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Legal Aspects of Recourse to Arbitration by an Investor Against the
Authorities of the Host State under Inter-State Treaties

*Les aspects juridiques du recours à l'arbitrage par un investisseur contre
les autorités de l'Etat hôte en vertu d'un traité interétatique*

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Part I General and Preliminary Issues

A. Introduction

1. Purposes and features of the Report

1. The purpose of a Report presented to the Members of the *Institut* who are renowned international lawyers, academics and practitioners of arbitration between private individuals and States, should not be that of summarizing a rather well-known subject but, preferably, that of encouraging and stimulating an in-depth study and discussion among all of us in view of possibly adopting shared solutions to be proposed and suggested by the Institute in order to facilitate the overcoming of problems and difficulties which presently characterize this important and continuously developing field of international law. In this perspective, your Rapporteur would consider appropriate to highlight hereinunder some developments of investment arbitration which appear the most problematic and capable of provoking further reflections on some of the basic characteristics and assumptions which have led to the present rapid developments of investment arbitration and, subsequently, also to some sharp reactions to those developments or, sometimes, even to the global system of investment arbitration.

Three fundamental characteristics, developments and problems of treaty-based investment arbitration will be shortly mentioned here in order to highlight the general prospective adopted for the presentation of the law in this important, continuously evolving and delicate field.

2. The first development is represented by the construction of the consent by States to international investment arbitration as expressed not only in the agreements to arbitrate but also in domestic laws and particularly in the same treaties providing for investment arbitration. On the basis of this construction the s.c. 'arbitration without privity' has rapidly developed in the field of the investment. This practice permits to investors to start 'unilaterally' arbitration against host States simply filing the request for arbitration against them. This filing is considered as the acceptance by the investor of the standing offer to arbitrate contained in the domestic law of the host State or in the investment treaties stipulated by the latter with the national State of the investor.

3. The second fundamental evolution is represented by the fact that starting from the middle of the 2010s, some important capital-exporting

States, as the US and Canada, have begun to be respondents in investment arbitration.

This has probably been the reason of some changes in the Model BITs adopted by these States, where better consideration is provided for certain public interests of the States. For instance the US and Canada BIT Models of 2004, in the Appendixes especially devoted to expropriations, have excluded from the concept of expropriation, and even from that of indirect or creeping expropriation, those regulatory measures adopted for protecting some public interest such as the protection of environment, human health, and human rights in general.

This new trend appears confirmed by the US Model BIT of 2012 which seems to demonstrate a permanent transformation of what seemed to be the traditional *opinio juris* of the US according to which regulatory measures were considered in the same manner as of all other forms of creeping or indirect expropriations.

Conclusively this Report will reserve particular attention to some new actors and new phenomena that have recently appeared in the world of international arbitration. Reference will be made to the transparency of arbitrations proceedings increasingly demanded and obtained by new actors from the civil society. Problems have been also raised by the association of numerous claims in some disputes and then arbitral procedures. For a couple of well known arbitration cases against Argentina even the expression of mass (or class) arbitration has been employed.

In addition also cases of conflict of interested have multiplied, due to the participation to the dispute of Third Party Founders and also the lack of a basic distinction of roles between personalities usually acting as counsel or arbitrators, or arbitrators usually appointed by investors and those usually appointed by States.

2. The success of international investment arbitration and its main ground

4. The great success of arbitration in the field of investments is fairly recent as it can be traced back only in the early nineties, when for the first time the consent to international arbitration by the host State of foreign investments has been based not on a traditional arbitration clause contained in a investment contract, but directly on a bilateral treaty for the promotion and protection of investments signed between the host State and the national State of the investor. Since then, some unofficial researches on the subject mention more than three hundred and fifty arbitral decisions¹. Furthermore this number seems to be destined to a

¹ Many of these arbitral awards can be easily consulted in the specialized websites, among

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rapid increase when one considers that the basis for the consent of the host State is found directly in the bilateral treaties and the number of such bilateral treaties has become really impressive, being currently evaluated as being more than three thousand and even continuing to increase exponentially².

5. In the period preceding the nineties, arbitrations between States and foreign investors had been rather limited since these were constituted only by certain well-known, though sporadic, ad hoc arbitration cases³ or arbitrations conducted in accordance with the common rules of international commercial arbitration⁴. Subsequently, the Washington

which, principally, <http://icsid.worldbank.org/ICSID/Index.jsp>;
<http://www.investmentclaims.com>; <http://ita.law.uvic.ca/news.htm>.

² These data are commonly reported. Cf. for some initial assessments: SACERDOTI, *Bilateral Treaties and Multilateral Instruments on Investment Protection*, RCADI, 269, 1997, 255 ff.; MAURO, *Gli accordi bilaterali sulla promozione e la protezione degli investimenti*, Turin, 2003. BIT texts are published in the UNCTAD website at <http://www.unctadxi.org/templates/DocSearch779.aspx>.

³ Among them, particular attention is obviously due to the three famous arbitrations of the 70's in the cases *British Petroleum, Liampo and Texaco-Calasiatic v. Libia*, as well as, more generally to the arbitral case law concerning the State Contracts, which has been analysed, among others in BERNARDINI, *The Law Applied by International Arbitrators to State Contracts, Liber Amicorum* Karl-Heinz Bockstiegel, Berlin, Bonn, Munich, 2001, 51 ff. Regarding these cases and the ones belonging to the previous period, cf. STERN, *Trois arbitrages, un même problème, trois solutions*, *Revue de l'Arbitrage* 1980, 22 ff.; GIARDINA, *State Contracts: National versus International Law*, *The Italian Yearbook of International Law*, 1980-81, 147 ff., at 158 ff.; LEBEN, *La théorie du contrat d'état et l'évolution du droit international des investissements*, RCADI, 302, 2003, 197 ff.

⁴ Among the cases administered by the International Chamber of Commerce, the cases of typical investment arbitrations, based on arbitration clauses included in the agreements between investors and host States are not rare. Cf., among the recent decisions by ICC arbitral Tribunals: the decision of 18 May 2000 in the case n. 9151, *Yashlar and Brida SAPIC v. Turkmenistan*; the decision of 27 April 2005 in the case n. 12913, *Capital India Power Mauritius 1 and Energy Enterprises (Mauritius) Company v. The State of Maharashtra (India) and others*; the decision of 6 August 2007 in the case n. 13176, *Balkaniki v. Republic of Macedonia*.

Numerous have then be the cases of *ad-hoc* arbitrations on the basis of the UNCITRAL Rules. As an example, cf. the decisions rendered in the following cases: *Biloune and Marine Drive v. Ghana*, Award on Jurisdiction and Liability of 27 October 1989; *CME v. Czech Republic*, Partial Award of 13 September 2001; *Saluka Investments BV v. Czech Republic*, UNCITRAL arbitration, Partial Award of 17 March 2006.

This is also the case of arbitrations before the arbitration tribunals of the Stockholm Chamber of Commerce. Among these, cf. for instance, the case *Bogdanov v. Republic of Moldova*, Award of 22 September 2005, and the preceding case *Sedelmayer v. Russian Federation* decided by an Arbitral Tribunal in Stockholm on

Convention of 18 March 1965 instituted a general legal framework and an institutional structure for this kind of arbitration, but still required, or was applied as still requiring, in a traditional manner, that the parties had expressed their written consent to the submission of their dispute to the arbitral mechanism and tribunal. The Preamble of the Convention specifically stated that the Contracting States, for the mere fact of ratification, acceptance or approval of the Convention, could not be considered to be obliged, without manifestation of an express consent, to submit a particular dispute to conciliation or arbitration. And indeed, the first ICSID cases until the years 1985-1990 were based on traditional arbitration clauses included in investment contracts that indicated the agreement of the parties to submit specific disputes to the World Bank arbitration.

6. The first innovative development therefore occurred in 1985 in the famous *Pyramids* case (*SPP v. Egypt*, Decision on Jurisdiction of 14 April 1988)⁵ where the consent of the Egyptian State to ICSID arbitration and, accordingly, the jurisdiction of the Centre and the competence of the Arbitral Tribunal, were based on a provision of Egyptian law, art. 8 of Law no. 43 of 1974 on foreign investments. The Arbitral Tribunal considered in that case that the arbitration agreement had, as constituent elements, in respect to Egypt, the consensus to ICSID arbitration as provided by art. 8 of Law no. 43 and, in respect to the investor, the Request for ICSID arbitration made by the foreign investing company. A second case worth mentioning is the *Tradex Hellas v. Albania*, Decision on Jurisdiction of 24 December 1996, where the consent of Albania to ICSID arbitration was identified in Article 8.2 of the Albanian law n. 7764 of 1993 on foreign investments. The solution adopted in these two cases seems commonly accepted within the ICSID arbitration, despite its undoubtedly innovative character. Indeed, the legal provisions of the kind of the Egyptian and Albanian ones could have been understood and applied in a traditional way, namely as simple policy expressions of the States concerned, favorable to the inclusion of ICSID arbitration clauses

7 July 1998, object of the subsequent decisions by the District Court of Stockholm on 18 December 2002 and of the Stockholm Court of Appeal on 15 June 2005, which rejected a request for annulment by the Russian Federation: the text of the initial arbitral Award is reproduced in *Stockholm International Arbitration Review*, 2005, 37 ff.

⁵ Cf. ICCA Yearbook 1991, 19 ff.. On this case and the issues it raises, cf. among others: SHIHATA, PARRA, *The Experience of the International Center for Settlement of Investment Disputes*, *Foreign Investment Law Journal* 1999, 304 ff.; GIARDINA, *International Investment Arbitration: Recent Developments as to the Applicable Law and Unilateral Recourse*, in DEL VECCHIO (Ed.), *New International Tribunals and New International Proceedings*, Milan, 2006, 42 ff.

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in future investment contracts with foreign individuals, and not as the expression of an actual written consent with regards to an indefinite series of specific future disputes.

7. It is well known that a subsequent decisive development took place with the ICSID arbitral award of 27 June 1990 in the case *AAPL v. Sri Lanka*. In such case, for the first time it was held that the clause, in a BIT selecting ICSID arbitration as a means for solving future disputes, could be considered as an expression of the consent of the State to ICSID arbitration in every single future case. This consent by the State was considered as such capable to combine with the will expressed by the investor through the presentation of the request for arbitration, with the result to represent for every subsequent case the basis of both the jurisdiction of the Washington Center and the competence of the Arbitral Tribunal. Notwithstanding that this conclusion was reached in a case where the existence of the jurisdiction of the Center and the competence of the arbitral Tribunal was not actually disputed by the parties, the said conclusion has not being questioned afterwards, despite the fact that this kind of clauses contained in BITs could have continued to be applied in the traditional way, as a simple engagement by the host State of investments to insert within the investment contracts to be entered into with the investors one of the mechanisms of settlement of disputes which are foreseen in the BIT, keeping however the States and the investors free to agree or not on the mechanism to be actually selected. The solution had never been conceived before nor realized in practice until then, despite the fact that the BITs practice dated back to the late 50's. In any case however, this solution can now be considered as accepted and representing the main basis for the explosion of investment arbitration in recent years⁶.

