or bribery may also lead to settlement of the dispute.18

g In most cases to date, allegations of bribery or corruption have been dismissed on the basis of insufficient evidence.19 This issue is discussed further in Section IV, regarding the burden and standard of proof.

13 id., paragraph 372.
14 id., paragraph 389.
15 id., paragraph 422.
16 See, for example, Ross; Llamzon 2008, pages 210–211.
17 See, for example, Llamzon, page 227; Hwang and Lim, pages 8–14.
18 See note 5.
19 See, for example, Vladislav Kim et al v. Republic of Uzbekistan, ICSID Case No. ARB/13/6, Decision on Jurisdiction, 8 March 2017 (Kim v. Uzbekistan); MOL Hungarian Oil & Gas Plc v. Republic of Croatia, UNCITRAL, PCA Case 2014-15, Award, 16 August 2014; EDF (Services) Ltd v. Romania, ICSID Case No. ARB/05/13, Award, 8 October 2009 (EDF v. Romania); Waguih Elie George Siag & Anor v. Arab Republic of Egypt, ICSID Case No. ARB/05/15, Award, 1 June 2009 (Siag v. Egypt); TSA Spectrum de
Corruption, Fraud and Abuse of Process in Investment Treaty Arbitration

Fraud, illegality, misrepresentation or breach of good faith

To date, at least nine tribunals have dismissed investor–state claims on the basis of fraud, illegality, misrepresentation or breach of good faith. 20 Three are discussed herein, together with one case where the tribunal found that the investor had ‘cured’ the relevant illegality.


The claimant alleged expropriation of its contractual rights in relation to vehicle inspection services, awarded in a public bid process. The state objected to jurisdiction on the basis of alleged fraud.

The tribunal found that the claimant’s contract bid was based on forged financial documents regarding its financial condition, intentional misrepresentation of its experience

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(1) Société d’Investigation de Recherche et d’Exploitation Minière v. Burkina Faso, ICSID Case No. ARB/97/1, Award, 19 January 2000 (SIREXM v. Burkina Faso); (2) Inceya Vallisoletana, SL v. Republic of El Salvador, ICSID Case No. ARB/03/26, Award, 2 August 2006 (Inceysa v. El Salvador); (3) Fraport AG Frankfurt Airport Services Worldwide v. Republic of the Philippines, ICSID Case No. ARB/03/25, Award, 16 August 2007 (Fraport v. Philippines Award I), Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide, 23 December 2010 (Fraport v. Philippines Annulment Decision); Fraport AG Frankfurt Airport Services Worldwide v. Republic of the Philippines, ICSID Case No. ARB/11/12, Award, 10 December 2014 (Fraport v. Philippines Award II); (4) Plama Consortium Limited v. Republic of Bulgaria, ICSID Case No. ARB/03/24, Award, 27 August 2008 (Plama v. Bulgaria); (5) Anderson et al v. Republic of Costa Rica, ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010 (Anderson v. Costa Rica); (6) Saba Fakes v. Republic of Turkey, ICSID Case No. ARB/07/20, Award, 14 July 2010 (Saba Fakes v. Turkey); (7) Libananco Holdings Co Ltd v. Republic of Turkey, ICSID Case No. ARB/06/8, Award, 2 September 2011 (Libananco v. Turkey) (part of a series of claims against Turkey; the other claims are discussed below in relation to abuse of process); (8) Valeri Belokon v. Kyrgyz Republic, UNCITRAL, Award, 24 October 2014 (Belokon v. Kyrgyz Republic Award) (dismissing the State’s allegation of money laundering on the basis of insufficient proof) and Cour D’Appel de Paris, No. 15/01650, 21 February 2017 (Belokon v. Kyrgyz Republic Court Decision) (setting aside the award on public policy grounds, finding that there was sufficient evidence of money laundering), D Charlotin, ‘BIT Award against Kyrgyzstan annulled in Paris, with court giving weight to money-laundering allegations that had earlier failed to persuade arbitrators’, Investment Arbitration Reporter, 23 February 2017 (the state gathered additional evidence of the illegal activities between the award and the court ruling); (9) Hesham Talat M. al-Warrag v. Republic of Indonesia, UNCITRAL, Final Award, 15 December 2014. See also, for example, KRIC v. Jordan Social Security Investment Fund, Award, August 2015 (LCIA arbitration against state fund dismissed on the basis of fraud in relation to the underlying share purchase deal; related ICSID and UNCITRAL claims were then discontinued) (not publicly available, but discussed in K Karadelis, ‘Jordan wins LICA case over share sale “fraud”’, Global Arbitration Review, 25 August 2015, https://globalarbitrationreview.com/article/1034714/jordan-wins-lcia-case-over-share-sale-%E2%80%98fraud%E2%80%99 (accessed 10 January 2018)); Lighthouse Corporation Pty Ltd and Anor v. Democratic Republic of Timor-Leste, ICSID Case No. ARB/15/2, Award, 22 December 2017 (tribunal declined jurisdiction on the basis of lack of consent to submit the dispute to ICSID arbitration; the state argued that key email evidence was fabricated by the claimant, but the tribunal did not make any express findings of fraud).
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and qualifications, and concealment of its relationship with another bidder.\(^{21}\) The tribunal held that it had no jurisdiction on the basis of, *inter alia*, lack of consent, fraud, illegality, international public policy and lack of good faith:

\[
\text{[T]he foreign investor cannot seek to benefit from an investment effectuated by means of one or several illegal acts and, consequently, enjoy the protection granted by the host State, such as access to international arbitration to resolve disputes, because it is evident that its act had a fraudulent origin and, as provided by the legal maxim, “nobody can benefit from his own fraud”.}
\]

By falsifying the facts, Inceysa violated the principle of good faith from the time it made its investment and, therefore, it did not make it in accordance with Salvadorian law. Faced with this situation, this Tribunal can only declare its incompetence to hear Inceysa’s complaint, since its investment cannot benefit from the protection of the BIT, as established by the parties during the negotiations and the execution of the agreement.

\[
\text{It is not possible to recognize the existence of rights arising from illegal acts, because it would violate the respect for the law which . . . is a principle of international public policy.}^{22}
\]

Although the relevant BIT did not expressly require an investment to be made ‘according to law’, the tribunal considered correspondence exchanged during the negotiation of the treaty and determined that the state parties intended to exclude investments in contravention of the host state’s laws from the scope of the BIT.\(^{23}\) The tribunal ordered the claimant to pay the costs of the proceedings, while each party was responsible for its own legal fees.\(^{24}\)

**Plama v. Bulgaria (2008)**

The claimant alleged expropriation and other breaches of the Energy Charter Treaty (ECT) in relation to an oil refinery. The state objected to jurisdiction on the basis that, *inter alia*, the claimant ‘obtained its investment . . . via misrepresentations in violation of Bulgarian law’.\(^{25}\)

In the jurisdictional phase, the tribunal reserved its decision on this issue, and ‘join[ed] the issue of misrepresentation to the consideration of the merits of the case’.\(^{26}\) The tribunal ultimately dismissed the claim, on the bases that the investment was obtained through fraud and misrepresentation, in breach of the principle of good faith and international public policy, and contrary to Bulgarian and international law:

\[
\text{The investment . . . was, therefore, the result of a deliberate concealment amounting to fraud, calculated to induce the Bulgarian authorities to authorize the transfer of shares to an entity that did not have the financial and managerial capacities required to resume operation of the Refinery . . . . [T]his behavior is contrary to other provisions of Bulgarian law and to international law and . . . it, therefore, precludes the application of the protections of the ECT.}
\]


\(^{22}\) id., paragraphs 234, 239, 242, 249 and 335–337.

\(^{23}\) id., paragraph 195.

\(^{24}\) id., paragraph 338. A decision on rectification was issued in November 2006, but is not public.

\(^{25}\) *Plama v. Bulgaria*, paragraph 96.

\(^{26}\) Decision on Jurisdiction, 8 February 2005, paragraphs 229–230.
Granting the ECT’s protections to Claimant’s investment would be contrary to the principle nemo auditur propriam turpitudinem allegans [27] . . . It would also be contrary to the basic notion of international public policy – that a contract obtained through wrongful means (fraudulent misrepresentation) should not be enforced by a tribunal.

. . . The Tribunal finds that Claimant’s conduct is contrary to the principle of good faith which is part not only of Bulgarian law . . . but also of international law. [28]

The tribunal reached this conclusion even though the ECT ‘does not contain a provision [expressly] requiring the conformity of the Investment with a particular law’. [29] The tribunal ordered the investor to pay over US$7 million of the state’s legal fees and costs. [30]

**Anderson v. Costa Rica (2010)**

The claimant alleged that the state failed ‘to provide proper vigilance and regulatory supervision over the national financial system’. [31] The state objected to jurisdiction on the basis that, *inter alia*, there was no investment, as the claimants had invested money in what turned out to be an illegal ‘Ponzi scheme’ run by two brothers (the Villalobos brothers). [32]

The tribunal dismissed the claim on the basis of lack of jurisdiction *ratione materiae*. The tribunal noted that the BIT expressly required all investments to be ‘made’ or ‘owned’ in accordance with the law, and this requirement had to be met ‘regardless of [the investor’s] knowledge of the law or his or her intention to follow the law’. [33] The tribunal found that the Villalobos brothers engaged in financial intermediation without the authorisation of the relevant state authority, the Central Bank, in contravention of Costa Rican law and the resulting acquisitions by the claimant were not legal:

> The entire transaction between the Villalobos brothers and each Claimant was illegal because it violated the Organic Law of the Central Bank. If the transaction by which the Villalobos acquired the deposit was illegal, it follows that the acquisition by each Claimant of the asset resulting from that transaction was also not in accordance with the law of Costa Rica. Although the Claimants may not have committed a crime by entering into a transaction with the Villalobos, the fact that they

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27 Nobody can benefit from his or her own wrong.
29 id., paragraphs 138–139. But see Anatolie Stati et al v. Republic of Kazakhstan, SCC Case No. V116/2010, Award, 19 December 2013, paragraph 812 (‘Respondent has also argued that Claimants’ investments were either illegal from the beginning or became so at a later stage. First, the Tribunal notes that the ECT contains no requirement in this regard. Indeed, if the contracting States had intended there to be such a requirement, they could have written it into the text of the Treaty. . . . This consideration is even more valid in view of the extremely detailed definition of investment and other details regulated in the ECT. At least with regard to jurisdiction, the Tribunal does not see where such a requirement could come from. Whether that aspect is also relevant for the merits of the case, will have to be examined later in this Award’), paragraph 1093 (rejecting the state’s claim of illegality, on the merits).
30 *Plama v. Bulgaria*, paragraph 324.
32 id., paragraphs 29–35.
33 id., paragraphs 51–53.
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Gained ownership of the asset in violation of the Organic Law of the Central Bank means that their ownership was not in accordance with the laws of Costa Rica and that therefore each of their deposits and resulting relationships with Villalobos did not constitute an “investment” under the BIT.34

The tribunal noted that this interpretation reflects ‘sound public policy’ and ‘sound investment practice’, and these investors had not undertaken sufficient due diligence before committing funds.35 The tribunal directed the parties to share the costs and fees of the arbitrators and ICSID, and to bear their own legal expenses.36

**Mamidoil v. Albania (2015)37**

The claimant commenced arbitration to resolve a dispute in relation to a lease in the country’s main port to build an oil storage container. The state objected to jurisdiction on the basis that the investor failed to acquire the necessary permits and the ‘purported investment . . . never acquired any legal status under Albanian law’.38

The tribunal dismissed the objections to jurisdiction, but ultimately found in favour of the state on the merits. On jurisdiction, the tribunal noted that the BIT expressly required legality of an investment, and that illegality of an investment may occur through breach of substantive law (i.e., ‘it does not comply with material norms regulating investments’) or procedural ‘norms and regulations’, such as fraud or corruption.39 The tribunal noted that ‘not every trivial, minor contravention of the law should lead to a refusal of jurisdiction’:

[The Tribunal] must strike a balance between two criteria. On the one hand, neither Claimant nor the Tribunal may presume that the host State waives its sovereignty and agrees to the arbitration of disputes when the investor made the investment in violation of its substantive or procedural legislation. On the other hand, States must not be allowed to abuse the process by scrutinizing the investment post festum with the intention of rooting out minor or trivial illegalities as a pretext to free themselves of an obligation. A State must act consistently with its obligations and not resist jurisdiction because it wants to escape the consequences of its standing agreement to arbitrate.40

In the circumstances of this case, the tribunal concluded that although the investment was originally made in violation of Albanian law, ‘the real issue is less one of the seriousness or triviality of the illegality but, rather, concerns finality’ because the state’s actions, including its offers to regularise or legalise the investment, were indications ‘that it was ready to disregard the illegality for the past, to suspend it for the present and to repair it for the future’.41 The tribunal concluded:

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34 id., paragraph 55.
35 id., paragraph 58. See also paragraph 22 (the investors did ‘little investigation and research’ and were ‘[d]rawn by the high interest rates and confidential nature of the scheme’).
36 id., paragraph 66.
38 id., paragraph 324.
39 id., paragraphs 372 and 378 (confirming that the ECT, an alternative basis for the claim, does not protect unlawful investments).
40 id., paragraph 483.
41 id., paragraph 493.

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It is true that a State cannot be expected to have consented to an arbitral dispute settlement mechanism for investments made in violation of its legislation. However, it can be expected to accept the jurisdiction of an arbitral tribunal when, in that State's own appreciation, the illegality of the investment was susceptible of being cured, as that State's legalization offers show.\textsuperscript{42}

In these circumstances, the tribunal found that it had jurisdiction to hear the case, but ultimately (by majority) rejected the claims on the merits.\textsuperscript{43} The illegality issue was thus not 'outcome-determinative' in this case, but it is included in this chapter in light of the unusual factual scenario (illegality cured by subsequent state conduct).

\textit{Commentary}

\textit{a} When an investor commits fraud, misrepresents material facts, violates the law of the host state or international law, or does not act in good faith, tribunals will generally dismiss the claim on jurisdictional or admissibility grounds or, less commonly, during the merits phase.\textsuperscript{44}

\textit{b} Tribunals will dismiss the claim even where the relevant treaty does not expressly require an investment to be made in good faith, or in accordance with the law of the host state or international law.\textsuperscript{45}

\textit{c} Tribunals will generally not accept jurisdiction over an illegal investment, even if the investor was unaware of the illegal nature of the investment (\textit{Anderson v. Costa Rica}).

\textit{d} Tribunals may accept jurisdiction over an illegal investment if the state has subsequently 'cured' the illegality, or otherwise waived the illegality issue (\textit{Mamidoil v. Albania}).

\textsuperscript{42} id., paragraph 494.

\textsuperscript{43} id., paragraphs 495 and 839.

\textsuperscript{44} See, for example, \textit{Gustav F W Hamester GmbH & Co KG v. Republic of Ghana}, ICSID Case No. ARB/07/24, Award, 18 June 2010 (\textit{Hamester v. Ghana}), paragraph 127 ('The Tribunal considers that a distinction has to be drawn between (1) legality as at the initiation of the investment ("made") and (2) legality during the performance of the investment. Article 10 [regarding investments made prior to the treaty's entry into force] legislates for the scope of application of the BIT, but conditions this only by reference to legality at the initiation of the investment. Hence, only this issue bears upon this Tribunal's jurisdiction. Legality in the subsequent life or performance of the investment is not addressed in Article 10. It follows that this does not bear upon the scope of application of the BIT (and hence this Tribunal's jurisdiction) – albeit that it may well be relevant in the context of the substantive merits of a claim brought under the BIT. Thus, on the wording of this BIT, the legality of the creation of the investment is a jurisdictional issue; the legality of the investor's conduct during the life of the investment is a merits issue'); \textit{Phoenix Action Ltd v. The Czech Republic}, ICSID Case No. ARB/06/5, Award, 15 April 2009 (\textit{Phoenix Action v. Czech Republic}), paragraph 104 ('There is no doubt that the requirement of the conformity with law is important in respect of the access to the substantive provisions on the protection of the investor under the BIT. This access can be denied through a decision on the merits. However, if it is manifest that the investment has been performed in violation of the law, it is in line with judicial economy not to assert jurisdiction'). But see \textit{South American Silver Limited v. Bolivia}, PCA Case No. 2013-15, Award, 22 November 2018, paragraph 453 ('Bolivia has not shown that the clean hands doctrine is part of international public policy or constitutes a principle of international law').

In assessing the legality of an investment, tribunals generally consider:

- the timing of the illegality;
- the ‘materiality’ of the illegality;\(^{46}\)
- whether denial of jurisdiction would be proportionate to the illegality;\(^{47}\) and
- whether the illegality, if known to the state, would have prevented the investment from occurring, applying some form of causation analysis.\(^{48}\)

Some tribunals have distinguished between illegality in procuring the investment, which is generally considered an issue of jurisdiction or admissibility, and illegality in operating the investment, which is generally considered an issue for the merits.\(^{49}\)

Where tribunals have found illegality, fraud, misrepresentation or a breach of good faith, the claimant is generally ordered to pay all or part of the state’s costs.\(^{50}\)

### iii Abuse of process

To date, at least 12 tribunals have dismissed investor–state claims on the basis of abuse of process (also known as ‘abuse of right’).\(^{51}\) Six are discussed herein.

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\(^{46}\) See also *Hochtief Aktiengesellschaft v. Argentine Republic*, ICSID Case No. ARB/07/31, Decision on Liability, 29 December 2014, paragraph 199 (‘not every technical infraction of a State’s regulations associated with an investment’ will constitute illegality); *Peter A Allard v. The Government of Barbados*, PCA Case No. 2012-06, Award on Jurisdiction, 13 June 2014, paragraph 94 (non-compliance with the Exchange Control Act was an inadvertent and technical breach of local law, and did not involve breach of fundamental legal principles of the state); *ECE Projektmanagement International GmbH & Anor v. Czech Republic*, PCA Case No. 2010-5, Award, 19 September 2013 (*ECE v. Czech Republic*), paragraph 3.170 (distinguishing between cases of fraud or corruption and a failure to comply with construction code rules, and noting that the latter is not of the same order of gravity); *Tokios Tokeles v. Ukraine*, ICSID Case No. ARB/02/18, Decision on Jurisdiction, 29 April 2004, paragraph 86 (‘minor errors’ do not constitute illegality).

\(^{47}\) See, for example, *Kim v. Uzbekistan* (majority decision), paragraph 541 (‘Respondent either has failed to establish that Claimants acted in noncompliance with various laws or that such acts of noncompliance do not result in a compromise of an interest that justifies, as a proportionate response, the harshness of denying application of the BIT’); see also Carmen Martinez Lopez and Lucy Martinez, ‘Proportionality in Investment Treaty Arbitration And Beyond: An “Irresistible Attraction”?’ *BCDR International Arbitration Review* No. 2 (2015) pages 1–28.

\(^{48}\) See, for example, *Inceya v. El Salvador*, paragraph 338; *SIREXM v. Burkina Faso*, paragraphs 5.29 and 5.33; *Hamester v. Ghana*, paragraph 135.

\(^{49}\) See, for example, *Hamester v. Ghana*, paragraph 127 (see note 44); *Fraport v. Philippines Award I*, paragraph 345; *Copper Mesa Mining Corporation v. Republic of Ecuador*, PCA Case No. 2012-2, Award (Redacted), 15 March 2016, paragraph 5.54; *Oxus Gold plc v. Republic of Uzbekistan*, UNCITRAL, Final Award, 17 December 2015, paragraphs 706–707; *ECE v. Czech Republic*, paragraphs 3.165 to 3.168.

\(^{50}\) See, for example, *Inceya v. El Salvador*, paragraph 338; *Fraport v. Philippines Award II*, paragraph 530; *Plama v. Bulgaria*, paragraph 324; *Saba Fakes v. Turkey*, paragraph 154.

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Phoenix Action v. Czech Republic (2009)

The claimant alleged expropriation in relation to metal companies. Ownership of these companies was transferred from Czech nationals to the Israeli claimant while disputes involving these companies were pending before Czech courts. The state objected to jurisdiction on the basis of, *inter alia*, there being no ‘investment’ within the meaning of the ICSID Convention or the BIT; and the claimant’s ‘abuse of a corporate structure’.

The tribunal dismissed the claim on the basis of lack of jurisdiction, concluding that: ‘only investments that are made in compliance with the international principle of good faith and do not attempt to misuse the system are protected’; and an investment made ‘not for the purpose of engaging in economic activity, but for the sole purpose of bringing international litigation against the [state]’ was not a ‘good faith’ investment and therefore was not entitled to protection:

> The purpose of the international mechanism of protection of investment through ICSID arbitration cannot be to protect investments made in violation of the laws of the host State or investments not made in good faith, obtained for example through misrepresentation, concealments or corruption, or amounting to an abuse of the international ICSID arbitration system. In other words, the purpose of international protection is to protect legal and bona fide investments.

States cannot be deemed to offer access to the ICSID dispute settlement mechanism to investments not made in good faith. The protection of international investment arbitration cannot be granted if such protection would run contrary to the general principles of international law, among which the principle of good faith is of utmost importance.

The Tribunal is concerned here with the international principle of good faith as applied to the international arbitration mechanism of ICSID. The Tribunal has to prevent an abuse of the system of international investment protection under the ICSID Convention, in ensuring that only investments that are made in compliance with the international principle of good faith and do not attempt to misuse the system are protected.

The tribunal considered that ‘the whole “investment” was an artificial transaction to gain access to ICSID’, was not *bona fide*, and was an abuse of process:

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53 id., paragraphs 38 and 40.
54 *id.*, paragraphs 113, 142–143 and 145, *Contra Saba Fakes v. Turkey*, paragraphs 104, 112–113 (noting the decision in Phoenix Action but holding that ‘good faith’ was not incorporated into the definition of ‘investment’ for the purposes of Article 25(1) of the ICSID Convention).
55 *Phoenix Action v. Czech Republic*, paragraphs 100, 106 and 113 (emphasis in original).
The abuse here could be called a “détournement de procédure”, consisting in the Claimant’s creation of a legal fiction in order to gain access to an international arbitration procedure to which it was not entitled. . . . The conclusion of the Tribunal is therefore that the Claimant’s initiation and pursuit of this arbitration is an abuse of the system of international ICSID investment arbitration.56

The tribunal ordered the claimant to bear all the costs and fees of the state.57

This appears to be the first investor–state decision dismissing a claim based on abuse of process.58

**Europe Cement v. Turkey (2009) and CNH v. Turkey (2009)**

These cases relate to hydroelectric plants repossessed by the state in 2003.59 In both cases, the claimants originally alleged that, prior to their repossession, they were non-Turkish investors. However, both cases were ‘unusual’ in that the parties eventually agreed that the case should be dismissed for lack of jurisdiction, albeit differing on the reasons for this request.60 In both cases, the tribunals found that the true claimants were Turkish nationals (the Uzan family) improperly trying to obtain the protection of the ECT by backdating share transfer transactions and other documents purporting to show timely ownership.61

The tribunal in *Europe Cement v. Turkey* found that ‘the claim to ownership of the shares at a time that would establish jurisdiction was made fraudulently.’62 The tribunal found that ‘there was in fact no investment at all, at least at the relevant time, and the lack of good faith is in the assertion of an investment on the basis of documents that according to the evidence presented were not authentic.’63 The tribunal concluded that the claimant had not acted in good faith and had committed an abuse of process, although this finding was not, strictly speaking, necessary, as the tribunal had already concluded that there was no ‘investment’:

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56 id., paragraphs 143–144.
57 id., paragraph 152.
58 In terms of precedents for lifting the corporate veil, see, for example, *Barcelona Traction, Light and Power Co Ltd (Belgium v. Spain)*, 1970, I.C.J. 3, paragraph 56 (‘the veil is lifted, for instance, to prevent the misuse of the privileges of legal personality, as in certain cases of fraud or malfeasance . . . or to prevent the evasion of legal requirements or of obligations’). In relation to the origins of abuse of process, see, for example, Hersch Lauterpacht, *The Development of International Law by the International Court*, London, 1958, page 164 (‘There is no right, however well established, which could not, in some circumstances, be refused recognition on the ground that it has been abused’); Vaughan Lowe, ‘Overlapping Jurisdiction in International Tribunals’, AYBIL, volume 20, 1999, page 203 (abuse of process ‘relates to the good order of judicial proceedings. [It] is common to all the major legal systems, and may be properly applied by a tribunal in any legal system, including the international legal system, in the exercise of the tribunal’s competence to regulate its own proceedings’). See also *Societe Generale iro DR Energy Holdings Limited and Empresa Distribuidora de Electricidad del Este, S.A. v. Dominican Republic*, UNCITRAL, LCIA Case No. UN7927, Award on Preliminary Objections to Jurisdiction, 19 September 2008, paragraph 110 (noting the need for a ‘bona fide transaction’).
59 The third case in this trifecta is *Libananco v. Turkey*, which was also dismissed on the basis of investor misconduct (misrepresentation), but not on the basis of abuse of process.
60 *CNH v. Turkey*, paragraph 109; *Europe Cement v. Turkey*, paragraph 81.
61 *CNH v. Turkey*, paragraphs 122–28; *Europe Cement v. Turkey*, paragraphs 141–144; see also *Libananco v. Turkey* paragraphs 150, 249–251; *Kemal Uzan & Ors v. Turkey*, ECHR Application No. 18240/03, Judgment, 29 March 2011 (dismissing the claim as manifestly ill-founded).
63 id., paragraph 175.
If, as in Phoenix, a claim that is based on the purchase of an investment solely for the purpose of commencing litigation is an abuse of process, then surely a claim based on the false assertion of ownership of an investment is equally an abuse of process.\textsuperscript{64}

Similarly, in \textit{CNH v. Turkey}, the tribunal found that the claim was ‘fraudulent’ and an abuse of process because the claimant has ‘intentionally and in bad faith abused the arbitration; it purported to be an investor when it knew that this was not the case. This constitutes indeed an abuse of process’.\textsuperscript{65} The tribunal also found that the claimant’s conduct ‘fails to meet the requisite standard of good faith conduct. The claim is manifestly ill-founded’.\textsuperscript{66}

In both cases, the tribunals rejected the state’s requests for moral damages arising from the claimant’s abuse of process.\textsuperscript{67} However, the tribunals ordered the claimants (collectively) to pay the state’s legal fees, expenses and costs (approximately: US$5 million for CNH; US$4 million for \textit{Europe Cement}; plus US$15 million for the parallel \textit{Libananco} claim).\textsuperscript{68}

\textbf{Philip Morris v. Australia (2015)}

The claimant alleged expropriation and other breaches of international law in relation to tobacco ‘plain packaging’ measures. Ownership of the relevant assets was transferred to a Hong Kong company two months before the final state measure.\textsuperscript{69} The state objected to jurisdiction on the basis that, \textit{inter alia}, the claimant had restructured its corporate group with the principal aim of commencing BIT arbitration.

The tribunal found that the claims were inadmissible and thus it was ‘precluded’ from exercising jurisdiction; the test for abuse of right or process revolved ‘around the concept of foreseeability’; and a dispute is foreseeable when there is ‘a reasonable prospect’ that ‘a measure which may give rise to a treaty claim will materialise’.\textsuperscript{70} The tribunal found that this dispute was foreseeable at the time of the restructuring, and rejected the claimant’s assertion that the restructuring had been for tax or other business reasons.\textsuperscript{71}

The tribunal concluded that:

\begin{quote}
[T]he commencement of treaty based investor-state arbitration constitutes an abuse of right (or abuse of process) when an investor has changed its corporate structure to gain the protection of an investment treaty at a point in time where a dispute was foreseeable.\textsuperscript{72}
\end{quote}

\begin{thebibliography}{99}
\bibitem{64} id.
\bibitem{65} \textit{CNH v. Turkey}, paragraph 159.
\bibitem{66} id., paragraph 157.
\bibitem{67} \textit{Europe Cement v. Turkey}, paragraph 181 (‘the Tribunal need not go this far as it does not consider that exceptional circumstances such as physical duress are present in this case to justify moral damages’); \textit{CNH v. Turkey}, paragraph 170 (‘the Respondent requests, in the case at hand, that the Arbitral Tribunal grant compensation for moral damages based merely on a general principle, i.e., abuse of process. It is doubtful that such a general principle may constitute a sufficient legal basis for granting compensation for moral damages’).
\bibitem{68} \textit{CNH v. Turkey}, paragraph 178; \textit{Europe Cement v. Turkey}, paragraph 186; \textit{Libananco v. Turkey}, paragraph 569.
\bibitem{69} \textit{Philip Morris v. Australia}, paragraphs 163–165.
\bibitem{70} id., paragraphs 554, 567–569 and 588.
\bibitem{71} id., paragraph 584.
\bibitem{72} id., paragraph 585.
\end{thebibliography}
In relation to costs, the tribunal ordered the claimant to bear at least some of the costs of the arbitration; the exact amount is unknown as the costs award is redacted. 73 The tribunal stated: ‘While a finding of abuse of right does not imply any bad faith on the part of a claimant . . . a respondent State that faces an abuse of right should, in principle, not be burdened with the costs of defending itself against such a claim.’ 74

**Ampal v. Egypt (2016)**

Various corporate and individual claimants commenced a number of UNCITRAL, ICSID and International Chamber of Commerce arbitrations in parallel under various BITs and contracts, to resolve a dispute in relation to a gas pipeline in Egypt. 75 The state objected to jurisdiction in the ICSID case on the basis of, *inter alia*, abuse of process. 76

In November 2015, the UNCITRAL tribunal apparently upheld jurisdiction over the claim under the Egypt–Poland BIT. 77 In February 2016, the ICSID tribunal (hearing the claim under the Egypt–US and Egypt–Germany BITs) found that, in one specific circumstance, pursuit of the two parallel BIT proceedings with overlapping claims ‘crystallized’ an abuse of process, but emphasised that there was no bad faith and the parallel proceedings were not abusive *per se*.

The Tribunal agrees with the Respondent that the four parallel arbitration[s] with, essentially, the same factual matrix, the same witnesses and many identical claims may look abusive. However, subject to one important qualification . . . the Tribunal is not persuaded that the four arbitral proceedings collectively or individually amount to an abuse of process.

It is possible, as a jurisdictional matter, for different parties to pursue distinct claims in different fora seeking redress for loss allegedly suffered by each of them arising out of the same factual matrix . . . None of the four arbitrations at issue here is, *per se*, an abuse. It may not be a desirable situation but it cannot be characterized as abusive especially when the Respondent has declined the Claimants’ offers to consolidate the proceedings.

However, there is one important exception to this finding of the Tribunal. It concerns the overlap of claims by Mr. Maiman in the present case and the UNCITRAL arbitration (the two treaty cases) for the recovery of the same sum.

. . . This is tantamount to double pursuit of the same claim in respect of the same interest. In the Tribunal’s opinion, while the same party in interest might reasonably seek to protect its claim in two fora where the jurisdiction of each tribunal is unclear, once jurisdiction is otherwise confirmed, it would crystallize in an abuse of process for in substance the same claim is to be pursued on the merits before two tribunals. However, the Tribunal wishes to make it very clear that this resulting abuse of

73 *Philip Morris v. Australia*, UNCITRAL PCA Case No. 2012-12, Final Award Regarding Costs, 8 March 2017 (redacted).
74 *id.*, paragraph 60.
75 *id.*, paragraph 12.
76 *id.*, paragraph 312. The state also objected on the basis of alleged illegality and corruption. The tribunal noted: ‘It is a well-established principle of international law that a tribunal constituted on the basis of an investment treaty has no jurisdiction over a claimant’s investment which was made illegally in violation of the laws and regulations of the Contracting State.’ *id.*, paragraph 301. However, the tribunal found that the state had failed to discharge its burden of proof on this issue, as discussed further in Part IV.
77 *id.*, paragraphs 12(iii), 332–333; see also *Yosef Maiman & Ors. v. Arab Republic of Egypt*, UNCITRAL PCA Case No. 2012-26, Decision on Jurisdiction and Admissibility, 5 May 2016 (not publicly available).
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process is in no way tainted by bad faith on the part of the Claimants as alleged by the Respondent. It is merely the result of the factual situation that would arise were two claims to be pursued before different investment tribunals in respect of the same tranche of the same investment.78

The ICSID tribunal invited the claimants to ‘cure’ the abuse of process by electing to pursue their claims before either the UNCITRAL tribunal or the ICSID tribunal.79 The ICSID claimants then withdrew a portion of their claims in the parallel UNCITRAL arbitration, and thus ‘cured’ the abuse of process.80 The commercial arbitration claims also proceeded under the relevant contracts.

Churchill Mining v. Indonesia (2016)

The claimants commenced arbitration to resolve a dispute in relation to coal mines. The state asked the tribunal to dismiss all claims on the basis that the survey mining licences and related approvals were forged and fabricated, and the upgrade to exploitation licences was secured through deception and fraud.81

The tribunal noted that the ICSID Convention and the relevant BITs did not ‘address . . . the consequences of unlawful conduct by claimant . . . during the performance of an investment’ and the BITs only contained ‘admission requirements applying at the time of establishment of an investment’.82 The tribunal thus considered general principles of international law to determine the consequences of the forgeries, and found the claims to be inadmissible as a matter of international public policy and as they were an abuse of process:

[Cl]aims arising from rights based on fraud or forgery which a claimant deliberately or unreasonably ignored are inadmissible as a matter of international public policy.

[T]he Tribunal cannot but hold that all the claims before it are inadmissible. This conclusion derives from the facts analyzed above, which demonstrate that the claims are based on documents forged to implement a fraud aimed at obtaining mining rights . . . the seriousness, sophistication and scope of the scheme are such that the fraud taints the entirety of the Claimants’ investment . . . As a result, the general principle of good faith and the prohibition of abuse of process entail that the claims before this Tribunal cannot benefit from investment protection under the Treaties and are, consequently, deemed inadmissible.83

78 Ampal v. Egypt, paragraphs 328–331.
79 id., paragraph 334–339.
80 Ampal v. Egypt, Decision on Liability and Heads of Loss, 21 February 2017, paragraph 22.
81 Churchill Mining v. Indonesia, paragraph 106.
82 id., paragraph 488.
83 id., paragraphs 508 and 528.
In reaching this conclusion, the tribunal emphasised the seriousness of the fraud, and the claimants’ lack of due diligence overseeing the licensing process and forgery allegations. The tribunal ordered the claimants to pay 75 per cent of the state’s expenses, plus the full tribunal and ICSID costs.

Commentary

a. When an investor commits an abuse of process, tribunals will generally dismiss the claim on jurisdictional or admissibility grounds, or, less commonly, during the merits phase.

b. Tribunals will generally dismiss the claim even when the relevant treaty does not refer to ‘abuse of process’ (which most treaties do not).

c. Abuse of process generally ‘denotes conduct that is not prima facie illegal’. Thus, abuse of process is distinct from illegality as an objection to jurisdiction or admissibility, but overlaps with the notion of conduct that is not in good faith. Cases that were decided solely on ‘good faith’ grounds before 2009 would perhaps also now be decided on ‘abuse of process’ grounds.

d. Tribunals generally recognise a distinction between abuse of process and procedural abuse (also known as due process abuse), such as a pre-hearing ‘document dump’.

e. To date, tribunals have found an abuse of process in three situations: (1) claimants attempting to establish international jurisdiction under an investment treaty by transfer of ownership or corporate restructuring while a dispute is pending or foreseeable (Philip Morris v. Australia) (this is separate from, but potentially overlaps with, ratiocination issues); (2) claimants pursuing parallel proceedings in different international forums involving essentially the same dispute (Ampal v. Egypt; Orascom v. Algeria); or (3) false or fraudulent assertions of ownership, involving forged documents (CNH v. Turkey; Europe Cement v. Turkey; Churchill Mining v. Indonesia).

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84 id., paragraph 509. See also id., paragraph 515 (‘the acts of forgery brought to light in these proceedings are of a particularly serious nature in light of the number and nature of forged documents and of the aim pursued, namely to orchestrate, legitimize and perpetuate a fraudulent scheme to gain access to valuable mining rights’), paragraphs 516 and 527 (‘The seriousness of the fraud just discussed is compounded by the Claimants’ lack of diligence . . . Claimants’ absence of diligence became apparent in the present proceedings when they filed or produced 34 forged documents to support their claims’).

85 id., paragraphs 553–556. The claimants’ application to annul the award was recently dismissed with costs, although the annulment decision is not yet public. See https://www.iareporter.com/articles/analysis-churchill-planter-mining-v-indonesia-annulment-committee-finds-that-parties-discovery-obligations-can-be-limited-by-domestic-law-on-confidentiality-and-that-procedural-orders-are/ (accessed 25 March 2019, subscription required).

86 Gaillard, page 2.

87 Phoenix Action v. Czech Republic; CNH v. Turkey; Europe Cement v. Turkey; Churchill Mining v. Indonesia.

88 Gaillard, page 2 (‘while it is not uncommon for a party to an arbitration to file large numbers of documents immediately before the start of an evidentiary hearing in order to hinder its opponent’s preparations and one might loosely refer to this conduct as “abusive”, such conduct should be properly characterized as a violation of due process and can be remedied under existing procedural rules, for example by a decision that such documents are inadmissible’).
In relation to bullet (e), point (1), the line between legitimate corporate restructuring and ‘abuse of process’ can be difficult to distinguish. One key issue is whether the dispute is ‘actual’, ‘foreseeable’, ‘highly probable’ or ‘crystallized’.

Tribunals will also consider:
- the timing of the investment;
- the timing of the claim;
- the substance of the transaction;
- the true nature of the operation, for example, any ‘economic activity in the market place’, business plan, refinancing programme and economic objectives; and
- the degree of foreseeability of the government action.

Tribunals should be cautious in labelling corporate restructuring an ‘abuse of process’.

In some circumstances, the abuse of process may be ‘cured’ by the claimant (Ampal v. Egypt) (similar to an illegality being ‘cured’ or ‘waived’ by the state, as discussed above, Mamidoil v. Albania).

To date, no tribunal has awarded moral damages to the state arising from an abuse of process, although it has been requested on at least two occasions.

Most tribunals award full or partial costs to the state, when dismissing a case on the basis of abuse of process.

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89 See, for example, Pac Rim Cayman v. The Republic of El Salvador, ICSID Case No. ARB/09/12, Decision on the Respondent's Jurisdictional Objections, 1 June 2012, paragraph 2.99 (the dividing-line occurs when the relevant party can see an actual dispute or can foresee a specific future dispute as a very high probability and not merely a possible controversy. . . . [T]his dividing-line will rarely be a thin red line, but will include a significant grey area; the tribunal went on to reject the state’s argument that the restructuring was an abuse of process); Levy v. Peru, paragraphs 185–189; Gaillard, page 4 (‘[a]buse of process will arise where a corporate claimant makes or restructures its investment in order to gain access to a dispute with the host State that is foreseeable, but may not yet have crystallized’).

90 See, for example, Phoenix Action v. Czech Republic, paragraphs 135–144; Transglobal v. Panama, paragraphs 102–103.

91 See note 67.

92 See, for example, Churchill Mining v. Indonesia, paragraph 556 (claimants to bear 75 per cent of the state’s costs, US$8.64 million); Levy v. Peru, paragraphs 201–202 (claimants to pay entire administrative costs plus contribute US$1.57 million to the state’s legal fees and expenses); Transglobal v. Panama, paragraphs 126–127 (claimants to pay almost all costs and fees of the arbitration); CNH v. Turkey, paragraphs 177–178 (claimants to bear all ICSID costs, plus around US$5 million of the state’s legal costs). Contra Capital Holdings v. Cameroon, paragraphs 481–482 (ordering the claimant to pay the arbitration costs, but each party to bear their own legal costs).
III TIMING OF THE CHALLENGE

In ICSID arbitrations, a respondent state may raise a challenge on the basis of alleged claimant misconduct at virtually every stage of the proceedings.93

First, a respondent state may raise a preliminary objection pursuant to ICSID Rule 41, asking the tribunal to reject the claim as ‘manifestly without legal merit’.94

Second, the state may raise issues of investor misconduct as a jurisdictional or admissibility objection, pursuant to Article 41 of the ICSID Convention.95 At this point, the tribunal may bifurcate the proceedings, and render a decision on jurisdiction or admissibility only, or join jurisdictional issues to the merits.

Third, the state may raise the objection in the merits phase, for example, when evidence of investor misconduct emerges during cross-examination of a factual witness.96

Fourth and finally, a state may request revision or annulment of the award on the basis of investor misconduct, pursuant to Articles 51 and 52 of the ICSID Convention, as was done in Siemens v. Argentina. However, new allegations or evidence of investor misconduct may not be raised in the annulment phase.97

For non-ICSID arbitrations, the respondent state may, depending on the applicable arbitration rules, raise allegations of investor misconduct as a preliminary objection, in the merits phase, in applications for recognition and enforcement, or in challenges to the award.

IV PROVING MISCONDUCT – BURDEN AND STANDARD OF PROOF

Once a respondent state has raised a challenge based on investor misconduct, at whatever stage of the proceedings, the state must then prove that allegation – but the question of burden and standard of proof remains unsettled.98

i Burden of proof

Tribunals have adopted different approaches to determine the burden of proof for establishing investor misconduct. Generally, the burden of establishing the factual basis of the claim, as

93 The Secretary-General may also refuse to register a request for arbitration on the basis that the dispute is 'manifestly outside the jurisdiction of the Centre', pursuant to Article 36 of the ICSID Convention. To date, and unsurprisingly, it appears that no such refusals have been based on investor misconduct.

94 ICSID Arbitration Rules (2006), Rule 41(5); see, for example, Rachel S Grynberg & Ors. v. Grenada, ICSID Case No. ARB/10/6, Award, 10 December 2010, paragraphs 4.6.15–4.6.16 (state alleging, inter alia, abuse of process through attempt to relitigate a claim), 7.31–7.37 (tribunal noting that 'the initiation of the present arbitration is thus an improper attempt to circumvent the basic principles set out in Convention Article 53 and the procedures available for revision and rectification of awards provided for in Article 51', but not applying the 'abuse of process' label).

95 See, for example, Fraport v. Philippines Award I; Azpetrol v. Azerbaijan; African Holding v. Congo.

96 See, for example, EDF v. Romania; Siag v. Egypt; Rumeli v. Kazakhstan.

97 See, for example, RSM Production Corporation v. Grenada, ICSID Case No. ARB/05/14, Annulment Proceeding, Decision on the Application of RSM for a Preliminary Ruling, 7 December 2009, paragraphs 21–30 (no new evidence regarding alleged corruption in the annulment phase).

98 See also, for example, Oil Platforms Case (Iran v. United States), Judgment on the Merits, [2003] ICJ Reports 161, 6 November 2003, Separate Opinion of Judge Higgins, paragraph 33 ('Beyond a general agreement that the graver the charge the more confidence must there be in the evidence relied on, there is thus little to help parties appearing before the Court (who already will know they bear the burden of proof) as to what is likely to satisfy the Court').
a whole, is upon the claimant. However, when it comes to proving an individual factual allegation, the burden generally rests upon the party alleging the fact, whether claimant or respondent (*actori incumbit probatio*, ‘who asserts must prove’).99

Some commentators have suggested a ‘shifting burden’ of proof to these evidentiary issues, at least partly due to the difficulty of procuring evidence of fraud, corruption, illegality, abuse of process and other investor misconduct.100 In other words, the state makes a *prima facie* showing of misconduct, through witness statements or documentary evidence, and the burden then shifts to the claimant–investor to establish that it has met the relevant requirements (legality, good faith, non-abuse of process, etc.). However, some tribunals have expressly rejected this ‘shifting burden’ approach.101

### ii Standard of proof

The standard of proof for allegations of investor misconduct is also unsettled. Some tribunals apply a heightened standard of proof (e.g., ‘clear and compelling evidence’) or a more flexible standard that takes into account the difficulty of obtaining evidence of fraud, corruption and other improper conduct.

Cases endorsing a high standard of proof for allegations of investor misconduct include:

- **Siag v. Egypt**: the state alleged that the claimant fraudulently obtained a different nationality to manufacture treaty jurisdiction.102 Noting that ‘[i]t is common in most legal systems for serious allegations such as fraud to be held to a high standard of proof,’ the tribunal applied a ‘clear and convincing evidence’ standard, which is ‘greater than the balance of probabilities but less than beyond reasonable doubt’.103 The tribunal ultimately rejected the state’s allegations of fraud.104

- **EDF v. Romania**: the tribunal rejected the claimant’s allegations of attempted bribery by the state and adopted a ‘high standard of proof’.105 The tribunal asserted: ‘corruption must be proven and is notoriously difficult to prove since, typically, there is little or no

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99 See, for example, Military and Paramilitary Activities in and against Nicaragua (Nicaragua v. United States of America), Jurisdiction and Admissibility Judgment, 29 November 1984, ICJ Reports 1984, paragraph 101 (‘That a litigant seeking to establish a fact bears the burden of proving it is a commonplace, well-established in the jurisprudence’).

100 See, for example, Mills, page 9 (‘Because of the near impossibility to “prove” corruption, where there is a reasonable indication of corruption, an appropriate way to make a determination may be to shift the burden of proof to the allegedly corrupt party to establish that the legal and good faith requirements were in fact duly met’); see also Europe Cement v. Turkey, paragraphs 163–164 (referring to evidence of fraud adduced by the state, and noting that the claimants could have rebutted this inference – thus suggesting a shifting burden).

101 See, for example, Llamzon, paragraph 9.09; Siag v. Egypt, paragraphs 315–317 (‘As to the burden of proof, the general rule, well established in international arbitrations, is that the Claimant bears the burden of proof with respect to the facts it alleges and the Respondent carries the burden of proof with respect to its defences. . . . Egypt asserted that it had proved Mr Siag’s non-Lebanese nationality and that accordingly “the burden has shifted.” The Tribunal does not accept this latter submission. Because negative evidence is very often more difficult to assert than positive evidence, the reversal of the burden of proof may make it almost impossible for the allegedly fraudulent party to defend itself, thus violating due process standards. It is for this reason that Tribunals have rarely shifted the burden of proof’).

102 Siag v. Egypt, paragraphs 219–221.

103 id. paragraphs 325–326.

104 id., paragraph 358.

105 EDF v. Romania, paragraph 221.
physical evidence. The seriousness of the accusation of corruption in the present case, considering that it involves officials at the highest level of the Romanian Government at the time, demands clear and convincing evidence. There is general consensus among international tribunals and commentators regarding the need for a high standard of proof.\textsuperscript{106} The EDF tribunal concluded that the investor’s allegations of bribery had not been proven because the investor’s witness lacked credibility, relied on hearsay evidence, and was not ‘clear and convincing’.\textsuperscript{107}

c \textit{Hamester v. Ghana:} the tribunal ‘examine[d] whether the investment was illegal from its very inception’, and found that the state ‘ha[d] not fully discharged its burden of proof in this regard’.\textsuperscript{108} There was evidence that some invoices had been inflated, but there was no proof that these invoices induced the state to sign the relevant agreement or that the alleged fraud prevented the state from entering into the agreement.

d \textit{African Holding v. Congo:} the tribunal dismissed the state’s allegation of corruption, finding that this allegation was ‘very grave’, requiring ‘irrefutable evidence’ and a particularly high standard of proof ‘such as the evidence required for the investigation or criminal prosecution of corruption in countries where it is considered a criminal offense’.\textsuperscript{109}

e \textit{Kim v. Uzbekistan:} the tribunal (by majority) found that the state ‘has not proven, either to the standard of “clear and convincing evidence”, or “reasonable certainty” that the payment of US$3 million to Mr Bizakov was an act contrary to the international public policy against corruption thereby rendering the claim inadmissible. The Tribunal therefore denies Respondent’s objection to its jurisdiction on these grounds’.\textsuperscript{110}

Commentators have recognised some contradiction in this approach, which recognises that corruption and other investor misconduct is notoriously difficult to prove and yet sets a very high standard of proof.\textsuperscript{111} Perhaps in light of this contradiction, other tribunals have adopted a lower standard of proof. For example:

\textsuperscript{106} \textit{id.}

\textsuperscript{107} \textit{id.}, paragraphs 224 and 227.

\textsuperscript{108} \textit{Hamester v. Ghana}, paragraphs 131–134, paragraph 138 (‘Hamester’s practices might not be in line with what could be called “l’éthique des affaires,” but, in the Tribunal’s view, they did not amount, in the circumstances of the case, to a fraud that would affect the Tribunal’s jurisdiction. The Tribunal sees the over-statement of invoices as an issue bearing upon the balance of equities between the two parties, rather than the existence itself of the contract or the investment. Such elements would have been taken into consideration by the Tribunal when discussing the merits, if it had found that any compensation was due to Hamester’).

\textsuperscript{109} \textit{African Holding v. Congo}, paragraph 52 (unofficial translation from the original French text).

\textsuperscript{110} \textit{Kim v. Uzbekistan}, paragraph 614. See also \textit{Saba Fakes v. Turkey}, paragraphs 131, 135 (‘The Tribunal considers that the burden of proof of any allegations of impropriety is particularly heavy. This burden of proof was not met in the present case. Consequently, the Tribunal accepts the Claimant’s submission as to the dates of the transfer of the temporary certificates to the Claimant’; the tribunal ultimately concluded that the claimant did not hold legal title over the relevant certificates and thus did not have a protected investment).

\textsuperscript{111} See, for example, Partasides, paragraphs 42–44 (commenting on \textit{EDF v. Romania:} ‘[t]he tribunal is telling us that allegations of this type of illegality are by definition “notoriously” difficult to prove. Yet, it nevertheless proceeds to impose an enhanced standard of proof on the allegation. Its message is difficult to accept: “Dear investor, you will inevitably find the allegation almost impossible to prove, but we are nonetheless going to raise the evidential hurdle to make it even harder”. I fear this kind of juxtaposition...')
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a  *Europe Cement v. Turkey*: the tribunal accepted the allegation of investor misconduct, based on ‘circumstantial evidence’ and the claimant’s refusal to produce documents: ‘the Tribunal has no direct evidence that any particular document placed before it was or was not authentic, but the implication of lack of authenticity is overwhelming. . . . Indeed, the evidence points to the conclusion that the claim to ownership of the shares at a time that would establish jurisdiction was made fraudulently.’

b  *CNH v. Turkey*: the tribunal noted that it ‘cannot allow evidentiary perfection to be the enemy of common sense and judgment. There is ample evidence to conclude that the claimed transactions never occurred’.

c  *Fraport v. Philippines Award I*: the (first) tribunal rejected the claimant’s request to apply a criminal standard of proof (i.e., beyond reasonable doubt) in determining whether the investor had violated Philippine law in procuring its investment.

d  *Libananco v. Turkey*: the tribunal recognised that fraud was a serious allegation but held that it did not require a ‘heightened standard of proof’.

Other tribunals have simply referred to multiple potential standards of proof, without deciding which standard should be applied. For example:

a  *Ampal v. Egypt*: the tribunal dismissed the state’s allegations of illegality as follows: ‘whether the Tribunal applies a high standard of clear and convincing evidence or even a less demanding one or a combination thereof, in the circumstances, the Tribunal is not persuaded that the Claimants’ investment was procured illegally. The Respondent’s allegations are all based on innuendos. In sum, the Respondent has failed to discharge its burden of proof.’

b  *Metal-Tech v. Uzbekistan*: the tribunal noted that it had ‘relative freedom’ to determine the standard of proof in relation to allegations of corruption, because the BIT provided no instruction on this issue. The tribunal concluded:

> While the debate about standards of proof and presumptions is an interesting one, the Tribunal finds that it does not require the application of the rules on burden of proof or presumptions to resolve the present dispute. In this case, facts emerged in the course of the arbitration. Because those facts raised suspicions of corruption, the Tribunal required explanations.

> As in World Duty Free, the present factual matrix does not require the Tribunal to resort to presumptions or rules of burden of proof where the evidence of the payments came from the Claimant and the Tribunal itself sought further evidence of the nature and purpose of such payments. Instead, the

("The tribunal recognises that it is very difficult to prove corruption, but we are regardless going to make it even more difficult to prove") is precisely where international arbitral tribunals can show themselves to live in the most remote of ivory towers").

112  *Europe Cement v. Turkey*, paragraph 167.
113  *CNH v. Turkey*, paragraph 121.
114  *Fraport v. Philippines Award I*, paragraph 399.
115  *Libananco v. Turkey*, paragraph 125.
117  *Metal-Tech v. Uzbekistan*, paragraph 238.
Tribunal will determine on the basis of the evidence before it whether corruption has been established with reasonable certainty. In this context, it notes that corruption is by essence difficult to establish and that it is thus generally admitted that it can be shown through circumstantial evidence.\(^\text{118}\)

Based on this brief survey, it appears that there is currently no consensus among international tribunals and commentators regarding the burden and standard of proof for allegations of investor misconduct. More certainty in this important area would be welcome.

V REMEDIES FOR INVESTOR MISCONDUCT

Once misconduct is established, a tribunal has a number of options to sanction such conduct and to discourage future such claims, including:

\(\text{a} \) dismissing the claim for lack of jurisdiction or inadmissibility, on the basis that:

- the investment or investor was not protected by the relevant treaty;
- the investment or investor was not ‘made in accordance’ with law;
- there was no ‘consent’; or
- there was a breach of international or transnational public policy;\(^\text{119}\)

\(\text{b} \) awarding costs in favour of the state;\(^\text{120}\)

\(\text{c} \) awarding moral damages to the state;\(^\text{121}\)

\(\text{d} \) ordering security for costs;

\(\text{e} \) suspending the arbitration pending the resolution of criminal proceedings related to the misconduct; and

\(\text{f} \) permitting counterclaims by the sovereign state against the investor, depending on the terms of the relevant treaty.\(^\text{122}\)

In addition to seeking the above remedies from tribunals, states may anticipate and seek to address such claims by re-drafting the definitions of ‘investor’ and ‘investment’ in investment treaties expressly to preclude protection of investments made or operated in contravention of domestic or international law, or to require express approval from the relevant state for all investments to be protected by the treaty.\(^\text{123}\)

\(^{118}\) id., paragraphs 239 and 243.


\(^{120}\) See, for example, \textit{CNH v. Turkey}, paragraphs 158 (citing ICSID tribunals awarding costs against parties ‘as a sanction against what they see as dilatory or otherwise improper conduct in the proceedings’), 159 (‘the misconduct of an arbitration proceeding leads generally to the allocation of all costs on the party in bad faith’), 178; \textit{Plama v. Bulgaria}, paragraph 324; \textit{Phoenix Action v. Czech Republic}, paragraph 152; \textit{Inceysa v. El Salvador}, paragraph 338; \textit{Europe Cement v. Turkey}, paragraph 186 (all awarding fees or costs, partial or complete, in favour of the state).

\(^{121}\) See note 67.

\(^{122}\) See, for example, ICSID Convention, Article 46; ICSID Arbitration Rule 40(2).

\(^{123}\) See, for example, US Model BIT 2012, footnote 2, definition of ‘investment’ (‘Among the licenses, authorizations, permits, and similar instruments that do not have the characteristics of an investment are those that do not create any rights protected under domestic law’).
VI CONCLUSION

The number of investor–state cases involving investor misconduct (alleged or proven) remains relatively small. However, as the number of investment treaty arbitrations continues to rise, it is likely that cases involving investor misconduct will also increase. The cases discussed in this chapter provide useful lessons for all participants in investor–state arbitration.

Investors: make sure your ‘house is in order’ before coming to a tribunal with an investment treaty claim. Gather all evidence of a bona fide investment before initiating arbitral proceedings. Such evidence will be helpful on jurisdiction and admissibility issues, and on quantum.

States: be aware that there are unscrupulous, vexatious, frivolous and fraudulent claimants lurking in the penumbra of investor–state arbitration. It may be a long and expensive battle, but usually these claimants end up where they belong – out in the cold, without treaty protection and often subject to significant costs orders. Due diligence of potential investors, and potential claims, is of the utmost importance – carefully scrutinise their financial statements and qualifications, and raise any concerns in writing at the earliest opportunity.

Tribunals: be aware of these issues, and be ready to sanction investor misconduct – where it is proven. Also, be aware that states are increasingly raising allegations of investor misconduct, sometimes without foundation, and tribunals must be ready to dismiss frivolous allegations of investor misconduct (potentially with costs).

Investors, states and tribunals: do not succumb to the ‘culture of litigiousness’ that is pervading certain parts of investor–state (and commercial) arbitration. Address and resolve allegations of investor misconduct as expeditiously as possible.

Academics: this is a fertile area for further research. The authors (as practitioners, not academics) hope this modest contribution will provide a useful starting point for future discussion of these important issues.

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124 Gaillard, page 2.
Chapter 12

CHALLENGES TO ARBITRATORS UNDER THE ICSID CONVENTION AND RULES

Chloe J Carswell and Lucy Winnington-Ingram

I INTRODUCTION

The year 2018 saw a record number of disqualification proposals to arbitrators and ad hoc committee members alike within the International Centre for Settlement of Investment Disputes (ICSID) context.² Having regard to the public availability of decisions and this flurry of activity, this chapter will focus on challenges to arbitrators (and committee members) brought under the ICSID Convention. The chapter begins by setting out the grounds for disqualification under the ICSID Convention and Rules, before briefly detailing the prevailing legal standard as developed through ICSID jurisprudence. The majority of this chapter will be devoted to a discussion of three categories of alleged conflict,³ concentrating on the reasoning of publicly available decisions published during 2018.

II THE RULES

The main grounds for disqualification of arbitrators under the ICSID Convention are prescribed by Article 57, which provides that:

[a] party may propose to a Commission or Tribunal the disqualification of any of its members on account of any fact indicating a manifest lack of the qualities required by paragraph (1) of Article 14.

A party to arbitration proceedings may, in addition, propose the disqualification of an arbitrator on the ground that he was ineligible for appointment to the Tribunal under Section 2 of Chapter IV.

Reference to Section 2 of Chapter IV is to the nationality requirements for appointment under Articles 38 and 39 of the ICSID Convention. A third ground for disqualification is found in Rule 8 of the ICSID Arbitration Rules, which provides for a situation where an arbitrator becomes incapacitated or unable to perform the duties of his or her office.

The most commonly invoked ground for disqualification is a manifest lack of the qualities required by Article 14(1):

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¹ Chloe J Carswell is a partner and Lucy Winnington-Ingram is an associate at Reed Smith LLP.
² The ICSID website reports that there were a total of 10 disqualification proposals in 2018 (https://icsid.worldbank.org/en/Pages/process/Decisions-on-Disqualification.aspx).
³ These categories have been selected on the basis of their recurrent appearance in the publicly available disqualification decisions from 2018.

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persons designated to serve on the Panels shall be persons of high moral character and recognized competence in the fields of law, commerce, industry or finance, who may be relied upon to exercise independent judgment. Competence in the field of law shall be of particular importance in the case of persons on the Panel of Arbitrators.

It is well settled that although the English text of Article 14(1) refers only to ‘independent judgment’, this provision also contains a requirement of ‘impartiality’ (deriving from the equally authentic Spanish text).

In practice, applications for disqualification under Article 14(1) are almost always premised on an alleged lack of independence or impartiality, and it is on these types of challenges that this chapter will focus.

III THE LEGAL STANDARD UNDER THE ICSID CONVENTION

The legal standard for disqualification in the ICSID context has been closely considered in decisions on disqualification proposals and scholarly commentary. The authors do not propose to rehearse that commentary here in full, but rather note that recent decisions suggest a welcome shift in the direction of a consistent and predictable standard.

i The applicable legal standard is objective

In determining whether an arbitrator lacks impartiality or independence, it is well established that the test is objective. As put by the chair of the ICSID Administrative Council in *Blue Bank* and *Burlington*:

> the applicable legal standard is an “objective standard based on a reasonable evaluation of the evidence by a third party”. As a consequence, the subjective belief of the party requesting the disqualification is not enough to satisfy the requirements of the Convention.\(^4\)

This has been consistently reaffirmed, including by a number of decisions in 2018.\(^5\)

ii It is sufficient to establish the appearance of dependence or bias

In the case of *Amco*,\(^6\) the very first challenge to an arbitrator brought under the ICSID Convention in 1982, Indonesia sought the disqualification of the claimants’ appointed arbitrator on a number of grounds, including that he had provided tax advice to a principal

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4 See *Blue Bank International & Trust (Barbados) Ltd v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/12/20, Decision on the Parties’ Proposals to Disqualify a Majority of the Tribunal, 12 November 2013 (*Blue Bank*) paragraph 60; and *Burlington Resources Inc v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Decision on the Proposal for Disqualification of Professor Francisco Orrega Vicuña, 13 December 2013 (*Burlington*), paragraph 67.


6 *Amco Asia Corporation and others v. Republic of Indonesia*, ICSID Case No. ARB/81/1, Decision on Proposal to Disqualify an Arbitrator, 24 June 1982 (unpublished) (*Amco*).
shareholder in the claimants’ company after the commencement of the arbitration. Prior to this, his law firm also had a profit sharing arrangement with the claimants’ counsel. The unchallenged arbitrators are reported to have dismissed the proposal noting that proof of the existence of facts that indicated a lack of independence was insufficient without strict proof of actual bias. The standard of proof imposed in Amco was accordingly significantly higher than the ‘justifiable doubts’ standard typically adopted by other arbitral institutions and rules.

This decision was heavily criticised, and a majority of subsequent decisions have confirmed that Articles 57 and 14(1) do not require proof of actual dependence or bias; rather, it will be sufficient for a party to establish the appearance of dependence and bias. The next challenge, some 20 years later, was to the president of the ad hoc committee in the annulment proceedings in Vivendi I. In that case, the unchallenged committee members rejected the findings in the Amco decision, noting a proper interpretation of the standard of proof was analogous to that in Rule 3.2 of the International Bar Association (IBA) Code of Ethics, which refers to an ‘appearance of bias’.

The rationale for this lower standard was neatly summarised in the 2010 Urbaser decision:

> [t]he requirements of independence and impartiality serve the purpose of protecting the parties against arbitrators being influenced by factors other than those related to the merits of the case. In order to be effective this protection does not require that actual bias demonstrate a lack of independence or impartiality. An appearance of such bias from a reasonable and informed third person’s point of view is sufficient to justify doubts about an arbitrator’s independence or impartiality.

This was also espoused by the chair of the ICSID Administrative Council in the Blue Bank and Burlington decisions, as well as more recently in the Raiffeisen decision, in which the chair relatedly noted that ‘[a]ll relevant facts shall be taken into account in establishing the appearance of dependence or bias.’

7 Compañía de Aguas del Aconcagua S.A. & Vivendi Universal v Argentine Republic, ICSID Case No. ARB/97/3, Decision on the Challenge to the President of the Committee, 3 October 2001 (Vivendi I), paragraph 21.
9 See, for example, PCA Arbitration Rules, Art. 12(1); UNCITRAL Arbitration Rules 1976, Art. 10(1); UNCITRAL Arbitration Rules 2010 and 2013, Art. 12(1).
10 See, for example, IBA Guidelines on Conflicts of Interest in International Arbitration Adopted by resolution of the IBA Council on Thursday 23 October 2014 (the IBA Guidelines).
11 See the opinion of the unchallenged members of the ad hoc committee in Vivendi I, paragraphs 21-22.
12 The qualities required of tribunal members pursuant to Article 14(1) apply mutatis mutandis to ICSID ad hoc committee members.
13 Vivendi I, paragraph 20.
14 Urbaser S.A. and Consorcio De Aguas Bilbao Bizkaia, Bilbao Biskia Ur Partzuergoa v. The Argentine Republic, ICSID Case No. ARB/07/26, Decision On Claimants’ Proposal to Disqualify Professor Campbell McLachlan, Arbitrator, 12 August 2010 (Urbaser), paragraph 43.
15 Blue Bank, paragraph 59; Burlington, paragraph 66.; Interocean Oil Development Company and Interocean Oil Exploration Company v. Federal Republic of Nigeria, ICSID Case No. ARB/13/20, Decision on the Proposal to Disqualify All Members of the Arbitral Tribunal, 3 October 2017 (Interocean), paragraph 68.
16 Raiffeisen, paragraph 83.
iii The requirements of impartiality or independence, or both, must be manifestly lacking

The nature of these requirements has twice been summarised by the chair of the ICSID Administrative Council in the following terms: ‘[i]mpartiality refers to the absence of bias or predisposition towards a party. Independence is characterized by the absence of external control.’

The requirement that these must be manifestly lacking is found in Article 57. As Professor Schreuer observed in his commentary, ‘[t]he requirement that the lack of qualities must be “manifest” imposes a relatively heavy burden of proof on the party making the proposal.’ The meaning of ‘manifest’ has been the subject of interpretation through ICSID jurisprudence.

Karel Daele’s monograph, Challenge and Disqualification of Arbitrators in International Arbitration, suggests the existence of three generations of decisions on this matter:

a The first comes from Amco. In that case, the unchallenged arbitrators interpreted ‘manifest’ to mean that a lack of the qualities required pursuant to Article 14(1) must be ‘quasi-certain or highly probable’.

b Daele’s second generation of decisions, starting with Vivendi I, refocused the discussion in this context on a requirement that the circumstances giving rise to the challenge must be established. In this regard, the unchallenged arbitrators noted that the term ‘manifest’ in Article 57 ‘must exclude reliance on speculative assumptions or arguments’. Instead, ‘the circumstances actually established (and not merely supposed or inferred) must negate or place in clear doubt the appearance of impartiality’. Without further discussion of the specific meaning of ‘manifest’, the unchallenged arbitrators concluded that any deficiency of the qualities in Article 14(1) so proven would be manifest.

c The third and most recent generation of decisions, starting with Blue Bank in 2013, preferred a more focused and specific interpretation of ‘manifest’ as meaning ‘evident’ or ‘obvious’.

17 See Blue Bank, paragraph 59; and Burlington, paragraph 66.
18 C. Schreuer et al., The ICSID Convention: A Commentary (2009), (Schreuer) p. 1202, paragraph 19.
20 id., page 237, paragraph 5-034.
21 id., page 239, paragraph 5-035.
22 Vivendi I, paragraph 25.
23 See, for example: BSG Resources Limited, BSG Resources (Guinea) Limited and BSG Resources (Guinea) SARL v. Republic of Guinea, ICSID Case No. ARB/14/22, Decision on the Proposal to Disqualify All Members of the Arbitral Tribunal, 28 December 2016, paragraph 54; Burlington paragraph 68 n.83; Abaclat and Others v. Argentine Republic, ICSID Case No. ARB/07/5, Decision on the Proposal to Disqualify a Majority of the Tribunal, 4 February 2014 (Abaclat) paragraph. 71 n.25; Blue Bank paragraph. 61 n.43; Repsol, S.A. and Repsol Butano, S.A. v. Argentine Republic, ICSID Case No. ARB/12/38, Decision on the Proposal to Disqualify a Majority of the Tribunal, 5 May 2014, (Conoco I) paragraph 47 and Decision on the Proposal to Disqualify a Majority of the Tribunal, 1 July 2015, (Conoco II) paragraph 82; Caratube International Oil Company LLP & Mr. Derincci Salah Howran v. Republic of Kazakhstan, ICSID Case No. ARB/13/13 Decision on the Proposal for Disqualification of Mr. Bruno Boesch, 20 March 2014 (Caratube II), paragraph 64; Raiffeisen, paragraph 79; Elitech, paragraph 40. As described by Daele: ‘These terms connote to something that is easily understood, that is readily apparent, that is discerned with little effort.'
Notably, in the Raiffeisen decision, the chair of the ICSID Administrative Council applied both the second and third generation standards relying on the terminology from Blue Bank and at the same time explicitly reaffirming the Vivendi I exclusion of reliance on mere speculation in favour of ‘circumstances actually established’.

The unchallenged arbitrators in Caratube II set out a succinct formulation of the overarching test as being: ‘whether a third party would find that there is an evident or obvious appearance of lack of impartiality or independence based on a reasonable evaluation of the facts in the present case’.

### IV CIRCUMSTANCES GIVING RISE TO CHALLENGE UNDER THE ICSID CONVENTION – A SELECTION OF DECISIONS

In establishing the circumstances giving rise to an alleged lack of independence or impartiality, parties have often relied upon the IBA Guidelines on Conflicts of Interest in International Arbitration (the IBA Guidelines). They are a non-binding source of guidance, which represent an international consensus on minimum standards in relation to conflicts of interest in international arbitration. As such, it is often argued that they can be equated with the view that a reasonable and informed third party would take of a set of circumstances, and that they would form a part of the analysis of a reasonable third party when assessing a conflict situation. Notwithstanding their non-binding nature, previous ICSID decisions have referred to them as ‘useful references’, ‘instructive’ and ‘a most valuable source of inspiration’.

**i Multiple appointments by (or against) the same party**

Challenges based on multiple appointments by the same party, or its affiliates, have a long history in ICSID arbitration.

The 2010 Tidewater decision remains highly relevant to challenges of this nature. In finding that ‘the question whether multiple appointments to arbitral tribunals may impugn the independence or impartiality of an arbitrator is a matter of substance, not of mere mathematical calculation’, the unchallenged arbitrators noted that ‘[t]he starting-point is that multiple appointments as arbitrator by the same party in unrelated cases are neutral, since...’

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24 Raiffeisen, paragraph 79.
25 id., paragraphs 88-89.
26 Caratube II, paragraph 64; see also paragraph 77.
27 Blue Bank, paragraph 62; Burlington paragraph 69.
28 Alpha Projektholding GmbH v. Ukraine, ICSID Case No. ARB/07/16, Decision on Respondent’s Proposal to Disqualify Arbitrator Dr. Yoram Turbowicz, 19 March 2010, paragraph 56.
29 Urbaser, paragraph 37.
in each case the arbitrator exercises the same independent arbitral function. The following factors may give rise to an appearance of a manifest lack of independence or impartiality: (1) the prospect of continued and regular appointment, with attendant financial benefits that might create a relationship of dependence or otherwise influence the arbitrator’s judgement; or (2) a material risk that the arbitrator may be influenced by factors outside the record as a result of his or her knowledge derived from the other cases, or both.

This has found support in a majority of later decisions, including the successful challenge in Caratube II and two recent decisions: Elitech and Raiffeisen.

In Caratube II, the only successful challenge in this category, the claimants challenged Kazakhstan’s appointed arbitrator, Mr Brunch Boesch, on two main grounds: (1) his three prior appointments by Kazakhstan’s counsel, Curtis Mallet-Prevost Colt & Mosle; and (2) his appointment by Kazakhstan (also represented by Curtis Mallet-Prevost Colt & Mosle) in the Ruby Roz UNCITRAL arbitration, said to have been premised on the same legal grounds and factual allegations as the claims in Caratube II.

In relation to (1), the unchallenged arbitrators noted that the claimants had not made any allegations of Mr Boesch’s financial dependency on either Curtis Mallet-Prevost Colt & Mosle or Kazakhstan and, following the proposition in Tidewater, the mere fact of his appointments (without more) could not suffice to indicate a manifest lack of independence or impartiality. As to (2), the unchallenged arbitrators concluded that there was a significant overlap in the underlying facts between the two arbitrations, which satisfied the objective test for disqualification. In particular, Mr Boesch would be privy to information and facts from the Ruby Roz proceedings (outside of the record of the instant proceedings) leading a reasonable third party to find it highly likely that Mr Boesch would prejudge legal issues in the present arbitration based on the facts underlying the Ruby Roz case. The claimants in each case were relying on the same fact witnesses. Relatedly, the same was held to give rise to an appearance of imbalance within the tribunal. The unchallenged arbitrators left it open as to whether this constituted an aggravating factor or a stand-alone ground for disqualification.

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31 Tidewater, paragraph 60.
32 id., paragraph 62.
33 However, this view was disavowed less than six months later by the unchallenged arbitrators in OPIC, Karimum Corporation v. The Bolivarian Republic of Venezuela, ICSID Case No. ARB/10/14, Decision on the Proposal to Disqualify Professor Philippe Sands, Arbitrator, 5 May 2011, paragraph 47, who concluded that multiple appointments is a factor that, without more, is worthy of consideration and may lead to the conclusion that it is manifest that the arbitrator cannot be relied upon to exercise independent judgement as required by the Convention.
34 See, for example, Caratube II, paragraph 75.
35 id., paragraph 107.
36 id., paragraphs 78-90.
37 id., paragraphs 90-91.
38 id., paragraph 86.
39 id., paragraphs 92-94.
40 id., paragraph 96.
In February 2018, the claimants in *Elitech* submitted an application to disqualify Croatia’s appointed arbitrator, Professor Brigitte Stern, on the basis that her repeat appointments by Croatia and Croatia’s counsel, Latham & Watkins,\(^\text{41}\) raised doubts as to her ability to exercise the qualities enshrined in Article 14(1) of the ICSID Convention.\(^\text{42}\) In particular, the claimants noted that between 2014 to 2016, Professor Stern had been appointed by Croatia in three other investor–state arbitrations, all of which were ongoing; and, including the instant case, Professor Stern had served as Croatia’s appointed arbitrator in four of the seven known investor–state proceedings brought against it.\(^\text{43}\)

The claimants relied upon the IBA Guidelines, which include at Clause 3.1.3 of the Orange List,\(^\text{44}\) whether the arbitrator has been appointed as arbitrator on two or more occasions by one of the parties within the past three years.\(^\text{45}\) To extend the temporal scope of this guideline, the claimants referred to the decision in *Highbury v. Venezuela*,\(^\text{46}\) relating to an (unsuccessful) challenge to Professor Stern three years earlier,\(^\text{47}\) which stated that it was sometimes appropriate in investment arbitrations to consider the period beyond the three years specified in the IBA Guidelines.\(^\text{48}\)

The claimants also argued that the other ongoing cases in which Professor Stern was appointed by Croatia concerned factual and legal issues that were substantially similar to those to be decided in the instant proceedings.\(^\text{49}\) Relying on Clause 3.1.5 of the IBA Guidelines,\(^\text{50}\) the claimants asserted that this fact created ‘reasonable or clear doubt or real risk in regard to the exercise of independent judgment’ and therefore served as a ground for disqualification.\(^\text{51}\)

Notably, the unchallenged arbitrators (Professors Kaufmann-Kohler and Goatanda) were divided on the issue, and the challenge was accordingly decided by the chair of the ICSID Administrative Council in accordance with ICSID Article 58.\(^\text{52}\) In a decision dated 23 April 2018, the chair rejected the claimants’ disqualification proposal, reaffirming the *Tidewater* decision and noting that the claimants had failed to set out any circumstance that would call into question Professor Stern’s impartiality and independence. The multiplicity of her appointments by Croatia by itself was insufficient,\(^\text{53}\) and the claimants had failed to

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41 Professor Stern had been appointed as arbitrator twice in the preceding six years by Croatia’s counsel, Latham & Watkins (*Elitech*, paragraph 20). This ground of complaint was not addressed in the decisions.
42 *Elitech*, paragraphs 12 and 41.
43 id., paragraph 15.
44 The Orange List is a non-exhaustive list of specific situations that, depending on the facts of a given case, may, in the eyes of the parties, give rise to doubts as to the arbitrator’s impartiality or independence (IBA Guidelines, Recital II, 3).
45 IBA Guidelines, Part II, Section 3, Clause 3.1.3.
46 *Highbury International AVV, Compañía Minera de Bajo Caroni AVV and Ramstein Trading Inc v. Bolivarian Republic of Venezuela*, ICSID Case No ARB/14/10, Decision on the Proposal to Disqualify Professor Brigitte Stern, 9 June 2015 (*Highbury*).
47 *Elitech*, paragraph 14.
48 *Highbury*, paragraph 84.
49 *Elitech*, paragraph 18.
50 IBA Guidelines, Part II, Section 3, Clause 3.1.5: ‘[t]he arbitrator currently serves, or has served within the past three years, as arbitrator in another arbitration on a related issue involving one of the parties, or an affiliate of one of the parties.’
51 *Elitech*, paragraph 19 (citing *Electrabel SA v. Republic of Hungary*, ICSID Case No ARB/07/19, Decision on the Claimant’s Proposal to Disqualify a Member of the Tribunal, 25 February 2008, paragraph 40).
52 id., paragraph 10.
53 id., paragraph 50.
discharge the burden of showing that the presence of common issues was ‘sufficient to give rise, objectively, to the appearance of dependence or bias’. Of relevance to this finding, the chair noted that Professor Stern’s other appointments were in cases that did not arise in the same industry as in Elitech. That those disputes arose under the same treaty was insufficient to give rise to any presumption of bias.

Also in February 2018, and in another ICSID arbitration involving Croatia, Croatia proposed the disqualification of the claimants’ appointed arbitrator, Dr Stanimir Alexandrov, in Raiffeisen. The application was premised on four points that Croatia asserted gave rise to objective and justifiable doubts as to Dr Alexandrov’s independence and impartiality, including Dr Alexandrov’s multiple appointments in treaty cases against Croatia.

In this regard, pointing to Dr Alexandrov’s appointment in three other ongoing treaty arbitrations against Croatia (and a further nomination that was voluntarily declined), Croatia stated that the effect of Dr Alexandrov’s serving on 45 per cent of ongoing ICSID claims against the state was that he ‘possesse[d] significant and unique influence over the Respondent’s financial situation and international reputation which no single arbitrator should possess’ and that he was highly likely to be negatively predisposed against Croatia (albeit if subconsciously) to secure further appointments by future claimants against the state. Furthermore, and as a result of Dr Alexandrov having become an independent arbitrator in September 2017, Croatia argued that his own income was heavily dependent upon arbitral appointments by claimants in investment treaty arbitrations. Dr Alexandrov’s multiple appointments in cases against Croatia was stated to be equivalent to multiple appointments of an arbitrator by the same claimant or counsel falling under Clause 3.1.3 of the IBA Guidelines Orange List.

Croatia stated that the overall circumstances surrounding Dr Alexandrov’s repeat appointments and, in particular, ‘the prospect of continued and regular appointment, with the attendant financial benefits’ gave rise to justifiable doubts as to his ability to exercise independent judgment.

Croatia also argued that Dr Alexandrov would be required to consider the same legal issues as in the case of Gavrilović, where he was also sitting as the claimants’ arbitrator. In this regard, and owing to the more advanced stage of the Gavrilović proceedings, it was contended that Dr Alexandrov would already have formed a view on the compatibility of the Austria–Croatia BIT and EU law, before any opportunity to hear the parties’ submissions in the instant case arose.

54 id., paragraph 52.
55 id., paragraph 54.
56 Raiffeisen, paragraphs 17-19.
57 Dr Alexandrov declined an appointment as the claimants’ arbitrator in Addiko Bank AG and Addiko Bank d.d. v. Republic of Croatia, ICSID Case No ARB/17/37.
58 Raiffeisen, paragraph 19.
59 id.
60 id., paragraph 20.
61 id., paragraph 23.
62 id., paragraph 22.
63 See Georg Gavrilović and Gavrilović d.o.o. v. Republic of Croatia, ICSID Case No. ARB/12/39.
64 Raiffeisen, paragraph 26.
More broadly, Croatia also noted that Dr Alexandrov had served as the claimant-investor’s appointee in 35 out of the 38 known investment treatment arbitrations in which he has sat as arbitrator.\(^\text{65}\)

For reasons that were not disclosed, Croatia’s appointed arbitrator, Mr Lazar Tomov, recused himself from deciding the application,\(^\text{66}\) which was accordingly considered instead by the chair of the ICSID Administrative Council.

In determining Croatia’s complaint regarding Dr Alexandrov’s multiple appointments in treaty cases against Croatia, and by claimant-investors more generally, the chair relied on the earlier stated proposition from *Tidewater* and further noted the principle in *Vivendi I*, stating that circumstances giving rise to a finding that a lack of impartiality of independence is manifest ‘must negate or place in clear doubt the appearance of impartiality’.\(^\text{67}\) In this regard, the chair determined that Croatia had failed to evince an appearance of bias or financial dependence that satisfied this requirement.\(^\text{68}\)

Specific to any overlap of factual or legal issues, the chair noted that ‘the mere exposure of an arbitrator to the same legal issue in multiple arbitrations is insufficient to disqualify that arbitrator’, and, relying on the unchallenged arbitrators’ reasoning in *Caratube II*, that ‘[t]here must be an additional – significant – overlap of facts that are specific to the merits and the parties involved’.\(^\text{69}\)

Both challenges made reference to the frequency with which the challenged arbitrators had been appointed by either investors or states: in the case of Dr Alexandrov, appointments by claimant-investors and, in the case of Professor Stern, appointments by respondent-states. So far as the authors are aware, no challenge based on this (relatively commonplace) occurrence in the ICSID context has ever been successful.

The subject of multiple appointments also arose in three separate challenges brought by Venezuela against Mr Alvaro Castellanos Howell.\(^\text{70}\) These challenges, all of which were decided in 2018, related to Mr Castellanos Howell’s appointment as the president of three *ad hoc* committees in ICSID annulment proceedings involving Venezuela. All three challenges were reported to have been brought on the same grounds, and all were rejected.\(^\text{71}\) The decision in the *Blue Bank* annulment proceedings (the only one of the decisions that is publicly available) is considered below.

Venezuela relied on Article 3.1.3 of the Orange List of the IBA Guidelines to argue that the appointment of Mr Castellanos Howell to five *ad hoc* committees overseeing annulment proceedings involving Venezuela was indicative of Mr Castellanos Howell’s reliance and

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\(^{65}\) id., paragraph 16.

\(^{66}\) id., paragraph 10.

\(^{67}\) id., paragraph 88 (citing to *Vivendi I*, paragraph 25).

\(^{68}\) id., paragraph 89.

\(^{69}\) id., paragraph 91 (citing to *Caratube II*, paragraphs 78, 84, 86 and 90).


Challenges to Arbitrators under the ICSID Convention and Rules

financial dependence on such repeat appointments and his resultant lack of independence.\(^{72}\) In determining the application, the unchallenged committee members noted that the potential risk of conflict identified by Article 3.1.3, which applies to multiple appointments by a party or its affiliate, was not applicable to a recurring professional relationship with ICSID, the appointing authority to ad hoc committees.\(^{73}\)

At the same time, relying on Article 3.1.5 of the Orange List of the IBA Guidelines, Venezuela also pointed to an alleged commonality of issues across the proceedings to be determined by the committees of which Mr Castellanos Howell sat as president. This was dismissed on the basis that Venezuela had failed to identify any overlap beyond all proceedings being related to the annulment of awards in proceedings involving Venezuela.\(^{74}\)

The 2018 decisions suggest that the test set out in Tidewater is likely to remain persuasive in determining these types of challenges, and that the threshold for establishing an appearance of dependence or partiality remains high.

ii  A pre-existing relationship with one of the parties or their affiliates

Pre-existing professional relationships have formed the basis for a number of challenges under the ICSID Convention. It does not define the kinds of relationships that should be disclosed by arbitrators or considered as a bar to appointment. As noted by Professor Schreuer:

>a relationship with a party affecting the eligibility as arbitrator may be of a personal, family or business nature. It would include a permanent attorney/client relationship, any other permanent or recurrent business relationship, employment by a party, including civil service in a State that is a party, substantial participation or shareholding in a company that is a party and any form of relationship in which the arbitrator stands to profit directly or indirectly from the financial gain of a party.\(^{75}\)

A pre-existing professional relationship, in this case in the context of a lawyer and client, formed the grounds for challenge in Amco. Although the challenge was dismissed, in noting the subsequent criticism of this decision, the unchallenged arbitrators in Vivendi I stated that any such relationship can only be justified under the de minimis exception.\(^{76}\) In their estimation, anything more would surely be sufficient to establish the appearance of dependence.

In Blue Bank, the respondent challenged the claimant’s appointee, Mr José María Alonso, on the basis that the firm at which he was a partner (Baker McKenzie) also represented the claimant in parallel arbitration proceedings. The chair of the ICSID Administrative Council upheld the respondent’s request, inter alia, because, in the words of Professor Schreuer, Mr Alonso ‘stood to profit directly or indirectly from the financial gain of a party’.\(^{77}\)

\(^{72}\) Blue Bank Annulment, paragraph 75.

\(^{73}\) id., paragraphs 98-99.

\(^{74}\) id., paragraphs 104-105.

\(^{75}\) Schreuer, p. 513, paragraph 22.

\(^{76}\) Vivendi I, paragraph 22.

\(^{77}\) Schreuer, p. 513, paragraph 22.
As the chair observed:

[The sharing of a corporate name, the existence of an international arbitration steering committee at a global level, and Mr. Alonso’s statement that his remuneration depends ‘primarily’ but not exclusively on the results achieved by the Madrid firm imply a degree of connection or overall coordination between the different firms comprising Baker & McKenzie International.]

In *Generation Ukraine*, the claimant challenged the respondent state’s nominee, Dr Jürgen Voss, on the basis that he had been involved in studies and investment policy reviews of Ukraine during his time as Deputy General Counsel of the Multilateral Investment Guarantee Agency. The claimant cited concerns that Dr Voss had developed personal connections with Ukrainian political officials and that these personal connections would deprive him of the capacity for independent judgement. On referral by the unchallenged arbitrators, the request was recommended to be dismissed by the Secretary General of the Permanent Court of Arbitration without reasoning. Nevertheless, it must presumably have been considered that previous professional relationships arising out of an arbitrator’s participation in a multi-state programme of cooperation, without any resultant financial dependency, was not a basis for disqualification.

The circumstances of the challenge in *Generation Ukraine* are similar in a number of respects to those raised by the claimant in its challenge to Kazakhstan’s appointed arbitrator, Professor Knieper, in *Big Sky*. The challenge, which was successful, centred on Professor Knieper’s previous work as a German employed consultant on various legal reforms across central Asia. In particular, it was alleged that Professor Knieper’s work had brought him into close contact with members of the Kazakh judiciary, whose actions the claimant criticises.

Two complaints in this regard were also raised in *Raiffeisen*. First, it was alleged that Dr Alexandrov and counsel to the claimants, Wilmer Cutler Pickering Hale and Dorr (WilmerHale), had developed a ‘special relationship’ based on cross-appointments of Dr Alexandrov as arbitrator by WilmerHale as counsel, and of Mr Gary Born, a partner at WilmerHale, as arbitrator by Dr Alexandrov as counsel. This was said to give rise to an appearance of dependence or bias.

Second, Croatia raised allegations of impropriety arising out of Dr Alexandrov’s purported long-standing and publicly recognised relationship with the Brattle Group, experts retained by UniCredit in *UniCredit Bank v. Croatia*. In this regard, Croatia asserted...
that Dr Alexandrov would be predisposed towards arguments put forward by the claimants where they mirrored the expert evidence put forward by the Brattle Group in UniCredit’s claim under the same treaty, which was said to be on ‘an identical factual basis’.  

Both of these complaints were dismissed. In respect of the alleged ‘cross-appointments’, without ‘something more’, these were held to be insufficient to satisfy the objective test that Dr Alexandrov appeared lacking in the ability to exercise independence or impartiality, or both. And, on the basis that the Brattle Group had not been instructed in the instant proceedings and that Dr Alexandrov should not be privy to the Brattle Group’s testimony in *UniCredit* (not being appointed to the tribunal in that case), this ground of complaint was likewise rejected.

Also in 2018, and on the same point, the president of the tribunal in *Gran Colombia Gold v. Colombia*, Ms Malintoppi, stepped down following a challenge by the claimant purportedly on the basis of her marriage to Mr Rodman Bundy, an international lawyer who has represented Colombia in a dispute before the International Court of Justice.

The 2018 decisions confirm that proposals of this nature will be considered on a case-by-case basis. The existence of a personal or professional relationship, without more, will be insufficient but, conversely, a risk of financial gain or profit arising out of that relationship is not a prerequisite to disqualification.

### iii Prejudgment of issues based on previously expressed views

Previously expressed opinions have formed the basis for a number of recent disqualification applications, all of which have been dismissed.

In *Urbaser*, the claimants sought to disqualify Professor Campbell McLachlan, the respondent-appointed arbitrator, on the basis that Professor McLachlan had expressed views in previous academic writings on a key point of law that was at issue in the case. The claimants’ argument was that Professor McLachlan would not be able to find against the respondent without contradicting his previous statements. The issue in question was whether a most favoured nation clause could apply in relation to dispute settlement provisions and, according to the claimant, the application of the most favoured nation clause in the Spain–Argentina BIT was an ‘essential element of the conflict that is the object of this arbitration’. Professor McLachlan had previously stated that the protections afforded by the most favoured nation clause ‘will not apply to the dispute settlement provisions, unless the parties expressly so provide’.