8. At present, investment arbitrations are started “unilaterally” by the investors, directly through the submission of the request for arbitration. Such request is considered the acceptance by the investor of the general offer of arbitration contained, with regards to the State, in a domestic law or in a BIT. This results in an asymmetry of positions between investor and State: whilst the former can directly start the procedure it chooses without any specific consent by the State with respect to the case at hand, the State cannot start any arbitral action against the investor if the latter

⁶ Cf.: ALEXANDROV, *The “Baby Boom” of Treaty-Based Arbitrations and the Jurisdiction of ICSID Tribunals. Shareholders as Investors under Investment Treaties*, JWIT, 2005, 387 ff.

has not signed an ad hoc arbitration clause. This phenomenon has been referred to with a successful expression, namely “arbitration without privity”, in order to emphasize the characteristic possibility for the investor to start an arbitration case, notwithstanding the absence of subscription by the State of an express arbitration clause with regards to that specific case⁷.

9. **Your Rapporteur shares the view** that the above developments have to be considered as definitive acquisitions producing the major positive result of opening the way to direct actions by individuals (investors) for protecting their rights against States having violated, or allegedly violated, such rights. This is a sure progress, in line with similar developments already existing in the field of the protection of human rights and fundamental freedoms and it must be preserved. But it is an undeniable fact that the effects of these developments, occurring in a system traditionally based and conceived for cases of specific agreements concluded between investors and host States, need to be carefully verified and controlled in order to avoid results perhaps contradicting or not harmonizing with the consent expressed by the State parties having concluded the treaties founding the investment arbitration at issue.

B. BITs and customary international law

1. In general

10. In this respect the key and seminal question has been and still is whether the extremely numerous bilateral treaties on the protection of foreign investments, given their substantially homogenous content, determined the creation of a body of international customary law.

A general positive answer to this question is offered by: SCHWEBEL, *The influence of Bilateral Investment Treaties on Customary International Law*, ASIL Proceedings 2004, TDM 2005; REINISCH, *Investment Protection and Dispute Settlement in Preferential Trade Agreements: A Challenge to BITs?*, ICSID Review, 2009, 416, at 421; CHALAMISH, *The future of BITs: a de facto multilateral agreement?*, Brooklyn JIL 2009, 304, at 314 ff.

A different approach could be that suggested in an answer (Treves) to the Questionnaire and approved by the Participants in the Rome Meeting of the Commission. This approach is based on the statement by the ICJ in

⁷ The definition is by PAULSSON, *Arbitration Without Privity*, ICSID Review, 1995, 232 ff. On this practice, cf. some critical comments by PRUJNER, *L'arbitrage unilatéral: un coucou dans le nid de l'arbitrage conventionnel?*, Revue de l'arbitrage, 2005, 63 ff., and by GIARDINA, *Clauses de stabilisation et clauses d'arbitrage: vers l'assouplissement de leur effet obligatoire?*, Revue de l'arbitrage, 2003, 347 ff.

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the *Diallo* case (*Republic of Guinea v. Democratic Republic of Congo*) ICJ Judgment on Preliminary objections of 24 May 2007 (ICJ Reports 2007, 582), at paras. 88-90, even though this judgment concerns the alleged impact of BITs and other treaties concerning investment on the customary law of diplomatic protection. The ICJ argues for the ambivalence of treaty practice, notably stating at para. 90: “*The fact invoked by Guinea that various international agreements, such as agreements for the promotion and protection of foreign investments and the Washington Convention, have established special legal regimes governing investment protection, or that provisions in this regard are commonly included in contracts entered into directly between States and foreign investors, is not sufficient to show that there has been a change in the customary rules of diplomatic protection; it could equally show the contrary*”.

11. According to the above approach, the first and different view maintaining that the initial of BITs have definitively created customary international law, appears to reflect the initial evaluation of the international investment practice as rapidly developed up to the middle of the 2010's, based on the large number of BITs concluded and arbitration awards which rather constantly expanded and consolidated the protection of foreign investors. Presently this trend seems to have concluded its process of consolidation.

It has to be added that the first general view referred above has been proposed in a moment when some changes and differences emerged from new Model BITs in 2004 adopted by important State actors in the international investment world such as the US and Canada, who expressed an opinion favourable to the protection of some public interests such as those relating to environment, public health and human rights. It has to be added that this trend is presently confirmed by the US 2012 BITs and the preparatory works of the new Canadian Model.

12. Consequently, at present the most appropriate - and in any case legally correct - approach appears to be that of the full respect of the different clauses of the various applicable BITs. This is so also because these clauses would necessarily apply, notwithstanding any possible differences with the alleged rules of customary law. Actually the latter can always be derogated, with the limited exception of some procedural and substantive international peremptory norms.

The approach here suggested appears to be confirmed by investment arbitration cases which show a variety of solutions, often contradicting

each other and suggesting a decisive attention to be given the characteristics of each particular case as well as the necessary caution in taking into account decisions in previous cases.

13. Obviously, when international law is referred to in the interpretation and application of BITs, such reference should be made correctly and appropriately. In this respect it seems worth noting that CRAWFORD, *Similarity of issues in disputes arising under the same or similarly drafted investment treaties*, BANIFATEMI (Ed.), *Precedent in International Arbitration*, Juris Publishing 2008, 97 ff., at 99, mentions numerous generic references in investment arbitration decisions to the Vienna Convention on the Law of Treaties or to the case law of the ICJ or the PCJ. In respect to the latter a critique is advanced to the common references in investment case law and doctrine to the famous dictum contained in the *Chorzow Factory* decision of 13 September 1928 for the case of quantification of damages when on the contrary, the principles established by the PCJ were affirmed and applied in a purely international dispute between States equally sovereign and not in a dispute between individuals and States, where different factors could come into consideration.

14. Considering the developments on the above Chapters, **your Rapporteur is inclined to express some reservations** regarding to a rather shared trend affirming the existence of a sort of body of law represented by previous awards and decisions which new arbitral tribunals should respect or, at least, carefully considers before distinguishing the new case from the previous ones.

2. Precedent in international investment arbitrations

15. Elements in favour of the existence of a body of precedents for investment tribunals can be found in: GAILLARD, BANIFATEMI (eds.), *Precedent in International Arbitration*, Juris Publishing 2008, esp. Part. II (WEIL, CRAWFORD, GUILLAUME, KAUFMANN-KOHLER); MARTINEZ-FRAGA, SAMRA, *The role of precedent in defining res judicata in investor-State arbitration*, 32 *Northwestern JILB* 2012, 419, at 433 ff.; SCHREUER, *Why Still ICSID?*, CALAMITA, EARNEST, BURGSTALLES (Eds.), *The future of ICSID and the place of investment treaties in international law*, BIICL 2013, 203 ff., at 207, who suggests the introduction of a sort of a preliminary ruling mechanism within the arbitration proceedings in order to assure greater uniformity in ICSID case law.

16. Among the ICSID decisions and awards cf. *SAIPEM, S.p.A. v. the People's Republic of Bangladesh*, Decision on jurisdiction and recommendation on provisional measures of 21 March 2007, para. 67; *Burlington Resources Inc. v. Republic of Ecuador*, Decision on

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Jurisdiction of 2 June 2010, paras. 99-101, espec.100, where “*The majority believes that, subject to compelling contrary grounds, it has a duty to adopt solutions established in a series of consistent cases... [and] it has 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 the certainty of the rule of law*”. And the minority arbitrator considered “*her duty to decide each case on its own merits, independently of any apparent jurisprudential trend*”.

In the ICSID case *Ambiente Ufficio S.p.A. and Others v. Argentina*, Decision on Jurisdiction and Admissibility of 8 February 2013, the Tribunal took a general preliminary position on this issue at paras. 12-13, and making special reference to the decision of its “sister Tribunal” in the *Abaclat and Others v. the Argentine Republic* case, Decision on Jurisdiction and Admissibility of 4 August 2011, stated: “*Far from adhering to any doctrine of stare decisis or considering itself legally bound by the findings of the Abaclat Tribunal, this implies a process of critically engaging with the majority decision, but also with the counter-arguments contained in the Dissenting Opinion of Professor Abi-Saab.*” The Tribunal however “*emphasize[s] ... that it is well aware that it is called upon to decide the case submitted to it by the Parties on its own needs and merits. The reasoning of the Abaclat Decision can thus be of relevance to that of the present Tribunal only if and to the extent that the Parties in the present case have submitted arguments similar to, and compatible with, those marshaled in the Abaclat case.*” On this specific point and on other points of the majority decision, cf. the Dissenting Opinion of Arbitrator Torres Bernardes dated 2 May 2013.

17. **Concluding on this related point** it seems appropriate to suggest the adoption of a prudent and careful attitude in drawing consequences from what seems to be a consolidated trend in previous case law. This is suggested in order to properly consider the peculiar features of each case and the proper interpretation and application of the relevant legal rules, both international and/or domestic.

18. Special attention has been often reserved to the FET (Fair and Equitable Treaty) and the FPS (Full Protection and Security) clauses contained in BITs and their relationship with the minimum standard required by customary international law as to the treatment of foreigners.

In this respect some cases are worth mentioning: in *Waste Management II v. United Mexican States*, Award of 30 April 2004, (para. 98), the

Tribunal had noted that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is “*arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety*”. However the standard is to be considered to some extent “*flexible*”.

In the ICSID case *Inmaris Perestroika Sailing Maritime Services GmbH and Others v. Ukraine*, Award of 1 March 2012, the Tribunal stated at para. 265 that in the BIT whenever the parties have not limited the FET to the standard required by customary international law, it is not necessary to establish that the government’s actions were in breach of customary international law in order to establish a breach of FET “[a] *government act could be unfair or inequitable if it is in breach of specific commitments, if it is undertaken for political reasons or other improper motives, if the investor is not treated in an objective, even-handed, unbiased, and transparent way, or for other reasons*”.

Having regard to Article 10.5 of the CAFTA-DR Agreement, the Tribunal in *Railroad Development Corporation (RDC) v. Republic of Guatemala*, Award of 29 June 2012, confirmed at para. 218 what has been previously affirmed in the ICSID Case (NAFTA), *ADF Group Inc. v. United States*, Award of 9 January 2003, namely that customary international law is not a static picture of the minimum standard of treatment of aliens and that “*both customary international law and the minimum standard of treatment of aliens it incorporates, are constantly in a process of development*”. The general conclusion reached in the last case, appears deserving full approval.

3. Interstate BIT arbitrations and interpretations by interstate organs.

19. In matter of BITs interpretation an interesting point is that of establishing whether interstate arbitration concerning BITs, or interpretations given by interstate organs, constitute relevant precedent for investor-State arbitration.

In favour of a positive answer to both questions, it can be considered that the interpretations and solutions offered by the interstate tribunals created according to bilateral (BIT) or multilateral treaties (NAFTA and CAFTA-DR) are binding for the States concerned and constitute the agreed law they are called to respect and implement. Therefore, a subsequent investor-State arbitral tribunal should consider the interpretations and solutions provided by the inter-State arbitral tribunal as an expression of the mutual agreement of the Contracting Parties on the relevant issues.

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The same positive conclusion is obviously to be reached in the cases the treaties themselves declare that the inter-State interpretations are to be respected and implemented by the investor-State arbitral tribunals.

20. As to interstate arbitration on the basis of BITs, the following cases can be mentioned.

In the case *République d'Italie c. République de Cuba*, Preliminary Award of 15 March 2005 and Final Award of 15 January 2008, the Tribunal decided a dispute between the two States relating to the application and interpretation of the 1993 BIT in force between them. Cf. TONINI, *La definizione di investimento nell'arbitrato tra Italia e Cuba*, *Rivista di Diritto Internazionale*, 2008, 1046 and POTESÀ, *Am. Jour. IL*, 2012, 341. Obviously, the Tribunal had to deal with various questions, such as the definition of investment and investor, the exhaustion of local remedies, the nationality of corporations, which are capable to be taken into account also by investor-State tribunals possibly applying the same BIT. According to POTESÀ, the only precedent of this kind of inter-State dispute is represented by the dispute started by Peru against Chile pursuant to the BIT in force between the two States and aimed at obtaining the suspension of investor-State proceedings in the ICSID case *Lucchetti v. Peru*, Award of 7 February 2005. The request for suspension was denied and the inter-State arbitration was discontinued.

As to the recent case *Ecuador v. United States of America* (PCA Case no. 2012-05) the Arbitral Tribunal issued its decision on 29 September 2012 (not public). It appears worth noting that such decision was deliberated and issued shortly before the ICSID Award of 5 October 2012 in the case *Occidental Petroleum Corporation v. The Republic of Ecuador*.

21. It is well-known that NAFTA provides for a special mechanism for authoritative interpretation of the Annexes to the Agreement. The 1994 Agreement, at Article 1132, states that where a disputing State asserts that a measure is within the scope of the exceptions or reservations set out in the Annexes, it may request the interpretation of the Free Trade Commission provided by the same NAFTA, and composed by governmental representatives. The Commission interpretation shall be binding on the arbitral tribunal, deciding the investor-State dispute.

22. An identical mechanism for interpretation, also with binding force for the investor-State tribunal, is adopted by the CAFTA-DR of 2004, at article 10.23. Recently, the US Model BIT of 2012, Article 31, provides that at the request of the respondent State in an investor-State dispute, the tribunal itself shall request an interpretation to the States parties to the

BIT, and that the joint decision of the parties' representatives designated for this purpose shall be binding on the tribunal.

For the first NAFTA Free Trade Commission Note of Interpretation of 31 July 2001 concerning the FET and FPS standards, and concluding that they “do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens”, cf. also below Report, Part II, M.

C. Are BITs *lex specialis* in respect to general customary law?

23. This problem is obviously linked with the general issue of the s.c. ‘Fragmentation’ of international law.

On the general issue cf. the Report of the Study Group of the ILC on Fragmentation of International Law, UN Doc A/CN.4/L.702 of 18 July 2006; CONFORTI, *Unité et fragmentation du droit international: glissez mortels, n'appuyez pas*, RGDIP, 2007/1, 5; TREVES, *Fragmentation of international law, the judicial perspective*, CS 2007, 821; MCLACHLAN, *The Principle of Systemic Integration and Article 31 (3)(c) of the Vienna Convention*, ICLQ, 2005, 279-320, for an appropriate reference to “any relevant rules of international law applicable in the relations between the parties” in the process of interpreting treaties, and at 296 ff. analysing the NAFTA case *Pope & Talbot v. Canada* (Award in Respect of Damages of 31 May 2002); SAVARESE, *La nozione di giurisdizione nel sistema ICSID*, Naples 2012, 185 ff. basically supporting this latter view, with additional arguments and details.

As to a particular issue of BITs interpretation cf. ARSANJANI, REISMAN, *Interpreting treaties for the benefit of third parties: the “Salvors’ doctrine” and the use of the legislative history in investment treaties*, in AJIL 2010, 597 ff..

24. As to ICISD cases, they can be distinguished between those adopting a sort of subjective approach and those favouring a sort of objective approach.

The subjective approach emphasizes the decisive importance of the agreement of the parties represented by the BITs themselves which are considered *lex specialis*, as it was decided in the *Fraport AG v. Philippines* (Award of 16 August 2007).

25. According to the objective approach the requirements of art. 25 of the Washington Convention relating to investments and investors have to be carefully respected in order to decide on the jurisdiction of the Centre and the competence of the ICSID tribunals, so giving pre-eminence to an objective interpretation of these requirements. The cases that can be mentioned along this line are, after the initial *Fedax v. Venezuela*

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(Decision on Objections to Jurisdiction of 11 July 1997), *Salini v. Morocco* (Decision on Jurisdiction of 23 July 2001), *Joy Mining v. Egypt* (Award on Jurisdiction of 6 August 2004), *Patrick Mitchell v. DRC* (annulment decision of 1 November 2006), *Malaysian Historical Salvors v. Malaysia* (Award on Jurisdiction of 17 May 2007). It is worth mentioning that the latter decision was subsequently annulled by an *Ad Hoc* Committee (decision of 16 April 2009) which found, by majority, that the Tribunal manifestly exceeded its powers denying jurisdiction for absence in the investment at issue of the requirement relating to the contribution of the investment to the development of the host State. To majority decision a sharp dissent was joined by the minority Member of the *Ad Hoc* Committee, Judge Shahabuddeen.

26. It appears worth adding that in three cases, *LESI-Dipenta v. Algeria*, Award of 10 January 2005, *Victor Pey Casado v. Chile*, decision of 8 May 2008, *Saba Fakes v. Turkey*, decision of 14 July 2010, also an objective approach has been adopted by ICSID Tribunals, but restricting to four the necessary requirements of investments in order to comply with article 25 of the Washington Convention and eliminating the requirement of the contribution of the investment to the development of the host State. For a comment of these cases and a proposal for a third ('appropriate') notion of investment, cf. SAVARESE, *La nozione di giurisdizione*, above para. 23, at 69 and 75 ff..

As to NAFTA cf. PUIG, KINNEAR, *NAFTA Chapter Eleven at Fifteen: Contributions to a Systemic approach in investment arbitration*, ICSID Review, 2010, 225, at 253 ff.

27. A related problem is whether the alleged autonomy and speciality of BITs' law would be maintained also in the presence of peremptory rules of international law (for instance, the procedural rule of due process, namely the equality of arms, and the substantive rules protecting the environment, human health and fundamental human rights in general, and the States' basic sovereign rights).

For basic reference on this item, cf. DUPUY, PETERSMANN, FRANCONI (Eds.), *Human Rights in International Investment Law and Arbitration*, CUP, 2009.

According to your Rapporteur, leaving aside some difficulties in precisely defining certain rules of *jus cogens*, the conclusion appears unavoidable that peremptory rules of international law should prevail and/or have precedence over both conventional and customary rules, in the matter of protection of foreign investments.

D. The Parties' consent and the prerequisites of the selected arbitration mechanism

1. The principle of consent

28. Parties' consent is the basis of arbitration, and also of international investment arbitration. Reference has already been made to the characteristic manner according to which the consent of the State has been constructed in international arbitration based on bilateral or multilateral treaty. The consent of State in such treaties has been constructed as directly covering a series of future disputes (cf. Report, Introduction, para. 2). The consent to arbitration is however twofold. On one side it has to comply with the requirements and restriction indicated in the instrument (in particular BITs) according to which it is considered and expressed. On the other side the consent has to comply also with the requirements and restriction proper to the selected arbitration mechanism; otherwise the consent would be inoperative in this respect and in capable of founding the competence of the tribunal.

As it is well known a typical BIT can express the consent of the State to various forms of mechanisms for dispute resolution or arbitration. It is obviously that each mechanisms proposed has its own characteristics and advantages. The major qualities and differences of the various mechanisms habitually indicated (ICSID, ICSID Additional Facility, Arbitration according to the UNCITRAL rules, the rules of the International Chamber of Commerce and the rules of the Stockholm Chamber of Commerce) are known and are clearly mentioned and analysed by BERNARDINI, *ICSID versus Non-ICSID Investment Treaty Arbitration*, Liber Amicorum Bernardo Cremades, 2010, 159.

29. The difference among the proposed arbitration mechanism are relevant. This is particularly so between ICSID and the other mechanisms including the ICSID Additional Facility.

For the purpose of this Report it appears necessary to emphasize the peculiarities of the ICSID system as to the prerequisites relating to the notion of the investment and that of the investor, and to the applicable law according to article 42 of the Washington Convention.

In addition mention has to be made to the *res iudicata* effects of the awards, in respect to the respondent State and to all other States parties to the ICSID mechanism, according to Articles 53 and 54 of the Convention and the decision on a challenge for nullity of the awards exclusively reserved to the *Ad Hoc* Committees, according to Article 52 of the Convention. The latter element appears essential for affirming the international character of the ICSID awards in respect to all different

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awards there are issued in arbitrations having each their own seat and been subject to possible challenge in such seat with the connected advantages and disadvantages.

2. Qualifications and limitations in the NAFTA and the Energy Charter Treaty

30. Having recalled above the impact of the s.c. 'arbitration without privity' on the present structure of investment arbitration, it seems appropriate to mention the slight, but significant, formal modification incurred by the mechanism of the s.c. 'unilateral' arbitration in the NAFTA and in the Energy Charter Treaty.

Pursuant to Article 1121 of NAFTA and Article 26 of the Energy Charter Treaty - and unlike the ICSID practice based on BITs - it is required that the private party manifest his consent to the form of arbitration chosen in an express statement.

31. In NAFTA, under the provision of Article 1119, the investor's intention to start arbitration proceedings against the host State must be notified to the State at least 90 days before the request for arbitration is submitted, with the indication of the essential elements of the request, and in particular the facts, the NAFTA provisions that the investor alleges to have been breached and the amount of compensation requested. Then a prerequisite for the presentation of the request for arbitration is that the investor signs a waiver of his right to resort to the administrative or civil courts of a Member State, or to other arbitral dispute resolution mechanisms. The consent to arbitration under NAFTA and the renunciation to any other possible dispute resolution means must be made in writing and filed together with the request for arbitration. This provides for an important remedy to those difficulties and conflicts that frequently arise in case of competition between the dispute resolution mechanisms provided for by NAFTA and those which may be different and which are provided for under investment contracts, in domestic laws.