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86 *id.*, paragraph 34.
87 *id.*, paragraph 95.
88 *Gran Colombia Gold Corp. v. Republic of Colombia*, ICSID Case No. ARB/18/23.
90 *Urbaser*, paragraph 41.
91 *id.*, paragraph 23.
92 *Urbaser*, paragraph 21.
In dismissing the claimants’ disqualification proposal, the unchallenged arbitrators in *Urbaser* observed as follows:

> [w]hat matters is whether the opinions expressed by Prof. McLachlan on the two issues qualified as crucial by Claimants are specific and clear enough that a reasonable and informed third party would find that the arbitrator will rely on such opinions without giving proper consideration to the facts, circumstances, and arguments presented by the Parties in this proceeding.93

In *Saipem*, Pakistan’s proposal to disqualify the claimant-appointed arbitrator was based, in part, on the assertion that the arbitrator had expressed opinions in his writing that, in the respondent’s view, showed preconceived positions with regard to some of the central issues of the arbitration. In their decision the unchallenged arbitrators dismissed the proposal, noting that an arbitrator’s doctrinal opinions ‘expressed in the abstract without reference to any particular case do not affect the arbitrator’s impartiality and independence’.94

This issue also formed the basis for a pair of 2018 challenges to Mr Gary Born in *KS Invest* and *Mathias Kruck*. In each case, Spain’s challenge was premised on the ground that Mr Born had prejudged issues relevant to the case, said to be demonstrated by Mr Born’s (1) dissenting opinion in *JWS Solar*;95 (2) questioning of counsel in *Masdar*;96 and (3) questioning of a fact witness presented by Spain during the hearing in *KS Invest*.97

The unchallenged arbitrators in *Mathias Kruck* issued their decision in March 2018, rejecting Spain’s challenge. Dealing first with Mr Born’s dissenting opinion in the *JWS Solar* case, the unchallenged arbitrators noted that the analysis and opinions contained therein were fact-specific to that particular case and accordingly did not consider that it gave rise to any doubts as to Mr Born’s impartiality in the present case.98 The unchallenged arbitrators also found that there was nothing improper in Mr Born’s questioning of counsel and witnesses in the *Masdar* and *KS Invest* cases.99 The reasoning set out in the *Mathias Kruck* decision was thereafter adopted by the unchallenged arbitrators in rejecting Spain’s parallel challenge in *KS Invest*.100

This issue also arose in Venezuela’s three separate challenges to Mr Castellanos Howell.101 In those cases, Venezuela took issues with an article written by Mr Castellanos Howell and published in a Guatemalan daily newspaper in 2017, ‘The Ideologization of Justice’.102 This

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93 id., paragraph 44.
96 *Masdar Solar & Wind Cooperative U.A. v. Kingdom of Spain*, ICSID Case No. ARB/14/1 (*Masdar*).
97 *Mathias Kruck*, paragraphs 28 - 29; *KS Invest*, paragraph 22.
98 *Mathias Kruck*, paragraph 54.
99 id., paragraph 55.
100 *KS Invest*, paragraph 48.
article discussed proposed amendments to the Guatemalan Constitution, detractors of which argued would lead ‘to a scenario like Venezuela’. Commenting on the debate, Mr Castellanos Howell rejected the suggestion that the proposed amendments to the constitution would result in ‘imminent “Venezuelisation”’, described as a ‘scenario where there is no judicial independency from other branches of government’.103

In rejecting the Blue Bank annulment proposal, the unchallenged committee members held that it was not possible to extrapolate from the article any explicit criticism, or prior judgment, of Venezuela by Mr Castellanos Howell. Rather, the article was intended to reproduce and comment on the views expressed by opponents to constitutional reform, and upon which Mr Castellanos Howell did not imply any value judgement.104

The 2018 cases confirm that the threshold for this category of challenge remains extremely high. Only in circumstances where an independent third party would find circumstances demonstrating the appearance of a firmly held predisposition or prejudgement (and accordingly a real risk that the challenged arbitrator would rely on such opinions without giving proper consideration to the facts and evidence put forward by the parties) is such a challenge likely to be successful.

V CONCLUSION

The 2018 disqualification decisions, which upheld only one of the 10 proposals, demonstrate that disqualification remains the exception, rather than the norm. The threshold for disqualification continues to be extremely high, regardless of the circumstances giving rise to the proposal (as to which, multiple appointments remains the most popular). It is likely that 2019 will see more disqualification proposals in the ICSID context, which (it is hoped) will build upon the emerging body of consistent case law as to the legal standard for disqualification.

103 id.
104 Blue Bank, paragraphs 88-89.
Part III

PRACTICAL AND SYSTEMIC ISSUES
Chapter 13

THE ROLE OF PRECEDENT IN INVESTMENT TREATY ARBITRATION

Beata Gessel-Kalinowska vel Kalisz and Konrad Czech

I INTRODUCTION

On the face of it, the issue of precedent in investment treaty arbitration is straightforward enough, and also amenable to empirical examination. It is certain that there is no formal doctrine of precedent in the field of investment treaty arbitration. Empirical research shows that arbitrators regularly refer to earlier cases at the same time. The high practical importance of arbitral decisions in the area of investment treaty arbitration is hence unquestionable, even though one can hardly speak of a binding precedent as understood under the common law doctrine of stare decisis. Yet, upon closer examination, the overall picture becomes more complex. The value of prior arbitral jurisprudence is often debatable. Because of the fragmentation of public international law, namely the existence of many differently worded international investment agreements (IIAs), earlier investment treaty decisions can be differentiated on legal grounds, and accordingly found unpersuasive unless referring to legal provisions of the same or largely similar IIAs. Investment treaty cases can also be differentiated on facts, seeing as their factual patterns, especially if referring to different state measures or to different jurisdictions, are rarely identical. Finally, on at least several occasions, it happened that arbitral tribunals blatantly ignored discussion of earlier decisions.

II OBSTACLES TO THE SYSTEM OF PRECEDENT

While investment treaty arbitration largely draws on commercial arbitration, and hence has a mixed status, it concerns international public law matters, including, first and foremost, treaty interpretation. The doctrine of precedent has never been formally adopted in the field of public international law (e.g., by the International Court of Justice or by other international institutions).
The Role of Precedent in Investment Treaty Arbitration

Law adjudicatory bodies. Judicial decisions are not sources of international law but, properly speaking, merely help in interpretation of international law provisions contained in IIAs, or are relied upon as ‘evidence for existence of customary international law’. Thus, each arbitral or other adjudicatory decision is of assistance in extrapolating general principles of international law, albeit it does not create any stand-alone international law standard per se (awards are binding only upon the parties). This important doctrinal obstacle on the road to development of the system of precedent is not the only one, however.

Even if one were willing to treat investment treaty arbitration and law as relatively distinct from classic fields of public international law, the lack of full transparency of investment treaty arbitration is another obstacle to development of the precedent system. The latter requires publicity of decisions. Not all arbitral awards are public, many are partially redacted before publication, and the United Nations Convention on Transparency in Treaty-based Investor–State Arbitration (the Mauritius Convention on Transparency) has, so far, been ratified only by three states. Moreover, even a wider adoption of the Mauritius Convention on Transparency and, accordingly, broader application of the UNCITRAL Rules on Transparency in Treaty-based Investor–State Arbitration will not, on its own, pave the way for the future development of a precedential system in investment treaty arbitration.

The major obstacle to the true development of a precedential system is posed in the fact that substantive investment law consists of 2,363 bilateral investment treaties (BITs) and 309 other treaties with investment protection provisions (there are 2,672 IIAs in force). In a word, the investment law framework is, by its very nature, fragmented. As the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID) is never applied on its own, and does not contain any substantive standards of foreign investment protection, the aforementioned relates equally to investment

7 See, e.g., Bureau Veritas, Inspection, Valuation, Assessment and Control, BIVAC BV v. Republic of Paraguay, ICSID Case No. ARB/07/9, Decision on Jurisdiction, 29 May 2009, para. 58.
8 Reinisch, ‘Investment Arbitration…’, 496.
arbitrations administered outside ICSID and to those within the ICSID system. The great number of substantive instruments, which are often differently worded, makes it difficult to indiscriminately draw on earlier cases, especially if they referred to interpretation of a differently worded investment protection standard of some other IIA. On the other hand, of course, many IIAs, in particular if agreed by the same capital-exporting state in a similar time period, or if based on the same model BIT, are quite similarly worded. For instance, many UK and French BITs define ‘investment’ in a similar manner. This facilitates referencing some earlier decisions in later cases.

On top of this, however, multiple IIAs are on par with each other. In consequence, findings of various arbitral tribunals dealing with investment protection matters, deriving their jurisdiction from different IIAs, have equal status. Unlike in the common law systems that adopted the stare decisis principle, there is no hierarchy of arbitral awards. There is also no arbitral appellate body, and ICSID annulment committees have procedural autonomy. This makes sorting out the relevance of arbitral decisions a discretionary task for counsel and arbitrators who can assign quite different values to them depending on a number of case-specific factors, including linguistic differences between the underlying instruments and fact-driven considerations. Indeed, arbitral tribunals can draw guidance from earlier cases, and usually do so if they concerned similar matters or were issued by respective arbitrators, but are not bound to strictly follow them. The persuasiveness of previous arbitral decisions is, in most cases, subject to debate between parties, that is to say, in the absence of formal guidelines in this respect, reasonable minds will often differ on the value of earlier awards.

III HIGH RELEVANCE OF PRIOR ARBITRAL DECISIONS

Notwithstanding the above, it has to be emphasised that prior arbitral decisions are nowadays regularly referenced, or even cited in extenso, by arbitral tribunals in their awards. It is fully

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14 Quasar de Valors SICAV SA and others (formerly Renta 4 SVSA and others) v. Russian Federation, SCC Case No. 24/2007, Award on Preliminary Objections, 20 March 2009, para. 16.
15 Urbaser SA and Consorcio de Aguas Bilbao Biskia, Bilbao Biskaia Ur Partzuergoa v. Argentine Republic, ICSID Case No. ARB/07/26, Decision on Claimants’ Proposal to Disqualify Professor Campbell McLachlan, Arbitrator, 12 August 2010, para. 49.
16 WNC Factoring Ltd v. Czech Republic, PCA Case No. 2014-34, Award, 22 February 2017, para. 310, where the arbitral tribunal states that ‘to the extent that they [arbitral awards – ed. note] are based on sound legal reasoning, the decisions of tribunals in prior international law cases can provide useful insights to subsequent tribunals considering those issues’.
true that ‘consideration of prior decisions allows tribunals to benefit from reasoning that has been developed in similar scenarios, possibly making their own more effective and efficient.’

As one commentator put it:

> “[e]ven those arbitrators who denounce attempts to impose a system of precedent on investment treaty arbitration do not eschew relying on or citing to other decisions for support and do not shy away from explaining why a particular decision should not be followed. Where there are inconsistent decisions, these issues are debated in scholarly articles, at conferences, on blogs, and, of course, by the parties in any dispute. Over the course of time, tribunals come to distinguish, interpret narrowly, or simply disagree with the less persuasive decisions, until such decisions eventually represent the minority view.”

Some commentators argue that an ICSID award can be annulled if prior arbitral awards are not properly discussed by an arbitral tribunal. Several commentators, who also happen to be notable arbitration practitioners, note a de facto system of precedent in the world of investment arbitration (as opposed to the de jure precedent system, which has not developed in investment treaty arbitration). One academic work notes ‘an informal, but powerful, system of precedent that constrains arbitrators to account for prior published awards and to stabilize international investment law’. A recent treatise on the matter of arbitral lawmaking adapts a similar tack, yet using different language. It argues that ‘the distinction between a de jure and de facto doctrine of precedent is artificial.’ Following this line of thinking, the doctrine of precedent does not require the doctrine of stare decisis and, accordingly, it can be submitted that not only common law jurisdictions, but also civil law jurisdictions, recognise precedents.

In other words, while the notion of precedent is ‘a common law term of art that is clearly distinguishable from civil law judicial lawmaking’, in civil law jurisdictions there stand concepts such as jurisprudence constante or ständige Rechtsprechung, which are quite similar, albeit they do not officially impose strict adherence to legal principles established in the previous decisions. Consequently, it can be argued that investment arbitration promotes a

21 See, e.g., Lucy Reed, ‘The De Facto Precedent Regime in Investment Arbitration: A Case for Proactive Case Management’ (2010) 25 _ICSID Review – Foreign Investment Law Journal_ 95–103 at 95, where the author asks ‘[w]hy else would the parties and the arbitrators in investment arbitration devote so much ink and time to citing’ arbitral decisions. See also Reinisch, ‘Investment Arbitration – The Role of Precedent’, 508, where arbitral decisions are characterised as being ‘quasi-authoritative manifestations of the law’.
hybrid’ approach to precedent as ‘[o]n the one hand, tribunals pay a higher deference to a civil law type of “jurisprudence constante”; on the other hand, lawyers and arbitrators and counsel readily engage in a common law style of reasoning’. It is suggested that ‘[n]either the common law conception nor the civil law conception is capable of capturing the role of past arbitral decisions.’ This ‘hybrid’ understanding of precedent can be a challenge for both common law- and civil law-trained lawyers.

If one thing is sure, it is that it is impossible to successfully argue an investment case without giving account to arbitral jurisprudence. No matter how scholars and practitioners phrase their views on the issue of precedent, they recognise the importance of prior arbitral awards. Most of them, however, either directly or indirectly reject the common law understanding of precedent, which, upon certain systemic conditions, requires a court to abide decisions issued by courts above it, or appellate courts. Whereas investment protection standards contained in IIAs are broadly drafted and require interpretation, making international investment law prima facie prone to the doctrine of precedent, it does not fall on fertile ground in the world of investment treaty arbitration. This is so for many doctrinal and structural reasons, most importantly because of the legal parity of different arbitral tribunals and their awards.

IV ARBITRAL DECISIONS ON THE ROLE OF PRECEDENT

There are many arbitral decisions declaring the lack of precedent in the area on international investment law but, concurrently, emphasising the relevance of prior awards. In one of the most notable cases regarding the role of precedent, namely in ADC v. Hungary, the arbitral tribunal stated that:

The Parties to the present case have . . . debated the relevance of international case law. . . . It is true that arbitral awards do not constitute binding precedent. It is also true that a number of cases are fact-driven and that the findings in those cases cannot be transposed in and of themselves to other cases. It is further true that a number of cases are based on treaties that differ from the present BIT in certain respects. However, cautious reliance on certain principles developed in a number of those cases, as persuasive authority, may advance the body of law, which in turn may serve predictability in the interest of both investors and host States.

A similar conclusion can be drawn, for example, from Jan de Nul v. Egypt. The same reasoning was also applied in two earlier well-known ICSID awards that were issued in a series of cases brought against Argentina after it experienced the economic crisis in 2001–2002.

In Enron v. Argentina, the arbitral tribunal rightly stated that ‘decisions of ICSID tribunals are not binding precedents and . . . every case must be examined in the light of

26 ibidem.
28 ADC Affiliate Limited and ADC & ADMC Management Limited v. The Republic of Hungary, ICSID Case No. ARB/03/16, Award, 2 October 2006, para. 293.
29 Jan de Nul NV and Dredging International NV v. Arab Republic of Egypt, ICSID Case No. ARB/04/13, Decision on Jurisdiction, 16 June 2006, para. 64.
The role of precedent in investment treaty arbitration is a matter of ongoing discussion and evolution. The Enron tribunal, for example, emphasized the importance of considering precedent in the context of its own circumstances. Having stated that, however, the tribunal equally correctly decided to adhere to the earlier jurisdictional decisions from other cases. To be more precise, the arbitral tribunal decided that:

> [t]he key issues raised by the parties in connection with jurisdiction in this case . . . are not really different from those raised in earlier cases. This being the case, the conclusions of the Tribunal follow the same line of reasoning, not because there might be a compulsory precedent but because the circumstances of the various cases are comparable, and in some respects identical.

The role of precedent was also discussed in AES v. Argentina. In this case, the arbitral tribunal stated that ‘each BIT has its own identity; its very terms should consequently be carefully analysed for determining the exact scope of consent expressed by its two Parties’ and hence ‘the findings of law made by one ICSID tribunal in one case in consideration, among others, of the terms of a determined BIT, are not necessarily relevant for other ICSID tribunals.’

After reaching this conclusion, the AES tribunal continued:

> Under the benefit of the foregoing observations, the Tribunal would nevertheless reject the excessive assertion which would consist in pretending that, due to the specificity of each case and the identity of each decision on jurisdiction or award, absolutely no consideration might be given to other decisions on jurisdiction or awards delivered by other tribunals in similar cases.

Following this line of reasoning, in Bayindir v. Pakistan the arbitral tribunal adopted the position that previous decisions are not binding but that, absent compelling reasons to decide otherwise, legal solutions established in a series of consistent awards should be followed, although subject to the specifics of a given IAA and circumstances of the case. The Bayindir tribunal explained that arbitrators have a ‘duty to seek to contribute to the harmonious development of investment law and thereby to meet the legitimate expectations of the community of States and investors towards certainty of the rule of law.’ This position of the Bayindir tribunal was cited a year later in Fakes v. Turkey. Also, in the 2012 award in Daimler v. Argentina, the arbitral tribunal acknowledged the principle of the rule of law that similar cases should be decided alike unless a strong reason exists to distinguish between them. It further stated that much depends on three factors, namely on: (1) how similar the prior and new cases are; (2) the degree to which a clear jurisprudence emerged; and (3) the

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30 Enron Corporation and Ponderosa Assets LP v. Argentine Republic, ICSID Case No. ARB/01/3 (also known as: Enron Creditors Recovery Corp. and Ponderosa Assets LP v. The Argentine Republic), Decision on Jurisdiction, 2 August 2004, para. 25.
31 ibidem.
33 AES Corporation v. The Argentine Republic, para. 27.
34 Bayindir Insaat Turizm Ticaret Ve Sanayi AS v. Islamic Republic of Pakistan, ICSID Case No. ARB/03/29, Award, 27 August 2009, para. 145.
35 ibidem.
36 Saba Fakes v. Republic of Turkey, ICSID Case No. ARB/07/20, Award, 14 July 2010, para. 96.
37 Daimler Financial Services AG v. Argentine Republic, ICSID Case No. ARB/05/1, Award, 22 August 2012, para. 22.
arbitral tribunal’s independent assessment of the persuasiveness of prior decisions. A similar reasoning has been adopted by the arbitral tribunals in *Austrian Airlines v. Slovak Republic*, in *Electrabel v. Hungary* and recently in *Jürgen Wirtgen v. Czech Republic*. Thus, arbitral tribunals strive to maximise the consistency of investment treaty jurisprudence.

In any case, there exists the ‘general consensus’ among arbitral tribunals that the doctrine of *stare decisis* is not applicable. Previous arbitral awards discussed by parties in their written submissions are generally taken into account by arbitrators who, in response to the parties’ submissions, address arbitral jurisprudence in virtually all awards. This tendency, however, does not fully prevent inconsistencies between decisions. While arbitral tribunals attempt to explain ‘the points on which the different case holdings can be distinguished, and the points on which there is analytical disagreement between tribunals’, they may still, of course, reach in their decisions quite different conclusions. Most, but not all, potential inconsistencies are therefore carefully resolved through the technique of distinguishing. To put it another way, arbitral tribunals that disagree with earlier decisions usually decide to discuss, at least in general terms, differences between the cases in a common law manner.

For instance, in *SGS v. Philippines*, the arbitral tribunal differentiated between two cases brought by SGS against Pakistan and the Philippines respectively. It pointed to ‘somewhat different legal and factual context’ of these cases and, hence, reached a different conclusion on interpretation of the umbrella clause than the arbitral tribunal in *SGS v. Pakistan*. Similarly, in *Bureau Veritas v. Paraguay*, the arbitral tribunal felt obliged to explain why it decided not to follow the approach adopted by other arbitral tribunals. In the past, however, not all arbitral tribunals that decided to deviate from previous arbitral awards saw fit to justify their decisions. There is little doubt that not only are contradictory arbitral awards on some issues possible, but also that the predictability of arbitral awards can be something of a challenge. To illustrate this, many writings on the topic refer to the award issued in *LG&E v. Argentina*.

38 ibidem.
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The LG&E tribunal did not cite the earlier award in *CMS v. Argentina*, although both cases concerned the ‘state of necessity defence’ relating to the very same factual circumstances, namely to the legislation on privatisation of gas utilities in Argentina.\(^47\) Also, in *Azurix v. Argentina*, the *ad hoc* ICSID Committee was ‘against a strict analysis of previous Committee decisions in stay applications as if they were common law precedents’.\(^48\) These two examples, even though the LG&E award and the Azurix annulment decision were issued over a decade ago, show best that arbitral tribunals dealing with investment treaty matters function independently from each other – namely, they all stay in a perfectly horizontal relationship.

### V OUTLOOK AND CONCLUSIONS

The inherent characteristics of investment law make it impossible to formally develop and apply the doctrine of precedent in investment treaty arbitration. Accordingly, looking from a traditional perspective, it may be misleading to speak about ‘precedent’ or ‘case law’ in the area of investment treaty arbitration. Arbitral tribunals are under no circumstances bound by earlier arbitral decisions and hence, strictly speaking, prior cases are not a source of investment law. One can safely speak about ‘precedent’ in investment treaty matters only if this term refers to prior arbitration decisions generally, but without implying their legally binding force in later cases. Notwithstanding this classic approach, as a matter of practice, most arbitral tribunals engage in discussion of earlier cases in their awards. The trend to cite prior investment treaty decisions is so well established that some commentators suggest the existence of a *de facto* precedent regime in investment treaty arbitration, or an informal system of precedent. It is often correctly argued that this system contributes to development, and also to greater consistency, of investment law. With that explained, it may sometimes prove somewhat difficult for counsel to foresee to what extent arbitrators will take into account earlier cases in their decision-making process. If arbitrators find some earlier decisions unconvincing, they normally try to carefully distinguish them from the case at hand, but sometimes, although definitely less frequently, also simply sweep them aside and proceed to draw from other cases.


\(^48\) *Azurix Corp v. Argentine Republic*, ICSID Case No. ARB/01/12, Decision on the Argentine Republic’s Request for a Continued Stay of Enforcement of the Award, 28 December 2007, para. 24.
Chapter 14

RES JUDICATA IN INVESTMENT TREATY ARBITRATION

Colin Ong QC

I GENERAL INTRODUCTION

This chapter deals with the challenges faced by arbitrators and parties alike in investment treaty arbitrations under both the arbitration rules of the International Centre for Settlement of Investment Disputes (ICSID) and the United Nations Commission on International Trade Law (UNCITRAL), in dealing with the doctrine of res judicata.

It is important for arbitration players to know and to predict whether an arbitral tribunal would consider itself bound by earlier court judgments, and findings of a court or other arbitral tribunal. If the latest arbitral tribunal is likely to consider itself bound by doctrines of res judicata or issue estoppel, the next question that arbitration players need to know is the extent to which the res judicata applies. The breadth and scope of this doctrine may very much influence and affect the final outcome of the arbitration proceedings. There are many troublesome issues regarding the exact scope of the effects on res judicata of previous court judgments or arbitral awards that emerge before both commercial and investment arbitration tribunals.

Though procedural conditions may differ from one jurisdiction to another, the common thread that runs through all jurisdictions is that a foreign commercial judgment or award shall be deemed to be both final and conclusive, if the original court or tribunal that had pronounced the judgment has conclusively and finally established the existence of the claim, with the effect that it makes it res judicata between the parties. For a foreign commercial judgment or award to be considered as res judicata, the following conditions need to be fulfilled. The original judgment or award must: (1) be final and conclusive; (2) have been made on the merits; and (3) have had proper jurisdiction over the subject matter and the parties.

It is widely accepted in most legal systems and jurisdictions that, although the system of the court or arbitral tribunal that rendered the original decision determines the exact relationship of the party to the proceedings, and the incidents of that relationship, it is ultimately for the local law of the courts at the place of enforcement to determine whether
that makes the party a proper one, for the purpose of the doctrine of estoppel by *res judicata*. It is also generally accepted that, in accordance with the *res judicata* principle, matters that have been judged on the merits are deemed binding on the parties, and may no longer be relitigated, re-arbitrated or decided differently in subsequent court or arbitral proceedings.

II DIFFERENT APPROACHES FROM CIVIL LAW AND COMMON LAW

Courts and arbitral tribunals in both common and civil law jurisdictions must decline their jurisdiction if the same dispute involving the same parties has already been finally resolved by a foreign court judgment or foreign arbitral award that is capable of recognition in the courts or tribunals of the second jurisdiction. Common law jurisdictions and common law have long recognised a ‘core of common agreement’ in respect of the doctrine of *res judicata*. The general principle that underpins the *res judicata* doctrine is that once a particular dispute has been settled by a judgment or arbitral award, it must be regarded as final and binding. This means that the same issues cannot thereafter be relitigated, re-arbitrated or challenged by way of collateral attack between the same legal persons who are bound by the earlier final and conclusive decision.

Some commentators have explained that ‘deeply-rooted considerations of public policy underlie rules of preclusion in national (and international) law’, and that such public policy focuses upon the injustice of allowing a party to relitigate the exact same claims and issues against an opposing party in repeated proceedings. If these practices are not curbed, it would increase both the costs of litigation and the risks of litigation, and there would be damage caused to the credibility and resources of the legal system.

As a general statement, in common law jurisdictions, a party is not entitled to attempt to reopen, by arbitration or litigation, any issue that has already been decided by a competent court or arbitral tribunal between the same parties. In addition, most common law jurisdictions do not allow a party to attempt to reopen, in new arbitration or litigation proceedings, any points that could and should have been properly raised and decided in previous arbitration or litigation. In common law jurisdictions, *res judicata* principles tend not to be not codified, but are instead based mainly or entirely upon judicial authority. Similarly, as a general statement, the doctrine of *res judicata* is more limited in civil law than it is under common law.

Civil law doctrine gives rise only to the direct petition of *res judicata*, and covers neither common law petitions of issue estoppel nor of abuse of process. Civil law jurisdictions accept

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7 See Spencer Bower and Handley, *Res Judicata* 2009 (Lexis Nexis 4 ed) at paragraph 1.01.

8 See Born, *International Commercial Arbitration* (Wolters Kluwer 2014), Volume III, Chapter 27 at pages 3733 to 3734. The commentator cites the phrase ‘interest reipublicae ut sit finis Baum’ (‘it is in the public interest that there should be an end to litigation’).

9 The rule against abuse of process was first laid down by the English Court of Chancery decision in *Henderson v. Henderson* (1843) 3 Hare 100, 67 ER 313, which ruled that a party may not raise any claim in subsequent litigation that it ought to have properly raised in a previous action.

the view that an arbitral award or a court judgment that determines a legal dispute between parties in a way that is final and conclusive is deemed as *res judicata.*¹¹ Civil law takes the approach that only the dispositive part of the award or judgment will become *res judicata*; the dispositive part of a judgment contains the court’s decision on the matters in dispute. The dispositive part only becomes *res judicata* in respect of matters that were distinctly raised and determined in adversarial proceedings. No *res judicata* effect attaches to any matters that were not raised during the proceedings, even though the original arbitral tribunal or court rendered a definitive decision on those issues. In addition, no *res judicata* effect attaches to matters that were raised during the original proceedings but that were not decided in the operative order by the arbitral tribunal or the original court.¹²

Unlike some common law jurisdictions that have the related doctrine of issue estoppel¹³ and abuse of process,¹⁴ these concepts are generally unknown in civil law jurisdictions.

### III RES JUDICATA IN INTERNATIONAL ARBITRATION

As a decision of an international arbitral tribunal is also considered to be final and binding, it is of no surprise that the doctrine of *res judicata* is equally important in international arbitration. The same subject matter could emerge in two different arbitrations taking place between the same parties in a number of different situations. For example, it is not uncommon for two arbitration proceedings to have been initiated under different putative contracts that relate to the same legal relationship because the parties had signed amendments to the original agreement and there may be an overlap in the subject matter. Similarly, in licensing agreements, the same parties could have entered into a number of different agreements relating to the same subject. It is also not uncommon for a party to take a position in an ensuing arbitration that the previous award did not completely deal with the disputes between the parties.

A final and conclusive decision on any particular matter by an arbitral tribunal is a decision that will be considered as *res judicata* and will be treated as conclusive and also preclusive in any subsequent proceedings that the same parties may attempt to bring against each other. It is considered as final and conclusive because the original decision is final and binding upon the parties. It is also considered as preclusive because the parties are prohibited from re-arbitrating or relitigating the same matter that has already been finally decided in the earlier original proceedings.

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¹² e.g.,: Article 114 (1) of the Japan Code of Civil Procedure provides that ‘A final and binding judgment, only for the contents thereof that are included in the main text, shall have *res judicata.*’

¹³ The principles of issue estoppel and abuse of process, as additional grounds of *res judicata,* are accepted across most common law jurisdictions. See, e.g., Carl Zeiss Stiftung v. Rayner & Keeler Ltd (No. 2) [1967] 1 A.C. 853 at 935, which held that the same parties to the proceedings involving the same decided issue are bound by an estoppel arising from the earlier original final decision.

¹⁴ The House of Lords in Johnson v. Gore Wood & Co [2000] 2 AC 1 extended the earlier estoppel rule in Henderson v. Henderson (1844) 6 QB 288 to be classified as part of the ‘abuse of process’ doctrine to preclude a party in subsequent litigation from raising an issue that could and should have brought before the court in the earlier proceedings.
IV  DOCTRINE OF COLLATERAL ESTOPPEL ESTABLISHED AS A GENERAL PRINCIPLE OF LAW

Case 1: Amco v. Indonesia

Both international commercial and investment arbitral tribunals have not been consistent in their approach to dealing with the res judicata doctrine when faced with the same issue or dispute that has already been decided by an earlier arbitral tribunal or state court. It appears that the trend of investment tribunals, which have had to deal with issues pertaining to decisions made by earlier tribunals and courts, is to apply the common law approach, including reliance on issue estoppel, rather than the civil law approach, in deciding on res judicata and the preclusionary effects of an earlier international arbitral award.

In the ICSID decision in Amco v. Indonesia, an earlier final ICSID award had been handed down but it had subsequently been partially annulled by an ad hoc committee pursuant to Article 52 of the ICSID Convention. When the matter was presented to a new ICSID tribunal, there were differences in the way the parties wanted the new tribunal to deal with the earlier award. Though both parties agreed that the undisturbed and non-annulled parts of the first award were subjected to the doctrine of res judicata, Indonesia submitted that the new tribunal was mandated to look beyond the dispositive part of the ad hoc committee’s award and to consider the reasoning provided in that award.

Amco claimed in its memorial that, although an earlier finding was res judicata, it was inapplicable in the second arbitration because Indonesian law makes market rate interest applicable to monetary awards for wrongful acts and for unjust enrichment claims. Indonesia took the opposite position and contended that the res judicata character of the finding of the first tribunal did not permit such arguments.

The second tribunal held that: ‘The problem is still to determine whether the reasons of the nullifying body are also res judicata for a subsequent Tribunal. The Orinoco Steamship Company case, Hague Court Reports (1916) 226; 5 AJIL (1911) 20 does not address that particular question.’ It went on to hold that:

*It is by no means clear that the basic trend in international law is to accept reasoning, preliminary or incidental determinations as part of what constitutes res judicata . . . Had the Decision of the ad hoc Committee as to what was and was not annulled (and as to what thus was and was not judicata in the Award) been unclear, all the points in the Decision would undoubtedly have to be relied on to interpret and clarify the dispositif. But the Decision is clear.*

The second tribunal went on to state that:

*If the present Tribunal were bound by “integral reasoning” of the ad hoc Committee, then the present Tribunal would have bestowed upon the ad hoc Committee the role of an appeal court.*

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underlying reasoning of an ad hoc Committee could be so extensive that the tasks of a subsequent Tribunal could be rendered mechanical, and not consistent with its authority as indicated in Article 52(6), which speaks of “the dispute” being submitted to a new Tribunal.17

At the next hearing and in its next decision two years later, the second tribunal held that the decision of the ad hoc committee was to annul with qualifications, but, as the decision went beyond mere affirmation of such illegality, it was not to be treated as res judicata.

ii Case 2: Grynbery v. RSM

The tribunal in Grynberg v. RSM18 had to deal with a contention of issue estoppel pertaining to an investment claim made by RSM who was the claimant in an earlier ICSID arbitration against Grenada (RSM v. Grenada) relating to the breach of an oil exploration agreement.19 The new ICSID arbitration included new claimants. The arbitration was initiated in accordance with a distinct bilateral investment treaty (BIT), but pertained to the same oil exploration agreement.

The parties in the case were agreed as to the requirements for the application of the doctrine of collateral estoppel. They agreed that a finding concerning a right, question or fact may not be relitigated (and is binding on a subsequent tribunal), if 'in a prior proceeding: (a) it was distinctly put in issue; (b) the court or tribunal actually decided it; and (c) the resolution of the question was necessary to resolving the claims before that court or tribunal'.20 The Grynberg tribunal held that: ‘It is also not disputed that the doctrine of collateral estoppel is now well established as a general principle of law applicable in the international courts and tribunals such as this one.’21

The Grynberg tribunal disagreed with the claimants’ submission that the questions that had been ‘put in issue’ in the prior arbitration concerning the agreement and treaty questions had not been considered by the prior tribunal. It held that the claimants’ submission ‘confuses issue preclusion and claim preclusion’.

The Grynberg tribunal relied upon the United States Supreme Court decision in Southern Pacific Railroad v. United States22 which held that:

The general principle announced in numerous cases is that a right, question, or fact distinctly put in issue, and directly determined by a court of competent jurisdiction as a ground of recovery cannot be disputed in a subsequent suit between the same parties or their privies, and, even if the second suit

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17 ibid., at paragraphs 32 and 44.
18 Rachel S. Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg and RSM Production Company v. Grenada, ICSID Case No. ARB/10/6, Award, 10 December 2010.
19 RSM Production Corporation v. Grenada, ICSID Case No. ARB/05/14; the award was issued on 13 March 2009 dismissing all claims (prior arbitration).
20 Rachel S. Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg and RSM Production Company v. Grenada, ICSID Case No. ARB/10/6, Award, 10 December 2010 at paragraph 7.1.1.
21 The Grynberg Tribunal cited Amoco Asia Corporation v. Republic of Indonesia, ICSID Case No. ARB/81/1, Decision on Jurisdiction (Re submitted Case) at paragraph 30 (10 May 1988) paragraph 7.1.2.
22 Southern Pacific Railroad Co v. United States, 168 U.S.1, 48-49 (1897).
Res Judicata in Investment Treaty Arbitration

is for a different cause of action, the right, question, or fact once so determined must, as between the same parties or their privies, be taken as conclusively established so long as the judgment in the first suit remains unmodified.23

The Grynberg tribunal agreed with Grenada, which did not seek to submit that the prior tribunal had not determined the treaty questions that claimants now raised. The tribunal agreed that the findings of the prior tribunal on a series of rights, questions and fact bound the Grynberg tribunal and held that those earlier findings must apply in the assessment of whether the claimants’ present treaty claims are ‘manifestly without legal merit’.24

The Grynberg tribunal held that an essential predicate to the success of each of the claimants’ claims was:

an ability for the tribunal to relitigate and decide in the claimants’ favour conclusions of fact or law concerning the parties’ contractual rights that had already distinctly been put in issue and distinctly determined by the prior tribunal. Since the Tribunal had already concluded, in the answer to the first question it has considered, that it could properly revisit those earlier conclusions, the Tribunal came to the conclusion that each of Claimants’ claims was manifestly without legal merit.25

The Grynberg tribunal felt obligated to dismiss each of claimants’ claims.

V TRADITIONAL CIVIL LAW APPROACH TO RES JUDICATA

Other international investment tribunals have applied the civil law approach to res judicata.

The majority decision in Gavazzi v. Romania26 considered whether the three elements pertaining to the test for res judicata were present. The majority set out the three elements and stated that: ‘Under international law, three conditions need to be fulfilled for a decision to have binding effect in later proceedings: namely, that in both instances, the object of the claim, the cause of action, and the parties are identical.’27

The tribunal had to deal with the respondent’s submission that the Romanian arbitration and the subsequent proceedings concerned the same cause of action. The respondent contended that the claims submitted in the second proceedings, although formally for breaches of the BIT, were in fact contractual claims based upon the share purchase contract. The respondent submitted that in both instances, the relief sought by the claimants for the alleged breaches was compensation through payment of pecuniary damages.28

In contrast, the claimants contended that the subject matters of the dispute in the previous 2002 arbitration and in the subsequent ICSID proceedings were different. That a

23 Rachel S. Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg and RSM Production Company v. Grenada, ICSID Case No. ARB/10/6, Award, 10 December 2010 at paragraph 7.1.3.
24 ibid., paragraph 7.1.3.
25 ibid., paragraph 7.2.1.
26 Marco Gavazzi and Stefano Gavazzi v. Romania, ICSID Case No. ARB/12/25, Decision on Jurisdiction, Admissibility and Liability, 21 April 2015 (‘Majority Decision’ of Professor Hans Van Houtte and VV Veeder, QC).
27 Apotex Holdings Inc. and Apotex Inc. v. United States of America (ICSID Case No. ARB(AF)/12/1), Award, at paragraphs 7.12 – 7.21, 7.31 and 7.59 (25 Aug. 2014).
28 Marco Gavazzi and Stefano Gavazzi v. Romania, ICSID Case No. ARB/12/25, Decision on Jurisdiction, Admissibility and Liability, 21 April 2015 at paragraph 167.
contractual claim and a treaty claim might both aim at obtaining monetary damages (even in similar amounts) was of no relevance, and it did not undermine the distinction between treaty claims and contractual claims. The issue in the 2002 Romanian arbitration was the alleged breach of the share purchase contract in the light of the applicable Romanian law. The issue in the subsequent ICSID proceedings were the alleged breaches of the BIT by the respondent to the prejudice of the claimants as Italian investors protected by the BIT under international law.

The majority of the tribunal found that the claims before them were based upon a breach of the BIT, the decision of which would turn on the provisions of the BIT. The majority held that the Bucharest Court of Appeal proceedings dealt with claims for breach of the share purchase contract governed by Romanian law, the decision of which turned on the duties and rights under that contract.29

The majority tribunal came to the conclusion that under international law:

\[
\text{there is no identity between the cause of the contractual claims put before the Romanian courts and that of the BIT claims put before this Tribunal. For this reason alone, the majority concludes that the Bucharest court decisions cannot have conclusive effect for the Tribunal under the doctrines of res judicata and issue estoppel.}^{30}
\]

The minority member dissented and concluded that the different causes of action of the two separate claims in the earlier proceedings and current proceedings would not stop an issue estoppel from operating. He gave the following dissenting view:

\[
\text{Issue estoppel is to be distinguished from res judicata even if the two doctrines apply common basic principles. . . . One has to distinguish cause of action estoppel from issue estoppel, since the former prevents a party from resubmitting the same claim which was previously decided, while issue estoppel prevents a party from re-litigating a point of law or of fact which was already decided by a previous judgment. . . . The issue estoppel doctrine is applied less frequently than res judicata since some jurisdictions concentrate on res judicata. . . . However, preclusion is a concept generally known to all jurisdictions. The effects of determination of issues by a previous judgment of a state court have then been dealt with.}^{31}
\]

The minority member went on to say that:

\[
\text{In my opinion, the conditions required in order to apply an issue estoppel are not as strict as those for res judicata, even if one does not accept the widening of the scope of res judicata under ILA's Recommendations, which examine the underlying nature of the dispute and are not based on formalistic concepts. To me the requirements for issue estoppel are the identity of the parties in both instances and identity of the facts and findings on which an issue is based (such as when the claims arise out of the same factual situation).}^{32}
\]
It is possible to see, therefore, that there are different approaches to preclusion and the doctrine of *res judicata* under the two different legal systems.

**VI PRIOR DECISIONS OF COURTS AND ARBITRAL TRIBUNALS ON QUESTIONS OF LAW**

If the governing law of an arbitration is common law, courts are obliged to adopt any relevant prior decisions of the higher courts of that legal system. This is because, in addition to applicable statutory legislation, one of the principles of common law is the doctrine of *stare decisis*, which makes decisions enunciated in earlier decisions of higher courts binding until distinguished or overruled. Notwithstanding that arbitral tribunals are not within the court system, in a common law jurisdiction they are still expected to comply with *stare decisis*. This is because domestic tribunals are perceived as being akin to a first instance court in domestic arbitrations and are expected to apply the law as affirmed by previous decisions of the supreme court, appeal and high courts on the same point of law.

Historically, the position of the apex court in England and Wales, then the House of Lords (now the Supreme Court), was that it was bound by its own earlier decisions. This traditional position changed in 1966 following the Practice Statement (Judicial Precedent). The Law Lords started off by stating that they believe in ‘the use of precedent as an indispensable foundation upon which to decide what is the law and its application to individual cases. It provides at least some degree of certainty upon which individuals can rely in the conduct of their affairs, as well as a basis for orderly development of legal rules’. They then concluded that:

> too rigid adherence to precedent may lead to injustice in a particular case and also unduly restrict the proper development of the law. They propose, therefore, to modify their present practice and, while treating former decisions of this House as normally binding, to depart from a previous decision when it appears right to do so.

Although supreme courts of common law jurisdictions are allowed to depart from their own rulings on legal issues, both lower courts and tribunals must still comply with the current pronouncement of law as set out in the supreme court of the seat of the arbitration.

Both civil and common law systems, however, take the same position that any prior decisions of an arbitral tribunal on any question of law is not binding and does not have any precedential value. A subsequent arbitral tribunal is not bound to follow the decision of an interpretation of law in an earlier tribunal award. If the subsequent tribunal finds that the interpretation is persuasive, it may follow the same interpretation but it is not compelled to do so.

As such, and because there is no *stare decisis* nor binding legal precedent to comply with, there is no *res judicata* for any prior arbitral tribunal decisions dealing with legal issues. However eminent the prior tribunal, there is no compulsion on another subsequent tribunal to follow the prior decision on points of law. There have been hundreds of ICSID cases filed.

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33 The Practice Statement (Judicial Precedent) [1966] 1 WLR 1234 dated 26 July 1966.

and this number is ever increasing. As was published by the United Nations Conference on Trade and Development, 'In 2017, at least 65 new investor–state dispute settlement (ISDS) cases were initiated pursuant to international investment agreements (IIAs), bringing the total number of known cases to 855. . . . In 2017, ISDS tribunals rendered at least 62 substantive decisions.'

As the number of investment arbitration awards is also growing rapidly, previous awards have become important sources of jurisprudence to arbitrators, counsel and end-users alike. However, despite the fact that such decisions are being referred to and even constantly cited, the prevailing view of these important tribunal decisions is that they have no precedential effect but are instead, at best, merely persuasive decisions.

Article 38(1)(c) of the Statute of the International Court of Justice states that: 'The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply the general principles of law recognized by civilized nations.' However, Article 59 goes on to state that: ‘The decision of the Court has no binding force except between the parties and in respect of that particular case.’

Article 59, therefore, clarifies that the doctrine of res judicata applies only to the parties and only in respect of the particular case that has been decided. The decisions of the International Court of Justice itself in relation to legal issues are also not considered as res judicata if the same dispute over legal interpretation were to come up between one of the parties to an earlier decision and a new party that was not a party to the earlier court hearing.

Article 53(1) of the ICSID Convention states that: ‘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.’ Article 53(1) can be interpreted to make the point that there is no res judicata or binding case precedent to subsequent ICSID cases dealing with exactly the same issue of fact or law.

The tribunal in AES Corporation v. Argentina agreed with Argentina and stated that the provisions of Article 25 of the ICSID Convention, together with fundamental principles of public international law, dictate that: ‘each decision or award delivered by an ICSID Tribunal is only binding on the parties to the dispute settled by this decision or award.’ The tribunal made the following statement:

There is so far no rule of precedent in general international law; nor is there any within the specific ICSID system for the settlement of disputes between one State party to the Convention and the National of another State Party. This was in particular illustrated by diverging positions respectively taken by two ICSID tribunals on issues dealing with the interpretation of arguably similar language in two different BITs.

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38 AES Corporation v. Argentine Republic (ICSID Case No. ARB/02/17) (Decision on Jurisdiction 26 April 2005).
39 ibid., at paragraph 23(d).
However, after having made this statement, the tribunal then went back on its statement and adopted a contrary position, and rejected the ‘excessive assertion’ that ‘absolutely no consideration might be given to other decisions on jurisdiction or awards delivered by other tribunals in similar cases’.  

The tribunal went on to state that:

An identity of the basis of jurisdiction of these tribunals, even when it meets with very similar if not even identical facts at the origin of the disputes, does not suffice to apply systematically to the present case positions or solutions already adopted in these cases. Each tribunal remains sovereign and may retain, as it is confirmed by ICSID practice, a different solution for resolving the same problem; but decisions on jurisdiction dealing with the same or very similar issues may at least indicate some lines of reasoning of real interest; this Tribunal may consider them in order to compare its own position with those already adopted by its predecessors and, if it shares the views already expressed by one or more of these tribunals on a specific point of law, it is free to adopt the same solution.

In essence, after having made sweeping statements on the limited role of precedential value of the previous decision, the AES tribunal actually went on to examine, consider and rely on previous decisions made by other tribunals.

While it is clear that international investment and commercial arbitration decisions do not hold any precedential value, many tribunals have also walked the fine line between precedent and adopting previous arbitral awards as being of ‘persuasive’ or even ‘extremely persuasive’ status. It has been established practice among many arbitrators to look to prior decisions on the same issue as guidance. The tribunal in LETCO v. Liberia stated that: ‘Though the Tribunal is not bound by the precedents established by other ICSID Tribunals, it is nonetheless instructive to consider their interpretations.’

VII CONTRADICTORY DECISIONS MADE BY DIFFERENT TRIBUNALS AND AVOIDANCE OF RES JUDICATA

In Orascom v. Algeria, the respondent opposed the claim and sought dismissal of the investor’s claims on the ground that the proceeding was an abuse of rights, as the claimant had ‘used his group of companies to seek to maximize his chances of success by introducing several arbitration proceedings against the Respondent at different levels of the chain of companies, which is an additional ground for the inadmissibility of the claims under the doctrine of abuse of rights’.

In essence, the arbitration proceedings were one of three arbitrations that had been filed under different investment treaties by different companies, which were all controlled by the same shareholder. The respondent state complained that there was a risk of multiple proceedings arising out of the same facts, with the ensuing possibility of conflicting outcomes.

40 ibid., at paragraph 27.
41 ibid., at paragraph 30.
42 Liberian Eastern Timber Corporation v. Republic of Liberia, ICSID Case No. ARB/83/2 (Award of the 31 March 1986).
43 Orascom TMT Investments S.a r.l. v. People’s Democratic Republic of Algeria (ICSID Case No. ARB/12/35) (Award dated 31 May 2017).
44 ibid., at paragraph 390.
and multiple recoveries, and that this was likely to be aggravated as Weather Investments, one claimant, had reserved its right to bring an arbitration against Algeria by filing a notice of dispute under the Italy–Algeria BIT, while Orascom Telecom reserved its rights to file ICSID arbitration under the Investment Agreement.45

The tribunal decided against allowing other entities in the vertical chain controlled by the same shareholder to seek protection for the same harm inflicted on the investment. The tribunal held that to do so would give rise to a risk of multiple recoveries and conflicting decisions, not to speak of the waste of resources that multiple proceedings involve. The occurrence of such risks would conflict with the promotion of economic development in circumstances where the protection of the investment is already triggered. The tribunal dismissed the claims as inadmissible and concluded on this point by saying that:

where multiple treaties offer entities in a vertical chain similar procedural rights of access to an arbitral forum and comparable substantive guarantees, the initiation of multiple proceedings to recover for essentially the same economic harm would entail the exercise of rights for purposes that are alien to those for which these rights were established.46

In its concluding remarks, the Orascom tribunal criticised the decisions reached by earlier UNCITRAL arbitral tribunals in the decisions of Lauder v. Czech Republic47 and CME Czech v. Czech Republic,48 and stated that:

it cannot be denied that, in the fifteen years that have followed those cases, the investment treaty jurisprudence has evolved, including on the application of the principle of abuse of rights (or abuse of process), as was recalled above. The resort to such principle has allowed tribunals to apply investment treaties in such a manner as to avoid consequences unforeseen by their drafters and at odds with the very purposes underlying the conclusion of those treaties.49

In Lauder v. Czech Republic and CME v. Czech Republic, the respective arbitral tribunals allowed claims based on the same facts and the seeking of damages for the same harm to continue under different investment treaties. The Orascom tribunal observed that the Czech Republic had refused several offers of consolidation in those cases resulting in the two tribunals reaching contradicting decisions.

The tribunal in Supervision v. Costa Rica50 had to deal with a similar issue but it came to a different conclusion (by a majority) and held that all investment arbitration claims that related to a dispute that had previously been submitted to the respondent state’s courts were inadmissible.

The majority held that:

45 ibid., at paragraph 173.
46 ibid., at paragraph 543.
49 Orascom TMT Investments S.a r.l. v. People’s Democratic Republic of Algeria (ICSID Case No. ARB/12/35) (Award dated 31 May 2017) at paragraph 547.
In any event, the Tribunal is of the view that the strict application of the triple identity test (same parties; same object; and same normative source) applied by some investment tribunals removes all legal effects from fork in the road clauses, which contravenes the effet utile principle applicable to the interpretation of treaties. What, in the end, matters for the application of fork in the road clauses is that the two relevant proceedings under examination have the same normative source and pursue the same aim. This is, in the Tribunal’s view, the case here.\textsuperscript{51}

The majority tribunal members came to this conclusion after comparing the claims in the domestic court proceedings and the investment arbitration proceedings. The tribunal held that: ‘In order to determine whether the proceedings before the local tribunals relate to the same dispute submitted to arbitration, the Tribunal will apply the fundamental basis of a claim test, used in various cases, among them \textit{Pantechniki v. Albania}.’\textsuperscript{52}

In applying the ‘fundamental basis of the claim’\textsuperscript{53} test, the majority concluded that:

\begin{quote}
the actions filed in the local proceeding and in the arbitration share a fundamental normative source and pursue ultimately the same purpose. The fundamental normative source is the same because compensation was claimed for lost profits derived from the failure of Costa Rica to adjust the VTI [Vanguard Total Stock Market Index] service rates according to what Claimant alleges was established in the Contract.\textsuperscript{54}
\end{quote}

The majority decision did not consider the fact that the causes of action in the two different forums were distinct in the sense that one was brought under an international treaty while the other was subject to domestic law. More importantly, the two separate cases had been initiated by different parties and the specific administrative acts alleged in each of the proceedings may not have been exactly the same. The dissenting opinion took the view that: ‘\textit{Riteve} and \textit{SyC} cannot be viewed as being identical. Secondly, even if they were identical, the applications by Riteve to local tribunals did not and do not constitute an attempt to litigate the same issues that are presented here.’\textsuperscript{55}

One of the perennial problems in investment arbitration is the lack of consistency and reasoning of decisions, particularly in situations where members of tribunals who sit in different cases reach contradictory conclusions when dealing with identical issues.

\textsuperscript{51} ibid., at 330.
\textsuperscript{52} ibid., at 330. Referring to \textit{Pantechniki S.A. Contractors & Engineers v. Republic of Albania}, ICSID Case No. ARB/07/21 (Award 30 July 2009).
\textsuperscript{53} This ‘fundamental basis of a claim’ emanated from the approach used by the tribunal in \textit{Pantechniki S.A. Contractors & Engineers v. Republic of Albania} (ICSID Case No. ARB/07/21) (Award 30 July 2009 at paragraphs 61-64).
\textsuperscript{54} \textit{Supervision y Control S.A. v. Republic of Costa Rica} (ICSID Case No. ARB/12/4) (Majority Award 18 January 2017) at 315.
\textsuperscript{55} \textit{Supervision y Control S.A. v. Republic of Costa Rica} (ICSID Case No. ARB/12/4) (Minority view of Klock, J. P. 18 January 2017) at page 7.
VIII SITUATIONS WHERE ONE TRIBUNAL REFERS TO AND RELIES UPON THE DECISION OF A PRIOR TRIBUNAL

In the case of Helnan v Egypt, the tribunal had to deal with a prior arbitral award that had been issued by an earlier tribunal sitting at the Cairo Regional Centre for International Commercial Arbitration (the CRCICA award). The Helnan tribunal decided that the CRCICA award was res judicata within Egypt, but it also went on to state that: ‘A national court and even less a private arbitral tribunal do not have the same authority. They are not performing their duties in the same legal order and their jurisdiction does not have the same scope.’

The Helnan tribunal came to the conclusion that a decision by a national court or by a private arbitral tribunal cannot be opposed as res judicata to the admissibility of an action filed with an international arbitral tribunal but an international tribunal must accept the res judicata effect of a decision made by a national court within the legal order where it belongs.

The tribunal then relied upon the dissenting opinion of Professor Cremades in Fraport v. Republic of the Philippines where Professor Cremades stated that:

The ICSID tribunal is not bound by the decision of the Philippine court, even the Supreme Court, but its own judgment on Philippine law must be premised on the Philippine law itself. It is res judicata in Philippine law that the Terminal 3 concession is null and void ex tunc and not ex nunc, and this must be accepted by the arbitral tribunal. . . . the tribunal should respect the consequences of the Supreme Court decision.

The Helnan tribunal took the view that even if the CRICA award and itself were addressing the same legal order, the CRICA award could not be opposed as res judicata to the admissibility of Helnan’s claims. Its reasoning was that ‘for an earlier final decision, issued by a competent court or arbitral tribunal, to be conclusive in subsequent proceedings, three cumulative basic conditions must be met: identity of parties, identity of subject matter or relief sought and identity of legal grounds or causes of actions.’ It held that the three cumulative conditions were not met in the instant case.

It is useful to contrast the position taken by the Helnan tribunal with the position taken by the tribunal in SGS v Philippines. The SGS v. Philippine tribunal stated that:

the present Tribunal does not in all respects agree with the conclusions reached by the SGS v. Pakistan Tribunal on issues of the interpretation of arguably similar language in the Swiss-Philippines BIT. This raises a question whether, nonetheless, the present Tribunal should defer to the answers given by

56 Helnan International Hotels A/S v. Arab Republic of Egypt, ICSID Case No. ARB/05/19 (Award of 3 July 2008).
57 ibid., at 124.
58 ibid., at 125.
59 ibid., at paragraph 125 where the Helnan tribunal cited paragraph 26 of the Dissenting Opinion of Professor Cremades from Fraport AG Frankfort Airport Services Worldwide v. Republic of the Philippines of 16 August 2007.
60 Helnan International Hotels A/S v. Arab Republic of Egypt, ICSID Case No. ARB/05/19 (Award of 3 July 2008) at 126.
Moreover, there is no doctrine of precedent in international law, if precedent is meant as a rule of the binding effect of a single decision.30

There is no hierarchy of international tribunals and, even if there were, there is no good reason for allowing the first tribunal to resolve issues for all later tribunals:

"Initially, it must be for the control mechanisms provided for under the BIT and the ICSID Convention, and in the longer term for the development of a common legal opinion or jurisprudence constante, to resolve the difficult legal questions discussed by the SGS v. Pakistan Tribunal and also in the present decision."62

The tribunal in Joy Mining v. Egypt63 took a more interesting path and refused to be drawn into the different views taken by the two tribunals, and stated that:

"There has been much argument regarding recent cases, notably SGS v. Pakistan and SGS v. Philippines. However, this Tribunal is not called upon to sit in judgment on the views of other tribunals. It is only called to decide this dispute in the light of its specific facts and the law, beginning with the jurisdictional objections."64

IX CONCLUSION

Tribunals and counsel alike need to look carefully into the facts of the case whenever they are faced with a dispute where the same issue has already been adjudicated upon by a state court or by a prior tribunal. The continuing debate in the breadth and approach as to how the doctrine of res judicata is to be implemented differs between legal systems and also between countries from the same type of legal system. This difficulty continues to lie at the implementation and scope of res judicata continuing to be tied down and dependent upon the law at the place of arbitration. There is no easy fix to this dilemma, but counsel and tribunals will need to understand the fundamental position of res judicata within the place of arbitration.

Although many arbitrators do tend to cite from prior ICSID or UNCITRAL investment awards in their own arbitral decisions, this may be fraught with potential danger. Depending on the factual circumstances, situations can be envisaged where clever counsel might try to mount an attack on an award on the basis that it has relied (or overly relied) upon a prior

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62 ibid., at 97.
63 Joy Mining Machinery Ltd v. Egypt, ICSID Case No. ARB/03/11 Award on Jurisdiction dated 6 August 2004.
64 ibid., at 80.
decision made by one or more tribunals in ICSID awards. It is quite possible for challenges to be made to an ICSID award on the basis that there has been inadequate detailed reasoning made by a tribunal and that it relied exclusively upon previous ICSID decisions.

Such awards might be susceptible to attack during an annulment process on the ground that the tribunal did not actually conduct any reasoning process itself, but instead relied overly (or fully) on ‘precedents’ in the form of often-cited earlier ICSID or UNCITRAL awards on the same point. Such a tribunal could well be accused of having acted in excess of its duties and failing to set out reasoning because the tribunal had decided to adopt and rely upon earlier awards without giving the parties a proper chance to deal with the earlier awards and to make submissions about such proposed reliance. If the challenging party can also show that there was a complete failure to state reasons, it could show that the tribunal had not come to its own independent decision but had allowed the decision-making process to be dictated by prior awards that have no precedential value at all.

The pressure of trying to find consistency when faced with the tests for *res judicata* is ongoing. Claimants will continue to seek to migrate from prior domestic court litigation onto the international investment treaty platform, while respondents will try to beat them back following the stricter tests of *res judicata*.

However, as more and more discourse and interaction take place between lawyers from the different systems of laws, it is hoped that the increasing number of decisions of investment treaty arbitral tribunals are likely to establish a more universal approach towards the doctrine of *res judicata*. It is possible that the increasing volume of investment arbitration awards will slowly generate the development of an accepted set of norms and standards as decisions made in prior awards get thoroughly evaluated by subsequent tribunals, academics, international legal bodies and by the states themselves.
Part IV

SUBSTANTIVE PROTECTIONS
FAIR AND EQUITABLE TREATMENT

Andre Yeap SC, Paul Tan, Matthew Koh and David Isidore Tan

I INTRODUCTION

The fair and equitable treatment (FET) standard in investment protection treaties remains at the core of states’ obligations and thus many disputes. With notable exceptions, particularly in the newer generation of treaties, the FET standard is also often left undefined. Notwithstanding that, tribunals have elaborated on this standard to develop both substantive and procedural principles. This chapter will provide a brief review of these standards and highlight some of the more recent cases.

II RECENT CASES ON THE PRINCIPLES OF FET

1 CC/Devas (Mauritius) Ltd, Devas Employees Mauritius Private Limited and Telecom Devas Mauritius Limited v. India

The claimants, three Mauritian companies, initiated proceedings against India pursuant to the Agreement between the Government of the Republic of Mauritius and the Government of the Republic of India for the Promotion and Protection of Investments (the Treaty), which entered into force on 20 June 2000. The claimants were shareholders of Devas Multimedia Private Limited (Devas), which had entered into a contract with Antrix Corporation Limited, an Indian state-owned company, in 2005 for the lease of part of the electromagnetic spectrum for the purposes of offering wireless broadband access and audio-video services throughout India. In 2011, Devas was notified that the contract had been annulled by India, following the government’s decision to reserve a part of the electromagnetic spectrum for ‘national needs’. The claimants contended that the annulment amounted to an expropriation of their investment and alleged that the expropriatory nature of India’s actions and the violation of their legitimate expectations as investors constituted a breach of the FET standard under the Treaty.

The tribunal held that India had breached the FET standard under the Treaty by frustrating the claimants’ legitimate expectations that India would deal with them in good faith. India did not deal with the claimants in good faith because it failed to inform them...

1 Andre Yeap SC is a senior partner, Paul Tan is a partner, Matthew Koh is a senior associate and David Isidore Tan is an associate at Rajah & Tann Singapore LLP.
3 See Article 9.4 of the Singapore–European Union Free Trade Agreement. See especially fn 11 of Chapter 9.
about the decision to annul the contract, which was taken in 2010. The text of the Treaty and the general obligation of good faith under international law formed the basis of such a legitimate expectation:

_The preamble of the Treaty mentions the desire of the Contracting Parties “to create favourable conditions for greater flow of investments.” In Article 3(2), it states that “[e]ach Contracting Party shall in accordance with its laws render assistance to the investors of the other Contracting Party, whose investments were made in its territory, for obtaining the required clearances and permissions.” To these general statements must be added the provisions of Articles 4 and 6 of the Treaty dealing with the treatment of investments and expropriation which have already been extensively considered in this award._

_If one searches for a general obligation of good faith under international law, one need not go further than the Vienna Convention on the Law of Treaties in which one can find no less than five mentions of the requirement of good faith. This principle of good faith is not only self-standing, but it also stems from the concept of FET. In this regard, the Tribunal agrees with the Tecmed panel that “the commitment of fair and equitable treatment . . . is an expression and part of the bona fide principle recognized in international law.”_  

The tribunal also addressed the parties’ arguments on whether the FET standard was the same as the minimum standard of treatment under customary international law, stating that customary international law ‘ha[d] evolved since 1926’ and the _Neer v. Mexico_ decision therefore did not reflect the current FET standard. Ultimately, the tribunal emphasised that legitimate expectations was a central feature of the FET standard regardless of its exact content and scope in this particular case:

_The Tribunal need not enter into a lengthy discussion of the concept and scope of the FET standard in general. Suffice it to say for the purpose of this case that, whatever the scope of the FET standard, the legitimate expectations of the investors have generally been considered central to its definition. That concept however is not unlimited._

ii **Olin v. Libya**

The claimant initiated proceedings against Libya pursuant to the Agreement on the Promotion and the Reciprocal Protection of Investments between the Government of the Republic of Cyprus and the Great Socialist Libyan Arab Jamahiriya of 30 June 2004 (the Agreement), alleging that Libya had breached several obligations under the Agreement, including the obligation to extend FET to Cypriot investors. The dispute arose out of Libya’s expropriation of the land on which the claimant’s factory was erected. In the 1990s, Libya initiated a series of legislative and economic reforms designed to attract foreign investment, including the Libyan Investment Law enacted in 1997. The claimant decided to invest in a factory in

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5 *Devas v. India*, para. 465.
7 *Devas v. India*, para. 456.
8 ibid., para. 463.
9 *Olin Holdings Ltd v. State of Libya*, ICC Case No. 20355/MCP (Award of 25 May 2018) (_Olin v. Libya_).
Libya and subsequently obtained governmental approvals to build and operate its factory. In November 2006, the claimant received an eviction order on the factory and only then became aware of an order issued a month earlier that had expropriated the claimant’s land.

The tribunal held that Libya violated the FET standard on several counts.

First, the claimants’ legitimate expectations that Libya was willing to establish an environment favourable to foreign investments were frustrated by Libya’s disregard of its Investment Law in expropriating the claimant’s land. Changes in Libya’s national and international legislative frameworks in the 1990s, combined with public declarations and assurances by Libyan authorities, were fundamental to the claimant’s decision to invest in Libya and gave rise to such legitimate expectations.¹⁰

Second, Libya’s measures prevented the claimants from operating its investment with a ‘minimum level of certainty as to its fate and . . . ability to implement basic business decisions in an unfettered manner’,¹¹ breaching the FET standard. Libya had transferred legal title of the land from the claimant to another party, attempted to evict it, destroyed buildings next to the claimants’ factory and surrounded the factory with the army.¹² This ‘rendered the fate of the claimant’s investment uncertain and undermined its ability to plan and to gain the confidence of its business partners’.¹³

Third, Libya’s failure to act in a transparent manner breached the FET standard as the claimant was only informed of the expropriation order several weeks after its enactment.¹⁴ The tribunal stated the requirements of transparency as follows:

_In the Tribunal’s view . . . a minimum requirement of fairness and equity would entail that investors are informed in advance that a decision to expropriate their investment is contemplated, and are given a reasonable opportunity to engage in a dialogue with the government to find an adapted solution._¹⁵

Fourth, Libya’s failure to authorise the importation of new equipment, to allow repatriation of the claimants’ profits and to assist it in accessing foreign currency, as well as attempting to restart domestic proceedings over the legality of the expropriation order, were in breach of the FET standard.¹⁶ However, the tribunal was not convinced that the liquidation of the claimant was in breach of FET as it had not been proven that Libya’s motives were ‘hostil[e]’.¹⁷

Fifth, Libya’s failure to afford the claimant administrative due process was in breach of the FET standard. There was a lack of transparency in the decision-making process of Libyan authorities, contradictory approaches of different governmental entities and the expropriation order did not comply with the Libyan Investment Law.¹⁸

However, the claimant failed to prove that there was lack of due process or a denial of justice before the Libyan courts. The tribunal observed that the standard to establish a denial of justice was high and it was necessary to show that court proceedings were in breach of due

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¹⁰ ibid., para. 308.
¹¹ ibid., para. 311.
¹² ibid., para. 314.
¹³ ibid., para. 316.
¹⁴ ibid., paras. 324-325.
¹⁵ ibid., para. 322.
¹⁶ ibid., para. 345.
¹⁷ ibid., para. 344.
¹⁸ ibid., para. 347.
process and were so unfair that they amounted to a denial of justice.\textsuperscript{19} Thus, a three-year delay in the claimant’s court proceedings and insufficiently substantiated bribery allegations failed to establish a denial of justice.\textsuperscript{20} The tribunal noted that unfair decisions could only constitute a denial of justice ‘if its shocking nature implies a breach of due process’.\textsuperscript{21}

iii Marfin v. Cyprus\textsuperscript{22}

The claimants initiated proceedings against Cyprus pursuant to the Agreement between the Government of the Hellenic Republic and the Government of the Republic of Cyprus for the Reciprocal Promotion and Protection of Investments, which entered into force on 26 February 1992, alleging that Cyprus breached several obligations under it, including the obligation to accord FET to Greek investors. The dispute concerned Cyprus’ issuance of a decree that increased the government’s participation in the Cyprus Popular Bank (the Bank) in which the claimants had invested, allegedly resulting in the takeover and removal of the Bank’s management and the Bank’s subsequent dissolution.

Addressing Cyprus’ contention that the state’s ‘margin of appreciation’ should be given due regard by the tribunal in determining whether the measures were proportional and therefore not in breach of the FET standard, the tribunal declined to consider whether the margin of appreciation theory, which was developed in international human rights jurisprudence, applied in international investment law. The tribunal emphasised that it was ‘not the role of an international arbitral tribunal to evaluate the substantive correctness of economic and policy choices made by a State’, and limited its consideration of proportionality to whether the measures had a ‘reasonable relationship to some rational policy’ and were ‘appropriately tailored so as not to impose an excessive burden on an investor’.\textsuperscript{23}

The tribunal also rejected the claimant’s contention that a breach of the expectation that Cyprus would conduct itself impartially, regularly and reasonably constituted a separate legal basis for finding a breach of the FET standard. Instead, the FET standard, ‘in and of itself, establishe[d] such an obligation’.\textsuperscript{24}

The tribunal rejected all claims of Cyprus’ violation of the FET standard.

First, the tribunal drew from its expropriation analysis, relating to the same impugned measure, that Cyprus’ conduct did not breach the FET standard as it was ‘not arbitrary, capricious, unrelated to a rational policy or manifestly lacking in even-handedness’.\textsuperscript{25}

Second, contrary to the claimants’ contentions, the tribunal found no discrimination of the Bank on the basis of its Greek nationality, which amounted to a violation of the FET standard. The tribunal compared the treatment of the Bank to the treatment of the Bank of Cyprus as both banks were comparable in size, systemically important for the health of the country’s financial system, similarly exposed to the Greek market, registered in Cyprus and traded on the Cyprus Stock Exchange, and required recapitalisation.\textsuperscript{26} There was no

\textsuperscript{19} ibid., para. 349.
\textsuperscript{20} ibid., paras. 350-351.
\textsuperscript{21} ibid., para. 352.
\textsuperscript{22} Marfin Investment Group Holdings S.A., Alexandros Bakatselos and others v. Republic of Cyprus, ICSID Case No. ARB/13/27 (Award of 26 July 2018) (Marfin v. Cyprus).
\textsuperscript{23} ibid., para. 1213.
\textsuperscript{24} ibid., para. 1215.
\textsuperscript{25} ibid., para. 1218.
\textsuperscript{26} ibid., para. 1241.
discrimination in the treatment of the Bank with respect to the removal of its management, as management in both banks were removed after emergency financial assistance was offered by the state. There was also no discrimination with regard to the state's grant of emergency liquidity assistance on the facts. Finally, the difference of treatment that led to the Bank's dissolution and the Bank of Cyprus' recapitalisation was de minimis as the existing shareholders and bondholders in both banks were 'completely wiped out'.

Third, the tribunal dismissed the claimant’s contentions that Cyprus breached the FET standard by failing to provide due process to their investment. The tribunal rejected the argument that the issuance of a worldwide freezing order of the claimant’s funds constituted a denial of justice by Cypriot courts, since the claimants failed to exhaust local remedies by appealing the decision and there was no opportunity for the judicial system to correct itself. Further, the tribunal rejected the argument that Cyprus failed to afford due process to the claimants and engaged in arbitrary and abusive conduct in the criminal proceedings initiated against its witnesses in the arbitration, as these allegations were not proven on the facts. Finally, the tribunal rejected the complaint that Cyprus had embarked on a 'public campaign of vilification and harassment’ against the claimants, on the ground that public statements by two Cypriot officials did not demonstrate ‘an animus’ against them and, in any case, were not sufficient to outweigh the evidence that their due process rights were complied with.

The other claims of Cyprus’ breach of the FET standard were not sufficiently supported by the evidence. The claimants contended that Cyprus failed to engage with the Bank’s recapitalisation plan, failed to quell rumours about the Bank's liquidity and viability, removed the claimants-led management of the Bank, was responsible for the conduct of the management of the Bank after December 2011 and intentionally deterred private investment in the Bank.

iv South American Silver v. Bolivia

The claimants initiated proceedings against Bolivia pursuant to the Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Republic of Bolivia for the Promotion and Protection of Investments BIT of 24 May 1988, alleging that Bolivia expropriated the claimant’s investment and failed to accord FET to it. The dispute concerned events leading up to and following Bolivia’s 2012 Reversion Decree, which revoked mining concessions that had been granted to the claimant’s subsidiary, Compañía Minera Malku Khota (CMMK). CMMK’s mining project was located in an area inhabited by various indigenous communities, which opposed the project, resulting in demonstrations and violent clashes.

27 ibid., para. 1245.
28 ibid., para. 1246.
29 ibid., para. 1247.
30 ibid., para. 1272.
31 ibid., paras. 1282-1299.
32 ibid., paras. 1306-1308.
33 ibid., paras. 1219-1232.
In relation to the claimant’s contention that Bolivia frustrated its legitimate expectations and failed to guarantee a stable legal and business framework in connection with its investment as a result of the Reversion Decree, a majority of the tribunal held that:

"the investor is entitled to protection of its legitimate expectations provided (i) that it exercised due diligence, and (ii) that its legitimate expectations were reasonable in light of the circumstances. The circumstances to be taken into consideration by the investor are not merely legal in nature, but they should also include the social, cultural, and economic environment of the host State of the investment, amongst other factors." 35

Further, the FET standard did not ‘entail relinquishing [states’] regulatory powers in the public interest or the need to adapt their legislation to changes and emerging needs’. 36

The majority found that there was no breach of legitimate expectations as the Reversion Decree was an expropriation, which had been a lawful measure under the BIT, in the case of Bolivia’s failure to make compensation. Furthermore, the claimant should have known about the particular political, social, cultural and economic circumstances in which it had invested in Bolivia. 37 The majority also held that the CMMK contributed to the social unrest by ‘generating divisiveness and escalating the clashes within the indigenous communities’. 38

There was also no violation of the FET standard in Bolivia’s actions preceding the Reversion Decree. The claimants could not claim that Bolivia’s immobilisation of the area surrounding its concession areas prevented the expansion of the project as it did not have rights over the immobilised areas and did not communicate any intention of expanding its projects to Bolivia. 39 The claimant’s contentions that Bolivia stoked opposition to the project to gain control of the mining concessions or that escalation of conflict was attributable to Bolivia’s conduct was not supported on the facts. 40 Bolivia’s alleged failure to deploy armed forces to protect CMMK’s employees and assets from alleged threats and actions by community members who opposed the project was not established on the facts. 41 Moreover, there was no evidence that militarisation of the area would have been an appropriate remedy to the social conflict or would have allowed the project to continue. 42

**v Bolivia v. Chile** 43

On 24 April 2013, Bolivia filed an application in the International Court of Justice instituting proceedings against Chile pursuant to the Pact of Bogotá, concerning a dispute relating to Chile’s alleged obligation to negotiate in good faith an agreement to grant Bolivia full sovereign access to the Pacific Ocean. Among other claims, Bolivia contended that Chile’s

35 ibid., para. 648.
36 ibid., para. 649.
37 ibid., para. 655.
38 ibid., para. 656.
39 ibid., paras. 622-623.
40 ibid., para. 664.
41 ibid., para. 671.
42 ibid., para. 672.
43 *Obligation to Negotiate Access to the Pacific Ocean (Bolivia v. Chile)*, Merits, Judgment, International Court of Justice, 1 October 2018 (*Bolivia v. Chile*).
denial of its obligation to negotiate and refusal to engage in further negotiations frustrated Bolivia’s legitimate expectations, a principle that had been widely applied in investment arbitration.

The Court held that the concept of legitimate expectations arose only in the context of investor–state disputes relating to FET guaranteed by treaties. Legitimate expectations, therefore, did not exist as a principle in general international law, which could give rise to a binding obligation on the part of Chile.44

vi Islamic Republic of Iran v. United States of America45

On 14 June 2016, Iran filed an application in the International Court of Justice instituting proceedings against the United States concerning a dispute over alleged violations by the United States of the Treaty of Amity, Economic Relations and Consular Rights, which entered into force on 16 June 1957. The dispute concerned the United States’ amendment of its Foreign Sovereign Immunities Act in 1996, which allowed assets owned by Iranian state entities to be made available for the satisfaction of judgment creditors, effectively removing the sovereign immunities previously accorded to such entities. Among other claims, Iran contended that the Court had jurisdiction to entertain the dispute as the United States’ failure to accord sovereign immunities to Iranian state entities breached its obligation to guarantee FET to Iranian nationals and companies under the Treaty.

The Court rejected Iran's contention that the FET provision under the treaty included an obligation to respect the sovereign immunities of the state and its entities under customary international law.46 Having regard to the context of the FET provision, the Court observed that its purpose was to guarantee certain rights and minimum protections for the benefit of natural persons and legal entities engaged in commercial activities. The FET provision, therefore, could not be interpreted as incorporating, by reference, the customary rules on sovereign immunities.47

44 ibid., para. 162.
46 Islamic Republic of Iran v. United States of America, para. 74.
47 ibid., para. 58.
Chapter 16

MOST FAVOURED NATION TREATMENT

Arthur Ma

I INTRODUCTION

Most favoured nation (MFN) treatment is a core element in bilateral investment treaties (BITs) and other international investment agreements. Like many other standards of investment protection offered under BITs, MFN treatment is designed to avoid discrimination. The purpose of an MFN clause is to provide a mechanism to ensure that each party to a treaty receives at least as favourable of terms as the other party offers to any third party.

The increase of investment disputes settled by international arbitration has had a strong impact on the substantive standards of investment protection provided by investment agreements. Before 2000, judicial and arbitral arguments regarding MFN clauses largely focused on the application of its substantive protection arising from the provisions of an investment treaty. Since the Maffezini v. Spain decision before the International Centre for Settlement of Investment Disputes (ICSID) in January 2000, there has been a large shift in the discussion in international investment dispute practice from substantive protections to the possibility of importing more favourable procedural provisions from other third-party BITs, such as international dispute resolution mechanism. While a number of cases have looked into the scope and interpretation of MFN clauses regarding dispute resolution provisions, the decisions among the arbitral tribunals have been inconsistent.

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3 ‘Most Favoured Nation Treatment Application in International Investment Arbitration: A Study on Conflicting Precedence in International Dispute Settlement Procedure’ (University of Oslo, 2011), p. 3. Available at: https://www.duo.uio.no/bitstream/handle/10852/22714/Master_thesis.pdf?sequence=1.
4 ibid.
While the MFN clause is still a cornerstone of modern commercial treaties, it has now become a controversial issue in investment treaties, and the subject of differing and unexpected interpretations by arbitral tribunals. Conflicting arbitral awards regarding the interpretation of MFN clauses have created difficulties in accurately assessing commercial and litigation risks for contracting parties.

This chapter will review the background of MFN treatment, examine arbitral cases with differing decisions on the application of MFN clauses to dispute settlement and, finally, introduce some recent recommendations on drafting MFN clauses suggested by the United Nations Conference on Trade and Development (UNCTAD), which are likely to shape MFN provisions.

II BACKGROUND

MFN treatment has been a central pillar of commercial treaties for centuries. MFN clauses are first found in international trade agreements going back to at least the 11th century. The earliest structure of an MFN clause resembling the current form was found in the 15th century, with the use of MFN clauses in investment treaties becoming a common practice in the 17th century. The MFN clause was originally used mainly with the aim of preventing discrimination in international trade. It was then extended to the area of international investments, first appearing in friendship, commerce and navigation treaties, and then BITs, with the aim of promoting and protecting international investments.

MFN treatment is intended to establish a ‘level playing field’ and ensure ‘equality of competitive opportunities’ among foreign investors from different countries. The International Court of Justice (ICJ) also states that the purpose of the MFN clause in BITs is ‘to establish and to maintain at all times fundamental equality without discrimination among all of the countries concerned’.

While there is no universal, internationally recognised definition and form of an MFN clause, as the MFN clause has become a standard of international investment treaties, the

19 Case Concerning Rights of Nationals of the United States of America in Morocco (France v. United States of America) (1952) ICJ Rep 176, p. 192.

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Most Favoured Nation Treatment

International Law Commission (ILC) in 1964 started a multi-year project to compose a set of draft articles on MFN clauses, which was finally published in 1978 as the Draft Articles on Most-Favoured-Nation Clauses (the ILC Draft Articles).\(^{20}\) The ILC Draft Articles provide a general analysis of MFN clauses and insight into the *ejusdem generis* (meaning ‘of the same kind’) principle, which has been used in the interpretation of a number of judicial and arbitral cases.\(^ {21}\) Although the ILC Draft Articles are not a binding agreement, they do explore the definition and provide guidance and rules governing the operation of MFN clauses.\(^ {22}\)

Article 4 of the ILC Draft Articles on MFN clauses states that: ‘[a] most-favoured-nation clause is a treaty provision whereby a State undertakes an obligation towards another State to accord most-favoured-nation treatment in agreed sphere of relations.’\(^ {23}\)

Article 5 of the ILC Draft Articles defines MFN treatment as follows:

*Most-favoured-nation treatment is treatment accorded by the granting State to the beneficiary State, or to persons or things in a determined relationship with that State, not less favourable than treatment extended by the granting state to a third State or to persons or things in the same relationship with that third State.\(^ {24}\)*

The ILC Draft Articles also describe the basic structure of the operation of MFN clauses, including the source\(^ {25}\) and scope\(^ {26}\) of MFN rights.

According to Article 9 of the ILC Draft Articles, the beneficiary state of MFN treatment can only request for more favourable treatment accorded to a third state when it falls within the limits of the subject matter of the MFN clause. This reinforces the *ejusdem generis* principle, which is a generally recognised principle of international law.\(^ {27}\)


\(^{22}\) Radi, p. 758.

\(^{23}\) Article 4 of the ILC Draft Articles.

\(^{24}\) Article 5 of the ILC Draft Articles.

\(^{25}\) Article 8 of the ILC Draft Articles states that ‘1. The right of the beneficiary State to most-favoured-nation treatment arises only from the most-favoured-nation clause referred to in article 4, or from the clause on most-favoured-nation treatment referred to in article 6, in force between the granting State and the beneficiary State. 2. The most-favoured-nation treatment to which the beneficiary State, for itself or for the benefit of persons or things in a determined relationship with it, is entitled under a clause referred to in paragraph 1, is determined by the treatment extended by the granting State to a third State or to persons or things in the same relationship with that third State.’

\(^{26}\) Article 9 of the ILC Draft Articles states that ‘1. Under a most-favoured-nation clause the beneficiary State acquires, for itself or for the benefit of persons or things in a determined relationship with it, only those rights which fall within the limits of the subject-matter of the clause. 2. The beneficiary State acquires the rights under paragraph 1 only in respect of persons or things which are specified in the clause or implied from its subject-matter.’

\(^{27}\) *Anglo-Iranian Oil Co. Case (United Kingdom v. Iran)* (Preliminary objection) [1952] ICJ Rep 93, p. 110.
In the context of the application of MFN clause, many arbitral tribunals have invoked *ejusdem generis* to limit applicability to issues belonging to the same subject matter or the same category of subjects to which the treaty or clause relates. For example, in *Maffezini*, the tribunal explained that:

> if a third-party treaty contains provisions for the settlement of disputes that are more favourable to the protection of the investor's rights and interests than those in the basic treaty, such provisions may be extended to the beneficiary of the most favoured nation clause as they are fully compatible with the *ejusdem generis* principle.  

This principle restricts the application of an MFN clause to the subject matter regulated by the treaty in question.

To better understand the scope of application of MFN clauses to be discussed in the following section, it is important to consider the legal nature and qualifications of MFN treatment, which are summarised by UNCTAD as follows:

1. It is a treaty-based obligation that must be contained in a specific treaty;
2. It is a relative standard, which means that it implies a comparative test;
3. It is governed by the *ejusdem generis* principle;
4. It requires a legitimate basis of comparison, i.e. similar objective situations;
5. It relates to discrimination on grounds of nationality;
6. It requires a finding of less favourable treatment;
7. It operates without prejudice to the freedom of contract;
8. It works differently from the MFN clause in the trade context; and
9. It has to be interpreted in the light of general principles of treaty interpretation.

**III APPLICATION OF AN MFN CLAUSE TO DISPUTE SETTLEMENT PROVISIONS**

In the past two decades, one of the most controversial issues regarding MFN treatment before arbitral tribunals has been whether a party can import procedural rules from a third-party treaty, and in particular, whether the MFN clause can allow for the incorporation of dispute settlement provisions contained in a third-party treaty when the wording of the MFN clause does not explicitly provide for such terms.

**i Maffezini v. Spain**

*Maffezini* was the first case in which a tribunal held that an investor could import favourable dispute settlement provisions from a third-party treaty through an MFN clause. This ICSID arbitration case arose from a dispute between an Argentine investor who had invested in an enterprise in Spain. Spain raised an objection to the jurisdiction of the arbitral tribunal on

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28 *Maffezini*, para. 55.
29 UNCTAD, 'Most-favoured nation treatment', p. 21–33.
30 Basic treaty is the treaty with MFN clause, which governs the rights of the beneficiary under the MFN clause.
31 Radi, p. 760.
the ground that the claimant failed to fulfil a condition precedent provided in the Argentina–Spain BIT that required the claimant to first bring the dispute to Spanish courts for 18 months before resorting to international arbitration.\(^{32}\)

The claimant failed to meet the condition precedent and averred that the arbitral tribunal had jurisdiction because of the MFN clause contained in the Argentina–Spain BIT provided that: ‘In all matters subject to this agreement, this treatment shall not be less favourable than that extended by each Party to the investments made in its territory by investors of a third country.’\(^{33}\)

The claimant pointed out that the Chile–Spain BIT contained no condition precedent equivalent to that contained in the Argentina–Spain BIT. The claimant therefore argued that Chilean investors were treated more favourably than Argentine investors in Spain, and therefore it relied on the more favourable dispute resolution provisions of the Chile–Spain BIT to forego Spanish courts. The tribunal upheld the claimant’s position.

The tribunal considered that ‘[t]oday dispute settlement arrangements are inextricably related to the protection of foreign investors, as they are also related to the protection of rights of traders under treaties of commerce.’\(^{34}\) The tribunal also welcomed the fact that the ‘application of the MFN clause to dispute settlement arrangements in the context of investment treaties might result in the harmonisation and enlargement of the scope of such arrangements.’\(^{35}\)

The subject matter of the MFN clause at issue in \textit{Maffezini} was particularly broad and sufficiently vague, which explicitly referred to ‘all matters subject to this agreement’.\(^{36}\) Being aware of the revolutionary nature of its decision, the tribunal tried to set limits to the application of MFN clauses:

\begin{quote}
\textit{As a matter of principle, the beneficiary of the clause should not be able to override public policy considerations that the contracting parties might have envisaged as fundamental conditions for their acceptance of the agreement in question, particularly if the beneficiary is a private investor. . . .}

\textit{[A] distinction has to be made between the legitimate extension of rights and benefits by means of the operation of the clause, on the one hand, and disruptive treaty-shopping that would play havoc with the policy objectives of underlying specific treaty provisions, on the other hand.}\(^{37, 38}\)
\end{quote}

In addition, the tribunal also emphasised the importance of identifying the contracting parties’ intention and assessing the past practice of states regarding the MFN clauses in BITs with other countries.\(^{39}\)


\(^{33}\) \textit{Maffezini}, para. 38.

\(^{34}\) ibid., para. 54.

\(^{35}\) ibid., para. 62.


\(^{38}\) \textit{Maffezini}, paras. 62-63.

\(^{39}\) ibid., para. 49, 57-58; See also ‘Most Favoured Nation Treatment Application in International Investment Arbitration: A Study on Conflicting Precedence in International Dispute Settlement Procedure’, p. 31.
ii  **Plama v. Bulgaria**

The *Plama* case stands in contrast to the *Maffezini* decision. This ICSID arbitration case arose from a dispute between a Cypriot investor and Bulgaria, concerning damage caused to a company owned by the investor by the alleged actions of the Bulgarian government.\(^{40}\)

The claimant insisted that the arbitral tribunal had jurisdiction by invoking the MFN clause of the Cyprus–Bulgaria BIT of 1987 and Part V of the Energy Charter Treaty. The Cyprus–Bulgaria BIT was limited to ICSID arbitration of disputes concerning setting the amount of compensation after Bulgarian courts had ruled on the merits of the underlying dispute. By relying on the MFN clause in the Cyprus–Bulgaria BIT, which provided that ‘[e]ach Contracting Party shall apply to the investments in its territory by investors of the other Contracting Party a treatment which is not less favourable than that accorded to investments by investors of third state’, the claimant sought to overcome such limitations, by importing the dispute resolution provisions of the Bulgaria–Finland BIT, which provided for wider jurisdiction.\(^{41}\)

In *Plama*, the arbitral tribunal found that the ‘basket of treatment’ and ‘self-adaptation’ of the MFN treatment would lead to ‘the option to pick and choose provisions from the various BITs’\(^{42}\). The tribunal considered that, in principle:

> an MFN provision in a basic treaty does not incorporate by reference dispute settlement provisions in whole or in part set forth in another treaty, unless the MFN provision in the basic treaty leaves no doubt that the Contracting Parties intended to incorporate them.\(^{43}\)

The tribunal further explained that:

> dispute resolution provisions in a specific treaty have been negotiated with a view to resolving disputes under that treaty. Contracting states cannot be presumed to have agreed that those provisions can be enlarged by incorporating dispute resolution provisions from other treaties negotiated in an entirely different context.\(^{44}\)

However, the tribunal in *Plama* agreed with the decision of *Maffezini* to the extent that there is a need to make a distinction between ‘a legitimate extension of rights and benefits through the operation of MFN clause’ and ‘disruptive treaty-shopping that would be disastrous for policy objectives reflected in specific treaty provisions’.\(^{45}\)

Further, the *Plama* tribunal specifically distinguished its ruling from *Maffezini*, highlighting that *Maffezini* had unique and unprecedented circumstances as it ‘concerned a curious requirement that during the first 18 months the dispute be tried in the local courts’.