32. In the Energy Charter Treaty, arbitration is regulated within Article 26. What needs to be underlined here with respect to the so-called arbitration without privity, is that the general principle is that by signing the Treaty, each Contracting Party gives his unconditional consent to arbitration or conciliation as provided for in Article 26. However, there is the exclusion of the Contracting Parties listed in Annex ID⁸ who do not

⁸ The Contracting Parties who do not allow an investor, in the two cases mentioned in the text, to opt for international arbitration as set forth in article 26 of the Treaty are quite

give their unconditional consent where the investor has previously submitted the dispute to the mechanisms referred to in letters (a) or (b). In addition, the Contracting Parties listed in Annex IA⁹ do not give their consent with regards to disputes whose object is the application of the last sentence of Article 10.1 which stipulates the commitment to comply with the obligations contractually undertaken with the investor (the so-called umbrella clause)¹⁰. Even the Energy Charter Treaty raises therefore some reasonable explanation and limitations of the investor's rights regarding the starting of arbitration proceedings, as these appear to be definitely consecrated by the so-called Arbitration Without Privity practice.

E. The prior recourse to local courts and subsequent waiting periods

33. In the case *Impregilo v. Argentina*, Award of 21 June 2011, para. 91, the Tribunal observed that Article 8(3) of the Argentina-Italia BIT provides a “mandatory – but limited in time – jurisdictional requirement” and recalled the *Maffezini* and *Wintershall* cases, where it was found, in

numerous, 24. Among them, the European Community and some of its Member States, like Italy. It should be noted in this regard that the declaration was also done by some States that have not yet completed the ratification proceedings concerning the Treaty, and by Canada and the United States, which did not even subscribe the Treaty. On this particular reservation to the Treaty, cf. VANDEVELDE, *Arbitration Provisions in the BITs and the Energy Charter Treaty*, WALDE (Ed.), *The Energy Charter Treaty*, London, The Hague, Boston 1996, 409 ff., at 415 ff., who observes that the reservation allows the States to avoid that a decision by its own tribunals could afterwards be overturned or overhauled by a subsequent International arbitral award, but at the same time this reservation will discourage investors to choose the local courts of the host State. Cf. also: CREMADES, *Arbitration Under the ECT and Other Investment Protection Treaties: Parallel Arbitration Tribunals and Awards*, RIBEIRO (Ed.) *Investment Arbitration and the Energy Charter Treaty*, 2006, 304 ff.; ENERGY CHARTER SECRETARIAT, *The Energy Charter Treaty and Related Documents*, The Hague, 2004..

⁹ The Contracting Parties are Australia, Canada, Norway and Hungary.

¹⁰ Article 10.1 of the Treaty raises consequently the issue to determine what the investors' contractual rights are which, if violated, amount to a violation to a Treaty. Indeed, not all the various contractual obligations that States assume towards foreign investors can have such an importance without it to be expressly stated in the Treaty. It has been correctly stated by HAPP, *Dispute Settlement Under the Energy Charter Treaty*, German YIL, 2002, 331 ff., at 345 ff., that the systematic interpretation of article 10.1 in the light of the Energy Charter Treaty as a whole, brings to the conclusion that the contracts which are in principle protected by the Treaty are solely those that directly relate to the investments and that list the conditions of such investments (the so-called “investment agreements” or “State contracts”) and that the breach of an obligation by the State, in order to be considered a violation of the Treaty, should not be a mere contractual breach, but it should be the consequence of the exercise by the State of its own governing power or, in any case, the exercise of public authority.

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respect to a very similar clause in the Argentina-Germany BIT, that the relevant provision containing a time-bound prior recourse to local courts clause “*mandates (not merely permits) litigation by the investor (for a definite period) in the domestic forum, before the right to ICSID can even materialize*”.

34. Cf. the ICSID case *Ambiente Ufficio* (above para. 16), having regard to Article 8 (3) of the Argentina-Italia BIT, quoting and distinguishing the decision in the *Abaclat* case (cf. above para. 16). The provision containing reference to the 18-month period as precondition for arbitration was examined in some other recent cases having Argentina as Respondent: *ICS Inspection And Control Services Limited v. Argentina*, PCA, Award on Jurisdiction of 10 February 2012; *Daimler Financial Services v. Argentina*, Award of 22 August 2012, and *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. Argentina*, Decision on Jurisdiction of 21 December 2012. In all these cases the Arbitral Tribunals considered that the 18-month requirement is a treaty-based pre-condition to the State’s consent for arbitration. In the *ICS Inspection* case, the Tribunal observed that it could not “*create exceptions to treaty rules*” even upon considering that the judicial litigation would have been “*futile or inefficient*” (paras. 263 ff., esp. 267). The above solutions, considering the time limitation as procedural requirements affecting the jurisdiction of the Centre and the competence of the Tribunal, **are shared by the Rapporteur and have been approved by the Participants to the Rome Meeting of the Committee.**

F. The interaction between international and domestic law in assessing certain arbitration prerequisites

1. The recourse to municipal law necessary to verify in concreto the existence of the investment and the nationality of the investor

35. As to the first issue the Rapporteur refers to the ICSID cases *Fedax v. Venezuela*, Award of 9 March 1998, para. 30 and *Salini v. Morocco* (cf. above para. 25), paras. 36 ff. Cf. also *Compania de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentina*, Award, 20 August 2007. As to legal doctrine, and also for previous reference, cf. recently SASSON, *Substantive Law in Investment Treaty Arbitration. The Unsettled Relationship between International and Municipal Law*, Wolters, Kluwer 2012.

2. As to the nationality

36. The Rapporteur makes here special reference to the following cases: *Soufraki v. United Arab Emirates*, Award of 7 July 2004, where the Tribunal applied Italian law and considered that Italian nationality was not proved by the investor, and *Renta 4 et al. v. Russian Federation*, Award on Preliminary Objections of 20 March 2009, where the Tribunal applied Spanish law and denied the status of investor according to Spain-Russian Federation BIT to certain claimants not possessing full legal personality, according to Spanish law.

3. As to legality of the investment

37. It seems important to mention that, in offering a definition of protected investments, various BITs include the addition that the investor's assets have to be invested "in accordance with the laws and regulations of the [hosting Party]" (cf. Article 1 of the Israeli- Czech Republic BIT), or "are accepted in accordance with the respective laws and regulations of either Contracting State"(cf. Article 1.1 of the Germany-Philippines BIT).

Cf. DOLZER, SCHREUER, *Principles of international investment law*, New York, 2008, 80 ff.; CARLEVARIS, *The conformity of investments with the law of the host State and the jurisdiction of international tribunals*, JWIT, 2008, 48; SACERDOTI, *Corruption in investment transactions*, ICSID Review, 2009, 565; DE LUCA, *La nozione di investimento illegale nella prassi arbitrale: il caso della corruzione*, Rivista dell'Arbitrato, 2013, 249.

Among the various relevant ICSID cases which confirm and develop this general conclusion, cf.: *Inceysa Vallisoletana v. El Salvador*, Award of 2 August 2006; *World Duty Free v. Kenya*, Award of 4 October 2006; *Fraport AG Frankfurt Airport Services Worldwide v. Philippines* (cf. above para. 24); *Phoenix Action Ltd v. Czech Republic*, Award of 15 April 2009 (the latter elaborating and applying the notion of *bona fide* investment); *Mr. Saba Fakes v. Republic of Turkey* (cf. above para. 26), opposing the latter notion. Other Tribunals in recent cases involving Argentina as Respondent State addressed the issue: *Teinver* (cf. above para. 34) and *SAUR International SA*, Decision on Jurisdiction and Liability of 6 June 2012. In the *Teinver* case, the Tribunal stated that the legality of the investment is to be evaluated at the time the investment is made and according to the law of the Host State. In the *SAUR* case the legality principle was affirmed by the Tribunal as a necessary requirement, even if it is not expressed by a treaty: "[I]a condition de ne pas commettre de violation grave de l'ordre juridique est une condition tacite, propre à tout APRI, car en tout état de cause, il est

incompréhensible qu'un Etat offre le bénéfice de la protection par un arbitrage d'investissement si l'investisseur, pour obtenir cette protection, a agi à l'encontre du droit" (para. 308).

G. New actors and problems in investment arbitration

1. Transparency, amicus curiae, intervention of third parties, joinder of proceedings

38. As to transparency, general reference has to be made to the findings and suggestions of the UNCITRAL Working Group II (Arbitration and Conciliation), Settlement of commercial disputes: Preparation of a legal standard on transparency in treaty-based investor-State arbitration, February 2013 (at <http://daccess-dds-ny.un.org/doc/UNDOC/LTD/V12/577/83/PDF/V1257783.pdf?OpenElement>).

It is obviously well known that the 2006 reform of Articles 32 and 37 of the ICSID Convention admitted the participation of third parties as *amicus curiae*.

For some precedents relating to the WTO Appellate Body, NAFTA, the Iran-US Tribunal and the European Court of Human Rights cf. BISHOP, CRAWFORD, REISMAN, *Foreign Investment Disputes*, 2005, 1504 ff.; the importance of third party participation and transparency are emphasized by STERN, *L'entrée de la société civile dans l'arbitrage entre Etat et investisseur*, *Revue de l'Arbitrage* 2002, 329 ff.; ALEXANDROV, CARLSON, *The opportunity to be heard: accommodating amicus curiae participation in investment treaty arbitration*, in Liber Amicorum Bernardo Cremades, 2010; CRIVELLARO, *Transparence de la procédure et l'accès des tiers*, in HORCHANI (ed.), *CIRDI, 45ans après, Bilan d'un système*, Paris 2011, 225 ff. As example of an intervention as "non-disputing party" in an ICSID proceeding, the intervention of the European Commission can be mentioned in the case *Electrabel S.A. v. The Republic of Hungary*, Decision on Jurisdiction, Applicable Law and Liability of 30 November 2012, on which cf. under e) below.

2. The nature of collective mass (or class) arbitration. Problems of due process. Does the consent to arbitrate contained in a BIT cover also atypical arbitral proceedings such as mass (or class) arbitration?

39. Reference is made here to recent and discussed ICSID decisions in the cases *Abaclat and Others v. the Argentine Republic* (cf. above para. 16), spec. Part III, C and D of the majority decision and the dissenting opinion by

Arbitrator *Abi-Saab*, spec. Part IV, and *Ambiente Ufficio v. the Argentine Republic* (cf. above para. 16), spec. Parts I, B and II, B of the majority decision and the dissenting opinion of Arbitrator Torres Bernades.

Cf. PARK, *La jurisprudence américaine en matière de «class arbitration»: entre débat politique et technique juridique*, *Revue de l'Arbitrage* 2012, n. 3, 1-32. The A. starting from the analysis of two decisions of the U.S. Supreme Court in the case *Stolt-Nielsen* of 27 April 2010 and *AT & T. Mobility* of 27 April 2011, presents a general and comparative analysis, including investment arbitration, and declares his preference for the expression “class arbitration” in the examined cases, reserving the expression “mass arbitration” to more extraordinary procedures such as those brought before the Claims Resolution Tribunal to the *Dormant Accounts* in Swiss banks.

The Participants in the Rome Meeting of the Committee share the view that investment arbitration has not been shaped for mass-claims under ICSID (reference is made to the *Abaclat* case). Therefore new procedures and rules should be elaborated. A possibility is to provide for a regulation to be developed under the PCA (which is a better forum rather than ICSID) or a new body to be created by IMF.

3. The impact of Third Party Founding on investment arbitration

40. Reference is here made to: PINSOLLE, *Le financement de l'arbitrage par les tiers*, *Revue de l'Arbitrage* 2011, 385; VAN BOOM, *Third Party Financing in International Investment Arbitration*, Erasmus School of Law, Rotterdam 2011; DE BRABANDERE, LEPELTAK, *Third Party Founding in International Investment Arbitration*, Grotius Centre Working Paper n. 2012/1, Leiden University; BENCH NIEUWVELD, SHANNON (eds.), *Third Party Founding in International Arbitration*, Wolters Kluwer 2012. It is worth noting that the UNCTAD IIA Issues Note no. 1 May 2013 at 25 states that the issues raised by TPF “need to be monitored closely with a view better to understand trends and their policy implications”.

The Participants in the Rome Meeting of the Committee expressed the view that this issue has implications on professional ethics and honesty of parties. They also expressed a general discontent on the occurrence of third party-founding and the agreement on the fact that transparency should have an impact on this as parties could be invited (not obliged) to disclose that costs are covered by a third party.

4. The Counterclaims in investors-State arbitration

41. As to ICSID Arbitration it is to be recalled that Article 46 of the Washington Convention provides that: “*Except as the parties otherwise agree, the Tribunal shall, if requested by a party, determine any incidental or additional claims or counterclaims arising directly out of the subject-matter of the dispute provided that they are within the scope of the consent of the parties and are otherwise within the jurisdiction of the Centre*” (emphasis added). On the interpretation of this clause, cf. SCHREUER, *The ICSID Convention*, 2nd ed. Cambridge U. Press, 2009, 733 ff. at points 18 ff., considering counterclaims by host States against investors as, in principle, admissible.

In the ICSID case *Roussalis v. Romania*, Award of 7 December 2011, the Tribunal, by majority, decided that the relevant BIT could not base the jurisdiction of the Centre on the State counterclaim, because the BIT Contracting States consented explicitly to investor-State arbitration only in respect to the disputes concerning the obligations of the State parties towards investors, not mentioning and thus excluding the disputes relating to the different obligations of the investors towards the States. Arbitrator Reismann, in a dissenting declaration, invoked in favour of the admissibility of the counterclaim reasons of efficiency and general coherence of the system, especially in order to avoid duplications with national litigations at the initiative of the host States.

In the ICSID case *Sergei Paushok, Cjsc Golden East Company, Cjsc Vostokneftegaz Company v. Mongolia*, Award on Jurisdiction and Liability of 28 April 2011, the Tribunal declined jurisdiction on the counterclaims because such counterclaims lacked a close connection with the principal claim.

The Participants in the Rome Meeting of the Committee agreed that in investment arbitration it is the investor - who has no obligations under the treaty – who starts the procedure against the State. Still it is possible to envisage that the State can submit a counterclaim against the investor, based on the fact that the latter failed to comply with some obligations of public international law, like the obligation to act in good faith, or avoid corruption, or minimize the costs of an investment in bad shape, or not to present himself in a false manner. Therefore counterclaims are not in principle excluded (cf. *Roussalis v. Romania* case), and they have to rely on the breach of a compulsory obligation. Such counterclaims should be encompassed in the jurisdiction of the tribunal, within the scope of the consent of the parties.

5. The issue whether the ICSID annulment mechanism needs some modifications and / or improvements

42. The Report makes here reference to the case law and the related comments presented above B 2. and particularly to SCHREUER, *Why still ICSID?*, cf. above para. 15, suggesting the introduction of a bank guarantee mechanism to assure the payment of the award in case the annulment claim is rejected by the *Ad Hoc* Committee.

The Participants in the Rome Meeting of the Committee found that the annulment is experiencing a crisis as it seems that it has been transformed in a sort of appellate jurisdiction.

Your Rapporteur shares the conclusion that *Ad Hoc* Committees should refrain to act as appellate courts, but expresses his preference for the maintenance of the present mechanism which has permitted necessary evolution of international investment law and procedures.

6. The EU framework and the notion of public interest. The possible outcomes to a conflict between BITs and EU law and policy

43. On the problem of compatibility with EU law for BITs concluded between Member States and third countries cf. the two parallel cases brought by the Commission of European Communities, one against Austria (Case C-205/06) and the other against (Sweden) (Case C-249/06), which led to two parallel decisions of the EU Court of Justice of 3 March 2009, condemning the two States for not having eliminated the incompatibilities of their BITs with third countries and EU law. This pattern was followed by the Court of Justice in a judgement of 20 April 2010 in a third case (Case C-246/07) involving Sweden.

44. In the *Eastern Sugar v. Czech Republic* Partial Award of 27 March 2007, decided according to the Arbitration Rules of the Stockholm Chamber of Commerce, the investor maintained that the Czech Republic had breached its rights under the 1991 BIT between the Czech Republic and the Netherlands, because of an alleged discriminatory application of the EU agricultural policy to the company.

The Czech Republic asserted that the Tribunal lacked jurisdiction because the BIT was terminated in 1991 due to the Republic having joined the European Union.

The Tribunal found that the dispute had arisen before the Czech Republic was admitted to the European Union, and therefore the arbitral clause continued to be valid and effective. Consequently the Tribunal declared it

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had jurisdiction and continued the proceedings as to the merits of the dispute.

A second arbitral award worth to be mentioned here is the one issued on 26 October 2010, Award on Jurisdiction, in the *Eureko v. Slovak Republic* case, in a proceeding conducted according to UNCITRAL rules on the basis of the 1991 BIT concluded between the Netherlands and the Czech Republic.

The Tribunal, considering that it had been constituted according to a provision contained in a BIT, concluded that “*Far from being precluded from considering and applying EU law the Tribunal is bound to apply it to the extent that it is part of the applicable law(s), whether under BIT Article 8, German law or otherwise*” (para. 281) and that “*The fact that, at the merits stage, the Tribunal might have to consider and apply provisions of EU law does not deprive the Tribunal of jurisdiction*” (para. 283).

In the ICSID case *Electrabel S.A. v. Republic of Hungary* (cf. above para. 38), the Tribunal affirmed its jurisdiction and rejected the submission by the European Commission, acting as a non-disputing party, according to which the Tribunal should have declined jurisdiction, because the case related to an intra-EU dispute governed by EU law.

As to the impact of the European Union on the development of international investment law, it is worth noting that recent EU legislation, draft legislation, political statements appear to announce an action by the new European actor capable of important contributions. Recently (May 2013) the European Commission (exercising the exclusive competence in matter of direct investments conferred on it by the Lisbon Treaty of 2009) asked the EU Member States to agree to it opening negotiation with China in order to conclude the first EU-wide BIT with a third country.

45. Conclusively, a quite interesting comparison may be proposed between the treaty based investment arbitration and a new form of arbitration which appears to emerge in the recent EU practice concerning competition, particularly in the field of merger control.

Actually the practice of the EU Commission shows numerous decisions in antitrust proceedings on the basis of the EC Regulation n.1/2008 imposing commitments to merging enterprises and providing arbitration as a means for the settlement of disputes between the enterprise obliged by the commitments and any third party claiming damages for the infringement of such commitments. The resulting arbitration is a sort of arbitration without privity similar to the more typical treaty-based

investment arbitration. Recently, an ICC Arbitral Tribunal, in the case *RTI v. Sky Italia*, Award of 17 February 2012, dealt with a dispute of this kind, affirming its jurisdiction/competence and the admissibility of a claim for damages filed by a third party against the enterprise addressee of the EU decision imposing commitments to the latter, considering that the arbitration agreement consisted, for the merger enterprise, in the provision for arbitration contained in the clause of the EU decision and for the third party alleging damages, in the filing of the request for arbitration. Cf. on the matter: CARBONE, *Antitrust Commitments and Arbitration in European Law*, *Rivista dell'Arbitrato*, 2013, 1; RADICATI DI BROZOLO, *EU Merger Control Commitments and Arbitration: Reti Televisive Italiane v. Sky Italia*, *Arb. Int.*, 2013, 223 ff.. For abstracts of the ICC Award cf. *Rivista dell'Arbitrato*, 2013, 201, note RADICATI DI BROZOLO.

Part II The Selected Relevant Issues

A. The notion of investment

1. In the BITs

46. The reasons for the extraordinary success of the BITs from the late 50's till today appear to be mainly due to the lack of certainty as to the content of the international customary rules caused by the emerging of new principles of International Law, such as that of the permanent sovereignty of States over their natural resources and the attempt to codify, by the UN General Assembly in 1974, new general rules concerning the economic rights and duties of States.

As well known the traditional areas covered by BITs are: the definition of the protected investments and investors; the admittance of investments and their treatment with particular reference to the transfer of profits; the regime of expropriations and nationalizations; the settlement of disputes between contracting States and, above all, disputes between private foreign investors and host States. For the purpose of this Presentation, the attention will be focused only on the areas relating to the issues selected for preliminary examination.

47. A broad definition of investment has been generally adopted in the treaty practice. The traditional indication of certain types of investments is not in any case restricted to usual property rights, but also includes other rights and interests. Consequently, the resulting lists of acts and/or activities which constitute investments simply represent examples of investments and do not exclude that other acts and/or activities may qualify as such.

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A classic example of this sort of definition may be the one contained in the UK BITs of the 1990's, which provided that: "*Investment means every kind of assets*" indicating five principal forms of investment, such as "(i) *movable and immovable property and any other related property rights; (ii) shares in, stocks bonds and debentures of, and any other form of participation in a company or business enterprise; (iii) claims to money and claims to performance under a contract; (iv) intellectual property rights, technical processes, and know-how; (v) rights conferred by law or under contract to undertake a commercial activity, including search for, cultivation, extraction or exploitation of natural resources*".

48. In recent practice, definitions have become more precise and expanded. For instance, very detailed *rights* are indicated and protected in the treaties stipulated by the US. In particular, the income produced by the investments themselves is also generally considered to be an investment, provided, however that it is re-invested. Moreover, always in the US BITs, also activities simply connected with the actual investments are protected as well. The 2012 US Model BIT thus provides that "*'investment' means 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*". According to the definition, the investment may take various forms, including "(a) *an enterprise; (b) shares, stock, and other forms of equity participation in an enterprise; (c) bonds, debentures, other debt instruments, and loans; (d) futures, options, and other derivatives; (e) turnkey, construction, management, production, concession, revenue-sharing, and other similar contracts; (f) intellectual property rights; (g) licenses, authorizations, permits, and similar rights conferred pursuant to domestic law*".

Given the non-exhaustive nature of the definitions adopted and their somehow tautological character (FADLALLAH, *La notion d'investissement: vers une restriction à la compétence du CIRDI ?*, *Liber Amicorum R. Briner*, 2005, 259 ff.) problems may arise in order to determine whether a certain activity can be considered an investment protected by a BIT. In this regard various, sometimes contrasting, solutions have been proposed by case law and doctrine. In any case broad and generous definitions largely prevail.