\(^{40}\) *Plama*, para. 21.

\(^{41}\) ‘Most Favoured Nation Treatment Application in International Investment Arbitration: A Study on Conflicting Precedence in International Dispute Settlement Procedure’, p. 43.

\(^{42}\) *Plama*, para. 219.

\(^{43}\) ibid., para. 223 (emphasis added).

\(^{44}\) ibid., para. 207.

\(^{45}\) ibid., paras. 222–223.
and the wording of its MFN clause was rather broad and vague. Therefore, the Plama tribunal stated that Maffezini should not be treated as a statement of general principle providing guidance to arbitral tribunals in which such special circumstances are not present.46

iii Analysis

Despite numerous criticisms of the Maffezini award and the fears that it raised, several tribunals have followed the same direction to import procedural provisions of more favourable BITs, including in Siemens v. Argentina,47 Gaz Natural v. Argentina,48 National Grid v. Argentina,49 AWG v. Argentina,50 Hochtieff AG v. Argentina,51 Suez v. Argentina52 and Impregilo v. Argentina.53 Notably, the cases in which the importation of dispute resolution provisions was upheld seem to primarily involve Argentina, whose BITs often require investors to bring disputes before national courts for 18 months before international arbitration, which has been considered (at least by the Plama tribunal) practically nonsensical.54

Other arbitral tribunals, such as in Salini v. Jordan,55 Vladimir Berschader v. Russian Federation,56 Wintershall v. Argentina,57 ICS Inspection v. Argentina,58 Daimler v. Argentina59 and Klick v. Turkmenistan,60 have rejected the course set out by Maffezini, and following Plama, decided that an MFN clause could not be used to import procedural rules, unless it is clearly and explicitly indicated in the agreement.

46 ibid., para. 224.
54 Plama, para. 224.
Most Favoured Nation Treatment

Given that arbitral tribunals seem to be split on this issue, it can be difficult to determine a current practice in international law. For example, *Siemens* and *Wintershall* share similar fact patterns and both were against the Argentine government, but the arbitral tribunals reached contradicting decisions. The *Wintershall* tribunal said that an MFN clause did not apply to dispute resolution provisions ‘unless of course the MFN clause in the basic treaty clearly and unambiguously indicates that it should be so interpreted’, 61 while the *Siemens* tribunal based its reasoning on the vagueness of the MFN clause in question to conclude that procedural rules can be included unless they are expressly excluded. 62

In the above cases, to argue in favour of importing other dispute resolution provisions, claimants have mostly focused on the relationship between the availability of arbitration and investor protections as a whole, the overall objectives of investment protection agreements, context of the treaty negotiations, and the language and interpretation of the MFN clause. On the other hand, state respondents have argued that there is a need for clear and unambiguous consent to import procedural elements and that there is no evidence of ‘less favourable’ treatment between the two treaties in question. Furthermore, states frequently highlight the need to limit the extent of MFN clauses in order to avoid the broader risk of treaty shopping. 63

Although no consensus has been reached on this issue, the tribunals in *Maffezini* and *Plama*, as well as other cases, seem to agree that the application of MFN clause must not lead to treaty shopping, which ‘undermine improved formulations of treaty provisions’. 64 While arbitral tribunals agree about the need to strike a balance between protecting foreign investors and the prevention of treaty shopping, there is still a significant amount of subjectivity on how to balance these contrasting points.

Another fundamental basis agreed upon by all tribunals is that investors will only be able to use MFN clauses as a means of incorporating more favourable dispute resolution provisions of other treaties where the circumstances indicate that the contracting states to the primary treaty clearly intended this to be possible. As pointed out in *Plama*, this will most often be the case where such an intention is clearly and unambiguously expressed by the wording of the MFN clause concerned. However, as most MFN clauses do not contain express language regarding the inclusion or exclusion of dispute resolution provisions, such an intention may also be established by interpretation with reference to those guidelines provided for interpretation of international treaties. 65

There is no universal tool for interpretation, but guidelines do exist. One of the basic principles of interpretation when interpreting an MFC clause is the *ejusdem generis* principle mentioned above. Articles 31 and 32 of the Vienna Convention on the Law of Treaties 1969 (VCLT) also provide for general rules of interpretation and other means that can be used for treaty clause interpretation. 66 The ultimate goal of utilising these basic principles of interpretation is to identify the intention of the contracting parties. 67

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61 *Wintershall*, para. 167.
62 *Siemens*, para. 106.
65 Fietta, p. 138.
67 Fietta, p. 132.
IV THE FUTURE OF MFN CLAUSES

As shown above, many MFN clauses are drafted broadly, without a clear indication of their intended scopes, which can lead to conflicting decisions from courts and arbitral tribunals on similar issues. Therefore, recently there has been more significant focus on expressing the parties’ intention more clearly in the MFN clause, with states needing to be ‘careful that the desired effects of newly crafted treaty provisions are not obviated by the application of a broadly worded MFN clause’.  

Further, given the inconclusive decisions of the tribunals in the past two decades, UNCTAD has recently recommended some options for future treaty drafting in order to address these challenges:

a) to specify in the treaty that the MFN clause does not allow for the importation of substantive or investor–state dispute settlement (ISDS) elements contained in older treaties;

b) to specify in the treaty that MFN treatment does not apply to ISDS provisions found in other existing or future third-party treaties;

c) to specify in the treaty that the MFN clause does not apply to substantive obligations undertaken in other existing or future third-party treaties;

d) to specify in the treaty that certain sectors or industries or certain policy measures are excluded from the MFN obligation through a general exclusion (applicable to both parties) or through country-specific reservations;

e) to specify in the treaty that the MFN obligation requires comparison of investors or investments that are ‘in like circumstances’, while preferably setting out criteria for determining whether investors or investments are in ‘like circumstances’;

f) not to include an MFN clause in the treaty; such approach preserves a maximum degree of flexibility.

It is important for those wishing to apply MFN clauses in international arbitration cases to monitor how newly worded clauses may limit their applicability.

V CONCLUSION

MFN treatment has been a basic standard of international economic relations for a long time, providing equal opportunities between nations. Although the application of MFN treatment to international investment is more recent than to international trade, it is broadly recognised as one of the most important provisions of substantive protection in investment treaties.

68 Siemens, para. 136.
69 For example, Azerbaijan–Croatia BIT (2007).
70 For example, the Free Trade Agreement (FTA) between the EU and Singapore (2014), the FTA between India and Malaysia (2011), the ASEAN–Australia–New Zealand FTA (2009), the Japan–Singapore FTA (2002) and the SADC Model BIT (2012).
72 Marie-France House & Fabrizio Pagani, p. 16.
The large number of treaties with varying substantive and procedural standards has created a particular challenge to the question of the scope of MFN clauses.\textsuperscript{73} Since Maffezini in 2000, even procedural provisions of third-party BITs can be invoked to settle disputes arising out of a treaty, causing uncertainty and instability for investors and states.\textsuperscript{74}

The application of broadly worded MFN clauses to dispute settlement mechanisms has given rise to various problems as arbitral tribunals attempt to ascertain the contracting parties’ intention while simultaneously striking a balance between the protection of investors and potential treaty shopping.

There seems to be some concern in the international community that the further extension of the scope of MFN clauses could be endless if states and tribunals do not set limits in a uniform and definitive manner.\textsuperscript{75} While UNCTAD has set out some recommendations that seek to advise states how to limit overly extensive MFN clauses,\textsuperscript{76} it remains to be seen how these may affect future treaties and arbitral decisions.

\begin{footnotesize}
\begin{enumerate}
\item [73] ‘Most Favoured Nation Treatment Application in International Investment Arbitration: A Study on Conflicting Precedence in International Dispute Settlement Procedure’, p. 73.
\item [74] Thulasidhass, p. 24.
\item [75] Nikiema, p. 25.
\item [76] UNCTAD, ‘Most-favoured nation treatment’, p. 84.
\end{enumerate}
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Chapter 17

FULL PROTECTION AND SECURITY

Ulyana Bardyn and Levon Golendukhin

I  INTRODUCTION

The guarantee of full protection and security (FP&S) appears in the vast majority of investment protection treaties. Although its formulation varies (some treaties refer to ‘full protection’ or ‘constant protection,’ and yet others provide for ‘continuous protection’), the key purpose of this guarantee is to protect the security and integrity of an investment.2

The FP&S standard requires states to refrain from actively interfering with foreign investments, and imposes on the state an obligation of due diligence and vigilance in protecting investments from actions of third parties. These two components are sometimes referred to as the duty to abstain and the duty to protect.3 The former is a negative obligation (i.e., the host state must not engage in actions that may jeopardise the security of aliens). The latter is a positive obligation (i.e., the state’s obligation to protect foreign investments from unlawful activities carried out by third parties on its territory and to punish the wrongdoers).4

II  OBLIGATION NOT TO INJURE

i  Duty to abstain from interference

It is widely accepted that the FP&S standard imposes on a state hosting a foreign investment the duty to refrain from undue interference with the investment. ‘The Arbitral Tribunal also does not consider that the “full security” standard is limited to a State’s failure to prevent actions by third parties, but also extends to actions by organs and representatives of the State itself.’5 This duty can be breached when a state takes specific actions that harm the integrity

1 Ulyana Bardyn is a senior managing associate and Levon Golendukhin is a managing associate at Dentons US LLP.
4 id.
5 Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania, ICSID Case No. ARB/05/22, Award, (22 July 2008), paragraph 730.
of the investment, or fails to prevent another state organ from taking such action.\textsuperscript{6} One example of interference by the state is undue harm to an investment sustained as a result of raids undertaken by the state’s military or police force.

However, not every claimed harassment purportedly at the hands of state officials immediately constitutes a breach of the FP&S clause. In \textit{Eureko v. Poland},\textsuperscript{7} the tribunal did not see sufficient evidence that the state was orchestrating the harassment\textsuperscript{8} and was not convinced that the ‘disturbing’ acts of harassment (which the award does not describe) ‘breached the standard of the full security and protection of the Treaty’.\textsuperscript{9}

\textbf{ii  Whose actions can lead to a breach of the host state’s duty?}

A necessary element of any claim for breach of the FP&S standard for affirmative actions taken by state parties (as distinct from omissions by the state from its duty to protect discussed below) is the determination that the action in question is legally attributable to the respondent state. Only conduct attributable to the state can form the basis of state responsibility and liability. Determinations of state attribution are made with reference to the rules of customary international law of state responsibility. These customary law rules have been codified in the International Law Commission’s (ILC) Draft Articles on Responsibility of States for Internationally Wrongful Acts (the ILC Articles).\textsuperscript{10} Under the ILC Articles, there are a handful of principal types of actors from whose conduct state responsibility arises.

First, under Article 4, state responsibility extends to all organs of the state, as well as any person or entity holding the status of state organ under domestic law.\textsuperscript{11} State organs are defined in the commentary as ‘all the individual or collective entities which make up the organization of the State and act on its behalf’, and includes organs of its central government and territorial units.\textsuperscript{12} Included within the scope of state organs are all branches of all levels of government. Notably, some tribunals have suggested that the involvement of acts by the judiciary engages a new dimension of the duty of non-interference. As the \textit{Frontier Petroleum v. Czech Republic} tribunal elaborated:

\textit{In this Tribunal’s view, where the acts of the host state’s judiciary are at stake, “full protection and security” means that the state is under an obligation to make a functioning system of courts and legal remedies available to the investor. On the other hand, not every failure to obtain redress is a violation of the principle of full protection and security. Even a decision that in the eyes of an outside observer, such as an international tribunal, is “wrong” would not automatically lead to state responsibility so}

\begin{flushright}
\begin{footnotesize}
\textsuperscript{6} \textit{Frontier Petroleum Services Ltd. v. Czech Republic}, UNCITRAL, Final Award (12 November 2010), paragraph 261 ("[T]he host state is under an obligation to take active measures to protect the investment from adverse effects that stem from private parties or from the host state and its organs.").

\textsuperscript{7} \textit{Eureko B.V. v. Republic of Poland}, Partial Award (19 August 2005).

\textsuperscript{8} id., paragraph 237. See also below for a discussion of attribution of conduct of state officials and other individuals and entities.

\textsuperscript{9} id., paragraph 236. The \textit{Eureko} tribunal, however, noted that a repetition of such harassment at the hands of state officials could establish a failure on the part of the state to prevent undue interference with the investment by state representatives. id., paragraph 237.


\textsuperscript{11} id.

\textsuperscript{12} id., art. 4(1) & comment (1).
\end{footnotesize}
\end{flushright}
long as the courts have acted in good faith and have reached decisions that are reasonably tenable. In particular, the fact that protection could have been more effective, procedurally or substantively, does not automatically mean that the full protection and security standard has been violated.\footnote{\textit{Frontier Petroleum Services Ltd. v. Czech Republic}, UNCITRAL, Final Award (12 November 2010), paragraph 273. See also \textit{Parkerings-Compagniet AS v. Republic of Lithuania}, ICSID Case No. ARB/05/8, Award (11 September 2007), paragraphs 360–361.}

Second, Article 5 of the ILC Articles holds conduct of persons and entities empowered with and exercising elements of governmental authority to be attributable to the state. This includes state agencies, as well as certain state-owned enterprises exercising public, regulatory or other non-commercial governmental authority. Thus, in addition to the decisions and orders made by the military or police – which are state organs – the conduct of individual soldiers and officers is too attributable to the state.

Further, under Article 8 of the ILC Articles, state attribution applies to conduct by persons or groups of persons under the direction and control of the state.\footnote{ILC Articles, art. 8.} For example, paramilitary groups not officially affiliated with a state but acting under its specific direction or control are deemed to act on behalf of the state. The key determinant of attribution under Article 8 is the degree of control exercised by the respondent state.\footnote{id., art. 8 comments (2), (4), (5).} A paramilitary group’s activities may still be attributable to a state even if it was not acting under the state's control. This may be the case if the state subsequently adopts the acts as its own,\footnote{id., art. 11.} or if the acts took place in the context of a civil uprising and regime change.\footnote{For a more detailed discussion of questions of attribution in the civil unrest context, see Meriam Al-Rashid et al., ‘Investment Claims Amid Civil Unrest: Questions of Attribution and Responsibility’, \textit{3 B.C.D.R. Int'l Arb. Rev.} 181, 183–197 (2016).}

\section*{iii \ What is the relationship to other international standards of protection?}

Much debate has arisen about the exact contours of the FP&S standard, especially in comparison with other international standards of protection. First, the FP&S standard’s roots in the customary law of diplomatic protection and the state’s obligation to protect foreign-owned property in its territory raise questions about whether the standard is equivalent to or greater than the international minimum standard of treatment. Second, the FP&S standard’s at-times flexible interpretation and application by prior investment arbitration tribunals has raised questions about the distinctions between FP&S and other investment protection standards dealing with state actions interfering with foreign investments, such as, for example, the fair and equitable treatment (FET) standard.

\section*{iv \ Distinction from the international minimum standard}

The distinction between the treaty-based FP&S standard from the customary law minimum standard of treatment has not always been viewed consistently. Given that the international minimum standard itself encompasses a duty to provide full protection and security, there has been a split of opinion as to whether the treaty-based standard reiterates the protection available in customary international law, or whether it promises an additional level of protection.
One reasoned approach advanced by commentators has been to distinguish standalone FP&S clauses in bilateral investment treaties (BITs) from those where the FP&S clause is subservient to an international minimum standard of treatment clause, as for example in the case of Article 1105(1) of NAFTA. Conversely, a standalone FP&S clause not stated in the context of the international minimum standard of treatment would carry with it a heightened ‘BIT standard’ that exceeded the customary international law standard.

Ultimately, the more material inquiry in most cases is not whether the FP&S clause provides protection beyond the international minimum standard, but what the international minimum standard itself provides. Whatever the gap between the BIT FP&S standard and the customary FP&S standard may have been before, it may now be more of an academic question than one with significant practical consequences. This is because tribunals have increasingly been finding that the traditional conception of the customary minimum standard of treatment has evolved substantially and moved towards the BIT standard.

v Distinction from FET

The flexible interpretations of FET and FP&S clauses adopted by prior tribunals have in some ways blurred the distinction between FET and FP&S with regard to claims for interference or harm to an investment caused by the state’s exercise of regulatory or other policing powers with the investment. For example, in *Rusoro v. Venezuela*, the tribunal suggested that the lack of any breach of the FET standard meant that ‘such measures can never imply a breach of the FP&S standard, however widely interpreted’.

The authors would posit that the FP&S protection is not necessarily subsumed within the broader FET protection, but rather that each of the two standards has its own sphere of operation, even though there is a high degree of overlap between them.

Moreover, the principle of effectiveness counsels in favour of a meaning for FP&S distinct from FET. The principle of effectiveness is a principle of treaty interpretation according to which all provisions of a treaty shall be given effective meaning. However, if FP&S was indeed subsumed within FET, that would render the FP&S clause meaningless in the large majority of BITs in which it appears alongside the FET clause. If the state parties to the BIT believed that the FP&S standard was subsumed with the FET standard, there would have been no need to expressly include the FP&S clause in such a treaty.

19 North American Free Trade Agreement, 32 I.L.M. 289, 605 (1993), art. 1105(1) (‘Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security’).
20 See, e.g., *Gold Reserve Inc. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)/09/1, Award (22 September 2014), paragraph 567.
21 *Rusoro Mining Ltd. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)/12/5, Award (22 August 2016), paragraph 548.
III OBLIGATION TO PROTECT

i What does the obligation to protect comprise?

The unique feature of the FP&S standard is that it requires the host state to not only abstain from conduct that may interfere with the operation of foreign investment but also to affirmatively protect and secure such foreign investment from injurious acts by third parties. As noted above, the latter obligation is sometimes referred to as the duty to protect.

Under the umbrella of that duty, host states have an obligation to prevent injury to investment by third parties. Where the circumstances causing injury nevertheless occur, they have an obligation to take steps repressing the harmful conduct and punishing the perpetrators. These two obligations are sometimes referred to as the ‘duty of prevention’ and the ‘duty of repression’.24 A failure to take appropriate steps in either regard may result in the host state’s violation of its FP&S obligation.

ii Whose actions may give rise to international responsibility of the host state?

Significantly, the host state’s responsibility may be implicated under this rubric even without attribution of the injurious conduct to the state. That is because the internationally unlawful conduct that the state is responsible for in such circumstances is its own inaction that allowed third parties to loot or otherwise injure the investment.25

iii What level of protection is required from the host state?

The level of protection required from the host state is not absolute. Absent a specific treaty provision obligating the host state to protect foreign investment against ‘any possible loss of value’ caused by persons whose acts could not be attributed to such state, the host state is not responsible for preventing ‘each and every injury’ to foreign investment. Rather, it is required to exercise due diligence in its efforts to protect and secure the investment.

23 *AES Summit Generation Limited v. Republic of Hungary*, ICSID Case No. ARB/07/22, Award (September 23, 2010), paragraph 13.3.2; *Oxus Gold v. Republic of Uzbekistan*, UNCITRAL, Final Award (December 17, 2015), paragraph 353.


25 *Ampal-American Israel Corp. and others v. Arab Republic of Egypt*, ICSID Case No. ARB/12/11, Decision on Liability and Heads of Loss (February 21, 2017), paragraph 245.

The concept of due diligence has a long pedigree in international law. Coined by jurist Hugo Grotius in the seventeenth century, it has received wider recognition due to its frequent use in the mixed claims commissions jurisprudence in the nineteenth century.  

In the Cutler case (US v. Italy), an American citizen complained about the destruction of his property that resulted from a mob attack in Florence. Italy accepted that it had an obligation of vigilance but not an obligation from preventing any harm. The United States conceded that, to state a claim, it would have to argue that the Italian authorities 'had knowledge, or should have had knowledge, of the impending attack, or failed to take precautions to thwart it'. The arbitrator agreed with the United States's position, noting:

'It cannot be said with absolute confidence that the State is responsible merely because the event could have been averted if sufficient police had been present. It must be established that the situation caused for more police which could have been provided in time and were not. Obviously there will be disagreement about the judgment that was made, and that might have been made, and the most that can be said is that a prima facie case exists when it is established that the facts were known to the authorities and that the action which they took, if any, proved inadequate.'

In Sambiaggio (Italy v. Venezuela), the case's umpire held that Venezuela could not be found responsible for acts of uncontrolled revolutionists in the absence of any evidence that the state had 'failed to exercise due diligence to prevent damages'. In Youmans (US v. Mexico), the US–Mexican mixed claims commission held that a state may be responsible for damage caused by mob violence where the state failed to punish the persons implicated in the crime.

Although the early decisions have not defined all the contours of this due diligence obligation, they have identified a series of factors to be considered by tribunals, including the degree of effectiveness of the state’s control over parts of its territory, the degree of predictability of harm and the significance of the interest to be protected.

This obligation of due diligence was subsequently developed further in modern investment treaty jurisprudence. Investment arbitration tribunals have sometimes characterised this obligation as one calling for 'vigilance', 'prudence', ‘reasonable care',

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29 id.
30 Sambiaggio (Italy v. Venezuela), 10 R.I.A.A. 499 (1903), page 524.
31 Youmans (US v. Mexico), 6 R.I.A.A. 100 (1926), page 115.
‘best efforts’\textsuperscript{36} or responsiveness.\textsuperscript{37} But, tribunals have generally agreed that the host state is to exercise reasonable care to protect and secure foreign investment. Some tribunals held that the host states are required to use ‘all possible measures that could be reasonably expected’ for purposes of protection and security of investment.\textsuperscript{38} Others noted that the obligation of due diligence is ‘nothing more nor less than the reasonable measures of prevention which [a] well administered government could be expected to exercise under similar circumstances’.\textsuperscript{39} In determining the parameters of such ‘reasonable measures,’ some tribunals considered it appropriate to take into account the state’s particular circumstances, including factors such as its level of development and stability, and availability of resources and capacity to deal with the circumstances that give rise to the injury.

For example, in \textit{Pantechniki v. Albania}, the claimant, a contractor selected for infrastructure works in Albania, complained that violent riots taking place over several days had damaged its investment, and that Albania had breached its FP&S obligation by failing to prevent the damage.\textsuperscript{40} The sole arbitrator held that the state’s FP&S obligations depend on the state’s ability to accord protection. The arbitrator compared the standard for denial of justice (which traditionally is not calibrated to the host state’s particular circumstances) with that for FP&S, concluding that the two standards are substantially different. The proportionality factor has not been accepted in the context of denial of justice claims because the state’s compliance with those obligations does not depend on physical infrastructure – ‘states are not liable for denial of justice because they cannot afford to put at the public’s disposal spacious buildings or computerized information banks’, instead what matters is ‘the human factor of obedience to the rule of law’.\textsuperscript{41} To apply the same reasoning to the FP&S protection would be ‘parlous’.

In the context of a denial of justice claim, the two standards are fundamentally different in that:

\textsuperscript{36} \textit{Deutsche Bank AG v. Democratic Socialist Republic of Sri Lanka}, ICSID Case No. ARB/09/2, Award (October 31, 2012), paragraph 537.

\textsuperscript{37} \textit{Wena Hotels Limited v. Arab Republic of Egypt}, ICSID Case No. ARB/98/4, Award (December 8, 2000), 41 ILM 896 (2002), paragraph 84.

\textsuperscript{38} See \textit{Asian Agricultural Products Ltd. v. Republic of Sri Lanka}, ICSID Case No. ARB/87/3, Final Award (June 27, 1990), paragraph 85(b); \textit{Saluka Investments B.V. (the Netherlands) v. The Czech Republic}, UNCITRAL, Partial Award (March 17, 2006), paragraph 484 (holding that the host state was under an obligation to ‘adopt all reasonable measures to protect assets and property from threats or attacks’); \textit{Al Tamimi v. Sultanate of Oman}, ICSID Case No. ARB/11/33, Award (November 3, 2015), paragraphs 449, 451; \textit{Técnicas Medioambientales Tecmed, S.A. v. United Mexican States}, ICSID Case No. ARB (AF)/00/2, Award (May 29, 2003), 19 ICSID Rev.-FILJ 158 (2004), paragraph 177; \textit{AES Summit Generation Limited v. Republic of Hungary}, ICSID Case No. ARB/07/22, Award (September 23, 2010), paragraph 13.3.2.

\textsuperscript{39} \textit{Asian Agricultural Products Ltd. v. Republic of Sri Lanka}, ICSID Case No. ARB/87/3, Final Award (June 27, 1990), paragraph 77; \textit{Al-Warraq v. Republic of Indonesia}, UNCITRAL, Final Award (December 15, 2014), paragraph 625; \textit{AES Summit Generation Limited v. Republic of Hungary}, ICSID Case No. ARB/07/22, Award (September 23, 2010), paragraph 13.3.3.

\textsuperscript{40} \textit{Pantechniki S.A. Contractors & Engineers (Greece) v. The Republic of Albania}, ICSID Case No. ARB/07/21, Award (July 30, 2009), paragraphs 12–13.

\textsuperscript{41} id., paragraph 76.

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The minimum requirement is not high in light of the great value placed on the rule of law. There is warrant for its consistent application. A failure of protection and security is to the contrary likely to arise in an unpredictable instance of civic disorder which could have been readily controlled by a powerful state but which overwhelms the limited capacities of one which is poor and fragile.\textsuperscript{42}

In a similar vein, the \textit{Tulip v. Turkey} tribunal noted similarly that '[t]he question of whether the State has failed to ensure FP&S is one of fact and degree, responsive to the circumstances of the particular case.'\textsuperscript{45}

\textit{In sum, when considering the host state’s obligation, ‘tribunals will likely consider the state’s level of development and stability as relevant circumstances in determining whether there has been due diligence.’}\textsuperscript{46} An investor investing in an area with endemic civil strife and poor governance cannot have the same expectation of physical security as one investing in London, New York or Tokyo.\textsuperscript{47}

\textbf{iv \hspace{1em} What types of measures are required from the host state?}

The nature of measures required of the host state will vary depending on the circumstances giving rise (or threatening to give rise) to the injury. Because this standard requires host states to act with vigilance and due diligence, it also provides these states with a substantial latitude in deciding what actions to take to prevent or repress unlawful and injurious actions. A wide spectrum of measures is available to host states, from ‘preventive’\textsuperscript{48} to ‘coercive’\textsuperscript{49} or ‘restorative’ measures,\textsuperscript{50} among others.

\begin{itemize}
\item \textsuperscript{42} id., at 77.
\item \textsuperscript{43} id.
\item \textsuperscript{44} id., at 82.
\item \textsuperscript{45} Tulip Real Estate Investment and Development Netherlands B.V. \textit{v. Republic of Turkey}, ICSID Case No. ARB/11/28, Award (March 10, 2014), paragraph 430.
\item \textsuperscript{46} Andrew Newcombe and Luis Paradell, \textit{Law and Practice of Investment Treaties: Standards of Treatment} (Kluwer Law International 2009), page 310.
\item \textsuperscript{47} id.
\item \textsuperscript{49} OI European Group B.V. \textit{v. Bolivarian Republic of Venezuela}, ICSID Case No. ARB/11/25, Award (March 10, 2015), paragraph 580; Pantechniki S.A. Contractors & Engineers (Greece) \textit{v. The Republic of Albania}, ICSID Case No. ARB/07/21, Award (July 30, 2009), paragraph 82.
\item \textsuperscript{50} WENA Hotels Limited \textit{v. Arab Republic of Egypt}, ICSID Case No. ARB/98/4, Award (December 8, 2000), 41 ILM 896 (2002), paragraph 84; Parkerings-Compagniet AS \textit{v. Republic of Lithuania}, ICSID Case No. ARB/05/8, Award (September 11, 2007), paragraph 355.
\end{itemize}
IV SCOPE OF SUBSTANTIVE PROTECTIONS

The scope of FP&S protection remains an open question even today. Specifically, there is a split of opinion as to whether the FP&S standard accords protection to physical security alone, or whether legal security is covered as well. Though some tribunals – for example, those in Siemens v. Argentina, Azurix Corp. v. Argentine Republic, Biwater Gauff (Tanzania) Ltd v. Tanzania and CME v. Czech Republic – have been willing to extend the FP&S standard to legal protection, others – for example, those in Gold Reserve v. Venezuela, Saluka v. Czech Republic and AWG v. Argentina – have been reluctant to do so. Political and economic volatility frequently impacts a state’s legal framework as much as its physical infrastructure, and therefore it is expected that more arbitral decisions addressing this issue will become available in the near future.

V CONCLUSION

Once one of the lesser-developed standards of international investment law, FP&S has now become a hallmark of that law. As this investment protection gains greater recognition, it also opens new horizons. For example, historically, FP&S has been viewed as a standard providing for exclusively physical protection to foreign investment, but nowadays many tribunals hold that it also promises legal protection. Though it remains to be seen whether, going forward, the already-broad purview of the FP&S protection will be expanded even further, the authors posit that the standard has the potential to assume an even more prominent role in investment law. Cyberattacks, environmental pollution and health crises threaten modern life and investments. The FP&S standard has the capacity to address many of these threats.

51 Siemens A.G. v. Argentine Republic, ICSID Case No. ARB02/8, Award (February 6, 2007), paragraph 303; Azurix Corp. v. Argentine Republic, ICSID Case No. ARB/01/12, Award (June 23, 2006), paragraphs 406–408; Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania, ICSID Case No. ARB/05/22, Award (July 24, 2008), paragraph 729; CME Czech Republic B.V. v. Czech Republic, UNCITRAL Arbitration Rules, Partial Award (September 13, 2001), paragraph 613.

52 Gold Reserve Inc. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/09/1, Award (September 22, 2014), paragraphs 622–23; Saluka Investments B.V. (the Netherlands) v. The Czech Republic, UNCITRAL, Partial Award (March 17, 2006), paragraphs 483–484; AWG Group v. The Argentine Republic, UNCITRAL Arbitration Rules, Decision on Liability (July 30, 2010), paragraph 179.
The debate about the seemingly innocuous ‘observance of obligations’ or ‘umbrella’ clause is ongoing, despite those who would believe that there is nothing left to be said on the matter. On key questions of scope and effect, the investment arbitration community remains divided. This chapter provides a brief review of the existing authorities and highlights the more recent cases to illustrate the main current open questions.

I INTRODUCTION

The framework for large-scale foreign investment is often set out in a contract with the state or a state-owned entity. These contracts may provide for international arbitration of disputes before a delocalised tribunal. In many cases, however, they do not, and the investor’s recourse is to the local courts or domestic arbitration. If the state of the investor’s nationality has concluded a bilateral investment treaty (BIT), multilateral treaty or free trade agreement with an investment chapter with the state in which the investment has been made, the investor might seek to bring its contract dispute before an international arbitral tribunal, rather than the local courts, and under the treaty rather than its contract. But how to get there when, generally, the violation of a contract governed by internal laws does not alone constitute a violation of international law in the absence of any exercise of puissance publique? Enter the umbrella clause, found in a number of BITs that, on the face of it, requires states to observe obligations that they have entered into with respect to investments.

One of the first investors to seek to enforce an umbrella clause was SGS Société Générale de Surveillance SA (SGS), a Swiss company that provides among other things certifications based on pre-shipment inspections of goods. In recent years, SGS was involved in three separate arbitrations, under three separate treaties, each invoking a form of umbrella
Observance of Obligations

clause and giving rise to diverging findings. In each case, SGS’s claims involved breaches of an underlying pre-shipment inspection contract, although the nature of the disputes differed slightly.

II JURISDICTIONAL DECISIONS

i SGS v. Pakistan

The first of those decisions, SGS v. Pakistan, is widely considered to be the first decision discussing the scope and effect of an umbrella clause in any detail. The dispute concerned, among other things, a claim that Pakistan had wrongfully terminated a pre-shipment inspection contract, which itself contained a domestic arbitration clause. The tribunal considered whether it had jurisdiction to hear SGS’s claims under Article 11 of the Switzerland–Pakistan BIT, which required Pakistan to ‘constantly guarantee the observance’ of commitments entered into with respect to investments. The question for the tribunal, as it put it, was whether Article 11 of the BIT transformed ‘purely contractual claims into BIT claims’.

Citing to customary canons of interpretation, the tribunal said that the wording of the clause did not signal the creation and acceptance of a new international law obligation where there was none before. Moreover, Article 11 of the BIT was not placed in the treaty ‘together with the substantive obligations undertaken by the Contracting Parties’ (Articles 3 to 7), but rather was towards the end. Given that the consequences of the claimant’s interpretation were, in the tribunal’s view, so ‘far reaching in scope, and so automatic and unqualified and sweeping in their operation, so burdensome in their potential impact’, the claimant was required, and had failed, to show ‘clear and persuasive evidence’ that the interpretation it sought had been the BIT contracting parties’ intent.

The ‘indefinite expansion’ concerning the tribunal was explained as the ‘incorporation by reference [of] an unlimited number of State contracts, as well as other municipal law instruments setting out State commitments including unilateral commitments’. That concern presumed a certain interpretation of the scope of the obligations to which the umbrella clause applies, which remains in contention. In reaching its conclusions, the tribunal also expressed concern that a broad interpretation of the umbrella clause would ‘nullify any freely negotiated dispute settlement clause in a State contract’, and render the substantive provisions of the BIT ‘superfluous’ as, it contended, there would be no need to demonstrate a violation of treaty standards if a simple breach of contract or municipal regulation would suffice to engage international responsibility. The tribunal concluded that it did not have jurisdiction under the treaty to hear SGS’s claims that Pakistan breached the contract.

5 SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan (SGS v. Pakistan), ICSID Case No. ARB/01/13, Award on Jurisdiction, 6 August 2003.
6 ibid., para. 164.
7 ibid.
8 ibid., paras. 165–166.
9 ibid., para. 169.
10 ibid., para. 167.
11 ibid., para. 173.
12 ibid., para. 166.
13 ibid., para. 168.
14 ibid.
Although the tribunal’s ruling left considerably in doubt what would be covered by the clause at issue, the tribunal indicated that the clause may be violated in ‘exceptional circumstances’ such as where a state ‘materially impedes’ an investor from going to international arbitration, having previously agreed to such arbitration in a contract.\textsuperscript{15}

\textbf{ii} SGS v. Philippines

The \textit{SGS v. Philippines}\textsuperscript{16} jurisdictional decision, rendered a little over half a year later, concerned a dispute about the amount of money owed under a similar contract, which itself provided for resolution of disputes before local courts. The tribunal considered Article X(2) of the Switzerland–Philippines BIT, which required the Philippines to ‘observe any obligation it has assumed’ with regard to investments.

The tribunal said that Article X(2) ‘means what is [sic] says’,\textsuperscript{17} namely that breaches of legally binding commitments made by states towards specific investments may be brought within the framework of the BIT,\textsuperscript{18} on the basis that the object and purpose of the BIT (to promote and protect investments) supported an effective interpretation of the relevant clause.\textsuperscript{19} After reaching this ‘provisional conclusion’,\textsuperscript{20} the tribunal went on to consider the \textit{SGS v. Pakistan} tribunal’s findings, noting the distinction between the wording of the two treaties but stating that the \textit{SGS v. Pakistan} findings were nevertheless still relevant to consider.\textsuperscript{21} The tribunal criticised the \textit{Pakistan} tribunal’s reasoning as ‘unconvincing’, and stated that it had failed to give any clear meaning to the clause.\textsuperscript{22} In particular, the tribunal cautioned that the clause did not transform a domestic obligation into an international obligation.\textsuperscript{23} It said that the ‘extent or content’ of the obligations to which the umbrella clause might apply were still matters of contract, ascertained and governed by the contractual proper law, which was Philippine law. It was only the performance of the obligation, once ascertained, that was an international law matter.\textsuperscript{24}

Although the tribunal disagreed with the \textit{SGS v. Pakistan} tribunal’s conclusion that there was no jurisdiction to hear pure contract claims, it had sympathy with the concern that the general provisions of the BIT should not override the specific exclusive dispute settlement arrangements in the contract.\textsuperscript{25} The tribunal concluded that the claim was for the time being inadmissible, given that the parties had agreed to an exclusive jurisdiction clause in the contract,\textsuperscript{26} and stayed the proceedings on the basis that the Philippine courts were to decide the scope or extent of the respondent’s obligation to pay before it could make a ruling on the umbrella clause.\textsuperscript{27}

\begin{itemize}
  \item \textsuperscript{15} ibid., para. 172.
  \item \textsuperscript{16} \textit{SGS Société Générale de Surveillance S.A. v. Republic of the Philippines (SGS v. Philippines)}, ICSID Case No. ARB/02/6, Decision on Jurisdiction, 29 January 2004.
  \item \textsuperscript{17} ibid., para. 119.
  \item \textsuperscript{18} ibid., para. 117.
  \item \textsuperscript{19} ibid., para. 116.
  \item \textsuperscript{20} ibid., para. 119.
  \item \textsuperscript{21} ibid.
  \item \textsuperscript{22} ibid., para. 125.
  \item \textsuperscript{23} ibid., para. 126.
  \item \textsuperscript{24} ibid.
  \item \textsuperscript{25} ibid., para. 134.
  \item \textsuperscript{26} \textit{SGS v. Philippines}, n.15, paras. 153–154.
  \item \textsuperscript{27} ibid., para. 155.
\end{itemize}
How did two tribunals, coincidentally seized with claims from the same claimant, come to such starkly opposite conclusions? Or, in the words of one tribunal, how can we ‘defend the coherence of the arbitration system in the face of apparently contradictory awards involving the same claimant’? Some tribunals and commentators have sought to explain the differences by distinguishing the wording of the treaty clauses, but others – including the tribunal in the final SGS case described next – have found that clauses with the wording that a state shall ‘constantly guarantee the observance of commitments’ can operate as umbrella clauses.

iii  SGS v. Paraguay

In the *SGS v. Paraguay* case, which like the Philippines case concerned a dispute about the payment of outstanding invoices, the tribunal considered Article 11 of the Swiss–Paraguay BIT, which contained the same language as the Swiss–Pakistan BIT: ‘constantly guarantee the observance of commitments’. The tribunal stated that it had little difficulty in establishing jurisdiction over the umbrella clause claims based on a reading of the ‘plain language’ of the clause and its ‘ordinary meaning’. The tribunal refused to read into the text any requirement that a breach could only be established through an abuse of state power: Article 11 had ‘no limitations on its face’ and was ‘unqualified’. The tribunal acknowledged that its findings directly contradicted those of the *SGS v. Pakistan* tribunal, but insisted upon its right to disagree.

The underlying contract in the *SGS v. Paraguay* case had an exclusive jurisdiction clause in favour of the Paraguayan courts. Unlike the tribunal in the *SGS v. Philippines* case, the tribunal in *SGS v. Paraguay* found that the claims were admissible. The tribunal stated that it would be ‘incongruous’ to find jurisdiction but then dismiss the claims on admissibility grounds because ‘the effect would be, once again, to divest the provision of its core purpose and effect, to the same extent as if we had denied jurisdiction outright’.

iv  Conclusions

Since the initial SGS decisions, opinion on the proper scope and effect of the umbrella clause has been divided among tribunals and commentators alike. Three often-cited cases decided in the early years following the *Pakistan* and *Philippines* decisions espoused the view that an umbrella clause does not confer jurisdiction on a tribunal to hear claims for ‘pure’ breaches...
of contract: Joy Mining v. Egypt, Pan American v. Argentina and El Paso v. Argentina. Two of these cases – Pan American and El Paso – shared the same presiding arbitrator and respondent-nominated arbitrator. These tribunals reasoned, among other things, that commercial transactions should be distinguished from state interference with the operation of a contract, and that the broad interpretation of the umbrella clause should not be upheld, as it would allow investors to invoke an umbrella clause for trivial disputes. Instead, the tribunals suggested that the umbrella clause was intended to safeguard ‘additional investment protections contractually agreed by the State as a sovereign – such as a stabilization clause – inserted in an investment agreement’; however, the umbrella clause would operate only where an independent violation of the substantive treaty standards was also established. The tribunals concluded that they had no jurisdiction over pure contract claims.

The Pan American and El Paso decisions, published in 2006, caused waves in the international arbitration community, as they appeared amid several awards that had without manifest difficulty found umbrella clauses effective to protect contractual rights. The nature of the debate continues to evolve. Although it might be said that the majority of published awards since the El Paso and Pan American decisions have sought to give an umbrella clause substantive meaning over and above the other substantive provisions of the BIT, there are still a number of issues that remain. The remainder of this chapter briefly highlights the direction of the debate on these issues.


38 Pan American v. Argentina and El Paso v. Argentina were both presided over by Lucius Caflisch, and Brigitte Stern was the respondent’s appointed arbitrator.


40 Pan American v. Argentina, paras. 106 and 110; El Paso v. Argentina, paras. 76, 82.


42 Pan American v. Argentina, para. 112; El Paso v. Argentina, para. 84.

43 Pan American v. Argentina, paras. 84–87; El Paso v. Argentina, paras. 112–116. Joy Mining v. Egypt also came to the same conclusion: para. 82.

44 CMS v. Argentina, n.3, cf. para. 299, cf. CMS v. Argentina, Decision on Annulment, 25 September 2007 (the CMS Annulment Decision), para. 97; Eureko B.V. v. Poland, ad hoc, Partial Award, 19 August 2005, para. 250; Noble Ventures v. Romania, n.28, para. 61, although the tribunal did not find that the parties had in fact concluded a contract in respect of which any violation could be established.

OBSERVANCE OF OBLIGATIONS

III FORUM SELECTION CLAUSES

In *BIVAC v. Paraguay*, the tribunal followed the approach of the *SGS v. Philippines* tribunal, and declined to hear the claim on the grounds of non-admissibility. The dispute concerned Paraguay’s failure to pay invoices under a pre-shipment inspection contract. The tribunal concluded that although the umbrella clause in the Netherlands–Paraguay BIT ‘has to be interpreted in such a way as to give it some meaning and practical effect’ and thus it ‘establishes an international obligation for the parties to the BIT to observe contractual obligation with respect to investors’, the claim was inadmissible because of the forum selection clause in the contract. The tribunal characterised the dispute as a purely contractual claim and concluded that the parties were not ‘free to pick and choose’ only parts of a contract to incorporate into an umbrella clause and to ignore others, especially their contractually negotiated dispute settlement arrangements. In *Bosh v. Ukraine*, the tribunal stated obiter that it would follow the *BIVAC v. Paraguay* tribunal’s ruling and decline to hear the claim.

In *Toto v. Lebanon*, the tribunal declined jurisdiction altogether over ‘pure contract’ claims brought under the umbrella clause on grounds that the underlying contract in question contained a conflicting dispute settlement clause. The dispute arose out of a contract to construct a highway. The claimant alleged both breaches of contract as well as breaches of treaty. In relation to the contract claims, the tribunal stated that it agreed with a view espoused by Judge Crawford, that ‘an umbrella clause is operative and may form the basis for a substantive treaty claim, but that it does not convert a contractual claim into a treaty claim’. For the tribunal, this meant that the umbrella clause did not change the proper law of the contract or its legal incidents, including provisions for dispute settlement, and

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46 Bureau Veritas, *Observance of Obligations*. For the umbrella clause in the Netherlands–Paraguay BIT, see *Paraguay* v. *Philippines*, ICSID Case No. ARB/03/2/3. According to the tribunal in *Toto v. Lebanon*, the umbrella clause in the Netherlands–Paraguay BIT ‘has to be interpreted in such a way as to give it some meaning and practical effect’ and thus it ‘establishes an international obligation for the parties to the BIT to observe contractual obligation with respect to investors’. The tribunal in *BIVAC v. Paraguay* declined to hear the claim on the grounds of non-admissibility. The claim concerned Paraguay’s failure to pay invoices under a pre-shipment inspection contract. The tribunal concluded that although the umbrella clause in the Netherlands–Paraguay BIT ‘has to be interpreted in such a way as to give it some meaning and practical effect’ and thus it ‘establishes an international obligation for the parties to the BIT to observe contractual obligation with respect to investors’, the claim was inadmissible because of the forum selection clause in the contract. The tribunal characterised the dispute as a purely contractual claim and concluded that the parties were not ‘free to pick and choose’ only parts of a contract to incorporate into an umbrella clause and to ignore others, especially their contractually negotiated dispute settlement arrangements.

47 The tribunal joined to the merits the issue of whether inadmissibility led to the claim being dismissed or stayed.

48 ibid., para. 141.

49 ibid., para. 149.

50 ibid., para. 148.

51 *Bosh International, Inc. and B&P LTD Foreign Investments Enterprise v. Ukraine (Bosh v. Ukraine)*, ICSID Case No. ARB/08/11, Award, 25 October 2012, paras. 252, 259. The tribunal stated obiter that given the Ukrainian courts had terminated the contract in accordance with applicable Ukrainian legislation, the claimants were not now entitled to assert that they had rights under the contract protected by the umbrella clause.


53 ibid., para. 200.

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although the clause could be used as a ‘mechanism for the enforcement of claims’, it did not ‘elevate pure contractual claims into treaty claims’. Thus, it found it had ‘no jurisdiction over the contractual claims arising from the contract referring disputes to Lebanese courts’.

In *Garanti Koza v. Turkmenistan*, which concerned a contract for the planning and construction of a highway, the tribunal indicated that if the claimant’s claims amounted merely to claims for breach of contract, they would be ‘beyond the jurisdiction of an ICSID tribunal and also that they would be subject to the forum-selection clause in the Contract’. However, given that a breach of the umbrella clause was asserted by the claimant in addition to other substantive BIT claims, and was ‘pleaded as a breach of the [BIT]’, the tribunal considered that it had jurisdiction over the umbrella clause claims.

In *Gavrilovic v. Croatia*, the tribunal adopted the analysis of the *SGS v. Paraguay* tribunal when considering whether a forum selection clause in a contract would impact its jurisdiction. The tribunal stated that it would not be ‘fulfil[ling] its mandate’ if it declined to ‘decide whether or not contractual obligations have been observed and, as a consequence, whether or not there has been a violation of the umbrella clause’.

### IV PRIVITY OF CONTRACT

One of the concerns driving the *SGS v. Pakistan* tribunal had been a fear that a certain interpretation of the umbrella clause might have opened the floodgates to a multitude of claims. Subsequent attention to the scope of obligations protected by the umbrella clause, and the parties who might avail of its protection, suggests those fears may have been overstated.

The majority view appears to be that umbrella clauses cannot be invoked by claimants who are not themselves party to the underlying contract (a question that commonly arises when the claimant’s local subsidiary has concluded the contract, rather than the claimant). In *WNC v. Czech Republic*, the tribunal identified and distinguished the few cases that have allowed claimants that were non-parties to the underlying contract to invoke an umbrella clause.

There is less consensus when it comes to the matter of privity concerning the state party to the underlying contract. A number of tribunals have found that where a legal entity separate

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55 ibid.
57 ibid., para. 244.
58 ibid., paras. 246–247.
60 ibid., paras. 856–860.
61 ibid., para. 422.
63 *WNC v. Czech Republic*, ibid., at paras. 331–333 (identifying *Continental Casualty v. Argentina* on the basis, among other things, that the tribunal’s statements in that case referred to general obligations of the host state and not obligations as a matter of contract); and paras. 338–339 (identifying *EDF v. Argentina*
to the state concludes a contract with the claimant, and under the proper law of the contract the state itself cannot be found to be a party to that contract, no umbrella clause claim can be brought. These tribunals reject the application of the rules of attribution under general international law,64 which do not open avenues to sue the state for breach of contractual obligations for which it is not directly bound.65 In Impregilo v. Pakistan, for example, the tribunal found that Pakistan's Water and Power Development Authority (over which Pakistan exercised control) was properly characterised as an autonomous corporate body, legally and financially distinct from Pakistan by reference to Pakistan's domestic laws.66 In rejecting jurisdiction over the claimant’s contract claims, the tribunal said that international law rules on state responsibility and attribution apply only to conduct that violates international law and not to responsibility of a state for the conduct of an entity that breaches a municipal law contract.67 Similarly, in Gavrilovic v. Croatia, the tribunal reminded the parties that the rules of attribution could not operate to impose primary obligations on a state under a contract to which the state was not a party.68

Other tribunals, however, have indicated that they would apply a different approach. The tribunals in Alpha Projecktholding v. Ukraine, Bosh v. Ukraine and CC/Devas v. India premised their findings that the umbrella clause was inapplicable on the basis that the conduct of the entities involved was not attributable to the state.69 In CC/Devas v. India, the tribunal said that because the relevant state-owned entity that had concluded the contract was not acting as an organ of the state under rules of attribution when entering into the contract, the contract did not constitute an obligation the state had entered into within the meaning of the umbrella clause.70

V ‘GOVERNMENTAL’ OR ‘MERELY COMMERCIAL’ CONDUCT

Although there is a line of decisions emphatically rejecting the notion that obligations protected by the umbrella clause must be governmental or sovereign in nature,71 in Gavrilovic

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64 Generally considered to be codified and developed in the ILC Articles, n. 3.
68 Gavrilovic v. Croatia, n. 58; para. 856, distinguishing findings made in Noble Ventures v. Romania and Amoco v. Iran. On the facts, the tribunal found the umbrella clause to be inapplicable, given Croatia was not party to the purchase agreement, and even though the liquidator's actions were attributable to Croatia, neither that nor the umbrella clause transformed the contract obligations into obligations of Croatia.
70 CC/Devas v. India, ibid., para. 281.
71 See cases cited at n. 43, SGS v. Paraguay, n. 29, para. 168.
Observance of Obligations

v. Croatia, the tribunal reasoned along the same lines as the CMS v. Argentina and EDF v. Argentina tribunals, when it cautioned that not just any breach of contract could amount to a breach of the treaty’s umbrella clause:

A failure by a government agency to pay for a box of pencils delivered pursuant to an agreement to provide office supplies, for example, would not come within the reach of Article 2(2), because it would have nothing to do with an investment. But an act of an organ of a state that results in the breach of a contractual obligation relating to an investment of a national or company of the other state party to the BIT does seem to this tribunal to come within the reach of that article, especially where the immediate cause of the breach is an action by an organ of the state other than the agency that is the party to the agreement. This is the situation presented by the facts of this case.

VI UNILATERAL COMMITMENTS

The final question is whether, in addition to contractual commitments, relevant obligations may be found in general legislation or unilateral commitments. Although there is arbitral support for the application of the umbrella clause to unilateral or legislative commitments, several tribunals have found that where the umbrella clause refers to obligations or commitments that have been ‘entered into’ by the state, the BIT is concerned with contractual obligations alone. In Micula v. Romania, the tribunal stated that the question of whether the state had an obligation was a matter of Romanian law, and the claimants had not proven that the relevant commitment was an obligation under such law.

While arbitral practice appears to have moved on from the early SGS cases and, in particular, there appears to be growing acceptance towards ascribing substantive meaning to the umbrella clause, separate from the other provisions of the treaty, there are still a number of unsettled questions. The umbrella clause continues to provide fertile ground for creative lawyering and further debate.

72 See CMS v. Argentina, n. 3, para. 299 (‘not all contract breaches result in breaches of the Treaty. The standard of protection of the treaty will be engaged only when there is a specific breach of treaty rights and obligations or a violation of contract rights protected under the treaty. Purely commercial aspects of a contract might not be protected by the treaty in some situations, but the protection is likely to be available when there is significant interference by governments or public agencies with the rights of the investor’); EDF v. Argentina, n. 44, para. 940 (‘This does not mean that all contractual breaches necessarily rise to the level of treaty violation.’).

73 Gavrilovic v. Croatia, n. 58.


75 See CMS Annulment Decision, n. 43, paras. 90, 95; Al-Bahloul v. Tajikistan, n.44, para. 257; SGS v. Philippines, n. 15, para. 121; Noble Ventures v. Romania, n. 28, para. 51; Philip Morris v. Uruguay, n. 27, para. 478.

76 ibid., n. 44, para. 447. See also Garanti Koza v. Turkmenistan, n.55, para. 331 (albeit in the context of contract).

77 An interpretation that would render a treaty provision ineffective or meaningless is not likely to be the correct one and should be avoided: Robert Jennings and Arthur Watts (eds), Oppenheim’s International Law (Longman, 1992) 1280.
Investments overseas, especially in politically unstable countries, may be exposed to the adverse effects of unpredictable actions or omissions of the host government. Political risk insurers can help manage these risks by providing coverage for certain losses related to political causes. If the insured investor’s loss satisfies the relevant terms and conditions under its insurance contract, the insurer will compensate the insured accordingly. By increasing confidence and reducing uncertainty in investment planning, the availability of political risk insurance (PRI) in a risky developing country helps investors obtain funding for insured investments and the host state attract more investment, thereby supporting the economic interests of all parties involved. In addition to this contractual arrangement, investors and their investments may be protected by and entitled to compensation under an investment treaty. Thus, on the road to recovering losses from government wrongdoing, PRI providers and insured investors may have to deal with the complicated interplay between insurance and investment treaty regimes.

This chapter will discuss how insurance contracts governed by applicable national law and investment treaties governed by public international law principles may differ on the protections available for risks and losses, and how claims are assessed. These differences are highlighted in the example of expropriation. If an investor is successful with an insurance claim, the insurer may want to recover the compensation paid and consider either stepping into the shoes of the investor to itself claim against the host state in an investment arbitration, which may involve complicated problems with bilateral investment treaty (BIT) subrogation clauses and issues of standing, or making other arrangements so that the investor can pursue investment arbitration and pass the ultimate benefits to the insurer.

I  AN INTRODUCTION TO THE POLITICAL RISK INSURANCE MARKET

Political risks are those associated with government actions or omissions that deny or restrict the right of an investor to use or benefit from the investor’s assets, or that reduce the value of the investment.2 According to the MIGA-EIU Political Risk Survey 2013, political risk ranks second place, after economic concerns, among the most important concerns for investors making foreign direct investment in developing economies.3 The top two political risks that worry investors in developing economies are adverse regulatory changes in the host state and

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1 Huawei Sun is a partner and Chang Liu is an associate at Zhong Lun Law Firm.
a breach of contract by the state. An example of the adverse regulatory change includes the Tanzanian government’s introduction of new regulations in 2017 to ban foreign exports in the natural resources sector.

Political risk insurers commonly provide coverage to protect against losses that arise from five types of risks: expropriation, transfer restrictions, political violence, arbitral award default (in relation to a breach of contract) and denial of justice.

There are three main types of PRI providers: (1) public state-sponsored providers, such as the Overseas Private Investment Corporation (OPIC), a governmental agency backed by the full faith and credit of the United States, and China Export & Credit Insurance Corporation (Sinosure), a company funded by the Chinese government with the purpose of promoting foreign trade and economic cooperation; (2) multilateral providers, such as the Multilateral Investment Guarantee Agency (MIGA) of the World Bank, the Asian Development Bank and the African Trade Insurance Agency; and (3) private providers, such as Sovereign Risk Insurance of Bermuda and the American International Group of the United States. In the Berne Union – a leading association for the global export credit and investment insurance industry with 84 members (including OPIC, Sinosure and MIGA) – public providers dominate the PRI market in overall amounts insured because of the availability of enormous funding support provided by its sovereign sponsors.

According to a Berne Union survey, the investment insurance cover provided by its members to new business totalled US$64 billion for 2017, which showed a notable fall versus 2016 levels. The Association of Southeast Asian Nations, the Commonwealth of Independent States and Latin American countries account for 20 per cent each of new business, with the top five countries by business volume being Kazakhstan, Vietnam, Indonesia, China and Uzbekistan. A total of US$232 million was paid by its members under investment insurance policies in 2017 – the most on record for any single year. This figure is dominated by a single recovery claim for political violence in Libya, followed by another recovery in the amount of US$11 million in relation to a claim in Turkey. Marking its 30th year of operation, MIGA issued a record US$5.3 billion in political risk insurance and credit enhancement guarantees in 2018.

As Chinese outbound investments have been robust in recent years, especially in infrastructure projects in developing countries, Chinese investors are increasingly facing political risks in those countries. For example, in 2011, tens of thousands of Chinese nationals were evacuated after a civil riot broke out in Libya, and Sinosure paid compensation of 490 million yuan for 29 companies that suffered losses in the riot.

It is apparent that PRI has become a useful tool for managing risks to outbound investments in politically unstable economies.

4 ibid., page 42.
5 ibid., page 32.
II INSURANCE CLAIMS VERSUS INVESTMENT TREATY ARBITRATION CLAIMS

Insurers will have their own governing policies for the terms of coverage for the five most common types of risks:

- **a** expropriation (government acts that deprive the investor of ownership or control rights to its investment);
- **b** transfer restrictions (to transferring currency or converting currency at the reference rate of exchange);
- **c** political violence (the destruction or disappearance of tangible assets, or the total inability of the investor to conduct operations as a result of violent political or military acts);
- **d** arbitral award default (where the government is not complying with an arbitral award against it in cases where it was found to breach a contract with the investor); and
- **e** denial of justice (an inability to obtain an award as a result of government acts that render the dispute resolution procedure specified in the contract impossible or impracticable).

From a review of publicly available OPIC arbitral awards and claims determinations, it appears that the precise terms of each insurance contract are negotiated and tailored according to the circumstances of the investment.9

The scope of protection and compensation for loss may be different under a PRI policy and under an investment treaty. Insurance policies exist in the ambit of contract law so the terms and conditions for successful claims and compensation from the insurer are defined by the contract, and interpreted in accordance with its applicable law. As these types of losses arise from government conduct, the investor may also have protected rights and claims under an investment treaty; these claims are assessed on the basis of treaty provisions, in accordance with international law. Thus, the scope of protection available to the investor and the investor's ability to be compensated under a PRI policy may not overlap completely with that under an investment treaty. For example, a loss that could be successfully claimed on the basis of the fair and equitable treatment (FET) principle under a treaty may not be covered by a PRI policy. Also, arbitral award default coverage is unique to PRI policies.

The difference and interaction between the two regimes can be seen in the course of claims determination. Some contracts, such as the MIGA draft contracts, provide that the applicable law should be 'general principles of law',10 which may allow for the consideration of principles of public international law. Other contracts, especially that of national PRIs, may provide for the law of the home state; for example, Sinosure's policy provides that all disputes between the insured and Sinosure shall be resolved before the China International Economic and Trade Arbitration Commission in accordance with Chinese law. A local law may not be as developed, or may even be silent, on certain issues that may find a resolution by applying the more developed jurisprudence of public international law; for example, indirect expropriation. However, the role of public international law in claims determinations under insurance contracts will depend on whether local laws allow for its consideration. Where

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9 See, generally, the arbitral awards published on the OPIC website www.opic.gov/who-we-are/transparency/claims-and-arbitral-awards.

international law was necessary to resolve a dispute but was restricted from applying by the domestic applicable law, tribunals have in the past invoked the idea of an ‘international contract’ and stated that it was ‘necessary to resort to the general principles of law and to apply them’ to resolve the dispute.\textsuperscript{11} An interplay also happens when the contractual terms of a PRI policy refer expressly to a particular BIT to define the scope of coverage; for example, a PRI policy provides that it covers losses as a result of taxes imposed in violation of the FET requirement under a BIT. Given the complexity of the issue, there will be uncertainties as to how international law principles will be applied by local tribunals.

A review of the OPIC claims determinations published on their website reveals OPIC taking a textual approach to interpreting the insurance contract, as is to be expected. These claim determinations did not involve in-depth discussions about public international law. However, an investor dissatisfied by a rejected claim may instigate commercial arbitration proceedings against OPIC, and the tribunal may treat the international law principles relating to the claim differently to OPIC. For example, in the case of Revere, OPIC determined the investor’s actions were the real cause of its loss and the investor was still in control of its assets; however, the tribunal held that the investor’s control was no longer effective because it could not continue to make certain business decisions.\textsuperscript{12}

An insurer may wish to be aware of all the nuances of public international law when it drafts its insurance contract and creates guidelines on claims determination. The insurer would then, in turn, be aware of how its own claims determinations may be aligned with or differ from the way (1) a commercial arbitration tribunal might assess an insurance compensation claim under a contract; and (2) an investment arbitration tribunal might assess a treaty claim against the host government at international law. This awareness would help the insurer make an informed decision about defining the scope of its mandate, and avoid, if it wishes to, the likely divergent results it may face in another forum for particular issues. The insurer will also have a clearer idea about which kinds of claims would be likely to be successful at treaty arbitration and are worth pursuing.

\section*{III\hspace{1em}EXPROPRIATION – INSURANCE CONTRACT TERMS VERSUS INTERNATIONAL LAW}

The differences between PRI policies and treaty protection can be seen, for example, in claims assessment for loss resulting from expropriation.

One of the requirements for finding expropriation is an interference by a host state causing the substantial loss of control or economic value of a foreign investment. International law and insurance contracts may differ on the level of deprivation required.

Some contracts contain a sufficiently detailed definition that resembles the widely accepted international law standard of ‘total or substantial deprivation’.\textsuperscript{13}

\begin{thebibliography}{9}
\bibitem{12} See, e.g., \textit{Revere Copper and Brass, Inc. v. OPIC}, reprinted in 17 I.L.M 1321 (1978).
\bibitem{13} See, e.g., \textit{Société Générale In respect of DR Energy Holdings Limited and Empresa Distribuidora de Electricidad del Este SA v. The Dominican Republic}, UNCITRAL, LCIA Case No. UN 7927, Award on Preliminary Objections to Jurisdiction, 19 September 2008, paragraph 64; \textit{Alpha Projectholding GMBH v. Ukraine}, ICSID Case No. ARB/07/16, Award, 8 November 2010, paragraph 408.
\end{thebibliography}
For example, MIGA’s draft guarantee for equity investments refers to:

*any executive or administrative action or omission, or any legislative action . . . in one or a series of events attributable to the Host Government that directly or indirectly causes: (a)(i) the Guarantee Holder to be (x) deprived of its ownership rights in, or effective control of, all or a substantial portion of the Guaranteed Investment, or (y) otherwise effectively deprived of all or substantially all economic value of the Guaranteed Investment; or (ii) the Project Enterprise to be deprived of a fundamental right without which it is not financially viable; provided, however, that the diminution of the Project Enterprise’s profit does not in itself constitute such deprivation.*

However, coverage is available on a limited basis for partial expropriation (e.g., confiscation of funds). Other contracts may make different stipulations. MIGA’s draft guarantee for shareholder’s loans provides for deprivation of the insured’s material rights as a lender or a creditor, and any deprivation of the insured’s repayment funds to constitute expropriation. Sinosure’s policies provide that partial deprivation may fall within the protection of its various policies. This calls into question whether the policies provide wider protection than investment treaties. However, Sinosure’s policies may tailor their coverage to a limited scope of the government acts.

MIGA’s reference to ‘a series of events’ (see above) also provides coverage for creeping expropriation. Sinosure’s policies do not make such an express reference so it may not provide coverage for creeping expropriation.

As another example of the difference between insurance policies and international law, MIGA excludes from its expropriation coverage ‘a bona fide, non-discriminatory measure of general application that governments normally take for the purpose of regulating economic activity, ensuring public safety, raising revenues or protecting the environment’ so long as this measure is not ‘designed by the Host Government to have a confiscatory effect’. Recent versions of Sinosure contracts contain similar exemptions. Unlike these contracts, treaties rarely contain such provisions and it is unclear how the scope of these exemptions compares to a state’s regulatory power under international law.

Few insurance contract claims determinations discuss international law principles in much depth. An OPIC determination involving expropriation summarised the international law principles and cited jurisprudence that supported its contractual terms, and briefly applied these principles in the determination. It further states that the OPIC provision ‘comports with customary international law in its recognition of both direct and indirect

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15 See, e.g., Article 4.1(b) of the MIGA Contract of Guarantee for Equity Investments (2018-Forms), October 2018.
16 See, e.g., Article 4.1(b) to (d) of the MIGA Contract of Guarantee for Shareholder Loans (2016-Forms), November 2016.
17 Based on our review of Sinosure’s sample terms, which are not publicly available.
expropriation and ‘reflects a body of international investment law that recognizes the expropriatory effects of state actions that prevent, unreasonably interfere with, deprive, or unduly delay effective enjoyment of an investor’s fundamental rights in its investment’.  

In any case, it may be fair to say that insurers have developed insurance policies to be a class of their own, which may or may not correspond to international law standards.

IV SUBROGATION

Insurers have an interest in recovering compensation paid to the insured, especially when the insured has the right to claim compensation from a host state in another forum. Thus, PRI contracts usually include a subrogation clause, where the insured investor’s rights and claims against the host state are assigned to the insurer after payment or with an undertaking to make payment. To seek compensation from a host state in investment arbitration, the PRI provider will also need to rely on a BIT provision that recognises its subrogation right. The next sections will address the subrogation rights provided for in the contract and by operation of an investment treaty. Local laws on subrogation may also operate in the absence of contractual subrogation; however, this chapter will not discuss this.

i Subrogation under contract

A standard contractual subrogation clause may look like this, from MIGA:

MIGA shall be fully subrogated, in the amount of any compensation paid for a Loss, plus interest and expenses, to all claims, causes of action, and other rights of recovery that the Guarantee Holder has against the Host Government, the Project Enterprise, or any other person or entity in respect of such Loss. The Guarantee Holder shall not impair or prejudice MIGA’s rights of subrogation.  

ii Recognition of subrogation under a BIT

BITs typically contain a provision expressly obliging the host state of the investment to recognise the subrogation of the investor’s rights under the BIT to the home state insurer or its designated agency. However, few BIT provisions cover all insurers, so private PRI providers are usually excluded from the subrogation clause. We consider some examples below.

Many BITs contain subrogation clauses similar to Article 7 of the China–Germany BIT 2003, which states:

If one Contracting Party or its designated agency makes a payment to its investor under a guarantee given in respect of an investment made in the territory of the other Contracting Party, the latter Contracting Party shall recognize the assignment of all the rights and claims of the indemnified investor to the former Contracting Party or its designated agency, by law or by legal transactions, and the right of the former Contracting Party or its designated agency to exercise by virtue of subrogation any such right to the same extent as the investor.

20 ibid., page 5.
21 ibid., page 6.
Some BITs provide for the subrogation of insurers generally, including private insurers, with the aim of protecting the different types of providers in the home market. For example, the Netherlands Model BIT 2018 at Article 14 states: ‘[i]f the investment of an investor of a Contracting Party is insured . . . any subrogation of the insurer . . . to the rights of the said investor pursuant to the terms of such insurance or under any other indemnity given shall be recognized by the other Contracting Party.’23 Nearly all the Dutch BITs contain such a subrogation clause.24 The Norway Model BIT (draft) 2015 also states: ‘[i]f the investments of an investor are insured against non-commercial risks, any subrogation of the claims of the investor pursuant to this Agreement shall be recognized by the other Party’.25

More interestingly, the Netherlands–Mexico BIT 1998 contains an unusual provision: the subrogation of ‘a wholly privately owned and controlled insurance corporation’ to the rights of the national (investor) of the same contracting party shall be recognised by the other contracting party and ‘[o]nly the national or the insurance corporation shall be entitled to exercise such rights and to engage in a dispute with respect to those rights’.26

Some BITs set out the rights of the investor after it subrogates its rights to the insurer. The New Zealand–China Free Trade Agreement (FTA) 2008 provides that ‘where a Party (or any agency, institution, statutory body or corporation designated by it) has made a payment to an investor of that Party and has taken over rights and claims of the investor, that investor shall not, unless authorized to act on behalf of the Party or the agency of the Party making the payment, pursue those rights and claims against the other Party.’27 The China–Korea FTA 2015 contains a similar provision and also clarifies: ‘[f]or greater certainty, the investor shall continue to be entitled to exercise its rights that have not been subrogated.’28

However, the China–Mexico BIT 2008 clearly excludes altogether the availability of arbitration (national or international) for resolving disputes between the subrogee and the other contracting party.29

**V THE INSURER’S STANDING TO EXERCISE ITS SUBROGATION RIGHTS IN INVESTMENT ARBITRATION**

Where a BIT subrogation clause covers the insurer, the rules of various dispute resolution institutions will determine whether the insurer has standing to bring a claim.

A state-backed insurer may not be eligible to be a party in an arbitration at the International Centre for Settlement of Investment Disputes (ICSID) under the ICSID Convention because ICSID arbitration is only available for investment disputes between a contracting state, or a designated subdivision or agency of the state, and a ‘national of another Contracting State’ as per Article 25(1).30 As the state-backed PRI provider is usually deemed a governmental entity, it would therefore not be a qualified ‘national of another Contracting

23 Article 14 of the Netherlands Model Investment Agreement 2018, 19 October 2018.
26 Article 7 of the Netherlands–Mexico BIT, signed on 13 May 1998 and effective from 1 October 1999.
27 Article 148.2 of the China–New Zealand FTA, signed on 7 April 2008 and effective from 1 October 2008.
28 Article 12.11.2 of the China-Korea FTA, signed on 1 June 2015 and effective from 20 December 2015.
29 Article 9.2 of the China–Mexico BIT, signed on 11 July 2008 and effective from 6 June 2009.
30 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention).
State’. The drafting history of the ICSID Convention shows that an exception to Article 25(1) was considered in the context of subrogation; however, ICSID deliberately chose to deny party status to an investor’s indemnifying state as a procedural matter of standing (but this does not affect the right to subrogation, per se).³¹

To distinguish private PRI providers from public ones, the tribunal in CSOB v. Slovak Republic confirmed that ‘for purposes of the Convention a mixed economy company or government-owned corporation should not be disqualified as a “national of another Contracting State” unless it is acting as an agent for the government or is discharging an essentially governmental function.’³² Thus, the determinative criterion for distinguishing public and private PRI providers is whether they administer the PRI system on behalf of the investor’s home state.³³ While some say ‘financial dependence’ on the host state is a criterion for disqualification from being a ‘national of another Contracting State’,³⁴ others say ownership or control of the government will not, alone, disqualify an entity.³⁵ As Sinosure is a state-owned and policy-oriented enterprise, its qualification as ‘investor’ under the ICSID Convention will be subject to challenge.

If ICSID arbitration is not available, given an effective subrogation clause in the BIT, the state-backed insurer may nevertheless have recourse to ad hoc arbitration if allowable under the relevant arbitration rules. For example, the UNCITRAL Arbitration Rules do not contain a definition of ‘investor’ and do not reject subrogation rights.³⁶ Interestingly, in addition to the subrogation clause, Annex C of the draft Norway Model BIT 2015 further states that if an insurer does not have legal standing under Article 25(1) of the ICSID Convention, the contracting parties consent to submission by an insurer of a dispute to arbitration under the UNCITRAL Arbitration Rules, but that the procedural rules of ICSID shall apply.³⁷

A private PRI provider covered by a BIT subrogation clause (such as the Dutch and Norwegian BITs) has standing to be a party to an ICSID proceeding in conformity with Article 25(1) of the ICSID Convention. However, many BIT subrogation clauses do not provide for the private PRI, so investment arbitration, at ICSID or otherwise, would nevertheless be unavailable.

VI SPECIFIC AGREEMENTS WITH HOST STATES TO RECOGNISE AND EXERCISE SUBROGATION RIGHTS

Some public PRI providers will only issue an insurance contract if the host state of the investment meets certain conditions. For example, OPIC may not offer insurance for a

³³ Above, 31, page 188.
³⁴ ibid.
³⁵ Above, 32, paragraph 18.
³⁶ See the UNCITRAL Arbitration Rules 2013.
project in a country with which the United States does not have an investment agreement, and it must determine that ‘suitable arrangements’ exist for protecting its interest, including its right to subrogation. These conditions are fulfilled in the form of an investment incentive agreement or investment guarantee, which provides for ad hoc interstate arbitration for disputes involving questions of international law. There is one case of interstate arbitration where the US government issued a Request for Arbitration to the government of India to claim for damages in excess of US$110 million, which is the amount OPIC compensated the investor.

MIGA issues guarantees for investments in a Member State (a signatory to the MIGA Convention) that flow from other Member States. The signatory member is required under the MIGA Convention to recognise MIGA’s right of subrogation; however, host states have the right to object to the issuance of a PRI contract. MIGA cannot conclude a contract of guarantee with an investor ‘before the host government has approved the issuance of the guarantee by the Agency (i.e., MIGA) against the risks designated for cover’, and approval is deemed to have been given unless the member objects within a reasonable period after notification. MIGA requires the insurer as subrogee to first engage in settlement negotiations with the member host state. Failing a resolution, MIGA may pursue ad hoc arbitration with the host state, which shall be guided by the procedures of the ICSID Arbitration Rules.

Sinosure, however, does not have a membership programme or any requirements similar to the above for the issuance of a contract. Any potential actions against the host state will be based on the clauses of the relevant BIT.

VII  WHEN THE INSURER IS UNABLE TO CLAIM IN ARBITRATION IN ITS OWN RIGHT

If the insurer cannot resort to the subrogation provisions of the BIT, it may still make the following arrangements to support or compel the investor to first make a claim against a host state with the aim of benefitting the insurer. The insurer will also have to make arrangements with the insured on the costs of the arbitration.

i  Assignment

The assignment of an ICSID claim from an insured investor to its insurer should be possible if the necessary jurisdictional conditions are fulfilled by the investor first and the assignment

38 22 USC 2197(a).
39 22 USC 2197(b).
42 Article 2(a) of the Convention Establishing the Multilateral Investment Guarantee Agency (the MIGA Convention), amended and effective 14 November 2010.
43 Article 18 of the MIGA Convention.
44 Articles 15 and 38(b) of the MIGA Convention.
45 Article 57(b) of the MIGA Convention and Article 2 of Annex II thereto.
46 Articles 4(a) and (e) of Annex II to the MIGA Convention.
occurs after arbitration is instituted. In *CSOB v. Slovakia*, the investor CSOB assigned its right to claim against Slovakia under a contract to its home state, the Czech Republic, against a monetary consideration, similar in effect to an insurance payout. Slovakia argued that the Czech Republic had become the real party in interest and that it was disqualified from stepping into CSOB’s shoes under Article 25(1) of the ICSID Convention. The tribunal noted that standing is a jurisdictional matter determined by reference to the date the proceedings are instituted (CSOB had standing at that date), and as the assignment occurred after that time, the tribunal had jurisdiction to hear the case.48 However, the issue of assignment sometimes refers to a case where it appears that the assignment was engineered to attract jurisdiction that was otherwise lacking. In such a case, a tribunal will likely react more negatively.

### ii Directing the investor to make a treaty claim

The insurer could also request the insured investor to pursue its rights under an investment treaty and arrange for the proceeds to pass to the insurer.

The insurer may require that the insured investor ‘exhaust’ its rights of recourse to proceedings before receiving compensation under insurance. Such a clause would reduce the attractiveness of the policy, and the insured will undoubtedly weigh up the cost of the premiums to be paid to obtain the insurance and its obligations to recover in another forum. Thus, the more common alternative is conditional payment – namely, the insurance policy provides that the insurer will compensate the insured on the condition that the investor pursues its rights of recourse.

Sinusure’s policy for equity investments provides that after it pays compensation, the insured is obligated to file claims in its own name against the host state if so requested by Sinusure. Otherwise, Sinusure has the right to refuse to pay further compensation and ask for repayment of the paid amounts.

MIGA’s 2018 draft Contract of Guarantee for Equity Investments provides for similar covenants following claim compensation paid to the insured, and clarifies that if it receives any compensation, the insured must hold those proceeds in trust for the benefit of MIGA.49

The relative market power of the insurers and potential investors, and the motivations of the insurer may affect whether the arrangement is more beneficial to the insurer or the insured, and account for different approaches among PRI providers.

A potential problem may arise against the investor’s right to claim in investment arbitration (for the insurer’s benefit) when it also has a right to compensation from an insurance provider. The tribunal in *Hochtief v. Argentina* stated that the insurance payment Hochtief received from the German Government’s Federal Guarantees for Direct Investments in Foreign Countries programme should not be deducted from the amount due to Hochtief from Argentina as awarded. The tribunal remarked that the insurance payment ‘does not reduce the losses caused by Respondent’s actions in breach of the BIT’ and there is no principle of international law that ‘requires that such an arrangement . . . should reduce Respondent’s liability’.50 The tribunal further recognised that the investor itself paid for the insurance arrangement with a third party (the insurer), and the investor may be obliged to hand over

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48 Above, 32, paragraph 31.
49 Articles 11.3 and 11.4 of the MIGA Contract of Guarantee for Equity Investments (2018-Forms), October 2018.
the damages recovered, but that was a matter of private contract into which the tribunal has no cause to enquire. In *Glencore Finance v. Bolivia*, where the investor claimed that the host state expropriated its metal mining plants and a mine, the respondent argued that if the tribunal were to award compensation to the claimant, any compensation already received by the claimant from its political risk insurer – which was caused by the same underlying facts – shall be offset from the amount awarded to the investor. The case is ongoing and it remains to be seen whether this argument will find any support by the tribunal.

After initiating an UNCITRAL investment treaty proceeding against Colombia in March 2017 pursuing over €1.3 billion in defaulted electricity payments, the Spanish energy company Naturgy reportedly filed in June 2018 an arbitration claim against its political risk insurer after the latter opted not to pay out on the default for over €400 million. It remains unclear whether and how these coexisting claims interact.

### iii An agreement with the host state regarding the investor

To prevent the type of challenge against investors discussed in *Hochtief*, some BITs contain a provision that indemnification by a third party would not affect the investor’s rights of recourse to arbitration (at ICSID or otherwise).

For example, the Canada–China BIT 2012 provides that ‘a disputing Contracting Party shall not assert, as a defence, counterclaim, right of setoff or otherwise, that the disputing investor has received or will receive, pursuant to an insurance or guarantee contract, indemnification or other compensation for all or part of its alleged damages.’ Other BITs may state that a contracting party cannot ‘raise as an objection’ that the investor has received indemnity for its losses, or that such payment shall not affect the right of the investor in a proceeding.

### VIII CONCLUSION

PRI policies and BITs provide separate regimes for protecting investors’ investments from wrongful government conduct. Investors attracted to the contractual protection of an insurance contract and its other benefits would prefer to obtain compensation under its policy, for which it paid a premium, over the costly and difficult process of claiming against a host state in investment arbitration. However, the insurer will likely want to recover compensation paid. The insurer’s right to commence investment arbitration against a host state will depend on an insurance contract clause providing for subrogation, an applicable BIT clause recognising the subrogation and having standing in a particular forum, each of which involves limitations and difficulties. The insurer could instead request the investor to institute a claim and make arrangements for assignment, or for the proceeds to be passed to the insurer. If investment arbitration against the host state is an option, through whichever

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51 ibid.
54 Article 13(2) of the China–Canada BIT, signed on 9 September 2012 and effective from 1 October 2014.
55 Article 8(1) of the Paraguay–UK BIT, signed on 4 June 1981 and effective from 23 April 1992.
avenue, the insurer will need to evaluate the claim’s chance of success under international law – the government wrongdoing must constitute a breach of a treaty. The possible differences between the substantive protections under an insurance policy and a BIT mean that not every risk insured will attract the same protection under a treaty, and government misconduct that leads to a successful claim under the contract may not give rise to a breach of a treaty obligation, as each jurisdiction applies its own system of legal principles to claims assessments.

Different insurers have different agendas when setting their insurance and coverage policies, and different insurers may invoke and be influenced by public international law principles and jurisprudence in different ways. Though insurers have rarely sought treaty arbitration, with increasing use of PRI (e.g., by Chinese investors investing in infrastructure projects in politically unstable economies) insurers may be more likely to confront situations involving huge claims where investment arbitration would be a worthy pursuit. It will be interesting to see how developments in international law, treaty arbitration and the global foreign investment environment may affect insurance policies and the PRI industry in the future.
Part V

DAMAGES
Chapter 20

COMPENSATION FOR EXPROPRIATION

Konstantin Christie, Esra Ogut and Rodica Turtoi

I INTRODUCTION

Generally, under customary international law, when a state breaches its obligations or exercises its power in a way that deprives a party of its property, that party is entitled to one of the following forms of reparation: restitution, compensation or satisfaction. Among these forms of reparation, when it comes to investment treaty arbitration (ITA), compensation is most often invoked by claimants as the pre-eminent means of reparation for expropriation. Investors also have a tendency to claim expropriation, as it is the most severe form of interference with property (and therefore could potentially lead to a decision awarding them higher damages) and since this type of compensation is typically explicitly provided for in the relevant international investment agreement (IIA).

This chapter will explore the treatment of compensation by tribunals composed under IIAs and the various approaches that have emerged. The authors will focus on the distinction between lawful and unlawful expropriation to the extent it is still relevant for the applicable compensation standards, and discuss some of the valuation methods most commonly used by the arbitral tribunals to compensate investors for expropriation and the issue of valuation date.

II GENERAL PRINCIPLES OF COMPENSATION FOR EXPROPRIATION

Under international law, the obligation to pay reparation for damage caused by wrongful acts has been considered an essential obligation. The seminal 1928 decision of the Permanent Court of International Justice (PCIJ) in the Chorzów Factory case recognised the function of full reparation in international law and identified the general principles of reparation as follows:

reparation must, as far as possible, wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed.

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2 Draft ILC Articles on the Responsibility of States for Internationally Wrongful Acts, Article 34.

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Compensation for Expropriation

Restitution in kind, or, if this is not possible, payment of a sum corresponding to the value which a restitution in kind would bear; the award, if need be, of damages for loss sustained which would not be covered by restitution in kind or payment in place of it.5

After the Chorzów Factory case, several tribunals established following the nationalisation in Libya and Iran grappled with the appropriate measures and meanings of reparation, restitution and compensation concepts, without developing a single standard.6 The International Law Commission's Draft Articles on the Responsibility of States for Internationally Wrongful Acts (the ILC Articles) of 2001 arguably represented a first successful attempt in solidifying the main principles of international law on reparation and compensation.

Pursuant to Article 31(1) of the ILC Articles, ‘[t]he responsible State is under an obligation to make full reparation for the injury caused by the internationally wrongful act.’ As the commentary to the ILC Articles makes clear, ‘reparation’ has a broad definition that covers both restitution and compensation.

The ILC Articles essentially followed the Chorzów Factory case – determining that reparation meant to ‘wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed’,7 with restitution deemed to come ‘first among the forms of reparation’ since it ‘most closely conforms to the general principle that the responsible State is bound to wipe out the legal and material consequences of its wrongful act’.8 The ILC Articles also adopted the customary international law view that where restitution is unavailable or inadequate, including when ‘the property in question has been destroyed or fundamentally changed in character or the situation cannot be restored to the status quo ante for some reason’,9 compensation is more appropriate.

In ITA practice, claims for restitution as expressed in the ILC Articles, and the PCIJ’s decisions have largely been replaced by claims for compensation.10 Most of the bilateral and multilateral international investment treaties today contain provisions with respect to the standard of compensation giving comfort and guidance to the investors and tribunals alike in terms of determining the appropriate measure of compensation (or reparation) to be provided to an investor.11 Further, many situations involving violations of IIAs do not allow for a restoration of the status quo ante, leaving only compensation as an option. Therefore, the more pertinent question in recent ITA practice has been the relevance of the distinction

5 Factory at Chorzów (Germany v. Poland), Merits, 1928 PCIJ (Ser. A) No. 17 (13 September), Composition of the Court: President Anzilotti; Former President Huber; Judges Lord Finlay, Nyholm, de Bustamante, Altamira, Oda, Pessoa; Deputy Judge Beichmann; National Judges Rabel, Ehrlich.
6 For further discussion on the historical development of the compensation standard, see I Marboe, Calculation of Compensation and Damages in International Investment Law, 2017, pages 44–50.
7 ILC Articles, commentary 2 to Article 31; See also S Ripinsky and K Williams, Damages in International Investment Law, 2015 (reprinted), page 53.
8 M W Friedman and F Lavaud, Damages Principles in Investment Arbitration in the Guide to Damages in International Arbitration, 2017, page 97; ILC Articles, commentary 3 to Article 35.
9 ILC Articles, commentary 4 to Article 35.
11 ibid., page 46.
between lawful and unlawful expropriation with respect to the determination of an applicable standard of compensation and the valuation method (including the valuation date). These subjects will be discussed in more detail below.

III THE IMPACT OF THE UNLAWFUL NATURE OF EXPROPRIATION ON COMPENSATION

Whether the payment of compensation is a prerequisite for lawful expropriation

Examination of recent ITA cases demonstrates that whether an expropriation is lawful or unlawful can have a significant impact on the applicable valuation method and the recovery process for the investor.

Traditionally, expropriation was deemed lawful only if it has been followed by compensation. However, over the years, and especially in the postcolonial debates, some commentators and tribunals started considering expropriation lacking the payment of compensation as lawful. With the proliferation of bilateral investment treaties (BITs) and other IIAs providing for specific mechanisms of compensation for lawful expropriation, the distinction has lost some of its poignancy; however, some variations in the treatment of this issue by tribunals remain.

Several decisions from the cases of nationalisation by Venezuela provide useful examples. Thus, in Mobil Cerro Negro v. Venezuela, the dispute arose out of taxation and eventual nationalisation of two oil projects in which the claimants had interests, and subsequent disagreements concerning the amount of compensation owed to the investor. It was not controversial that Venezuela made proposals during the negotiations with the investors but did not make any payment. The tribunal considered that compensation not being paid was insufficient to find that the expropriation was unlawful, commenting that:

> the mere fact that an investor has not received compensation does not in itself render an expropriation unlawful. An offer of compensation may have been made to the investor and, in such a case, the legality of the expropriation will depend on the terms of that offer. In order to decide whether an expropriation is lawful or not in the absence of payment of compensation, a tribunal must consider the facts of the case.\(^\text{15}\)

Having reviewed the evidence before it, the tribunal found that the claimants did not demonstrate that the proposals made by Venezuela were incompatible with the requirement of ‘just’ compensation as required under the BIT and that, therefore, an unlawful expropriation did not occur.

In Tidewater v. Venezuela, the tribunal engaged in a similar analysis. After noting that the claimants agreed that their investment was expropriated for a public purpose, it analysed whether such expropriation was lawful or unlawful.\(^\text{16}\) The tribunal recalled a number of cases

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\(^{12}\) ibid., page 55.

\(^{13}\) ibid., pages 63–65.


\(^{15}\) Mobil Cerro Negro v. Venezuela, para. 301.

\(^{16}\) Tidewater Inc., Tidewater Investment SRL, Tidewater Caribe CA et al v. The Bolivarian Republic of Venezuela, Award of 13 March 2015, ICSID Case No. ARB/10/5, Tribunal: C McLachlan (President), A R Sureda.
and scholarly opinions that considered that an expropriation only requiring fair compensation was lawful, and found that in the given case the expropriation represented a ‘provisionally lawful expropriation’ until the determination of compensation due in accordance with the BIT.\textsuperscript{17} The tribunal also rejected the claimants’ argument that the expropriatory decree limiting the compensation due to investors to the book value of the investment was contrary to the standard of ‘market value’ under the BIT.\textsuperscript{18}

However, in \textit{Rusoro Mining v. Venezuela}, the mere offer by the state to provide compensation limited to the net worth of the expropriated companies and unsuccessful negotiations for six consecutive months were found to be insufficient to comply with the terms of the BIT.\textsuperscript{19} As part of its analysis, the tribunal found that although Venezuela made an offer to compensate Rusoro, this offer – which was even below the cap provided for in the Nationalization Decree – was found insufficient to render the expropriation lawful, especially where the amount offered was never paid or deposited.\textsuperscript{20}

Similarly, in \textit{Koch Minerals v. Venezuela}, the tribunal agreed in principle with the approach taken by the ICSID tribunal in \textit{Mobil Cerro Negro v. Venezuela} that the lack of paid compensation does not in itself render an expropriation unlawful. However, the tribunal noted that in the case before it Venezuela did not make ‘any meaningful offer of compensation’ or ‘any meaningful procedure for compensation’ that would satisfy the ‘effective and adequate compensation’ requirement of the BIT. The tribunal therefore considered the expropriation as unlawful.\textsuperscript{21}

As the cases above demonstrate, the offers or the circumstances under which the non-payment of compensation occurred still remain relevant for the distinction between lawful and unlawful expropriation. The timing of the offer and the length of negotiations may have an effect on the tribunals’ findings as to whether an expropriation is lawful. In each case, the tribunals tend to consider the facts and the specific wording used under the agreements as suggested in the \textit{Mobil Cerro Negro v. Venezuela} decision.