49. The only point of relative consensus seems to be that sales, and probably other purely commercial transactions, are excluded from the definition of investment because the operation can be considered

concluded with the payment of the price. Evidently, the definition is a problem of interpreting the BIT that has to be applied, in compliance with the hermeneutic criteria and principles applicable to all international treaties, which are embodied in the 1969 Vienna Convention on the Law of Treaties and have to be respected. It follows that the treaty's purpose and object will be conclusive, as they can be derived from the text of the treaty as a whole, including the preamble, and from the context in which the treaty has been concluded.

50. Some of the interpretative elements that may be drawn from the preamble of a given BIT seem particularly important for the purposes of contributing to the complete definition of investment adopted in the text of the agreement. In the first place, the parties, by means of a BIT, intend to promote the investment of resources provided by individuals or companies from one State in the territory of another. Secondly, it is apparent that the flow of private capital promoted by BITs contributes to the economic development of the party receiving the investment.

51. In any case, the concept of investment should be determined in each individual and specific case by a precise application of the text of the treaty concerned, taking into account its object and purpose and the context in which it has been concluded. In this connection the analysis of the preambles plays an important role. It should be remembered that all BITs contain definition of investment, and that if the definitions adopted have certainly evolved over time, their scope and precision have progressively improved.

Then the attention will be devoted to what appears to be a new phase of BITs started with the US Model and the Canadian Model, both of 2004. They will be examined and compared with the solution adopted and the results achieved by the mechanisms provided for by NAFTA and the Energy Charter Treaty from the second half of the nineties onwards.

The analysis will be conducted, taking into account relevant doctrine and authorities, such as, for the US Model, SCHWEBEL, *The influence of Bilateral Investment Treaties on Customary International Law*, cf. above para. 10, and *The United States 2004 Model Bilateral Investment Treaty: an Exercise in the Regressive Development of International Law*, *Liber Amicorum* R. Briner, 2005, 815 and, for the Canadian Model, MCILROY, *Canada's new foreign investment protection and promotion agreement. Two steps forward, one step back?*, JWIT, 2004, 621.

2. According to the Washington Convention of 1965

52. The problem of the definition of investment in the BITs becomes more difficult in multilateral conventions, namely the Washington

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Convention of 1965 instituting ICSID. This is especially true in recent years, after the consolidation of the international practice of the *s.c. arbitration without privity* (cf. below).

Moreover, as well known, the 1965 Washington Convention does not contain an explicit definition of investment in its Article 25. However, from the Preamble of the Washington Convention and from the arbitral practice of ICSID Tribunals, general criteria of reference have been deduced and applied. Consequently, these criteria need to be verified and observed in every single case (cf. FADLALLAH, *La notion d'investissement: vers une restriction à la compétence du CIRDI?*, above para. 48; SCHLEMMER, *Investment, Investor, Nationality, and Shareholders*, MUCHLINSKY, ORTINO, SCHREUER (Eds). *The Oxford Handbook of International Investment Law*, 2008, 49 ff.).

53. The criteria generally identified are, according to the *s.c. Salini* test (cf. below): *a*) a certain duration in time of the operation, on the basis of which instantaneous transactions, such as purchases and sales, or other transactions where the dealing is concluded by the payment of a price are normally excluded; *b*) the operator's expectation of profit on and remuneration from the investment; *c*) the risk taken by the investor, which is not the case if the host state itself takes on itself the *alea* of the same investment. This risk ought, moreover, to be distinguished from the mere risk of non-performance of the contract by the other party to the operation; *d*) a certain value of the resources brought in by the investor; *e*) the contribution made by the operation to the economic development of the host state, as indicated by the Preamble to the Washington Convention.

54. As to the issue of the development of the host State as a requirement for the investment, further to the *Salini* case (cf. above para. 25) some awards have stated that the development was not only an essential element of the investment, but the contribution to the economic development of the host State must also be "significant" (*Jan de Nul N.V. and Dredging International N.V. v. Arab Republic of Egypt*, Decision on Jurisdiction, 16 June 2006; *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, Decision on Jurisdiction, 14 November 2005; *L.E.S.I.-DIPENTA v. Algeria*, cf. above para. 26). Later, the *Ad Hoc* Committee in the *Patrick Mitchell v. Democratic Republic of Congo* (cf. above para. 25) also stated that it "*suffices for the operation to contribute in one way or another to the economic development of the host State, and this concept of economic development is, in any event,*

extremely broad but also variable depending on the case”, thus adopting a broader approach, simply requiring some form of contribution to the economy of the host State. The Tribunal in the case *Malaysian Historical Salvors v. Government of Malaysia* (cf. above para. 25) , denied its jurisdiction considering that the Contract was not a “*readily recognizable*” investment, having as object a marine salvage obligation. Therefore the Tribunal concluded that “*the question of contribution to the host State’s economic development assumes significant importance because the other typical hallmarks of ‘investment’ are either not decisive or appear only to be superficially satisfied*” (para. 130). The decision was later annulled on 16 April 2009, by concluding that even if demonstrated that any, or all, of the *Salini* criteria are not satisfied, this would not necessarily be sufficient – in and of itself – to deny jurisdiction.

55. Consequently, purely commercial transactions or those that are of brief duration ought as a rule to be excluded from the ICSID’s concept of investment. It should be noted, however, that in a case that raised considerable interest, *Fedax v. Venezuela* (cf. above para. 35), an ICSID Tribunal, while fully accepting the fundamental, general criteria set out above, qualified a request for payment of bills of exchange issued by Venezuela in connection with a contract for a loan concluded between the parties, which was a typically commercial transaction, as one relating to an investment. The result was achieved by stressing Venezuela’s basic public interest in issuing bills of exchange, in the context of its legislation on public credit, and the close relation between the transaction in question and the economic development of the country.

56. Other ICSID awards are of interest as they have affirmed the existence of an investment according to the Convention in various specific cases. In this regard it is worth mentioning *CSOB v. Slovak Republic*, Decision on Objections to Jurisdiction of 24 May 1999 relating to a loan; *ME Cement v. Egypt*, Award of 12 April 2002 relating to a licence; *Salini v. Morocco* (cf. above para. 25), relating to a contract for civil works; *SGS v. Pakistan*, Decision on Objections to Jurisdiction of 6 August 2003 and *SGS v. Philippines*, Decision on Objections to Jurisdiction of 29 January 2004, both relating to service contracts.

The few cases in which the activity of the private party was not considered an investment under the Convention have been amply debated. Mention is to be made of the awards: *Mihaly v. Sri Lanka*, Award of 15 March 2002 relating to pre-contractual expenses; *Nagel v. Czech Republic*, Final Award of 9 September 2003, relating to certain credits considered to be merely hypothetical by the Tribunal; *Joy Mining v.*

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Egypt (cf. above para. 25), relating to a request for liberation of performance guarantees; *Patrick Mitchell v. Democratic Republic of Congo* (cf. above para. 25), where the activity of a counsel in that specific case was not considered an investment by the *Ad Hoc Committee* (cf. BEN HAMIDA, *La notion d'investissement, notion maudite du système Cirdi?*, *Gazette du Palais*, 14-15 December 2007, 33 ff.; SCHLEMMER, *Investment, Investor, Nationality, and Shareholders*, cf. above para. 52).

57. In particular, there is no reasonable doubt as to the qualification of oil-related activities as an investment, as they are regulated by the relevant contracts with the state and with the competent state entity, both in terms of duration and expected remuneration, with the correlated element of risk and the contribution to the economic development of the host state.

58. In regard to the definition of investment, it seems important to stress that, in the initial application phase of the Washington Convention, the need for a definition of the term investment did not seem essential, when the ICSID's jurisdiction and the competence of the tribunals were based exclusively on an arbitration clause or agreement directly and individually stipulated in the investment contract by the investor and the host State. This definition has now become of considerable importance when ICSID arbitration can be based as follows: on the part of the State, by the adoption of a domestic law or the conclusion of a BIT and, on the investor's part, by the direct submission of a request for arbitration to the Centre. This form of arbitration is commonly called *arbitration without privity* (the expression is PAULSSON'S, *Arbitration Without Privity*, cf. above fn. n. 7; cf. however for some reflections and critical remarks: PRUJINER, *L'arbitrage unilatéral: un coucou dans le nid de l'arbitrage conventionnel*, above fn. n. 7; ALEXANDROV, *The "baby boom" of treaty-based arbitrations and the jurisdiction of ICSID tribunals. Shareholders as investors under investment treaties*, cf. above fn. n. 6). In respect to this form of arbitration it is suggested that an objective and clear definition of investment becomes necessary because of the absence of a direct and specific agreement of the parties offering evidence that the envisaged activity of the foreign citizen or company is considered by them as an investment under the Convention.

59. Thus, the question which arises with an increasing frequency is that of a possible definition of investment contained in an applicable BIT, which is different or broader than that resulting from the general objective criteria derived from the Washington Convention. Since the

BITs constantly refer to ICSID as a mechanism for dispute settlement between states and foreign investors, it is necessary to verify whether ICSID jurisdiction and the competence of the tribunals can be affirmed in all those cases in which the definition of investment given by the applicable BIT does not in fact correspond to that of the Washington Convention. In such cases the conclusion suggested by various authorities seems to be that the clause contained in the BIT and constituting the basis for the recourse to ICSID becomes non effective because of the absence, in the case at issue, of a basic substantive prerequisite of the same ICSID mechanism (cf. BROCHES, *Bilateral investment protection treaties and arbitration of investment disputes*, in SCHULTSZ, VAN DEN BERG (Eds.), *The art of arbitration. Essays on international arbitration. Liber Amicorum Pieter Sanders*, Deventer, 1982, 63 ff.; SCHREUER, *The ICSID convention*, above para. 41; FADLALLAH, *La notion d'investissement: vers une restriction à la compétence du CIRDI?*, cf. above para. 48).

60. It has to be recalled in this respect that the founding fathers and first commentators of the Washington Convention, in the initial context described above, either felt the question of the definition of investment to be of limited interest (DELAUME, *Convention on the settlement of investment disputes between States and nationals of other States*, *International Lawyer*, 1966, 64 ff.) or considered it to be essentially integrated and absorbed with the question of the jurisdiction of the Centre (BROCHES, *The convention on the settlement of investment disputes: some observations on jurisdiction*, *Columbia Journal of Transnational Law*, 5, 1966, 263 ff.). Other commentators simply stressed the parties' wide discretionary powers in this regard (starting from TUPMAN, *Case studies in the jurisdiction of the International Centre for Investment Disputes*, *ICLQ*, 1986, 813).

61. **In conclusion, your Rapporteur shares the view** that the notion of investment according to Washington Convention needs to be strictly complied with especially after the radical evolution of the ICSID system represented by the s.c. 'arbitration without privity' where the consent of the State is expressed *a priori* and only once, with the issuing of a piece of domestic legislation or with concluding a treaty, bilateral or multilateral, providing for international arbitration.