The distinction between lawful and unlawful expropriation in turn bears on the applicable standard of compensation. Scholars generally agree that it has been ‘rightly pointed...’

\textsuperscript{17} Tidewater v. Venezuela, paras. 141; 145–146.
\textsuperscript{18} Tidewater v. Venezuela, para. 145.
\textsuperscript{19} Rusoro Mining Limited v. Bolivarian Republic of Venezuela, Award of 22 August 2016, ICSID Case No. ARB(AF)/12/5, Tribunal: J Fernández-Armesto (President), F Orrego Vicuña, B Simma, para. 410.
\textsuperscript{20} Rusoro Mining v. Venezuela, para. 408.
\textsuperscript{21} Koch Minerals Sàrl and Koch Nitrogen International Sàrl v. Bolivarian Republic of Venezuela, Award of 30 October 2017, ICSID Case No. ARB/11/19, Tribunal: V V Veeder (President), M Lalonde, Z Douglas, paras. 7.28–7.29. See also Bear Creek Mining Corporation v. Republic of Peru, Award of 30 November 2017, ICSID Case No. ARB/14/21, Tribunal: K-H Böckstiegel (President), M C Pryles, P Sands, paras. 448–449, where the tribunal held that ‘Article 812.1 of the FTA provides that an expropriation, in order to be lawful, must be effected in a non-discriminatory manner and on prompt, adequate and effective compensation. It is undisputed that Supreme Decree 032 did not provide for any compensation to Claimant. Therefore, also for this reason, the Decree is a breach of the FTA... In view of its above considerations, the Tribunal concludes that Supreme Decree 032 constituted an unlawful indirect expropriation, in violation of Article 812.1 of the FTA.’
out that compensation of lawful and unlawful expropriation cannot be the same.\textsuperscript{22} Hence, the distinction between lawful and unlawful expropriation could be relevant for valuation purposes since the resulting compensation may be different.\textsuperscript{23}

Notably, most of the provisions and guidelines for awarding compensation under IIAs today deal with lawful expropriation and usually do not contain separate standards of compensation for unlawful expropriation.\textsuperscript{24} Thus, questions arise as to the differences that apply to the applicable standard of compensation with respect to unlawful expropriation.

On this topic, the decisions of tribunals relating to the applicable valuation standards diverge significantly.\textsuperscript{25} One often-cited decision in this respect is \textit{ADC v. Hungary}, where the tribunal emphasised the difference between lawful and unlawful expropriation and held that:

\begin{quote}
\textit{The BIT only stipulates the standard of compensation that is payable in the case of a lawful expropriation, and these cannot be used to determine the issue of damages payable in the case of an unlawful expropriation since this would be to conflate compensation for a lawful expropriation with damages for an unlawful expropriation.}\textsuperscript{26}
\end{quote}

The tribunal further noted that the BIT did not contain rules on the issue of the standard of compensation for an unlawful expropriation and stated that the default standard contained in customary international law would apply in this case.\textsuperscript{27} Accordingly, the tribunal applied the \textit{Chorzów Factory} standard to compensate the claimants.\textsuperscript{28}

\begin{thebibliography}{99}
\footnotesize
\item \textsuperscript{22} S Ripinsky and K Williams, page 65, referring to M Sornarajah, \textit{The International Law on Foreign Investment}; I Marboe, page 83.
\item \textsuperscript{23} I Marboe, ‘Valuation in Cases of Expropriation’ in M Bungenberg, J Griebel, H Hobe, and A Reinisch (eds), \textit{International Investment Law}, 2014, page 1062.
\item \textsuperscript{24} B Sabahi and N J Birch, \textit{Comparative Compensation for Expropriation}, 2010, page 763; S Ripinsky and K Williams, page 83.
\item \textsuperscript{25} S T Ratner classified the decisions in terms of remedies provided into four groups: Group 1 – Compensation based on Treaty Formula, Silence on the Lawful/Unlawful Distinction, Group 2 – Lawful/Unlawful Distinction Noted, but Damages the Same as a Legal Matter, Group 3 – Lawful/Unlawful Distinction Noted, but Treaty Formula Used Due to Special Facts and Group 4 – Lawful/Unlawful Distinction Noted, with an Effect on Damages. See S T Ratner, ‘Compensation for Expropriations in a World of Investment Treaties: Beyond the Lawful/Unlawful Distinction’, the American Society of International Law (2017), pages 15–17.
\item \textsuperscript{26} \textit{ADC Affiliate Limited and ADC & ADMC Management Limited v. The Republic of Hungary}, Award of 2 October 2006, ICSID Case No. ARB/03/16, Tribunal: N Kaplan (President), C N Brower, A J van den Berg, para. 481 (emphasis added).
\item \textsuperscript{27} \textit{ADC v. Hungary}, para. 483.
\item \textsuperscript{28} P Bienvenu and M J Valasek, \textit{Compensation for Unlawful Expropriation in ICCA Congress Series No.} 14, 2009, pages 250–252.
\end{thebibliography}

Other tribunals, such as in Rumeli Telekom v. Kazakhstan, Siag v. Egypt and Koch Minerals v. Venezuela, citing practical and other reasons, did not consider the relevance of the distinction between lawful and unlawful expropriation to be significant in terms of the applicable standard of compensation.

What is then the practical significance of the finding of unlawful expropriation to the investors? Ripinsky and Williams summarise the consequences of the unlawful qualification in three main points:

> in case of unlawful expropriation: 1) the primary remedy would be restitution, not compensation; 2) if the value of the expropriated property has increased between the date of the taking and the date of the arbitral decision, this increased value is to be awarded; 3) compensation may include incidental expenses or other consequential damages.

As seen from this enumeration, investors may benefit from the finding that an unlawful expropriation took place. Another potential benefit is that tribunals may award higher amounts as punitive or moral damages. Although international practice does not generally


34 Caratube International Oil Company LLP and Deiuncci Salah Hourani v. Republic of Kazakhstan, Award of 27 September 2017, ICSID Case No. ARB/13/13, Tribunal: L Lévy (President), I Aynès, J Salès, para. 1082 et seq.

35 Bear Creek v. Peru, paras. 448–449.


37 Rumeli Telekom AS and Telsim Mobil Telekomunikasyon Hizmetleri AS v. Republic of Kazakhstan, Award of 29 July 2008, ICSID Case No. ARB/05/16, Tribunal: B Hanotiau (President), S Boyd, M Lalonde, para. 793.

38 Waguih Elie George Siag and Clorinda Vecchi v. The Arab Republic of Egypt, Award of 1 June 2009, ICSID Case No. ARB/05/15, Tribunal: D A R Williams (President), M C Pryles, F Orrego Vicuña, para. 541.

39 Koch Minerais v. Venezuela, para. 9, 194.

40 S Ripinsky and K Williams, pages 86–87.

41 I Marboe, page 78. To date, only two tribunals have awarded moral damages – in Desert Line v. Yemen (Award of 2008) and Benvenuti & Bonfanti v. Congo (Award of 1980) – although more claimants have put forward moral damages as one of the claims. See further I Marboe, page 315 et seq.
recognise punitive damages, tribunals’ decisions awarding higher damages and lost profits in the case of unlawful expropriation have been considered to represent a deterrent effect against the unlawful conduct of states akin to punitive damages.

In summary, it appears that although there is a trend towards recognising the distinction between lawful and unlawful expropriation with respect to the financial consequences, case law still does not provide a clear guidance in terms of standard of compensation applied in the case of unlawful expropriation, especially as this applies to valuation standards and valuation dates used to award appropriate compensation.

ii Methods of compensation for unlawful expropriation

Most commonly, in cases of expropriation, arbitral tribunals are requested to award claimants the fair market value (FMV) of their investment as compensation. It has been noted that the FMV determines ‘how much the asset is worth, or would be worth on the market’. As the Crystallex tribunal recently observed:

> it is well-accepted that reparation should reflect the "fair market value" of the investment. Appraising the investment in accordance with the fair market value methodology indeed ensures that the consequences of the breach are wiped out and that the situation which would, in all probability, have existed if the wrongful acts had not been committed is reestablished.

Since compensation is but one form of reparation, the FMV standard would appear to be an appropriate standard for the measure of such compensation. However, a tribunal in another recent ICSID case observed that the FMV standard is only ‘sometimes applied . . . in case of unlawful expropriations’. Yet, in its 2012 study, the United Nations Conference on Trade and Development concluded that:

> While in theory, compensation for lawful expropriation should be different from reparation for an unlawful one, in many cases the two are determined by reference to the same fair market value of the expropriated investment.

While FMV is defined by multiple sources of secondary international law, it is often referred to in a significant number of IIAs and model BITs in the context of the expropriation clause.

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42 The tribunal in Siag v. Egypt explicitly rejected the claimants’ request for punitive damages. Siag v. Egypt, paras. 544–546; Bear Creek v. Peru, para. 657. See also Marboe, page 79.
43 See Bear Creek v. Peru, para. 596, stating that ‘damages for an unlawful expropriation should at least be as much as the compensation for a lawful expropriation.’
45 S Ripinsky and K Williams, page 188.
47 Caratube v. Kazakhstan, para. 1084 (emphasis added).
49 See, for example, the World Bank Guidelines on the Treatment of Foreign Direct Investment that indicate: ‘In the absence of a determination on agreed by, or based on the agreement of, the parties, the fair market value will be acceptable if determined by the State according to reasonable criteria related to the market.
For instance, Article 6 of the 2012 US Model BIT provides that ‘[t]he compensation . . . shall . . . be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place’. The 2004 Canadian Model BIT includes virtually the same language as its southern neighbour.  

To determine the FMV of an investment that was expropriated, several valuation methodologies are used. The most common method used by markets is the discounted cash flow (DCF) method that represents an income-based approach to valuation that ‘generates the value of an asset at a particular date by computing the present value of earnings the asset is likely to generate during its useful life’. The DCF method has been recognised in investment arbitration as an efficient and realistic valuation method for assessing the FMV.  

Although the DCF method ‘is considered to be theoretically the strongest’, given uncertainties involved, other valuation methods were accepted by tribunals in certain expropriation cases, such as the book value of a business or an asset, the replacement value, the comparative transactions method or the market-based approach. In other instances, the tribunals opted for an FMV based on the ‘amounts actually invested by Claimant’.

iii The valuation date

The valuation date plays a significant role in the valuation of an expropriated investment, principally because ‘[t]he value of an object changes constantly in the course of time.’ Numerous model BITs and IIAs specify the valuation date in their clauses dealing with expropriation, that is, typically selecting as the valuation date the date on which the expropriation occurred or ‘the date before the impending expropriation became public

value of the investment, i.e., in an amount that a willing buyer would normally pay to a willing seller after taking into account the nature of the investment, the circumstances in which it would operate in the future and its specific characteristics, including the period in which it has been in existence, the proportion of tangible assets in the total investment and other relevant factors pertinent to the specific circumstances of each case.’ See also the International Glossary of Business Valuation Terms (National Association of Certified Valuators and Analysts) that defines Fair Market Value as follows: ‘the price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts.’

50 See Article 6 of the US Model BIT (2012); Article 13 of the Canadian Model BIT (2004).
51 S Ripinsky and K Williams, pages 195–196.
52 W Peter, ‘Compensation and Damages – What is different in Investment Arbitration?’ in: ASA Special Series No. 34, May 2010, page 193. See also S Ripinsky and K Williams, page 201, noting that investment tribunals are generally cautious in using the DCF method.
53 S Ripinsky and K Williams, page 193.
55 In the Crystallex award the tribunal used the ‘stock market approach’, in which the tribunal’s wording ‘reflects the market’s assessment of the present value of future profits, discounted for all publicly known or knowable risks (including gold prices, contract extensions, management, country risk, etc.) without the need to make additional assumptions’. (para. 890).
56 See, for instance, Bear Creek v. Peru, para. 604. For further examples, see I Marboe, pages 290–294.
57 I Marboe, page 129.
knowledge, whichever is earlier’. In the two cases mentioned above where the tribunals held that the expropriation was lawful, the ‘recovery was limited to fair market value of the asset at the moment of dispossession’.\textsuperscript{59}

The practice is more nuanced and less straightforward when the expropriation is deemed unlawful, as the tribunals have more leeway to depart from provisions of the relevant BIT. In particular, the tribunals dealing with unlawful expropriation ‘have been increasingly confronted with the issue of increases in value of property after an expropriation’.\textsuperscript{60} For instance, in two such cases against Venezuela and one against Hungary,\textsuperscript{61} the tribunals considered that the valuation date must be the date of the award. Similarly, the \textit{Yakos v. Russia} tribunal held that ‘in the event of an illegal expropriation an investor is entitled to choose between a valuation as of the expropriation date and as of the date of the award’ and decided that the date of the award was appropriate as it yielded a higher value.\textsuperscript{62}

In creeping expropriation cases, where a series of expropriatory measures are found to constitute a ‘taking’, establishing the time of the expropriation and, subsequently, the valuation date, becomes less obvious.\textsuperscript{63} Marboe observes that the tribunals have taken different approaches in setting the valuation date, with one tribunal deciding that the first action or omission that led to the breach is determinant, with another tribunal making a discretionary choice for a date that it considered ‘fair and reasonable’, and several tribunals relying ‘on the last date of the actions which in their totality amounted to an indirect expropriation’.\textsuperscript{64}

\textbf{iv} \quad \textbf{The risk of double counting in function of the approach favoured by the tribunal}

When dealing with DCF and compensation for lost profits, the tribunals run the risk of awarding a double compensation. This situation can be the result of the wrongful application of the distinction between the concepts of \textit{damnum emergens} (invested capital) and \textit{lucrum cessans} (lost profits).\textsuperscript{65} The double counting problem appears where the DCF method is used by the tribunal to compensate the investor for lost profits only (and in addition to \textit{damnum emergens}), because ‘a DCF calculation does not simply measure lost profits, but includes by

\textsuperscript{58} S Ripinsky and K Williams, pages 243–244. See also the US and Canada model BITs, which mandate that the valuation date is ‘immediately before the expropriation took place’. See also \textit{UP and C.D Holding Internationale v. Hungary}, para. 560.
\textsuperscript{59} M W Friedman, F Lavaud, page 99 referring to \textit{Tidewater v. Venezuela} and \textit{Mobil Cerro Negro v. Venezuela}.
\textsuperscript{60} I Marboe, page 137.
\textsuperscript{61} \textit{ADC v. Hungary}, paras. 496 and 499, where the tribunal observed that ‘the value of the investment after the date of expropriation . . . has risen very considerably’; \textit{Compañía de Aguas del Aconquija SA and Vivendi Universal SA v. The Argentine Republic}, ICSID Case No. ARB/97/3, Award of 20 August 2007 para. 8.3.19 where the date of the award appears to be considered the valuation date; \textit{ConocoPhillips v. Venezuela}, para. 343. See S Ripinsky and K Williams, page 245. See also I Marboe, pages 138–139, referring to \textit{Yakos v. Russia}.
\textsuperscript{62} See \textit{Hulley Enterprises Limited v. The Russian Federation}, Final Award of 18 July 2014, see note 32 above, paras. 1769 and 1777.
\textsuperscript{63} S Ripinsky and K Williams, page 246.
\textsuperscript{64} I Marboe, pages 144–146, referring to \textit{Alpha Projektholding v. Ukraine}, \textit{Unglaube v. Costa Rica} and \textit{Rumeli Télékom v. Kazakhstan}.
\textsuperscript{65} W Peter, page 199.
definition both lost profits and the recovery of the investment value.' To avoid the double counting, Marboe suggests that ‘international investment tribunals should either award amounts that represent the investment undertaken or compensate for the lost future income.'

v Proving past profits to demand lost future profits

Another common issue in FMV-based valuations and those based on DCF is whether past profits have to be demonstrated to be able to claim lost profits for the future. Generally, all investment tribunals would usually expect a track record of profitability or at least reasonable assurances of profitability in the future on the basis of all circumstances, such as concession fees, royalties and stabilisation clauses. The commentary to ILC Article 36(2), which provides that ‘[t]he compensation shall cover any financially assessable damage including loss of profits insofar as it is established,’ notes the following:

In cases where lost future profits have been awarded, it has been where an anticipated income stream has attained sufficient attributes to be considered a legally protected interest of sufficient certainty to be compensable. This has normally been achieved by virtue of contractual arrangements or, in some cases, a well-established history of dealings.

The above comments target a notion of predictability since compensation of lost profits involves an element of future damages, which becomes the governing principle and allows for award of lost profits even in the absence of past profitability.

IV CONCLUSION

As a brief review of the most recent ITA jurisprudence demonstrates, differences continue to exist as to the applicable standard for compensation for expropriation. Often, this is driven by the particular facts of a case, and no one measure or method can cover all of the possible factual scenarios. However, on the issue of compensation for unlawful expropriation, all parties would benefit from more clarity and consistency in the ITA jurisprudence and model IIAs. One would hope that such a standard might soon evolve with increased scrutiny of IIAs and the decision-making process within arbitral tribunals.

66 ibid. See also the Yukos v. Russia Awards, see note 32 above, paras. 1790 and 1791, which granted claimants two sets of damages in addition to interest: (1) Compensation for the value of Yukos as of the valuation date; and (2) the loss of dividends that would otherwise have been paid to [claimants] as Yukos shareholders. As the respondent pointed out in the subsequent challenge proceeding (see the writ of summons filed by respondent in the Dutch court proceedings against one of the Yukos claimants, Veteran Petroleum, as translated on: www.italaw.com/sites/default/files/case-documents/italaw4158_0.pdf, last accessed on 26 February 2018), this appears to have involved at least a partial double counting of the value of the compensation due, since the value of the shares of Yukos calculated under the first head of damages – even if done based on the comparable companies method – would have included at least some measure of the anticipated dividend payments due to shareholders.

67 I Marboe, page 108.

68 ILC Articles, commentary 27 to Article 36.

69 I Marboe, page 112, see also Crystallex v. Venezuela, para. 868.
Chapter 21

PRINCIPLES OF DAMAGES FOR VIOLATIONS OTHER THAN EXPROPRIATION

Ruxandra Ciupagea and Boaz Moselle

I INTRODUCTION

In another chapter of this book, ‘Compensation for Expropriation’, Konstantin Christie, Esra Ogut and Rodica Turtoi discuss the issue of compensation for expropriation from a legal perspective. This chapter is complementary in both subject matter and approach. We proceed from the perspective of economists who do not claim to make legal judgments, and we address the assessment of damages in treaty violations other than expropriation.

We focus on four key questions that, in our experience, arise in most disputes that require the assessment of damages, albeit with differing weights depending on specific circumstances:

a What are the fundamental standards for assessing damages?
b What is the date at which damages should be assessed (the date of assessment)?
c How should estimates of losses incurred at dates before or after the date of assessment be brought forwards or backwards to the date of assessment?
d What interest should be applied to bring the damages estimate forwards from the date of assessment to the date of the award?

This chapter will address each of the four questions in turn. Our discussion is certainly not exhaustive. In any specific matter a quantum expert will need to undertake further inquiry, guided where necessary by instruction on relevant matters of fact and law, to identify and correctly apply the relevant principles.

i Standards for assessing damages

The choice of standard for assessing damages is a question of law. To our understanding and in our experience, the relevant standard for assessing damages arising from investment treaty violations is usually that of ‘full reparation’. In the frequently cited Chorzow case, the Permanent Court of International Justice stated that ‘reparation must, as far as possible, wipe out all consequences of the illegal act and reestablish the situation which would, in all probability have existed if that act had not been committed.’

The full reparation standard gives rise to a number of questions. One issue is the application of the requirement to compensate for ‘all consequences’, which can give rise to

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1 Ruxandra Ciupagea is a vice president and Boaz Moselle is an executive vice president at Compass Lexecon.
2 We only address issues of financial damages (as opposed to, for example, restitution in kind).
3 As a general matter, these questions are equally relevant to both expropriation and other investment treaty violations (and indeed to damages in commercial disputes).
4 Case concerning the Factory at Chorzow (Merits), PCIJ, Series A, No. 17, 1928, p. 47.
debate as to the level of certainty required before a tribunal will find it appropriate to include certain heads of damages. Here, expert evidence may be relevant to help the tribunal assess the level of certainty, although the question of what level of uncertainty or ‘remoteness’ disqualifies a claimed consequence from meriting compensation is, again, one of law.

A second issue arises from what ‘the situation which would, in all probability have existed if that act had not been committed’ refers to. It begs the question of what date should be considered in making this determination. Is it to restore the situation that would have existed at the date of the treaty violation (the date of violation), at the date of award or at some other point in time?

From the perspective of financial damages, full reparation requires awarding the damaged party with a sum of money that leaves them in the same financial position as if there had been no violation. To estimate the damages required to effect full reparation, quantum experts generally adopt a methodology that, as a first step, maps out two scenarios:

a. The ‘actual’ scenario, which represents the circumstances since the violation occurred. The actual scenario often extends beyond the time at which the expert is performing his or her analysis, and may therefore require forecasting of future events.

b. The ‘but-for’ or ‘counterfactual’ scenario, which represents what would have happened in the absence of the violation. The but-for scenario also often extends into the future, and may therefore require both ‘back-casting’ and forecasting of what past and future outcomes would have been. In some circumstances, there may be significant uncertainty as to what those outcomes would have been, and experts address that uncertainty in various ways that we do not discuss in this chapter.

Thus, we may informally define damages as the sum of money that would make the investor indifferent between the actual scenario (defined to include receipt of that sum of money at the relevant date, the choice of date being an issue that we discuss in subsection ii) and the but-for scenario. In other words, damages be defined as the sum of money that would place the investor in the same financial position in the actual scenario as it would have held in the but-for scenario.

Having carried out this first step, a number of different approaches are possible, including:

a. estimating the value of the investor’s assets as at the date of assessment in both the but-for and the actual scenarios. Damages as at the date of assessment are then given by the difference between these two numbers. For example, if the investor has an asset that would have been worth US$200 million absent the violation, but instead is worth US$150 million at that date, prima facie, the damages are US$50 million;

b. estimating the difference between the cash flows that the investor would have enjoyed in the two scenarios, and value that difference to estimate damages (using the method of discounted cash flows (DCF)). For example, if the violation deprived the investor of

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5 The definition leaves open the question of whether it is the specific investor, or a hypothetical ‘typical’ investor, who should be considered.

6 We do not touch on additional considerations that might give a different answer (notably the issue of mitigation).

7 In brief, DCF methodology entails forecasting cash flows over time, discounting so as to bring them all to a single date (usually, the chosen date of assessment, as discussed later in this chapter), and then summing. Discounting is performed through the use of a ‘discount rate’. For example, if the annual discount rate is 5 per cent then US$1 million to be received a year from now has a ‘present value’ of US$1 million divided...
annual cash flows of US$10 million for five years, damages are the value as at the date of assessment of the five years of annual US$10 million cash flows (the expert applies financial techniques to estimate a figure for this value).

These two approaches do not differ in terms of what is being measured. In both cases, the expert estimates damages as the difference between (1) the financial position in which the investor is actually in; and (2) the financial position that the investor would have been in but for the actions against which damages are claimed. However, from a practical and technical perspective they have some important differences. In particular, the second approach has the advantage that a person does not have to assess the value of the investor’s asset in the two scenarios, only the value of the difference in cash flows. Any elements of the cash flows that are the same across both scenarios are irrelevant and can be ignored.

In some cases, this is a great convenience. For example, in recent years, there have been many disputes arising from investments in renewable generation in various EU Member States. The ‘typical’ picture is that an investor builds renewable generation assets (e.g., solar PV or wind energy generation) under a mechanism whereby it would obtain revenue over many years from ‘support payments’ from the public authorities, as well as from the sale of electricity. At some point, the authorities lower the level of those support payments, and investors claim that those changes are in violation of applicable treaty obligations. To assess damages in this case following the first approach, the assets would have to be valued, and their value at a particular date might depend on a number of uncertain factors such as the expected future level of costs, the expected future level of market prices for electricity and the expected technical life of the plant. However, the impact of the alleged violation is much more certain: it involves the removal of a certain stream of support payments, whose level and longevity was clear.8

This is one important difference between estimating damages in the context of expropriation relative to other violations. In cases of expropriation, the investor’s interest in the expropriated asset is typically valued, rather than comparing but-for and actual scenarios, and the option of looking only at the difference in cash flows therefore does not exist (formally, it might be said that it exists because cash flows can be compared in the but-for scenario with cash flows of zero in the actual scenario, but in practice that amounts to saying that the asset is only valued in the but-for scenario).

To value an asset under the first approach, experts typically rely on some combination of the DCF methodology and (depending on the availability of appropriate comparators) certain benchmarking techniques. For example, a company can be valued at a given date by finding a group of comparable companies and estimating the average ratio of enterprise value to earnings before tax, interest, depreciation and amortisation (EBITDA) for those companies. That ‘multiple’, applied to the company’s EBITDA, gives an estimate of its enterprise value. Only the DCF approach is discussed in this chapter.

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8 The total level of support payments would typically depend on annual plant output, and is therefore not 100 per cent certain. In our experience, however, reliable forecasts exist.
Date of assessment

The standard of full reparation requires compensation so as to ‘reestablish the situation which would, in all probability have existed if that act had not been committed’, but does not identify the date at which the situation should be re-established (i.e., the date of assessment). We consider two possible approaches to the choice of date:

a. The ‘ex post’ approach: estimate the sum of money ‘US$X’ such that if the investor is given that sum on the date of the award, it will be in the same financial position as it would have been had the violation not occurred. The date of assessment is therefore the date of the award. Under the ex post approach, information available as at the date of award is used, not information that only becomes available later.9

b. The ‘ex ante’ approach: estimate the sum of money ‘US$Y’ such that if the investor had been given US$Y at the time the treaty violation occurred, it would have been in the same financial position as if the violation had not occurred. The date of assessment is therefore the date of violation, and therefore information available as at the date of violation is used, and no further. That sum of money is brought forward to the date of the award (as discussed later in this chapter).

Although the question posed by ex ante versus ex post may sound theoretical, it can be of the greatest practical importance. In the Yukos dispute, the tribunal set the date of the treaty violation at 19 December 2004, and estimated damages at that date of US$22 billion, compared with a figure of US$67 billion at the date of award (i.e., 30 June 2014).10 The choice of date of assessment therefore made a difference (before interest) of approximately US$45 billion.11 The main driver of the difference was that oil prices as at December 2004 were much lower than in June 2014 (and that the oil price would increase so much after December 2004 was not known as at that date).

We consider the choice between the ex ante and ex post approaches to be fundamentally a question of law.12,13 However, understanding the economic consequences of each approach may be relevant to the choice.

First, the ex ante approach can in some circumstances provide damages even if with the benefit of hindsight the violation did not lead to actual harm. Thus, suppose that an investor is deprived of the ability to make an investment that at the date of violation was expected to be very profitable. For example, the investment was in oil and gas production at a time when prices were forecasted to remain high for many years. Suppose subsequently the oil price fell

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9 At least that is the theory: in practice, the latest date that is practical is used, since it is not possible to finalise calculations on the day the award is given.
10 PCA Case No. AA 227 Yukos Universal Ltd (Isle of Man) v. Russian Federation, Final Award, 18 July 2014, paras 1819 and 1825.
11 ibid., 1763–1769. The tribunal in that dispute determined that whichever date gave the higher value award should be used.
12 It is not uncommon for investment treaties to specify a standard for compensation in the case of expropriation. For example, Article 13(1) of the Energy Charter Treaty stipulates that ‘[s]uch compensation shall amount to the fair market value of the Investment expropriated at the time immediately before the Expropriation or impending Expropriation became known in such a way as to affect the value of the Investment’.
13 Some economists have, however, opined on the subject. An example is the article of Franklin M. Fisher and R. Craig Romaine, ‘Janis Joplin’s Yearbook and the Theory of Damages’, *Journal of Accounting, Auditing and Finance* (1990).
and remained low, such that the investment would have turned out to be loss-making (the profits from sales would not have been sufficient to cover the original expense of developing the field).

More generally, the *ex ante* approach can give rise to damages that are very different from what was actually incurred. Consider a variant of the example above, where the expected value of the investment at the date of violation was US$500 million, but owing to the fall in oil prices it turned out with hindsight to be worth just US$100 million. Under the *ex ante* approach, the investor will receive damages of US$500 million (plus interest), a figure that is considerably higher than what is required to leave them in the same position, as at the date of award, as if the violation had never happened.

However, the *ex post* approach can also give rise to outcomes that may appear unintuitive. Suppose that an investor was going to engage in oil and gas exploration in two separate areas, but that it was improperly deprived of those opportunities for two different reasons, each of which was a separate violation of an applicable investment treaty. Suppose that another company instead undertook exploration in the first area, spent US$200 million but found nothing; and in the second area, where it found reserves, undertook production, and made a profit of US$200 million. If the investor could establish that the deprivation of the opportunity with regard to the second area was a treaty violation, it could receive damages of US$200 million, even though the combined effect of both violations was to leave the investor no better or worse off.14

### iii Estimating damages as at the date of assessment

Damages can be determined on the basis of the additional cash flows that would have accrued to the investor absent the treaty violation. Under the *ex ante* approach, these additional flows necessarily occur in the future (i.e., on or after the date of assessment) because under this approach the date at which the violation occurred is used as the date of assessment, and all consequences of the violation must therefore arise at or after that date. These consequences are future losses.15

To determine the value of future losses as at the date of assessment, one cannot simply focus on the nominal value of these additional cash flows as they would accrue to the investor at the relevant times. For example, if the investor would have had an additional US$10 million in cash flows two years after the date of assessment, one cannot affirm that the investor’s damages as at the date of assessment in respect of these additional cash flows equals US$10 million. The principle of full reparation requires one to find a sum of money as at the date of assessment that is equivalent, from an investor’s perspective, to receiving those cash flows at their actual dates.

Holding all else equal, future cash flows are generally worth less than cash at the present time (owing to the ‘time value of money’). In addition, future cash flows are often uncertain

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14 This relates to the point in Fisher and Romaine, ibid., that it is not possible to seek negative damages. That is, the first of the two violations in this example saved the investor US$200 million, the second one cost it US$200 million: the investor can seek damages of US$200 million for the second violation, but the state cannot seek an award of negative damages (i.e., it cannot ask to be awarded US$200 million) in relation to the first violation. This is less likely to be an issue with the *ex ante* approach, since a state is unlikely to engage in a treaty violation that creates positive value, as of the date of violation, for an investor.

15 Here, the ‘future’ is relative to the date of assessment; and also the consequences may include both losses and gains, so that the stream of ‘losses’ over time may be a mix of positive and negative amounts.
and, therefore, holding all else equal, are worth less than risk-free cash flows. Therefore, future cash flows must be discounted to account for both the passage of time and any additional risk associated with these cash flows.

Applying the DCF methodology under either the *ex ante* or the *ex post* approaches, therefore, generally requires the application of a discount rate to future cash flows. However, under the *ex post* approach the date of assessment is later than the date of violation, typically by some years, and the losses suffered therefore occur in the past as well as in the future. Regarding past or ‘historical’ losses, it is clear that had the investor had the money corresponding to these additional cash flows at the time, it could have made certain use of this money that would have likely generated additional cash flows. Examples of this include: using the money to reduce its existing debt or avoid raising future debt, investing the money in its own business or alternative projects, or simply holding the money in interest-bearing deposits. In describing the but-for scenario, what those uses would have been must be stated.

In our view, the required approach is conceptually clear: the most realistic possible assessment must be attempted of what would have happened as of the date of assessment but for the violation (in essence, this follows from the meaning of date of assessment). However, that leaves potentially challenging practical questions as to how to estimate what the resulting cash flows would have been. Regarding the latter, though it is often easy to determine the correct return on this money assuming that it is held in interest-bearing deposits (or even that the investor uses it to reduce or avoid debt), it is not so straightforward to do so if it its considered that the investor might have used the money to invest in alternative projects (and for some reason was not able to raise money to do so from other sources). The same issue can arise in the context of pre-award interest, and we discuss it in more detail under that rubric.

**Determining the discount rate**

The DCF methodology determines the value of future additional cash flows as of the date of assessment based on the principles discussed above. DCF is very widely used in practice, and is often viewed as the ‘gold standard’ for valuation (in the absence of direct market evidence). Typically, the most material question that arises during arbitration proceedings – which gives rise to the highest number of discussions among experts (apart from estimating the cash flows themselves) – is not related to the use of DCF in itself but to what is the correct discount rate to apply to the specific streams of cash flows in question.

Future cash flows should be discounted for two reasons. First, to compensate purely for the passage of time (ignoring any risks associated with future cash flows); economic theory and evidence indicate that there is a material cost to waiting to receive money, even absent any associated risks. Second, to compensate investors for the risk associated with these cash flows; economic theory and evidence also indicate that there is a material cost to bearing risk: human beings are naturally ‘risk averse’ and require larger rewards to invest in a more risky venture.

A key point in this regard, that unfortunately is frequently misunderstood (by quantum experts as well as lawyers), is that it is the riskiness of the incremental cash flows that must be assessed. This can be very different from the riskiness of the investor’s other assets. For

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16 Albeit, there may be some discussion as to issues such as whether the behaviour of a typical investor or the actual investor is assumed.
17 Because *inter alia* human beings may die while waiting and because they tend to become wealthier as time goes by, and the marginal value of money, and consumption falls as one becomes wealthier.
example, suppose that an investor invests in a certain business, whose costs and revenues are uncertain and potentially risky. Suppose, however, that one part of those future revenues comprises ‘support payments’ from a public authority, and that those payments are very certain, until the government changes policy so as to abolish those payments (the example of support payments for investments in renewable generation comes to mind, depending on the specific circumstances of the case). If the government’s actions are found to be a violation of an investment treaty that merits compensation, the compensation will be for the loss of the (previously) certain cash flows arising from the support payments, and the discount rate will be appropriate to that stream of income, which may, for example, be comparable in its level of risk to the payments a person would receive as a holder of government bonds. This discount rate can be significantly lower than the discount rate that would be applied to the cash flows of the whole asset (the project’s ‘cost of capital’). In the example of renewable generation, the latter rate may reflect risks related to construction and the future market price of electricity, etc., that are simply irrelevant to the cash flows that have been lost as a result of the alleged violation.

The discount rate, therefore, can be viewed as the sum of two components: a ‘risk-free rate’ plus a ‘risk premium’. With respect to the first component, experts usually agree on the use of a risk-free rate determined by the yield on highly secure government bonds, such as US or German bonds (since it is considered that the probability of default on these bonds is negligible in this context).18

Greater disagreement usually arises when experts try to determine the second component. As a starting point, experts usually rely on the capital asset pricing model (CAPM), a fundamental ‘workhorse’ of finance theory.19 The CAPM posits that investors hold a wide portfolio of assets, and the risk associated with any individual investment may therefore be hedged through diversification. However, some risks apply to many different assets and are therefore not removed through diversification. The CAPM seeks to use market data to measure the extent to which the relevant asset or cash flows is subject to these non-diversifiable risks, and estimate the appropriate return to reward investors for bearing them.

Beyond the CAPM, factors such as the location of the investment or the currency in which additional cash flows would accrue to the investor are commonly considered by experts (usually referred to as country risk and currency risk premium). The intuition behind this is that investments placed in a country with, for example, an unstable political environment are worth less, holding all else equal, than investments in a stable economy. Similarly, investments that pay off in currencies from unstable environments are worth less than, for example, investments that pay off in dollars or euros.

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18 We do not touch here on the issue of ‘real versus nominal’ returns, and the risks associated with inflation (in our experience, this is rarely a major issue in practice), or on various complexities around estimating the appropriate risk-free rate in practice.

19 The CAPM is described in any corporate finance textbook (e.g., Brealey, Myers & Allen, op cit).
II PRE-AWARD INTEREST

Finally, once a tribunal finds in the favour of the investor, the respondent owes the investor a certain amount in the size of the damages award. The respondent owes the investor this amount from the date of assessment until the moment when the investor is finally compensated, namely the moment when the respondent pays the investor the full amount of the damages award.

It is conventional to distinguish between (1) interest to cover the period between the date of assessment and the date of award (pre-award interest); and (2) interest to cover the period between the date of award and the date when any damages are actually paid (post-award interest). Our comments here focus on pre-award interest, although most of what is said will apply equally to post-award interest.

Pre-award interest only arises if the date of award is later than the date of assessment. Under the *ex post* approach, therefore, there is in principle no issue of determining pre-award interest. However, this distinction is a formal one since under the *ex post* approach the issue of historical damages must be dealt with—here, our discussion will focus on the *ex ante* approach.

Different pre-award interest rates can have a very significant impact on damages awards. As an example, suppose that damages as at the date of assessment are US$100 million, and the date of the award is 10 years later. Adding on pre-award interest at 3 per cent per annum would give an award of US$134 million, while at 6 per cent per annum the figure would be US$179 million and at 9 per cent it would be US$237 million (in the last case the interest would be greater than the pre-interest damages).

From a legal perspective, a number of factors may determine or influence the choice of a pre-award interest rate. For the specific case of investment treaty arbitration, different bilateral investment treaties (BITs) give rise to different principles for the determination of pre-award interest rates. For example, the BIT between the Netherlands and Egypt defines just compensation as including ‘interest at a normal commercial rate until the date of payment’ (without further specification of the meaning of a ‘normal’ commercial rate). The BIT between Georgia and Kazakhstan specifies that compensation for expropriation should include ‘interest at the London Inter-Bank Offered Rate (LIBOR)’.

From an economic perspective, however, the appropriate choice of interest rate follows from the requirement for full reparation. Again, different interpretations are possible (and the choice between them is a matter of law). One of those is the following. In the case of the *ex ante* approach, to be in the same financial position, the investor must in fact be indifferent between the but-for scenario and the actual scenario, where it understands that as at the date of award it will receive US$Y plus pre-award interest determined according to a specified methodology.

The question therefore arises of what that methodology should be. One approach is to consider what the investor would have done with the US$Y, had it been given that money as of the date of assessment, and then to identify the equivalent interest rate to be applied to the US$Y.

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20 In practice, there will necessarily be some time lapse between the date of assessment and the date of award, and some amount of pre-award interest is therefore required.


Different options can be considered for the investor’s hypothetical alternative use:

\( a \) If the investor had debt (or was going to incur debt after the date of assessment), it could have used some or all of these sums to reduce existing debt, or avoid falling into new debt. In that case, the pre-award interest relating to these funds corresponds to the rate on the debt that the investor could or would have avoided – most likely, its most expensive debt (or if where the investor was going to incur debt after the date of assessment, the rate at which it would be able to secure this new financing).

\( b \) If the investor did not have (and would not have incurred) debt, the investor would have either kept the money in interest-bearing deposits at the commercial deposit rates in place at the time, or it would have found an alternative use for the money, such as investing it in alternative projects.

\( c \) With respect to alternative uses, the investor could either have invested the money in its own business or into any alternative investment.

A second approach is to consider that the damages award amount represents a loan from the investor to the respondent (the ‘coerced loan theory’). In that case, the pre-award interest rate applied would correspond to the respondent’s borrowing rate, which is usually determined by several factors (the respondent’s credit risk or location, or the currency of the damages award). In sum, in this case the pre-award interest should reflect not only the time value of money, but also the default risk of the respondent.

Correctly estimating the pre-award interest rate can be more or less complex depending on which of the approaches above is used. Determining the investor’s or respondent’s borrowing rate is often simpler than identifying potential alternative investments for the investor (and the corresponding rates of return).

The ‘correct’ approach among the ones listed above is likely a matter of law, and may also depend on the level of proof an investor is able to provide to the arbitral tribunal. However, if a principle based upon the investor’s alternative use of the damages amount is applied, the investor would have chosen the alternative use that would have maximised its financial position and, if employing the money for a new investment, would have made the investor better off than reducing its debt.

The issue with the above is that it is often difficult to assess what this alternative investment may have been, or what rate of return the investor would have obtained from it. Moreover, for both new investments or investments in the investor’s own business, the rate of return usually demanded by the investor reflects, *inter alia*, the investor’s expectations regarding the risk associated with this investment: in simple words and as explained above, the more risky an investment is perceived to be, the higher the rate of return the investor would require. However, when being deprived of the money for a certain period (and compensated for it afterward), the future risk associated with this presumed investment is fully removed, since the investor did not actually have the opportunity to invest in this opportunity. Therefore, it would no longer make sense to compensate the investor for this risk.

The key subtlety is to identify not only the expected return from what the investor would have done, but also the level of risk it would have incurred. An investor would normally accept a lower rate of interest on the US$Y, if it is given for certain, than the expected return on a risky investment. Identifying the specific risk associated with the investment that has been removed (and the corresponding reduction in the required rate of return) is often a very complex task.
Chapter 22

THE DISCOUNTED CASH FLOW
METHOD OF VALUING DAMAGES
IN ARBITRATION

Jeff D Makholm and Laura T W Olive

I

INTRODUCTION

The discounted cash flow (DCF) model is a widely used and effective method for valuing enterprises. As such, it is useful for assessing damages associated with enterprise lost profits in international arbitration. The strengths of the DCF model relate to its straightforward simplicity, the way in which it embraces the income and growth prospects for an enterprise, and the way it incorporates the market’s assessment of investment risk in any part of the world. Particularly for cases involving infrastructure assets, such as regulated enterprises or those supporting competitive energy or transportation markets, the DCF model is popular among tribunals as an objective method that focuses on the essential underlying elements that spur such arbitrations – the interruption of stable, going-concern profitability.

Being so computationally straightforward, a paradox in the use of the DCF model is that it was invented only comparatively recently. Economist Myron Gordon sought to bring together economic theory and the long-standing rule-of-thumb practices of financial analysts of the late 1950s: what he called the ‘imprecise’ finance literature. He grounded those financial practices with a theoretical economic foundation. The resulting DCF model he described soon came to the attention of administrative regulatory agencies, courts and arbitral tribunals as a tractable tool for deriving enterprise value and the cost of capital when used with objective market, industry or enterprise data. Gordon’s success made him famous. The ‘Gordon growth model’ is part of all modern finance courses and textbooks.

II

THE DCF AMONG ITS PEERS FOR ENTERPRISE VALUATION

In cases where courts or arbitral tribunals must value an enterprise in a dispute, it is widely accepted that there are three available methods of doing so. The first looks to the cost of the enterprise’s assets. The second is based on the market value drawn from comparable companies or the arm’s-length sale of similar enterprises. The third charts the expected capitalised income from the enterprise as a going concern brought back to the present – of which, the DCF model is the principal method. All three have useful attributes under the right circumstances.

1 Jeff D Makholm is managing director and Laura T W Olive is senior consultant at NERA Economic Consulting.


3 Financial literature mentions other income-based approaches, such as the adjusted present value and capitalised cash flow, but they are simply variants of the basic DCF model. See Kantor, M., Valuation for...
The cost method

Valuation based on the cost of the assets involved – either recorded-book cost or replacement cost – has some direct applicability to regulated enterprises whose values may be built more or less directly on such costs. But the method is sharply limited when assessing the going-concern value of infrastructure assets that draw their value from unregulated markets. For infrastructure assets that provide services over time, the cost method has sharp practical limitations based on the way that capital costs are handled by accountants – principally, because of depreciation. There has always been an unresolved tension between economists’ and accountants’ views of such depreciation. To economists who must value enterprises, depreciation charges merely reflect an allocation of the costs for investment decisions already made. In other words, such depreciation charges:

> refer to an expenditure that has already taken place, and are merely a special method of writing history. Depreciation accounting enables the business firm to make several ledger entries, instead of one, when a capital expenditure occurs.4

As such, depreciation charges are only useful in determining the value of enterprises if future profitability is somehow a function of those depreciation charges – as is the case with regulated enterprises for which consumers’ prices are derived from investment costs, including accounting depreciation.5

ii The market value method

Valuations based on market prices depend on comparable companies or comparability in arm’s-length sales. As awards in court or before arbitral tribunals are designed to assess an objective value for an enterprise, a market price is generally only applicable to demonstratively similarly situated enterprises. This would be the case for a dispute related to land or housing where reasonable markets exist involving related transactions of sufficient numbers to create a usable sample of comparative transactions. But the nature of international arbitration often involves disputes with unique firms for which comparable transactions can be rare or non-existent either because of the site-specific nature of the investments or the unique nature of the international market in question.

Economists have long studied whether the technologies inherent in particular businesses permit reasonable comparisons for regulation, damage assessment or the evaluation of organisational efficiency.6 Literature points to the problems inherent in making comparisons across enterprises in the private sector. Market comparisons between private enterprises are sharply limited in situations where input choice or ‘environmental factors’ (a broad category, including differing countries, institutional environments and industrial histories) cannot be controlled. Any direct comparison of sales prices among enterprises assumes that they all can

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attain the same level of production given their factor endowment – that is, that they belong to what economists would call the same ‘production function’. Although this assumption may hold for some public sector enterprises (such as public schools) or for particular private sector applications (such as the ubiquitous Starbucks coffee shops), it does not generally hold for the types of assets involved in international arbitration.7

iii The income capitalisation method

The inherent difficulties associated with cost or market prices is a principal reason why the income approach represented by the DCF method is so evidently popular among tribunals. To be sure, the DCF method also draws the cost of capital specific to the type of enterprise in question from market benchmarks, and its location in the world from the competitive capital markets. Nevertheless, the principal innovation of the DCF method is how it uses that market information to tie finance and enterprise valuation to a reliable underlying economic theory.

III ORIGIN OF THE DISCOUNTED CASH FLOW MODEL

In an era of intense interest and research into stock valuation models and methods, and highly sophisticated markets in financial instruments, it is useful to reflect briefly on the comparatively backward nature of the field of business valuation in the 1950s. When it came to valuing business enterprises at that time, there was no intersection between the practical rules of thumb developed by stock analysts or insurance actuaries and neoclassical theoretical economics.

Gordon wished to fill that gap. In 1962, he published, in book form, his theoretical work on the value of corporations, reflecting his published research in the late 1950s.8 His book constituted both a deconstruction of economists’ various theories of investing and a straightforward presentation of a new method of valuing business enterprises. Prior to Gordon, economists had only highly abstract theoretical models of firm investment flowing from Keynesian theories of income determination. They had to rely on ‘business practices’ to investigate problems of investment and financing. Gordon offered something better: a theoretical foundation for explaining the value of a corporation that could, in turn, be used to find the cost of capital without resorting to ad hoc business methods.

The economic theories of the era embodied the assumptions that the future is certain and the firm can borrow freely at a given rate of interest.9 When trying to bring uncertainty into their theoretical analyses, economists became irretrievably bogged down in particular complicated cases that did little more than provide ‘a very able statement of the generalization found in the unprecise literature of finance’, as Gordon wrote.10

Gordon sought a cogent tie between neoclassical economic theory and the generally accepted notions that a firm’s value is a function of its investment. As he wrote:

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under neoclassical theory, the objective of the firm is to maximize its value, the value is a function of its future income, and the future income is a function of its investment. The task of the theory is to provide information on the nature of these two functions.11

As is often the case in economics, advances in theory are often less like Darwin’s ‘gradualism’ and more like the late evolutionary biologist Stephen J Gould’s ‘punctuated equilibrium’ – with episodic evolutionary leaps. Gordon’s theoretical discovery was such a leap, taking one page of not-too-difficult mathematics to tie maximising value to future income and to future investment. The result was the first statement of the DCF model in economic literature:12

Equation 1

\[ P_0 = \frac{(1 – b)Y_0}{k – rb} \]

Where:
- \( P_0 \) = price of a share of common stock;
- \( b \) = the fraction of income retained in future period (i.e., not paid out as dividends);
- \( Y_0 \) = income per share;
- \( k \) = required return on investment; and
- \( r \) = expected return on investment.

Gordon recognised that for his theory to be of any practical use, it had to have some means for establishing \( k \), an enterprise’s cost of capital. Using his model to solve for the cost of capital using discrete time periods gives the following:

Equation 2

\[ k_e = \frac{D_0 \times (1+g)}{P_0} + g \]

Where:
- \( g = (r \times b) \), expected dividend growth rate;
- \( P_0 \) = price of stock;
- \( D_0 = (1 – b)Y_0 \), previous dividend paid; and
- \( k_e \) = cost of equity.

Here, the rate of profit investors require on a share of stock is equal to the dividend yield at which it is selling (the first term on the right hand side of the equation) plus the rate of growth in the dividend (the second term).

11 Gordon, 1962, p. 43.
12 Gordon cited Gordon, M., and Shapiro, E., ‘Capital Equipment Analysis: The Required Rate of Profit,’ Management Science, Volume 3, Issue 1, 1956, as the first appearance of the continuous time theory. Gordon noted that other writers claimed the equation reflected a standard actuarial formula. He also noted that those formulae had no economic content and did not deal with the future values of \( b \) and, particularly, \( r \).
IV WHY THE DCF METHOD WORKS

As outlined by Gordon when he first presented the theory, the key theoretical advance of the DCF model was that it did not presume that investors knew more than they could reasonably know. They had only broad notions of how investment conditions would change in future years. The DCF model worked because it simplified the future by not overstating the kind of information that investors use to make decisions in the market. Specifically, the values of \( r \) and \( b \) (the expected return on investment and the retention rate) are not dated – Gordon assumed them to be constant. Without such an assumption, any investment model would quickly become empirically unmanageable, which was the very problem that had vexed those earlier economists trying to link economic theory with finance. But, as Gordon correctly observed, investors rarely have any clear notion of how these variables change over time. And in any event, without specific information to the contrary it is reasonable to conclude that retention ratios and expected returns are stable for going concerns. Established corporations commonly follow a policy of paying a stable fraction of their earnings as dividends \((b)\). Investors will also only, at best, have a broad idea as to any future change in the expected return on investments \((r)\). With such an assumption, the value of a share of stock is merely a function of the current dividend and the rate of growth of those dividends (which is a product of \( b \times r \)).

Equation 1 can be written out to include the whole future income stream discounted by a constant expected cost of capital, \( k_e \), as follows:

\[
P_0 = \frac{D_1}{(1+k_e)} + \frac{D_2}{(1+k_e)^2} + \ldots + \frac{D_n}{(1+k_e)^n} + \ldots
\]

Alternatively:

\[
P_0 = \frac{D_0(1+g)}{(1+k_e)} + \frac{D_0(1+g)^2}{(1+k_e)^2} + \ldots + \frac{D_0(1+g)^n}{(1+k_e)^n} + \ldots
\]

This is the form of the DCF model (for which Equation 1 is merely a mathematically reduced form) that populates the values supporting damages estimates before arbitral tribunals. This DCF model values a share of stock according to a discounted stream of future dividends growing at a constant rate, \( g \). Although the basic Gordon model uses dividends to compute a share value, dividend payments are not necessary for such an analysis – cash flow or earnings can be used instead as these are more reflective of the value that investors place in the future profitability of the enterprise. That assumption of a constant growth rate can be changed if data on near-term expected growth differs from long-term growth. For example, corporate business plans may specify near-term income growth, \( g \), reflecting particular business conditions known by management – after which, a long-term growth rate deals with future years.
V THE STRENGTH OF THE DCF MODEL IN INDUSTRIAL AND INSTITUTIONAL SETTINGS

The attraction of this theory for administrative agencies and arbitral tribunals soon revealed itself. Gordon himself describes how he was retained in 1966 to provide evidence before the US Federal Communications Commission (FCC) on the cost of capital of AT&T. The FCC appreciated the straightforward simplicity of such a theoretical model that rendered AT&T’s cost of capital as the sum of a measurable dividend yield and a growth rate. The agency was highly complementary regarding Gordon’s analysis, structuring its findings to be consistent with it, and encouraging further study of the DCF model. As a result of that first application to regulated enterprises, the DCF model has dominated tariff proceedings in the United States and Canada to find the cost of capital for regulated firms.

Used to derive the price of a share of stock, $P_0$, as in Equation 4, the DCF model has become the principal ‘income-based’ method for valuation. In this form, the model has wide-ranging applicability in many contexts. It is useful to assess the loss of a business in its entirety and lost profits within an ongoing concern. It is also useful for both measuring direct damages (e.g., for the loss a productive asset) and indirect damages (e.g., flowing from changes in risk – affecting return – or prospective growth rates). Essentially, the DCF model is a framework within which to apply financial and operating information, from both the enterprise in question and from the surrounding markets (including capital markets). The accounting and operational data used to populate the model in any setting depends on what is available and, if none is readily available, the obvious alternative is to use the shortest and most objective path to developing useful proxies. This work is conceptually straightforward but, often enough, complex and subject to dispute in such settings as international arbitration.

The DCF model has specific applicability to industries characterised by the dedication of capital to certain sorts of going concerns relating to regulated or competitive markets – those industries where the assumptions of constant retention ratios and growth rates work well. Such businesses include regulated utilities, and oil and gas companies with capital facilities that support competitive markets (such as liquefied natural gas terminals, refineries, port facilities or airports) where long-lived infrastructure investments, in specific locations with specific supply and demand conditions and risks, require a valuation method that takes into account a long-term payoff for unique arrangements of assets.

VI MODERN PERMUTATIONS OF THE DCF METHOD

Gordon gave an economic foundation to the ‘imprecise’ financial literature and the reasonably effective rules of thumb of financial analysts of the 1950s. But Gordon was not the only economist looking for a theory by which to value corporations in the 1950s. His contemporaries, Franco Modigliani and Merton Miller were looking for the same thing.
Their model, called the Capital Asset Pricing Model (CAPM) first appeared in 1958.\textsuperscript{15} 
CAPM looks at the behaviour of stock prices in the market at large – not simply prospective earnings – to judge what investors require as the return on equity investments. It began to appear before administrative agencies (in North America and elsewhere) in the late 1970s and early 1980s.\textsuperscript{16}

Both methods propelled an explosion of scholarly literature on how practically to value businesses using each.\textsuperscript{17} This literature displays endless permutations, adjustments and increasingly thin slivers of time (with fractional exponents) to derive ever-finer special cases of the DCF model. To a certain extent, the complexity evident in this literature tends to obscure the essential nature of what Gordon provided – the method by which, with limited information in the capital market, capital cost and expected earnings from an enterprise relate to each other in an uncertain world. Mathematical models may be sliced in endless ways. But genuinely objective information, in the market, to drive the DCF model – reflecting what investors expect for the market’s growth rate – is rare. More complicated modelling does not make this information any less rare.

VII THE CENTRAL ROLE OF THE GROWTH RATE

Gordon’s DCF model uses enterprise value and future income as two sides of a coin: either side can face up. Equation 1 shows the enterprise value on top with the income capitalised at the growth rate ($r \times b$) underneath. Equation 2 has the cost of capital on top, with the additive terms of dividend plus the growth rate underneath. Either way, the growth rate is on the bottom of the coin, operating unseen. The DCF model rests on that unseen growth rate – it either permits observed income to translate into value, or it permits an observed dividend yield to translate into the cost of capital (which is how Gordon himself used it in finding the regulated cost of equity for AT&amp;T). Where is that growth rate from?

In the capital markets that tie the top and the bottom of the DCF coin together, the growth rate is in the mind of the investors: they price the shares in question based on the way the capital markets reflect their collective expectations. The growth rate in the DCF model exists in the world – the problem is to find it in a sufficiently objective way to be credible before judges or tribunals.

The long-standing depth of the US capital market provides many sources by which to gauge investors’ growth expectations. The accuracy of these analyses, in the sense of whether they are predictive of the future, is not the issue. The crux of the matter is whether they reflect widely held expectations. In recent years, the availability of sources of financial analysis has expanded to include the following, widely considered objective and credible.

\begin{itemize}
  \item \textit{Annual Valuation Handbook – US Industry Cost of Capital, Duff & Phelps}
\end{itemize}

Duff & Phelps, founded in 1932 in Chicago as an investment research firm, took over the widely respected publication of Roger G Ibbotson and Rex A Sinquefield, begun in 1977 (with stock, bond and inflation data reaching back to 1926), in 2014. Duff & Phelps uses

\begin{footnotesize}
\begin{itemize}
  \item \textsuperscript{16} Phillips, Charles F., \textit{The Regulation of Public Utilities}, Public Utilities Reports (Arlington, VA), 1993, pp. 396-397.
\end{itemize}
\end{footnotesize}
data from Standard & Poor’s and Barclays to develop annual industry statistics, including return on equity, CAPM betas, enterprise valuation multiples and long-term earnings per share growth projections.\(^{18}\)

**ii Institutional Brokers Estimate System (I/B/E/S), Refinitiv**

Refinitiv, a new company built from the Financial & Risk business of Thomson Reuters, publishes I/B/E/S, which compiles estimates from 18,000 analysts pertaining to companies in more than 90 countries. Established in 1976, available metrics include traditional financial indicators and I/B/E/S Key Performance Indicators that vary by industry.\(^{19}\)

**iii NYU Stern School of Business, Aswath Damodaran**

Aswath Damodaran, professor and holder of the Kerschner Family Chair in Finance Education at the NYU Stern School of Business, publishes several useful current and historical data sets on his website. Professor Damodaran annually updates industry averages for US and global companies on corporate finance and valuation metrics, including return, capital structure, dividend yield, capital expenditures and depreciation, multiples and growth rates. He also provides data on country risk premiums and corporate tax rates. He uses various published sources of data.\(^{20}\)

**iv Value Line**

Founded in 1931, Value Line is one of the oldest and largest independent, subscription-funded investment research services. Value Line employs independent analysts to assess various financial metrics such as individual company growth anticipated from new products, overall financial health and three-to-five year projections.\(^{21}\)

**v Zacks Investment Research**

Founded in 1978, Zacks uses mathematical models combined with industry analyst research to estimate earnings growth of particular companies and industries. Analysts provide commentary and quantitative research to provide expectations for stock prices, fund performance, other financial metrics.\(^{22}\)

**vi Final thoughts**

The DCF model does not presume that investors are omniscient with perfect knowledge of the future. Similarly, those who employ the DCF model do not have perfect knowledge – but they do have the ability to draw objective, disinterested assessments, from sources such as those above.

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20  http://pages.stern.nyu.edu/~adamodar/.
VIII CONCLUSION

There have been a number of recent assessments of the DCF model available to the audiences of legal practitioners in the field of international arbitration. Some look closely at the accounting inputs needed for the model, and others on the particular facts of the model’s use in specific cases. Although such reviews are useful, they do not reflect what, to economists, is the ultimate underlying attraction of the model among the various methods of deriving value. That ultimate attraction is that the DCF model links together finance and economic theory in an uncertain world in a highly effective way. Far from being unduly abstract or restrictive as a model of investment behaviour, the DCF model has a demonstrated track record among administrative agencies, courts and arbitral tribunals. The method reasonably ties market expectations with measurable features of current markets, yet makes no aggressive claims about what is known about future business conditions. Its underlying economic assumptions strengthen the DCF model’s use by international tribunals for whom objectivity is of paramount importance.

Chapter 23

OTHER METHODS FOR VALUING LOST PROFITS

Gervase MacGregor and Andrew Maclay

I INTRODUCTION

In this chapter, we set out the basic principles of a loss-of-profits calculation, together with some of the specific issues that commonly arise and need to be considered by the quantum expert, the lawyers and the arbitration panel. We do not consider damages in the context of an expropriation or damages calculated on the discounted cash flow basis, as these commonly used approaches are covered in other chapters.

Any damages claim needs to be calculated on the basis of the law that applies to the loss, and this may vary depending on the loss that is claimed or the jurisdiction that governs the claim; for example, some legal systems may not permit loss-of-profit or *lucrum cessans* claims at all. The basic starting point for the quantum expert is to put the claimant back into the position in which it would have been but for the intervening event that caused loss, whether that is a breach of contract, an expropriation, or a fire or flood. This means that a loss of profit is calculated as the difference between:

- the profit that would have been generated in the absence of the intervening event.
- the profit actually generated.

Quantum experts commonly refer to the profits the company would have generated as the 'but-for' or counterfactual scenario; and

The profit the company actually generated should be quite straightforward to calculate. However, calculating the profit in the but-for scenario may be rather more complicated, and may require a combination of legal analysis, accounting skill and industry knowledge, in terms of forecasting what would have happened if the contract had not been breached or what may happen in an uncertain future.

II THE LENGTH OF THE LOSS

A key issue is the length of time the damages last for, or for which one can claim. In practice, this may depend on the legal principles in the jurisdiction or the length set out in a business interruption insurance policy. But, theoretically, it is simply the length of time from the breach of contract or other event until the company is once again earning the profits it would have earned had the event not taken place. In the case of a supermarket that is closed for a certain number of weeks, it is reasonably clear that the loss lasts for the period of closure plus

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1 Gervase MacGregor is international head of advisory, risk and quality, and Andrew Maclay is a forensic services principal at BDO LLP.
a lesser loss for some weeks after it reopens while it is rebuilding its sales to the level it would normally have expected. In other cases, the breach may have caused a factory never to be able to operate at capacity, in which case the damages may continue in perpetuity.

III THE BASIC CALCULATION

While in theory one can calculate the overall loss of profit in the but-for scenario directly, in practice, it is usually easier to break the calculation down into its constituent parts, namely:

\[ \begin{align*}
\text{a} & \quad \text{loss of revenue}; \\
\text{b} & \quad \text{gross profit margin}; \\
\text{c} & \quad \text{variable overheads}; \text{ and} \\
\text{d} & \quad \text{fixed overheads}. \\
\end{align*} \]

We also find it helpful to carry out an overall reasonableness check on the loss calculated, by adding the loss to the actual profits earned, and comparing the resulting figure to the company's profits before and after the period of loss. It may be useful to illustrate this check on a graph, which may also bring the loss calculation to life for the arbitral tribunal. For example, such an overall reasonableness check may illustrate an error if the recalculated profit spikes up or down during the period of the loss.

IV CALCULATING THE LOSS OF REVENUE

The key driver of a loss-of-profit calculation tends to be the company's revenue. This is because the gross profit margin and the overhead costs generally vary less over time, and so are easier to calculate. The loss of revenue also tends to be the most tendentious parameter in the calculation because it may be subject to major fluctuations depending on whether the company wins a particular contract or not, and by its very nature it involves forecasting what would have happened in the future, which is simply unknown and speculative. At this point, it is worth emphasising that estimating what would have happened or forecasting the future is not an exact science, and the goal of the quantum expert is to calculate the most likely outcome, but without normally being able to say that that outcome is the only possible outcome.

For this reason, some arbitrators find it difficult to award damages for loss-of-profit claims. Equally, however, it is necessary for the quantum expert to work out the most reliable way of calculating what the revenue would have been absent the breach of contract or other intervening event. There are various ways of doing this, such as those detailed in the subsections below.

i Identified contracts lost

For a construction or engineering company, the most reliable way of calculating future revenue may be by identifying specific contracts that the company is likely to have won or identifying specific contracts that it did actually win, but that it would probably have won at an earlier date.

ii The company’s own forecast

If the company had its own forecast of the future profits it expected to make, this may be the best data to use to estimate what would have happened but for the breach. However,
before relying on a forecast, one needs to consider the purpose for which it was prepared, and how accurate it is likely to be. If the forecast was prepared for the company's bank, which had carried out due diligence and lent the claimant money based on this forecast, and if the company's actual results over the past five years had always been within 5 per cent of its forecasts, then one could feel reasonably confident in relying on the forecast. If, on the other hand, the company's forecast was limited to a single sheet of paper prepared by the directors after the breach of contract occurred, and it had never actually achieved its budget in the past, one would not feel confident in relying on the forecast without first making serious adjustments to it or discounting it for uncertainty.

### iii Extrapolating from the past to the future

Where a company has been operating for many years, and has a track record of always achieving a certain level of sales and profit, and where profits have grown consistently at, say, 5 per cent per year, the best estimate of future profits may be an extrapolation of past profits. This may be based on professional judgement or it may be based on a statistical regression line, which estimates the future based on the past.

### iv Comparison with what actually happened to a similar company or retail outlet

If one can find a similar company operating in the same field and show that the claimant's results have closely correlated with the results of that company in the past, the best way of estimating what would have happened may be to consider what actually happened to the comparator company in the same period. In circumstances where the loss of revenue is uncertain, it may be appropriate to calculate it by calculating the loss on a number of scenarios, and then applying a percentage likelihood to each scenario to calculate an overall estimate of the loss of revenue.

There are particular statistical tools that one can use in estimating the loss of revenue. These include:

- **Regression analysis**: this is a statistical tool that estimates unknown results based on historic data and relationships, and also generates an indication of the reliability of the projections. So, if a company has been growing over the previous five years, one might be able to take its revenues for the previous five years and project those into the future. Alternatively, one might be able to estimate the relationship between sales and the size of a supermarket, and use the trend of these to project the sales lost by a different supermarket store.

- **Seasonal adjustment**: if one is estimating the loss of profit for a short period of time, it may be important to consider the impact of seasonality on sales. So, for example, sales for a retailer may be much higher in the run up to Christmas, or sales by a heating company may be much higher in winter. In such circumstances, it will be necessary to adjust the damages calculation to take account of seasonality, for example, by using an adjustment factor calculated from previous Christmases or winters.

### V CALCULATING THE GROSS PROFIT PERCENTAGE

The reason for calculating the gross profit separately and after the revenue is that the gross profit of many companies tends to remain fairly constant over time. For example, a retailer may always reckon on marking up its purchases by 30 per cent, and it is common to find that companies' gross profit margins, as set out in their published financial statements, do not vary

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Other Methods for Valuing Lost Profits

greatly from year to year. Alternatively, if they do vary, this may be because of the breach of contract or interruption itself, and so a comparison of the gross profit margin over time may itself help to indicate the loss of profit.

For a company that is dependent on a small number of very large contracts, the profitability of which varies, one may instead need to base the estimated gross profit margin on the estimated gross profit margin in the company’s bid documents when it tendered for the contract.

Alternatively, for a natural resources company, the costs of extracting the minerals may be relatively fixed, but the revenue may fluctuate dramatically based on world prices; so the most reliable calculation of the loss of gross profit may be based on the quoted futures market price for the commodity less the cost of mining it. And, in a period of low commodity prices, if the selling price is lower than the cost of extraction, it may be that an interruption to a mine actually saves the mining company from losses that it might otherwise have incurred.

VI FIXED AND VARIABLE OVERHEADS

It is very important to understand the difference between fixed and variable costs in loss-of-profit claims and how to treat them, as this is an area where errors and misunderstandings frequently occur. It is important to understand the distinction between costs that a company does not incur during the period in which it suffers a loss of profits, and costs that continue in any event.

If costs continue irrespective of the interruption, then the company’s position would have been the same in the but-for scenario as in the actual scenario, so there is no basis for any claim for loss of these fixed costs in a loss-of-profits claim. Examples of fixed costs may be head office costs, which continue to be incurred irrespective of the closure of any factory or the loss of any particular contract, or rent that continues to be incurred even if a factory or supermarket is closed.

On the other hand, variable costs are costs that are directly linked to revenue, and so may be saved when the breach of contract occurs; such saved variable costs, thus, need to be deducted from the loss-of-profit claim. Examples of variable costs may be employee overtime, which is not incurred when the factory is closed, heating and lighting, or transport costs if no vehicles are used in the period of closure.

VII SUNK COSTS

A similar cost that causes confusion is sunk cost – for example, the cost of building a factory. If a factory is idle as a result of a breach of contract, it may be tempting to claim for the cost of building that factory as part of the loss-of-profit claim because the factory is not making anything or generating any income. However, to do so would be to double count the loss of profit; this is because the company cannot generate any profits at all or suffer any loss of profits if it has not incurred the cost of building a factory (i.e., the cost of building the factory would have been incurred in both the but-for and the actual scenarios).
VIII OTHER ISSUES THAT ARISE

i Overhead recovery rates and intra-group charges
An issue that often arises is the definition of what a cost exactly is. For example, the cost of employees may be measured as the amount actually paid to them (e.g., overtime, pension) divided by the number of hours they work, or as their hourly ‘charge-out rate’ (which may be equal to direct salary cost multiplied by a factor of three or four, to take account of the general and administrative, and other fixed cost overheads of the company) or the rate that is charged by a service company in the group.

Related to this is the impact of costs recharged between companies in the same group at a mark-up, sometimes to move profits around a group. Thus, where the company has been charged employee costs based on a mark-up over direct costs, it may be important to consider whether the variable costs that have been suffered as damages should be based on the costs charged to the company or the original lower costs actually suffered by another group company.

ii Management time
The principles here may vary between jurisdictions, but generally the rule is that one can only claim damages for lost management time if the claimant can demonstrate that this management time would otherwise have been spent on generating profits on other projects (i.e., it is an opportunity cost). This is because management time is a fixed cost that would have been incurred whether or not the event causing the loss had occurred.

iii Tax
If the goal of a damages award is to place the claimant in the same position as it would have been in if the relevant breach had not occurred, the damages calculation needs to take account of tax. Thus, both the actual and the but-for calculations need to be carried out on a post-tax basis. If the tax rates have changed considerably over time, or if damages awards are taxed on a different basis to income, or if dividends from a project would have been subject to withholding tax but a damages award is not, the impact of tax may be considerable. Consequently, care must be taken to make sure that tax has been treated consistently in the loss-of-profit calculation.

iv Currency
The choice of which currency a claim is made in may have a considerable impact on the size of the claim, particularly in developing economies or economies with hyperinflation. Again, legal principles may vary between jurisdictions, but the general principle is that the claimant should be compensated for what it has lost. Thus, the loss should generally be calculated in the currency in which the loss of profit has been suffered. A claimant generally also has a right to be compensated in a freely convertible currency – so, even if the damages are calculated in a local currency, the tribunal may translate the award into US dollars or euros at the rate of exchange on the date of the award.

v Discounting
If the loss of profits continues into the future, into a period after the date of the award, it will be necessary to discount the future losses back to the date of the award, to take account of risk and the time value of money. There may be different rates that could be used to discount
the claim, depending on the circumstances – the most common approach is to calculate the discount rate on the basis of the company’s weighted average cost of capital, which includes consideration of the risk suffered by the company, but if there is no risk premium needed, the appropriate discount rate may be the company’s borrowing rate or some other rate of interest.

IX CONCLUSION

Throughout this chapter, we have set out in detail the normal approach for calculating loss of profits in damages claims. However, we conclude by touching briefly on two very different methods that may be used to calculate damages.

i Loss-of-chance claims

The first method is the loss of a chance method. This method is commonly used in litigation in the United Kingdom, but is not so prevalent elsewhere. It is based on the principle that losses of profits are uncertain, and that it is up to the judge or arbitrator to assess the degree of uncertainty and to take this into account in awarding damages. Thus, the approach assesses the loss of profits on the assumption that the company would have been able to make the profits claimed – but then reduces the damages by a percentage to take account of the fact that in reality the company might not have made those profits as some other event might have impacted on its ability to generate the profits or simply that the calculation of loss of profits is by its very nature uncertain.

ii Wasted cost claims

Finally, although it is not really a method for calculating loss of profits, a method commonly used by tribunals in assessing damages, particularly in circumstances where the loss of profits is very uncertain or speculative, where the company has never in fact traded or generated any profits or where the future projections are unreliable, is for damages to be awarded on the basis of wasted costs.

This method compensates the claimant for the costs it has incurred, but from which it has not benefited, but does not award any additional damages to the claimant on the basis of its expected future profits. It is, thus, an alternative claim to a claim for loss of profits, rather than a claim in addition to a loss-of-profits claim; so, for example, a company may claim for the sunk costs of building a factory as a wasted costs claim as an alternative to a loss-of-profits claim, but not in addition to a loss-of-profits claim.
Chapter 24

CAUSATION

Chudozie Okongwu and Erin B McHugh

I  INTRODUCTION

Most investment treaty arbitrations involve a claim that a respondent state has breached its obligations under an investment treaty. A claimant’s recoverable damages are limited to those caused by the respondent state’s wrongful act (or acts). Establishing causation or a ‘causal link’ between the wrongful act and the harm claimed is thus a critical element in a damages determination.

In this chapter, Section II sets out the principles of causation as described in the International Law Commission Articles on State Responsibility (the ILC Articles). Section III discusses some arbitral awards that have dealt with certain key issues that have arisen in interpreting these principles of causation. Section IV describes how a statistical technique called ‘regression analysis’ can be used to help assess causation and addresses some of the questions raised in the awards discussed in Section III.

II  PRINCIPLES OF CAUSATION

The ILC Articles codify customary rules of international law concerning the responsibility of states for ‘internationally wrongful acts’. Article 2 states that ‘a breach of an international obligation of the State’ (such as an investment treaty) is considered an ‘internationally wrongful act’. Article 31 articulates the principle of causation in the context of assessing damages for such acts, stating:

1. The responsible State is under an obligation to make full reparation for the injury caused by the internationally wrongful act.
2. Injury includes any damage, whether material or moral, caused by the internationally wrongful act of a State.

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1 Chudozie Okongwu is a managing director and Erin B McHugh is an associate director at NERA Economic Consulting. The authors would like to thank Timothy McKenna, Robert Patton and Raphael Starr for their assistance in relation to this chapter.
2 Some treaties may provide a jurisdictional basis for arbitrating other types of disputes, such as contractual disputes arising from investment agreements. See Abby Cohen Smutny, ‘Principles Relating to Compensation in the Investment Treaty Context’, 19 September 2006, pp. 1–2.
4 Crawford, p. 201.
Thus, reparation is to be made only for the injury ‘caused by’ (i.e., ‘resulting from and ascribable to’) the wrongful act. Losses because of unforeseeable events or other concurrent factors may be excluded in the calculation of recompense.

Arbitral awards have clarified that establishing causation entails showing both ‘factual causation’ (also referred to as ‘cause in fact’) and ‘legal causation’. Factual causation is typically determined through an analysis of whether the injury would have occurred ‘but for’ the state’s wrongful act (i.e., in the ‘counterfactual’ or ‘but-for’ scenario). Economic tools can be used (as described in Section IV) to isolate the injury caused by the wrongful act from that caused by other factors (e.g., an economic downturn).

Even if an injury can be factually linked to a wrongful act, there may be legal limits on liability. Legal causation relates to whether the causal link between the wrongful act and the claimed injury is sufficiently proximate to require reparation. The commentary to Article 31 of the ILC Articles states:

> [C]ausality in fact is a necessary but not a sufficient condition for reparation. There is a further element, associated with the exclusion of injury that is too “remote” or “consequential” to be the subject of reparation. In some cases, the criterion of “directness” may be used, in others “foreseeability” or “proximity”.

Here, foreseeability concerns whether the state could have reasonably foreseen that its wrongful act would cause the claimed damages. The commentary to Article 31 explains that other factors may also be relevant in establishing legal causation. Moreover, the relevant criteria may differ from case to case depending upon the specifics of the breach.

### III DISCUSSION OF CAUSATION IN ARBITRAL AWARDS

#### i Biwater v. Tanzania: Factual causation

A frequently cited investment treaty arbitral award analysing issues of causation is that rendered by the ICSID tribunal in *Biwater v. Tanzania*. Biwater, a British water company, had invested in the water and sewerage system of Dar es Salaam and the surrounding area. Biwater claimed that actions by Tanzania constituted an expropriation of Biwater’s investment and unreasonable or discriminatory treatment in violation of the Tanzania–United Kingdom bilateral investment treaty (BIT).

In its award dated 24 July 2008, the tribunal analysed the issue of causation at length, finding that the claim failed on factual causation grounds. The award states:

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5 Crawford, p. 204.
7 Crawford, p. 204.
8 ibid.
9 *Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania*, ICSID Case No. ARB/05/22, Award, 24 July 2008.
There is little guidance as a matter of international law on the precise test of causation to be applied (there being a number of different possible formulations) . . . The key issue in this case is the factual link between the wrongful acts and the damage in question, as opposed to any issue as to remoteness or indirect loss.10

Although the tribunal considered the respondent’s actions to constitute an illegal expropriation, the tribunal was persuaded by the respondent’s expert that Biwater’s investment was of no economic value at the date of the expropriation because of serious problems already existing with its performance.11 Thus, the tribunal found that none of the respondent’s violations of the BIT “in fact caused the loss and damage in question, or broke the chain of causation that was already in place”.12

One of the arbitrators in the matter, Gary Born, disagreed with the conclusion by the other tribunal members (representing the majority) that the claim failed on causation grounds. In a ‘Concurring and Dissenting Opinion’ issued in connection with the award, Mr Born stated that it was clear that the respondent’s actions had caused injury to Biwater by ‘depriving it prematurely of the use and enjoyment of its property’.13 However, Biwater’s claim for monetary damages failed because the injury ‘had no quantifiable monetary value’.14 Mr Born considered the majority’s analysis to have confused issues of causation with the quantum of damages.

**ii Metalclad v. Mexico: Remoteness**

The 30 August 2000 award rendered by the tribunal in the *Metalclad v. Mexico* ICSID arbitration considered the issue of remoteness with respect to causation.15 Metalclad claimed that Mexico had interfered with its development and operation of a hazardous waste landfill (the La Pedrera development), thereby violating the investment provisions of the North American Free Trade Agreement.

Although the tribunal awarded Metalclad damages for its investment in the project, the tribunal disallowed an additional claim made by Metalclad on causation grounds. In particular, Metalclad had sought an additional US$20–25 million in damages for the alleged negative impact that the respondent’s conduct had on its other business operations by reference to the change in the company’s share price during the relevant period. The award states:

*The Tribunal disallows this additional claim because a variety of factors, not necessarily related to the La Padrera development, have affected Metalclad’s share price. The causal relationship between Mexico’s actions and the reduction in value of Metalclad’s other business operations are too remote and uncertain to support this claim. This element of damage is, therefore, left aside.*16

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10 Biwater v. Tanzania (Award), paras. 784–786.
11 ibid., paras. 792–797.
12 ibid., para. 798.
13 Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania, ICSID Case No. ARB/05/22, Concurring and Dissenting Opinion, 18 July 2008, para. 17.
14 Biwater v. Tanzania (Concurring and Dissenting Opinion), para. 21.
15 Metalclad Corporation v. The United Mexican States, ICSID Case No. ARB(AF)/97/1, Award, 30 August 2000.
16 Metalclad v. Mexico (Award), para. 115.
Hence, here the claim failed because the tribunal considered the causal link between the respondent’s actions and the claimed damages to be ‘too remote and uncertain’. Specifically, the claimants had failed to show that factors related to the La Padrera development, and not other factors, led to declines in Metalclad’s share price.

### iii Micula v. Romania: Sufficient certainty

The 11 December 2013 award in *Micula v. Romania* clarified the degree of certainty required to establish a causal link between an alleged wrongdoing and claimed damages.\(^{17}\) Claimants were Swedish nationals who claimed that they had made investments in several manufacturing companies in Romania in reliance upon certain economic incentives introduced by the state in 1998. These economic incentives were revoked in 2005 in the context of Romania’s accession to the European Union. The claimants alleged that the revocation caused damage to their investments and breached their rights under the Sweden–Romania BIT.

In addition to claims for actual or realised losses directly resulting from the revocation, claimants also advanced several claims for lost profits. The tribunal acknowledged in its award that lost profits must be established with ‘sufficient certainty’.\(^{18}\) The tribunal stated that ‘the sufficient certainty standard is usually quite difficult to meet in the absence of a going concern and a proven record of profitability’, but that these claims must be considered ‘on a case by case basis, in light of all the factual circumstances’.\(^{19}\)

The claimants’ first such claim was for lost profits on sales of finished goods. The claimants alleged that increased costs (resulting from the revocation) caused them to increase prices on finished goods and thereby lose market share and profits. The claimants’ expert employed the statistical technique of regression analysis (which will be described in the next section) to estimate the relationship between prices and market share for the relevant goods, and used the regression results to estimate a but-for market share had the price increases not been made. The claimants’ expert assumed that revocation of the economic incentives had caused claimants to increase prices, relying upon witness evidence as well as ‘the evidential pattern and timing of the price increase’.\(^{20}\)

The tribunal accepted the claimants’ arguments with respect to causation in the absence of ‘another, more plausible explanation’ for the price increase.\(^{21}\) The tribunal also found that the claimants had proved this claim with ‘sufficient certainty’.\(^{22}\) However, the tribunal rejected the claimants’ other claims for lost profits, as they related to new lines of business in which claimants never actually engaged (but purportedly would have entered but for the respondent’s wrongful acts).\(^{23}\)

### iv Conclusion

These decisions make clear that empirical evidence that supports or refutes an alleged causal link between a state’s actions and any claimed injury would be of assistance to an arbitral tribunal in reaching a fully informed decision. The claim in *Metalclad v. Mexico* failed because

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17 Ioan Micula et al v. Romania, ICSID Case No. ARB/05/20, Award, 11 December 2013.  
18 ibid., paras. 1006–1007.  
19 ibid., para. 1010.  
20 ibid., para. 1018.  
21 ibid., para. 1019.  
22 ibid., para. 1020.  
23 ibid., paras. 1041, 1065.
the claimants had not distinguished the effect of the wrongful act from other (concurrent) factors affecting the share price. Interestingly, in *Micula v. Romania*, the tribunal’s award stated that the presence of other concurrent factors contributing to the injury does not necessarily break the chain of causation from the state’s wrongful act. The tribunal considered that under the ILC Articles, a state is held responsible for all consequences ‘not being too remote’ of its conduct, unless there is contributory fault by the injured party or an identifiable element of injury can be allocated to the concurrent causes.\(^{24}\)

Economic tools can help to distinguish harm resulting from an alleged wrongful act from losses attributable to other factors. In the next section, we discuss one of these tools – regression analysis.

### IV THE USE OF REGRESSION ANALYSIS TO ASSESS CAUSATION

In the previous section, we discussed one arbitral award (*Micula v. Romania*) where a regression analysis was used by one of the experts (in concert with witness testimony and other evidence) to establish causation with respect to damages. To our minds, however, regression analysis remains an underutilised tool in investment treaty arbitration. For example, where there is a claim for lost profits, regression analysis can be used as a control for other factors affecting a company’s profits (e.g., economic conditions) to isolate any decline in profits attributable to an alleged wrongful act.

Regression analysis allows an economist to evaluate the relationship between a variable of interest (the dependent variable) and one or more other factors that may help explain movements in the variable of interest (these are referred to as explanatory or independent variables). This technique allows an economist to isolate the impact of a particular factor on the variable of interest, by controlling for other factors. The results of a regression model can shed light on whether the proposed explanatory variables meaningfully explain the observed variation in the dependent variable (i.e., whether the estimated ‘coefficients’\(^{25}\) on the explanatory variables are deemed ‘statistically significant’).\(^{26}\) Regression analysis also produces estimates with known rates of statistical error. This means, for example, that using regression analysis we may find that the probability that the observed change in a company’s profits results from chance alone (rather than as a result of the alleged wrongful act) is one in 20 (5 per cent) or less.\(^{27}\) If the regression results support the proposition that, after controlling for other relevant factors, there is very little chance that the observed decline in

\(^{24}\) ibid., paras. 925–926.

\(^{25}\) The estimated coefficients show the relationship between the dependent variable and the explanatory variables.

\(^{26}\) In broad terms, this is done by examining the covariance of the explanatory variable and the dependent variable, and determining whether the observed degree of covariance is unlikely to occur exclusively owing to chance (say, only 5 per cent of the time). Common standards used to deem something ‘unlikely’ include if an outcome has a probability of occurring of only 1 per cent (or less) or 5 per cent (or less). For details, see Federal Judicial Center, *Reference Manual on Scientific Evidence*, 3rd edition (Washington, DC: National Academies Press, 2011), pp. 249–253.

\(^{27}\) The assessment of the probability that an observed result is owing to chance is an inference from a statistical test. The typical framework for this test is to assume that a factor (in this case, the alleged wrongful act) has no impact on the variable of interest (in this case, profits). Under this assumption, one then computes the probability that the estimated size of the effect on profits could occur owing to chance. See Robert V. Hogg and Allen T. Craig, *Introduction to Mathematical Statistics*, 5th edition (Englewood Cliffs, NJ: Prentice Hall, 1995), pp. 280–287.
profits was attributable to anything other than the alleged wrongful act, these findings could provide powerful evidence of causation to an arbitral tribunal. However, the regression results may attribute some or all of the observed decline in profits to factors other than the alleged wrongful act – thereby providing evidence to refute a claimed causal link.

In this section, we present two hypothetical scenarios inspired by the types of disputes that can arise in the context of investment treaty arbitration. For each of these hypothetical scenarios, we discuss how regression analysis could be employed to assist the tribunal in limiting the losses under consideration to those caused by the alleged wrongful act or acts.

i Hypothetical scenario 1: Claimed lost profits owing to fair and equitable treatment violation

Consider the example of Global Construction Enterprises Ltd (GCE), a (fictional) privately held, UK-based construction firm. GCE builds commercial office space worldwide, but over 40 per cent of the firm’s profits come from its operations in the Republic of Freedonia.

On 1 April 2010, the Freedonian government announced a new construction-permitting policy that allegedly discriminated against non-Freedonian firms, breaching the fair and equitable treatment standard under the Freedonia–UK BIT. The allegedly discriminatory policy remained in place until the end of 2012, when it was rescinded. GCE is now pursuing compensation for lost profits from Freedonia under the BIT, asserting that the firm’s revenues and profits during the period from April 2010 to December 2012 would have been greater but for Freedonia’s allegedly discriminatory policy.

How one might establish causation will depend upon the available evidence. For instance, if there was clear evidence indicating specific projects for which GCE would have won contracts but for the new construction permitting policy, this would assist in establishing causation for losses associated with those projects. However, let us assume that here no such unambiguous evidence is available. GCE’s profits during the relevant period were affected not only by the allegedly discriminatory policy, but also by other factors. It is therefore necessary to isolate the impact of the state’s actions on GCE’s profits. Regression analysis lends itself to such an exercise.

An economist would consider the market forces that drive GCE’s business in Freedonia. Potential explanatory variables for GCE’s profits might include commercial mortgage interest rates, central bank rates, commercial real estate prices, overall construction activity and proxies for the overall business climate, such as GDP growth or business confidence.

To perform a regression analysis, one would collect data for each of these variables at regular intervals (for instance, on a monthly basis). One could then estimate a regression model using the data for these variables to explain GCE’s monthly profits (as the dependent variable).28 To estimate the impact of the alleged discriminatory policy, one could add a binary ‘indicator’ variable to the model specification. This indicator variable would take a value of one during the months where the allegedly discriminatory policy was in place – April 2010 to December 2012 – and zero in the other months.

In this model, the estimated coefficient for the indicator variable measures the average difference between GCE’s profits during the months where the allegedly discriminatory policy was in place and the months where it was not, controlling for the other factors that explain

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28 For ease of understanding, we explain the approach using profits as the dependent variable. In some cases, it may be more appropriate to estimate the model using revenues as the dependent variable. Cost assumptions would then be used to estimate the profit impact of the alleged wrongful act.
GCE’s profitability. If the estimated coefficient is negative and statistically significant, this could provide compelling evidence to an arbitral tribunal that the allegedly discriminatory policy caused a reduction in GCE’s profits. It could also form the basis for a damages estimate. This estimate would be limited to the injury caused by the alleged wrongful act, as the regression model controls for the other factors affecting GCE’s profitability.

ii Hypothetical scenario 2: Claimed discriminatory tax policy

Let us assume that PubliCo is a publicly traded manufacturing company operating in Freedonia. The majority owner of PubliCo is a UK-based holding company, HoldCo. In early 2015, Freedonia unexpectedly announced a substantial tax increase applicable to PubliCo, from 25 per cent to 50 per cent (the first tax increase). Six months later, Freedonia unexpectedly announced a second tax increase applicable to PubliCo, from 50 per cent to 75 per cent (the second tax increase). Both tax increases applied only to manufacturing companies whose majority owners were based outside Freedonia.

Let us further assume that PubliCo submits a request for arbitration claiming damages for discriminatory treatment under the UK–Freedonia BIT. Respondent Freedonia disputes causation with respect to PubliCo’s damages, claiming that other factors, such as a concurrent economic downturn, affected PubliCo’s profitability.

Although there are several methods that could potentially be used to assess damages in such a case, discussing all such methods is outside the scope of this chapter. We will focus on one method and its relevance to issues of causation – the application of regression analysis to perform an ‘event study’. The event study is a well-established empirical technique that is used to measure the market’s assessment of the impact of a specific event or announcement on a company’s market value – here, for example, the announcements of the two tax increases.

An event study is a particularly effective technique for assessing damages in cases where, as here, there is a discrete announcement or announcements of the alleged breaches. Because, as elaborated upon below, the price of a company’s shares reflects the present discounted value of the cash flows expected to accrue to shareholders, the event study can be thought of as the market’s assessment of the effect of the breach on discounted future cash flows. An advantage of the event study method is that it employs actual market data rather than potentially subjective assumptions. It can be used where the company in question has shares that are publicly listed and are traded in a liquid market.

It is particularly useful in the context of establishing causation as it allows one to isolate the impact (if any) of an alleged wrongful act from other factors influencing the company’s share price (e.g., market and industry-wide factors). Regression analysis is used to model the counterfactual scenario – namely, the predicted change in share price (share price ‘return’) but for the alleged wrongful act. Tests of statistical significance may allow one to conclude, for example, that there is only a 5 per cent chance or less that the observed share price movement is owing to chance alone (rather than resulting from the alleged wrongful act). An arbitral tribunal could arguably find such results compelling for the purposes of determining causation.

Recall that in the Metalclad v. Mexico award, the tribunal rejected a claim for damages where the claimants had not isolated the impact of the alleged wrongful act from other factors affecting the share price. It is possible, depending on the timing and nature of these factors, that an event study may have been able to assist in such an exercise.
The event study method is extensively used and has been applied in hundreds of articles in leading academic journals.\textsuperscript{30} It is also the most widely used method for proving and establishing loss causation and damages in US securities litigation.\textsuperscript{31} The method is premised on two assumptions: (1) that a company’s share price equals the market’s estimate of the present value of the cash flows expected to accrue to holders of those shares; and (2) that the company’s share price reflects all publicly available information and adjusts quickly to new information (i.e., semi-strong market efficiency).\textsuperscript{32} Market efficiency, like liquidity, is a continuum, with shares trading in more well-developed and liquid markets generally exhibiting a higher degree of market efficiency. An economist can perform tests of market efficiency to determine whether the event study method is applicable for a particular company’s shares, in a particular market and at a particular point in time.

Let us assume for present purposes that one has performed tests of market efficiency for PubliCo and has determined that the event study method is applicable. The steps involved in estimating damages using the event study method are described in the following subsections.

\textit{Prepare a detailed chronology of events and identify the relevant dates}

The first step is to prepare a detailed chronology of all news potentially affecting the company’s share price during the period of examination. This would include company-specific news, as well as news relating to the industry in which the company operates. The contents of the chronology might also be supplemented with fact witness testimony to the extent that this provides further context to events potentially affecting the company.

With regard to the first and second tax increases, it is necessary to determine the exact timing of the announcements (including whether they occurred before or after the market close for the day). Let us assume that PubliCo’s share price declined by 30 per cent following the announcement of the first tax increase and by 50 per cent following the announcement of the second tax increase. In the steps that follow, ‘excess’ share price returns (i.e., the returns after controlling for market and industry movements) associated with these announcements are estimated.

It is important to thoroughly examine the chronology on and around the relevant event dates to determine whether any other news released concurrently could have also affected the price of PubliCo’s shares. In the absence of any other factors that would affect PubliCo’s share price, one would assume that any statistically significant excess share price returns are attributable to the alleged wrongful acts.


\textsuperscript{31} See, for example, \textit{In re Imperial Credit Indus Inc. Sec. Litig.}, No. CV 98-8842 SVW, 2003 WL 1563084 (C.D. Cal.), which granted the defendants’ motion for summary judgment on all claims ‘because, after viewing the evidence in the light most favorable to Plaintiffs and with all reasonable inferences drawn in favor of Plaintiffs, there is no legally sufficient evidentiary basis for a reasonable jury to find for Plaintiffs as to the existence of loss causation and damages. Plaintiffs’ expert report on damages . . . is deficient for failure to provide an “event study” or “similar analysis”. Also see \textit{In re Executive Telecard Ltd. Sec. Litig.}, 979 F. Supp. 1021 (S.D.N.Y. 1997).

Estimate a market model
An economist would then estimate a regression model (market model) to determine the typical relationship between PubliCo’s share price movements and the movements of the market (as proxied by one or more indices: a market index, an industry index or an index of comparable companies). The regression model is ideally estimated over a ‘clean period’ that is unaffected by the alleged wrongful acts. Alternate model specifications might be examined to determine the one that best explains PubliCo’s share price movements. As described below, the market model is used as a control for market and industry movements to isolate the effect of the announcement being studied on share price.

Estimate predicted share price returns
For each event date (here, the first and second tax increases), an economist would need to decide upon the appropriate ‘event window’ for examination (i.e., the period over which one examines share price movements following the announcement). The event window typically begins immediately before the announcement (e.g., at the end of the previous trading day, if daily price data are used) and concludes within a few days following the announcement.

One would then estimate the predicted returns for PubliCo’s shares during each event window, using the market model. First, the returns over each event window of the indices chosen as explanatory variables for the purposes of estimating the market model are observed. To determine a predicted share price (i.e., the price that would be observed if the only factors affecting the price that day were those captured by the indices), those returns are then adjusted to reflect the typical relationship between the returns of the indices and the returns of PubliCo’s share price. For example, if the market return was -2.5 per cent on the day the first tax increase was announced, and the coefficient estimate was 2, then one would predict a return of -5 per cent (-2.5 per cent multiplied by 2) for PubliCo on that date.

Estimate excess share price returns on relevant dates and test for statistical significance
The next step is to compare the predicted returns with PubliCo’s actual returns in each event window, with the difference representing the abnormal or excess return. As noted above, absent any other company-specific news released concurrently that could have also affected the price of PubliCo’s shares, one assumes that any statistically significant excess return is attributable to the alleged wrongful act. This is because the event study procedure controls for price changes attributable to the factors affecting the broad market and the industry.

If there is only a small difference between the actual return and the predicted return in an event window (meaning that the excess return is close to zero), it is likely that the alleged wrongful act announced at that time did not affect the share price. The larger the excess return, the more likely it is that the alleged wrongful act affected the share price. Economists use standards of statistical significance to determine the threshold at which an excess return is

33 See Tabak and Dunbar, pp. 8–10 for further information on selecting the appropriate estimation window.
34 For example, an economist could review regression statistics such as the r-squared.
35 For further information on selecting the appropriate event window, see Tabak and Dunbar, pp. 7–8, and Dmitry Krivin, Robert Patton, Erica Rose, and David Tabak, ‘Determination of the Appropriate Event Window Length in Individual Stock Event Studies,’ NERA Working Paper, 4 November 2003.
36 For ease of understanding, we assume that the estimated value of the constant in the regression is zero for this calculation.
If the observed price movement is statistically significant, one can draw an inference that the alleged wrongful act caused the excess share price return.

For example, recall that PubliCo’s share price had a return of -30 per cent following the announcement of the first tax increase. Using the market model, a predicted return of -5 per cent was estimated on that date in the previous step. This would imply an excess return of -25 per cent (the difference between -30 per cent and -5 per cent). If this excess return were determined to be statistically significant, one could infer that this price movement was attributable to the announcement of the first tax increase.

Let us assume, however, that on the same date of the second tax increase there was another announcement by the company earlier in the day (e.g., that the earnings forecast would be revised downwards). This would be considered an example of confounding news or a concurrent event, in which case one would separate the effects of this announcement from the effects of the alleged wrongful act, where possible. There are techniques used to deal with such situations and the manner in which one might do so would depend upon the nature of the announcements and the available data.

Estimate aggregate damages

An economist would treat the two unanticipated tax increases spaced six months apart as separate disclosure events. For each tax increase, the change in share price implied by any statistically significant excess return would be estimated separately. By multiplying by the appropriate number of shares, one can then estimate the effect of each announcement on PubliCo’s market capitalisation.

These estimates can form the basis for a damages claim that isolates the impact of the announcements from that of other market and industry factors through use of the event study method. The event study method could be used alone, or to support the results of another method (e.g., a discounted cash flow method). However, if an economist found no statistically significant share price movement following either the first or the second tax increase, these results could potentially be used to dispute a claim for damages.

If PubliCo’s parent company HoldCo’s shares are publicly traded and trade in a liquid market, an economist could also analyse HoldCo’s share price movements following the announcements of the two tax increases. The efficacy of this approach would depend on various factors, including the proportion of HoldCo’s profits (or cash flows to equity) that PubliCo contributes.

As both of these examples show, the economic tool of regression analysis can be used to assess causation with respect to claimed damages. Regression analysis can isolate alleged injury resulting from an alleged wrongful act from that caused by other factors (i.e., to show that the causal link is not ‘too remote’). Moreover, because regression analysis relies upon empirical data, arbitral tribunals may find the results compelling for the purposes of establishing or refuting ‘sufficient certainty’.

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37 As noted above, testing for statistical significance involves determining whether the probability that the observed share price movement was owing to chance (rather than the alleged wrongful act) meets or is less than a pre-specified level (for example, 1 per cent or 5 per cent).

38 See Tabak and Dunbar, p. 11, for further information.
V CONCLUSION

Because of their usefulness in assessing issues of causation, we expect that in the future we will see the increasing use of economic and statistical tools in investment treaty arbitration. The reliance of these methods on empirical data – in contrast with potentially subjective opinion – and their ability to specify a known rate of error will provide arbitral tribunals with important information when considering issues of both factual and legal causation. Ultimately, these tools will allow both claimants and respondents to make a quantitative case for their positions with regard to causation. As one legal academic recently posited, ‘Close cooperation between lawyers and economists may lead to more rigorous causation analyses in future.’39 Our strong belief is that it will.

Chapter 25

CONTRIBUTORY FAULT,
MITIGATION AND OTHER
DEFENCES TO DAMAGES CLAIMS

Rasmus Josefsson

I INTRODUCTION

For the purposes of this brief review, a foreign investor is assumed to be, in principle, entitled to compensation in damages, resulting from a breach by a host state of its obligations relating to the protection of an investment (wrongfulness).\(^2\) The right to compensation arises under the applicable law, which is here taken to be ‘rules of international law’ as may be the case when the claims are based on the breach of a treaty, the parties have expressly or implicitly agreed that such rules shall apply, or when the arbitrators in some institutional arbitrations find that the application of rules of international law is most appropriate. What is said may also be of interest when national law applies to the dispute, but its application must be checked with reference to rules of international law; compare International Centre for Settlement of Investment Disputes (ICSID) Convention Article 42(1) and ICSID Additional Facility Rules (Arbitration) Article 54(1).\(^3\)

It is further assumed that the host state puts up a defence with a view to reduce the entitlement of the investor. Such defence may be that compensation should be denied or reduced because of contributory fault or failure to mitigate the loss. A defence may also be based on the doctrine of investment risk, the doctrine of necessity, the very fact that the respondent is an entity of a public nature or that the investor has conducted some form of corrupt act relating to the investment.

II REDUCTION OF DAMAGES OWING TO CONTRIBUTORY FAULT

Contributory fault is recognised within international law.\(^4\) The International Law Commission Articles of State Responsibility (the ILC Articles) Article 39 sets out: ‘In the determination

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2 Consequently, we will not discuss circumstances that may preclude wrongfulness such as consent, self-defence, countermeasures, force majeure and distress. See further, International Law Commission’s Articles of State Responsibility Chapter V. See hereto, A Newcombe and A Paradell, Law and Practice of Investment Treaties, 2009, page 510 et seq. We will, however, touch upon the doctrine of necessity in spite of the fact that necessity may preclude wrongfulness altogether.
of reparation, account shall be taken of the contribution to the injury by wilful or negligent action or omission of the injured State or any person or entity in relation to whom reparation is sought.\(^5\) Contributory fault has been successfully invoked by states in a number of disputes.

**MTD v. Chile**\(^6\) (an ICSID arbitration under the Chile–Malaysia bilateral investment treaty (BIT)) regarded a contract between MTD and Chile’s Foreign Investment Commission (FIC) for the development of a real estate project consisting of the construction of a self-sufficient satellite city. The project required the rezoning of the land by the Ministry of Housing and Urban Development. MTD had made its investment upon approval of the contract by the FIC, although the necessary rezoning had not yet been approved. As it turned out, MTD could not start the works and suffered economic loss. The arbitral tribunal found that Chile, by authorising an investment that could not take place for reasons of its urban policy, was in breach of the fair and equitable treatment standard defined in the BIT. The tribunal did, however, also find that MTD was in contributory fault, since it failed to adequately control that the project would receive necessary permits, or at least failed to structure the investment in such a way that the injury would be as small as possible if necessary permits were not granted. MTD was found not to have acted as a ‘wise investor’ and hence that it had contributed to its own misfortune.\(^7\) The arbitral tribunal found that MTD should bear 50 per cent of the damages it had suffered, but did not develop the reasoning behind the apportionment.

An ICSID annulment committee reviewed the award in 2007 after an application for annulment filed by Chile.\(^8\) In its decision, the committee *inter alia* emphasised the general difficulties in apportioning fault in investor–state disputes and also noted that contributory fault by an investor often leads to a fifty-fifty apportionment of the damages in international investment arbitrations. The committee stated that:

As is often the case with situations of comparative fault, the role of the two parties contributing to the loss was very different and only with difficulty commensurable, and the Tribunal had a corresponding margin of estimation. Furthermore, in an investment treaty claim where contribution is relevant, the respondent’s breach will normally be regulatory in character, whereas the claimant’s conduct will be different, a failure to safeguard its own interests rather than a breach of any duty owed to the host State. In such circumstances, it is not unusual for the loss to be shared equally. International tribunals which have reached this point have often not given any “exact explanation” of the calculations involved.\(^9\)

One way to rationalise the outcome would be to say that given the difficulties, an apportionment may end anywhere between the end points on a stick. The least arbitrary point on the stick is the middle point. So if none of the parties can convince the tribunal that another apportionment is more reasonable, the middle point will be chosen as it is the least arbitrary point of decision.

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\(^6\) *2 MTD Equity Sdn Bhd and MTD Chile SA v. Republic of Chile*, final award of 25 May 2004, ICSID Case No. ARB/01/7.

\(^7\) Paragraph 242.

\(^8\) Decision of 21 March 2007.

\(^9\) Paragraph 101.
The middle-point approach is not generally prevailing, however. In the ICSID arbitration *Occidental v. Ecuador*, the arbitral tribunal came to the conclusion (with a dissent) that the investors should bear 25 per cent of the loss. The award illustrates an upside-down application of contributory fault. The investor was in breach, but the state's reaction to the breach was disproportionate so that the investor became entitled to an apportioned compensation. Occidental had, in 1999, entered into a participation contract with Ecuador to explore and exploit hydrocarbons in a certain region of the country. Occidental later concluded an agreement with another investor to which a share of Occidental's hydrocarbon interest was transferred. This triggered Ecuador to terminate the participation contract and to resort to certain expropriation measures.

The arbitral tribunal found that Occidental's agreement with the other investor amounted to a breach of the participation contract as well as Ecuadorian law. The tribunal, however, also found that Ecuador's termination of the participation contract had not only been made in violation with Ecuadorian law, the BIT and customary international law, but also was a disproportionate response to Occidental's actions. The tribunal found that Ecuador had not suffered any quantifiable loss as a direct result of the other investor taking economic interest in the hydrocarbon exploitation. Since Ecuador's measures were disproportionate, Occidental was entitled to damages. However, as a party in breach, Occidental was found to have contributed to its own loss, which caused a 25 per cent reduction of the claimed damages by the tribunal.

*Occidental v. Ecuador* can be compared with *Genin et al v. Estonia*. The dispute concerned the cancellation by a state-owned bank of an operating licence held by a financial institution in which the claimants were shareholders. The reason for the cancellation was said to be financial uncertainties with the financial institution. The tribunal found that the bank had taken actions because of the behaviour of the investors comprising the non-disclosure of the true ownership of the financial institution. The behaviour of the investors was found to have caused the bank's cancellation of the operating licence, and was the sole cause for the alleged injury. The state's conduct, therefore, was not found to be in breach of the relevant BIT, and the investors' claim was therefore denied in its entirety.

More recently, the principle of contributory fault was applied in the consolidated arbitrations usually referred to as the *Yukos Awards*. The arbitrations concerned measures taken by Russia primarily between 2003 and 2007. The investors claimed that Russia

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10 *Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador*, final award of 5 October 2012, ICSID Case No. ARB/06/11. The award was partially annulled; decision of 2 November 2015.

11 One of the co-arbitrators (appointed by ICSID), Professor Brigitte Stern, found that the 'contribution of the Claimants to the damage has been overly underestimated [by the majority]'. Professor Stern moves on to compare the case at hand with the *MTD v. Chile* case and concludes that 'there the split 50/50 would have been even more justified [than in the *MTD* case], as the Claimants have acted imprudently and illegally.'


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had breached the Energy Charter Treaty (ECT) by failing to treat the investments in a fair, equitable and non-discriminatory manner. The investors further claimed that Russia unlawfully expropriated the investments.

The tribunal found that Russia’s measures had included forced sale of one of Yukos’ main oil production complexes, tax reassessments, harassment and more. Russia, however, as defence, invoked several instances of alleged misconduct by the investors, including skimming of profit, abuse of Russian corporate law, engagement in a tax optimisation scheme and obstruction of enforcement of tax claims.

The arbitral tribunal found that one of the invoked misconducts was to be seen as contributory fault by the investors according to Article 39 of the ILC Articles, namely the investors’ abuse of low-tax regions. The tribunal seemingly regarded this to be one of the underlying causes of events that followed (i.e., wrongful measures taken by Russia).

Because of this, the tribunal reduced the claimed damages by 25 per cent, without any detailed explanation of the basis for the apportionment, however. The tribunal acknowledged that it had a wide discretion to apportion responsibly, and that a 25 per cent reduction would best represent the parties’ shares of responsibility.

The most recent discussions regarding contributory fault in ICSID arbitrations can be found in the awards in Bear Creek Mining Corporation v. Republic of Peru\(^{14}\) and Burlington Resources v. Republic of Ecuador,\(^{15}\) both rendered in 2017. In both cases, one of the appointed arbitrators found that the compensation to the claimants should be reduced due to the contributory fault.\(^{16}\) The majority in both cases, however, found that the states failed to meet its burden to prove contributory fault and thus dismissed the state’s claims for liability of the investor. Since the principle of contributory fault was not \textit{de facto} applied by the tribunal, the cases will not be discussed further in this review.

### III REDUCTION OF DAMAGES OWING TO FAILURE TO MITIGATE LOSS

Reduction resulting from failure to mitigate loss refers to a situation where the injured party is, in principle, entitled to compensation, but fails to take ‘reasonable steps’ to reduce the loss.

Although it is widely recognised in civil law\(^{17}\) as well as in common law that failure to mitigate may lead to a reduction of the compensation, the standing and closer meaning of the principle as part of international law is not entirely clear. It finds its strongest manifestation in international contract law. A duty to mitigate is, for example, explicitly expressed in the UNIDROIT Principles of International Commercial Contracts (PICC) and in the Convention on the International Sale of Goods (CISG).\(^{18}\)

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\(^{14}\) Bear Creek Mining Corporation v. Republic of Peru, final award of 30 November 2017, ICSID Case No. ARB/14/21.

\(^{15}\) Burlington Resources Inc. v. Republic of Ecuador, final award of 7 February 2017, ICSID Case No. ARB/08/5.

\(^{16}\) See Professor Philippe Sands’ (QC) dissenting opinion to the Bear Creek Mining Award, para 39 and Professor Brigitte Stern’s dissenting opinion as regards contributory fault in footnote 1113 of the Burlington Resources Award. Professor Stern also served as co-arbitrator in the Occidental case discussed above where she also had a dissenting opinion as regards the issue of contributory fault, see note 11.

\(^{17}\) It should be noted, however, that the principle is not applied in all civil law jurisdictions. For example the principle is not recognized under French law, see Herfried Wöss, et. al., Damages in International Arbitration Under Complex Long-Term Contracts (2014), page 215.

\(^{18}\) See, for example, Article 7.4.8 in the PICC and Article 77 in the CISG.
Contributory Fault, Mitigation and Other Defences to Damages Claims

In the case concerning the Gabčíkovo-Nagymaros Project (Hungary v. Slovakia), a leading International Court of Justice case, the court established that although the principle of an injured party’s duty to mitigate is internationally recognised, it can only be invoked as a base for calculating damages. Thus, failure to mitigate can never materially justify a wrongful act. The court concluded that the duty to mitigate is not a legal obligation that itself entails responsibility, but rather that a failure to mitigate by the injured party precludes recovery to that extent.

In AIG v. Kazakhstan, the dispute arose after Kazakhstan’s expropriation of the investors’ investment in a joint-venture real estate development project. The state argued that the investors had failed to mitigate since they had declined an offer to develop on an alternative site instead of on the site that had been expropriated. The tribunal found that the investors were under no circumstances obligated to accept the alternative site, by law or by contract. Hence, the choice by the investors to decline the offer did not amount to a failure to mitigate. The tribunal stated that:

> When it comes to taking of the property of a foreign investor and to offers of “an alternative solution” more favourable to the host State, this Tribunal is of the view that once the host State decides to expropriate or to take measures tantamount to expropriation of property, it would be wrong in principle to impose on the injured party (the creditor or foreign investor) a “duty” to examine (and if reasonable, to accept) an alternative solution. Such an imposition would only encourage Governments to breach with impunity solemn provisions of an international treaty and weaken the protection of foreign investors – which such a treaty is expressly designed to safeguard.

IV INVESTMENT RISK

Investments are always subject to risk, meaning that the expected return on the investment may not materialise because of ordinary business risk. International investments are further exposed to an additional risk – country risk – which causes the investor to seek a higher rate of return. A portion of the country risk may be referred to as political risk. The country risk increases in proportion with the expected timescale of the investment. The doctrine of investment risk seeks to filter out losses resulting from commercial risk and some elements of the country risks, so that investment treaties do not work as an insurance against risks that the investor shall bear. Any part of the loss that results from impudence shall be eliminated from the compensation. In brief summary, it seems correct to say that when a loss is caused by a number of factors, the compensation shall be based only on the factors that are relevant to the purpose of the treaty.

Himapurna v. PLN illustrates one way to go about it. The arbitration took place under the UNCITRAL arbitration rules. The substantive law governing the energy sales contract under dispute was found to be Indonesian law. The parties had agreed, however, that the tribunal should not be bound by rules of law insofar as their application would

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19 ICJ GL 92, final award of 25 September 1997.
20 Paragraph 80.
21 AIG Capital Partners Inc and CJSC Tema Real Estate Company Ltd v. The Republic of Kazakhstan, final award of 7 October 2003, ICSID Case No. ARB/01/6.
22 Paragraph 10.6.4(5)(a).

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Contrary to the terms of the contract, the tribunal applied international law since the parties had referred to international authorities in their pleadings and submissions showing 'tacit common position as to the permissibility of such references'. Himapurna was found to be entitled to compensation for *lucrum cessans*. Himapurna submitted that the total projected revenues through 2030 would amount to US$4.048 billion if discounted at 8.5 per cent. Himapurna then deducted the present value of costs at the same discount rate to get the *lucrum cessans*. The tribunal reduced the compensation sought because of a number of factors, which we will not detail here. As regards the remaining portion of the claim, the tribunal determined the present value of the future net income. Himapurna had, as mentioned above, applied a discount rate of 8.5 per cent to the projected revenue stream and to the costs associated with the revenues. The tribunal adjusted the discount rate, having regard to the risks facing the project, and found that the rate should be 19 per cent, which brought down the compensation considerably. The tribunal pronounced:

*The fact remains that it is riskier to enter into a 30 year venture in Indonesia than in more mature economies. . . . [T]here are documents which by their terms allot 100 per cent of the risk to the debtor bonds. Although they may be denominated in US dollars, although they may stipulate absolute obligation to pay, it still makes a difference whether the issuer is Switzerland or Swaziland.*

Thus, the level and type of risk that an investor generally needs to assess depends on the risk profile of the state where the investment is made. This is also illustrated by the *AMT v. Zaire* dispute. It concerned damage that had been made to certain property owned by the investor by Zairean armed forces. The tribunal found that Zaire was in breach of the relevant BIT but did not award the investor the claimed damages in full. The tribunal indicated that the awarded damages should be lower than they would have been if the investment had been made in a more economically and politically stable state. The tribunal found that the investor seemed to have calculated the claimed damages with a method practicable under normal circumstances in an 'ideal country' with a very stable climate of investment and, therefore, decided to use another method for calculating fair compensation. The tribunal pronounced that:

*Preferably, the Tribunal will opt for a method (for calculating damages) that is most plausible and realistic in the circumstances of the case, while rejecting all other methods of assessment which would serve unjustly to enrich an investor who, rightly or wrongly, has chosen to invest in a country such as Zaire, believing that by doing so the investor is constructing a castle in Spain or a Swiss chalet in Germany without any risk, political or even economic or financial or any risk whatsoever.*

There are also examples where states, as a ground for reduction or decline of damages claims, have successfully argued that the investor has made an inadequate assessment of relevant investment risks prior to the investment, or voluntarily accepted the relevant risks, which should lead to a reduction of damages. See for example the *MTD v. Chile* dispute, mentioned under Section II.

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24 Paragraph 358.
Azurix v. Argentina\textsuperscript{27} is an example of when a tribunal specifically considers business risk taken by the investor when deciding on the apportionment of damages. An American company, through an Argentinian subsidiary, invested in a 30-year water concession in the Buenos Aires province. The concession was, however, terminated by the province in only its third year. The tribunal found that the termination by the state was wrongful. It also found, however, that the investor had made an irrational business decision by overpaying for the concession. Because of this, the tribunal found that the investor had to have assumed the risk of not recouping the investment. The tribunal found that most of the investor's loss was because of the irrational business decision rather than because of the state's conduct.

V STATE OF NECESSITY

The ILC Articles describe ‘necessity’ as circumstances that may preclude wrongfulness by a state.\textsuperscript{28} A state of necessity refers to a situation where a state's only option to safeguard an essential interest against a grave and imminent peril is to pursue actions in breach with, for example, a BIT. Article 25 of the ILC Articles provides the following:

1. **Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:**
   (a) is the only way for the State to safeguard an essential interest against a grave and imminent peril; and
   (b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

2. **In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:**
   (a) the international obligation in question excludes the possibility of invoking necessity; or
   (b) the State has contributed to the situation of necessity.

Article 27(b) of the ILC Articles defines state of necessity as a circumstance that may be invoked as a circumstance precluding wrongfulness regarding the question of damages. The possibility for a state to invoke necessity (or similar) as a defence, and the preconditions to do so, is also, in some cases, explicitly stated in BITs.\textsuperscript{29}

State of necessity has been invoked by Argentina in several international investment disputes with American companies with similar factual circumstances. In **CMS**,\textsuperscript{30} **Enron**\textsuperscript{31}

\textsuperscript{27} Azurix Corp v. The Argentine Republic, final award of 14 July 2006, ICSID Case No. ARB/01/12.
\textsuperscript{28} In international investment arbitrations, parties sometimes argue that the ILC Articles cannot apply in investor–state disputes since the articles only address responsibilities between states. However, according to the wording of, for example, Articles 1 and 76 it is clear that they are intended to cover all international obligations of the state. For further discussion regarding this, see, for example, K Hobér, *Selected Writings on Investment Treaty Arbitration*, page 53 et seq.
\textsuperscript{30} CMS Gas Transmission Company v. The Republic of Argentina, final award of 12 May 2005, ICSID Case No. ARB/01/8. The award was partially annulled; decision of 25 September 2007.
\textsuperscript{31} Enron Corporation and Ponderosa Assets LP v. Argentine Republic, final award of 22 May 2007, ICSID Case No. ARB/01/3. The award was partially annulled; decision of 30 July 2010.
and *Sempra Energy*,

Argentina invoked state of necessity, both treaty-based and according to customary international law, because the state, as a result of a political, social and economic crisis in the late 1990s and early 2000s, had to take certain measures to maintain public order and protect its essential security interests.

In all of the above-mentioned arbitrations, the necessity defence was rejected by the tribunal since the requirements according to international law for invoking state of necessity were not met. Since necessity could not be invoked according to international law, the tribunals did not find it necessary to take further judicial overview according to the BIT.

However, in *LG&E v. Argentina*, which had similar factual circumstances to the disputes discussed above, the tribunal found Argentina’s invocation of necessity according to the relevant clause in the BIT and general international law justified. The tribunal considered the overall conditions that were invoked by Argentina and found that they ‘constituted the highest degree of public disorder and threatened Argentina’s security interests’. Argentina was, therefore, excused from liability during the specific period when the tribunal found that it was in a state of necessity. The state, however, had to pay damages for wrongful measures taken outside this period.

VI THE PUBLIC NATURE OF THE STATE

Sergey Ripinsky and Kevin Williams observe that there are indications that the public nature of the respondent state may have an effect on compensation because of a wrongdoing. This may be the case when the wrongdoing does not result in any transfer of wealth and in cases where a large amount of compensation would have a serious adverse effect on the state’s welfare.

The emerging view was perhaps aptly summarised by Professor Sir Ian Brownlie in his separate opinion in *CME v. Czech Republic*:

> [I]t is simply unacceptable to insist that the subject-matter is exclusively commercial in character or that the interests at issue are, more or less, of essential elements in a Treaty relation. The first element is the significance of the fact that the Respondent is a sovereign State, which is responsible for the well-being of its people. This is not to confer a privilege on the Czech Republic but only to recognize its special character and responsibilities. The Czech Republic is not a commercial entity.


33 The tribunals and, in the CMS case, the annulment committee, did put a lot of attention to the issue whether the invoking of the relevant clause in the BIT should be considered as independent to the invoking of international law as manifested in the ILC Articles. For further discussion regarding this issue, see, for example, *Yearbook on International Investment Law & Policy* 2008–2009, page 370 et seq.


35 Decision of liability, 3 October 2006, paragraph 231.

36 S Ripinsky and K Williams, op cit, pages 353 et seq.

VII CORRUPTION

Most states perceive corruption to be a violation of international public policy and international law. However, in numerous developing countries corruption is still a real and widespread problem. Corruption and bribery by the investor has been invoked as a defence by host states in several ICSID arbitrations. In World Duty Free Co Ltd v. Republic of Kenya, the investor brought a claim against Kenya for an alleged expropriation of a contract to operate duty-free concessions at Kenya’s international airports in Nairobi and Mombasa. Kenya was, however, able to show that the concession contract had been procured through the payment of a cash bribe to the former President of Kenya. The tribunal found that a contract procured by a bribe was in violation of international public policy and thus void on contractual grounds. The tribunal therefore dismissed all claims against Kenya since the investor was found:

\[\text{not legally entitled to maintain any of its pleaded claims in these proceedings as a matter of ordre public international and public policy under the contract's applicable law.}\]

In another case, Metal-Tech Ltd v. Republic of Uzbekistan, the tribunal found that it lacked jurisdiction to decide the dispute because of corruption related to Metal-Tech’s investment. Metal-Tech had in 2000 formed a joint venture with two state-owned Uzbek companies to build and operate a plant for production of molybdenum products. In 2006, a criminal proceeding was initiated because it was suspected that officials of the joint venture had abused their authority. Shortly thereafter, the Cabinet of Ministers in Uzbekistan adopted a resolution that abolished the joint venture’s exclusive rights to purchase certain raw materials required to produce molybdenum and to export the products. In 2010, Metal-Tech initiated arbitration, claiming that Uzbekistan had breached its obligations under domestic law and the Israel–Uzbekistan BIT.

The tribunal’s decision that it lacked jurisdiction was based on its finding that Metal-Tech’s investment was not ‘implemented’ in accordance with the laws and regulations of Uzbekistan (Uzbekistan had under the relevant BIT only consented to ICSID arbitration relating to such investments). The tribunal found that payments had been made by Metal-Tech to, *inter alia*, a government official and the brother of the then Prime Minister in connection with Metal-Tech’s initial investment. This, according to the tribunal, constituted corruption to the extent that the investment was considered to not have been established in accordance with the laws and regulations of Uzbekistan and, as a consequence, the dispute could not be subject to arbitration under the BIT.

Lastly, in an arbitration under the ECT, the state (Croatia) raised corruption as a defence to the investor’s (MOL Hungarian Oil and Gas Company Plc) claims. Croatia argued that a certain shareholder’s agreement relating to MOL’s investment was procured through bribery of Croatia’s then Prime Minister. Croatia relied on a jurisdictional objection.

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38 See, for example, a review of such cases under the tribunals decision in World Duty Free Company Limited v. The Republic of Kenya, final award of 4 October 2006, ICSID Case No. ARB/00/7, paragraph 148–155.
40 Paragraph 188.
41 Metal-Tech Ltd. v. Republic of Uzbekistan, final award of 4 October 2013, ICSID Case No. Arb/10/3.
42 MOL Hungarian Oil and Gas Company Plc v. Republic of Croatia, ICSID Case No. ARB/13/32.
based on the argument that the corruption that underlies the shareholder’s agreement entailed, *inter alia*, lack of consent by the host state, lack of investment and violation of international public policy.

**VIII CONCLUSION**

This chapter has discussed some of the most commonly seen defences in investor–state arbitrations. However, the law regarding defences to damages claims in investment arbitrations appears to be under development. This is, in the author’s opinion, particularly true when it comes to the doctrine of investment risks, which also requires that the arbitrators shall be susceptible to economic theory. Another field under development is the consideration of the public nature of the respondent state, which in some instances may be an answer to some of the political criticism voiced against international investment arbitration.
The question of interest is fundamentally linked to the time lags that exist in all arbitration proceedings. The date of expropriation and the date of the arbitration decision never coincide, and neither do the date of the arbitration decision and that of effective payment of compensation. The time elapsed between these dates represents a value for the parties that can be measured by financial interests.

I PRE-AWARD INTEREST

Pre-award interest concerns the period from the date of expropriation to the date of the arbitration decision. It applies to sums of which the investor has been unjustly deprived and requires the application of a market rate.

Quantifying pre-award interest therefore implies determination of the basis (i.e., the basis for calculating the interest) and the interest rate applicable to this basis. These two parameters are examined below.

a Determination of the basis

Determination of the basis for calculating interest requires an examination of what the investor’s financial position would have been if the alleged acts had not occurred. This question requires a distinction to be made between two situations:

a The expropriation is unlawful only because of the absence of fair or prior compensation. In the absence of the alleged acts, the investor would certainly have been expropriated, but would have received fair and prior compensation in exchange. The interest base, therefore, corresponds to the amount of compensation that should have been received on the date of expropriation.

b The expropriation is unlawful because of a series of violations not limited to the sole absence of fair and prior compensation. In the absence of the alleged acts, the investor would not have been expropriated: consequently, he or she would not have received any compensation. He or she would, however, have kept his or her property and generated funds from its operation that would have been available to him or her between the date of expropriation and the date of the decision. Consequently, the interest base corresponds to these funds between the date of expropriation and the date of the arbitration decision.

1 Mikaël Ouaniche is chair of the OCA.
Determination of the applicable rate

In the context of the limits set by the bilateral investment treaties, arbitration tribunals may have a wide range of possibilities available to them in choosing the interest rate to be applied. The choice of interest rate may significantly change the total amount of compensation awarded to the investor. Adopting the interest rate is therefore neither simple nor easy for the arbitration tribunal.

The payment of pre-award interest must compensate the investor for the financial loss suffered as a result of the deprival of funds of which he or she was a victim by putting the investor in the position in which he or she would have been if the event that generated the loss had not occurred. To decide on the interest rate, arbitration tribunals must thus determine the use the investor would have made of the sums of which he or she was deprived had they been available to him or her between the date of expropriation and the date of the decision.

Several questions must therefore be asked:

a. Would the investor have used all or part of these funds to clear his or her debts or avoid falling into debt?

b. Would he or she have invested these sums in liquid assets?

c. Would he or she instead have used these funds to make alternative investments? If so, which ones?

d. Would he or she have invested them in his or her own business?

According to the responses given to these questions by the tribunal (depending on the investor’s claims and the proof provided), different approaches may be considered, which can be divided into two broad categories: approaches in terms of costs incurred and approaches in terms of lost profit.

Approach in terms of costs incurred

This approach consists of considering that, in the absence of harmful events, the investor could have avoided resorting to debt in the amount that he or she should have received if the event that generated the loss had not occurred. The purpose of pre-award interest is, therefore, to compensate for the cost of the additional debt resulting from the loss of funds of which the investor was a victim. The financial loss is therefore analysed as a cost incurred. In this context, the interest rate to be adopted is logically the interest rate relative to the investor’s additional debt.

Two approaches may then be considered: an approach via the rate of the investor’s own debt and an approach via market debt rates.

Approach via the interest rate of the investor’s own debt

The interest rate of the investor’s own debt is that corresponding to the investor’s borrowings between the date of expropriation and the date of the arbitration decision.

Since this is an incurred financial cost, it is up to the investor to provide proof of the interest rate that he or she actually had to pay as a result of the harmful event.

If the investor had several outstanding loans during the period, it seems logical to adopt the highest interest rate, namely a marginal interest rate rather than an average interest rate over the period. Indeed, if the investor had the funds of which he or she was deprived at his or her disposal, he or she would reasonably have used them in such a way as to avoid falling into debt or to clear his or her debt with regard to the most costly loan instalments.
In practice, however, arbitration tribunals do not seem to refer to this approach, which nevertheless seems to be the most appropriate for calculating the financial costs incurred by the investor.

**Approach via market debt rates**

In practice, tribunals predominantly have recourse to LIBOR, EURIBOR or EONIA as a rate of reference. These average rates are those at which banks can borrow from other banks on the London interbank market (for LIBOR) or on the Eurozone interbank market (EURIBOR, EONIA).

The advantage of these rates is that they are published daily for different maturities and currencies, and are recognised as a calculation base for different interest rates.

Tribunals customarily add a premium to these rates, most often in the order of 2 per cent, in order to extend the rate towards that at which the investor borrowed money to fund his or her activities.

In the *Lemire v. Ukraine* case, the six-month average US-dollar LIBOR rate was used as the rate of reference to which the arbitration tribunal added a 2 per cent margin, a margin considered ‘adapted’ in reference to Article III(1) of the bilateral investment treaty that was in force for this case:

> Since the compensation is expressed in USD, the appropriate rate of reference for the calculation of interest should be the LIBOR rates for six month deposits denominated in USD, calculated as of the date of delivery of this Award. The rate shall be adjusted every six months thereafter, to reflect changing market conditions.

In the *M Meerapfel Söhne AG v. Central African Republic* case, the tribunal adopted simple interest at the one-year EURIBOR rate, to which it added two points:

> However, the tribunal adopts simple interest at the one-year Euribor rate + 2 points, which it considers likely to ensure adequate and full compensation for the prejudice suffered by the Claimant.

Finally, in the *Crystallex v. Venezuela* case, the tribunal also opted for the six-month average US-dollar LIBOR rate as the rate of reference, to which it added a margin of 1 per cent per year:

> In the Tribunal’s view, taking into account the circumstances of the case, the most appropriate interest rate which will adequately compensate Crystallex is the 6-month average U.S. dollar LIBOR plus

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3 For example, we refer to a one-week EURIBOR or a three-month EURIBOR.


1 per cent per year at the valuation date. In the tribunal’s view, this approach approximates a commercially reasonable rate and provides adequate compensation for the financial loss caused to a company engaged in international business.6

In certain cases, tribunals have used another rate of reference from the money market: the central banks’ marginal lending rate (marginal lending facility). The marginal lending rate corresponds to the rate at which central banks lend liquidities to commercial banks. This is the highest rate at which the latter can finance themselves (since interbank lending rates are necessarily lower than or equal to this rate). In the Mitchell v. Congo case, the arbitration tribunal adopted the Federal Reserve Board’s marginal lending rate (called the prime lending rate):

The Claimant considered that the interest rate to be applied to this amount is the prime lending rate of the “Federal Reserve Board of Governors Bank”, which was at 7.75% in March 1999. . . . The tribunal is of the opinion that the rate indicated by the Claimant is appropriate and, consequently, the sum of USD 750,000 bears interest at the rate of 7.75% per year as from 6 March 1999.7

However, the reliability of interbank rates may be questionable: the scandals involving manipulation of these interbank rates, particularly in 2012, may have led certain arbitration tribunals, as in the Cyprus v. Russia case, to question the use of these rates, which are suspected to have been manipulated by banks:

1646. In response to a question by the Chairman whether Claimants “still rely on LIBOR”, counsel for Claimants noted that he had “avoided making any comment on the reliability of LIBOR.”
1679. LIBOR, as Claimants’ counsel implicitly recognized during the Hearing, has been discredited.8

Above all, the recourse to rates of reference by arbitration tribunals poses a real conceptual difficulty. The interbank lending rates are effectively average market lending rates, which do not correspond to the rates at which banks actually lend to investors. In an attempt to come close to them, tribunals adapt the market rates to the investor’s profile by applying premiums. This very approximate approach is never clearly documented.

There is, however, no reason to have recourse to average market rates when it is up to the investor to quantify the amount of financial interest he or she was effectively forced to pay as a result of the debt to which he or she was exposed during the period from expropriation to the date of the decision. The use of rates of reference by tribunals thus falls short of our sense of economic foundation insofar as it leads to approximations.

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7 Patrick Mitchell v. Democratic Republic of Congo, prev. note 3, § 94. This decision was subsequently invalidated on 1 November 2006 by the ad hoc committee on procedural grounds.
8 Veteran Petroleum Limited (Cyprus) v. The Russian Federation, UNCITRAL, PCA Case No. AA 228, Award, 18 July 2014, § 1646 and 1679.
Approach in terms of lost profit

In certain particular cases, the investor may not have been forced to borrow or maintain his or her debt to compensate for the loss of cash suffered as a result of expropriation. In these situations and in the absence of the alleged acts, the investor could consequently have been able to place or invest the sums of which he or she was deprived in order to derive interest from them for which he or she is henceforth entitled to obtain compensation.

If it is considered that the funds would simply have been deposited in the investor’s bank account, the approach based on the remuneration rate for bank deposits will be adopted.

Several other approaches may be adopted according to whether it is considered that the funds would have been invested by the investor between the date of expropriation and the date of the decision:

- in risk-free assets: approach based on the risk-free rate;
- in certain well-identified projects: approach based on the rate of return on an alternative investment;
- in the expropriating state’s debt bonds: forced loan approach; and
- in the investor’s general activities: approach based on the average return on capital employed.

Approach based on the remuneration rate for bank deposits

Considering that the investor would have been able to place the funds in a deposit account, his or her lost profit must be calculated with reference to the remuneration rate for the investor’s bank deposits. These rates vary according to the currency and maturity of the deposits in question.

However, this hypothesis is rarely adopted insofar as the remuneration of bank deposits is low and that an investor, in theory, does not keep his or her liquidities, but rather invests them to increase the return on his or her funds.

Thus, the scenario according to which the investor would have invested this money in an alternative investment is more frequently adopted.

Approach based on the rate of return on an alternative investment

The approach based on the return on an alternative investment is based on the logic according to which the investor would have used the sums that he or she was deprived of to make investments other than those that were the subject of the expropriation proceedings.

This approach was adopted by majority opinion in the *Sylvania Technical Systems v. Iran* case:

> [T]he tribunal will derive a rate of interest based approximately on the amount that the successful claimant would have been in a position to have earned if it had been paid in time and thus had the funds available to invest in a form of commercial investment in common use in its own country.9

The difficulty with this approach consists of determining what the nature of this alternative investment would have been and the rate of return that would have been associated with it.

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In theory, a rational investor’s interests will always lie in using his or her money in such a way as to maximise his or her expected gains, while at the same time taking into account the probability of the investment’s failure. Although this approach is based on a theoretical principle – the rationality of investors – that is not exempt from criticism, it does have the merit of allowing the establishment of an operational decision rule for the appraiser and subsequently for the tribunal.

Among the possible alternative investments offered to the investor, it would therefore be necessary, in the application of this rule, to adopt the highest interest rate from among those possible, on the condition that the investor has submitted a request to this effect and provided proof of the existence of these alternative investment opportunities. This may prove to be complicated when the alternative investment appears too uncertain or the causal link to the harmful event is not sufficiently established. For example, in the Crystallex v. Venezuela case, the tribunal rejected the interest rate proposed by the investor because the latter was unable to prove that he would have used the amount of the monetary compensation to invest in the bonds indicated (causal link not proven). The tribunal preferred to use the six-month average US-dollar LIBOR rate plus 1 per cent per year. It considered that this rate was a more accurate reflection of a ‘commercially reasonable’ interest rate:

With regard to the interest rate, the tribunal is unable to accept the Claimant’s proposed rate, i.e. 8% per annum based on the coupon rate of bonds used by PDVSA. In the tribunal’s view, the Claimant has not proven that either pre- or post-award Crystallex would have used any awarded amounts to purchase or invest in PDVSA bonds or, for that matter, any instrument or investment producing a similar return.

In the tribunal’s view, taking into account the circumstances of the case, the most appropriate interest rate which will adequately compensate Crystallex is the 6-month average U.S. dollar LIBOR plus 1 per cent per year at the valuation date. In the tribunal’s view, this approach approximates a commercially reasonable rate and provides adequate compensation for the financial loss caused to a company engaged in international business. At the hearing, experts of both sides confirmed that LIBOR plus a certain percentage constituted a normal commercial rate in the circumstances.10

In the same vein, in the M Meerapfel Söhne AG v. Central African Republic case, it is specified:

The OHADA law, while providing for the principle of payment of interest on sums due, does not include indications relative to the applicable rate. CAR law does not include any further indications relative to this matter either. The tribunal considers that the rate of 12% claimed by MMS has no basis whatsoever, no more than the capitalisation of interest, which is also claimed. MMS did not provide proof that it could have invested the sums claimed at a rate of 12% with capitalisation of interest, particularly in CAR. However, the tribunal adopts simple interest at the one-year Euribor rate + 2 points, which it considers will ensure adequate and full compensation for the loss suffered by the Claimant.11

The alternative investment approach is thus frequently rejected by tribunals because of insufficient demonstration of the existence and expected return of these investment opportunities and the causal link to the harmful event.

**Forced loan approach**

The forced loan approach consists of resorting to use of the expropriating state’s lending rate. The investor’s loss of funds as a result of the harmful event implicitly forces him or her to lend money to the expropriating state insofar as the state has been in possession of the funds that should have been in the hands of the investor during the period from the expropriation to the date of the decision. In this context, the investor finds himself or herself exposed to the risk of the expropriating state failing to reimburse this forced loan so that the interest rate should include this default risk.

The interest rate associated with the forced loan is thus measured by the rate at which the expropriating state effectively borrowed on the financial markets during the period in question (i.e., from the date of expropriation to the date of the decision). This rate includes a risk premium, which compensates for the risk of the sovereign state defaulting on its financial commitments.

Certain authors have reproached this logic for taking into account the state’s default risk when this risk no longer exists on the date of the decision. 12

This approach suffers, above all, from a methodological bias since it boils down to noting the retrospective existence of the compensatory amount due on the date of occurrence of the harmful event.

**Approach based on the risk-free rate**

Tribunals have sometimes resorted to risk-free lending rates, such as the American Treasury bond rate. The reasoning adopted consists of considering that the premium for the risk with which the investor is faced is already taken into account by the arbitration procedure on the date of the decision. The investor should not receive compensation for risks he or she no longer bears. Recourse to the risk-free rate therefore consists of simply adopting the value of the compensation on the date of the decision in order to take the monetary erosion linked to elapsed time into consideration.

This approach seems inappropriate for several reasons. First, it may be argued that the monetary erosion linked to elapsed time can only be measured by the rate of inflation. In the logic adopted by the tribunal, the sole objective of calculating interest is to express the amount of compensation in constant currency. However, there may be differences between the rate of inflation in a particular country and the rate of return on state bonds.

Secondly, if the risk with which the investor was confronted between the date of expropriation and that of the decision concerns a period elapsed on the date of appraisal, the fact remains that the investor may not necessarily have invested his or her money in risk-free assets during this period.

**Approach based on the average return on capital employed**

This approach consists of considering that the investor would have used the sums of which he or she was deprived to invest in his or her own activity. To measure the corresponding financial interest, tribunals frequently adopt the weighted average cost of capital (WACC) indicator for the investor.

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12 In this context, see Irmgard Marboe, *Calculation Of Compensation And Damages In International Investment Law* (2009).
This cost measures the average rate of return expected by the investor’s capital providers – namely shareholders on the one hand and financial creditors on the other. The WACC therefore simultaneously measures:

a  the investor’s financing cost on the debt and capital market; and

b  the return expected by the investor on the investment of his or her resources.

This measurement could therefore be used both for an approach in terms of costs incurred and an approach in terms of lost profit. However, we consider that the WACC is not appropriate for implementation of the approach in terms of costs incurred, which implies recourse to an interest rate directly linked to the investor’s debts.

Similarly, recourse to the WACC for implementation of the approach in terms of lost profit poses a problem because this indicator measures a rate of return expected and hoped for by the capital providers (shareholders and creditors), and not a rate of return necessarily realised.

To measure the effective return on the capital invested by the investor, it is necessary, in our opinion, to adopt the return on the capital invested in the past. The return on capital employed (ROCE) rate corresponds to the ratio of the after-tax operating result for the sum of the investor’s equity and financial debts.

Recourse to the investor’s ROCE nevertheless presents a major difficulty with regard to its implementation. If the return on the capital invested by the investor is calculated for the period from the date of expropriation to the date of the decision, it will quite logically be negatively affected by the expropriation for which compensation is claimed by the investor. It will therefore be up to the appraiser to calculate the return on the capital invested as it would have been noted with the investor in the absence of the alleged acts.

Although this exercise is theoretically possible, it may often be faced with insufficient proof or an insufficiently supported causal link. A more operational solution will consist of adopting the average return on capital invested in the investor’s sector of activity during the period from the date of expropriation to the date of the decision.

Where appropriate, it may be justified to take into account a premium or discount according to the proven past capacity of the investor to outperform or underperform the market.

Summary of applicable interest rates

It is up to the arbitration tribunal to determine the appropriate interest rate for each case according to the proof provided by the investor to support the existence of a causal link between the financial loss calculated and the event that generated the loss.

Ripinsky and Williams favour the use of the approach via return on alternative investments except when expropriation forces the investor to resort to a loan, in which case the lending rate of the latter will be more appropriate:

In most cases, the “alternative investment” approach would thus best meet the objective of fully compensating a claimant for the loss of the use of money as well as give much-needed uniformity to the practice and predictability of the parties. However, in situations where the debtor’s actions force the claimant to borrow funds, it would be correct to award interest at the claimant’s actual borrowing rate, in order to place the claimant in a position it would have been in the absence of the breach.13

In other words, when it is proved that, in the absence of a harmful event, the investor could have avoided falling into debt or maintaining his or her debt, the corresponding financial costs are analysed as a compensable incurred cost. It is therefore necessary to calculate the financial cost incurred on the basis of the funding rates that the investor effectively had to face, which must lead to excluding recourse to interbank rates of reference.

On the contrary, when it is proved that, in the absence of a harmful event, the investor would have placed or invested the sums of which he or she was deprived, the corresponding financial products are analysed as compensable lost profit.

As such, recourse to approaches in terms of forced loan or risk-free assets to determine pre-award interest appear to lack any economic foundation and, moreover, appear contrary to the principle of full compensation for the investor’s loss.

However, the approach in terms of ‘return on alternative investments’ or ‘average return on capital employed by the investor’ appears more appropriate than that based on the rate of remuneration of bank deposits if the rationality of investors principle is accepted.

In the context of the approach based on returns on capital, we have reservations concerning use of the WACC because this indicator is based on a return expected by the markets and not on the return the investor would have actually realised from his or her investments.

To determine the rate of return on capital invested that the investor could have obtained in the absence of a harmful event, recourse to the ROCE rate appears to be the most appropriate indicator. In practice, determination of the internal ROCE rate that the investor could have realised in the absence of the alleged acts may prove to be very complicated to implement. As an alternative, reference could be made to the rate of return observed in the investor’s sector of activity for the period from expropriation to decision. This rate could be adjusted upwards or downwards, as the case may be, according to the investor’s past recorded individual performance compared with that of his or her sector of activity.

Finally, let us note that it is essential to determine the applicable interest rate in line with the currency into which the compensation will be converted. An economic relationship effectively exists between the interest rate and the exchange rate. A fall in the interest rate on loans and deposits in a country, in theory, brings about a depreciation of the currency in the country in question. Thus, it is essential to choose the interest rate in line with the currency used for payment of the monetary compensation. For example, if the monetary compensation is expressed in American dollars, the interest rate to use must itself be relative to American assets, loans or deposits.

iii Compound interest or simple interest

Interest is called simple when it is not added to the capital at the end of each term. The initial capital therefore generates interest alone during each period.

Interest is called compound when it is added to the capital at the end of each term. The interest itself generates interest during the following period. Consequently, the amount of interest generated during the following periods is higher than the interest generated during the preceding periods.

Calculation of compound interest thus leads to higher amounts than that of simple interest. Is it therefore more appropriate to have recourse to one method of calculation rather than another?

Remember that pre-award interest compensates the investor’s financial loss resulting from not being able to use the funds of which he or she was deprived. Had he or she had this cash at his or her disposal, he or she would either have put it to work by placing or investing
it (approach in terms of lost profit) or used it to clear his or her debt or avoid falling into debt (approach in terms of costs incurred). At the end of each term, the investor would either have obtained the financial products of his or her placement or investment – interest that he or she would have invested again – or he or she would have avoided having to pay interest to his or her bank – interest that, more often than not, is subject to capitalisation.

In our opinion, only the recourse to compound interest makes it possible to respect the full compensation principle because it puts investors back in the financial position they would have been in if the alleged acts had not taken place.

In the lost profit approach, using compound interest is tantamount to acknowledging that an investor never lets his or her money ‘sleep’ in an account without receiving interest. This calculation method is thus realistic and in keeping with the business world.

Moreover, compound interest compensates for the unjustified enrichment of the state, which has had the opportunity to put the money of which it deprived the investor to work in order to generate interest.

Although the approach predominantly followed has been that of simple interest, over the past 20 years we have nevertheless observed a progressive change in the practice of tribunals, which now increasingly opt for compound interest. The Costa Rica v. Santa Elena\textsuperscript{14} case marks a major turning point with the decision of the arbitration tribunal to compound interest semi-annually.

Following the date of this decision, many arbitration decisions have taken the side of compounding due interest annually. For example, in the Metalclad v. The United Mexican States case, it is specified: ‘So as to restore the Claimant to a reasonable approximation of the position in which it would have been if the wrongful act had not taken place, interest has been calculated at 6\% p.a., compounded annually.’\textsuperscript{15}

In the Crystallex v. Venezuela case, the pre-award interest is also compounded: ‘Thus, for the reasons stated above, the tribunal awards interest on the principal sum awarded, compounded annually, at the rate of the 6-month average U.S. Dollar LIBOR plus one percent, which shall accrue from 13 April 2008 until the date of the Award.’\textsuperscript{16}

However, the discretionary powers of tribunals in this matter remain intact. It may thus be regretted that, in the famous Yukos v. Russia case, the arbitration tribunal, while acknowledging that compound interest was now the subject of jurisprudence constante, decided to resort to simple interest for the pre-award interest:

\begin{quote}
As to whether the interest awarded should be simple or compound, while the tribunal recognizes that the awarding of compound interest under international law now represents a form of “jurisprudence constante” in investor-state expropriation cases, the tribunal has concluded that, in the circumstances of this case, it would be just and reasonable to award Claimants simple pre-award interest and post-award interest compounded annually if Respondent fails to pay in full to Claimants the damages for which it has been held liable before the expiry of the grace period hereinafter granted.\textsuperscript{17}
\end{quote}

\textsuperscript{14} Compañía del Desarrollo de Santa Elena S.A. v. Republic of Costa Rica, ICSID Case No. ARB/96/1, Award, 17 February 2000.
\textsuperscript{15} Metalclad Corporation v. The United Mexican States, ICSID Case No. ARB (AF)/97/1, Award, 30 August 2000, § 128.
\textsuperscript{16} Crystallex International Corporation v. Bolivarian Republic of Venezuela, prev. note 3, § 938.
\textsuperscript{17} Yukos Universal Limited (Isle of Man) v. The Russian Federation, UNCITRAL, PCA Case No. AA 227, Award, 14 July 2014, § 1689.
II POST-AWARD INTEREST

This interest applies from the date of the arbitration decision until the date of effective payment of the monetary compensation. In practice, the tribunal may grant a grace period starting on the date of the decision, a period during which interest does not run. This was decided in the *Yukos v. Russia* case:

> In the circumstances of the present case, in view of the significant amount of damages which Respondent owes Claimants as a result of this Final Award, the Tribunal considers it reasonable to grant to Respondent a grace period of 180 days following the date of the Award before interest will accrue if not paid in full to Claimants by then.18

A more accurate qualification of post-award interest lies in the term ‘default interest’. It is ‘intended to compensate for the loss resulting from lateness in executing an obligation’.19 In the *Aucoven v. Venezuela* case, the arbitration tribunal considered: ‘post-award interest is intended to compensate the additional loss incurred from the date of the award to the date of final payment.’20

Post-award interest therefore differs fundamentally from pre-award interest insofar as post-award interest aims to favour execution that is fast or within the deadlines imposed by the arbitration decision. In practice, we nevertheless note that pre-award interest is rarely dissociated from post-award interest by tribunals, which, more often than not, adopt an identical rate and calculation method.21

Although this practice certainly has the advantage of ensuring greater simplicity in decisions, it has the major disadvantage of maintaining confusion between two very different logics: one, economic (pre-award interest calculated in application of the full compensation principle) and the other, legal (post-award interest aiming to favour fast execution of arbitration decisions).

As for pre-award interest, tribunals have a certain amount of discretion when awarding post-award interest, whether it be the interest rate adopted or its method of calculation. There are effectively no rules specifically established in the matter apart from those established in the context of bilateral investment treaties.

i Applicable interest rate

A possible approach for determining the post-award interest rate is the forced loan approach described above. Between the date of the decision and the date of payment, the investor is exposed to a risk of default by the expropriating state with regard to effective payment of the monetary compensation. An investor who is the holder of a compensatory debt obligation

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18 *Yukos Universal Limited (Ile of Man) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 227, Award, 18 July 2014 § 1691.
21 *Swisslion DOO Skopje v. The Former Yugoslav Republic of Macedonia*, ICSID Case No. ARB/09/16; *Dunkeld International Investment Ltd. v. The Government of Belize (Number 1)*, PCA Case No. 2010-13, UNCITRAL; *Metalclad Corporation v. The United Mexican States*, ICSID Case No. ARB (AF)/97/1; *Compañía del Desarrollo de Santa Elena S.A. v. Republic of Costa Rica*, ICSID Case No. ARB/96/1; *Crystallex International Corporation v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB (AF)/11/2.
by virtue of an arbitration decision effectively becomes a creditor of the state in the same way as holders of treasury bonds, and it seems, therefore, logical to consider that the interest rate relative to his or her debt must include a premium covering the default risk of this state.

ii Compound interest or simple interest

For the reasons indicated above, when post-award interest is pronounced, it seems to us preferable to adopt compound interest. This was particularly the case in *Crystallex v. Venezuela*:

*The Respondent shall thus pay post-award interest on the total amount of damages, compounded annually, at the rate of the 6-month average U.S. Dollar LIBOR plus one percent, from the date of the Award until full payment.*

In the *Cyprus v. Russia* case, the arbitration tribunal also decided to compound the post-award interest fully:

*In the event that Respondent fails to pay in full to Claimants the costs awarded to them in Part XIII of the present Award before the expiry of the grace period, post-award interest will accrue on any outstanding amount, compounded annually.*

Finally, it seems necessary to compound interest in line with the post-award interest rate adopted. For example, if the treasury bonds held in the expropriating state generate interest every six months, it is necessary to compound the post-award interest over the same period (i.e., over six months).

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23 *Veteran Petroleum Limited (Cyprus) v. The Russian Federation*, UNCITRAL, PCA Case No. AA 228, § 1690.
Chapter 27

COUNTRY RISK PREMIUM

Ronnie Barnes, Phillip-George Pryce and Dustin Walpert

I INTRODUCTION

The treatment of expropriation risk in quantum assessments in international arbitration is an issue that has recently received a lot of attention, and it is fair to say that nothing that even vaguely resembles a consensus has yet to emerge. The objective of this chapter is to provide a simple and clear overview of the challenges faced by a quantum expert when addressing expropriation risk, and, in particular, to show how a pragmatic approach may be needed to address what is a conceptually complex issue. Relatedly, this chapter explains the importance of distinguishing between country risk and expropriation risk (the former a broader concept that has the latter as one of its components), and ensuring that attempts to incorporate expropriation risk into a quantum assessment do not inadvertently lead to the double counting of other components of country risk.

II DISCOUNTED CASH FLOW ANALYSIS

In many international arbitrations, whether an investor–state dispute or an international commercial arbitration, the role of the quantum expert is to determine the value of an asset or project, with the results of this valuation exercise being used as an input to the assessment of compensation. In recent years, quantum experts have increasingly relied upon, and arbitral tribunals have increasingly accepted, the discounted cash flow (DCF) method as an approach to these valuations. The implementation of the DCF method requires an estimation of the stream of future cash flows that the asset or project is expected to generate over its lifetime, followed by the discounting of these cash flows back to the date of valuation using a discount rate that accounts for both the time value of money and the risk or uncertainty that is associated with the future cash flow stream.

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However, although opposing quantum experts might agree as to the appropriateness of the DCF valuation method, they often fundamentally disagree on its inputs, in particular, the discount rate. As even a cursory review of any corporate finance textbook will indicate, this is far from unique to international arbitrations – the estimation of expected future cash flows and the determination of the appropriate discount rate are inherently complex exercises. However, there is a specific feature of international arbitrations that potentially make such disagreements particularly pronounced, namely that these disputes typically arise out of cross-border investments whereby an investor in one country invests in a second, often emerging market country, thus exposing itself to the ‘country risk’ associated with that second country. Consequently, it is often the case that one of the main points of contention between the quantum experts on a given matter relates to the definition and quantification of this country risk, and how it should be incorporated into the asset’s or project’s valuation.

### III COUNTRY RISK

Broadly, country risk ‘is a . . . concept that encompasses both the potentially adverse effects of a country’s political environment and its economic and financial environment’. In simple terms, it refers to those risk factors the foreign investor would not face in its domestic market, such as political instability in the host country and potential shifts in a government’s economic policy; for example, the nationalisation of private industries and the imposition of protective tariffs. In principle, to account for the effect of country risk on value, the quantum expert could either adjust downwards the expected cash flows stemming from the asset or project, or incorporate a ‘country risk premium’ into the discount rate. The rationale for the latter approach – one that is frequently advocated for by quantum experts – is that the higher the degree of uncertainty arising from actions taken by the government in the host country, the higher the discount rate, and therefore the lower the stream of discounted future expected cash flows and, consequently, the value of the asset or project.

However, as explained in a related article, from a conceptual point of view, this approach is problematic. That article introduces the capital asset pricing model (CAPM), which is ‘by far the most commonly used approach for determining discount rates in a wide range of practical settings’, and explains how the CAPM – originally developed in a single country setting – can be modified to an international setting.

The article goes on to lay out the following ‘recipe’ for cross-border valuations:

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5 This is not necessarily the case. A quantum expert might argue that any assessment of future cash flows is too speculative, and that a valuation based on book value or the original cost of investment is appropriate. Alternatively, the quantum expert may be a proponent of the ‘multiples-based’ approach to valuation, which relies on the identification of comparable investments or transactions, or both. A discussion of the relative merits of these different valuation methodologies is beyond the scope of this chapter.


a Estimate expected future cash flows, taking account of country risk – in other words, ensure that any factors that contribute to country risk are accounted for through a reduction in the expected cash flows from the asset or project being discounted.

b Determine the discount rate as the sum of a risk-free rate, plus a risk premium. The latter is not a country risk premium – rather, it is the premium that investors demand to compensate them for what is referred to as the systematic risk of the cash flows being valued.

c Do not increase the discount rate to reflect country risk, since 'increasing the discount rate to reflect country risk would be either double counting the project’s systematic risk, or bringing diversifiable, non-systematic risk into the discount rate calculation, neither of which is appropriate'. Discount rates should not reflect risks that are diversifiable.

That a country risk premium should not be added to the discount rate does not mean that the international nature of the valuation is irrelevant to the determination of the appropriate discount rate. To the contrary, an important assumption that a quantum expert is required to make – but one that is often overlooked – when estimating the risk premium component of the discount rate relates to the extent to which capital markets across the globe are integrated. Assuming fully integrated capital markets implies that investors in all countries hold portfolios that are well diversified internationally. However, assuming fully segmented capital markets implies that investors hold portfolios of assets in a particular country (e.g., US investors hold only US investments). The two assumptions lead to potentially quite different risk premiums and, consequently, discount rates, although the degree of difference is essentially an empirical question.

In reality, capital markets are neither fully integrated nor fully segmented. For example, in many countries, there are restrictions with regard to foreign investments. Furthermore, even if there were no such restrictions, investments in assets or projects are often not divisible into smaller fractions. As a consequence, for instance, a firm investing in a large power plant or mining operation may have to commit a substantial portion of its capital to a single project, making it impossible to diversify the risk exposure to the host country in which the investment is located.

This therefore necessitates a pragmatic approach to the determination of the discount rate, and in particular the risk premium element. The recommendation is that risk premiums

13 The determination of the risk-free rate is somewhat more straightforward, although there are moderately complex issues to address regarding, for example, the maturity or tenor of the rate to use. The key point is that the rate used must match the currency in which the expected future cash flows are denominated. Even if the investment is located in an emerging market country, if the forecasts of expected future cash flows are denominated in US dollars, a US risk-free rate should be used in the discount rate. The rationale is as follows: the emerging market risk-free rate is higher than the US risk-free rate because of an anticipated depreciation of the emerging market currency with respect to the US dollar. However, this anticipated depreciation will (or at least should, if the exercise has been performed properly) have been incorporated into the expected future cash flow forecasts. Consequently, discounting this expected US dollar denominated future cash flow stream at a discount rate that includes the emerging market risk-free rate, would lead to a double counting of the expected future weakness of the emerging market currency.
Country Risk Premium

should be estimated under both assumptions (fully integrated and fully segmented capital markets). To the extent that these differ significantly, the relative weighting given to the two estimates should be driven by a consideration of the level of diversification in the portfolio of the investor from whose perspective the valuation is being assessed. This is an admittedly imprecise recommendation. However, that there is no single clear-cut right answer to the question should not be taken to mean that the issue can be ignored – a failure to even address the question can potentially lead to the use of a risk premium, and consequently a discount rate, that is wildly inappropriate.

IV COUNTRY RISK AND INTERNATIONAL ARBITRATIONS

Though motivated by questions of quantum in an international arbitration setting, the preceding discussion regarding the appropriate treatment of country risk is in fact applicable to any situation where there is a need to incorporate the cross-border nature of an investment into a valuation. A question that is, however, specific to an international arbitration quantum assessment is whether the resulting valuation is an appropriate starting point for the determination of compensation. Specifically, such a valuation is what may be termed a ‘fundamental value’ or a ‘fair market value’, and is the value that is appropriate when considering an arms-length transaction between a willing buyer and a willing seller, since it properly and fully accounts for all of the risks that the investment is exposed to, including country risk. As such, it may also be a suitable basis for a quantum assessment in an international commercial arbitration. Once we move to the investor–state arena, however, the situation becomes considerably less clear.

A key element of country risk is political risk, which may be defined as ‘a special case of country risk in which a government or political action negatively affects a company’s cash flow’. In turn, a key element of political risk is expropriation risk; namely the risk that the host government takes some action that diverts some or all of the cash flows generated by the asset or project being valued away from the investors in the asset or project, and towards that government. Consequently, a valuation that fully and properly accounts – by adjusting downwards the expected cash flows – for country risk will, by definition, reflect expropriation risk. Of critical importance to the investor–state arbitration community is the question of whether this is appropriate – in other words, should expropriation risk be taken into account when determining a measure of compensation?

The argument made in certain investor–state arbitrations against the inclusion of expropriation risk is as follows: the more a host state takes actions that increase the perceived

14 For example, an investment banker advising a US client on a potential investment in South Africa.
17 The repeated use of the word ‘perceived’ in the following discussion is deliberate. Even if a host government knows with certainty that it will take actions in the future that will, in whole or in part, expropriate an investment, what matters when determining the value of the investment at a given point in time is the perceived likelihood that such actions will be taken. Different perceived likelihoods will lead to different valuations – by definition, when attempting to determine the fair market value, what is sought is an estimate of the market consensus as to this likelihood. Though easy to articulate, this is of course an extremely challenging exercise in practice.
expropriation risk, the greater are the downward adjustments to the expected cash flows and the lower is the resulting valuation. If this valuation is then used as the basis for an award of compensation after an expropriation has actually taken place, the host state has benefited – in the form of having to pay a lower amount of compensation – from its actions. This can be analysed with a simple example. Suppose that: (1) an international investor owns a project located in a host country and expects this project to generate a single cash flow of US$100, (2) there is a perceived probability ‘p’ that the government of the host country will expropriate the project with no compensation and (3) the discount rate is zero. The fair market value of this project is US$100 multiplied by the perceived probability that the government does not expropriate.

If p is equal to 50 per cent, the fair market value of the project is US$50. The more the government’s actions increase p, the lower the fair market value of the project is. For example, if p increases from 50 to 75 per cent, the fair market value of the project decreases from US$50 to US$25. Suppose that the government then exercises its sovereign right to expropriate. If p becomes very high immediately prior to the expropriation, the fair market value of the project and, therefore, the compensation that the investor receives would be reduced, potentially significantly. However, the host country would pay the investor an amount of compensation that is lower than the compensation that the host country would have paid if this had been based on the fair market value prior to the increase in p. A tribunal deciding a dispute between the investor and the host state could, in principal, decide to account for the increase in p in determining compensation. Whether this is appropriate is of course a legal question. Nonetheless, determining how to handle expropriation risk in that valuation generates a number of challenges from the perspective of a quantum expert. In this simple case, the arbitral tribunal could require different calculations depending on its determinations regarding the expropriation:

a. Consider the expropriation risk on the eve of the expropriation of the project without any adjustment. This approach appears to be consistent with tribunal awards in which the expropriation was found to be lawful.

b. Eliminate the expropriation risk in its entirety and compensate the investor at the ‘full’ value that the project would have had absent the expropriation. That is, p would be set to zero. As explained below, this appears to be the approach undertaken by certain tribunals in the case of an unlawful expropriation. In other words, even if p was greater than zero, because investors feared a lawful expropriation, if the form of the actual expropriation was unlawful, the concept of full reparation could lead the tribunal to compensate the investor with the full value of the project, eliminating the effect of any government conduct on the expropriation risk.

18 If the perceived probability that the government expropriates is p, the perceived probability that it does not expropriate is 1 – p.
19 That is, US$100 × (1 – 50 per cent) = US$50.
20 That is, US$100 × (1 – 75 per cent) = US$25.
21 These approaches include a list of examples and are not intended to be exhaustive.
22 See, for example, *Tidewater Investment SRL and Tidewater Caribe C.A. v. The Bolivarian Republic of Venezuela* (ICSID Case No. ARB/10/5), Award, 13 March 2015, paragraph 146.
23 See also Alberro, J. (2016). ‘Should Expropriation Risk Be Part of the Discount Rate?’, *Journal of International Arbitration*, 33(5), pp. 525–547 at p. 526 citing the *Factory at Chorzów* judgment (‘It follows that the compensation due . . . is not necessarily limited to the value of the undertaking at the moment of
c Eliminate the expropriation risk in part and compensate the investor accordingly. The perceived probability of expropriation could be set to the level that prevailed at the time when the investor made its investment. Alternatively, it is possible that expropriation risk has increased after the investment was made due to legal or legitimate policies enacted by the government. In this case, the tribunal may wish to attempt to isolate the perceived increase in the probability of expropriation that can be traced back to unlawful conduct on the part of the host state.

A number of arbitral tribunal awards have focused on the distinction between lawful and unlawful expropriation, and the impact of expropriation risk on the value of the assets or project at issue. For example, in the Gold Reserve v. Venezuela award, the tribunal found that the manner by which the state regulatory powers were exercised led to the finding of a serious breach by the state of the fair and equitable treatment standard under the bilateral investment treaty (BIT). The tribunal award stated that the ‘seriousness of the breach shall be duly taken into account when determining the amount of the compensation due to Claimant in that regard’. It appears that, based on this conclusion, the tribunal decided to adjust the expropriation risk component of the discount rate. In particular, the tribunal stated that ‘it is not appropriate to increase the country risk premium to reflect the market’s perception that a State might have a propensity to expropriate investments in breach of BIT obligations.’ The tribunal did not engage the parties’ quantum experts to provide a quantification of the effect of the state’s propensity to expropriate on country risk. Instead, the ‘Tribunal decide[d] to adopt a country risk premium of 4% as used in one of the source documents provided disposition, plus interest to the day of payment. This limitation would only be admissible if the Polish Government had had the right to expropriate, and if its wrongful act consisted merely in not having paid to the two Companies the just price of what was expropriated; in the present case, such a limitation . . . would be tantamount to rendering lawful liquidation and unlawful dispossession indistinguishable in so far as their financial results are concerned. The essential principle contained in the actual notion of an illegal act . . . is that reparation must, as far as possible, wipe out all the consequences of the illegal act and reestablish the situation which would, in all probability, have existed if that act had not been committed’). See Factory at Chorzów (Germany v. Poland), Merits, Judgment, PCIJ (Ser. A) No. 17 (13 Sept. 1928), p. 47.

25 See, for example, Ol European Group B.V. v. Venezuela (ICSID Case No. ARB/11/25), Award, 10 March 2015; Flughafen Zürich A.G. and Gestión e Ingeniería IDC S.A. v. Venezuela (ICSID Case No. ARB/10/19), Award, 18 November 2014; and Gold Reserve Inc. v. Venezuela (ICSID Case No. ARB(AF)/09/01), Award, 22 September 2014. See also Alberro, J., 2016, ‘Should Expropriation Risk Be Part of the Discount Rate?’ Journal of International Arbitration, 33(5), pp. 525–547.

26 Gold Reserve Inc. v. Venezuela (ICSID Case No. ARB(AF)/09/1), Award, 22 September 2014, paragraph 668.

27 Gold Reserve Inc. v. Venezuela (ICSID Case No. ARB(AF)/09/1), Award, 22 September 2014, paragraph 841. Almost without exception, tribunal discussions regarding expropriation risk have been framed around the question of the country risk premium to add to the discount rate to capture expropriation risk. As explained above, this is conceptually problematic – country risk (including expropriation risk) should be accounted for via adjustments to expected cash flows, rather than the discount rate – although the practical complexities of adjusting expected cash flows in this way are acknowledged. That notwithstanding, the tribunal rulings referenced here are informative in that they address the question of the extent to which (rather than how) expropriation risk should be incorporated into an award of compensation.

28 Gold Reserve Inc. v. Venezuela (ICSID Case No. ARB(AF)/09/1), Award, 22 September 2014, paragraph 842.
by the claimant’s quantum expert, and explained that it accepted the respondent’s quantum expert explanation that this ‘premium appropriately considers political risks, together with other risks, but has not been over-inflated on account of expropriation risks’.  

There were two main questions that the tribunal believed needed to be taken into account. First, had the expropriation policy enacted by the state led to an effective increase in the expropriation risk between the time Gold Reserve undertook its investment and the time the state expropriated Gold Reserve’s investment? If the answer to this question is no, excluding the expropriation risk might lead to an excessively low discount rate, which, in turn, would lead to an overvaluation of the investment. Second, is it reasonable to assume that a sophisticated investor, such as Gold Reserve, would evaluate the existence of expropriation risk – among other political risks – when undertaking its investment decision in an emerging market country such as Venezuela? If the answer to this question is yes, excluding the expropriation risk in its entirety might lead to an excessively low discount rate, which, in turn, leads to an overvaluation of the investment.

V ACCOUNTING FOR EXPROPRIATION RISK – SOME PRACTICAL CONSIDERATIONS

Given that quantum experts and tribunals face the challenge of measuring expropriation risk, and incorporating this risk into valuations and compensation, an obvious question to ask is how this is actually done in practice. A recent academic article tabulates a number of widely used methods for addressing the question of how to adjust the discount rate to reflect country risk and, 30 based on anecdotal evidence and a review of arbitral practitioner publications, 31 it appears that the vast majority of the approaches used to account for expropriation risk are based on these methods. In other words, it appears that many quantum experts bring expropriation risk into the picture by adjusting the discount rate using methods that were developed to address country risk. This is potentially problematic for a number of reasons. First, as noted earlier, expropriation risk is only one component of country risk – to the extent that a given method leads to a risk premium that covers components of country risk other than expropriation risk, this may lead to an inappropriately high discount rate, and an inappropriately low valuation. Second, the methods themselves (as noted by Bekaert et al. (2016))32 are created and modified *ad hoc*, and are therefore based on strong assumptions. Third, the methods all involve adjustments to the discount rate, whereas (as noted earlier) country risk should ideally be accounted for through adjustments to expected cash flows.

This clearly puts a quantum expert into a difficult position. Valuation is a practical endeavour, and the fact that the conceptually ‘pure’ approach cannot be implemented does not mean that he or she should simply throw up his or her hands and admit defeat. Rather, a pragmatic approach is needed whereby there is a clear identification of the risks that the expert

29 Gold Reserve Inc. v. Venezuela (ICSID Case No. ARB(AF)/09/1), Award, 22 September 2014, paragraph 842.
32 ‘Over time, several *ad hoc* modifications to the base case were proposed.’ See Geert Bekaert, Campbell R. Harvey, Christian Lundblad, and Stephan Siegel (2016). ‘Political Risk and International Valuation’. *Journal of Corporate Finance* 37, pp. 1–23 at p. 4.

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is seeking to incorporate into the valuation, followed by a careful qualitative consideration of how closely the various available methods match what the quantum expert is looking to do. In other words, it may be that in many cases, there is no practical alternative to addressing expropriation risk via the discount rate, and that the best a quantum expert can do is identify the risk premium that best accounts for the degree of expropriation risk that is to be included in the valuation.

With that in mind, we now summarise the various approaches to determining a country risk premium – these include different variants of the sovereign spread model, the use of country credit ratings and the use of political risk sovereign spreads.

The starting point for the models that are based on sovereign spreads is, unsurprisingly, the sovereign spread itself – namely, the difference between the yield on a bond issued in US dollars by the host country in which the project is located and a US Treasury bond with similar maturity. The first variation of this model was introduced by Mariscal and Lee (1993), and several *ad hoc* modifications of this approach were made thereafter by Mariscal and Dutra (1996), Godfrey and Espinosa (1996), Mariscal and Hargis (1999), Damodaran (1999 and 2003), Zenner and Akaydin (2002), and Abuaf (2015). For example, Mariscal and Dutra introduced an adjustment to the sovereign spread by multiplying it by the ratio of the volatility in equity returns in the country at issue and the volatility in equity returns on the world or US markets. Godfrey and Espinosa proposed a similar adjustment, but in the attempt to reduce the potential double counting of political risk, they used a downward adjustment of 60 per cent. Damodaran (1999) proposed adjusting the sovereign spread by multiplying it by the ratio of the volatility in equity returns and the volatility in bond returns in the country at issue, arguing that risk premiums on bonds have to be adjusted upward to be similar to risk premiums on equity. However, it has long been recognised that a sovereign spread reflects a number of local macroeconomic factors and fiscal conditions beyond political spreads. Therefore, these methods cannot be directly used to measure political or expropriation risks. A similar critique can be levied against the country credit rating model developed by Erb, Harvey and Viskanta (1996). This model focuses on the use of credit ratings, which are assumed by these authors to be a proxy for country risk. Specifically, the model empirically estimates the relationship between equity returns and country credit ratings published by *Institutional Investor*. The results of this empirical analysis are then used to estimate country risk premiums.
Perhaps the most promising approach to identifying the risk premium to be added to the discount rate is to use the concept of the political risk sovereign spread proposed by Bekaert, Harvey, Lundblad and Siegel (2014). This is based on a framework that allows for the disaggregation of that element of the sovereign spread that arises from political risk. However, even this framework does not allow for the separation of expropriation risk from political risk.

VI CONCLUSIONS

There is no question that measuring expropriation and country risks are two of the most challenging issues faced by quantum experts in international arbitrations, and that a careful balance needs to be struck between what is conceptually appropriate and what is practically feasible.

There are three key takeaways from this chapter:

a The extent to which expropriation risk should be incorporated into a valuation that is to be used as a basis for an award of compensation is a legal question – the job of the quantum expert is to ensure that his or her valuation comports with the answer to this question.

b Expropriation risk is a subset of country risk – consequently, methods used to address country risk need to be reviewed carefully before being adopted to address questions relating to expropriation risk, with a failure to do so likely leading to a biased estimate of expropriation risk, an inappropriate discount rate and an unreliable valuation.

c Addressing either expropriation risk or country risk via the discount risk is conceptually problematic and, to the extent possible, these risks should be accounted for via adjustments to expected cash flows. To the extent that this is not possible, the expert should strive to reduce the element of ad hoc subjectivity in the approach taken and to match any adjustment to the discount rate as closely as possible to the risks he or she is seeking to capture.

38 In other words, ‘the political risk spread takes the fraction of the predicted value for the sovereign spread accounted for by the political risk . . . and multiplies it with the current sovereign spread. The computation . . . embeds up to date information from the forward looking sovereign spread at the same time as the current information in the current political risk rating in a particular country (relative to the U.S.).’ See Geert Bekaert, Campbell R. Harvey, Christian Lundblad, and Stephan Siegel (2016). ‘Political Risk and International Valuation’. Journal of Corporate Finance 37, pp. 1–23 at p. 12. Interestingly, this approach can also be couched in terms of the required adjustments to expected cash flows. Barnes, R., 2018, Investor-State Arbitration 2019, Chapter 4: ‘Issues in Cross-Border Valuation and the Implications for Damages Assessments in Investor-State Disputes’, ICLG, 1st ed., pp. 22–23.
Chapter 28

ANNULMENT OF INVESTMENT ARBITRATION AWARDS

Asian International Arbitration Centre

I INTRODUCTION

The finality of the award is one of the main features associated with arbitration. It is based on the general principle that arbitral awards are not subject to review on the merits. Generally, the correctness of the award is subordinate to its finality. However, like all general principles of law, its operation is defined by limited exceptions, such as found in the remedy of annulment.

II DISTINGUISHING BETWEEN ANNULMENT AND SETTING-ASIDE APPLICATIONS

Although in terms of procedure there are many similarities between International Centre for Settlement of Investment Disputes (ICSID) and non-ICSID arbitrations, the annulment mechanism is unique to the former.

Particularly, in arbitrations conducted outside the framework of the ICSID Convention, including that under the Additional Facility Rules, awards may be challenged by way of a setting-aside application in national courts at the seat or otherwise resisted at the enforcement stage. Yet, ICSID tribunals' awards ‘shall not be subject to any appeal or to any other remedy’ other than the annulment. The ad hoc committee in CDC v. Seychelles noted:

[The annulment] mechanism protecting against errors that threaten the fundamental fairness of the arbitral process (but not against incorrect decisions) arises from the ICSID Convention’s drafters’ desire that Awards be final and binding, which is an expression of “customary law based on the concepts of pacta sunt servanda and res judicata,” and is in keeping with the object and purpose of the Convention. Parties use ICSID arbitration (at least in part) because they wish a more efficient way or resolving disputes than is possible in a national court system with its various levels of trial and appeal, or even in non-ICSID Convention arbitration (which may be subject to national courts’ review under local laws and whose enforcement may also be subject to defenses available under, for example, the New York Convention).

1 This chapter is based on earlier revisions prepared by Sundra Rajoo, the former director of the Asian International Arbitration Centre (AIAC), with the assistance of Eleo Szulc and Smrithi Ramesh. All have since left the AIAC.

2 Article 53 of the ICSID Convention.

3 CDC Group plc v. Republic of the Seychelles, (ICSID Case No. ARB/02/14), Decision on Annulment, 29 June 2005, at para. 36.
Together with the provisions on the enforcement of awards, the annulment mechanism manifests the self-contained nature of the ICSID regime. The same nature dictates that the grounds for annulment of ICSID tribunals' awards are limited to those set out in the ICSID Convention.

III GROUNDS FOR ANNULMENT

Article 52 of the ICSID Convention specifies that either party may request annulment of the award on any of the following grounds:

a. the tribunal was not properly constituted;

b. the tribunal has manifestly exceeded its powers;

c. there was corruption on the part of a member of the tribunal;

d. there has been a serious departure from a fundamental rule of procedure; or

e. the award has failed to state the reasons on which it is based.

The ad hoc committee in *Wena Hotels v. Egypt* observed:

> These grounds for annulment are enumerated exhaustively... The power for review is limited to the ground of annulment as defined in this provision. These grounds are to be interpreted neither narrowly nor extensively.\(^5\)

As such, more often than not a party seeking annulment of the award would rely on several grounds listed in Article 52 in its application to the Secretary-General. In any event, an *ad hoc* committee is not bound by the scope of the annulment application and can annul the award in whole or in part.\(^6\)

However, an *ad hoc* committee is not authorised to provide its determination of the issues contained in the annulled parts of the award or substitute the reasoning of the tribunal for its own.\(^7\)

A brief analysis of the grounds for annulment is given below.

i Improper constitution of the tribunal

Article 52(1)(a) of the ICSID Convention mirrors other instruments providing for post-award remedies (e.g., Article V(d) of the New York Convention and Articles 34(2)(a)(iv) and 36(1)(a)(iv) of the UNCITRAL Model Law on International Commercial Arbitration). Professor Schreuer notes that Article 52(1)(a) ‘was intended to cover a variety of situations such as absence or invalidity of the agreement between the parties, non-compliance with a nationality requirement or another form of eligibility’.\(^8\)
However, as the procedural irregularities are closely monitored by the Secretariat of the ICSID,\(^9\) this ground is seldom relied on\(^10\) in the annulment proceedings and does not play a role in practice.\(^11\)

### ii Manifest excess of powers

According to Article 52(1)(b) of the ICSID Convention, the excess of powers must be manifest, meaning clear, obvious, easily recognisable or evident, as interpreted by \textit{ad hoc} committees.\(^12\) In addition, some \textit{ad hoc} committees have added the requirement of seriousness or materiality to the outcome of the case.\(^13\)

According to Professors Dolzer and Schreuer, ‘[a]n excess of power occurs where the tribunal deviates from parties’ agreement to arbitrate’.\(^14\) An analysis of annulment decisions’ discussions on this ground indicates that such a deviation is deemed to have occurred when the tribunal either exceeds its jurisdiction or erroneously declines it, or fails to apply the applicable law.

A jurisdictional excess of powers takes place when the tribunal wrongly assumes jurisdiction over a dispute, exceeds the scope of its jurisdiction or erroneously declines its jurisdiction.\(^15\) While deciding on its jurisdiction, the tribunal must consider the jurisdictional requirements set out in Article 25(1) of the ICSID Convention\(^16\) and other requirements as may be set by the relevant treaty or contract.\(^17\) The tribunal is bound to decline its jurisdiction if one or more of these requirements are not fulfilled, even if the parties do not raise jurisdictional objections.\(^18\)

A failure to apply the proper law may take the form of either a total disregard of the applicable law or applying a law other than law determined pursuant to Article 42(1) of the

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\(^9\) ibid., p. 929.

\(^10\) See e.g., \textit{Sempra Energy International v. Argentine Republic} (ICSID Case No. ARB/02/16), Decision on Annulment, 29 June 2010.


\(^12\) Updated Background Paper on Annulment for the Administrative Council of ICSID, 5 May 2016, at para. 82.

\(^13\) \textit{Compañía de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic} (Vivendi I) (ICSID Case No. ARB/97/3, Decision on Annulment of 3 July 2002, para. 86.