B. The nationality of the Investors

62. All BITs define the essential characteristics of the protected investors, both in case of individuals and in the case of companies and other legal persons.

63. For individuals, the nationality is commonly determined and ascertained in conformity with the law of the state that grants it. Problems

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arise only in particular cases, when the investor has dual of multiple nationalities. If the investor is a national of a third state in addition of being a national of one of the contracting states, then based on the principle of effective nationality established by the International Court of Justice in its decision of 6 April 1955 in the *Nottebohm* case, the prevailing nationality is that of the state with which the investor has the closest link. Should the investor be a national of both states which are parties to the BIT, the solution traditionally accepted with regard to diplomatic protection of nationals is that the investor in question is not considered a foreigner by the host state (GECK, *Diplomatic protection, Encyclopedia of public international law*, vol. X, 1987). The most recent trend emerging from the case-law of the Iran-United States Claims Tribunal from the mid-1980's should however be mentioned, according to which even in this case the criterion of effective nationality has to be applied. This was stated in the decision by the Full Tribunal in the case A/18 of 6 April 1984.

64. In the sector of investments, it should be noted how the 1965 Washington Convention, at Article 25, para. 2, a) follows the traditional orientation of the BITs and excludes the Centre's jurisdiction in the case that the investor with dual nationality is also a national of the host state against whom arbitral proceedings have been initiated. It is to be mentioned in this regard that in the case *Hussein Nuaman Soufraki v. United Arab Emirates* (cf. above para. 36), the jurisdiction of the Centre was denied because the investor could not provide sufficient evidence to be a national of a contracting State. Consequently the tribunal did not consider necessary to rule on the issue of the dominant nationality of the investor (cf. SCHLEMMER, *Investment, Investor, Nationality, and Shareholders*, above para. 52). As to the points in time when the link of nationality has to exist, cf. the dissenting opinion of Orrego Vicuña in the above mentioned case. The issue of the investor nationality has been also decided in the ICSID case *Mr. Tza Yap Shum v. Peru*, Decision on Jurisdiction and Competence of 19 June 2009 affirming, on the basis of the Chinese applicable law, the Chinese nationality of a person born in China and residing in Hong Kong.

65. Differently from the Convention, the United States BIT Models of 2004 and 2012 adopt the criteria of dominant and effective nationality of the individuals even when US nationality competes with that of the other state party to the BIT. According to the definitions contained in Article 1 of the US Model, under the indication "*investor of a Party*" it is specified

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*”.

66. With regard to companies and other legal persons, the starting point for any reconstruction of the topic according to customary international law is obviously the decision of the International Court of Justice in the *Barcelona Traction* case of 5 February 1970, according to which diplomatic protection of companies is a right for the State in which the companies have been incorporated and have their registered office, and not for the State of which the majority of shareholders are nationals, provided, however, that connections with the State in which the companies have been set up are real and not fictitious.

67. In this respect, Article 25, para. 2, b) of the Washington Convention provides that the Centre’s jurisdiction shall extend to legal persons who are nationals of the State hosting the investment, when, “*because of foreign control,*” the parties have agreed they should be treated as nationals of another Contracting State for the purposes of the Convention. This provision led to a considerable volume of case law and numerous comments in legal literature, up to more recent decisions such as the ICSID cases *Tokios Tokelès v. Ukraine*, decided in the matter of jurisdiction on 29 April 2004, (cf. CARLEVARIS, *La competenza dei tribunali arbitrali internazionali, tra violazione dei trattati sugli investimenti e violazione delle obbligazioni contrattuali*, Rivista dell’Arbitrato, 2004, 431 ff.), *El Paso v. Argentina*, Decision on Jurisdiction of 27 April 2006, and *Noble Energy v. Ecuador*, Decision on Jurisdiction of 5 March 2008, on the matter of indirect shareholding. With regard to the protection of the investment of foreign minority shareholders in a local company, cf. the ICSID Decision on Objections to Jurisdiction of 17 July 2003 in *CMS Gas Transmission Company v. Argentina* (cf. the note by ALEXANDROV, *The “baby boom” of treaty-based arbitrations and the jurisdiction of ICSID tribunals. Shareholders as investors under investment treaties*, above fn. n. 6, and in general, ORREGO VICUÑA, *The protection of shareholders under international law: making state responsibility more accessible*, RAGAZZI (edited by) *International responsibility today. Essays in memory of Oscar Schachter*, Leiden, 2005, 161 ff.). Lastly, as to the requirement that the company having initiated the arbitration has to continue to maintain the nationality of a Contracting State, the 26 June 2003 Award in *Loewen v. USA* is to be mentioned (cf. ACCONCI, *The requirement of continuous corporate nationality and customary international rules on foreign investments. The Loewen case*, Italian yearbook of international law, Leiden, 2004).

Moreover the notion of investor has been discussed in relation to entities and corporate bodies not possessing legal personality in the ICSID case *Renta 4 et al. v. Russian Federation* (cf. above para. 36).

68. **In conclusion on this point your Rapporteur suggests** that also the prerequisites *ratione personarum* established by the Washington Convention have to be punctually respected in all cases of ICSID arbitration. This implies that when an arbitration is based on a State's agreement expressed in a BIT which may adopt definitions different from or broader than those contained in the Washington Convention, the ICSID arbitration, possibly chosen by the investor, ought nevertheless to be conducted in full compliance with the criteria for jurisdiction *ratione personarum* as set out in the Convention.

69. The differences between the ICSID mechanism and the other mechanisms alternatively provided for in the BITs, as to the prerequisites *ratione materiae* (the definition of investment) and *ratione personarum* (the definition of protected investors), may contribute to explain the persisting success of also these other forms of arbitration for the settlement of the investment disputes based on BITs. Obviously, also other factors play an important role on the selection of an ICSID or a non-ICSID mechanism. They mainly relate, first, to the impact of ICSID arbitration on the diplomatic protection of investors by their national States, according to Article 27.1 of the Convention, establishing that States shall refrain to exercise their protection in respect to disputes that their nationals have consented to submit or have submitted to ICSID arbitration, unless the other Contracting State has failed to abide by the award rendered in the dispute. Secondly, these factors relate to the real international character of ICSID arbitration and its independence from any national law. For the effects and enforcement of the awards as final judgements of a State court (Article 54) and their possible challenge only before an *Ad Hoc Committee* (Article 52 and 53). In any case also the jurisdictional prerequisites *ratione materiae* and *personarum* mentioned above play surely a precise role in the selection by the investors of the settlement mechanisms (cf. BERNARDINI, *ICSID Versus Non-ICSID Investment Treaty Arbitration*, above para. 28).

C. Treaty Claims and Contract Claims

1. Definition and preliminary observations

70. The umbrella clauses (UC) are commonly defined as provisions whose aim is to ensure that each party to the treaty (possibly a BIT) will

respect specific understandings vis-à-vis nationals of the other party. The inclusion of an UC might have the effect to extend the jurisdiction *ratione materiae* of the arbitral tribunal over contractual claims. Still the extent of subject matter differs depending on the wording of the clauses in the BIT and the interpretation of such clauses.

71. Among the first arbitral tribunals faced with the interpretation of an UC inserted in a BIT was the Tribunal appointed in the ICSID case *SGS Société Générale de Surveillance SA v. Pakistan*, cf. above para. 56 (actually the earliest case of a tribunal faced with a provision like an UC seems to be the Arbitral Tribunal in the ICSID case *Fedax v. Venezuela*, cf. above para. 25). The issue was clearly identified as one of the “core issues” of the case and it was formulated with the question to know whether Article 11 of the Agreement Concerning the Promotion and Reciprocal Protection of Investments (Pakistan/Switzerland) (11 July 1995) RO 1998 2601, entered into force 6 May 1996 (‘Switzerland–Pakistan BIT’), a so-called ‘umbrella clause’, could transform purely contract claims into BIT claims.

Various tribunals were confronted with the issue of the difference between contract-based claims and treaty-based claims. Among others, this matter has been discussed in the ICSID cases *Lauder v. Czech Republic* (Final Award, 3 September 2001); *Genin v. Estonia* (Award, 25 June 2001); *CMS v. Argentina* (cf. above para. 67); *Azurix v. Argentina* (Decision on Jurisdiction, 8 December 2003); the Annulment Committee in *Wena v. Egypt* (5 February 2002); *Salini v. Jordan* (Decision on Jurisdiction, 9 November 2004); *Eureko v. Poland* (Partial Award, 19 August 2005); *Joy Mining v. Egypt* (cf. above para. 25); *Pan Am BP v. Argentina* (Decision on Preliminary Objections, 27 July 2006); *EDF v. Romania* (Award, 8 October 2009); *BIVAC v. Paraguay* (Decision on Objections to Jurisdiction, 29 May 2009); *Lemire v. Ukraine* (Decision on Jurisdiction and Liability, 14 January 2010).

72. More recently, the interpretation of the UC in the Argentina-US BIT was discussed by the Arbitral Tribunal in the ICSID case *PanAmBP v. Argentina* (cf. above para. 71), and the question was formulated as follows: “*The question is whether, through an ‘umbrella clause’, sometimes also called an ‘observance-of-undertakings clause’, in a BIT, contract claims of an investor having a contract either with the State or with an autonomous entity are automatically and ipso jure “transformed” in treaty claims benefiting from the dispute settlement mechanism provided for in the BIT*” (para. 99).

73. There are divergent positions in literature and arbitration practice on the extent of such effect determined by an UC. It has been noted that

“[t]his question has divided practitioners and legal commentators and remains unsettled in the international arbitral case law” (GAILLARD, *Treaty-Based Jurisdiction: Broad Dispute Resolution Clauses*, New York Law Journal, 2005, cited in the ICSID case *PanAmBP v. Argentina*, cf. above para. 71).

2. Origins and diffusion of the UC in the BIT and in international conventions

74. Various types of UC have been included in investment protection treaties since the 1950s, using different language. It has been suggested that the first reference to an UC, also defined “parallel protection” clause, can be traced in the advice rendered in 1953-1954 by Lauterpacht to the Anglo-Iranian Oil Company with respect to the Iranian oil nationalization dispute (cf. SINCLAIR, *The Origins of the Umbrella Clause in the International Law of Investment Protection*, Arbitration International, 2004, 411).

75. Presently, according to YANNACA-SMALL (*Interpretation of the Umbrella Clause in Investment Agreements, OECD Working Papers on International Investment*, 2008) more than 40 % of the BITs in existence contain an UC. However the practice of the States shows that there is no uniform treatment of such clauses in the BITs.

76. With regard to the international treaties, the Energy Charter Treaty provides that (final sentence of Article 10 (1)) “*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*”. It is to be mentioned however that the Energy Charter Treaty allows the contracting parties to opt out of this clause and so maintain the protection of the investor limited to the contract provisions.