\(^14\) ibid., p. 304.

\(^15\) Updated Background Paper on Annulment for the Administrative Council of ICSID, 5 May 2016, at para. 87.

\(^16\) Article 25(1) of the ICSID Convention reads: ‘The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.’

\(^17\) Updated Background Paper on Annulment for the Administrative Council of ICSID, 5 May 2016, at para. 85.

\(^18\) Article 25 of the ICSID Convention.
ICSID Convention. Therefore, a mere error in application of the law may not constitute a ground for the annulment. This is in line with the principle that an annulment is not an appeal, a principle that ad hoc committees routinely stress.

### iii  Corruption

Article 52(1)(c) of the ICSID Convention allows an ad hoc committee to annul the award should it be proved that there was corruption on the part of a member of the tribunal. This ground closely resembles that set out in Article 52(1)(a) and its purpose is to safeguard the integrity of the arbitral process.

### iv  Serious departure from a fundamental rule of procedure

Article 52(1)(d) of the ICSID Convention sets a double threshold for a violation capable of annulment to be found. First, the infringed rule must be of fundamental character. Second, the violation of the rule must be serious.

The requirement of a ‘fundamental rule’ means that only violations of the most important procedural principles may amount to a ground for annulment, such as the right to be heard, impartiality of the arbitral tribunal, equality between the parties, and rules of treatment of evidence and burden of proof, as well as deliberation between the members of the tribunal. Further, a violation has to be serious.

### v  Failure to state the reasons

Article 48(3) of the ICSID Convention states that the award shall consider every issue put before the tribunal and shall state the reason for the tribunal’s decision. This provision is closely connected to Article 52(1)(e) of the ICSID Convention, which gives the ad hoc committee the power to annul the award if the tribunal failed to motivate its award.

The rationale behind the duty to state reasons is to enable the parties to follow and understand the tribunal’s thinking. It is not material whether the tribunal’s reasons are correct or convincing.

A failure to state reasons can take different forms. It may be a total absence of reasons or a failure to deal with every question. Contradictory or frivolous reasons also fall within the notion of the failure to state reason.

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19 Article 42(1) of the ICSID Convention reads: ‘The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable.’
20 Updated Background Paper on Annulment for the Administrative Council of ICSID, 5 May 2016, at para. 90.
21 Article 52(1)(c) of the ICSID Convention.
22 Updated Background Paper on Annulment for the Administrative Council of ICSID, 5 May 2016, at para. 99.
24 Updated Background Paper on Annulment for the Administrative Council of ICSID, 5 May 2016, at para. 105.
IV PROCEDURE

The procedure for annulment of an ICSID award is set in Article 52 of the ICSID Convention and supplemented by the ICSID Arbitration Rules, that apply mutatis mutandis, similarly to Articles 41 to 45, 48, 49, 53 and 54, and of Chapters VI and VII. 26

According to Article 52(2), the annulment application shall be made to the Secretary-General within 120 days of the date the award was rendered. However, when the applicant invokes Article 51(1)(c) of the ICSID Convention (‘corruption on the part of a member of the tribunal’), the 120 day-period starts to run from the date when such grounds were discovered, yet in any event within three years of the date the award was rendered.

As it follows from Article 52(2), only an award can be subject of annulment. Any decision made before the award is rendered, such as decision on jurisdiction or interim measures, must become a part of the award. As such, a party needs to await the award before bringing the application for the annulment. 27

Upon receipt of the application, the chair of the Administrative Council of ICSID shall appoint a three-member ad hoc committee to hear the annulment application. The members of the ad hoc committee are appointed from the ICSID panel of arbitrators, provided that none of the members of the committee:

- have been a member of the tribunal that rendered the award;
- are of the same nationality as any such member;
- are a national of the state party to the dispute or of the state whose national is a party to the dispute;
- have been designated to the panel of arbitrators be either of those states; or
- have acted as a conciliators in the same dispute. 28

The parties' procedural agreements entered into with regard to the arbitration in which the challenged award was rendered will often apply to the annulment proceedings. Yet, during the first session of an ad hoc committee, the parties may diverge from their original agreements. 29

The ad hoc committee may, if it considers that the circumstances so require, stay enforcement of the award pending its decision. 30 Granting a stay of the enforcement may be made subject to furnishing a security. 31

In addition, any of the parties applying for the annulment may also request the Secretary-General for a provisional stay of the award's enforcement. As soon as the ad hoc committee is constituted it shall, if either party requests, rule within 30 days on whether the stay should be continued and, unless it decides to continue the stay, the provisional stay is automatically terminated. 32

26 Article 52(4) of the ICSID Convention.
27 Updated Background Paper on Annulment for the Administrative Council of ICSID, 5 May 2016, at para. 30.
28 Article 52(3) of the ICSID Convention.
30 Article 52(5) of the ICSID Convention.
31 See e.g., Adem Dogan v. Turkmenistan, (ICSID Case No. ARB/09/9), Decision on Annulment, 15 January 2016.
32 Rule 54(2) of the ICSID Arbitration Rules.
When considering the application for annulment, the *ad hoc* committee shall neither interpret the invoked grounds in a restrictive nor a broad manner, rather its interpretation should be appropriate and reasonable.\(^{33}\) There is no presumption in favour of either annulment or validity of the award.\(^{34}\) The annulment of the award is at the discretion of the *ad hoc* committee.\(^{35}\)

According to Article 52(6), if the award is annulled, the dispute shall, at the request of either party, be submitted to new a tribunal for reconsideration.

V  CONCLUSION

Annulment is the exceptional remedy. It is intended to protect the fundamental principles of due process and be balanced against a principle of finality of arbitral awards. As such, annulment is available only on a limited number of grounds expressly provided in Article 52 of the ICSID Convention.

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Introduction

After the duty of the arbitral tribunal has been completed, another fully fledged battle takes place, where winners and losers face the following question: to annul, to enforce or to obstruct enforcement? And how to do it? These concerns may remain subdued during the proceedings, as litigation attorneys are usually more concerned with procedural and substantive law intricacies while the actual enforcement of the arbitral award seems at times a distant goal.

Annulment proceedings in International Centre for Settlement of Investment Disputes (ICSID) cases have increased over 60 per cent during the past decade. However, as official statistics show, less than 5 per cent of them have led to actual annulment of the challenged arbitral award. In terms of the overall defence strategy – especially for the losing party – this shows that the bar for award annulment within the ICSID system is statistically high, hence requiring consideration of counter-enforcement measures in the different nations where assets are recoverable as an alternative path to annulment.

There are currently two main enforcement systems to be taken into consideration. The first is laid down by the 1965 Washington Convention (the ICSID Convention) and the second stems from the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention). The ICSID Convention establishes a multi-layered recognition and enforcement system in Articles 54(1) and 54(3). Article 54(1) states that signatory states should recognise awards as binding, enforcing them as final judgments issued in their own territory. For courts of the host state, this would entail an obligation to proceed to execution of the award as soon as the formal requirements entrenched in Article 54(2) are met.

Article 54(3) of the ICSID Convention, which deals with arbitral awards to be enforced in jurisdictions other than that of the host state, enshrines the law ‘in whose territories execution is sought’ as the applicable legislation for enforcement purposes. In that context,
Enforcement of Awards

it is only natural to find restrictions and constraints arising from public policy, a concept inherent to legal systems worldwide. Therefore, as can be seen in the case of countries more prone to an absolute take on state immunity, public policy considerations are frequently mentioned in decisions denying execution of state assets.

The second enforcement system, the New York Convention, focuses on the law of the country where recognition and enforcement is sought, and the law applicable to the agreement as sources of standards for recognition and enforcement. Parties’ capacity, the validity of the arbitration agreement and compliance with the rules of due process are considered against the backdrop of procedural rules chosen by the parties, and procedural law of the place where recognition and enforcement is sought.

The law of the country where enforcement is sought may obstruct enforcement in seven instances, as per Article V of the New York Convention: there may be a lack of arbitrability of the matters decided in the award (e.g., the arbitration tribunal ruled on non-pecuniary claims); or a public policy violation.

The New York Convention’s system prompts more judicial review if compared with that of the ICSID as it centres the enforcement procedure at the place where enforcement is sought. In every jurisdiction where enforcement is sought there is a chance of judicial review of compliance with the seat’s rules pertaining the procedure.

ICSID’s enforcement standards start from states’ commitment to enforce awards, a constitutive element of the Washington Convention. The rules of the seat of arbitration are immaterial to ICSID’s awards, whereas the legal system of the enforcement venue is more relevant.

In theory, this could create a distinct treatment in terms of which law to apply when dealing with immunity from execution. Despite that, courts tend to observe their national rules (cumulatively with those of the seat, in non-ICSID cases) irrespective of the ‘mode’ of investment award, be it ICSID or non-ICSID. This means that aside from considering award recognition formalities, the standard of review will most likely also take into account the domestic threshold for execution of state assets.

Neither one of the systems could be evaluated as better or worse from the standpoint of compliance, as literature only refers to the alleged outstanding compliance levels of ICSID awards, without providing official figures or audited statistics. Therefore, it is not the authors’ contention that either of the systems enjoys more acceptance than the other.

In common, these conventions leave regulatory space for states to apply domestic rules. In other words, there is not an internationally applicable regime on state immunity, reinforcing the case-by-case profile of enforcement in investment arbitration.

The aim of this article is to reflect on arbitration strategy in light of the prospects for enforcement in different jurisdictions. Comprehending the options and viable ways of entertaining or frustrating enforcement is an exercise that counsel should bear in mind at every moment of contract negotiation or the drafting of arbitration agreements.

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II METHODOLOGICAL NOTE

For the purpose of this analysis, only cases where the respondent is a state will be mentioned, a sample that represents the majority of investment cases. The authors believe that the discussions below are useful for both counsel of an investor-creditor-claimant on execution proceedings and counsel representing a state-debtor-respondent.

Considering enforcement may be broached from the perspective of host country’s national courts or that of the countries where the state (respondent) has assets, this chapter analyses the highlights of the three most-demanded host states and three jurisdictions that traditionally receive such requests for enforcement. It will focus on cases where states’ assets were called into question. Some of the top jurisdictions in that regard were not mentioned owing to professional reservations of the authors.

III JURISDICTIONS OF FREQUENTLY DEMANDED HOST STATES

i Argentina

Argentina is one of the states with most investment arbitration cases, featuring in 60 as respondent and only four as claimant. The large demand is a reflection of the increasing number of ratified treaties involving investment arbitration: it signed 61 bilateral investment treaties (BITs) – 55 of which are still active – 18 treaties with investment provisions – with 12 active — and 19 investment-related instruments. Out of the existing cases, 35.9 per cent were decided in favour of the state and 28.2 per cent in favour of the investor, while the remaining had no winner, were discontinued or are pending. Since 2015, Argentina has been condemned in five cases.7 One is AWG Group Ltd v. The Argentine Republic, filed in 2003 with a claim for US$34.1 million in compensation. On 30 July 2010, the arbitral tribunal sentenced Argentina to pay US$21 million in liability matters.8

On 6 July 2015, after presenting the calculations and the liquidated amount, Argentina presented in the Columbia District Court in the United States a petition to vacate the arbitration award, invoking the 1958 New York Convention.9 On 30 September 2016, Judge Beryl A Howell presented the memorandum opinion, dismissing the arguments challenging one of the arbitrators (which had been appointed by Argentina), and confirming the arbitral award.10 On 3 July 2018, the Court of Appeals for the District of Columbia issued its final judgment.11 At the moment, there is no information on the execution of the values to which the state was condemned.

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Another case, *HOCHTIEF Aktiengesellschaft v. Argentine Republic*, shares similarities with those mentioned above. Having started in 2007, the decision on liability was published on 29 December 2014. Two years later, on 19 December 2016, the arbitral tribunal rendered an award, later contested by the state, which requested its annulment on 25 April 2017. At the present time, the request is pending decision.

In *Suez, Sociedad General de Aguas de Barcelona, SA and Interagua Servicios Integrales de Agua, SA v. Argentine Republic*, started in 2003, the respondent challenged a member of the arbitral tribunal twice. After the award, Argentina acted in the same way as in the previous cases and filed a petition for annulment. The final judgment was published on 14 December 2018.

Another case involving the Suez companies started in the same year but together with Vivendi Universal, SA. Claimants requested US$834.1 million in damages, and the arbitral tribunal rendered an award granting damages in the amount of US$383.6 million. As in the previous case, Argentina challenged a member of the arbitral tribunal, managing to suspend the proceeding until its request was analysed, which took place on 22 October 2007. Again, the challenge was denied and on 9 April 2015 an award was rendered condemning the state to indemnify the claimants. Acting with the same strategy, Argentina then started annulment proceedings arguing the impediment of an arbitrator. On 5 May 2017 the *ad hoc* ICSID Committee formed to decide on the annulment proceeding reaffirmed the competence of the arbitrator. Dissatisfied with the decision, Argentina appealed to the Columbia Court of Appeals in the United States and again the court ruled that ‘Argentina has not satisfied the Act’s or the New York Convention’s elements required to vacate the award.’

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14 ibid.
20 ibid.
In Autobuses Urbanos del Sur SA, Teinver SA and Transportes de Cercanías SA v. Argentine Republic, the arbitral tribunal condemned the state in the payment of a US$320.8 million in damages. After the award was issued on 21 July 2017 the state once again sought its annulment. So far, there has been no decision on the matter.22,23,24

The five cases have undeniable similarities, mainly the state’s strategy to postpone the end of the dispute and, consequently, the enforcement of the award. In addition, all cases arose under the ICSID Convention, pertaining to controversial BITs signed in the early 1990s, a period in which Argentina was believed to undergo an ‘economic miracle’. Finally, after the awards were rendered, the state began annulment proceedings arguing the partiality or lack of independence of one of the arbitrators.

Previously considered an economic powerhouse until a few years ago, the country has since turned victim of a growing economic recession. This has led to legislative changes. Provisions on arbitration and their enforcement in the legal sphere are, more often than not, influenced by politics, and the change from an unorthodox government to an orthodox one has directly impacted arbitration legislation in Argentina. On 1 August 2015, at the end of the mandate of then President Cristina Kirchner, the new Civil and Commercial Code entered into force and changed other laws of civil practice. With the election of the current President Mauricio Macri, legislation was altered once again. With the entry into force of Law No. 27449, which regulates international commercial arbitration, some provisions of the Civil and Commercial Code and the Civil and Commercial Procedure Code were also amended.25

On September 2017, before the new law entered into force, the Minister of Justice and Human Rights, Germán Garavano, announced that the new regulations constituted a fundamental tool to attract foreign investment. The change in the standards would allow Argentina to have uniform rules adapted to international trade, giving legal certainty and incorporating universally accepted principles in arbitration. In the same note, the Minister argued that the resolution of conflicts in international trade needs flexible, fast and reliable tools for the parties, and that the use of state justice is very onerous and slow, and discourages investments when facing market globalisation, which has modified the rules of international competition.26,27

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The new legislation regulating private–public contracts, Law No. 27328, provides that cases opting for arbitration with extension of jurisdiction must be expressly approved by the national executive power and communicated to Congress. The contract may provide that liabilities that should be performed by the contractor must be effective, although not discussed in the arbitration proceeding. In this case, assuming that the administration or the technical consultant designated for that purpose verifies that the contractor has duly fulfilled his or her contractual obligations, all resources obtained by the controversy shall be deposited by the contractor in an escrow account until a final decision is issued on which party is entitled to the values.28

Changes in a short time span make it difficult to understand the new mechanisms created, which can ultimately influence their effectiveness. It is impossible to know whether the recent changes in Argentine law will be sufficient to ensure enforcement in cases where the state is condemned. However, they can potentially attract foreign investors and consequently reduce the economic problems that the country – and investors – has been facing.

ii Russia

Russia has not been considered – since the turmoil surrounding the Yukos case and all arbitration proceedings stemming from it – an arbitration-friendly venue concerning the recognition and enforcement of foreign arbitral awards. However, despite the Yukos ruckus, Russia is still an investment-gathering country, as for most investors the benefits seem to outweigh the risks. In this sense, it is useful for those doing business with Russia to be aware and prepared for the possible challenges they might face when enforcing their arbitral awards in Russian courts.

Russia’s international arbitration law (No. 5338-1) was enacted on 7 July 1993, with its latest amendment on 25 December 2018, which added text to Article 7 (on the definition, form and interpretation of arbitration agreements). This text is largely an adaptation of the 1985 UNCITRAL Model Law on International Commercial Arbitration and governs international commercial arbitration throughout the Russian territory.

In the international trade area, Russia is a party to 79 BITs, 63 of which are in force as at the time of writing. Though signed, the other 16 BITs are not yet in force. Historically, Russia has terminated 5 BITs.29

On the matter of recognition and enforcement of arbitral awards, Russia is a party to the New York Convention and the 1961 European Convention on International Commercial Arbitration.30 Russia (at the time, the USSR) made a reservation in 1960 that the application of the provisions of the New York Convention would only apply to non-parties that granted reciprocal treatment.31 Moreover, despite having signed the ICSID Convention in 1992, Russia is not a contracting party, as it did not ratify the Convention.

31 United Nations. ‘The Union of Soviet Socialist Republics shall apply the provisions of this Convention in respect of arbitral awards made in the territories of non-contracting States only to the extent to which they grant reciprocal treatment.’ Russia: 1960. Available at: http://newyorkconvention1958.org/index.php?lvl=c
Internally, the recognition and enforcement of foreign arbitral awards is a task for Russia's commercial courts, following the provisions of Chapter 31, Articles 241 through 246 of the Arbitrazh Procedural Code (No. 95-FZ) (APC) of 24 July 2002 and its amendments. The legal basis for the enforcement of such awards is the New York Convention. According to Article 244 of the APC, a commercial court may deny recognition and enforcement of a foreign court decision (including arbitral awards) fully or in part if:

- the decision on the law of the state in whose territory it is made has not entered into legal force;
- the party against which the decision was taken was not timely and properly notified of the time and place of consideration of the case, or, for other reasons, could not submit explanations to the court;
- consideration of the case in accordance with international treaties or federal law refers it to the exclusive competence of Russian courts;
- there is a court decision in Russia that has entered into legal force, which is a dispute between the same persons, on the same subject and on the same grounds;
- a Russian court is analysing a case on a dispute between the same persons, about the same subject and on the same grounds that was initiated before the initiation of proceedings in a foreign court, or the court in Russia was the first to take a production statement on the dispute between the same persons, on the same subject and on the same grounds;
- the statute of limitations for enforcing a foreign court decision has expired, and this term has not been restored by the arbitral tribunal; or
- the execution of a foreign court decision would be contrary to the public policy of Russia.

A recent study by the Russian Arbitration Association provides a general overview of the enforcement proceedings in Russian courts, such as their success rate and the most common grounds for rejection. According to this study, between 2008 and 2017, Russian courts received 472 requests for recognition and enforcement of arbitral awards. From this total, 378 were granted, 45 rejected and 49 were not considered owing to various – mostly procedural – reasons. The most cited grounds under Article V of the New York Convention were: violation of public policy (42 cases); lack of proper notice or inability to present the case (34 cases); and excess of mandate by arbitrators (13 cases). These numbers show that Russia could be considered an arbitration-friendly venue when recognising and enforcing arbitral awards. However, as in all statistical analysis, the conclusions must be taken with a grain of salt.

Analysing the rate of granted and rejected applications for recognition and enforcement as it relates to the amount in dispute, a tendency can be found in Russian courts of granting mostly lower amount awards. In cases amounting to less than €1 million, out of the 358 cases judged in Russian courts, 333 were granted recognition, leading to a 93 per cent success rate. However, as the amount in dispute rises, the number of granted applications plummets.


33 Excluding the set of 49 cases that were not considered by courts because of various reasons.
When considering amounts between €1 million and €10 million, Russian courts granted 35 applications out of 46 (success rate of 76 per cent). When values were over €10 million, they granted 10 out of 19 applications (success rate of 52.6 per cent).

On top of that, when considering investment arbitration cases, Russia seems to have failed to honour all publicised awards rendered against it. Further, Russia has challenged the awards at the seat of arbitration and resisted seizure of its assets. Russian officials have also condemned, on the grounds of sovereign immunity, the enforcement of awards against Russian state assets in other jurisdictions.34

Therefore, considering the low success rates of enforcement in Russia regarding high-value arbitrations, parties should prepare themselves to be confronted by common defences raised in the enforcement phase: (1) violation of public policy; and (2) lack of proper notice or inability to present the case. This is especially true of investment arbitrations, as those proceedings tend to involve larger amounts and are, thus, less likely to be enforced.

To avoid possible arguments on violation of public policy, it is useful to: at the contract signature stage, negotiate agreements compliant with provisions of Russian law that could be viewed by Russian courts as mandatory, especially Russian corporate law concerning governance of Russian-based companies,35 even if Russian law is not the applicable law to the contract. Then, if a dispute arises, consider accepting the application of those same Russian law provisions, in place of or jointly with the applicable law to the contract. The same advice goes to the arbitral tribunal. A failure to apply provisions of Russian law deemed mandatory by Russian courts might later negatively affect recognition and enforcement proceedings.

Moreover, to avoid arguments on the lack of proper notice or inability to present the case, it is useful for parties to always keep original delivery receipts of the notice of arbitration and any other key documents of the proceedings sent to the Russian party (or state). A person must assure that documents are sent to both the registered address in the proceedings and the most recent address of the party registered in the Joint State Register of Companies. This correspondence can also be sent directly by a Russian lawyer, who could ask for an official stamp and signature to prove due delivery of the documents. Additionally, it is important to ask for the counterparty to provide an original or certified copy of the power of attorney granted to its lawyer, making sure that the powers contained therein cover all actions made by their counsel, including the receipt of documents.

There are many other ways of increasing the ‘success rate’ of enforcement of awards in Russian courts. The examples presented are only meant to shed some light on the matter.

An alternative to avoid difficulties in recognising and enforcing an award in Russian courts is to avoid Russian courts completely. A considerable number of parties seeking to enforce their awards, especially in foreign investment arbitrations, look for assets of the counterparty outside its home state.36

In Everest et al. v. Russia, Ukrainian companies in the real estate business initiated an ad hoc arbitration proceeding under the 1976 UNCITRAL Arbitration Rules against Russia based on the 1998 Russian Federation–Ukraine BIT. The companies alleged that Russia had

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Expropriation of properties following the 2014 Russian annexation of Crimea. Russia did not participate in any step of the proceedings, instead sending a letter to the Permanent Court of Arbitration stating that it ‘does not recognize the jurisdiction of an international arbitral tribunal at the Permanent Court of Arbitration in settlement of [the claimants’ claims]’. 37 However, the arbitral tribunal informed Russia of every procedural act, including the hearing, sent it all relevant documents, including the minutes of the hearing, and offered it the opportunity to submit its comments. On 2 May 2018, the arbitral tribunal rendered its award on the merits, recognizing that Russia had illegally expropriated the property of the Ukrainian investors in violation of Article 5 of the 1998 Russian Federation–Ukraine BIT. The Ukrainian investors were awarded approximately US$130 million.

The recognition and enforcement proceedings took place in Ukrainian courts. On 5 September 2018, the Kiev Court of Appeal arrested or prohibited the sale of Russian and Russian companies’ shares in financial institutions (especially investment banks) in Ukraine. On 25 September 2018, the Kiev Court of Appeal decided to recognize and enforce the arbitral award. The decision stresses that the issue of recognition and enforcement of a foreign arbitral award does not allow the court to analyze the merits of the case or make any changes in its content, but only to assess if the award is in accordance with the procedural law of the territory in which recognition and enforcement are sought. The Kiev Court of Appeal found no ground to refuse recognition and enforcement of the award under either the New York Convention or Ukrainian law. Russia, represented by its Ministry of Justice, did not file a statement of objection to the court, but again sent a letter restating that it did not recognize the jurisdiction of the arbitral tribunal or its award.

The financial institutions that had part of their shares arrested or were prohibited to sell them in the market – and against whom Ukrainian investors were enforcing their award – appealed to both decisions of the Kiev Court of Appeal. Inter alia, the enforced parties argued that the shares belonged to state-owned companies, and not the Russia.

The case was taken up to the Ukrainian Supreme Court, which issued a decision on 25 January 2019 denying most of the grounds for appeal. It understood that, as the shares of the financial institutions in question were held by state-owned or joint-stock companies, ultimately held by Russia, they could be the target of execution during enforcement of the arbitral award. In the matter of sovereign immunity, the Supreme Court held that Russia had waived its immunity of execution when it signed and ratified the Russian Federation–Ukraine BIT. However, the Supreme Court highlighted that the only shares associated with Russia were amenable to seizure, so as not to interfere with the individual rights of Ukrainian nationals or other foreign parties holding shares in the specific financial institutions. In this sense, the Ukrainian Supreme Court decided that the arbitral award was to be enforced against Russia through the assets it held in the financial institutions established in Ukraine, excluding from it the remaining assets held by Ukrainian nationals or other foreign parties in those institutions.

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iii  Venezuela

Venezuela has seen a dramatic rise in investment arbitration proceedings against it after President Hugo Chávez initiated, in 2007, a series of nationalisations of foreign-owned investments in key sectors of the country's economy, notably oil and mining, but including industries in a variety of areas as well. Until then, the country had been called as a respondent in only four investment arbitration proceedings, even though most of its BITs had entered into effect during the 1990s, at a time when a more mainstream economics-oriented stance was adopted by the Venezuelan government. Only 12 years later, 41 proceedings have been initiated against it — so far.

Though at the beginning of his expropriation agenda Chávez seemed willing to compensate foreign investors, the situation changed as the country's debt continued to increase, and payments for expropriations and other debts (such as bonds and other loans) began to default. The scenario worsened in 2013, after Hugo Chávez died and was replaced by Nicolás Maduro.

As prospects for payments plummeted and Maduro began talks of debt restructuring, investors began movements to seize Venezuela's state-owned assets located in foreign jurisdictions — especially in the United States and Caribbean countries, where the country owns many oil storage and refinement facilities. The Venezuelan government’s two most important foreign assets are in the oil sector: domestic Petróleos de Venezuela SA (PDVSA) and Houston-based Citgo Petroleum Corporation (Citgo). Citgo operates refineries and gas stations in the United States and is Venezuela’s largest foreign asset. Investment award claimants thus find themselves against a larger backdrop of different modalities of creditors – as discussed below – seeking to seize Venezuelan property in foreign nations, in what has been dubbed by observers a ‘race to the bottom’ for the declining Venezuela’s assets.

More recently, in late 2018, Maduro was re-elected president for a second six-year term, in an election process whose legitimacy was questioned by the opposition and dozens of

43 Citgo is controlled via Houston-based Citgo Holding, in turn wholly owned by PDV Holding Inc, a Houston-based subsidiary of PDVSA. This chain-like ownership structure becomes important below.
of foreign spectators. The leader of the opposition at the Venezuelan National Assembly has proclaimed himself president with the support of the US government, many Latin American countries as well as the European Union.

Foreign recognition notwithstanding, de facto power remains in Maduro's hands, who currently has support from the Venezuelan military. In addition, Maduro enjoys the support of Russia and China, major oil-for-loan creditors that may stand to lose if a successor government decides to question the legality of such deals and thus default on their payment. All of this results in a complex web of obligations with important consequences for the liquidity of Venezuela's assets, and thus for investors' ability to reach them through judicial proceedings in either the United States or the Antilles.

Before discussing the impacts of this scenario on the enforcement of investment arbitration awards, however, the variety of credits owed by Venezuela and their relation to the country's assets must be understood. Only then can the rationale behind the current strategies adopted by investors and the venues available for potential litigants be understood.

As mentioned above, the Venezuelan government is the sole owner of PDVSA, and seemingly exercises direct political control of the company. This means that the socialist-inspired policies enacted by Chávez and Maduro have also had direct impact upon the obligations incurred by PDVSA, leading to claims of contract breach that have since given rise to multiple commercial arbitration proceedings. This has led to International Chamber of Commerce awards favourable to companies such as Dutch ConocoPhillips, which managed in May 2018 to obtain favourable rulings in Dutch Caribbean courts (famously asset-seizure friendly) attaching PDVSA's assets in the region – comprising a number of refineries and oil storage facilities. This led to energetic reactions by the Venezuelan government – at the

50 Although Guaidó has signaled he intends to honor the government’s deals with China – Venezuela’s biggest oil consumer market – no such promise has been made to Russia. cf. CBCnews. 'To understand Venezuela's future, look to the bond market, not politics and protest’. 21 Sept. 2018. Available at: www.cbc.ca/news/world/venezuela-oil-debt-refugees-bonds-maduro-1.4807633. Accessed 1 Mar. 2019.
time, PDVSA even withdrew its vessels from Caribbean waters. Months later in August, ConocoPhillips was able to strike a US$2 billion settlement deal with the Venezuelan company, although it is unclear whether PDVSA has been honouring this agreement.

This matters for ICSID award creditors not only because it suggests Venezuela’s Dutch assets are a surefire way to get it to sit at the negotiating table, but also because such assets are likely to be once again pursued by ConocoPhillips as it decides to enforce its recent US$8 billion ICSID award or if the above settlement goes awry – something creditors who have yet to pursue claims or award enforcement proceedings against the country ought to keep in mind, as what little liquid assets it has may soon become unreachable.

As is the case with Citgo, PDVSA’s Caribbean assets are highly valuable to Venezuela, serving as an intermediary point in its oil supply chain to China and India. Ownership of these facilities is, however, also under PDVSA, and not the sovereignty of Venezuela directly. As such, the legal hurdles creditors must overcome to reach them are not significantly more burdensome than those who target Citgo. The main difference is in forum, as Dutch Caribbean assets fall within Dutch jurisdiction, which is apparently more investor-friendly than US courts. As such, though the specifics of investment award enforcement in the US shall be discussed below, the specifics of the Dutch legal system will not be covered.

As with its Antilles assets, the Venezuelan government has remained intent on maintaining control of Citgo in the United States. In late 2016, Citgo and its controlling companies carried out a series of financial acts that seemingly had the net effect of transferring US$3 billion in Citgo assets to Venezuela via PDVSA, as well as pledging 49.9 per cent of PDV Holding Inc’s interest in Citgo to Russian state-owned Rosneft in exchange for a US$2.8 billion loan. The remaining 50.1 per cent of Citgo, in turn, was used to secure PDVSA’s 2020 bonds. The net effect of this has been to take Citgo further outside the reach of potential investors, as both the 2020 bondholders and the Russian government have a

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competing claim over Citgo shares against other asset-seizing creditors. This set of financial moves were questioned in multiple fronts by investment award creditors keen on executing Citgo, including Canadian-based Crystallex and Rusoro Mining.

Next to (secured and unsecured) bond and promissory note holders, Russia and China, stand the 14 or so creditors of ICSID awards against Venezuela — as well as, potentially, the claimants in the 12 currently pending ICSID proceedings, and a number of other investors hurt by expropriation bills who have not yet initiated proceedings against Venezuela. For the latter three categories, the path to enforcement has additional hurdles. For BIT creditors, the only appropriate respondent in an enforcement proceeding before municipal courts is the Venezuelan government — and not PDVSA or Citgo, both of which enjoy a presumption of separateness arisen from their corporate independence. This drastically reduces the number of foreign assets amenable for seizure. Moreover, as Venezuela is a sovereign entity in public international law, it enjoys immunity against the execution of its assets located in foreign states. The same is true for the foreign assets of its ‘instrumentalities’ — namely, PDVSA. Most, if not all, municipal legal systems grant such immunity, and this is the case with US and Caribbean courts.

Faced with the intricate scenario above, an equally complex legal strategy has been employed by ICSID creditors in enforcement attempts, beginning with Crystallex in 2017 and later followed by both Rusoro Mining in 2018 and OI European Group in 2019. In an oversimplification, this strategy works by asserting a claim of PDVSA as Venezuela’s ‘alter ego’, thus overcoming the presumed separation between the two legal entities. In addition, the immunity PDVSA enjoys as an ‘instrumentality’ of Venezuela must be overcome. Both steps are outlined in greater detail below in the analysis of the US BIT award enforcement system.

61 As per First Nat'l City Bank v. Banco Para El Comercio Exterior de Cuba, 462 U.S. 611, 627 (1983) (Bancec): ‘[D]uly created instrumentalities of a foreign state are to be accorded a presumption of independent status’. Indeed, Bolivia has few foreign assets in its name. Its US assets, for instance, are mostly employed for diplomatic uses, which therefore makes them immune as per FSIA.
Another aspect of this discussion is how the Venezuelan legal system treats sovereign immunity. Although state parties may not claim jurisdictional immunity before Venezuelan courts, state assets seemingly enjoy de facto (if not de jure) immunity from execution, requiring the observance of procedural rules entailing a notice to the Venezuelan Attorney General, followed by a 90-day suspension of the enforcement proceeding and the enactment of a ‘plan to ensure the continuity of functionality of the State entity’.66 No reports of enforcement efforts before local courts were found in the authors’ research – which is of little surprise given Venezuela’s stance on foreign enforcement courts.

IV JURISDICTIONS FREQUENTLY SOUGHT FOR RECOGNITION AND ENFORCEMENT OF FOREIGN ARBITRAL AWARDS

i United States

Though governments usually grant each other sovereign immunity as a rule, there is no unified treaty concerning the subject,67 and as such, legal systems have treated immunity in different ways. In general, it is possible to distinguish between absolute and restrictive sovereign immunity. On one hand, a legal system may grant all property owned by a foreign sovereign found inside its territory absolute immunity from enforcement, regardless of the nature or character of the use to which such property is put – such is the case of China, for instance.68 On the other hand, a restrictive immunity system – as in the United States, United Kingdom and most Western nations – customarily works by attempting to outline a principled distinction between assets employed by the foreign government as a sovereign and those exploited in a commercial manner.

According to the 1976 US Foreign Sovereign Immunities Act (FSIA),69 any ‘foreign state shall be immune from the jurisdiction of the courts of the United States’. For this reason, all factual disputes regarding a sovereign immunity defence should be overcome by the court from the outset of an enforcement case – and before any discussions on its merits.


69 Codified at Title 28, §§ 1330, 1332, 1391(f), 1441(d), and 1602–1611 of the United States Code.
can occur. Exceptions to this general presumption are laid out in Sections 1605 to 1607 of the FSIA. Section 1605 is particularly interesting to this discussion. Notably, a foreign sovereign is not immune from US jurisdiction:

a if it has waived its immunity;

b if the action is based:

• 'upon commercial activity carried on in the US by the foreign state';
• 'upon an act performed in the United States in connection with a commercial activity of the foreign state elsewhere'; or
• 'upon an act outside the territory of the United States in connection with a commercial activity of the foreign state elsewhere and that act causes a direct effect in the United States'; or

c if the situation involves 'rights in property taken in violation of international law' and that said property (or its substitute) is:

• present in the United States 'in connection with a commercial activity carried on in the United States by the foreign state'; or
• 'owned or operated by an agency or instrumentality of the foreign state', which is 'engaged in a commercial activity in the United States',

Other exceptions include situations involving damages to assets located in the United States, actions seeking the recognition of arbitration awards and situations linked to terrorism. Exception (c) above (the expropriation exception) is particularly relevant here, as it likely encompasses all cases in which there has been an award recognising expropriation as unlawful (e.g., one of Venezuela's). Still, determining that a potential enforcement target's assets are employed in 'commercial activity' remains a necessity for BIT creditors before US courts. Most systems under a restrictive sovereign immunity regime work with distinctions such as this. The problem is, as always, in the details, and specific systems vary in how they procedurally define 'commercial' and 'sovereign' property usage in enforcement actions. Further, it is not always straightforward in practice to distinguish between the two, as often

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70 This has been made clear by the US Supreme Court in *Venezuela v. Helmerich & Payne International* (581 U.S. (2017): 'Simply making a nonfrivolous argument [that a case falls within a FSIA exception] is not sufficient . . . a court should resolve any factual disputes about a foreign sovereign's immunity defense as near to the outset of the case as is reasonably possible.'

71 Numbers between parentheses match those of statutory text.

72 28 U.S. Code § 1605 (a)(5).

73 28 U.S. Code § 1605 (a)(6).

74 28 U.S. Code § 1605A and 1605B.
an asset may either have mixed uses\textsuperscript{75} or its commercial use may be too tied to the exercise of sovereign power by the foreign country. In Venezuela’s case, PDVSA also enjoys sovereign immunity in virtue of its being an instrumentality of Venezuela under the FSIA.\textsuperscript{76}

More often than not, however, sovereign entities do not hold assets under their own name in foreign countries. As mentioned above, Venezuela holds little more than diplomatic assets in the United States. Its economic interests there are exerted indirectly through its control of PDVSA, which in turn controls PDV Holding Inc, a US-based company who owns all of the interest in Citgo. To reach Citgo’s assets, its BIT creditors must also pierce through PDVSA’s corporate veil. One strategy for this, adopted successfully by Crystallex and others, consisted of claiming PDVSA functions effectively as Venezuela’s alter ego. Briefly, an alter ego claim is possible under two circumstances: when a ‘corporate entity is so extensively controlled by its owner that a relationship of principal and agent is created’, (an extensive control prong), or when the sovereign has ‘abused the corporate form, or where recognizing the instrumentality’s separate status works a fraud or an injustice\textsuperscript{77} (the fraud or injustice prong).

In its claim, Crystallex pursued both arguments, though it only succeeded in meeting the burden to establish its extensive control alter ego allegation. With regard to PDVSA’s involvement in the expropriation process, mentioned by the Canadian company as evidence for its fraud or injustice argument, Judge Leonard P Stark of the Delaware District Court found that its allegations did ‘not sufficiently allege that Venezuela used PDVSA as an instrument to defraud Crystallex’, as Venezuela could have acted in the same manner regardless of PDVSA’s involvement or existence.\textsuperscript{78}

As for its successful extensive control claim, Crystallex was able to demonstrate that Venezuela ‘used PDVSA’s property as its own’, that it ‘ignored PDVSA’s separate status’ and that it required PDVSA to ‘obtain approvals for ordinary business decisions’, showing the instrumentality’s lack of ‘independence from close political control’. These and other closely related factors were sufficient to rebut, before a US district court, a Bancec presumption of separateness. They are not exhaustive, of course. A footnote in Judge Stark’s ruling is enlightening in this regard:

\textsuperscript{75} One famous example is the Swedish Supreme Court ruling that denied recognition of immunity to a set of apartments owned by the Russian government in Högsta Domstolens Beslut [Supreme Court Decision] Ö170-10 in 2011. Although some lots were used to house diplomats and state documents, most were rented for profit, leading to the asset being considered sufficiently ‘commercial’ in usage, and therefore not immune and thus amenable to seizure. cf. Hofverberg, Elin. ‘Sweden: Supreme Court Rejects State Immunity Claim Against Enforcement Measures | Global Legal Monitor’, The Library of Congress, 19 Oct. 2011. Available at: www.loc.gov/law/foreign-news/article/sweden-supreme-court-rejects-state-immunity-claim-against-enforcement-measures/. Accessed 6 Mar. 2019.

\textsuperscript{76} As per the FSIA, (28 U.S. Code § 1603 (b)): An “agency or instrumentality of a foreign state” means any entity – (1) which is a separate legal person . . . (2) which is an organ of a foreign state or political subdivision thereof, or a majority of whose shares or other ownership interest is owned by a foreign state or political subdivision thereof” (3) who is not a citizen of the United States. For this reason, US-based subsidiaries of PDVSA PDV Holding Inc and CITGO Holding, are not immune under the FSIA.

\textsuperscript{77} Letelier v. Republic of Chile, 748 F.2d 790, 794 (2d Cir. 1984).

\textsuperscript{78} See Justice Stark’s August 9, 2018 Opinion for United States District Court for the District of Delaware - Case 1-17-mc-00151-LPS (14 August 2017).
The pertinent factors are not exhaustive – the Court can (and does) consider other factors, and not every factor need be present – nor are they mutually exclusive, as many of them overlap. Reasonable minds will differ as to the category into which to place any specific allegation or evidence.

Although other strategies for piercing the corporate veil of a foreign state’s instrumentality may be available, the alter ego claim has been employed with success by Venezuela's BIT creditors in the United States. Both Crystalex and Rusoro were able to strike payment agreements with Venezuela after attaching Citgo’s assets. In their particular cases, it is unclear yet whether this will suffice, as Crystalex has raised a breach claim against Venezuela after PDVSA filed an appeal against the Citgo attachment – its counsel alleging that ‘PDVSA is not a party to a settlement with Crystalex’. On the other front, Venezuela's payment of Rusoro's agreement has been hampered – ironically – by US sanctions against Venezuela. Additionally, the aforementioned securitisation of Citgo’s shares to bondholders and Rosneft – both of which have asked to intervene in various of these enforcement proceedings – place doubt on the ultimate efficacy of attaching assets that have been previously used to secure other deals.

ii United Kingdom

Restrictive immunity is a standard in the United Kingdom as per its 1978 State Immunity Act. Granting or refusing to grant the execution of an asset owned by a foreign state will depend largely on the underlying transaction that originated the dispute and the arbitral award thereafter. In addition, the 1982 Civil Jurisdiction and Judgment Act sets out further conditions for the enforcement of foreign judgments via a multi-tier test.

In addition, the United Kingdom is also a contracting state of the 1972 EU Convention on State Immunity. The cases selected for this overview relate to both intra-EU disputes and disputes between EU and non-EU members.

In NML v. Republic of Argentina, the UK Supreme Court revisited the tenets of the State Immunity Act to determine whether enforcement admissibility required an analysis of legality of the foreign judgment itself (according to English standards) or of the underlying transaction. Justice Blair, recounting the historical development of the doctrine of execution of foreign awards, implemented a test based on Article 32 of the 1982 Civil Jurisdiction and Judgment Act. If and only if the award is equally admissible against a hypothetical

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83 As at the time of writing, the United Kingdom is still member of the European Union.


85 The following is said provision in full: ‘(1) A judgment given by a court of an overseas country against a state other than the United Kingdom or the state to which that court belongs shall be recognised and enforced in the United Kingdom if and only if: (a) it would be so recognised and enforced if it had not
private party, may any such award be enforced. Those conditions were satisfied and, as a result, by majority, the New York judgment was enforced against Argentinian assets in the United Kingdom.

In deciding which type of asset is subject to enforcement, in the Orascom case, the English court asserted that oil shares held in an account were not immune to execution. As pointed out by observers, UK case law underpins the necessity of separating which assets are used to carry out consular, governmental or other sovereign activities of the state, and which ones are employed in commercial use.

Mixed use of the same bank account for commercial and sovereign uses, for instance, has raised major concerns. In the United Kingdom, the High Court in the Alcom v. Republic of Colombia case did not execute such accounts, in accordance with Article 14 of the State Immunity Act, which proscribes execution of a number of properties from the list of executable items.

In ICSID case Micula v. Romania, investors filed for enforcement at the High Court in London after untroubled proceedings. Nevertheless, Romania and the European Commission attempted to set aside the enforcement on the ground that the award would not be compatible with EU law.

Romania became a Member State of the European Union in 2007. The 2013 award ruling in the claimant's favour would allegedly amount to ‘state aid’. This final understanding of the European Commission was appealed by Swedish company Micula and final review is still pending. The vexata questio was the following: should enforcement attempts be halted until the General Court of the European Union's decision?

iii France

France evolved from an absolute approach to state immunity to a more restrictive approach. Aside from the 1972 European Union Convention on State Immunity, other provisions on that subject are found in the Sapin II Law and in the French Monetary and Financial Code.

France is also a contracting party to the 2004 UN Convention, which the Court of Cassation has been citing as a source even though it has not yet entered into force.

been given against a state; and (b) that court would have had jurisdiction in the matter if it had applied rules corresponding to those applicable to such matters in the United Kingdom in accordance with sections 2 to 11 of the State Immunity Act 1978.’


The same seems to be true of Dutch courts, even though the Netherlands have not signed the UN Convention.

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Traditionally a *favor arbitrandum* jurisdiction, France has a cautious approach with respect to the execution of state-owned assets, with a certain degree of fluctuation. In the case *Commisimpex v. Democratic Republic of Congo*, the French Supreme Court\(^93\) reinstated the necessity of not only referring to an explicit prior consent by the state regarding execution, but also drawing a specific list of assets that may be subject to recovery. The underlying assumption is that any waiver of rights should be clearly stated and this standard of interpretation, which may be found in private matters, should also be extended to foreign states (Article L.111-1-2, Sapin II Law).

At last, the French Supreme Court has reverted the stay in the enforcement of an arbitral award issued under an Energy Charter Treaty (ECT) bilateral investment agreement between Ukraine and Moldova in an April 2018 ruling. No mention to EU law was made, as the main issue was the Paris Court of Appeal’s attempt to extend the definition of the ECT under the treaty.

V EU LAW COMPATIBILITY WITH DISPUTE RESOLUTION IN INVESTMENT CASES POST-ACHMEA

The discussion is not new and since 2015 the European Commission has been targeting Intra-EU BITs, in an effort to persuade states to terminate them. Currently, there are currently approximately 190 intra-EU BITs.\(^94\) Infringement proceedings were launched against the Netherlands, Sweden, Slovakia, Austria and Romania to frame those countries for continuing to use the BIT investment regime and, in 2018, the European Court of Justice completed the circle, via its decision of *Slovak Republic v. Achmea* case.\(^95\) Confirming the European Commission’s understanding, the European Court of Justice stated that arbitral tribunals cannot ensure a stable and uniform interpretation of the principles governing allocation of powers in the European Union.

The investment arbitration model created by said intra-EU BITs, in that sense, would be in violation of Article 344 of the Treaty on the Functioning of the European Union. Deferring jurisdiction to arbitral tribunals was not deemed an acceptable way to ascertain rights and obligations in a fully effective manner under EU law.\(^96\)

As a consequence, even an arbitral tribunal’s decision, despite all textbook characteristics normally attributed to an arbitral award, started to be challenged and reviewed by the

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European Commission. This is the situation in Micula, in which the European Commission is seeking to prevent Romania from collecting any amount of the award under the argument that any such payments would constitute illegal state aid according to EU law.97

Legal certainty is a major concern for investors as the process of regulatory enlargement of the European Union seems to be taking a toll on investor–state arbitration’s efficiency. In this context, the proposal of the creation of a multilateral investment court, which should in the near future replace the investment arbitration system by a European-based model, fits the European Commission’s ambition to perfection.

Though it may seem reasonable to conclude that the scope of a full-blooded European system of dispute resolution would only cover intra-EU investments, it remains to be seen whether a multilateral investment court will not outgrow its competence – as the European Commission’s brief explanation suggests – and institutionalise the application of EU law beyond its borders. It is also subject to much speculation whether the court will have any competence in respect of enforcement initiatives, something that has the potential to completely deplete the sovereign powers of EU Member States regarding execution of state-owned assets.98 There are striking policy concerns, both for EU Member States and developing countries, involved in the supranational effects of this multilateral court.

In the coming months, more mobilisation around this theme is expected. However, for the time being – at least in Europe – the effects of the Micula and Achmea cases have only gone as far as to halt proceedings in countries where enforcement of intra-EU BITs awards were sought.

VI CONCLUSION

Regarding the recognition and enforcement of arbitral awards in foreign forums, companies (especially their counsels) must always be aware of the political and economic circumstances surrounding their case, as those may play an important role in the success rate of their enforcement attempt. Moreover, alternative strategies, such as executing the counterparty’s assets outside its home state should also be taken into consideration.

Most companies believe that, in the realm of international arbitration (be it commercial or investment), after a dispute with a business partner arises, reaching a final decision on the matter – and getting your rights recognised – would lead to a peaceful resolution. However, as can be seen from the issues and cases presented above, recognising and enforcing an arbitral award in another jurisdiction can prove to be a rather difficult journey.

This is the reason why private entities should carefully consider not only their choice of counsel in the arbitration proceedings and their appointed arbitrator, but also their counsel on the recognition and enforcement proceedings. These often-forgotten individuals are a key component in the attainment of the companies’ rights and, of course, their money.

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Part VII

MULTI-LATERAL TREATIES
I INTRODUCTION

While investment arbitration remains a ‘hot topic’ in international politics and the negotiation of free trade agreements is overshadowed by disagreements about chapters on investment protection, the practice of investment arbitration continues. It remains a popular means for investors worldwide to seek the protection of their rights under bi- or multilateral investment treaties. This holds especially true for the Energy Charter Treaty (ECT), which in 2018 again saw a big influx of new cases and remains the international investment agreement most used by investors.

In the past, the prominence of the ECT could be explained by its geopolitical and economic origin. At times, it protected investors in the highly profitable but also often strictly governed energy sectors, especially after the breakdown of the Soviet Union, when several countries had regained – for the first time in decades – sovereignty over their natural resources.

However, in the past few years, the key factor for the activity surrounding the ECT is its availability for investors in the solar energy sector to challenge the revocation of incentives states had granted to them during the 2000s. The number of cases brought by investors is still expanding, with Spain and Italy still being the most targeted states.

Fittingly, this chapter’s 2017 edition dealt with the awards rendered in the Isolux Infrastructure Netherlands BV v. Spain and the Blusun SA, Jean-Pierre Lecorcier and Michael Stein v. Italian Republic arbitrations. Though factual background and arguments will still be different on a case-to-case basis, the legal reasoning is similar. The reader is invited to turn to the 2018 chapter, which dealt with substantial issues of solar claims. This year, one of the most controversial judgments of the decade forced arbitral tribunals tasked with deciding solar claims against Spain and Italy to deal with a whole other animal: European Union law.
With its judgment of 7 March 2018 in Slovak Republic v. Achmea BV, the Court of Justice of the European Union (CJEU) turned the arbitration world in Europe upside down.8

There are several reasons why the Achmea judgment is of particular importance to the ECT. First, it may be argued that the Achmea judgment is not that surprising in what it explicitly states, but in what it implies. Although the ECT is not mentioned in the judgment, its potential implications on the application of the ECT remain subject to debate. Second, besides its legal implications, its effect on the investment climate — especially given the created uncertainty by the Achmea judgment — is significant. A number of claims initiated against Spain and Italy after the Achmea judgment may have been guided by the awareness of investors to act quickly before the Member States of the European Union start to implement the Achmea judgment, which might also involve changes to the ECT.9

This year’s chapter will also deal with a second objection to the jurisdiction of tribunals constituted under the ECT, which is becoming increasingly frequent: the tax carve-out in Article 21(1) of the ECT.10 In fact, most of the solar claims include the submission of a breach of the ECT through tax on the value of the production of electrical energy.11 This chapter sheds some light on how the 2018 awards rendered under the ECT have dealt with the tax carve-out and taxes on the merits.

II THE ECT AND AN OVERVIEW OF ITS INVESTMENT PROTECTION REGIME

The ECT12 is a multilateral treaty with its inception and origin dating from the early 1990s. The breakdown of the Soviet empire, the fall of the Berlin Wall and the following reunification of Germany led to a general reconfiguration of east–west relations. Russia and its eastern European neighbours’ richness of energy resources combined with western Europe’s general anxiety to diversify its sources of energy supply led to an initiative by the European Communities to establish a new legal basis of commercial relations in the energy sector.

In 1991, both western and eastern European states signed the European Charter, the political foundation of the ECT and as such a non-binding declaration of principles, including guidelines for the negotiation of a subsequent binding treaty. The result of the ensuing negotiations was the conclusion of the ECT, which was signed in December 1994 and entered into effect in April 1998.13

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9 Compare the declaration by 22 of the 28 Member States regarding the implementation of the Achmea judgment.
10 See, in particular, the awards at p. 5.
11 See e.g., Foresight et al. v. Kingdom of Spain, SCC Case No. 2015/150, Award, paras. 223 et seq.
13 As at the time of writing, 52 states have signed the Energy Charter Treaty. All EU Member States are individual signatories, but the Treaty has also been signed collectively by the European Union and Euratom bringing the total number of parties to the Treaty to 54, although five of these states have not ratified the Treaty yet. Belarus expressly applies the Treaty provisionally.
The following is an overview of the ECT’s most pivotal provisions, limiting itself to Article 13 (i.e., the protection against undue and uncompensated expropriation), Article 10(1) (guaranteeing fair and equitable treatment (FET)) and Article 26 of the ECT (i.e., the dispute settlement mechanism under the ECT).

i Protection against direct or indirect expropriation under the ECT

The ECT follows the standard under customary international law and investment treaty practice and does not per se prohibit expropriation – whether it be ‘direct’, by transfer of legal title, or ‘indirect’ by measures doing without the transfer of legal title, leading to a substantial loss of control or economic value. The ECT recognises a host state’s right to expropriate the property of investments made in that state by investors but predicates the lawfulness of the expropriation on the conditions set out in Article 13(1):

Investments of Investors of a Contracting Party in the Area of any other Contracting Party shall not be nationalised, expropriated or subjected to a measure or measures having effect equivalent to nationalisation or expropriation (hereinafter referred to as ‘Expropriation’) except where such Expropriation is: (a) for a purpose which is in the public interest; (b) not discriminatory; (c) carried out under due process of law; and (d) accompanied by the payment of prompt, adequate and effective compensation.

Such compensation shall amount to the fair market value of the Investment expropriated at the time immediately before the Expropriation or impending Expropriation became known in such a way as to affect the value of the Investment (hereinafter referred to as the ‘Valuation Date').

Such fair market value shall at the request of the Investor be expressed in a Freely Convertible Currency on the basis of the market rate of exchange existing for that currency on the Valuation Date. Compensation shall also include interest at a commercial rate established on a market basis from the date of Expropriation until the date of payment.

For the purpose of determining a breach of Article 13(1), tribunals will simply try to establish: (1) the transfer of title or a measure having the same effect; (2) whether the transfer was made for a public purpose; (3) whether the transfer was conducted in a non-discriminatory manner; (4) whether the transfer was carried out under due process of law; and (5) whether the transfer was followed by payment of adequate and prompt compensation.

In the context of expropriation, tribunals are inclined to not only take into account the effect of the measure, but also the purpose, the manner and context in which the state acted (the ‘police powers doctrine').

ii Guarantee of FET under the ECT

The FET clause of the ECT can be found in sentence 2 of Article 10(1), which, in its pertinent parts, reads:


15 Saluka Investments BV v. The Czech Republic, Permanent Court of Arbitration, Partial Award, 17 March 2006. However, the ECT itself is silent on the question of whether requirements other than those listed in Article 13(1) are to be included in a tribunal’s analysis.
Each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area. Such conditions shall include a commitment to accord at all times to Investments of Investors of other Contracting Parties fair and equitable treatment. Such Investments shall also enjoy the most constant protection and security and no Contracting Party shall in any way impair by unreasonable or discriminatory measures their management, maintenance, use, enjoyment or disposal. In no case shall such Investments be accorded treatment less favourable than that required by international law, including treaty obligations. Each Contracting Party shall observe any obligations it has entered into with an Investor or an Investment of an Investor of any other Contracting Party.

As a result of the generally broad and unspecific definition of the FET standard, a great range of attempts to define the standard exist. Over the years, jurisprudence made clear that to find the FET standard violated, it is of the greatest importance to assess the specific factual elements of the state’s conduct with regard to the investor.

Based on this analysis, tribunals will analyse, *inter alia*, whether the state acted in accordance with its representations of a stable and predictable business, and legal environment.\(^\text{16}\)

As indicated above, any analysis of the FET standard under the ECT is first and foremost based on the facts of the case. There are certain indications on which tribunals place special importance. For example, not every violation of the host state’s law is a violation of the FET standard.\(^\text{17}\) However, changes in the legal framework of the investment have to be communicated and applied in a transparent, non-arbitrary manner and with consistency. Otherwise, the host state’s conduct may very well be an infringement of the investor’s rights under Article 10(1).

As stated by Dolzer:

> Inconsistent conduct by the host state confuses the investor, stands in the way of proper planning, and is not conducive to an investment-friendly climate. Not surprisingly, arbitral tribunals have confirmed that inconsistency of conduct by the host state, as regards the investor’s obligations, is not compatible with the requirement of FET.\(^\text{18}\)

Prominently featuring in the discussions on investment arbitration, the issue at heart is the host state’s ‘right to regulate’. The jurisprudence on the ECT has not developed consistent case law in dealing with this matter. Rather, the decisions may be divided into two categories.

A narrower approach demands that expectations must be based on clear and concrete assurances from the host state expressed in direct communication aimed at the investor regarding the specific business or relationship.

The more flexible approach only requires the investor to prove that it identified a basis for its expectations in generally applicable laws – namely the legal and regulatory framework that existed at the time of making the investment.

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\(^\text{16}\) Schreuer, footnote 14.

\(^\text{17}\) ibid.

When balancing investor rights and the host state’s right to regulate, tribunals will, however, accord to states a right to change policies over time.\(^\text{19}\)

As stated by Dolzer:

*Consistency may not be required under circumstances in which the host state had convincing reason to change course. As regards its legislative power, the host state will, in principle, have the right to pursue its interests in the light of the new circumstances, but not ignore the interests of the investor who had earlier adjusted his conduct to the previous course required by the host state. The power to regulate operates within the limits of rights conferred upon the investor. Correspondingly, it will have to be assumed that the reversing of a position in a dramatic manner with serious negative effects upon the investor will be consistent with FET only in the presence of serious exceptional reasons, compelling the host state to reverse its previous decision and to require the investor to re-adapt its business.*\(^\text{20}\)

As stated by Patrizia et al:

While the existing arbitral decisions on claims asserted under the ECT do not provide clear guidance, arbitral decisions applying other investment treaties indicate that tribunals will examine the specific circumstances of each case when considering whether the investor’s expectations were reasonable under the FET standard. The tribunals . . . will likely consider, on a case-by-case basis, the conduct of the state as a whole, including whether the state made any specific assurances to investors and the reason for, and form of, the changes in legal framework, as well as any other circumstances surrounding the investment.\(^\text{21}\)

### iii Dispute settlement under the ECT

The dispute settlement mechanism of the ECT is enshrined in its Article 26(1), which sets out that disputes between ‘a Contracting Party and an Investor of another Contracting Party relating to an Investment of the latter in the Area of the former’ shall be resolved amicably. If an amicable resolution of the dispute cannot be reached within three months, the investor is entitled to submit the dispute to either the national courts or administrative tribunals of the contracting party, the forum previously agreed by the parties or international arbitration. Should the investor choose to submit the dispute to arbitration, the investor will face the decision of whether it wants the case to be administered under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention),\(^\text{22}\) *ad hoc* arbitration under the UNCITRAL Arbitration Rules or arbitral proceedings under the Arbitration Institute of the Stockholm Chamber of Commerce (SCC).


\(^{20}\) Footnote 18.

\(^{21}\) Patrizia et al, op cit, footnote 15, pages 78–79.

\(^{22}\) If one but not both of the host state and investor’s state have not ratified the ICSID Convention, the investor may elect arbitration under the ICSID Additional Facility Rules.
iv The provisional application of the ECT

Because of its immediate implications in practice, it is worth taking a look at Article 45(1) of the ECT regulating the treaty's provisional application. Article 45(1) reads: 'Each signatory agrees to apply this Treaty provisionally pending its entry into force for such signatory in accordance with Article 44, to the extent that such provisional application is not inconsistent with its constitution, laws or regulations.'

The following paragraphs of Article 45 set out the regulatory framework for a declaration to not apply the Treaty provisionally (Article 45(2)) or to terminate the provisional application once a state has subjected itself to it (Article 45(3)). Article 45 follows the international standard of multilateral treaties and economic-related treaties of being applied provisionally, while containing quite elaborate language. Indeed, when comparing Article 25 of the Vienna Convention on the Law of Treaties (VCLT) with Article 45 of the ECT, the sophisticated wording of the latter is striking.

v The ECT's tax carve-out

One of the ECT’s provisions that features heavily in solar claims as well as other proceedings is the tax carve-out. Article 21(1) of the ECT provides that: 'Except as otherwise provided in this Article, nothing in this Treaty shall create rights or impose obligations with respect to Taxation Measures of the Contracting Parties.' Therefore, the provision effectively seeks to carve out measures relating to tax from the ECT’s investor protection regime.

However, Article 21(5) of the ECT stipulates that Article 13, protection against unlawful expropriation, still applies to taxes. In this case, a special regime applies. Article 21(5) of the ECT requires the investor to refer the issue of whether the tax amounts to an expropriation or is discriminatory to the competent tax authority of the host state.

Tribunals are split over the question of whether this stipulates a compulsory requirement for the investor to fulfil before initiating arbitral proceedings. In Plama v. Bulgaria, the tribunal ruled that it was, in fact, a compulsory requirement.\(^\text{23}\) The tribunal in Yukos et al. v. Russia came to the opposite conclusion for cases where referral to relevant authorities would be an exercise in futility.\(^\text{24}\) In addition, Article 21(1) of the ECT does not apply, according to the Yukos et al. v. Russia tribunal, if the alleged action does not constitute a bona fide exercise of a state's regulatory powers.\(^\text{25}\)

III THE ECT CASES OF 2018

The table below contains decisions of arbitral tribunals that emerged during 2018 and up to the time of writing.\(^\text{26}\) Of the 10 decisions, the investor emerged victorious in eight of them.
IV  A CLOSER LOOK AT THE 2018 ECT DECISIONS

The following is a closer look at the impact of the Achmea judgment on the ECT. As all awards rendered against European states dealt with this issue, the analysis will, instead of looking at each case individually, provide an overview of the general notions that the tribunals applied to assess the potential impact of Achmea.

i  The intra-EU objection and the CJEU’s Achmea judgment

In 2008, the Dutch insurance company Achmea BV (formerly known as Eureko BV) commenced an arbitration against the Slovak Republic under the Dutch–Slovakian bilateral investment treaty (BIT) claiming compensation based on the state’s repeal of the liberalisation of its healthcare market.27

In its 2012 award, the tribunal constituted under the UNCITRAL rules found the state in breach of the FET standard and awarded Achmea damages in the amount of €22.1 million.28 Slovakia decided to bring set-aside proceedings before the Higher District Court of Frankfurt of Main, Germany, the court of the seat of the arbitration. The Higher District Court rejected all of Slovakia’s arguments, which had, inter alia, argued that the tribunal lacked jurisdiction over the dispute because the BIT’s arbitration clause was incompatible with EU law.29

On appeal, the German Federal Court of Justice made use of its power under Article 267 of the Treaty on the Functioning of the European Union (TFEU) and referred several questions to the CJEU, including the question on the compatibility of the ECT’s arbitration clause with EU law.30

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28  ibid., paras. 283 and 352.
29  Judgment of the Higher Regional Court of Frankfurt (German), 18 December 2014, paras. 33, 50–57.
30  Decision of the German Court of Justice, 3 March 2016.
The starting point for the CJEU’s judgment is its understanding of the primacy and uniform application of EU law, which Member States, including their domestic courts, are obliged to enforce. Member State courts, especially, as noted by the CJEU, are given the opportunity through Article 267 of the TFEU to resolve potential conflicts between national and EU law by referring questions in cases before them to the CJEU.

The CJEU then went on to find that an arbitral tribunal constituted under a BIT might have to rule on matters of EU law where, based on the text of the BIT, it must apply the law of the respondent state, which automatically also includes EU law. A potential safeguard against possible divergent judgments and awards was supported by Advocate General Wathelet in his opinion. He stated that the arbitral tribunal enjoyed the power of requesting a ruling from the CJEU on referred questions, as the arbitral tribunal constituted a ‘court or tribunal of a Member State’ pursuant to Article 267 of the TFEU.

The CJEU departed from these considerations of its Advocate General and held that an arbitral tribunal constituted under the BIT is outside of the jurisdiction of the European Union and its Member States, this being the reason for the existence of the arbitration clause in a BIT in the first place. Accordingly, it is not open for arbitral tribunals constituted under BITs to call on the CJEU to have contentious issues of EU law resolved.

In a next step, the CJEU examined the award, which it found to be final and only subject to a very limited review by the courts of the Member States. Interestingly, the CJEU here points to the difference between commercial and investment treaty arbitration. With regard to commercial arbitration, the CJEU had already found that the limited review of arbitral awards by Member State courts is justified ‘provided that the fundamental provisions of EU law can be examined in the course of that review and, if necessary, be the subject of a reference to the Court for a preliminary ruling’.31 However, the CJEU identifies certain differences between commercial and investment arbitration with the latter being ‘not based on freely expressed wishes of the parties, but derive from a treaty by which Member States agree to remove from the jurisdiction of their own courts and thus also from the regime that may ensure the uniform application of EU law’.32 The CJEU found that by virtue of concluding the BIT, the Member States established a regime that effectively prevents ‘disputes from being resolved in a manner that ensures the full effectiveness of EU law’.33 The violation of the principle of the effectiveness of EU law then leads to the CJEU’s final ruling ‘that Articles 267 and 344 TFEU must be interpreted as precluding’ a dispute settlement clause in an intra-EU BIT.34 This means, in practice, that a valid arbitration agreement between a Member State of the European Union and an investor of another EU Member State cannot be concluded. The lack of a valid arbitration agreement is one of the limited grounds under the New York Convention, and most national arbitration laws, on which an award may be set aside or refused recognition and enforcement.35

31 Slovak Republic v. Achmea B.V., Case C-284/16, Judgment of 6 March 2018, para. 54. This view was formed by the CJEU in Eco Swiss, Case C-126/97, Judgment of 1 June 1999, EU:C:1999:269, paras. 35, 36 and 40; 26 October 2006; Mostaza Claro, C-168/05, Judgment of the CJEU, 26 October 2006, EU:C:2006:675, paras. 34 to 39.
33 ibid., para. 56.
34 ibid., para. 60.
35 See, New York Convention, Article 1(a): ‘the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made.’
The referring court, the German Federal Court of Justice, set aside the *Achmea* award. Thereby, the German Federal Court of Justice followed the decision by the CJEU in substance and rejected any arguments presented by the investors as to why the CJEU’s *Achmea* judgment would not lead to an annulment of the award.36

The potential impact of this decision on the ECT is manifold, including political and legal implications alike, affecting past, current and future proceedings initiated under the ECT.

In *Novenergia v. Spain*, Spain – unsuccessfully – turned to the arbitral tribunal, which had rendered an award on 15 February 2018, namely a month before the CJEU’s decision in *Achmea*, and requested a revision of the award. Being denied revision by the tribunal, Spain advanced its argument before the competent court of the seat of the SCC arbitration, the Svea Court of Appeal in Sweden, which, under the New York Convention, acts as the annulment court in respect of arbitral awards. On 15 May 2018, the Svea Court of Appeal stayed enforcement of the award pending a final ruling in the case.37 At the same time, Spain is urging the Svea Court of Appeal to refer the case to the CJEU.

On 15 January 2019, the Member States of the European Union issued a political declaration in which the consequences of the *Achmea* judgment were discussed. Exposing divergences among the Member States, two additional declarations (one by Finland, Luxembourg, Malta, Slovenia and Sweden, and another by Hungary) were issued due to different positions regarding the impact of the *Achmea* judgment on the ECT.38

In the past, the European Commission and Member States argued that the ECT’s investment protection regime does not apply to inter-EU proceedings. The crux of this issue lies in the wording of Article 26 of the ECT. Member States on the receiving end of intra-EU arbitrations argued that intra-EU proceedings are ‘disconnected’ from the ECT’s scope because of an implicit disconnection clause, incorporated in the ECT through the 2007 EU Lisbon Treaty, which modified EU Member States rights and obligations, and removed intra-EU disputes from the scope of Article 26 of the ECT.39 The Lisbon Treaty qualifies, according to their argument, as a ‘successive treat[y] relating to the same subject-matter’ pursuant to Article 30 of the VCLT. Under this article, such a modification is possible if the earlier treaty provides that ‘it is subject to, or that it is not to be considered as incompatible with, [a] later treaty’. Article 16 of the ECT states that it is subject to a treaty ‘more favourable’ than it when it comes to the ECT’s provisions on investment protection. According to the respondent states, this is exactly what the Lisbon Treaty provides for and this practice is in line even when applying to a multilateral treaty within the scope of Article 41 of the VCLT.

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36 Para. 14 *Achmea* argued *inter alia* that Slovakia was barred from invoking the invalidity of the arbitration agreement according to the principle of good faith enshrined in section 242 of the German Civil Code.

37 *Novenergia II – Energy Environment (SCA) v. Kingdom of Spain*, Case No. T 4658-18, Judgment of 16 May 2018. This did not prevent Novenergia from seeking enforcement of the award in the United States. Enforcement proceedings are currently pending before the District Court of Columbia, Case No. 1:18-cv-1148.

38 The separate declaration issued, *inter alia*, by Sweden is of particular relevance to the ECT, as Sweden, diverging from the majority of Member States, will not direct its state-owned companies to end any commenced arbitration. Thus, the *Vattenfall AB et al. v. Germany* arbitration will not be affected.

39 *Athena Investments AS et al. v. Italy*, SCC Case No. 095/2015, Award, 23 December 2019, para. 265.
The European Commission, which appears as amicus curiae in almost all intra-EU disputes, further argues that it was not the European Union or its Member States’ intention to create obligations between the Member States, as they acted throughout the negotiations of the ECT as one block with the Commission as their voice.40

A second line of argument advanced by the European Commission highlights certain provisions of the ECT, which, according the European Commission, show that the ECT acknowledges that EU Member States never offered to arbitrate with investors from another EU Member State.41 One of the requirements for an investor to submit a dispute to arbitration according to Article 26(1) of the ECT is that it made an investment in the area of another contracting party. Pursuant to Article 1(10) of the ECT, ‘area’ is defined as the territory of a state or as ‘the areas of the member states of a [Regional Economic Integration Organization]’. The European Commission argued that an investment made by an investor from an EU Member State on the territory of another EU Member State is made within the same area, meaning the area of the European Union as a Regional Economic Integration Organization.42

In their latest amicus curiae brief, the European Commission seems to have adopted a very general argument. In the Commission’s view, ‘EU law forms part of the “applicable rules and principles of international law” under Article 26(6) ECT, and the “relevant rules of international law applicable in the relations between the parties” pursuant to Article 31(3)(c) VCLT.’43 As such, EU law is part of the applicable law determinative for assessing the validity of an arbitration. Adherence to ‘systemic coherence’ and the principle of autonomy of EU law requires an interpretation avoiding any conflict with EU law, which ‘leads to the conclusion that there is no offer to arbitrate’.44

Notably, as at the time of writing, every tribunal has rejected the intra-EU objection before it and ruled that it enjoyed jurisdiction over the dispute. The starting point for the tribunals is an interpretation of Article 26 of the ECT pursuant to Article 31(1) of the VCLT, which provides that treaties ‘shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in light of its object and purpose’. As the plain wording of Article 26 of the ECT does not include a qualification of any kind with regard to intra-EU arbitrations – and circumstances and context of the ECT do not suggest otherwise – tribunals conclude that the ECT continues to apply to intra-EU arbitrations.45

Also, the argument that an investment has been made in the same area has been quickly dealt with by tribunals. In *Masdar v. Spain*, the tribunal referenced the decision in *PV Investors*46 where the tribunal found that the term ‘in the area’ in Article 26(1) of the ECT

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40 ibid., para. 283.
41 ibid., para. 279.
42 ibid., para. 280.
43 *Vattenfall AB et al. v. Germany*, ICSID Case No ARB/12/12, Decision on the Achmea Issue, 18 August 2018, para. 81.
44 ibid., para. 83.
45 *Athena Investments A/S et al. v. Italy*, SCC Case No. 095/2015, Award, 23 December 2019, para. 397; *Masdar Solar & Wind Coopératif U.A. v. Spain*, ICSID Case No. ARB/14/1, Award, 16 May 2018, para. 312.
46 *The PV Investors v. The Kingdom of Spain*, PCA Case No. 2012-14, Preliminary Award on Jurisdiction, 13 October 2014, paras. 178-180.
must be seen in light of the specific dispute. If an investor chooses to initiate arbitration proceedings against an EU Member State and not the European Union, ‘the area’ referenced in Article 26(1) of the ECT means the territory of that particular Member State.

With regard to the Achmea judgment, respondent EU Member States and the European Commission are of the opinion that the judgment does also apply to the ECT. The view is based on the argument that the findings of the CJEU can be transported and applied to arbitrations under the framework of the ECT. In the words of the European Commission, arbitral tribunals under the ECT are like tribunals established under intra-EU BITs ‘not “national courts or tribunals” in the sense of Article 267 TFEU, and there is no complete review of arbitral awards by such tribunals through national courts within the EU, even less so for ICSID arbitrations’. Hence, tribunals should either find a ‘harmonious interpretation of the ECT in conformity with EU law, or second, in the event of a conflict, the primacy of EU law as lex posterior’.

Taking into account the CJEU’s Achmea judgment, tribunals found throughout 2018 that the CJEU carefully limited its ruling to BITs concluded between EU Member States, and left it open for investors to initiate arbitral proceedings under other international instruments that are not solely intra-EU BITs.

First, tribunals established under the ECT derive their jurisdiction exclusively from Article 26 of the ECT. In that respect, tribunals found that Article 26(6) of the ECT, contrary to the submissions of the European Commission and most respondent EU Member States, only constitutes an agreement regarding the law applicable to the merits of the dispute. Thus, by operation of Article 26(6) of the ECT, EU law does not form a part of the applicable law to determine the jurisdiction of the tribunal.

For example, the tribunal in the ICSID arbitration Vattenfall AB et al. v. Germany found that the assessment of jurisdiction must be made under the ICSID Convention and the instrument containing the consent to arbitration, namely Article 26 of the ECT, interpreted and applied in accordance with international law. Similar to the intra-EU objections raised by the European Commission and EU Member States in the past, the arguments based on the Achmea judgment failed to survive interpretation of Article 26 of the ECT under Article 31(1) of the VCLT. According to the tribunals, the plain wording of the ECT does not leave any room for harmonious interpretation under Article 31(3)(c) of the VCLT.

Second, there are significant differences between intra-EU BITs and the ECT. The former is concluded between two EU Member States, while the latter is signed by the European Union, its Member States and 25 other countries that are not Member States.

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47 Masdar Solar & Wind Cooperatief U.A. v. Spain, ICSID Case No. ARB/14/1, Award, 16 May 2018, para. 319. See also, Vattenfall AB et al. v. Germany, ICSID Case No ARB/12/12, Decision on the Achmea Issue, 18 August 2018, para. 179 et seq.
48 Vattenfall AB et al. v. Germany, ICSID Case No ARB/12/12, Decision on the Achmea Issue, 18 August 2018, para. 85.
49 ibid.
51 Vattenfall AB et al. v. Germany, ICSID Case No ARB/12/12, Decision on the Achmea Issue, 18 August 2018, para. 122.
52 ibid., para. 128.
53 ibid., para. 158.
of the European Union. This distinction was made by Advocate General Wathelet in his opinion predating the CJEU’s Achmea judgment and not addressed or rejected by the CJEU in its judgment.

And finally, in the context of ECT arbitrations, tribunals are tasked with adjudicating alleged infringements of rights under international law, not under EU law, which thus does not conflict with the CJEU’s decision in Achmea.

ii Cases related to taxation measures

Another jurisdictional challenge by respondent states that appears to feature ever more often in arbitrations under the ECT is the tax carve-out pursuant to its Article 21(1).

Traditionally, taxes play an important role in a state’s regulatory strategy when it comes to energy investments. States that are rich in natural resources may use taxes to have the public participate in profits made by investors who exploit those resources; other states may use taxes to incentivise the making of investments in a certain field of energy production according to the state’s overall energy strategy. In view of this, energy investments are always subject to a complex and often changing tax system, which might negatively impact foreign investments.

At the same time, energy politics is often seen as one of the most strategically important subjects. Challenges of taxation measures by foreign investors before an international tribunal is therefore a delicate subject.

During the negotiations leading up to the ECT, the different stances on energy politics among the negotiating states came to light. A coalition of the United States, Canada and the United Kingdom favoured excluding taxation measures from arbitration under Article 26 of the ECT. Germany, however, argued that excluding arbitration entirely would have a devastating effect on the investors’ position, and pointed to eastern Europe, where indirect expropriation through taxation measures was not unlikely.

Owing to support from the chair of the legal group, Craig Bamberger, who endorsed the German position, the final text of Article 21, in its pertinent parts, now reads:

(1) Except as otherwise provided in this Article nothing in this Treaty shall create rights or impose obligations with respect to Taxation Measures of the Contracting Parties.

(5) Article 13 shall apply to taxes.

This provision would become one of the most contested issues, not in relation to measures by eastern European countries, but in the solar claims against Spain, Italy and the Czech Republic. All of these countries introduced a tax that adversely affected the position of foreign investors.

Spain, pursuant to Law 15/2012 of 1 January 2013, introduced a tax measure that taxes the production of electricity and its feeding into the Spanish electricity grid. In 2008, Italy introduced a ‘Robin Hood’ tax that applied to all energy producers but photovoltaic, biomass and wind energy. In 2011, the tax was extended to also cover renewable energy

55 ibid., para. 397.
56 Taxation of Foreign Investments, Article 21 of the Energy Charter Treaty in Context, Ugur Erman Özgür, 2015, p.44.
57 ibid., p.45.
In 2011, the Czech Republic enacted a law which established ‘a levy on revenues generated by photovoltaic power plants’.\(^\text{59}\) Also in 2011, the Czech Republic repealed the income tax exemption for producers of renewable energy.\(^\text{60}\)

### Spain's taxation measure

In *Masdar v. Spain*, the claimant argued that ‘there is prima facie evidence that the [tax] is arbitrary’ and would thereby not be triggering the carve-out in Article 21(1) of the ECT. According to the claimant, the tax did not constitute a taxation measure but was in fact a tariff reduction for renewable energy producers limiting the effectiveness of the incentive regime based on which the claimant made its investments.\(^\text{61}\) The claimant's case that it put before the tribunal was thus whether Spain's tax measure was a *bona fide* tax, apt to trigger the exemption from the carve-out as identified by the *Yukos* tribunal.\(^\text{62}\)

The tribunal went on to establish that *Yukos* concerned ‘an extreme case’, dealing with ‘measures which were egregious and which, in reality, had little, if anything, to do with the *bona fide* raising of tax revenues for public purposes’.\(^\text{63}\) The *Yukos* tribunal not only noted that states generally enjoy wide discretion when imposing and enforcing taxes, but even where these measures might result in substantial deprivation without compensation. The threshold that is derived from the above was then applied by the tribunal, which ultimately found that it ‘does not have jurisdiction to entertain claims arising out of the introduction of the [tax]’,\(^\text{64}\) even if there are ‘undoubtedly questions that might be raised about the economic effects and the purpose of the [tax]’.\(^\text{65}\)

### Italy's taxation measure

The claimants in *Athena et al. v. Italy* adopted a different approach. Given the standard applied to the exemption from the tax carve-out, the claimant only challenged whether a decision by the Italian Constitutional Court, which rendered the tax invalid on an *ex nunc* basis rather than on an *ex tunc* basis, was in accordance with the ECT.\(^\text{66}\) The claimant explicitly stated that it was not contesting the tax measure itself.

The tribunal still found the claim to fall outside of the tribunal's jurisdiction pursuant to Article 21(1) of the ECT. The tribunal's starting point in that regard was the wording of the Article, which provides that nothing in the ECT shall ‘impose obligations with respect to taxation measures’. If the tribunal were to award damages based on the Constitutional

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\(^{58}\) *Athena Investments A/S et al. v. Italy*, SCC Case No. 095/2015, Award, 23 December 2019, para. 167 et seq.

\(^{59}\) *Antaris Solar GmbH and Dr. Michael Göde v. the Czech Republic*, PCA Case No. 2014-01, Award 2 May 2018, para. 96.

\(^{60}\) ibid., para. 100.

\(^{61}\) *Masdar Solar & Wind Cooperatief U.A. v. Spain*, ICSID Case No. ARB/14/1, Award, 16 May 2018, paras. 273 et seq.

\(^{62}\) *Yukos Universal (Isle of Man) et al. v. Russian Federation*, PCA Case No. AA 228, Final Award, 18 July 2014, para. 1407.

\(^{63}\) *Masdar Solar & Wind Cooperatief U.A. v. Spain*, ICSID Case No. ARB/14/1, Award, 16 May 2018, para. 284.

\(^{64}\) ibid., para. 295.

\(^{65}\) ibid., para. 290.

\(^{66}\) *Athena Investments A/S et al. v. Italy*, SCC Case No. 095/2015, Award, 23 December 2019, para. 225.
Court’s decision, it would, according to the tribunal, seem to impose ‘obligations with respect to taxation measures’.\(^{67}\) For that reason, the tribunal considered the distinction between the tax measure and the court’s decision not meaningful enough.\(^{68}\)

**The Czech Republic’s taxation measure**

In *Antaris et al. v. the Czech Republic*, the claimant advanced two grounds why Article 21(1) of the ECT should not apply. First, Article 31(1) of the VCLT warrants interpretation in light of the principle of good faith, the context, object and purpose of the treaty at hand. As confirmed by the Energy Charter Secretariat, ‘taxes shall be imposed in good faith’.\(^{69}\)

With regard to the *Yukos* tribunal’s findings and the threshold associated with it, the claimant submitted that the standard is not limited to extreme circumstances but shall rather prevent states from evading ‘international liability by disguising a measure as a tax’.\(^{70}\) To underpin its contention, the claimant pointed to a decision by the Czech Constitutional Court, which confirmed that the tax measure was in fact not a tax.

The respondent argued that, under Article 21(7) of the ECT, a taxation measure includes ‘any provision relating to taxes of the domestic law of the contracting party’.\(^{71}\) The tribunal would thus only be tasked with assessing whether the claim concerned a measure constituting a tax according to the respondent’s domestic laws.\(^{72}\)

Meeting this argument, the claimant brought forward, as a second argument, that the tax measure does not even qualify as tax under the Czech Republic’s domestic laws, as it would be paid for a specific purpose, namely to reduce the burden on consumers without negatively impacting the state deficit, and, second, the producers received a direct consideration for paying the tax.\(^{73}\) In addition, the tribunal’s task of interpreting Article 21(7) of the ECT does not stop at assessing the nature of the measure under the domestic law of the respondents but must take into account the interpretation of the ECT as an instrument of international law as well.

The tribunal brought some clarity by finding that it would follow a two-step test: first, performing a characterisation under the domestic law and then applying ‘Article 21’s inherent limits’.\(^ {74}\) According to the tribunal, this follows already from the ordinary meaning of Article 21 of the ECT, which can only be applicable where the domestic law characterises a measure as a tax.\(^ {75}\) It further adopted a substantive not a formalistic approach to this issue. Declaring a measure as a tax would not suffice, according to the tribunal; rather, the measure must meet substantive criteria to identify as tax. To assess this question under the domestic laws of the Czech Republic, it found support in various Czech court decisions, which it

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\(^{67}\) ibid., para. 227.

\(^{68}\) ibid.

\(^{69}\) *Antaris Solar GmbH and Dr. Michael Göde v. the Czech Republic*, PCA Case No. 2014-01, Award 2 May 2018, paras. 195 et seq.

\(^{70}\) ibid., para. 201.

\(^{71}\) ibid., para. 221.

\(^{72}\) ibid., 223.

\(^{73}\) ibid., paras. 207, 208.

\(^{74}\) ibid., para. 224.

\(^{75}\) ibid., para. 225.
considered to be ‘authoritative on this point’.\textsuperscript{76} The tribunal followed a decision by the Czech Supreme Administrative Court in which the court found that the measure would not constitute a tax in substance.\textsuperscript{77}

It also rejected submissions by the respondent that the tribunal should adopt a formalistic approach by stating that:

\begin{quote}
If an ECT Tribunal were to considered only the form of the measure rather than its substance, it would provide the scope for abuse of the ECT’s tax carve-out, as the contracting states would be able to escape their obligations under Part III of the ECT, and thus liability from their violations thereof, simply by labelling governmental actions as “taxation” measures.\textsuperscript{78}
\end{quote}

By that, the tribunal found that the measure was unable to engage Article 21(1) of the ECT at all, which is why the tribunal enjoyed jurisdiction over the claims.\textsuperscript{79}

\section{Looking back at the 2018 cases}

The cases discussed above from 2018 exemplify the complexity surrounding investment arbitration under the ECT nowadays.

The 	extit{Achmea} judgment might lead to attempts by the European Union to modify, reform or renew the ECT – an undertaking that, until now, was not a subject of debates. It might also involve interests of EU Member States openly clashing. At the same time, it is remarkable that awards against eastern European and central Asian countries are a rarity nowadays. That may be, inter alia, explained by the fact that the Ukrainian–Russian crisis, which resulted in a couple of arbitrations, falls outside of the scope of the ECT.

The guidance and insights provided by tribunals in 2018 decisions on the interpretation of the tax carve-out cannot be emphasised enough. Taxation related claims are increasing and with it the need for an understanding of the tax carve-out, given the minefield between public welfare, state’s sovereignty and an investor’s legitimate expectation to have its investment unharmed by arbitrary taxation measures. In that context, it is a particularly welcomed sight that tribunals very thoroughly examined the issues before them, oftentimes analysing domestic laws and related decisions by courts but also inviting parties to comment on similar arbitral awards. Tribunals, so it seems, are more aware of the expectations of the users of system in them to create a uniform regime of investment protection under the ECT. The 2018 arbitral awards were a step in that direction.

\textsuperscript{76} ibid., para. 233.
\textsuperscript{77} ibid., para. 243.
\textsuperscript{78} ibid., para. 249
\textsuperscript{79} ibid., paras. 252, 253.
VI OUTLOOK

The 2018 developments surrounding the ECT mainly concerned the western European community. It is to be expected that the European Union and its Member States will spend much of 2019 dealing with issues between themselves, which were already clearly identified in the three different notes issued by EU Member States after the Achmea judgment, which differ as to the application of the Achmea judgment to the ECT.80

Before that backdrop, it can be expected that it will take some time for the European Union and its Member States to identify common ground regarding the implementation of the Achmea judgment with respect to the ECT. Countries concerned with solar claims, especially, will push for immediate reforms or political actions. However, the consensual nature of EU politics might cause significant delay if Member States are not able to find such consensus.

But it should not be overlooked that the ECT’s signatories are not only western European states, but also many capital-importing countries in eastern Europe and central Asia. With China’s belt and road initiative now well underway and the commencement of construction of the Nord Stream II project, the focus might again shift east. Not least because of the dozens of treaty claims pending against western European states, being a politically contested subject, the ECT will therefore remain an important legal instrument of investment protection in the years to come.

80 Compare footnote 9.
NAFTA IN TRANSITION: THE CURRENT STATE OF PLAY AND WHAT COMES NEXT

Lisa M Richman

I THE ‘NEW NAFTA’ – INTRODUCTION TO NAFTA AND USMCA

After multiple rounds of negotiation, and years of speculation and discussion about the fate of the North American Free Trade Agreement (NAFTA), a revised North American trade pact, known in the United States as the United States–Mexico–Canada Agreement (USMCA) was signed by US President Donald Trump, then Mexican President Enrique Peña Nieto and Canadian Prime Minister Justin Trudeau on 30 November 2018 to replace NAFTA, originally executed in 1994.

The (maybe) soon-to-be-abandoned NAFTA, born with popularity as well as controversy, was initially negotiated by the governments of the United States, Canada and Mexico in an effort to liberalise trade by eliminating tariffs on products traded between and among these three countries. NAFTA also offered other innovations, including cross-border intellectual property protection and a dispute resolution mechanism under which private investors from one of the Member States were permitted to bring claims directly against one of the other Member States. The idea was to create greater trade opportunities, broader protection for investors and innovative mechanisms to create the world’s largest international free trade zone. In fact, NAFTA helped contribute to a tremendous increase in trade among the United States, Canada and Mexico, and substantially reshaped North American economic relations. Apart from its economic contributions to both regional and world economy, NAFTA also plays a significant role in foreign relations and in promoting political stability within the region.

However, NAFTA has been a perennial target for President Trump, who describes it as ‘the worst trade deal ever’. Soon after his election, he proposed the renegotiation of NAFTA to Congress as part of his plan to reduce the trade deficit. After more than a year of negotiation, a new agreement, USMCA, was signed. It addressed some of the major concerns of certain constituents arising from NAFTA.

Although USMCA and NAFTA contain many similarities, there also are important changes. For example, USMCA expands intellectual property protection and adjusts treatments on important industries, such as automobile and agriculture. Perhaps the most significant change relates to the investment dispute resolution mechanism available under USMCA. Although the substantive protections for foreign investments in USMCA Chapter 14 largely mirror those contained in NAFTA Chapter 11, the scope of investor–state
dispute settlement (ISDS) is reduced considerably. Additionally, in a significant departure from NAFTA, Canada has not agreed to the investment arbitration mechanism. This means that neither US nor Mexican investors will be able to bring claims against Canada under USMCA, nor will Canadian investors be entitled to bring such claims against Mexico or the United States. Other important changes to the substance of investment protections contained in USMCA as compared with NAFTA will be discussed in more detail in Section IV.

To date, USMCA has not yet gone through domestic procedures for finalisation and implementation in any of the three Member States. Although it is unclear whether USMCA will be ratified, investors should be prepared for the potential transition from NAFTA to USMCA, and be aware of the significant changes USMCA introduces.

II HOW AND WHEN COULD USMCA BE RATIFIED?

i The process in the United States

In the United States, the future of USMCA now largely depends on Congress. Although the President has the authority to negotiate trade agreements without interference, members of Congress have the power to vote on trade promotion agreements without amendment.

Under normal ‘fast-track’ procedures for trade agreements, a simple majority vote is needed in the House of Representatives (within 60 session days) followed by a simple majority vote in the Senate within 30 session days thereafter to approve or refuse a trade agreement. Before the final text of the agreement is introduced to Congress, a report describing the required changes to US law drafted by the US Trade Representative (USTR) and a study on the agreement’s economic impact drafted by the International Trade Commission (ITC) also are to be provided to Congress. The USTR report was submitted by Representative Lighthizer in early February. The ITC’s impact study was issued on 18 April 2019, delayed because of the 35-day government shutdown in early 2019. Because trade agreements are typically subject to an up or down vote with no amendments within the quick deadlines identified above, things could move swiftly. The Trump administration could also wait to send the agreement to Congress for a vote until concerns have been addressed through either a side agreement or changes to US laws, as necessary. Historically, prior administrations have pulled free trade agreements where they detected they would not pass in Congress.

However, there also is the question of what the Trump administration might do to force Congress’s hand. On 1 December 2018, the day after USMCA was signed, President Trump gave Congress formal notice that he would terminate NAFTA in the ‘near future’. Article 2205 of NAFTA provides that a Member State wishing to withdraw must provide written notice, and then six months later withdrawal becomes effective for that Member State (but not the others) unless the Member State takes back the withdrawal.

Assuming President Trump follows through on his announcement and does not delay a vote to address concerns (as prior administrations have done where congressional concerns regarding a free trade agreement remained to be addressed), it could leave Congress with limited options: accept the new agreement, risk having no deal at all or try to enact legislation that mandates that the President must seek congressional approval before withdrawing from NAFTA.

If Congress formally approves USMCA, it will take the place of NAFTA and become the new law governing the commercial relationships between the United States, Mexico and Canada. There is also the possibility of Congress striking down the whole deal completely. In that case, NAFTA might remain since the President’s power to withdraw from an international treaty without congressional approval is currently in dispute.

Even if President Trump attempts to withdraw from NAFTA, the NAFTA Implementation Act, which ensures the domestic implementation of NAFTA, would basically stay intact. This means that, absent congressional action, the effect of withdrawal will not mean that all parts of NAFTA end, although the reciprocal tariff concessions could expire or be modified by the President. Unless the President issues an immediate tariff proclamation, tariff concessions will not revert to their prior most favoured nation (MFN) level for one year after the termination of a free trade agreement. And, as noted above, Congress could also enact legislation calling on President Trump to obtain congressional assent.

It is hard to predict whether USMCA will stall for some period (and for what length of time), whether and when it could be approved, or whether the United States will withdraw from NAFTA as President Trump could be blocked by the newly Democrat-controlled Congress.

ii  The process in Canada

In Canada, the decision of whether USMCA will be ratified domestically lies in the hands of Parliament. Since the Prime Minister of Canada already approved the deal and the Liberals have a majority in Parliament at present, the implementation of USMCA would likely go through in Canada without difficulty.

The ratification process in Canada contemplates that, after signature, the new agreement, along with an explanatory memorandum, is tabled in the House of Commons for debate. If there is sufficient support in the House of Commons, it proposes a motion to recommend action within 21 sitting days, including ratification of the agreement. A vote is not required. The cabinet would exercise full control over the ratification process. It would authorise the Minister of Foreign Affairs to sign an Instrument of Ratification. Then, an implementing bill, which contains the changes required to Canadian law at the national level, would be tabled and debated in the House of Commons and Senate respectively. Members of Parliament may suggest changes to the implementing laws and ask questions of the government, but they cannot change the substance of the new agreement.

iii  The process in Mexico

The ratification process in Mexico is simpler than that of the United States and Canada, which means USMCA likely would be approved quickly and without trouble.

The ratification process in Mexico contemplates that, after signature, the new agreement is sent to the Senate for a vote. If a simple majority votes for USMCA, it would then be published and entered into force. Although there is no mandatory time limit for the whole process, it took Mexico fewer than seven weeks to ratify the Comprehensive and Progress Agreement for Trans-Pacific Partnership (CPTPP).

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5  H.R. 3450, North American Free Trade Agreement Implementation Act, Section 201.
6  Trade Act of 1974, Section 125.
Concluding thoughts regarding ratification

Even though the ratification procedures in Canada and Mexico appear easier than that of the United States, neither Canada nor Mexico has ratified or implemented USMCA to date. Commentators have speculated that Canada and Mexico are worried about the fate of USMCA in the United States. If US Congress strikes down the deal, it is pointless to go through the process only to find that a key partner in the agreement is not going forward with it. Perhaps more importantly, and as described in more detail below, Canada and Mexico appear to be awaiting the resolution of the related issue of national security tariffs under Section 232 of the 1962 Trade Expansion Act. Until this issue is resolved, it is unlikely that any of the USMCA parties will take any meaningful action towards ratification of the deal as a whole.

Investors will want to continue to watch closely for developments in Congress. Until USMCA has been ratified, NAFTA will remain in place and offer broader protection for investors. But even after USMCA enters into force, investors with ‘legacy investments’ will still have a three-year period to bring a dispute under NAFTA, even though NAFTA will terminate upon entry into force of USMCA, three months after the Member States have all ratified it. Investors with potential claims concerning legacy investments will want to take all necessary preliminary steps and submit a formal notice of arbitration no later than three years after USMCA enters into force to avoid risks and uncertainties caused by the transition. Investors who establish investments after the entering into force of USMCA will not be able to bring claims under NAFTA.

III MOST SIGNIFICANT DIFFERENCES BETWEEN USMCA AND NAFTA

i Dispute resolution mechanism

Compared with NAFTA, some of the biggest changes in USMCA are set forth in its Chapter 14. Perhaps the biggest change is that Canada has not signed on to Annex 14-D (US–Mexican investment disputes) or Annex 14-E (covered government contracts). As a result, other than for legacy investments and pending claims under Annex 14-C, neither US nor Mexican investors can bring arbitration claims against Canada under USMCA, nor can Canadian investors bring such claims against the United States or Mexico. Canadian investors in Mexico and Mexican investors in Canada, however, have access to investment arbitration under the CPTPP, which entered into force in December 2018. However, the application of ISDS in CPTPP Chapter 9 is not as broad as in NAFTA. For example, Mexico has carved out its consent to investment arbitration under the CPTPP with respect to government contracts-related infrastructure projects.

USMCA also contains numerous changes to the availability and terms of ISDS for claims against Mexico (by US investors) or the United States (by Mexican investors). The
four most significant changes relate to the restriction of covered claims under Article 14.6, the requirement to exhaust local remedies under Article 5 of Annex 14-D, the definition of ‘investment’ under Article 14.1 and the definition of ‘claimant’ under Article 1 of Annex 14-D.

First, USMCA limits the types of claims that can be brought in arbitration as compared with NAFTA. Two of the most common claims under NAFTA, for indirect expropriation or for a breach of the minimum standard of treatment, are no longer covered under the new agreement. Nonetheless, investors who enter into government contracts related to oil and natural gas, power generation, telecommunications, transportation services, or ownership or management of infrastructure, are exempted from those changes (in part) and offered a broader set of ISDS protections. Additionally, USMCA limits the scope of ‘fair and equitable treatment’ and ‘full protection and security’ by giving these terms specific definitions under minimum standard of treatment. Moreover, Annexes 14-D and 14-E provide that the MFN clause (Article 14.5) cannot be used to import substantive or arbitration provisions from other treaties. This change is unprecedented – no other investment treaty explicitly restricts an MFN clause in this way.

Second, the new procedural requirements in USMCA create additional burdens for investors. They must pursue national court proceedings to completion or for at least 30 months before submitting claims to arbitration under USMCA, unless they can demonstrate that this would be ‘futile’ or ‘manifestly ineffective’. Meanwhile, the four-year overall time limit for bringing claims from the date on which the investor first acquired, or should have acquired, knowledge of the alleged breach includes the 30 months that must be spent before the domestic courts. This means that, in practice, investors who plan to bring claims under USMCA will need to watch the calendar very carefully and consider preparing a notice of claim even before or while national proceedings are pending. In what has been described as an ‘asymmetrical fork-in-the-road provision’, a US investor may not bring to arbitration a claim for a breach of USMCA, as distinguished from a breach of other obligations under Mexican law, that the investor previously has submitted to national court proceedings or an administrative tribunal of Mexico. Although this provision has not been tested in practice, this seems to suggest that US investors who intend to bring claims for violation of USMCA need not exhaust domestic remedies and, in fact, would waive their right to arbitrate in doing so. The procedural requirement of going to national courts or

12 USMCA, Chapter 14, Article 6.
13 USMCA, Annex 14-D, fn 22. Chapter 17 also contains similar limitations as it relates to investment arbitrations relating to the financial services sector. Chapter 17 contains a slightly different set of procedures.
15 USMCA, Chapter 14, Article 5 and Annex 14-D, fn 24.
17 USMCA, Annex 14-D, Appendix 3.
18 There are no such restrictions for Mexican investors; presumably, because unlike Mexico, where the international treaties automatically become domestic law, meaning it is possible for US investors to directly
administrative tribunals before arbitration also does not apply to an investor who is a party to certain government contracts, as mentioned above. And, the overall time limit of claims involving such government contracts is three years instead of four.19

Finally, certain clarifications were made in USMCA to the definition of ‘investment’, and ‘claimant’ was added as a new term (which modifies the definition of ‘investor’).

Under Article 1139 of NAFTA, investment is defined by a finite list of 10 examples, which include ‘an enterprise’, ‘credit security’ and ‘debt security’ in an enterprise, a ‘loan . . . [or] interest in an enterprise’, ‘real estate or other property, tangible or intangible’, and ‘claims to money’. In contrast, Article 14.1 of USMCA defines investment more broadly and like many other investment treaties (including more modern US free trade agreements), as ‘every asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, including such characteristics as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk’.20 This general definition is followed by an open list of examples, which includes an express exclusion only for ‘an order or judgment entered in a judicial or administrative action’ or ‘claims to money that arise solely from commercial contracts for the sale of goods or services’, and related extensions of credit. It is unclear whether this change to the definition of investment will be interpreted in a different and more expansive way than investments under Article 1139 of NAFTA.

Under Article 1 of Annex 14-D of USMCA, claimant is defined as ‘an investor of an Annex Party [i.e., the United States or Mexico], excluding an investor that is owned or controlled by a person of a non-Annex Party that the other Annex Party considers to be a non-market economy, that is a party to a qualifying investment dispute’. This restriction is new. Though both NAFTA (in Article 1113) and USMCA (in Article 14.14) already contain denial of benefits clauses, those clauses only allow a respondent state to deny the benefits of the investment chapter, including access to ISDS, to an enterprise of another party that is owned or controlled by third-state nationals and that has no substantial business activities in the territory of the party in which it is incorporated. The new exclusion of US or Mexican claimants owned or controlled by a national or enterprise of a non-market economy is broader because it excludes a potential claimant from arbitration even if the US or Mexican company engages in substantial business activities in its state of incorporation.

When NAFTA was initiated, private investors’ wide range of rights were strongly supported by the United States and Canada to obtain the maximum protection against what was perceived to be ‘Mexican nationalism’.21 It seems the tides have turned and that there is a greater emphasis in USMCA on the Member States’ sovereign right to regulate public policy, especially with respect to environmental regulation.

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19 USMCA, Annex 14-E.
20 USMCA, Chapter 14, Article 1.

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Arbitral proceedings

In addition to the changes described above, USMCA contains additional changes that appear to be focused on streamlining arbitral proceedings and making them more transparent. Whether the changes will lead to a more effective, efficient and fair dispute settlement system remains to be seen.

USMCA includes new provisions intended to increase the transparency of arbitral proceedings by explicitly providing that the public have access to relevant arbitration documents and the hearings, whereas NAFTA contained provisions relating to publication of the award, and of the notice and request for arbitration. In practice, many of the written submissions, awards and other documents relating to NAFTA cases have been made publicly available (at least in redacted form) already such that this provision may have little practical effect.

USMCA contains new requirements to prevent ‘double-hatting’. Annex 14-D provides that arbitrators must comply with the IBA Guidelines on Conflicts of Interest and are prohibited from ‘acting as counsel or as party-appointed expert or witness in any pending arbitration under the annexes to this Chapter for the duration of the proceedings’. Given the already relatively small pool of arbitrators with investment arbitration experience, this change will further limit the available pool of arbitrators, but also may help to avoid a perception that arbitrators could be involved as counsel in a dispute with related issues and therefore have an underlying if indirect conflict of interest.

In contrast with the NAFTA requirement that the arbitration be seated in a NAFTA state, USMCA allows the tribunal to choose the place of arbitration in any state that is a party to the New York Convention. As the seat of arbitration can influence the proceedings in many ways, from the commencement of arbitration to the annulment of a final award, more choice over the seat of arbitration could introduce more flexibility, but will also require the parties to be on guard and ensure they provide input to ensure selection of a seat strategically best suited to the dispute at issue.

Another new feature of USMCA is that the disputing parties are given the right to review and comment on the tribunal’s award on liability prior to its issuance. Again, it remains to be seen how this innovation will play out in practice and whether it will simply lead to a never-ending circle of post-hearing and pre-final award briefings.

USMCA also provides an expedited hearing procedure for certain objections; for example, jurisdictional objections and objections that a claim is manifestly without legal merit. Again, whether these changes will lead to more efficient or just more expensive and drawn-out proceedings remains to be seen; much will depend on arbitrators’ willingness to kick out claims at the jurisdictional stage.

Investment fields

Apart from the dispute resolution mechanism, changes were also made in several investment fields.

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22 USMCA, Annex 14-D, Article 8.
23 NAFTA, Chapter 11, Section C, Articles 1126 and 1137.4.
24 USMCA, Annex 14-D, Article 6.5.
25 ibid., Article 7.1.
26 ibid., Article 7.12.
27 ibid., Articles 7.4 and 7.5.
Auto industry

Significant changes were made to provisions relating to rules of origin and minimum wages. While NAFTA requires only 62.5 per cent of cars produced in the trade zone to be made in North America, the new agreement increases the percentage to 75 per cent.\(^{28}\) A new requirement on minimum wages was added in USMCA, which provides that at least 40 per cent of automobile parts have to be made by workers who earn at least US$16 an hour by 2023.\(^{29}\) The change was intended to encourage the signing countries to enhance their labour protections, particularly in Mexico.

Agriculture

USMCA creates new market access opportunities for US exports to Canada of dairy, poultry, and eggs. In return, the United States will provide new access to Canada for dairy, peanuts, processed peanut products, and a limited amount of sugar and sugar-containing products. The most significant change was made relating to the dairy industry, where the United States will be able to export to Canada the equivalent of 3.6 per cent of Canada's dairy market, up from the existing level of about 1 per cent.\(^{30}\) Additionally, USMCA changes market access, sale and distribution regulations, relating to wine and other alcoholic beverages in a significant win for US wine and other alcohol exporters.

Intellectual property rights

Generally, as compared with NAFTA, USMCA offers broader protection in respect of intellectual property rights. Although NAFTA offers statutory protection for intellectual property rights, USMCA contains clarified definitions and stronger language. These changes appear to offer a wider range of protection in respect of addressing digital trade,\(^{31}\) expanding the scope of intellectual property rights and enhancing the remedies for infringement.

Procurement

Although the public procurement provisions between the United States and Mexico essentially stay the same, Canada is excluded from the procurement chapter\(^{32}\) in USMCA. Instead, Canada's relationship with the United States regarding procurement would be governed by the World Trade Organization Agreement on Government Procurement (GPA). And procurement as it relates to Canada and Mexico would be governed by the CPTPP.

The exclusion of Canada from the procurement chapter of USMCA is not expected to have a significant impact as between the United States and Mexico, or Mexico and Canada. But it may slightly reduce US companies' access to procurement in Canada as the procurement thresholds for goods and services in Canada under NAFTA will no longer apply.\(^{33}\) Also, while under NAFTA, all services except for those Canada lists as excluded in NAFTA are available

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28 USMCA, Chapter 4.
29 ibid.
31 USMCA, Chapter 19.
32 ibid., Chapter 13, Article 2.
33 ibid., Annex 13-A, Section A; NAFTA, Chapter 10, Article 1001.
NAFTA in Transition: The Current State of Play and What Comes Next

for procurement;\(^{34}\) GPA provides a narrower list of services.\(^{35}\) This difference in the scope of applicable services may reduce US companies’ access to procurement opportunities in Canada as well.

**US national security tariffs**

During negotiation, Mexico and Canada asked the United States to lift its national security tariffs on steel and aluminium under Section 232 of the 1962 Trade Expansion Act. But USMCA does not mention this protection. Instead, the United States reached two separate side agreements with Mexico and Canada respectively to reduce national security tariffs on automobiles and automobile parts.\(^{36}\) Under these agreements, 2.6 million passenger vehicles and US$32.4 billion in auto parts from Canada will be exempt from duties. For Mexico, 2.6 million passenger vehicles will also be exempt, as well as US$108 billion in auto parts.\(^{37}\) As noted above, until this issue is resolved, there likely will be little movement relating to USMCA ratification.

**Sunset clause**

Unlike NAFTA, a sunset clause was included in Chapter 34 of USMCA. The Member States settled on a 16-year expiration term. Every six years, the United States, Mexico and Canada will conduct a joint review and decide whether to extend the term of the agreement for another 16-year period.\(^{38}\)

**IV STATUS OF CURRENT CLAIMS UNDER NAFTA CHAPTER 11**

Although various US constituents have expressed significant concerns about and opposition to the NAFTA dispute resolution mechanism, it is notable that the United States has not lost in a single investor–state case as a respondent. However, US (and other) investors have benefited from NAFTA protections.

Approximately 94 known disputes have been filed under Chapter 11 of NAFTA. While about half of the claims were brought against Canada, only 21 claims have been brought against the United States and approximately 30 claims have been brought against Mexico. Among the cases that went through to a final award on the merits, Canada and Mexico lost six and five cases, respectively, while the United States lost none. Eleven of the 21 claims filed against the United States were dismissed by the arbitrators, and the remainder were either settled without damages (one case), withdrawn (two cases) or are inactive (seven cases).\(^{39}\)

\(^{34}\) NAFTA, Chapter 10, Annex 1001.1b-2.
\(^{35}\) WTO GPA, Canada Annex 5: Services.
\(^{37}\) id.
\(^{38}\) USMCA, Chapter 34, Article 7.

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Although USMCA contains several substantial changes to NAFTA, there are approximately 14 claims pending under NAFTA that should not be affected by the coming into force of USMCA.\(^{40}\) Information about available details and status of each of these claims is set forth in the table in the Appendix to this chapter.

Of these claims, one prominent NAFTA claim is notable in light of recent US court litigation that may cause the NAFTA arbitration to be activated. In 2016, a Canadian company, TransCanada PipeLines Ltd, brought claims for US$15 billion against the United States.\(^{41}\) TransCanada alleged that the delay and eventual rejection by the Obama administration of the Keystone XL pipeline discriminated against the company, denied it fair and equitable treatment, and expropriated its investment under NAFTA Chapter 11. After the Trump administration approved the project, the investor and the US government agreed to discontinue the NAFTA claims. In March 2017, the ICSID Secretary-General formally discontinued the arbitral proceedings. On 8 November 2018, in response to a lawsuit brought by environmental and Native American groups against the US Department of State and TransCanada, a federal court in Montana ordered a pause in the construction of the Keystone XL pipeline. Presently, it is unclear whether TransCanada will seek to revive its NAFTA claims in light of this latest setback to the project.

V RECOMMENDATIONS FOR INVESTORS

The ISDS arbitration provisions in USMCA represent a significant departure from those in NAFTA. US and Mexican investors in Canada will be unable to bring claims against Canada under USMCA, and Canadian investors also will be prevented from bringing such claims against the United States or Mexico. US and Mexican claimants also will have fewer potential grounds for claims, except where they are relying on a government contract in a covered sector, and will be required to comply with domestic litigation requirements (under certain circumstances) before commencing arbitration.

The full impact of the changes in USMCA remains to be seen. Though investors may not need to rethink their investment plans, there are some issues investors should consider while the fate of USMCA remains unclear.

For those who have NAFTA claims pending, the possible transition from NAFTA to USMCA will likely not have an impact on the ongoing procedure. The NAFTA dispute resolution mechanism will still be in place until the end of the dispute. This would likely not be the case, however, if a case relating to a legacy investment is annulled and later resubmitted if the resubmission occurs more than three years after NAFTA is terminated.

Investors with legacy investments who have potential claims and want to take advantage of the NAFTA dispute settlement mechanism, will want to submit a formal notice of arbitration no later than two years and nine months after the entry into force of USMCA. That is because legacy investment claims must be brought within three years after NAFTA is terminated; NAFTA contains a (minimum) 90-day notice provision, so investors will want to closely watch the clock and submit their claims in good time.

For investors who intend to establish or acquire investments after the entry into force of USMCA, special consideration should be given to address how to avoid or resolve potential

\(^{40}\) This excludes approximately 23 claims that have been inactive for an extended period.

\(^{41}\) TransCanada Corporation and TransCanada PipeLines Limited v. The United States of America, ICSID Case No. ARB/16/21.
conflicts when drafting agreements with government entities. NAFTA remedies would no longer be available and USMCA does not provide investors the same broad rights to initiate arbitration directly against the Member States. As a result, investors will want to include in such agreements clear and unambiguous language concerning their dispute resolution rights, including, if applicable, the right to resort to arbitration.

In spite of the fact that USMCA has narrowed the scope of available procedure and remedies in the dispute resolution context, the progress made in other areas could provide certain benefits. For instance, the inclusion of broader intellectual property protections and new market access may prove more favourable.

Although President Trump has described USMCA as ‘the largest, most significant, modern and balanced trade agreement in history’, the real impact of USMCA (if ratified) remains to be seen. Investors awaiting the ultimate fate of NAFTA and USMCA will want to carefully consider their current and future investments. Given USMCA’s limitations, beyond considering whether they should bring claims now rather than waiting until USMCA is ratified, investors should evaluate other potential means of protecting their investments in the Member States beyond those contained explicitly in USMCA. In any event, investors will want to be prepared to move swiftly to protect their current and future rights if USMCA is ratified.

### APPENDIX: NAFTA CHAPTER 11 CLAIMS

The table below is drawn in part from Scott Sinclair, Trade and Investment Research Project, Canada Center for Policy Alternatives.  

<table>
<thead>
<tr>
<th>Case and date</th>
<th>Issue</th>
<th>Status</th>
<th>Arbitration information</th>
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</table>
| Amtrade International v. Mexico  
Administering institution: N/A  
Arbitral tribunal: Not constituted |
| Halchette Corp. v. Mexico  
Administering institution: N/A  
Arbitral tribunal: Not constituted |
| Signa SA v. Canada  
Notice of Intent submitted on 4 March 1996 | The investor alleged Canada expropriated its investment and violated the minimum standard of treatment. Damages sought: C$50 million. | Notice of intent was withdrawn by investor. Arbitration never commenced. | Arbitration rules: N/A  
Administering institution: N/A  
Arbitral tribunal: Not constituted |
| Ethyl Corporation v. Canada, ad hoc (UNCITRAL)  
Administering institution: N/A  
Arbitral tribunal: Karl-Heinz Böckstiegel (President), Charles N Brower (appointed by claimant), José Luis Siqueros (appointed by respondent) |
| Sun Belt Water, Inc v. Canada  
Administering institution: N/A  
Arbitral tribunal: Not constituted |
| Metalclad Corp v. Mexico, ICSID Case No. ARB(AF)/97/1  
Notice of Intent submitted on 2 October 1996 | US waste management company challenged decisions by a Mexican local government to refuse it a permit to operate a hazardous waste treatment facility and landfill site. Damages sought: US$90 million. | In August 2000, the tribunal ruled that Mexico's failure to grant the investor a municipal permit and the state decree declaring the area an ecological zone was 'tantamount to expropriation' without compensation and breached the 'minimum standard of treatment' in NAFTA 1105. Mexico was ordered to pay US$16.7 million (of the US$90 million requested) in compensation. Mexico applied for statutory review of the tribunal award before the BC Supreme Court on the ground that the tribunal had exceeded its jurisdiction. The court set aside part of the award dealing with minimum standards of treatment, but it allowed US$15.6 million of the tribunal's original award of damages to stand. | Arbitration rules: ICSID Additional Facility Rules  
Administering institution: ICSID  
Arbitral tribunal: Elihu Lauterpacht (President), Benjamin R Civiletti (appointed by claimant), José Luis Siqueros (appointed by respondent) |

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<table>
<thead>
<tr>
<th>Case and date</th>
<th>Issue</th>
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<tr>
<td>Robert Azizian v. Mexico, ICSID Case No. ARB(AF)/97/2 Notice of Intent submitted on 24 November 1996</td>
<td>US waste management company challenged Mexican court ruling revoking its contract for non-performance of waste disposal and management in Naucalpan de Juárez. Damages sought: more than US$17 million.</td>
<td>On 1 November 1999, the tribunal dismissed the investor's claims. It held that the annulment of the concession contract was not an act of expropriation and based on the circumstances of this case, if there was no violation of Article 110, there was none of Article 1105 either.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Jan Paulsson (President), Benjamin R Civiletti (appointed by claimant), Claus Von Wobeser (appointed by respondent)</td>
</tr>
<tr>
<td>Marvin Roy Feldman Karpas v. Mexico, ICSID Case No. ARB(AF)/99/1 Notice of Intent submitted on 20 February 1998</td>
<td>US cigarette exporter challenged Mexican government decision not to rebate taxes on its cigarette exports. Damages sought: US$50 million.</td>
<td>On 16 December 2002, the tribunal rejected the investor's expropriation claim, but upheld the claim of a violation of national treatment. Mexico was ordered to pay compensation of US$0.9 million plus US$1 million in interest. Mexico appealed the award in the Ontario Superior Court of Justice. In December 2003, the court dismissed Mexico's application. Mexico's appeal of this decision was rejected by the Ontario Court of Appeal on 11 January 2005.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Konstantinos D Kerameus (President), Jorge Covarrubias Bravo (appointed by claimant), David A Gantz (appointed by respondent)</td>
</tr>
<tr>
<td>Waste Management, Inc v. Mexico, ICSID Case No. ARB(AF)/98/2 Notice of Intent submitted on 20 February 1998</td>
<td>US waste management company challenged state and local government actions in contract dispute with a Mexican subsidiary over waste disposal services in Acapulco. Damages sought: US$60 million.</td>
<td>Case registered at ICSID on 18 November 1998; tribunal was constituted on 3 June 1999. In its award rendered on 2 June 2000, the tribunal held it lacked jurisdiction because Waste Management had not properly waived domestic legal remedies as required by NAFTA. One of the arbitrators, Mr Keith Highet, issued a dissenting opinion.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Bernardo M Cremades (President), Keith Hight (appointed by claimant), Eduardo Siqueiros T (appointed by respondent), Julio C Treviño (appointed by respondent) (replaced)</td>
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<tr>
<td>SD Meyers, Inc v. Mexico, ad hoc (UNCITRAL) Notice of Intent submitted on 21 July 1998</td>
<td>Waste disposal firm challenged temporary ban on export of toxic PCB waste. Damages sought: US$20 million.</td>
<td>Tribunal held that Canada violated NAFTA Articles 1102 and 1105. It awarded the investors around CS2 million in compensation (including CS$850,000 in interest), plus CS$500,000 in costs. Canada applied to the federal court to set aside the tribunal's award. On 13 January 2004, the court dismissed Canada's application.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: J Martin Hunter (President), Bryan P Schwartz (appointed by claimant), Edward C Chiasson (appointed by respondent), Bob Rae (appointed by respondent) (replaced)</td>
</tr>
<tr>
<td>The Loewen Group Inc v. US, ICSID Case No. ARB(AF)/98/3 Notice of Intent submitted on 29 July 1998</td>
<td>Loewen, a Canadian funeral home operator, challenged a jury verdict in a Mississippi state court that awarded US$500 million in compensation against it. Loewen also alleged that bond requirements for leave to appeal were excessive. Damages sought: US$725 million.</td>
<td>In June 2003, the tribunal determined that it 'lacked jurisdiction' to determine the investor's claims and dismissed them. The Loewen Group went bankrupt and assigned its NAFTA claims to a newly created Canadian corporation owned and controlled by the US corporation. The panel ruled that this entity was not a genuine foreign investor capable of pursuing the NAFTA claim. On 31 October 2005, a US court denied Raymond Loewen's petition to vacate the tribunal's award.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Anthony Mason (President), Abner J Mlwaka (appointed by claimant), Michael Mustill (appointed by respondent), L Yves Fortier (appointed by claimant) (replaced)</td>
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<td>Case and date</td>
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<td>Pope &amp; Talbot Inc v. Canada, ad hoc (UNCITRAL) Notice of Intent submitted on 24 December 1998</td>
<td>Challenge to lumber export quota system implementing Canada–US softwood lumber agreement. Damages sought: US$500 million.</td>
<td>Tribunal ruled that Canada violated NAFTA Article 1105. Canada ordered to pay US$460,000 in compensation (plus interest) and part of the investor’s legal costs, for a total of nearly US$600,000.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Lord Dervaird (President), Benjamin J Greenberg, Murray J Belman (arbitrators)</td>
</tr>
<tr>
<td>Mondev International Ltd v. US, ICSID Case No. ARB(AF)/99/2 Notice of Intent submitted on 6 May 1999</td>
<td>The investor alleged that a Massachusetts law immunising local governments from tort liability violates minimum standards of treatment under NAFTA. Damages sought: US$50 million.</td>
<td>In October 2002, the tribunal dismissed the investor’s claims. It ruled that Mondev’s claims were time-barred because the underlying dispute pre-dated NAFTA.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Ninian Stephen (President), James R Crawford (appointed by claimant), Stephen M Schwedel (appointed by respondent)</td>
</tr>
<tr>
<td>Methanex Corp v. US, ad hoc (UNCITRAL) Notice of Intent submitted on 2 July 1999</td>
<td>Challenge to California’s phase-out of MTBE, a gasoline additive that contaminated ground and surface water throughout California. Damages sought: US$970 million.</td>
<td>On 9 August 2005, the tribunal dismissed the investor’s claims. It ordered Methanex to pay the US government legal costs of US$3 million and the full cost of the arbitration.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: V V Veeder (President), J William F Rowley (appointed by claimant), W Michael Reisman (appointed by respondent)</td>
</tr>
<tr>
<td>Fireman's Fund Insurance Co v. Mexico, ICSID Case No. ARB(AF)/02/1 Notice of Intent submitted on 15 November 1999</td>
<td>US insurance company alleged that the Mexican government discriminated against it by facilitating the sale by Mexican financial institutions of peso-denominated debentures, but not the sale of US dollar-denominated debentures by Fireman’s Fund. Damages sought: US$50 million.</td>
<td>On 17 July 2006, tribunal dismissed the investor’s claim. It determined that, while the investor had been subjected to discriminatory treatment, under the NAFTA financial services chapter rules only claims involving expropriation were open to investor-state challenge. It ruled that Mexico’s treatment of the investor did not rise to the level of expropriation.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Albert Jan Van Den Berg (President), Andreas F Lowenfeld (appointed by claimant), Alberto Guillermo Saavedra Olavarrieta (appointed by respondent), Francisco Carrillo Gamboa (appointed by respondent) (replaced)</td>
</tr>
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<td>United Parcel Service of America Inc v. Canada, ICSID Case No. UNCT/02/1 Notice of Intent submitted on 19 January 2000</td>
<td>Multinational US courier company alleged that Canada Post’s limited monopoly over letter mail and its postal service infrastructure enable it to compete unfairly in express delivery. UPS also alleged that Canada Post enjoyed other advantages denied to the investor (e.g., favourable customs treatment). Damages sought: US$160 million.</td>
<td>Notice of Arbitration filed on 19 April 2000. On 24 May 2007, the tribunal dismissed the investor’s claims. It determined that key NAFTA rules concerning competition policy could not be invoked by an investor under Chapter 11, and that certain activities of Canada Post were essentially at arm’s length from the Canadian government and therefore not subject to challenge by the investor. (Such activities could be scrutinised in a government-to-government dispute.) It also rejected claims that Canada Post unduly benefited from more favourable treatment.</td>
<td>Arbitration rules: UNCITRAL Administering institution: ICSID Arbitral tribunal: Kenneth Keith (President), Ronald A Cass, I Yes Fortier (arbitrators)</td>
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</table>
### NAFTA in Transition: The Current State of Play and What Comes Next

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<tr>
<td><strong>ADF Group Inc v. US, ICSID Case No. ARB(AF)/00/1</strong> Notice of Intent submitted on 1 March 2000</td>
<td>Challenge to US ‘Buy America’ preferences requiring that US steel be used in federally funded state highway projects. Damages sought: US$90 million.</td>
<td>In January 2003, the tribunal dismissed the investor’s claim. It concluded that the measures in question were procurement measures exempted under Article 1108.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Florencia P. Feliciano (President), Armand De Mestral (appointed by claimant), Carolyn R. Lamm (appointed by respondent)</td>
</tr>
<tr>
<td><strong>Waste Management Inc v. Mexico, ICSID Case No. ARB(AF)/00/3</strong> Notice of Arbitration submitted on 19 June 2000</td>
<td>US waste management company challenged state and local government actions in contract dispute with a Mexican subsidiary over waste disposal services in Acapulco. Damages sought: US$60 million.</td>
<td>The investor resubmitted its Notice of Arbitration in this case to address the deficiencies in its waiver of domestic remedies (see above). The tribunal subsequently confirmed its jurisdiction. On 30 April 2004, it dismissed the investor’s claims on the ground that there was nothing that could be properly described as an expropriation by Mexico and the conduct of Mexico did not otherwise violate NAFTA.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: James R. Crawford (President), Benjamin R. Civiletti (appointed by claimant), Eduardo Magallón Gómez (appointed by respondent), Guillermo Aguilar-Alvarez (appointed by respondent) (replaced)</td>
</tr>
<tr>
<td><strong>Trammel Crow Co v. Canada</strong> Notice of Intent submitted on 7 September 2001</td>
<td>US property management company alleged that Canada Post treated it unfairly in the outsourcing of certain real estate services. Damages sought: US$32 million.</td>
<td>Claims were withdrawn by investor in April 2002 after it reached an undisclosed settlement with Canada Post.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
</tr>
<tr>
<td><strong>Lomas de Santa Fe v. Mexico</strong> Notice of Intent submitted on 28 August 2001</td>
<td>US investor alleged that it was treated unfairly and inadequately compensated in a dispute over the expropriation of land by Mexican authorities. Investor sought US$210 million in damages.</td>
<td>Claim is inactive.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
</tr>
<tr>
<td><strong>Canfor Corporation v. US</strong> Notice of Intent submitted on 5 November 2001</td>
<td>Canadian lumber company challenged US anti-dumping regulation and countervailing duties imposed on Canadian softwood lumber exports as well as relating to the Byrd Amendment. Damages sought: US$250 million.</td>
<td>Notice of Arbitration submitted on 9 July 2002. On 7 September 2005, at the request of the US government, the Canfor, Terminal and Tembec claims were consolidated into a single arbitration. On 6 June 2006, the tribunal determined that it had no jurisdiction over claims relating to US dumping and countervailing duty law, but that it did have jurisdiction to decide claims regarding the Byrd Amendment. Canfor withdrew its claim as a condition of the October 2006 Softwood Lumber Agreement between the US and Canadian governments.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal (before consolidation): Emmanuel Gaillard (President), Joseph Weiler, Conrad Harper (arbitrators) Arbitral tribunal (after consolidation): Albert Jan Van Den Berg (President), Armand L.C. de Mestral, Davis R Robinson (both appointed by the Secretary-General of ICSID)</td>
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<td>Gami Investments Inc v. Mexico, ad hoc (UNCITRAL) Notice of Intent submitted on 1 October 2001.</td>
<td>US shareholders in a Mexican sugar company claimed that their interests were harmed by Mexican government regulatory measures related to processing and export of raw and refined sugar, as well as the nationalisation of failing sugar refineries. Damages sought: US$55 million.</td>
<td>On 15 November 2004, the tribunal ruled that it had no jurisdiction and dismissed the investor's claim.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Jan Paulsson (President), W Michael Reisman (appointed by claimant), Julio Lacarte Muró (appointed by respondent)</td>
</tr>
<tr>
<td>Chemtura Corp v. Canada, PCA Case No. 2008-01 (UNCITRAL) Notice of Intent submitted on 6 November 2001.</td>
<td>Challenge to the Canadian government’s ban on the sale and use of lindane, an agricultural pesticide. Damages sought: US$100 million.</td>
<td>On 2 August 2010, the tribunal dismissed the investor's claims. It ordered the investor to pay the costs of the arbitration (US$688,000) and to pay 50 per cent of the government of Canada's costs in defending the claim (C$5,778 million).</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: Gabrielle Kaufmann-Kohler (President), James R Crawford, Charles N Brower (arbitrators)</td>
</tr>
<tr>
<td>Francis Kenneth Haas v. Mexico Notice of Intent submitted on December 12, 2001</td>
<td>US investor in manufacturing company in Mexico alleged unfair treatment by Mexican courts and authorities in the investor's dispute with local partners in the company. Damages sought: approximately US$35 million.</td>
<td>Claim is inactive.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
</tr>
<tr>
<td>International Thunderbird Gaming Corp v. Mexico, Ad hoc (UNCITRAL) Notice of Intent submitted on 22 March 2002</td>
<td>Canadian gambling company challenged the regulation and closure of its gambling facilities by the Mexican government. Damages sought: US$100 million.</td>
<td>On 26 January 2005 the tribunal dismissed the investor's claim. Thunderbird Gaming was ordered to pay Mexico's legal costs of approximately US$1.2 million and three-quarters of the cost of the arbitration. On 14 February 2007, a US court rejected Thunderbird Gaming's petition to vacate the NAFTA tribunal’s ruling.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Albert Jan Van Den Berg (President), Thomas W Walde (appointed by claimant), Agustin Portal Ariosa (appointed by respondent)</td>
</tr>
</tbody>
</table>
### NAFTA in Transition: The Current State of Play and What Comes Next

#### Case and date
- **Doman Inc v. US**
  - Notice of Intent submitted on 1 May 2002
- **Tembec Inc et al v. US**
  - Notice of Intent submitted on 3 May 2002
- **Paget et al & 800438 Ontario Limited v. US**
  - Notice of Intent submitted on 9 September 2002
- **Corn Products International v. Mexico, ICSID Case No. ARB(AF)/04/1**
  - Notice of Intent was submitted on 28 January 2003
- **Terminal Forest Products Ltd v. US**
  - Notice of Intent submitted on 12 June 2003

#### Issue
- **Doman Inc v. US**
  - Challenge to US anti-dumping regulation and countervailing duties imposed on Canadian softwood lumber exports as well as relating to the Byrd Amendment. Damages claimed: US$513 million.
- **Tembec Inc et al v. US**
  - Challenge to US anti-dumping regulation and countervailing duties imposed on Canadian softwood lumber exports as well as relating to the Byrd Amendment. Damages claimed: US$200 million.
- **Paget et al & 800438 Ontario Limited v. US**
  - Property of three Florida subsidiaries of an Ontario company was seized following allegations of racketeering, corrupt practices and tax violations. Ontario Ltd claimed that the US improperly refused to return its property and destroyed its financial records. Damages claimed: US$38 million.
- **Corn Products International v. Mexico, ICSID Case No. ARB(AF)/04/1**
  - Challenge to a range of Mexican government measures that allegedly discouraged the import, production and sale of high-fructose corn syrup (HFCS), including a tax on soft drinks sweetened with HFCS. Mexico argued that it applied the 20 per cent tax to protect its sugar cane industry, which is losing domestic market share to imported HFCS, while facing barriers in selling sugar in US. Damages sought: US$325 million.
- **Terminal Forest Products Ltd v. US**
  - Challenge to US anti-dumping regulation and countervailing duties imposed on Canadian softwood lumber exports as well as relating to the Byrd Amendment. Damages claimed: US$90 million.

#### Status
- **Doman Inc v. US**
  - Claim is inactive.
- **Tembec Inc et al v. US**
  - Notice of Arbitration and Statement of Claim submitted on 3 December 2004. On 7 September 2005, the Canfor, Terminal and Tembec claims were consolidated into a single arbitration. In December 2005, Tembec withdrew its claim. It then unsuccessfully challenged the consolidation order in US courts. In July 2007, the tribunal ordered Tembec to pay part of the arbitration costs as well as part of the legal costs of the US.
- **Paget et al & 800438 Ontario Limited v. US**
  - Claim is inactive.
- **Corn Products International v. Mexico, ICSID Case No. ARB(AF)/04/1**
  - Mexico sought to consolidate the claims with those of Archer Daniels. A consolidation tribunal denied the request. In January 2008, the tribunal ruled that Mexico had violated NAFTA's national treatment obligation. It dismissed the investor's claims that the tax was a prohibited performance requirement and tantamount to expropriation. After a July 2008 hearing on quantum, in August 2009, Mexico was ordered to pay the investor US$58.4 million. On 1 October 2009, the claimant filed a request for correction and interpretation of the award. On 23 March 2010, the tribunal issued a decision denying the claimants' request for correction and interpretation.
- **Terminal Forest Products Ltd v. US**
  - Notice of Arbitration submitted on 31 March 2004. On 7 September 2005, the Canfor, Terminal and Tembec claims were consolidated into a single arbitration. On 6 June 2006, the tribunal determined that it had no jurisdiction over claims relating to US dumping and countervailing duty law, but that it did have jurisdiction to decide claims regarding the Byrd Amendment. Terminal withdrew its claim as a condition of the October 2006 Softwood Lumber Agreement between the US and Canadian governments.

#### Arbitration information
- **Doman Inc v. US**
  - Arbitration rules: N/A
  - Administering institution: N/A
  - Arbitral tribunal: Not constituted
- **Tembec Inc et al v. US**
  - Arbitration rules: UNCITRAL
  - Administering institution: N/A
  - Arbitral tribunal: Albert Jan Van Den Berg (President), Armand LC de Mestral, Davis R Robinson (both appointed by the Secretary-General of ICSID)
- **Paget et al & 800438 Ontario Limited v. US**
  - Arbitration rules: N/A
  - Administering institution: N/A
  - Arbitral tribunal: Not constituted
- **Corn Products International v. Mexico, ICSID Case No. ARB(AF)/04/1**
  - Arbitration rules: ICSID Additional Facility Rules
  - Administering institution: ICSID
  - Arbitral tribunal: Christopher Greenwood (President), Andreas F Lowenfeld (appointed by claimant), Jesus Serrano De La Vega (appointed by respondent), Manuel E Tron (appointed by respondent) (replaced)
- **Terminal Forest Products Ltd v. US**
  - Arbitration rules: UNCITRAL
  - Administering institution: N/A
  - Arbitral tribunal (after consolidation): Albert Jan Van Den Berg (President), Armand LC de Mestral, Davis R Robinson (both appointed by the Secretary-General of ICSID)

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<tr>
<td>Glamis Gold Ltd v. US Notice of Intent submitted on 21 July 2003</td>
<td>Allegations that regulations intended to limit environmental impact of open-pit mining and to protect indigenous peoples' religious sites made proposed gold mine in California unprofitable, thereby expropriating investment and denying fair and equitable treatment. Damages claimed: over US$50 million.</td>
<td>Notice of Arbitration submitted on 9 December 2003. On 8 June 2009, the tribunal dismissed the investor's claims, finding that the environmental regulations were not sufficiently severe to constitute an expropriation or minimum standards or treatment. It ordered the company to pay two-thirds of the costs of the proceeding.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Michael K Young (President), Kenneth D Hubbard (appointed by claimant), Donald L Morgan (appointed by claimant) (resigned), David Caron (appointed by respondent)</td>
</tr>
<tr>
<td>Grand River Enterprises Six Nations Ltd et al v. US, ad hoc (UNCITRAL) Notice of Intent was submitted on 15 September 2003</td>
<td>Allegations that business was harmed by the treatment of non-participating manufacturers' under the terms of a settlement agreement between 46 US states and the major tobacco companies to recoup public monies spent to treat smoking-related illnesses. Damages sought: more than US$340 million.</td>
<td>In January 2011, after protracted proceedings, the tribunal dismissed the manufacturer's claim on jurisdictional grounds and dismissed the wholesaler's claim on its merits. It ruled that the costs of arbitration be split equally between the parties.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Fali S Nazirian (President), James Anaya (appointed by claimant), John R Crook (appointed by respondent)</td>
</tr>
<tr>
<td>Archer Daniels Midland v. Mexico, ICSID Case No. ARB(AF)/04/5 Notice of Intent was submitted on 14 October 2003</td>
<td>Challenge to a range of Mexican government measures that allegedly discouraged the import, production and sale of HFCS, including a tax on soft drinks sweetened with HFCS. Damages sought: US$100 million.</td>
<td>In November 2007, the tribunal ruled that Mexico had violated NAFTA’s national treatment obligation, and that the tax on HFCS constituted a prohibited performance requirement. Mexico was ordered to pay the investors US$33.5 million.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Bernardo M Cremades (President), Arthur W Rovine, Eduardo Siqueiros (arbitrators)</td>
</tr>
<tr>
<td>Albert J Connolly (Brownfields Holding, Inc) v. Canada Notice of Intent submitted on 19 February 2004</td>
<td>US investor claimed actions of Ontario mining agency resulted in forfeiture of investor's interest in a quarry site. Amount in dispute not available.</td>
<td>Claim is inactive.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<tr>
<td>Canadian Cattlemen for Fair Trade v. US Notice of Intent submitted on 12 August 2004</td>
<td>Over 100 Canadian cattle farmers challenged US ban on imports of Canadian live cattle following discovery in 2003 of a cow infected with bovine spongiform encephalopathy from a herd in Alberta. Damages claimed: over US$235 million.</td>
<td>The first Notices of Arbitration were submitted on 16 March 2005; with subsequent Notices of Arbitration by each of the claimants submitted between 16 March 2005 and 2 June 2005. Over 100 claims were consolidated into a single arbitration. In January 2008, the tribunal dismissed the claims on jurisdictional grounds because they determined the claimants did not make or have an investment in the US, but only in Canada.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Karl-Heinz Böckstiegel (President), James Bacchus (appointed by claimant), Lucinda Low (appointed by respondent)</td>
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<td>Bayview Irrigation District et al v. Mexico, ICSID Case No. ARB(AF)/05/1</td>
<td>Seventeen Texas irrigation districts claimed that the diversion of water from Mexican tributaries of the Rio Grande watershed discriminated against downstream US water users, breached Mexico's commitments under bilateral water-sharing treaties and expropriated water 'owned' by US interests. Damages sought: US$554 million.</td>
<td>On 21 June 2007, the tribunal dismissed the claims and ruled that the claimants, who were US nationals whose investments were located within the territory of the US, did not qualify as foreign investors entitled to protection under NAFTA.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Vaughan Lowe (President), Edwin Meese III (appointed by claimant), Ignacio Gómez Palacio (appointed by respondent)</td>
</tr>
<tr>
<td>Cargill Inc v. Mexico, ICSID Case No. ARB(AF)/05/2</td>
<td>A large US agri-business challenged a range of Mexican government measures that allegedly discouraged the import, production and sale of HFCS, including a tax on soft drinks sweetened with HFCS. Damages sought: more than US$100 million.</td>
<td>The tribunal found against Mexico in an award rendered on 18 September 2009. The award has not yet been publicly released. Mexico was ordered to pay the investor US$77.3 million plus US$13.4 million in interest for a total award of US$90.7 million. The decision was upheld by the Supreme Court of Canada.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Michael C Pyles (President), David D Caron (appointed by claimant), Donald M McRae (appointed by respondent)</td>
</tr>
<tr>
<td>Peter Petis v. Canada</td>
<td>US investor claimed that Canadian government decision not to extend his temporary work visa impaired his investments in Canada.</td>
<td>Notice of intent to submit claim to arbitration was withdrawn by the investor.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<tr>
<td>Merrill &amp; Ring Forestry LP v. Canada, ICSID Case No. UNCT/07/1</td>
<td>US forestry company alleged that Canadian federal and provincial regulations and policies restricting export of forestry products represent discriminatory treatment, expropriation and violate minimum standards of treatment. Damages claimed: US$25 million.</td>
<td>Award on 31 March 2010. Tribunal dismissed the investor's claims and ordered the costs of the proceedings be split between the two parties. It determined the investor had not demonstrated that minimum standards of treatment had been violated.</td>
<td>Arbitration rules: ICSID Administering institution: ICSID Arbitral tribunal: Francisco Orrego Vicuña (President, appointed by Secretary-General), Kenneth Dam (appointed by claimant), J William Rowley (appointed by respondent)</td>
</tr>
<tr>
<td>Vito G Gallo v. Canada</td>
<td>Claim filed following transfer of control of a project asserting legislation was 'tantamount to expropriation' and depriving the minimum standard of treatment. Damages sought: CS$105 million.</td>
<td>Statement of Claim submitted on 23 June 2008. Jurisdictional hearing in February 2011. Award issued on 15 September 2011 dismissing the claims on jurisdictional grounds. The tribunal concluded that Mr Gallo could not prove that he acquired ownership and control prior to enactment of the legislation. He was ordered to pay Canada US$450,000 towards its legal costs.</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: Juan Fernández-Armesto (President), Jean-Gabriel Castel (appointed by claimant), Laurent Lévy (appointed by respondent)</td>
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<td>Mobil Investments Canada Inc &amp; Murphy Oil Corporation v. Canada, ICSID Case No. ARB(AF)/07/4 Notice of Intent for Mobil Investments submitted on 2 August 2007; Notice of Intent for Murphy Oil submitted on 3 August 2007</td>
<td>The investors alleged that Canadian guidelines stipulating that energy companies active in the offshore invest in research and development within Newfoundland and Labrador were NAFTA-inconsistent performance requirements. The claimants previously challenged these guidelines in the Canadian courts and lost. Damages sought: C$60 million.</td>
<td>On 22 May 2012, the tribunal ruled that the local R&amp;D requirements constituted a ‘prohibited performance requirement’ under Article 1106. It rejected Canada's arguments that the guidelines fell within the scope of the Canadian reservation with respect to Article 1106. It also dismissed the investors’ claim that the R&amp;D guidelines breached Article 1105. The tribunal majority found Canada has been violating NAFTA Article 1106 since 2004, meaning that as long as the R&amp;D guidelines remain in effect, damages will accrue. The award was issued in February 2015. Damages were set at US$132 million. A set-aside application by Canada in the Federal Court was dismissed.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Hans Van Houtte (President), Merit Janow (appointed by claimant), Philippe Sands (appointed by respondent)</td>
</tr>
<tr>
<td>Apotex Inc v. US (I), ICSID Case No. UNCT/10/2 Notice of Intent submitted on 21 September 2007</td>
<td>In 2003, Apotex sought US Food and Drug Administration (FDA) approval to develop a generic version of Pfizer's anti-depressant medication, Zoloft (sertraline hydrochloride once Pfizer's patent expired in 2006). Apotex later went to court to dispel uncertainty regarding the status of the Pfizer patents. US courts dismissed Apotex's suit for a declaratory judgment clarifying the patent situation. Apotex alleged that the US court judgments discriminated against it, denied it minimum standard of treatment and expropriated its investment in sertraline. Damages sought: US$8 million.</td>
<td>On 14 June 2013, the tribunal dismissed the claim on jurisdictional grounds, ruling that Apotex did not have investments in the US that qualified for protection under NAFTA Chapter 11. Apotex was ordered to pay all costs of the proceedings.</td>
<td>Arbitration rules: UNCITRAL Administering institution: ICSID Arbitral tribunal: Toby Landau (President), Clifford M Davidson (appointed by claimant), Fern M Smith (appointed by respondent)</td>
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<td><strong>Apopthe Inc v. US (II). ICSID Case No. UNCT/10/2</strong> Notice of Intent submitted on 2 March 2009</td>
<td>Apotex sought FDA approval to develop a generic version of heart medication pravastatin sodium tablets marketed by Bristol Myers Squibb (BSM) (under the brand name Pravachol once BSM's patent expired in 2006). Apotex alleged that certain US court judgments and FDA decisions discriminated against it, denied it minimum standard of treatment and expropriated its investment in pravastatin. Damages sought: US$8 million.</td>
<td>By agreement of the parties, the jurisdiction phase in this arbitration (the pravastatin claim) and the above arbitration (the sertraline claim) were held concurrently, even though they were not consolidated. Determinations on preliminary issues in both arbitrations were set out in a single award. Both claims were dismissed on jurisdictional grounds. The tribunal held that Apotex did not have investments in the US that qualified for protection under NAFTA Chapter 11. Apotex was ordered to pay all costs of the proceedings.</td>
<td>Arbitration rules: ICSID Administering institution: ICSID Arbitral tribunal: Toby Landau (President), Clifford M Davidson (appointed by claimant), Fern M Smith (appointed by respondent)</td>
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<tr>
<td><strong>Gentileh Investors Group v. Canada</strong> Notice of Intent submitted on 22 April 2008</td>
<td>US-based private investor group alleged that changes in tax treatment of energy income tax trusts discriminated against US entities and were equivalent to expropriation, and violated minimum standards of treatment. Damages sought: US$6.5 million.</td>
<td>The investor was barred from bringing the expropriation claim. It could have proceeded on its other claims (Articles 1102, 1103 and 1105) but No Notice of Arbitration has been submitted to date. The claim has been inactive since the determination made by US and Canadian tax authorities.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<tr>
<td><strong>Clayton/Bilcon Inc v. Canada, PCA Case No. 2009-04 (UNCITRAL)</strong> Notice of Intent submitted on 5 February 2008</td>
<td>The investor alleged that the administration of an environmental assessment review, along with various provincial and federal government measures, were discriminatory or violated minimum standards of treatment, or both. Damages sought: US$101 million.</td>
<td>The tribunal found in favour of Bilcon, noting that the regulatory process was unfair in that it introduced new concepts and principles without notice. Canada attempted to have the award set aside by the Federal Court in an application filed on 16 June 2015, but it was dismissed by the Court on 2 May 2018. A hearing on damages was held between 19–27 February 2018. Bilcon claimed over US$440 million. On 10 January 2019, the tribunal issued an award granting claimants only US$7 million, a bit more than their sunk costs. The tribunal appears to have reached this conclusion because it was not convinced that the quarry project would have been approved absent Canada's NAFTA breaches.</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: Bruno Simma (President), Bryan Schwartz (appointed by claimant), Donald M McRae (appointed by respondent)</td>
</tr>
<tr>
<td><strong>Georgia Basin Holdings LP v. Canada</strong> Notice of Intent submitted on 5 February 2008</td>
<td>Allegations that Canadian federal and provincial regulations and policies restricting export of forestry products represent discriminatory treatment, expropriation and violate minimum standards of treatment. Damages sought: US$55 million.</td>
<td>This claim is inactive. In late 2007, counsel for Merrill &amp; Ring requested Georgia Basin Holdings be added as a party to the Merrill &amp; Ring arbitration. On 31 January 2008, the tribunal decided not to allow Georgia Basin to participate in the arbitration. Claimant has not brought separate claims against Canada to date.</td>
<td>Arbitration rules: UNCITRAL Administering institution: ICSID Arbitral tribunal: Francisco Orrego Vicuña (President), Kenneth W Dam (appointed by claimant), J William Rowley (appointed by respondent)</td>
</tr>
<tr>
<td><strong>Melvin J Howard, Centurion Health Corporation v. Canada, PCA No. 2009-21</strong> Notice of Intent submitted on 11 July 2008</td>
<td>US investor alleged plans for private, fee-for-service health clinics in British Columbia and Alberta were frustrated by local, provincial and federal regulatory measures. Damages sought: US$160 million.</td>
<td>Notice of Arbitration submitted on 5 January 2009. Revised Statement of Claim submitted on 2 February 2009. In August 2010, the tribunal terminated the claim because the investor failed to make the required deposits to continue the claim. The claimant was ordered to pay Canada's share of the arbitration costs.</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: Peter Tomka (President), Marjorie Florestall (appointed by claimant), Henri C Álvarez (appointed by respondent)</td>
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<td>Dow Agro Sciences LLC v. Canada</td>
<td>Dow Agro Sciences manufactures 2,4-D, an active ingredient in many commercial herbicides. In 2006, the Province of Quebec banned the use of these pesticides. Dow Agro Sciences alleged that the ban is without scientific basis and was imposed without providing a meaningful opportunity for the company to demonstrate that its product is safe. Dow further alleged that the ban is ‘tantamount to expropriation’. Damages sought: more than US$12 million.</td>
<td>On 25 May 2011, the parties reached a settlement under which Dow withdrew its claim. In return, the government of Quebec formally acknowledged that 2,4-D does not pose an ‘unacceptable risk’ to human health. The disputed regulatory measures related to pesticides are maintained and no compensation has been paid to the claimant.</td>
<td>Arbitration rules: UNCITRAL&lt;br&gt;Administering institution: Data not available&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<tr>
<td>William Jay Greiner and Malbaie River Outfitters Inc v. Canada</td>
<td>Allegations that conservation measures taken by Quebec provincial government to reduce the number of salmon fishing licenses and efforts to restrict access to certain salmon fishing areas, amounted to expropriation and discriminated against investor in favour of Canadian-owned fishing lodges in violation of minimum standards of treatment. Damages sought: US$7.5 million.</td>
<td>Notice of Arbitration was submitted on 2 November 2010. Amended Notice of Arbitration was submitted on 2 December 2010. Claim was withdrawn by investor on 10 June 2011.</td>
<td>Arbitration rules: N/A&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<td>Shell Family v. Canada</td>
<td>US family group of investors alleged Canadian courts and government agencies treated them unfairly during bankruptcy proceedings. Damages sought: US$21.3 million.</td>
<td>Claim is inactive.</td>
<td>Arbitration rules: N/A&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<td>David Bishop v. Canada</td>
<td>Allegations that conservation measures taken by Quebec provincial government to reduce the number of salmon fishing licenses and efforts to restrict access to certain salmon fishing areas, amounted to expropriation and discriminated against investor in favour of Canadian-owned fishing lodges in violation of minimum standards of treatment. Damages sought: US$1 million.</td>
<td>No Notice of Arbitration has been filed to date. Claim is inactive.</td>
<td>Arbitration rules: N/A&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<tr>
<td>Christopher and Nancy Lacich v. Canada</td>
<td>US investors alleged changes in tax treatment of energy income tax trusts were discriminatory, equivalent to expropriation of their investment and violated minimum standards of treatment. Damages sought: approximately US$1.2 million.</td>
<td>Notice of Intent was quickly withdrawn by investor.</td>
<td>Arbitration rules: N/A&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<td>AbitibiBowater Inc v. Canada, ICSID Case No. UNCT/10/1</td>
<td>In December 2008, the provincial government enacted legislation to return AbitibiBowater’s water use and timber rights to the Crown and to expropriate certain AbitibiBowater lands and assets associated with the water and hydroelectricity rights. Damages sought: C$467.5 million.</td>
<td>In August 2010, the Canadian federal government announced that it had agreed to pay AbitibiBowater C$130 million to settle the claim.</td>
<td>Arbitration rules: UNCITRAL&lt;br&gt;Administering institution: ICSID&lt;br&gt;Arbitral tribunal: Andreas Bucher (President), Doak Bishop (appointed by claimant), Gavan Griffith (appointed by respondent)</td>
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<td><strong>CANACAR v. US</strong>&lt;br&gt;Notice of Arbitration submitted on 2 April 2009</td>
<td>Truckers asserted that the US failed to permit Mexican truckers into the US to provide cross-border trucking services, barred them from investing in US companies providing cross-border trucking services and violated minimum standards of treatment by refusing to comply with a NAFTA government-to-government panel ruling. Damages sought: approximately US$2 billion a year.</td>
<td>Notice of Arbitration filed on 2 April 2009. In 2011, US and Mexico agreed to a three-year memorandum that allowed Mexican trucks to enter the US under certain conditions. In exchange, Mexico eliminated US$2.3 billion tariffs on US goods. There is no information that this case was withdrawn or otherwise terminated, although there has been no activity for many years.</td>
<td>Arbitration rules: UNCITRAL&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Thomas Heather Rodríguez (appointed by claimant)</td>
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<td><strong>Cemex v. US</strong>&lt;br&gt;Notice of Intent reportedly submitted in September 2009</td>
<td>Cemex is embroiled in a dispute with the state government of Texas over royalty fees on quarrying. The NAFTA claim is an attempt by Cemex to protect itself against potential losses in Texas courts.</td>
<td>Unavailable.</td>
<td>Arbitration rules: N/A&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<td><strong>Detroit International Bridge Company v. Canada, PCA Case No. 2012-25 (UNCITRAL)</strong>&lt;br&gt;Notice of Intent was submitted on 25 January 2010</td>
<td>Detroit International Bridge Company (DIBC) objected to Canadian government plans to build a second bridge across the Detroit River. Canada contended that the arbitration should be ‘time-barred’ because the investor filed the claim more than three years after learning about the alleged breaches. Damages sought: US$3.5 billion.</td>
<td>DIBC alleged that Canada had reneged on a commitment to build a direct connection between the Ontario 401 highway to the Ambassador bridge owned by DIBC and instead connected to the new proposed Gordie Howe bridge. On 2 April 2015, the NAFTA tribunal issued its award on jurisdiction dismissing the DIBC claim against Canada. The majority determined that the ongoing lawsuits by DIBC against Canada in the US District Court for the District of Columbia with respect to the same measures as those alleged in NAFTA meant that DIBC had failed to comply with the waiver requirements in Article 1121, which deprived the tribunal of jurisdiction of the entire dispute. The tribunal ordered DIBC to pay Canada C$2 million in costs.</td>
<td>Arbitration rules: UNCITRAL&lt;br&gt;Administering institution: PCA&lt;br&gt;Arbitral tribunal: Yves Derains (President), Michael Chernoff, Vaughan Lowe (arbitrators)</td>
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<td><strong>John R Andre v. Canada</strong>&lt;br&gt;Notice of Intent submitted on 19 March 2010</td>
<td>Allegations that conservation measures taken to decrease the number of caribou that can be hunted expropriated investment. Damages sought: over US$4 million.</td>
<td>No Notice of Arbitration has been submitted to date. Claim is inactive.</td>
<td>Arbitration rules: N/A&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<td><strong>International Vision (INVISA) et al v. Mexico</strong>&lt;br&gt;Notice of Intent submitted on 15 February 2011</td>
<td>A group of US investors alleged a decision not to renew a 10-year agreement regarding billboards on Mexican land near the US–Mexico border crossing constituted expropriation and violation of minimum standards of treatment. Damages sought: US$7.5 million.</td>
<td>No Notice of Arbitration has been submitted to date. Arbitration never commenced.</td>
<td>Arbitration rules: N/A&lt;br&gt;Administering institution: N/A&lt;br&gt;Arbitral tribunal: Not constituted</td>
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<td>St Mary's VCNA LLC v. Canada, PCA Case No. 2012-19 (UNCITRAL) Notice of Intent was submitted on 13 May 2011</td>
<td>St Mary's VCNA, alleged that its Canadian subsidiary, St Mary's Cement Inc, was the victim of political interference in its attempt to open a quarry. The Ontario Ministry for Municipal Affairs and Housing issued a zoning order that prevented the site from being converted from agricultural to extractive industrial use. St Mary's claimed the 2010 zoning order was unfair, arbitrary, discriminatory and expropriatory. Damages sought: US$275 million.</td>
<td>Canada attempted to have the claim dismissed pursuant to NAFTA Article 1113 on the grounds that St Mary's VCNA was a Brazilian-owned company without substantial US business activities and therefore did not qualify as a US investor. The parties reached a settlement on 28 February 2013, which saw St Mary's withdraw the claim in exchange for US$15 million in compensation from the Ontario government.</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: Michael C Pryles (President), Richard Stewart (appointed by claimant), Brigitte Stern (appointed by respondent)</td>
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<td>Mesa Power Group LLC v. Canada, PCA Case No. 2012-17 (UNCITRAL) Notice of Intent submitted on 6 July 2011</td>
<td>The Ontario feed-in tariff (FIT) programme provides incentives for renewable energy producers. Under this programme, projects are ranked to determine priority for government power purchase agreements and access to the transmission grid. The claimant alleged that 2011 changes to the FIT programme discriminated against Mesa by favouring other local and international investors. Damages sought: C$775 million.</td>
<td>In May 2016, the tribunal, with one dissent, dismissed all of Mesa's complaints and awarded Canada 30 per cent of its legal costs of C$3 million. Mesa appealed this decision to the District Court in Washington, DC. The court denied Mesa's petition to vacate and granted Canada's counter-petition to enforce the award issued on 15 June 2017. The case is concluded.</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: Gabrielle Kaufmann-Kohler (President), Charles N Brower (appointed by claimant), Toby Landau (appointed by respondent)</td>
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<td>Apotex Holdings Inc and Apotex Inc v. US, ICSID Case No. ARB(AF)/12/1 Notice of Intent submitted on 23 November 2011</td>
<td>Following an inspection of Apotex in 2009, Canadian manufacturing facilities and the FDA discovered deficiencies and issued an import alert on drugs produced in Apotex's facilities. Apotex claimed that the import alert resulted in substantial lost sales and claimed that similar measures were not taken by the FDA against Apotex's competitors. Therefore, the measures were discriminatory and violated minimum standards of treatment. Damages sought: US$520 million (reported).</td>
<td>On 25 August 2014, the tribunal dismissed all claims. By a 2:1 majority, the tribunal ruled that it lacked jurisdiction over certain claims that the tribunal found to be res judicata. The tribunal concluded that the import alert was a 'lawful and appropriate' exercise of the FDA's regulatory authority. The tribunal ordered Apotex to pay the US government's legal costs and three-quarters of the costs of the arbitration.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: V V Veeder (President), J William Rowley (appointed by claimant), John R Crook (appointed by respondent)</td>
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<td>Mercer International, Inc v. Canada, ICSID Case No. ARB(AF)/12/3 Notice of Intent submitted on 26 January 2012</td>
<td>Allegations that US investor was disadvantaged regarding other mills in the province with self-generating capabilities because of subsidies, preferential treatment and other measures by the provincial government towards its competitors. Damages sought: C$232 million.</td>
<td>Notice of Arbitration submitted on 30 April 2012. Registered at ICSID on 16 May 2012. Tribunal was constituted on 9 October 2012. It rendered an award on 6 March 2018, dismissing the claimant's claims and ordering it to pay C$9 million toward Canada's legal costs. The parties were ordered to split the arbitration costs. Claimant registered a request for a supplementary decision on 20 April 2018. The tribunal issued a decision on that request on 10 December 2018.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: V V Veeder (President), Francisco Orrego Vicuña (appointed by claimant), Zachary Douglas (appointed by respondent)</td>
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<td>Windstream Energy LLC v. Canada, PCA Case No. 2013-22 (UNCITRAL) Notice of Intent submitted on 17 October 2012</td>
<td>In 2009, Windstream signed a 20-year FIT contract with the Ontario Power Authority for the purchase of renewable energy. In February 2011, the government of Ontario announced a moratorium on freshwater offshore wind development on the grounds that further scientific research was needed into the impacts. Windstream claimed that the moratorium is discriminatory and tantamount to expropriation. Damages sought: C$475 million.</td>
<td>In December 2016, the tribunal ruled that it would dismiss the Windstream indirect expropriation claim but grant the claim that the offshore moratorium was unfair and inequitable, awarding Windstream damages of C$25 million and C$3 million in legal costs.</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: Veijo Heiskanen (President), R Doak Bishop (appointed by claimant), Bernardo Cremades (appointed by respondent)</td>
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<td>Eli Lilly and Company v. Canada, ICSID Case No. UNCT/14/2 Notice of Intent submitted on 7 November 2012</td>
<td>Zyprexa was first patented in Canada in 1980. Eli Lilly received a patent extension in 1991 on the ground that it had found new uses for the drug. In 2009, the Canadian Federal Court invalidated the patent extension based on a finding that the drug allegedly had not delivered the promised utility. Eli Lilly contested the invalidation of its patents in the Canadian courts. When it lost there, Eli Lilly filed under NAFTA claiming the new test was discriminatory. Damages sought: C$500 million.</td>
<td>On 17 March 2017, the tribunal dismissed Eli Lilly's claims and concluded that Canada was in full compliance with its NAFTA obligations. The tribunal ordered Eli Lilly to bear 75 per cent of Canada's legal costs, in addition to Canada's arbitration costs. Those costs were approximately C$85.2 million.</td>
<td>Arbitration rules: UNCITRAL Administering institution: ICSID Arbitral tribunal: Albert Jan Van Den Berg (President), Daniel Bethlehem (appointed by claimant), Gary B Born (appointed by respondent)</td>
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<td>Lone Pine Resources Inc v. Canada, ICSID Case No. UNCT/15/2 Notice of Intent submitted on 8 November 2012</td>
<td>US oil and gas exploration company challenged the government of Canada's revocation of exploration licenses located in the St Lawrence River, claiming that it was not meaningfully consulted or compensated for the revoked permit and loss of potential revenue. Damages sought: US$119 million.</td>
<td>This case is pending. Notice of Arbitration was submitted on 6 September 2013. Response to the Notice of Arbitration was submitted on 27 February 2015. A hearing on the merits was held in Toronto in October 2017.</td>
<td>Arbitration rules: UNCITRAL Administering institution: ICSID Arbitral tribunal: V V Veeder (President), David R Haigh (appointed by claimant), Brigitte Senn (appointed by respondent)</td>
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<td>Kellogg, Brown and Root (KBR) v. Mexico, ICSID Case No. UNCT/14/1 Notice of Intent submitted on 19 February 2013</td>
<td>A US energy services company sought damages against the government of Mexico related to a 2011 decision by the Mexican courts to annul a US$320 million arbitration award issued by the International Chamber of Commerce in December 2009. The original arbitration related to a contract dispute between Pemex, the Mexican state energy company, and COMMISSA, a KBR subsidiary. Damages sought: more than US$400 million.</td>
<td>On 30 April 2015, in an unpublished award the arbitrators dismissed the claim. KBR was using the NAFTA claim to collect a large commercial arbitration award KBR had obtained against the Mexican state oil company. That award was set aside by the Mexican court and was subject to enforcement proceedings in the US and Luxembourg. The dispute between Pemex and COMMISSA was settled.</td>
<td>Arbitration rules: UNCITRAL Administering institution: ICSID Arbitral tribunal: Andrés Rigo Sureda (President), Gabrielle Kaufmann-Kohler (appointed by claimant), Gerardo Lozano Alarcón (appointed by respondent)</td>
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<td>JM Longyear, LLC v. Canada Notice of Intent submitted on 14 February 2014</td>
<td>Assertion that companies were improperly denied tax incentives for sustainable forestry management. Damages sought: C$12 million.</td>
<td>Notice of Arbitration was submitted on 20 May 2014. Investor formally withdrew the claim on 26 June 2015.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Not constituted</td>
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### NAFTA in Transition: The Current State of Play and What Comes Next

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<td>B-Mex, et al v. Mexico, ICSID Case No. ARB(AF)/16/3 Notice of Intent submitted on 23 May 2014</td>
<td>US gaming investors allege that after parting ways with their Mexican business partner, their five Mexican casinos were targeted and harassed by Mexican authorities. Damages sought: US$100 million.</td>
<td>Notice of Arbitration submitted on 15 June 2016. Respondent's memorial on jurisdictional objections submitted on 30 May 2017. A hearing on jurisdiction was held from 21–25 May 2018. In August 2018, both claimants and respondent submitted post-hearing submissions. The US and Canada both filed a written submission as non-disputing state parties on 28 February and 17 August 2018. On 23 November 2018, the tribunal invited the parties and non-disputing state parties to submit additional written submissions on a jurisdictional issue by 7 December 2018. On 21 December 2018, both parties provided written submissions in response to the tribunal's procedural order. On that same date, the US also filed an additional written submission as a non-disputing state party. The case has not yet proceeded to the merits phase as an award on jurisdiction is still pending.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Glaëtan Verhoosel (President), Gary B Born (appointed by claimant), Raúl E Vinuesa (appointed by respondent)</td>
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<td>Mobil Investments Canada, Inc v. Canada (II), ICSID Case No. ARB/15/6 Notice of Intent submitted on 16 October 2014</td>
<td>In 2012, a NAFTA tribunal (see above) ruled that Canadian guidelines stipulating that energy companies active offshore invest a certain percentage of their revenue in R&amp;D within Newfoundland and Labrador are NAFTA-inconsistent performance requirements. Since the R&amp;D guidelines remain in effect, Mobil is seeking ongoing damages for the period 2012 to 2014. Damages sought: C$20 million.</td>
<td>This case is pending. Notice of Arbitration was submitted on 16 January 2015. Counter-memorial was submitted on 30 June 2016. A hearing on jurisdiction, merits and quantum was held from 24–28 July 2017. On 13 July 2018, tribunal issued a decision on jurisdiction and admissibility, holding that the tribunal has jurisdiction and the claims are admissible. A decision on scope of damages phase was issued on 11 December 2018.</td>
<td>Arbitration rules: ICSID Convention Arbitration Rules Administering institution: ICSID Arbitral tribunal: Christopher Greenwood (President), J William Rowley (appointed by claimant), Gavan Griffith (appointed by respondent)</td>
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<td>Murphy Oil Corporation v. Canada (II) Notice of Intent submitted on 16 October 2014</td>
<td>In 2012, a NAFTA tribunal ruled that Canadian guidelines stipulating that energy companies active offshore invest a certain percentage of their revenue in research and development within Newfoundland and Labrador are NAFTA-inconsistent performance requirements. Since the R&amp;D guidelines remain in effect, Murphy is seeking ongoing damages for the period 2012 to 2014. Damages sought: C$5 million.</td>
<td>This case is pending. Notice of Arbitration was submitted on 16 January 2015.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>Canadian real estate investment firm disputes the cancellation by Mexican courts of mortgages on three properties that secured loans provided by LMC to Mexican nationals. LMC alleges that its Mexican counterparties forged key legal documents and the Mexican courts have not provided their firm a fair opportunity to dispute this fraud and recover its investments. Damages sought: US$200 million.</td>
<td>This case is pending, Notice of Arbitration submitted on 11 December 2015. On 24 August 2016, Mexico filed a preliminary objection on jurisdiction. It was dismissed on 12 December 2016. A hearing on jurisdiction was held from 22–23 March 2018. A decision on jurisdiction was issued on 30 July 2018. The respondent filed a counter-memorial on the merits on 26 October 2018 and the tribunal issued a procedural order concerning production of documents on 3 January 2019.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Juan Fernández-Armesto (President), David J A Cairns (appointed by claimant), Laurence Beisson De Chazournes (appointed by respondent), Ricardo Ramírez Hernández (appointed by respondent) (replaced)</td>
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<td>Allegations that Canada breached NAFTA’s non-discrimination and minimum standard of treatment provisions when Health Canada denied CEN Biotech Inc a license. The company has been the object of numerous allegations of public misrepresentation and insider trading. Damages sought: US$4.5 billion.</td>
<td>This case is pending, but the Notice of Arbitration has not yet been submitted.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>The US supercalendered paper producer alleged that provincial government financial assistance to a competing mill in Nova Scotia discriminated against Resolute, resulted in unfair competition and provoked US trade remedy action, which ultimately led to the closure of one of Resolute’s Quebec mills. Damages sought: US$70 million.</td>
<td>Notice of Arbitration submitted on 30 December 2015. Statement of Defence submitted on 1 September 2016. The tribunal held jurisdictional hearings in August 2017. A decision on jurisdiction and admissibility was made on 30 January 2018, holding that the tribunal has jurisdiction and claims are admissible, although certain claims dating prior to September 2012 were dismissed by the tribunal. Damages claimed are between US$163–201 million. Claimants submitted a memorial on 28 December 2018. A revised procedural timetable was adopted on 19 February 2019 and an oral hearing is expected in May 2020. This case is pending. Canada filed related proceedings at the WTO to contest trade measures brought by the US. The US alleged the bailout of the mill breached international trade law. The WTO found in favour of Canada, which the US appealed.</td>
<td>Arbitration rules: UNCITRAL Administering institution: PCA Arbitral tribunal: James R Crawford (President), Ronald A Cass (appointed by claimant), Céline Lévesque (appointed by respondent)</td>
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<td>Canadian energy company alleged that the delay and eventual rejection by the Obama administration of the Keystone XL pipeline disadvantaged against the company, denied it fair and equitable treatment and expropriated its investment. After the Trump administration approved the controversial project, the investor and the US government agreed to discontinue the NAFTA claim. Damages sought: US$15 billion.</td>
<td>This case is discontinued by request of the parties. Notice of Arbitration submitted on 24 June 2016. On 24 March 2017, at the request of the parties, the ICSID Secretary-General formally discontinued the arbitral proceeding. On 8 November 2018, in response to a lawsuit brought by environmental and Native American groups against the US Department of State and TransCanada, a federal court in Montana ordered a pause in the construction of the Keystone XL pipeline.</td>
<td>Arbitration rules: ICSID Convention Arbitration Rules Administering institution: ICSID Arbitral tribunal: David R Haigh (appointed by claimant), Sean D Murphy (appointed by respondent)</td>
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### NAFTA in Transition: The Current State of Play and What Comes Next

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<td>Primoza Mining Corp v. Mexico Notice of Intent submitted on 2 June 2016</td>
<td>The investor alleged that actions taken by Mexican tax authority, which were intended to revoke investor's previously granted legal rights, were unfair, inequitable and discriminatory, and therefore violated Mexico's NAFTA obligations. The amount of damages in dispute has not been quantified.</td>
<td>Notice of Arbitration has not been submitted to date. Claim is inactive.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>Vento Motorcycles, Inc v. Mexico, ICSID Case No. ARB(AF)/17/3 Notice of Intent submitted on 20 February 2017</td>
<td>Vento assembles motorcycles in the US for export to Mexico. Its vehicles are now subject to a 30 per cent import duty. The company asserted its Mexican-owned competitors, whose assembly practices are allegedly similar, do not pay such a duty, resulting in discrimination against Vento. The amount of damages claimed by the investor is unavailable.</td>
<td>This case is pending. Notice of Arbitration submitted on 7 August 2017 (partially published). The respondent filed a counter-memorial on the merits and a memorial on jurisdiction on 12 November 2018. The tribunal issued a procedural order on document production issues on 25 January 2019.</td>
<td>Arbitration rules: ICSID Additional Facility Rules Administering institution: ICSID Arbitral tribunal: Andrés Rigo Sureda (President), David A Gantz (appointed by claimant), Hugo Perezcano Diaz (appointed by respondent)</td>
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<td>Tennant Energy, LLC v. Canada Notice of Intent submitted on 2 March 2017</td>
<td>US-owned energy company alleged that it was treated unfairly by Ontario authorities administering the province’s FIT programme. Damages sought: C$3116 million.</td>
<td>This case is pending. Notice of Arbitration was submitted on 1 June 2017. No statement of Defence on the merits has been submitted to date.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>Omnitrax Enterprises Inc v. Canada Notice of Intent submitted on 14 November 2017</td>
<td>Allegations that the Manitoba government's decision not to approve the company's proposals to transport oil by rail for export from Churchill further undermined its investment. Damages sought: C$150 million.</td>
<td>This case is pending. But the Notice of Arbitration has not yet been submitted.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>Alicia Grace and others v. Mexico, ICSID Case No. UNCT/18/4 Registered at ICSID on 19 June 2018</td>
<td>Twenty-seven US investors in a petroleum services venture brought claims relating to oil exploration and production equipment against Mexico.</td>
<td>Tribunal was constituted on 25 January 2019. Request for Arbitration submitted on 19 June 2018. This case is pending.</td>
<td>Arbitration rules: UNCITRAL Administering institution: ICSID Arbitral tribunal: Diego P Fernández Arroyo (President), Andrés Jana Linetzky (appointed by claimant), Gabriel Bottini (appointed by respondent)</td>
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<td>Westmoreland Coal Company v. Canada Notice of Intent submitted on 20 August 2018</td>
<td>A US entity purchased mine-mouth coal operations adjacent to a coal-fired power station. In 2015, Canada changed its regulations, deciding to phase out coal-fired power by 2030. The investor alleged that Canadian companies were compensated for this change in an amount of over US$1.4 billion, but Westmoreland was excluded from the compensation, which it claims is tantamount to expropriation and violation of the minimum standard of treatment. Damages sought: US$470 million.</td>
<td>Notice of Arbitration and statement of claim were submitted on 19 November 2018. This case is pending.</td>
<td>Arbitration rules: UNCITRAL Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>Legacy Vulcan, LLC v. Mexico, ICSID Case No. ARB/19/1 Notice of Intent submitted on 3 September 2018</td>
<td>US investor brought claims against Mexico relating to limestone extraction and exportation.</td>
<td>This claim was registered in ICSID on 3 January 2019. This case is pending.</td>
<td>Arbitration rules: ICSID Convention Arbitration Rules Administering institution: ICSID Arbitral tribunal: Not constituted</td>
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<td>Odyssey Marine Exploration v. Mexico Notice of Intent submitted on 4 January 2019</td>
<td>US marine and development company alleged Mexico breached its NAFTA obligations and minimum standard of treatment, and national treatment by refusing to grant environmental permits for the exploration of large phosphate deposit located off the coast of Baja, California. Damages sought: more than US$3.5 billion.</td>
<td>This case is pending.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>Renaud Jacquet et al v. Mexico Notice of Intent submitted on 17 January 2019</td>
<td>Investors from France, Canada and Portugal filed claims regarding several beachfront parcels in Tulum, Mexico on which they have hotels. Claimants allege, among other things, expropriation and breach of fair and equitable treatment standards under NAFTA, the France–Mexico BIT and the Mexico–Portugal BIT. Damages sought: US$70 million.</td>
<td>This case is pending.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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<td>Jonathan Levy v. Canada Notice of Intent submitted on 16 February 2019</td>
<td>US investor claimed that the Alberta Securities Commission ignored his rights as a cross-border legal service provider and treated him as a layperson to allegedly circumvent the attorney–client privilege. He also alleged discriminatory treatment. Damages sought: at least US$2 million in alleged lost investments and billings.</td>
<td>This case is pending.</td>
<td>Arbitration rules: N/A Administering institution: N/A Arbitral tribunal: Not constituted</td>
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I INTRODUCTION

What is the future of investor–state arbitration? In recent years, observers have questioned whether investor–state arbitration will or should be a feature of the next generation of free trade and bilateral investment treaties (BITs). Commentators have suggested a ‘backlash’ against the system of investor–state arbitration that has developed over the past half-century. Critics allege that investor–state arbitration disproportionately favours investors; that private lawyers sitting as arbitrators are too close to claimants; and that investment awards encroach upon state sovereignty and upon states’ ‘right to regulate’. Others more broadly object to investor–state arbitration on the ground that it uses mechanisms derived from ‘private law’ to resolve ‘public’ disputes without sufficient transparency.2

Proponents of investor–state arbitration respond that: (1) statistics do not support the notion that investor–state dispute settlement disproportionately favours investors;3 (2) mechanisms already exist to address arbitrator conflicts of interest;4 and (3) that the international investment law system only infringes upon state sovereignty to the extent

1 Carlos Ramos-Mrosovsky is counsel and Rajat Rana is a senior associate at Alston & Bird LLP.
3 Statistics maintained by the United Nations Conference on Trade and Development indicate that of the concluded investor–state arbitrations, 28.1 per cent have been decided in favour of investors, 22.9 per cent settled and 35.9 per cent decided in favour of states, with the remainder having either been discontinued or resulting in a finding of liability without damages awarded. See United Nations Conference on Trade and Development, Investment Policy Hub, ‘Concluded original arbitration proceedings’, http://investmentpolicyhub.unctad.org/ISDS.
4 See, e.g., Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention) Articles 14, 56–58 (requiring that arbitrators in investor–state disputes be
that such incursions have been consented to by states seeking to attract lawful investment by entering into investment treaties. Nevertheless, these criticisms, whatever their merits, prompted some governments to demand changes to treaty frameworks and led to the emergence of alternative investment treaty models.

Some states, like Brazil, have rejected investor–state arbitration outright. Tanzania, for example, enacted several pieces of legislation prohibiting international arbitration in disputes relating to natural resources. Other states, like Ecuador, Bolivia, Indonesia, India and South Africa, have repudiated the BITs they had previously signed.6

Still, other states and groups of states have tried to revise the legal framework for investment treaty dispute resolution. Most notably, the United States, Mexico and Canada agreed to replace the North American Free Trade Agreement (NAFTA) with the US–Mexico–Canada Trade Agreement (USMCA), which systematically narrows the availability of investor treaty dispute resolution.7 More dramatically, perhaps, the European Union has pressed for replacing the system of investment treaty arbitration with a new permanent multilateral investment court.8

Nevertheless, and especially in the Pacific Rim, a number of states have sought incremental changes – to adjust the scope of treaty provisions in light of their experience in past cases and often to enhance transparency in arbitration proceedings – while remaining committed to arbitration as the standard mechanism for resolving investor–state disputes. As at the time of writing, efforts are underway to forge a free trade arrangement among 16 Asia-Pacific countries called the Regional Comprehensive Economic Partnership (RCEP), whose investment chapter is widely expected to provide for institutional arbitration of investor–state disputes.9

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5 See e.g., the Written Laws (Miscellaneous Amendments) Act (2017); the Natural Wealth and Resources (Permanent Sovereignty) Act (2017); the Natural Wealth and Resources Act (2017); and Public-Private Partnership (Amendment) Act, No. 9 (2018).

6 Having previously cancelled all of its BITs, Ecuador has recently asked 16 former treaty partners to renegotiate those BITs on the basis that investor–state arbitrations under its terms are seated in Latin America. See Tom Jones, ‘Ecuador begins talks over new BITs’, Global Arbitration Review (February 23, 2018), https://globalarbitrationreview.com/article/1159285/ecuador-begins-talks-over-new-bits. In 2017, India terminated BITs with 58 countries, including 22 EU countries. Alison Ross, ‘India’s Termination of BITs to begin’, Global Arbitration Review (March 22, 2017); see also Ben Bland and Shawn Donnan, ‘India to Terminate More Than 60 Bilateral Investment Treaties’, Financial Times (March 26, 2014).

7 Bill Chappell, ‘USMCA: Trump Signs New Trade Agreement with Mexico and Canada to Replace NAFTA’, National Public Radio (Nov. 30, 2018). USMCA, however, requires ratification in the House and Senate as well as legislatures in Canada and Mexico before it can replace the original NAFTA that took effect in 1994.

8 Recently, in a speech by the European Commissioner for Trade, Cecilia Malmström, at a high-level event hosted by the Belgian Minister for Foreign Affairs, Didier Reynders, Commissioner Malmström noted that the European Union’s latest agreements with Canada, Singapore, Vietnam and Mexico all provide for an international investment court system. See the speech by European Commissioner for Trade Cecilia Malmström, ‘A Multilateral Investment Court: A Contribution to the Conversation About Reform of Investment Dispute Settlement’, Nov. 22, 2018.

Conscious of the limits of any attempt to generalise developments concerning a system of international investment law defined by thousands of distinct bilateral and multilateral agreements, this chapter attempts to summarise recent investment treaty dispute resolution proposals emerging from some of the world’s largest economies.

II USMCA TO REPLACE NAFTA

One of the most significant developments of 2019 in the area of international investment law was the 30 November 2018 agreement in principle between the United States, Canada and Mexico to revise and replace NAFTA with USMCA, which is a new stand-alone agreement comprising no less than 34 chapters, 13 annexes and 14 side letters. President Donald J Trump called USMCA ‘the most modern, up-to-date, and balanced trade agreement in the history of our country, with the most advanced protections for workers ever developed’, while Canadian Prime Minister, Justin Trudeau, announced that USMCA would ‘maintain stability for Canada’s entire economy’.

USMCA largely preserves NAFTA’s substantive protections. These include a guarantee of a minimum standard of treatment under customary international law, protection against indirect expropriation and free transfer of investment (such as profits and dividends). However, claims based on the most favoured nation provision, or national treatment with respect to the establishment or acquisition of an investment, are expressly excluded in investor-state arbitration for US–Mexico claims. But this limitation is inapplicable if a claimant is a party to a covered government contract (i.e., activities related to oil and natural gas; supply of power generation, telecommunication and transportation services; and...
ownership or management of infrastructure). 16 In those circumstances, the claimant may rely on other benefits in USMCA, including claims for violations of the minimum standard of treatment afforded under customary international law, claims for indirect expropriation or claims with respect to the establishment of acquisition of an investment.

USMCA, if ratified, would nevertheless significantly curtail investors’ ability to bring international arbitration claims17 by: imposing important procedural prerequisites on claims involving the United States and Mexico, and US and Mexican investors; and phasing out investor–state arbitration for disputes involving Canada or Canadian investors entirely.18

This would leave US and Canadian investors with the option of: (1) pursuing contractual or other remedies available in national courts; (2) seeking to escalate disputes to the state level within Chapter 31 of USMCA; or (3), potentially for Mexican and Canadian investors, taking advantage of the dispute settlement provisions in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) to which Canada and Mexico are both parties.19 Once USMCA goes into effect, it is likely that Canada may negotiate a separate agreement to provide for an international arbitration mechanism for Canadian and US investors.

With respect to Mexican and US investors, USMCA imposes a number of conditions precedent before an investment arbitration claim may be commenced by an investor. USMCA requires an investor to start a domestic proceeding and obtain a ‘final decision from a court of last resort’ or wait for ‘30 months’ from the initiation of the domestic proceeding before commencing international arbitration.20 To the extent that an investor seeks to bring a claim based on a taxation measure, USMCA, however, requires the investor to first refer the dispute to domestic authorities, and if the domestic authorities ‘do not agree to consider the issue or . . . fail to agree that the measure is not an expropriation within a period of six months’, the investor may then move forward with international arbitration.21

USMCA also includes a fork-in-the-road provision barring a US investor from bringing an international arbitration claim against Mexico if that investor has ‘alleged that breach of an obligation’ under USMCA ‘as distinguished from breach of other obligations under Mexican law’ before Mexican courts.22

Whether USMCA will ever be ratified remains an open question. While the Trump administration has threatened to denounce NAFTA to force the US Congress’ hand, USMCA has met with a lukewarm reception in Congress, from trade sceptics and free-trade advocates who are reluctant to abandon NAFTA.23

16 See Annex 14-E, USMCA.
17 USMCA would have no effect on disputes arising out of investments made between 1 January 1994 and NAFTA’s termination, providing that the respective investors start arbitral proceedings within three years of NAFTA’s termination. See Annex 14-C, USMCA. If USMCA is ultimately ratified, its first consequence may well be to provoke last minute legacy NAFTA claims.
18 See Article 14.2(4) and Annex 14-D (Mexico–United States Investment Disputes), USMCA and Annex 14-D.
19 Mexico has carved out its consent to investment arbitration under the CPTPP relating to government contracts involving infrastructure projects. See Chapters 9 and 14, CPTPP; Annex-14-E (Mexico–United States Investment Disputes Related to Covered Government Contracts).
20 Article 14.D.5, USMCA.
21 Article 32.3(8), USMCA.
22 Appendix 3, Annex 14-D, USMCA.
III THE EUROPEAN UNION’S INTERNATIONAL INVESTMENT COURT PROPOSAL

Since 2017, the official position of the European Union – which claims authority to negotiate trade and investment treaties agreements on behalf of its 28 Member States – has been that, at least ‘for the EU’, investor–state arbitration is ‘dead’.24 European officials have been explicit that Europe intends to pursue an international ‘system of investment courts’ in all future investment agreements.25 The European Union’s campaign against investor–state arbitration has drawn momentum from the Achmea judgment, holding that intra-EU BITs, namely BITs among EU Member States, are incompatible with the European Union’s legal order. As a result, EU Member States have warned the ‘investor community that no new intra-EU investment arbitration proceeding should be initiated’, and that Member States ‘will terminate all bilateral investment treaties concluded between them’.26

24 See, e.g., EU–Japan Free Trade Agreement Factsheet, European Commission (December 8, 2017) at 6 (‘A new system – called the Investment Court System, with judges appointed by the two parties to the FTA and public oversight – is the EU’s agreed approach that it is pursuing from now on in its trade agreements . . . Anything less ambitious, including coming back to the old Investor-to-State Dispute Settlement, is not acceptable. For the EU ISDS [investor–state dispute settlement] is dead’), http://trade.ec.europa.eu/doclib/docs/2017/july/tradoc_155684.pdf. By way of background, the European Union’s commitment to an international investment court emerged in the context of hostility towards investor–state arbitration from European non-governmental organisations and other pressure groups during the negotiation of the Transatlantic Trade and Investment Partnership (TTIP) with the United States. In a May 2015 ‘Concept Paper’, the European Commission proposed that Europe ‘should pursue the creation of one permanent court’ that ‘would apply to multiple agreements and between different trading partners’ and with a view ultimately ‘to multilateralise the court either as a self-standing international body or by embedding it into an existing multilateral organisation’. See European Commission Concept Paper, ‘Investment in TTIP and beyond – the path for reform: enhancing the right to regulate and moving from current ad hoc arbitration towards an Investment Court’ (May 5, 2015), at 11-12, http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF. See also European Parliament, Resolution of 8 July 2015 containing the European Parliament’s recommendations to the European Commission on the negotiations for the TTIP (2014/2228(INI)) (instructing the European Commission to pursue the replacement of investor–state arbitration by a ‘new system’ in which disputes would be decided ‘in a transparent manner by publicly appointed, independent professional judges in public hearings and which includes an appellate mechanism’), http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P8-TA-2015-0252+0+DOC+XML+V0//EN. By November of 2015, the European Union had presented a formal proposal for an investment court system to the United States. See Proposal for Investment Protection and Resolution of Investment Disputes (November 12, 2015) (EU TTIP Proposal), http://trade.ec.europa.eu/doclib/docs/2015/november/tradoc_153955.pdf. Support for a multilateral investment court dovetails with the European Commission’s long-standing objection to BITs providing for investor–state arbitration between EU Member States, which it considers incompatible with the European Union’s competence over investment protection issues. The European Commission’s position appears to have been upheld by the European Court of Justice (ECJ) in the Achmea case, in which the ECJ found investor–state arbitration under intra-EU BITs to have an adverse effect on the autonomy of EU law; and are therefore incompatible with EU law. See ECJ Judgment (Grand Chamber) in Case C-284/16 Slowakische Republik v Achmea BV (March 6, 2018) (ECCLI:EU:C:2018:158), http://curia.europa.eu/juris/document/document.jsf. However, at least in one ICSID arbitration, the tribunal rejected the applicability of the Achmea decision to investment treaty arbitration under the ICSID Convention. UP and C.D. Holding Internationale v. Hungary, ICSID Case No. ARB/13/35, Award (Oct. 9, 2018).


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The European Union’s enthusiasm for replacing the ‘old, traditional system’ of investor–state arbitration with the ‘public justice’ of an investment court in ‘all . . . ongoing and future trade negotiations’ has been on display in the investment chapters of three of the European Union’s most recent international trade and investment agreements. The EU–Canada Comprehensive Economic and Trade Agreement (CETA), the EU–Vietnam free trade agreement (FTA) and the EU–Singapore FTA (none of which are yet in force), each provide for an investment tribunal system in place of standard investor–state arbitration.

The European Union’s approach in these treaties breaks away from arbitration of investor–state disputes in several important ways. In particular:

a. A fundamental aspect of investor–state arbitration – the parties’ opportunity to participate in the choice of arbitrators and structuring of the applicable procedure – would be abandoned in favour of proceedings before standing bodies whose members, comprised in equal thirds of members chosen respectively by the European Union, the other treaty party and jointly from third countries, would serve for fixed terms. European officials have praised this system as one that would ‘break the link’ between parties and arbitrators in favour of ‘independent’ judges, but critics have noted that a standing international investment court or ‘Tribunal’ whose members would be appointed entirely by governments, would only break the link for claimants.

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29 See CETA, Article 8.27(5) (providing for 15 members appointed to five-year terms, renewable once); EU–Vietnam FTA, Article 12(2)-(5) (providing for nine members appointed to four-year terms, renewable once); EU TTIP Proposal, Article 9(2)-(5) (providing for 15 judges appointed for six-year terms, renewable once); EU–Singapore FTA, Article 3.9(2) (providing for six members for eight-year terms).

30 See European Commission Concept Paper, ‘Investment in TTIP and beyond – the path for reform: enhancing the right to regulate and moving from current ad hoc arbitration towards an Investment Court’ (May 5, 2015), at 7, http://trade.ec.europa.eu/doclib/docs/2015/may/tradoc_153408.PDF. But see ‘The Proposals of the European Commission for Investment Protection and an Investment Protection System’, Remarks by Judge Stephen M Schwebel (May 17, 2016) (‘The question arises, if there is a risk, real or perceived, of bias of ad hoc arbitral tribunals, as the EU appears to insinuate, is there not a risk, real or perceived, of bias – in favor of States and against investors – in the EU Commission’s proposals?’), http://isdsblog.com/wp-content/uploads/sites/2/2016/05/THEproposalsoftheEuropeanCommission.pdf.
The European Union’s approach would provide for appellate review, including for ‘errors in the application or interpretation of applicable law’ and ‘manifest errors in the appreciation of the facts, including the appreciation of relevant domestic law’ before a separately established ‘Appeal Tribunal’.\(^{31}\) Appellate review is highly anomalous in the international arbitration context, where awards may ordinarily be set aside by the courts of the seat of arbitration or through an ICSID annulment process only on the narrowest of grounds.\(^{32}\) Moreover, although the concept of binding precedent is also largely absent from arbitration, proponents of the European Union’s approach have urged that, ‘[b]y sitting permanently and deciding cases over time, judges would deliver consistent decisions’.\(^{33}\)

Investor–state proceedings would be largely public. Through incorporation of the UNCITRAL Rules on Transparency in Treaty-Based Investor–State Arbitration into both the CETA and the EU–Vietnam FTA, hearings would be open to the public and submissions published, as would be the case in many countries’ courts.\(^{34}\)

In addition, the CETA, the EU–Vietnam FTA and the EU–Singapore FTA explicitly anticipate a future transition to a multilateral dispute settlement mechanism, and call upon the parties to work toward the establishment of such multilateral arrangements.\(^{35}\)

Interestingly, and despite these changes, the European approach seeks to make use of both the physical and legal infrastructure of the investor–state arbitration system that it aspires to replace. Under the CETA and the EU–Vietnam FTA, proceedings before the investment tribunal would be administered through the ICSID Secretariat or the Permanent Court of Arbitration in The Hague.\(^{36}\) Strikingly, in the context of an attempted shift towards a ‘court’, the results of investor–state proceedings under both agreements are styled ‘awards’ and are

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\(^{31}\) See CETA, Article 8.28(2); EU–Vietnam FTA, Article 28(1); EU TTIP Proposal (Article 29(1)). The EU–Singapore FTA provides for rules on public access to the documents, hearings and the possibility of third persons to make submissions under Annex 8.

\(^{32}\) The grounds for annulment found in Article 52 of the ICSID Convention are incorporated into the CETA (Article 8.28(2), EU–Vietnam FTA (Article 28(1), EU TTIP Proposal (Article 29(1))); and EU–Singapore FTA (Art. 3.19).


\(^{34}\) See CETA, Article 8.36; EU–Vietnam FTA, Article 20; EU TTIP Proposal, Article 18, (incorporating the UNCITRAL Transparency Rules into both treaties); and EU–Singapore FTA, Article 3.16.

\(^{35}\) See CETA Text, Article 8.29 (‘The Parties shall pursue with other trading partners the establishment of a multilateral investment tribunal and appellate mechanism for the resolution of investment disputes. Upon establishment of such a multilateral mechanism, the CETA Joint Committee shall adopt a decision providing that investment disputes under this Section will be decided pursuant to the multilateral mechanism and make appropriate transitional arrangements’); EU–Singapore FTA, Article 312 (‘The Parties shall pursue with each other and other interested trading partners, the establishment of a multilateral investment tribunal and appellate mechanism for the resolution of international investment disputes. Upon establishment of such a multilateral mechanism, the Committee shall consider adopting a decision to provide that investment disputes under this Section will be resolved pursuant to that multilateral mechanism, and to make appropriate transitional arrangements.’) Compare EU–Vietnam FTA, Article 15 (providing that the Parties shall enter into negotiations for an international agreement providing for a multilateral investment tribunal’ and that ‘the Parties may consequently agree on the non-application of relevant parts of this Section’).

\(^{36}\) See CETA, Article 8.27(6); EU–Vietnam FTA, Article 12.3. However, under EU–Singapore FTA, proceedings would be administered only through the ICSID Secretariat. Article 3.9(16). See also CETA,
(hoped) to be enforceable under the ICSID or New York Conventions. Thus, even while breaking away from what may be investor–state arbitration's most material aspects – the party's role in arbitrator selection and the finality of awards – the European Union's approach would retain many of its forms.

All this being said, these agreements have yet to come into force. At present, the CETA remains mired in a complex process of ratification by each of the European Union's individual Member States, while the EU–Vietnam FTA faces related hurdles. The EU–Singapore FTA was only recently approved by the European Parliament on 13 February 2019. That said, there is every indication that, for the foreseeable future, the European Union will remain committed to its vision of a multilateral investment court.

IV THE PACIFIC RIM FAVOURS INCREMENTAL ADJUSTMENTS TO A FAMILIAR ARBITRATION-BASED MODEL

In contrast with Europe and North America's apparent scepticism towards investment treaty arbitration, the CPTPP will join Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam in a common trade and investment framework that provides a much more familiar arbitration-based approach to investor–state dispute resolution reform. The CPTPP entered into force among Canada, Australia, Japan, Mexico, New Zealand and Singapore on 30 December 2018, and Vietnam on 14 January 2019.

It extends reciprocal investment protections comparable to those available under most BITs. It also stays within the ambit of investor–state arbitration, allowing investors to

Article 8.27(16) ('The ICSID Secretariat shall act as Secretariat for the Tribunal and provide it with appropriate support'); EU–Vietnam FTA, Article 12(18); and EU TTIP Proposal, Article 9(16) (providing for similar support from the ICSID Secretariat or the Permanent Court of Arbitration).

See CETA, Article 8.41; EU–Vietnam FTA, Article 31; EU TTIP Proposal, Article 30, EU–Singapore FTA, Article 3.22. It is not clear that an enforcing court would agree that the product of the proposed investment court would constitute an 'award' under either instrument.


arbitrate claims under the ICSID Convention, the UNCITRAL Rules or other rules of the parties’ choice.\textsuperscript{41} Consistent with the principle of party autonomy, both claimant investors and respondent states will participate in choosing arbitrators to hear their dispute.\textsuperscript{42}

This is not to say that the CPTPP ignores concerns – warranted or otherwise – about investor–state arbitration. To the contrary, a number of its provisions are plainly intended to advantage respondent states in arbitration. For example:

\textbf{a} In direct response to critics of the ‘regulatory chill’, the CPTPP explicitly affirms states’ authority to regulate and warns that its provisions should not be construed ‘to prevent a Party from adopting, maintaining or enforcing any measure’ intended to ‘ensure that investment . . . is undertaken in a manner sensitive to environmental, health or other regulatory objectives’.\textsuperscript{43} A special Annex similarly records the parties’ ‘shared understanding’ that a state’s ‘nondiscriminatory regulatory actions’ directed towards ‘legitimate public welfare objectives’ will not ordinarily constitute indirect expropriation.\textsuperscript{44}

\textbf{b} In addition, language in the CPTPP may arguably be read to narrow the scope of its guarantee of ‘fair and equitable treatment’ (FET) to foreign investors.\textsuperscript{45} This is significant because claimed breaches of FET are perhaps the most common basis for investor–state claims, and the scope of the FET obligation is a matter of recurrent debate.\textsuperscript{46} Reflecting the resistance of some states to a broad reading of FET, the CPTPP warns that ‘the mere fact that’ a state may act in a manner ‘inconsistent with an investor’s expectations’ will not in itself constitute a breach of FET.\textsuperscript{47}

In addition to these provisions,\textsuperscript{48} other aspects of the CPTPP respond to many of the same criticisms of investor–state arbitration that seem to animate the European Union’s push for a permanent multilateral court, without breaking from the widespread acceptance of arbitration as a means of resolving investor–state disputes. For example:

\begin{itemize}
\item \textsuperscript{41} See TPP Article 9.19(4) (incorporated by reference at Article 1(1) of the CPTPP).
\item \textsuperscript{42} See TPP Article 9.22 (incorporated by reference at Article 1(1) of the CPTPP).
\item \textsuperscript{43} See TPP Article 9.16 (incorporated by reference at Article 1(1) of the CPTPP).
\item \textsuperscript{44} See TPP Annex 9-B (incorporated by reference at Article 1(1) of the CPTPP). Notably, neither the CPTPP nor the TPP explain how states will reconcile this understanding with the consequences of regulatory measures that have the direct effect of destroying private law property rights.
\item \textsuperscript{45} See TPP Article 9.6(1) (incorporated by reference at Article 1(1) of the CPTPP).
\item \textsuperscript{46} See Rudolf Dolzer \& Christoph Schreuer, \textit{Principles of International Investment Law} (2d ed. 2012) at 130 (‘Most . . . investment treaties provide for fair and equitable treatment (FET) of foreign investments. . . . Today, this concept is the most frequently invoked standard in investment disputes’).
\item \textsuperscript{47} See TPP Article 9.6(4) (incorporated by reference at Article 1(1) of the CPTPP). This language stops short of the question of whether a state may induce an investment with implicit or explicit promises and then withdraw those promises without liability.
\item \textsuperscript{48} The CPTPP also omits the ‘umbrella clause’ included in the earlier TPP, which would have allowed investors to bring claims on the basis of ‘investment agreements’ and ‘investment authorizations’. See CPTPP Article 2 and Annex (suspending provisions of the TPP to this effect). See also New Zealand Ministry of Foreign Affairs \& Trade, ‘CPTPP vs TPP’ (‘Suspensions in the Investment Chapter will mean that claims are no longer permitted in relation to investment contracts and approvals (called “investment agreements” and “investment authorisations” in the TPP). This means that under CPTPP private companies who enter into an investment contract with the Government will not be able to use ISDS
a Hearings in arbitrations pursuant to the CPTPP will be open to the public, with the parties’ submissions and the tribunal’s decisions also being made publicly available.\textsuperscript{49} This represents a step away from typical investor–state arbitration practice in which, as in commercial arbitration, pleadings and hearings are usually private.\textsuperscript{50}

b The CPTPP calls for the establishment of an official commission appointed by the state parties with the power to issue binding joint interpretations of treaty provisions on behalf of the state parties.\textsuperscript{51}

c In addition, the CPTPP parties are to provide binding ‘guidance’ on a code of conduct for arbitrators as well as ‘on the application of other relevant rules or guidelines on conflicts of interest’ prior to the agreement’s entry into force.\textsuperscript{52} This guidance may reflect concerns about private arbitrators’ conflicts and incentives in the context of investor–state arbitration.

In contrast with Europe’s push for an international investment court and USMCA’s truncated arbitration regime, the CPTPP can be characterised as calibrating but not abandoning the familiar mechanism of investor–state arbitration. Other recent investment agreements suggest that the CPTPP’s incrementalism is broadly consistent with its signatories’ preferences and with those of other non-European economies.

In this regard, it may be significant that Canada – a party to both the EU–CETA and the CPTPP – agreed to the CPTPP despite the latter’s lack of provision for a court comparable to that found in the CETA. This would seem to indicate that the eventual establishment of a multilateral investment court is of significantly greater concern to the European Union than it is to Canada.

Japan’s attitude may also be indicative, inasmuch as investor–state dispute settlement was left out of the final EU–Japan Economic Partnership Agreement – the European Union’s largest trade and investment agreement to date. Japan, a party to the CPTPP and more than 40 international investment agreements, has historically favoured arbitration of investor–state disputes.\textsuperscript{53} Over the course of extensive negotiations, Japan refused to accept the European Union’s proposed inclusion of an investment court, even while the European Union in turn refused to accept Japan’s proposed inclusion of an investor–state arbitration clause. Although

\textsuperscript{49} See TPP Article 9.24 (incorporated by reference at Article 1(1) of the CPTPP).
\textsuperscript{50} Article 9.24 of the CPTPP is in step with a broader movement towards increased transparency in investor–state arbitration that appears to be gaining momentum, as reflected in the 2014 UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration and the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration (adopted on 10 December 2014, opened for signature on 17 March 2015). That said, a number of states, including the United States, have consistently published all pleadings submitted in their disputes.
\textsuperscript{51} See TPP Articles 27.1-27.4 (incorporated by reference at Article 1(1) of the CPTPP).
\textsuperscript{52} See TPP Article 9.22(6) (incorporated by reference at Article 1(1) of the CPTPP).
Tokyo and Brussels initially announced that they will negotiate the issue, the result is that the EU–Japan Economic Partnership Agreement entered into force on 31 January 2019 without an investor–state dispute settlement mechanism.54

Although it is not a party to the CPTPP, China’s investment treaty practice promises to be highly influential for the future of investor–state dispute resolution. Since the adoption of its Second Model BIT in the late 1990s, China, with more than 100 investment agreements in place, has broadly favoured classical investor–state dispute settlement provisions consistent with a strategy of promoting Chinese foreign investment abroad.55 The 2012 Canada–China Foreign Investment Protection Agreement provides for investor–state arbitration, while incorporating transparency provisions.56

In any case, China appears less likely to support a judicialised approach to investor–state disputes given both its substantial pro-sovereignty stance in international affairs and reluctance to subject itself to supranational jurisdiction. These traditional policy stances reinforce China’s ongoing efforts to promote arbitration of investment disputes within China as part of the ‘Belt and Road Initiative’. Chinese arbitral institutions are readying themselves for this role. The China International Economic and Trade Arbitration Commission announced dedicated investment arbitration rules and a ‘Silk Road Arbitration Centre’, as well as the Shenzhen Court of International Arbitration’s amendment of its rules to administer investment disputes.57 China’s views are also likely to be decisive in the development of the RCEP among the Association of Southeast Asian Nations (ASEAN)-6 countries, whose investment chapter is widely expected to provide for institutional arbitration of investor–state disputes among 16 Asia-Pacific economies.58 Cambodia is hosting the seventh RCEP Intersessional Ministerial Meeting to negotiate market access for goods, services and investment.

54 ‘EU-Japan Trade Agreement Enters into Force’, Press Release (January 31, 2019), http://europa.eu/rapid/press-release_IP-19-785_en.htm. This outcome resembles the terms of Australia and New Zealand’s agreement to participate in the CPTPP. Both governments are sceptical of investor–state arbitration and have signed onto the CPTPP subject to a side agreement clarifying investment disputes arising between Australia or New Zealand, and their reciprocal investors will not be subject to arbitration under the CPTPP. See Exchange of Notes between Trade Ministries, constitutive of an agreement between Australia and New Zealand (February 4, 2016), http://dfat.gov.au/trade/agreements/tpp/official-documents/Documents/australia-new-zealand-investor-state-dispute-settlement-trade-remedies-and-transport-services.PDF.


56 See Canada–China Foreign Investment Protection Agreement (FIPA-2012), Section C, Articles 19 to 32. China’s most recent new BIT with Tanzania, for example, also provides for traditional investor–state arbitration before ICSID or under UNCITRAL Rules. See China–United Republic of Tanzania Bilateral Investment Treaty (2014), Art. 13.


V CONCLUDING THOUGHTS

All told, investor–state arbitration appears likely to endure as the standard model for resolving disputes, despite its detractors and perennial debates about its proper scope.

Outside of Europe’s uniquely supranational institutional context, the quest for a multilateral investment court seems to have found little support. Smaller or ideologically sympathetic negotiating partners may well agree to resolve disputes in an investment court, of course, but one lesson from the negotiation of the EU–Japan Economic Partnership Agreement may be that it will be difficult for European negotiators to persuade peer economies to buy into the concept of submitting their measures to a permanent multilateral court.

This should not necessarily come as a great surprise. Though a bilateral court established under an agreement like the CETA might give states some advantages in disputes with investors, its evolution into a multilateral body would likely increase the distance between states and adjudicators, evolving toward a scenario in which neither the state nor the claimant will ultimately have much role in selecting those charged with deciding their dispute. Thus, to the extent that concern over investor–state arbitration is driven by resistance to the prospect of states being bound by the decisions of international tribunals, the perceived threat to sovereignty might be even greater from a court. In addition, in the context of the current nationalist backlash to economic globalisation, internationalists critical of investment treaty arbitration, but concerned with preserving some form of investor–state dispute resolution, may decide to backtrack from efforts at reform, concluding that reform negotiations are more likely to be hijacked by forces hostile to any international system than lead to the types of reforms sought by the European Union’s multilateral investment court model.

The United States may be a case in point. Although historically a driving force behind the development of international investment law, US policymakers have lately taken a negative view, even entertaining the possibility that investor–state arbitration could be eliminated from the NAFTA framework as seen in the current draft of USMCA relating to Canada. Crucially, however, these kinds of proposals have been justified in terms of the supposed threat to ‘sovereignty’ posed by investor–state arbitration. If the United States has historically been reluctant to commit to supranational courts, such a proposal would be particularly difficult to reconcile with an ‘America First’ trade policy. Yet, even a change in US politics after the 2020 elections may not bring an administration into power that is committed to investor–state arbitration.

Even amid such concerns, the apparent success of the CPTPP, the ongoing negotiation of other treaties including investor–state arbitration and the practical political difficulty of enacting dramatic institutional changes at the international level, all seem to confirm that


Investor–State Arbitration and the ‘Next Generation’ of Investment Treaties

most states believe there are benefits to be realised from including investor–state dispute mechanisms in their investment agreements. As a result, incremental adjustments to settled practice – whether through carefully wording substantive provisions, or greater provision for transparency, which does not implicate sovereignty concerns to the same degree – seem more likely to characterise the next generation of investment treaties than widespread adoption of a multilateral judicial regime.

61 See, e.g., Burlington Resources Inc. v. Republic of Ecuador, ICSID Case No. ARB/08/5, Decision on Reconsideration and Award dated February 7, 2017; Occidental Petroleum Corporation and Occidental Exploration and Production Company v. The Republic of Ecuador, ICSID Case No. ARB/06/11, Award dated October 5, 2012; Chevron Corporation (USA) and Texaco Petroleum Company (USA) v. The Republic of Ecuador, UNCITRAL, PCA Case No. 34877, Award dated August 31, 2011.
I  INTRODUCTION

The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) has evolved out of the long-negotiated Trans-Pacific Partnership Agreement (TPP). Entered into force on 30 December 2018, the CPTPP constitutes one of the world’s largest regional free trade and investment agreements, encompassing a combined GDP of US$10 trillion – almost 13.5 per cent of global GDP – 495 million people and over 15 per cent of global trade.2

The CPTPP’s investment chapter contains a number of interesting provisions that clarify the scope of substantive investment protections and address some of the concerns about the current investor–state dispute settlement (ISDS) regime. This piece will focus on the most relevant provisions of CPTPP’s investment chapter and explain why it can be qualified as a modern investment agreement.

II  NEGOTIATION HISTORY

i  TPP

The TPP was negotiated with the goal to reduce tariff and non-tariff barriers across substantially all aspects of international trade in the Asia-Pacific region, and to cover intellectual property, investments and dispute settlement for investors, among others. Negotiations for the TPP started in January 2008 between the United States and members of the Trans-Pacific Strategic Economic Partnership Agreement – Brunei, Chile, Singapore and New Zealand. In November 2008, Australia, Vietnam and Peru joined the negotiations, followed by Mexico and Canada in October 2012, and finally by Japan in July 2013. Due to the involvement of the United States, the TPP initially encompassed nearly 40 per cent of global GDP, over 800 million people and around one-third of global trade.3

The TPP was shaped in 19 official negotiation rounds spanning from March 2010 to August 2013. The end of official negotiations coincided with the late addition of Japan in July 2013, after which unofficial negotiations in the form of chief negotiator meetings

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and ministerial meetings took place. The terms of the TPP were finally agreed upon on 4 October 2015. On 4 February 2016, 12 Pacific Rim states – Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam – signed the TPP.

The TPP was to enter into force when at least six parties accounting for 85 per cent of the combined GDP of the 12 member states ratified the agreement. Thus, essentially both Japan and the United States had to ratify the TPP for it to enter into force. On 23 January 2017, on his fourth day in office, US President Donald J Trump withdrew from the TPP by Executive Order, effectively preventing the TPP from ever taking effect, as the United States accounted for 60 per cent of the combined GDP of the TPP Member States.

ii CPTPP

With the TPP unable to enter into force after the withdrawal of the United States, the remaining member states remained intent on executing a binding agreement. In negotiations for a revised TPP, the newly dubbed CPTPP, and with Japan leading the way, all of the TPP member states, less the United States, agreed to revive the agreement in May 2017. In doing so, 22 provisions from the original TPP that had primarily been pushed by the United States were suspended or modified, as they were not widely supported by the remaining members. After less than a year of negotiations, the CPTPP was signed by Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam on 8 March 2018.

The CPTPP was ratified by Mexico, Japan, Singapore, New Zealand, Canada, Australia and Vietnam in late 2018, and, as of 30 December 2018, the CPTPP entered into force between Australia, Canada, Japan, Mexico, New Zealand and Singapore, and for Vietnam as of 14 January 2019. The CPTPP is open for subsequent accession by other, mainly Asia-Pacific Economic Cooperation member states, and Thailand, Indonesia, Colombia, South Korea and Taiwan seem to have expressed interest in joining the CPTPP.

III CONTENT OF THE CPTPP INVESTMENT CHAPTER

The CPTPP largely incorporates the terms of the TPP by reference and makes them part of the CPTPP mutatis mutandis (CPTPP, Article 1.1). This also applies to the TPP Chapter 9 on ‘Investment’ (the CPTPP Investment Chapter).

The CPTPP leaves the substantive investment protections in Section A of Chapter 9 unchanged. With respect to ISDS contained in Section B of Chapter 9, however, the CPTPP

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4 Although Japan had expressed interest in joining the TPP as early as October 2010, domestic resistance, particularly from the agriculture industry, hindered Japan’s attempts to join the free trade agreement. (See JETRO Newsletter, ‘Japan Looks to Trans-Pacific Partnership to Transform its Economy’, February 2011, https://www.jetro.go.jp/ext_images/en/reports/survey/pdf/2011_01_epe.pdf.) Furthermore, the shift from official negotiation ‘rounds’ to unofficial meetings seemingly correlates to the addition of Japan to the negotiations, in light of the 2013 deadline to conclude the negotiations. (See Office of the United States Trade Representative, ‘Joint Press Statement TPP Ministerial Meeting Bandar Seri Begawan, Brunei Darussalam’, 23 August 2013, https://ustr.gov/Joint-Press-Statement-TPP-Ministerial-Brunei.)


suspends the application of provisions on claims arising out of investment authorisations and investment agreements originally foreseen by the TPP (CPTPP, Article 2 and Annex, Article 2). This means that under the CPTPP only claims that relate to a breach of the substantive investment protections contained in Section A of the CPTPP Investment Chapter can be submitted to ISDS.

i Scope of investment protection

Article 9.2 regulates the scope of the CPTPP Investment Chapter. To benefit from its protections, the threshold definitions of investor and covered investment must be satisfied, as well as the threshold for the CPTPP Investment Chapter’s application ratione temporis. When it comes to the imposition of performance requirements (Article 9.10) or regulation in the public interest (Article 19.16), the CPTPP Investment Chapter applies to all investments, also non-CPTPP investments, because in certain circumstances a partial application or non-application of those measures could create competitive disadvantages for CPTPP investments.7

Investor

Defined as broadly as under the 2012 US Model Bilateral Investment Treaty (BIT), an investor of a CPTPP member state means a CPTPP member state itself, or a national or an enterprise of a CPTPP member state, that attempts to make, is making or has made an investment in the territory of another member state (Article 9.1).8 Thus, not only nationals and enterprises, but also CPTPP member states and even separate customs territories for which the CPTPP is in force, fall under the definition of an investor (Article 9.1).

The rather broad notion of ‘investor’ is counterbalanced by CPTPP member states reserving the right to deny the benefits of the CPTPP Investment Chapter to certain investors and their investments in either of the following two situations (‘denial of benefits’):

a First, if the investor is an enterprise of another CPTPP member state owned or controlled by a person of a non-CPTPP member state or the host state, that has no substantial business activities in the territory of a CPTPP member state other than in the host state (Article 9.15.1).9

b Second, if the investor is an enterprise of another CPTPP member state owned or controlled by a person of a non-CPTPP member state, and the host state adopts or maintains measures, with respect to the non-CPTPP member state or a person thereof, that prohibit transactions with the enterprise or that would be violated or circumvented if the benefits of the CPTPP Investment Chapter were accorded to the enterprise or its investments (Article 9.15.2).

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8 Sub-definitions are as follows: ‘Party means any State or separate customs territory for which the Agreement is in force’ (Article 1.3); ‘National means a “natural person who has the nationality of a Party” according to Annex 1-A (Party-Specific Definitions) or a permanent resident of a Party’ (Article 1.3); and ‘Enterprise means an enterprise constituted or organized under the law of a Party, or a branch located in the territory of a Party and carrying out business activities there’ (Article 9.1).
9 Similar provisions can also be found in other investment agreements. See NAFTA, Article 1113; Argentina–United States BIT, Article 1(2); 2012 US Model BIT, Article 17; Austria–Jordan BIT, Article 10.
Where a respondent state successfully establishes either of the above situations in an ISDS proceeding, a claim will likely be rejected.  

**Investment**

The definition of ‘investment’ is correspondingly broad. Similar to the 2012 US Model BIT, the CPTPP Investment Chapter utilises the term ‘characteristics of an investment’, which includes the commitment of resources, expectation of profit or assumption of risk (Article 9.1). Unlike some other investment agreements, the CPTPP Investment Chapter contains no ‘in accordance with host state’s law’ requirement. Further, as in many other investment agreements, a non-exhaustive list of forms of investments is set out – however, expressly excluding an order or judgment entered in a judicial or administrative action (Article 9.1). Whether an arbitral award may constitute an investment remains unclear but, in light of the wording, cannot be ruled out.

**Application ratione temporis**

The CPTPP Investment Chapter defines covered investments as those investments in existence as of the date of entry into force of the CPTPP, or established, acquired or expanded thereafter (Article 9.1). In other words, the CPTPP Investment Chapter applies to all investments, whether made before or after its entry into force. However, the CPTPP Investment Chapter will not bind a CPTPP member state in relation to an act or fact before CPTPP’s entry into force for that member state (Article 9.2.3).

**Limitations of scope for certain areas**

Investments into financial services are governed by the Financial Services Chapter (Chapter 11), which incorporates only some of the provisions of the CPTPP Investment Chapter by reference. Accordingly, investors can only invoke these provisions in ISDS proceedings (Article 11.2.2(a) and (b)).

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10 See, e.g., Pac Rim Cayman LLC. v. Republic of El Salvador (ICSID Case No. ARB/09/12), Decision on the Respondent’s Jurisdictional Objections, 1 June 2012, para. 4.30.

11 Some authors have pointed out that it is somewhat circular to define the term ‘investment’ by invoking the ‘characteristics of an investment’. See, e.g., Rudolf Dolzer and Christoph Schreuer, Principles of International Investment Law, 2nd ed. (2012), pages 63, 64.

12 See, e.g., Lithuania–Ukraine BIT, Article 1.1; ASEAN Comprehensive Investment Agreement, Article 4(a); and India–Brunei Darussalam BIT, Article 1(b).

13 See Maximilian Clasmeier, ‘Arbitral Awards as Investments: Treaty Interpretation and the Dynamics of International Investment Law’, International Arbitration Law Library, Vol. 39 (2016), page 70: ‘From a mere textual approach, it is difficult to see how an arbitral award could be previously invested before it is rendered. Nevertheless, it is a matter of interpretation to allocate its function in a broader context and the object and purpose of the respective BIT. It must in any case be taken into consideration.’

14 Annex 9-K, however, contains a carve-out with respect to certain claims under government procurement contracts with Malaysia for a period of three years after the date of entry into force of the CPTPP for Malaysia.

15 See Article 11.2.2(a), making reference, e.g., to Article 9.6 (Minimum Standard of Treatment) and Article 9.8 (Expropriation). See also the express limitation in Article 9.3.3.
With respect to taxation measures, the scope of substantive protections is narrowed down (Article 29.4). 16

ii Substantive standards of investment protection
The most frequently invoked substantive standards of investment protection addressed below seem to have been somewhat curtailed in the CPTPP Investment Chapter, presumably to ensure adequate regulatory power of the member states. This ‘right to regulate’ is emphasised throughout.

In a similar vein, the member states retain control over the scope of the substantive standards. Chapter 27 provides for the forming of a Trans-Pacific Partnership Commission (the Commission), which can issue interpretations of the CPTPP Investment Chapter, which shall be binding on a tribunal (Article 9.25.3).

National treatment and most favoured nation (MFN) treatment
Like practically all investment agreements, the CPTPP Investment Chapter prohibits nationality-based discrimination by the host state. The CPTPP Investment Chapter’s national treatment clause requires CPTPP member states to guarantee investors of another CPTPP member state and covered investments treatment no less favourable than treatment they accord, in like circumstances, to their own investors and their investments in their territories (Articles 9.4.1, 9.4.2). It also requires CPTPP member states to guarantee investors of another CPTPP member state and covered investments treatment no less favourable than treatment they accord, in like circumstances, to investors of any other state and their investments (Articles 9.5.1, 9.5.2).

It is widely accepted that differentiations are justifiable if rational grounds can be shown. The CPTPP Investment Chapter clarifies in a footnote that whether treatment is accorded in ‘like circumstances’ depends on the totality of the circumstances, including whether the relevant treatment distinguishes between investors or investments on the basis of legitimate public welfare objectives (Article 9.4, footnote 14). 17

Article 9.5.3 of the CPTPP Investment Chapter answers the long-standing controversy of whether MFN clauses can apply to dispute settlement provisions by clarifying that the treatment referred to in the MFN clause does not encompass international dispute resolution procedures or mechanisms, such as ISDS covered in Section B of the CPTPP Investment Chapter.

Another limitation of the MFN clause arises out of all of the CPTPP member states appearing to have expressed in some form that the MFN clause shall not extend to legal

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16 Only Article 9.4 (National Treatment), Article 9.5 (Most Favoured Nation Treatment), Article 9.8 (Expropriation) and Article 9.10.2 (Performance Requirements) apply.
17 See also the Drafters’ Note on Interpretation of ‘In Like Circumstances’ Under Article 9.4 (National Treatment) and Article 9.5 (Most Favoured Nation Treatment).
protects in their investment agreements already in force, but only to such protections in investment agreements a member state is to sign in the future.\footnote{See, e.g., Japan’s Annex II to the Investment Chapter, page 18, concerning MFN treatment (Articles 9.5 and 10.4) states ‘Japan reserves the right to adopt or maintain any measure that accords differential treatment to countries under any bilateral or multilateral agreement in force on, or signed prior to, the date of entry into force of this Agreement.’ See also Canada’s Annex II to the Investment Chapter, page 13; Australia’s Annex II to the Investment Chapter, page 19; and New Zealand’s Annex II to the Investment Chapter, page 9. This is the case, e.g., in Canada–Burkina Faso FIPA (2015), Annex III.1: ‘Article 5 (Most-Favoured-Nation Treatment) does not apply to treatment accorded by a Party under a bilateral or multilateral international agreement in force on or signed prior to the date on which this Agreement came into effect.’} This will require the CPTPP member states to adopt consistent practices when they conclude future investment treaties.\footnote{Suzy H. Nikièma, ‘The Most-Favoured-Nation Clause in Investment Treaties’, IISD Best Practice Series, February 2017, para. 6.2.}

\textit{Customary international law minimum standard of treatment of aliens (minimum standard of treatment)}

Similar to the North American Free Trade Agreement (NAFTA),\footnote{NAFTA, Article 1105.} the CPTPP Investment Chapter equates the fair and equitable treatment (FET) standard (and full protection and security) with the minimum standard of treatment under customary international law (Article 9.6.1). Moreover, the CPTPP Investment Chapter incorporates a NAFTA Free Trade Commission’s Note,\footnote{NAFTA Free Trade Commission: Notes of Interpretation of Certain Chapter 11 Provisions, 31 July 2001.} and provides that the concepts of FET and full protection and security do not require measures in addition to or beyond that which is required by the minimum standard of treatment of aliens, and do not create additional substantive rights (Article 9.6.2). This is echoed in a significant and growing number of recent international investment agreements involving CPTPP member states.\footnote{See, e.g., the Agreement Establishing the ASEAN–Australia-New Zealand Free Trade Area (2009), the Japan–Philippines EPA (2006), the China–Peru FTA (2009), the Malaysia–New Zealand FTA (2009).}

By limiting the FET standard to customary international law, the CPTPP Investment Chapter seeks to rein in the discretion of tribunals when considering the standard’s content. In reality, however, the minimum standard itself is quite indeterminate and requires interpretation. The process of establishing the content of customary international law (determining state practice and \textit{opinio juris}) is methodologically difficult and puts an onerous burden on the claimants.\footnote{UNCTAD Series on Issues in International Investment Agreements II, ‘Fair and Equitable Treatment’ (2012), pages 28, 29. See, e.g., \textit{Apotex Holdings Inc. and Apotex Inc. v. United States of America} (ICSID Case No. ARB(AF)/12/1), Award, 25 August 2014, paras. 9.47-9.65, where the tribunal set a ‘high threshold of severity and gravity before finding that a state has breached any elements of [NAFTA] Article 1105’, and dismissed claimants’ claim because they had failed to pass such a threshold.} This may become an issue under the CPTPP Investment Chapter according to which an investor has the burden of proving all elements of its claims, consistent with general principles of international law applicable to international arbitration.
In arbitral practice, the linkage to the minimum standard of treatment has hardly led to differing interpretations and applications of the FET standard, irrespective of which governing standard is ultimately assumed.\(^{25}\)

There are also other novel attempts to articulate the content of the FET standard in the context of certain controversial issues, by the clarification that the mere facts that (1) a party takes or fails to take an action that may be inconsistent with an investor’s expectations, and (2) a subsidy or grant has not been issued, renewed or maintained, or has been modified or reduced, by a CPTPP member state, do not themselves constitute a breach of the FET standard, even if there is loss or damage to the covered investment as a result (Articles 9.6.4, 9.6.5).

**Expropriation**

CPTPP member states agree not to expropriate or nationalise covered investments, either directly or indirectly, except (1) for a public purpose; (2) in a non-discriminatory manner; (3) on payment of prompt, adequate and effective compensation; and (4) in accordance with due process of law (Article 9.8.1). These elements are generally in line with many other international investment agreements.

An annex to the CPTPP Investment Chapter elaborates on the meaning of expropriation and requires, in determining an indirect expropriation, a case-by-case, fact-based inquiry that considers, among others, the economic impact, legitimate expectations and character of the government action. Non-discriminatory regulatory actions that are designed and applied to protect legitimate public welfare objectives do not constitute indirect expropriation (Annex 9-B(3)).\(^{26}\)

The CPTPP Investment Chapter clarifies the concept of expropriation in the context of subsidies and grants. A CPTPP member state’s decision not to issue, renew or maintain a subsidy or grant, or a decision to modify or reduce a subsidy or grant, in the absence of a legal or contractual commitment to do so, or in accordance with terms of the subsidy or grant, standing alone, does not constitute expropriation (Article 9.8(6)).

**Performance requirements**

The CPTPP Investment Chapter prohibits member states from imposing performance requirements such as export requirements, local content requirements and technology transfer requirements on investors (Articles 9.10.1 and 2). This aims to ensure that investors’ efficient business activities are undisturbed by host states’ demands in the interest of developing their economies.

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\(^{24}\) In a number of arbitral cases, tribunals relied on past arbitral decisions that did not refer to state practice or *opinio juris* in ascertaining the content of the minimum standard of treatment, see, Dumberry, *The Role and Relevance of Awards in the Formation, Identification and Evolution of Customary Rules in International Investment Law*, *Journal of International Arbitration*, Vol. 33.3, pages 277-284.

\(^{25}\) Marc Jacob and Stephan W. Schill, ‘Standards of Protection I. Fair and Equitable Treatment: Content, Practice, Method’, in: Marc Bungenberg et al. (eds.), *International Investment Law* (2015), page 708. In a number of cases, arbitrators seemed to be less interested in the theoretical discussion on the relationship between the FET and the minimum standard of treatment, and turned their attention primarily to the content of the FET obligation, and to whether it is qualified by the minimum standard of treatment, see UNCTAD, above note 23, pages 59, 60.

\(^{26}\) The 2004 Canada Model BIT and the 2004 US Model BIT have a similar annex with respect to expropriation.

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Most of the requirements stipulated in the CPTPP Investment Chapter are similar to those in past investment agreements, such as NAFTA. However, the CPTPP Investment Chapter sets forth novel performance requirements prohibited in relation to the use of technology. One is the requirement to use or accord preference to a technology of the host state or a person of the host state (Article 9.10.1(h)), and the other is the requirement to adopt certain terms as required by the host state in the technology licensing agreement freely entered into between the investor and a person of the host state (Article 9.10.1(i)). These provisions are expected to help investors investing in manufacturing and high-tech industries to freely make use of the technology they developed.

These new provisions are subject to an exception that allows the host state to adopt or maintain measures to protect legitimate public welfare objectives (Article 9.10.3(h)).

Right to regulate and corporate social responsibility

Apart from emphasising the right to regulate with respect to various substantive standards of protection as indicated above, the CPTPP Investment Chapter expressly, but somewhat declaratorily, acknowledges that CPTPP member states can undertake measures otherwise consistent with the CPTPP Investment Chapter to ensure that investment activity will be undertaken in a manner sensitive to environmental, health or other regulatory objectives (Article 9.16).

In a similar declaratory fashion, CPTPP member states reaffirm the importance of encouraging enterprises operating in their territory to voluntarily comply with corporate social responsibility standards (Article 9.17).

iii ISDS

The CPTPP Investment Chapter contains a modernised form of investment arbitration to address ISDS. This distinguishes it from NAFTA’s successor, the United States–Mexico–Canada Agreement, which has largely abolished ISDS, or the investment agreements negotiated by the European Union, which aim to establish an investment court system.

ISDS mechanism

A claimant may submit a claim under one of the following alternatives: the ICSID Convention and the ICSID Rules; the ICSID Additional Facility Rules; the UNCITRAL Rules; or, if the claimant and respondent agree, any other arbitral institution or any other arbitration rules (Article 9.19.4).

When doing so, the claimant must be aware of:

27 The provision was just adopted in the US Model BIT (2012); see Caplan and Sharpe, note 7 above, page 799.
28 A similar provision can be found in Japan’s recent treaty practice, see, Japan-Mongolia EPA, Article 10.7.1(k).
30 Provided that both the respondent and the claimant are parties to the ICSID Convention.
31 Provided that either the respondent or the claimant is a party to the ICSID Convention.
the mandatory six-month prior consultation and negotiation period (Articles 9.18, 9.19);  

b the three-year-and-six-month time limitation from the date on which the claimant first acquired, or should have first acquired, knowledge of breach or damage (Article 9.21.1);  

c the requirement of a mandatory written waiver of any right to initiate or pursue the same claims before any court or administrative tribunal, or through any other dispute settlement procedures (Article 9.21.2(b)); and  

d a fork-in-the-road-clause in the case of Chile, Mexico, Peru or Vietnam, which provides that an investor must elect between litigation before these state's domestic courts or administrative tribunals, on the one hand, or an investment arbitration claim, on the other hand. The election is definitive and exclusive, and choosing the former will prevent the investor from submitting the claim to arbitration (Annex 9-J).

Selection of arbitrators

In contrast to proposals by the European Union to replace investment arbitration with a standing investment court, parties under the CPTPP Investment Chapter continue to be able to select their arbitrators. However, the Chapter addresses perceived legitimacy concerns that arise when a system of adjudication permits adjudicators to act as arbitrator in one case and legal counsel in another (double hatting).

On 19 January 2019, the Commission established the Code of Conduct for Investor-State Dispute Settlement Proceedings (the Code of Conduct), which is required under Article 9.22.6. As a countermeasure against double hatting, the general principles of the Code of Conduct require that an arbitrator, upon selection, shall refrain for the duration of the proceedings from acting as counsel or party-appointed expert or witness in any pending or new investment dispute under the CPTPP Investment Chapter or any other international agreement (Code of Conduct, 3(d)). In the event of an alleged breach of the Code of Conduct, the rules governing the arbitration shall apply to any challenge, disqualification or replacement of an arbitrator (Code of Conduct, 3(f)).

Conduct of the arbitration

The CPTPP Investment Chapter offers procedural provisions to improve the efficiency of arbitral proceedings.

A tribunal shall address and decide as a preliminary question any objections by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favour of the claimant may be made under Article 9.29 (Awards) or that a claim is

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32 As explained above, the claimant cannot avoid this requirement by invoking a more favorable dispute settlement clause of another treaty that does not contain such a requirement because the treatment under the CPTPP MFN clause does not encompass the dispute resolution mechanism.

33 Neither the various arbitration rules (i.e., ICSID, SCC, ICC, and UNCITRAL) nor the IBA Guidelines on Conflicts of Interest in International Arbitration explicitly prohibit this practice, although the latter list ‘double hatting’ in the Orange List. For an empirical analysis of ‘double hatting’, see, e.g., Malcolm Langford, Daniel Behn, Runar Hilleren Lie, ‘The Revolving Door in International Investment Arbitration’, Journal of International Economic Law, Volume 20, Issue 2, 1 June 2017, pages 321-324.


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manifestly without legal merit (Article 9.23.4). A similar provision can be found in ICSID Arbitration Rule 41.5, but the CPTPP Investment Chapter allows a respondent to submit the above-referenced objections even in arbitral proceedings under other arbitration rules. Further, if the respondent so requests within 45 days after the tribunal is constituted, the tribunal shall decide on an expedited basis such an objection or any objection that the dispute is not within the tribunal’s competence, including an objection that the dispute is not within the tribunal’s jurisdiction. The tribunal shall suspend any proceedings on the merits, and issue a decision or award on the objection, stating the grounds therefore, no later than 150 days after the date of the request (Article 9.23.5).35

Most notable, a tribunal shall, before issuing a decision or award on liability, transmit its proposed decision or award to the disputing parties for their comments. They may submit written comments on the proposed award on liability, which the tribunal shall consider for its decision or award (Article 9.23.10). It remains to be seen whether the party review effectively addresses tribunal oversights, or whether it will be used by the parties to reargue their case.

Probably with a nod to reform efforts regarding the ISDS system currently undertaken within the UNCITRAL Working Group III, the CPTPP Investment Chapter provides that if an appellate mechanism for reviewing awards rendered by ISDS tribunals is developed in the future under other institutional arrangements, the CPTPP member state shall consider whether awards rendered under Article 9.29 should be subject to such an appellate mechanism (Article 9.23.11).

Side letter to the CPTPP

On 8 March 2018, alongside signing the CPTPP itself, New Zealand also signed side letters with five signatories to the CPTPP – Brunei, Malaysia, Peru, Vietnam and Australia – to exclude compulsory ISDS by the following two approaches:

The first approach is to fully exclude an investor’s right to ISDS. This can be seen in the side letters exchanged with Peru and Australia.36 Investors of Australia and New Zealand may nevertheless be able to draw on the ASEAN–Australia–New Zealand free trade agreement (AANZFTA) to get around this exclusion. By contrast, as of March 2019 New Zealand has no overlapping investment agreement with Peru, meaning that the exclusion of ISDS between those two states is effective.

The second approach, taken in the remaining three side letters,37 is more complex and provides for dispute resolution on a staged basis. In the case of a dispute, an investor should make a written request for consultations and negotiations, briefly describing the facts

35 However, the same article also provides that if a disputing party requests a hearing, the tribunal may take an additional 30 days to issue the decision or award. Regardless of whether a hearing is requested, a tribunal may, on a showing of extraordinary cause, delay issuing its decision or award by an additional brief period, which may not exceed 30 days. In addition, when the tribunal makes a determination on such objections, it may, if warranted, award to the prevailing disputing party reasonable costs and attorney’s fees incurred in submitting or opposing the objection. In determining whether such an award is warranted, the tribunal shall consider whether either the claimant’s claim or the respondent’s objection was frivolous, and shall provide the disputing parties a reasonable opportunity to comment (Article 9.23.6).

36 New Zealand–Peru Side Letter, paras. 1-2, and New Zealand–Australia Side Letter, paras. 3-4, both stating that no investor of a party shall have recourse to dispute settlement against the government of another party under Chapter 9, Section B (ISDS) of the CPTPP.

regarding the measures at issue. The state and the investor will then try to resolve the dispute amicably within six months by using non-binding third-party procedures, including good offices, conciliation and mediation, failing which the dispute may be submitted to arbitration in accordance with the CPTPP Investment Chapter, provided that the states concerned consent (and, in case of the Vietnam side letter, ‘specifically’ consent) to its application. However, despite the new requirement for specific host state consent, investors from those four states may be able to draw on the general consent to arbitration in a prior treaty such as AANZFTA to pursue ISDS against one of the states, even without the respondent state’s specific consent to arbitrate that dispute.

**Joint declaration on ISDS**

In addition to signing the side letters, New Zealand, together with Chile and Canada, made a joint declaration on ISDS. While reaffirming the right of each state to regulate within its territory to achieve legitimate policy objectives, this declaration recognises the strong procedural and substantive safeguards that are included in the CPTPP Investment Chapter, and ‘the important role of civil society and other interested groups on public policy matters relating to ISDS’, and intends ‘to consider evolving international practice and the evolution of ISDS including through the work carried out by multilateral international fora’.38

**IV  CONCLUSION**

As the above shows, the CPTPP Investment Chapter is calibrating, but not abandoning, familiar substantive and procedural investment protections.39 The contracting states have addressed current concerns about the investment protection system in an ‘evolutionary’ rather than a ‘revolutionary’ manner. This stands in stark contrast to the renegotiations of NAFTA or the European Union’s efforts to replace the tried and tested ISDS investment arbitration with an investment court system.

It would therefore not be surprising if the CPTPP Investment Chapter became an inspiration for other states seeking to modernise their investment agreements, in Asia and beyond.

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38 Joint Declaration on Investor State Dispute Settlement among New Zealand, Canada and Chile.

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In addition to serving as a testifying expert, Dr Barnes also leads teams that support Cornerstone Research’s affiliated experts. In this role, he has consulted on numerous matters requiring sophisticated accounting, financial and economic analysis.

Dr Barnes co-authored ‘The Use of Econometric and Statistical Analysis and Tools’, a chapter in The Guide to Damages in International Arbitration, and The Role of Economic Analysis in U.K. Shareholder Actions, a Cornerstone Research report. He has also published articles on valuation methods and damages analyses. A UK-qualified chartered accountant, Dr Barnes previously held positions in accounting and investment banking firms, as well as a consulting firm and in academia. Who's Who Legal has named Dr Barnes as a leading international arbitration economist. He was educated at London Business School, PhD; London Business School, MSc; University of Cambridge, master of advanced study in mathematics; and University of Oxford, BA (with honours).
MARINN CARLSON
Sidley Austin LLP

Marinn Carlson, co-leader of the firm’s global arbitration, trade and advocacy practice, focuses on international investment disputes, with an emphasis on investor–state arbitration. She represents both cross-border investors as well as respondent governments in ICSID and UNCITRAL arbitrations under bilateral investment treaties and free trade agreements, including NAFTA. She counsels clients in sectors ranging from financial services to energy to infrastructure development on the implications of international trade and investment rules for their global operations.

Marinn is consistently recognised for her work and experience. A recent academic analysis of the investment treaty arbitration community placed her in the top 25 most experienced investor–state dispute settlement counsel in the world, among the ‘core of lawyers who dominate the caseload’ (Journal of International Economic Law 2017). She is named as one of the Top 250 Women in Litigation by Benchmark, and as one of Latin America’s Top 100 Female Lawyers in Arbitration and Litigation by Latinvec.

Marinn is an adjunct professor at George Washington University Law School and American University’s Washington College of Law, a vice president of the American Society of International Law and serves on the Executive Committee of the Foundation for International Arbitration Advocacy.

CHLOE J CARSWELL
Reed Smith LLP

Chloe J Carswell’s practice is almost entirely focused on international arbitration, in particular investment treaty arbitration and public international law. Chloe has been involved with both ad hoc arbitrations and arbitrations under the rules of major international arbitration institutions, including the ICC, ICSID, and ad hoc arbitration under the UNCITRAL Rules. She acts for claimant investors and respondent states, and has handled cases in the mining, energy, hotel, construction, banking and telecommunications sectors. She has a wealth of experience dealing with disputes arising out of bilateral investment treaties and the Energy Charter Treaty, dealing with such issues as jurisdiction, unlawful expropriation, unfair and inequitable treatment, and denial of justice. She also advises clients on pre-contract structuring and the restructuring of investments. Her recent experience includes disputes over the transfer of licences, the alleged nationalisation of strategic assets, the interpretation of provisions in production sharing agreements, the effect and enforceability of stabilisation provisions, and breaches of other commercial agreements. Chloe also has significant experience of rail–related disputes, having acted for train operating companies against the national infrastructure provider and the regulator in arbitration, adjudication, expert determination, industry-specific dispute resolution procedures, mediation and judicial review.

PATRICK T CHILDRESS
Sidley Austin LLP

Pat Childress focuses his practice on international dispute settlement, particularly investment treaty arbitration and international commercial arbitration. He has represented foreign investors as well as respondent governments in proceedings before ICSID and its
Additional Facility, as well as in arbitrations under the UNCITRAL Arbitration Rules. Pat has also represented clients in commercial arbitrations under the auspices of the International Chamber of Commerce and the London Court of International Arbitration.

Pat has been invited to speak on international arbitration-related matters at Harvard Law School, Columbia Law School, New York University School of Law, George Washington University School of Law and Georgetown University Law Center, as well as various other professional events and conferences. He has also served as an arbitrator in the Foreign Direct Investment International Arbitration Moot Competition, and as a judge at the international finals of the Jessup International Law Moot Court Competition. Pat also teaches classes on international arbitration to foreign government officials at the International Law Institute.

KONSTANTIN CHRISTIE
Peter & Partners International Ltd
Konstantin Christie is a partner at Peter & Partners. For the past 10 years, his practice has focused on international commercial and investment arbitration, as well as disputes under public international law. A native Russian speaker, he regularly handles cases from eastern Europe, Russia and the former CIS. Konstantin was admitted to the Bars of New York and Massachusetts in 2007, and trained in Geneva and Paris. He has a law degree (JD) from Suffolk University and a bachelor of science (criminal justice) degree from Northeastern University in Boston.

RUXANDRA CIUPAGEA
Compass Lexecon
Ruxandra Ciupagea is a vice president at Compass Lexecon based in Madrid and London. Ruxandra works on litigation and international arbitration matters, focusing on pricing, valuation and damages assessments in energy and infrastructure markets. She has extensive experience in the fields of natural gas and liquefied natural gas, electric power, renewable energy and regulated infrastructure. Ms Ciupagea’s roles in international arbitration matters have included drafting expert reports, analysing data and developing models, as well as the preparation of expert witnesses for hearings.

Ms Ciupagea also has particular expertise in electricity market modelling, including valuation of transmission assets and storage technologies, as well as in the environmental arena, where she has consulted on issues related to air quality impacts, carbon leakage risk and carbon credits. She has participated in designing models related to the UK Domestic Renewable Heat Incentive and renewable energy support policies in Europe.

Ruxandra holds an MPhil in economics and finance from the Centre for Monetary and Financial Studies (Madrid), where she specialised in microeconomics, with a special focus on industrial organisation and regulation, and competition policy. She holds a BA in economics from Carlos III University (Madrid). Previous to joining Compass Lexecon, Ms Ciupagea worked for the energy and environment practices of another major economic consulting company.
KONRAD CZECH

Gessel, Koziorowski spk

Konrad Czech specialises in commercial and investment arbitration, and dispute resolution. He also advises on international trade and investment matters.

He has built up comprehensive experience in international arbitration, participating in a number of investment and commercial arbitration cases (under, among other rules, ICC 1998, ICC 2012, UNCITRAL 1976, UNCITRAL 2010, SCC 2010, Copenhagen Arbitration). Before joining Gessel he worked for the Office of General Counsel to the Republic of Poland, where he was a member of the international and European law department, and earlier for one of the major international law firms. In 2016, he also completed an international arbitration internship at a top German arbitration boutique in Hamburg. He has been with Gessel since 2018.

He is a graduate of the faculty of law and administration at the University of Warsaw (summa cum laude, 2010). He also holds a dual LLM degree in global business law from the New York University School of Law and in international and comparative law from the National University of Singapore Faculty of Law (2014). He received his PhD (cum laude) in legal studies from Kozminski University in Warsaw in 2016. His recent monograph, which is the publication of his PhD dissertation, titled ‘Evidence and Evidentiary Proceedings in International Commercial and Investment Arbitration. Selected Issues’, is the most comprehensive Polish-language writing on evidence in arbitration.

BEATA GESSEL-KALINOWSKA VEL KALISZ

Gessel, Koziorowski spk

As of 1995, arbitration has been an important element in Beata’ Gessel-Kalinowska VEL Kalisz’s professional practice. She has built up comprehensive experience in ADR, participating – whether as arbitrator, counsel or expert – in approximately 100 arbitration cases, domestic as well as international (conducted according to rules, including those of the ICC, UNCITRAL, FCC, IAA, SCAI, Lewiatan, Polish National Chamber of Commerce and the National Depository for Securities). The majority of the arbitral proceedings she has been involved in have concerned, but were not limited to, M&A transactions and construction law (including FIDIC regulations).

Between 2011 and 2017, she served as president of the Lewiatan Arbitration Court; upon leaving this position, she was appointed honorary president. She is an alternate member of the ICC International Arbitration Court (2015).

Beata Gessel is also an adjunct professor in commercial arbitration and M&A transactions at the Cardinal Stefan Wyszynski University.

In 2015–2016 she ran comparative law research on breach of M&A transactions as a visiting academic at Oxford University’s law department, and in 2016–2017 continued her research at the Cambridge University law department within the Herbert Smith Freehills visiting professor scheme.

A member of the Polish Arbitration Association, she also chairs the audit committee of the Polish Private Equity Association, an organisation assembling all the private equity funds active in Poland.
CATHERINE GILFEDDER

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Catherine Gilfedder is a senior associate in the international arbitration group of the Dentons UK and Middle East LLP London office. She specialises in investment treaty arbitration, public international law, and commercial arbitration and litigation. Catherine holds a first-class honours degree in law from the University of Cambridge and an LLM in international law (distinction) from University College London. Catherine is admitted as a solicitor in England and Wales, and the Republic of Ireland, and has Higher Rights of Audience before the English courts.

LEVON GOLENDUKHIN

Dentons

Levon Golendukhin has successfully counselled clients through all stages of the dispute resolution process, from pleadings to appeals to enforcement, and has appeared in both federal and state courts, and before arbitration tribunals. Clients for whom Mr Golendukhin has acted range from sovereign states to private companies in mining, agricultural and transportation sectors.

Mr Golendukhin has authored publications on topics in international investment law and investor–state arbitration, and has spoken at international arbitration events and conferences. He holds an LLM in international business law from the London School of Economics and Political Science, and a JD from Columbia Law School, where he was a Harlan Fiske Stone scholar, international programme chair for the Columbia Society of International Law and a staff editor on the Columbia Journal of Transnational Law.

NAOKI IGUCHI

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Naoki Iguchi is a partner of the international projects and arbitration practice team of Nagashima Ohno & Tsunematsu. Mr Iguchi has been advising construction companies, investment companies and infrastructure management companies in construction, transportation, crude oil pipeline and other infrastructure projects in various jurisdictions, including Asia, the Middle East, Africa and the American continent. Mr Iguchi also provides advice to national and foreign construction and investment companies with projects in Japan, including advising on the construction of a famous entertainment facilities project.

Mr Iguchi has represented many companies in international arbitration in Asian regions. Mr Iguchi was the country representative of Japan for the Dispute Resolution Board Foundation and a regular workshop lecturer of the Overseas Construction Association of Japan, Inc. Mr Iguchi also taught international project law at Keio Law School. Mr Iguchi studied at the University of Tokyo (LLB; LLM), Stanford Law School (LLM) and Beijing Language University (Mandarin training), and worked at law firms in Japan, China, Taiwan and the United States. Mr Iguchi is a member of the Japan ICC Arbitration Committee and was a member of ICC Workforce on Costs. Mr Iguchi is fluent in Japanese, English and Mandarin, and he also understands Spanish.
SHIMPEI ISHIDO

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Shimpei Ishido has been active in the field of international trade matters and international investment disputes for many years. He advises governments and major corporations with regard to anti-dumping and countervailing duties proceedings, as well as ICSID and PCA arbitrations. He currently serves as a member of the Japanese delegation to the UNCITRAL Working Group III (Investor–State Dispute Settlement Reform). Before joining Nishimura & Asahi, he led, as legal counsel to the Ministry of Foreign Affairs of Japan, the negotiations of Japan’s international investment agreements, including the investment chapters of the Trans-Pacific Partnership, the Japan–EU EPA, the ASEAN–Japan Comprehensive Economic Partnership, the Japan–Australia and the Japan–Mongolia EPAs, and the Japan–Mozambique BIT.

RASMUS JOSEFSSON

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Rasmus Josefsson is an associate at Sandart & Partners law firm. He specialises in domestic and international dispute resolution, and acts as counsel for international and Swedish parties in litigations and arbitrations in various commercial fields.

SAE YOUN KIM

*Yulchon LLC*

Sae Youn Kim chairs the international dispute resolution practice at Yulchon. Ms Kim practises primarily in the areas of litigation and arbitration, with an emphasis on commercial and international law. Before joining Yulchon, she served as a judge at various Korean district courts including the Seoul District Court, the Daejeon District Court and the Suwon District Court.

Ms Kim is currently an arbitrator at the Korean Commercial Arbitration Board and the Singapore International Arbitration Centre, and is licensed to practise in Korea and New York. She is regularly selected as a leading lawyer by publications such as *Chambers Global* and *Asialaw*.

CEYDA KNOEBEL

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Ceyda Knoebel is an English and Turkish-qualified solicitor advocate in the London office of Gibson, Dunn & Crutcher. She is a member of the firm’s dispute resolution and international arbitration groups.

Ms Knoebel advises on a wide range of disputes involving public international law and general commercial matters in common and civil law jurisdictions. She has experience in both commercial and investment treaty arbitration proceedings under the UNCITRAL, ICSID, ICC, VIAC and LCIA Rules. She teaches international investment arbitration at King’s College London. Ms Knoebel represents and advises clients across a broad spectrum of industries, including energy, oil and gas, financial services, banking and construction. Ms Knoebel continues to write on legal issues for a wide range of publications and is currently...
a senior editor of *The Turkish Commercial Law Review*, an independent English-language print journal of legal scholarship aimed at those in the international business, legal and academic communities with an interest in Turkey.

Ms Knoebel was admitted to the Bar in Turkey in 2007.

**MATTHEW KOH**  
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Matthew Koh (LLB (Hons) NUS, LLM (international legal studies) NYU) is a senior associate with Rajah & Tann Singapore LLP. His practice focuses on international arbitration, construction disputes and commercial litigation, as well as representing clients to enforce or set aside arbitral awards in Singapore.

**KOH SWEE YEN**  
*WongPartnership LLP*

Ms Koh Swee Yen is a partner in the commercial and corporate disputes, and international arbitration practices at WongPartnership LLP. Her practice focuses on complex, high-value, and cross-border commercial and investment disputes spanning various business sectors, including energy, international sales, investment, natural resources and trade, under the major institutional rules, including ICSID, ICC, ICDR, SIAC and UNCITRAL.

Ms Koh is the vice chair of the IBA Arbitration Committee, and a member of the editorial board of the *ICC Dispute Resolution Bulletin* and the ICCA-ASIL Task Force on Damages. She has served as co-chair of the YSIAC Committee and IBA Arb40, and is on the panel of arbitrators in the AIAC and HKIAC. She is a council member of the International Law Association – Singapore branch.

Ms Koh is recommended in various legal publications, including *The Legal 500* and *Chambers*. Regarded as ‘exceptional’, ‘in a league of her own’, ‘an especially good courtroom advocate’, ‘brilliant, decisive and fearless’ and ‘very well known for her arbitration practice and knowledge’, sources also praise her for a ‘keen sense of strategy’ and ‘great ability to quickly grasp her clients’ perspective and understand their commercial issues’.

**BARTON LEGUM**  
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Bart Legum is a partner in the Paris office of Dentons and head of the firm’s investment treaty arbitration practice. Bart has over 30 years’ experience in litigating complex cases and has argued before numerous international arbitration tribunals, the International Court of Justice, and a range of trial and appeals courts in the United States. His practice focuses on international arbitration and litigation in general, and arbitration under investment treaties in particular.

From 2000 to 2004, Bart served as chief of the NAFTA Arbitration Division in the Office of the Legal Adviser, United States Department of State. In that capacity, he acted as lead counsel for the United States government defending over US$2 billion in claims submitted to arbitration under the investment chapter of the North American Free Trade Agreement. The United States won every case decided under his tenure.
Bart is a past chair of the Section of International Law of the American Bar Association, an international bar organisation with over 24,000 members from over 90 countries around the world. In 2012–2013, he served as chair of the Section and chaired its Executive Committee, Council and Administration Committee.

In addition to being the editor of The Investment Treaty Arbitration Review, Bart is the editor of International Litigation Strategies and Practice (2nd ed. 2014; 1st ed. 2005), a book published by the American Bar Association. Bart publishes often on international dispute resolution topics, and frequently speaks at conferences on international arbitration and litigation.

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Chang Liu is an associate in the Beijing office and specialises in international commercial and investment treaty arbitration. She has experience with HKIAC, LCIA, SIAC, ICSID and CIETAC arbitration. She is a PRC-registered lawyer and received a master's degree in international law from China University of Political Science and Law.

ARTHUR MA
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Arthur Ma is a partner in DaHui Lawyers' litigation and arbitration team. Over the years, by focusing on complex commercial disputes resolution, Arthur has accumulated extensive experience in commercial arbitration and litigation involving foreign interests, and is especially adept at cross-border disputes and enforcement of foreign arbitration awards. He also honed his expertise in international arbitration. Prior to joining DaHui, Arthur worked with major international and PRC law firms in their Shanghai, London, Washington, DC, Hong Kong and Beijing offices for more than 12 years. During this period, he represented clients in both domestic and foreign litigation and arbitration proceedings under different jurisdictions and different laws and rules, including disputes arising out of large-scale engineering and construction, joint ventures, equity transfers, private equity investments, international sales of goods, etc. He has attended nearly 20 international arbitration hearings in different cities around the world and has obtained rich experience in hearing advocacy. He also has experience in compliance and FCPA investigations. Arthur is a native Mandarin speaker and is fluent in English.

GERVASE MACGREGOR
BDO LLP
Gervase MacGregor is the head of international advisory, risk and quality at BDO LLP. Gervase is one of the most experienced accounting expert witnesses in the United Kingdom and has extensive experience of international arbitrations. He has worked on cases in London (LCIA and ICC), Stockholm (SCC), Geneva (ICC), Paris (ICC, ICSID), Zurich (ICC, ad hoc cantonal) and Rotterdam (NAI). He has also worked on cases before the Court of First Instance of the European Communities, the High Court in London, the Copyright Tribunal and the Restrictive Practices Court.

He is the author of various books, including Expert Accounting Evidence, Solicitors Accounts, and Surveyors, Architects and Estate Agents. He has also written numerous articles for
Accountancy and other technical publications. His main areas of expertise are in the fields of natural resources, particularly oil and gas claims; state/operator disputes; takeover disputes; regulatory matters; and valuing companies and damages.

Prior to joining BDO, he worked as a petroleum geologist in the North Sea, Australia and West Africa. He has investigated and reported on the affairs of the MG Rover Group and Phoenix Venture Holdings on behalf of the Secretary of State and DTI.

ERIN B MCHUGH
NERA Economic Consulting

Erin McHugh is an associate director in NERA’s London and New York offices, and is a member of the firm’s European finance, litigation and dispute resolution group. She leads projects in the areas of financial economics and valuation. She has consulted on litigation and arbitration matters in various venues, as well as on internal and regulatory investigations. She has also provided testimony as an expert witness.

Ms McHugh has extensive experience in estimating quantum in matters involving an alleged breach. She also has considerable valuation experience, including the valuation of financial products (including various derivatives) and business assets (including those in emerging markets). She has worked on a number of disputes between brokerage firms and customers over investments in equities, derivatives, fixed-income and structured finance securities. Ms McHugh is listed in Who’s Who Legal: Arbitration.

Ms McHugh holds an MBA from the MIT Sloan School of Management and a BA, magna cum laude, in economics and French from Amherst College. She is also a CFA charterholder. Ms McHugh has presented at industry conferences and law firms on various topics, including damages estimation and valuation techniques. She is a co-author of ‘Floating-Rate Mortgage Securities’ in The Handbook of Mortgage-Backed Securities.

IAIN C MCKENNY
Profile Investment

Iain C McKenny is a director and co-founder of Profile Investment (PI), and heads its legal analysis division. Iain spent his formative years as a disputes lawyer with Freshfields Bruckhaus Deringer and subsequently Latham & Watkins in London and Paris. Prior to founding PI in 2018 with Alain Grec, he was general counsel of disputes and managing director at Vannin Capital. Iain specialises in international commercial and investment treaty arbitration across various sectors, including construction, technology, finance and general commercial.

In addition to being a qualified UK solicitor, registered foreign lawyer at the Paris Bar and co-founder of PI, Iain is a co-founder of the 2018 legal innovations GAR award winner – Delos Arbitration. Delos is an international arbitration institution specifically designed for small and medium-sized businesses.

ANDREW MACLAY
BDO LLP

Andrew Maclay is a forensic accountant who specialises in the quantification of damages in international arbitration, asset tracing and investigations, and has worked on disputes
in many jurisdictions, particularly France, Switzerland, west and east Europe, Africa, the Middle East and the CIS. Between 1991 and 1994 he worked in Burundi, Africa, and he is fluent in French.

He is a chartered accountant, a certified fraud examiner, an accredited accountant expert witness and a member of the Chartered Institute of Arbitrators. He has an MA in economics from the University of Cambridge.

He has given evidence in ICC, LCIA and ICSID tribunals, the English High Court, a criminal court and by way of deposition in US proceedings.

JEFF D MAKHOLM
NERA Economic Consulting

Jeff D Makholm concentrates on the issues surrounding the privatisation, regulation and operation of resource and infrastructure industries, including those that operate networks (such as oil and gas pipelines, electricity transmission and gas distribution systems, telecommunications and water utility systems) and those operating at specific sites, such as oil refineries, electricity generation plants, oil and gas storage facilities, gas treatment plants, mines, sewage treatment plants and airports. Disputes for such industries include the broad categories of valuation, pricing, market definition (including assessments of market power and mergers), and the components of reasonable regulatory and business practices.

On these issues, among others, Dr Makholm has prepared expert testimony, reports and statements, and has appeared as an expert witness on more than 250 occasions in LCIA, AAA, International Chamber of Commerce and ICSID cases, high courts in a number of countries (including US district courts), regulatory commissions and parliamentary panels.

In Who’s Who Legal: Arbitration, the ‘superb’ Dr Makholm was singled out for his work as an expert witness. Who’s Who Legal: Consulting Experts (Quantum of Damages) reported that Dr Makholm ‘is extremely knowledgeable and well thought of as an expert witness’.

DAVID MANNERS-WEBER
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David Manners-Weber is an associate at Jenner & Block. Prior to joining the firm, Mr Manners-Weber clerked for the Hon Guido Calabresi of the United States Court of Appeals for the Second Circuit; he received his JD from the Yale Law School in 2017.

LARS MARKERT
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Lars Markert is a foreign law partner at Nishimura & Asahi, Tokyo office. He is admitted to the German and New York Bars, a registered foreign lawyer in Japan, and advises clients in both investor–state and international commercial arbitrations. Lars has experience in representing investors and states in proceedings under the ICSID Convention and the UNCITRAL Arbitration Rules, and in advising on potential claims under bilateral investment treaties and related negotiation strategies. He holds a PhD in investment arbitration from the University of Cologne on the topic of dispute settlement clauses in investment agreements. He is an academic adviser to the International Investment Law Centre Cologne, teaches investment
law and procedure at the University of Cologne, and regularly speaks and publishes on issues of commercial and investment arbitration. Lars is recommended for his arbitration expertise by various legal directories.

**LUCY MARTINEZ**

*Martinez Arbitration*

Lucy Martinez is an independent counsel and arbitrator, with extensive experience in advising and representing investors and states in complex, high-value international arbitrations, including before AAA, ICC, ICSID, LCIA and UNCITRAL tribunals, pursuant to investment treaties and contracts. Lucy has worked on cases involving oil and gas, electricity, highway construction, telecommunications, satellite technology, waste processing and rock concerts, in various regions of the world, including Africa, Asia, Europe, Latin America and North America. She also sits as arbitrator (sole, chair and co-arbitrator) in ICC, LCIA and SIAC arbitrations. Lucy has been recognised in the 2017, 2018 and 2019 *Who's Who Legal: Arbitration* and ‘Future Leaders’ directories, and in *The Legal 500 UK* for expertise in public international law.

**CARMEN MARTINEZ LOPEZ**

*Three Crowns LLP*

Carmen Martinez Lopez is a partner in the London office of Three Crowns. She has appeared as advocate in numerous investment treaty and commercial arbitrations, both under the rules of the major arbitral institutions and *ad hoc*, and involving a variety of jurisdictions, with a particular focus on Latin America and Spain. Carmen is recognised in many major publications, with sources describing her as ‘a great legal mind’ and ‘an excellent practitioner’, who ‘understands problems very well in a global way’, ‘has a lot of availability for the client’, and ‘has certainly been building up a fantastic reputation’ in the market for her work in both investment treaty and commercial arbitrations. Carmen is dual-qualified in civil law and common law, and regularly handles contentious work in English, Spanish and French. She is admitted to the New York and Madrid Bars, in addition to being a solicitor of the Senior Courts of England and Wales. Carmen holds law degrees from Columbia Law School, the College of Europe and the University of Murcia (Premio Nacional Fin de Carrera and Premio Extraordinario Fin de Carrera). She is the President of the British Chapter of the Spanish Arbitration Club and a member of the Arbitrator Appointment Committee of the Madrid Arbitration Court.

**BOAZ MOSELLE**

*Compass Lexecon*

Boaz Moselle is an executive vice president at Compass Lexecon based in London. He is an economist who has worked in academia, consulting and government.

Dr Moselle began his career as an assistant professor at Northwestern University, where he taught courses in quantitative methods and in game theory. He holds a PhD in economics from Harvard University, and an MA and PhD in mathematics from the Universities of Cambridge and London. He was previously a managing director of the UK energy regulator.
Ofgem. He teaches in the Brussels School of Competition on competition and regulation, and as a guest lecturer at Queen Mary University of London School of Law on issues related to damages and disputes in the energy industry.

Boaz has provided expert witness testimony in approximately 50 international arbitrations, in the context of both commercial and investment treaty disputes. *Who's Who Legal* 2017 notes that ‘Boaz Moselle draws praise for his “exceptional genius” and prowess in gas-pricing disputes’, and that ‘one client describes him as “the best expert I have ever seen under cross-examination, and possibly the brightest I have seen in my whole career”’.

Dr Moselle’s areas of expertise include oil and gas; other energy sources; regulated infrastructure; and competition and anti-trust issues in the energy industry.

**PATRICIA NACIMIENTO**

*Herbert Smith Freehills LLP*

Dr Patricia Nacimiento is the co-head of the German dispute resolution practice. She has over 20 years of experience as a disputes practitioner. Her practice spans a wide range of disputes work with a special focus on domestic and international arbitration, as well as investor–state disputes. Patricia has significant experience in disputes related to energy, construction and post-M&A. The German government appointed her in 2007 as one of four arbitrators to the panel of arbitrators at the International Centre for Settlement of Investment Disputes (ICSID).

As a party representative, she has conducted over 120 arbitration proceedings under the rules of numerous arbitration institutions – including ICC, ICSID, SCC, CIETAC, DIS, LCIA, ICDR, the Swiss Chamber of Commerce, the Indian Council of Arbitration and the Danish Institution of Arbitration, as well as *ad hoc* proceedings. She is also regularly appointed as an arbitrator and has led numerous international ICC, DIS and *ad hoc* arbitration proceedings as a chairperson, sole arbitrator or party-appointed arbitrator.

For years, Patricia has been listed as a leading disputes expert in renowned rankings. She publishes regularly on disputes-related subjects and is co-editor of the leading arbitration manuals *Arbitration in Germany – The Model Law in Practice* (Kluwer 2015) and *The New York Convention – a Global Commentary* (Kluwer 2008).

Patricia gives lectures on arbitration at the universities of Berlin, Heidelberg, Frankfurt and Saarbrücken. A native German speaker, Patricia is also fluent in English, Spanish, Italian and French.

**ADRIANE NAKAGAWA BAPTISTA**

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Adriana Nakagawa Baptista has an LLB from the Faculty of Law of the University of São Paulo, where she is a PhD candidate in international trade. She has been working in domestic and international arbitrations since 2006. Mrs Nakagawa offers consultancy, and represents Brazilian and foreign clients in matters of international trade law, arbitration and construction law. She received a LExs Gold Scholarship and is a master in advanced studies in european and international business law, Leiden University (Netherlands). Her specialisation is in arbitration, contract negotiation and construction law by the International Chamber of Commerce (ICC-Paris), American University Washington College of Law (coordinated by Horacio Grigera Naón) and The Hague Academy. In the international trade area, she works as a researcher at the School of Economics of São Paulo of the Getulio Vargas Foundation,
and in several projects of Professor Dr Vera Thorstensen at the Center for Global Trade and Investment. A member of the World Business Law Institute of the International Chamber of Commerce, the Brazilian Institute of Construction Law and the Young International Council for Commercial Arbitration, Mrs Nakagawa Baptista lectures regularly and has written articles in the field of arbitration and trade.

MICHAEL D NOLAN
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Michael D Nolan is a partner in the Washington, DC office of Milbank LLP. He has served as counsel or arbitrator in cases under AAA, ICC, ICSID, HKIAC, SIAC, UNCITRAL and other rules. Michael represents companies and states in court proceedings involving sovereign immunity, acts of state, and recognition and enforcement of foreign judicial and non-judicial awards. He is consistently recognised as a leading international practitioner by Chambers USA, Euromoney and Super Lawyers. He writes frequently on transnational disputes and has co-edited a collection of determinations in political risk insurance disputes (Oxford University Press). Michael is an adjunct professor of law at Georgetown University and general counsel of the Intellectual Property Owners Association. He is a member of the board of directors and international advisory committee of the American Arbitration Association, the Users Council of SIAC and the ICSID panel of arbitrators, and is a fellow of the Chartered Institute of Arbitrators.

OBIOMA OFOEGO
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Obioma Ofoego is an associate in the Dentons Paris office. He specialises in public international law, investment treaty arbitration and international commercial arbitration. Prior to joining Dentons, he practised as a barrister in London, and served as an assistant legal adviser in the Foreign and Commonwealth Office.

ESRA OGUT
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Esra Ogut is an associate at Peter & Partners who specialises in international commercial and investment arbitration. As part of a counsel team, she advises and represents clients on high-value arbitrations governed by different institutional rules, including ICC, UNCITRAL, Swiss and ICSID arbitration rules. As a dual-qualified lawyer (admitted to the New York and Istanbul Bars), Esra handles cases involving major international and Turkish corporations in relation to arbitration and litigation proceedings. Esra received her LLB from Koç University, Istanbul, and her LLM degree from Columbia Law School, New York.

CHUDOZIE OKONGWU
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Chudozie Okongwu is a managing director in NERA’s London and New York offices, and heads NERA’s European finance, litigation and dispute resolution group. He specialises in the areas of financial economics and valuation.
Dr Okongwu has provided expert witness testimony in multiple international arbitration venues, including ICSID, the ICC International Court of Arbitration and the Arbitration Institute of the Stockholm Chamber of Commerce, and in ad hoc arbitration forums. He has also submitted expert evidence and testified in various national court systems as well as in US domestic arbitration forums. Dr Okongwu is listed in Who’s Who Legal: Arbitration and Who’s Who Legal: Consulting Experts. He is also a member of the P.R.I.M.E. Finance panel of finance experts.

Prior to joining NERA, Dr Okongwu was a member of Banque Paribas’ fixed income emerging markets team in London and New York. He holds a PhD and an MA in economics from the University of California, Berkeley, and an SB in economics from the Massachusetts Institute of Technology. He is the lead author of ‘Credit Derivatives and Mortgage-Backed Securities’ in The Handbook of Mortgage-Backed Securities and has authored articles in The Journal of Structured Finance, International Journal of Finance & Economics, The Guide to Damages in International Arbitration and Wall Street Lawyer.

LAURA T W OLIVE
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In 2010, he became the first non-senior judge from ASEAN to be elected as a Master of the Bench of the Inner Temple. He was the first ASEAN national lawyer to be appointed Queen’s Counsel. He is a chartered arbitrator (FCIArb, FMIArb, FSIArb) and has a PhD, LLM, DiplCArb and LLB (Hons).
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He has intervened at the request of states, investors and corporate clients in disputes in many sectors, including mining and port concessions, railway projects and infrastructure construction.

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In the field of international arbitration, Mr Yeğinsu has been described as ‘fiercely clever but also a true team player; he knows arbitration inside out and is a very elegant and effective advocate’ (Chambers UK), possessing ‘serious legal brainpower, accompanied with a deft touch with clients’ (The Legal 500) and ‘in a class of his own’ (Chambers Global), with experience of advising on and appearing in commercial and investment arbitrations, including under the ICSID, UNCITRAL, LCIA, ICC, LMAA and CIArb Rules. Mr Yeğinsu also accepts appointments and is recognised by Who’s Who Legal as ‘very thorough and decisive as arbitrator’. In 2019, he was shortlisted for Barrister of the Year in International Arbitration by The Legal 500.

Frequently appearing in the English Commercial Court, Administrative Court and the Chancery Division, Mr Yeğinsu has acted in over 30 cases in the English Court of Appeal, UK Supreme Court and the European Court of Human Rights.

Mr Yeğinsu is adjunct professor of law at Georgetown University Law Center in Washington, DC and Koç University Law School in Istanbul, where he teaches investment law and arbitration. Mr Yeğinsu is also a lecturer in law (teaching public international law) at Columbia Law School in New York and partner fellow at the Lauterpacht Centre for International Law, University of Cambridge.

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Appendix 2

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