3. Different versions of UC

77. The view is generally shared that a universally agreed model of UC does not exist, and many differences may exist as the specific language they contain and to where they are located into the BITs.

a. Differences in the language

78. As commonly understood, the UC was originally designed to guarantee by treaty the terms of a contract entered into by a State and an investor (cf. Lauterpacht’ 1953-54 Advice, above para. 74). Its purpose was hence to offer an alternative protection to the investor, additional to the dispute settlement mechanism already contained in the contract. The

applicability and the broadness and effectiveness of such protection represent the real problem discussed among commentators and arbitrators. The language of many UC is in fact broad and unrestricted, thus becoming often crucial in order to evaluate the effects of those clauses.

Considering model BITs practice, an UC usually has the following language: *“Each Contracting Party shall observe any obligation it may have entered into with regard to investments of nationals or companies of the other Contracting Party”*. This formulation is quite common in European model BIT.

79. Two common elements of the UC can be traced out of the various BITs: (i) the use of mandatory language, modulated on different degrees and (ii) the fact that they refer to obligations undertaken by the States and not to obligations between private individuals.

80. The UC might provide that each contracting party “shall observe” or “shall respect” or “shall guarantee”

In the Swiss Model BIT the language is: *“Each Contracting Party shall observe any obligation it has assumed with regard to ...”*.

The 2008 German Model BIT slightly modified the previous language of the UC. Article 8(2) of the former German model BIT included in a non-derogation article a provision almost identical to the UC found in the majority of European model BITs. Article 8 reads: *“1. If the legislation of either Contracting State or obligations under international law [...] contain a regulation [...] entitling investments by investors of the other Contracting State to a treatment more favourable than is provided for by this Treaty, such regulation shall to the extent that it is more favorable prevail over this Treaty.*

2. Each Contracting State shall observe any other obligation it has assumed with regard to investments in its territory by investors of the other Contracting State”.

Article 7 (2) of the latest 2008 German Model BIT now reads as follows: *“Each Contracting State shall fulfill any other obligations it may have entered into with regard to ...”*.

81. In the former US Model the UC was similar to the Swiss and German models: *“Each Party shall observe any obligation it may have entered with regard to....”*. The same language was in the 1991 US-Argentina BIT, in the 1991 Dutch-Polish BIT Relevant in the *Eureko* case (cf. above para. 71), in the 1998 France-Mexico BIT.

However the clause is no more present in the US Model BIT. No UC can be traced in the Model BIT of France, Canada and Norway. It is to be

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noted that the 2006 French Model BIT (Article 9) provides as follows: “*Investments having formed the subject of a special commitment of one Contracting Party, with respect to the nationals or companies of the other Contracting Party, shall be governed, without prejudice to the provisions of this Agreement, by the terms of the said commitment if the latter includes provisions more favourable than those of this Agreement*”. The 2012 US Model BIT provides under Art. 24 that “*1. In the event that a disputing party considers that an investment dispute cannot be settled by consultation and negotiation: (a) The claimant, on its own behalf, may submit to arbitration under this Section a claim (i) that the respondent has breached [...] (C) An investment agreement*”.

82. Some BITs provide a more ambiguous language, thus leaving room for diverging interpretations. The Swiss-Pakistani BIT, at the basis of the ICSID case *SGS v. Pakistan* (cf. above para 56), reads as follows (Article 11): “*Chacune des Parties Contractantes assure à tout moment le respect des engagements assumés par elle à l’égard des investissements des investisseurs de l’autre Partie Contractante*”.

The UC might refer to “commitments” or “any obligation” or “any other obligation”. In particular the wording “any obligation” has been commented in the case *Eureko BV v. Poland* (cf. above para. 71), where the Ad-Hoc Tribunal affirmed that the expression “*‘Any’ obligations is capacious; it means not only obligations of a certain type, but ‘any’ – that is to say, all – obligations entered into with regard to investments of investors of the other Contracting Party*” (para. 246).

b. Differences in the position of the UC within the BIT

83. In the practice, some tribunals have considered that the location of the UC has a particular significance in relation to the interpretation of the clause.

In the case *SGS Société Générale de Surveillance SA v. Pakistan* (cf. above para 56), the Arbitral Tribunal noted that (paras 169-171): “*Given the above structure and sequence of the rest of the Treaty, we consider that, had Switzerland and Pakistan intended Article 11 to embody a substantive ‘first order’ standard obligation, they would logically have placed Article 11 among the substantive ‘first order’ obligations set out in Articles 3 to 7. The separation of Article 11 from those obligations by the subrogation article and the two dispute settlement provisions (Articles 9 and 10), indicates to our mind that Article 11 was not meant to project a substantive obligation like those set out in Articles 3 to 7, let alone one that could, when read as SGS asks us to read it, supersede and render*

largely redundant the substantive obligations provided for in Articles 3 to 7”.

84. In the *PanAmBP* case (cf. above para. 71), the claimants supported their position, referring to “... *the position of the umbrella clause within the Treaty which, unlike what was the case in the Swiss-Pakistani context, is placed among the ‘first-order standard obligations’.* This proves, according to the Claimants, that it was the intention of the Contracting Parties to convert claims based on mere contractual relations between investors and the host State into treaty claims” (para. 95).

85. On the contrary some tribunals held that the location of the UC has only a limited significance, as in the case *SGS Société Générale de Surveillance SA v. Philippines* (cf. above para. 56). In the *Ad Hoc Arbitration in the case Eureka BV v. Poland* (cf. above para. 71), the Tribunal considered that “*insofar as the placement of the umbrella clause in the BIT – among the substantive obligations or with the final clauses – is of any significance (in this Tribunal’s view, little), it should be noted that Article 3.5 of the BIT between the Netherlands and Poland places its umbrella clause amidst the rendering of the Parties’ substantive obligations*” (para. 259).

4. The interpretation of the UC by the arbitral tribunals: the main lines

Four main lines of interpretation of an UC can be identified.

a. The UC automatically transforms a contractual obligation into an international obligation

86. In *Fedax v. Venezuela* (cf. above para. 35), the Arbitral Tribunal concluded that Venezuela was “*under the obligation to honour precisely the terms and conditions governing such investment, laid down mainly in Article 3 of the Agreement*” (para. 29) on the basis that Article 3 (4) of the BIT between Netherlands and Venezuela provided as follows: “*Each Contracting Party shall observe any obligation it may have entered into with regard to the treatment of investments of nationals of the other Contracting Party*”.

In *Impregilo v. Pakistan* (Decision on Jurisdiction, 22 April 2005), the Tribunal stated that (para. 258): “*the fact that a breach may give rise to a contract claim does not mean that it cannot also – and separately – give rise to a treaty claim. Even if the two perfectly coincide, they remain analytically distinct, and necessarily require different enquiries*”. A similar statement was in the case *Consortium RFCC v. Kingdom of Morocco* (Arbitral Award of 22 December 2003).

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In the case *Lemire v. Ukraine* (cf. above para. 71), the Tribunal agreed in principle with the claimant's assertion, stating that (para. 498): "*Article II.3 (c) of the BIT [“Each party shall observe any obligation it may have entered into with regard to investments”] brings the Settlement Agreement into the ambit of the BIT, so that any violation of the private law agreement becomes ipso iure a violation of the international law BIT*", even if this conclusion did not have any significance for determining the award.

87. SHIHATA, *Applicable Law in International Arbitration: Specific Aspects in Case of the Involvement of State Parties, The World Bank in a Changing World*, vol. II, 1995, 601 ff., observed that the treaties containing an UC "elevate contractual undertakings into international law obligations".

It has been affirmed by SCHREUER, *Travelling the BIT Route: of Waiting Periods, Umbrella Clauses and Forks in the Road*, *Journal of World Investments*, 2004, 231 ff., that the UC "add the compliance with investment contracts, or other undertakings of the host State, to the BIT's substantive standards. In this way, a violation of such a contract becomes a violation of the BIT".

b. The effect of the UC is limited to the State's *iure imperii* acts

88. In the case *PanAm BP v. Argentina* (cf. above para. 71), the Tribunal concluded that (paras. 108-112) "*it is necessary to distinguish the State as a merchant from the State as a sovereign. ... In the Tribunal's view, this umbrella clause does not extend its jurisdiction over any contract claims that the Claimants might present as stemming solely from the breach of a contract between the investor and the Argentina State or an Argentine autonomous entity*".

89. In the case *El Paso Energy v. Argentina* (cf. above para. 67), the Tribunal held that the UC, even if drafted as broadly as possible, can only confer jurisdiction to an arbitral tribunal on the basis of a BIT when the State is acting in its capacity as a sovereign authority.

90. In *Impregilo v. Pakistan* (cf. above para. 86), the Tribunal noted that (para. 260) "*the State or its emanation, may have behaved as an ordinary contracting party having a difference of approach, in fact or in law, with the investor. In order that the alleged breach of contract may constitute a violation of the BIT, it must be the result of behaviour going beyond that which an ordinary contracting party could adopt. Only the State in the exercise of its sovereign authority ('puissance publique'), and not as a*

contracting party, may breach the obligations assumed under the BIT". In conclusion, declining to exercise its jurisdiction over the contract claims presented by the claimant, the Tribunal held that (para. 262) "*the overlap or coincidence of treaty and contract claims does not mean that the exercise of determining each will also be the same*".

c. The UC should be interpreted restrictively

91. In the famous case *SGS v. Pakistan* (cf. above para. 56), according to the complex evaluation made by the Arbitral Tribunal, the UC is to be read in a narrow manner. The Tribunal stated that (paras 162-174) "*On the reading of Article 11 urged by the Claimant, the benefits of the dispute settlement provisions of a contract with a State also a party to a BIT, would flow only to the investor. For that investor could always defeat the State's invocation of the contractually specified forum, and render any mutually agreed procedure of dispute settlement, other than BIT-specified ICSID arbitration, a dead-letter, at the investor's choice. The investor would remain free to go to arbitration either under the contract or under the BIT. But the State party to the contract would be effectively precluded from proceeding to the arbitral forum specified in the contract unless the investor was minded to agree. ... We believe, for the foregoing considerations, that Article 11 of the BIT would have to be considerably more specifically worded before it can reasonably be read in the extraordinarily expansive manner submitted by the Claimant. The appropriate interpretive approach is the prudential one summed up in the literature as in dubio pars mitior est sequenda, or more tersely, in dubio mitius*". Conclusively, the Tribunal came to the conclusion that Tribunal came to the conclusion that it did not have jurisdiction over contract claims "*which do not also constitute or amount to breaches of the substantive standards of the BIT*".

92. In the case *Joy Mining Machinery Limited v. Egypt* (cf. above para. 25), the Tribunal concluded negatively that (paras. 71-82): "*In this context, it could not be held that an umbrella clause inserted in the Treaty, and not very prominently, could have the effect of transforming all contract disputes into investment disputes under the Treaty, unless of course there would be a clear violation of the Treaty rights and obligations or a violation of contract rights of such a magnitude as to trigger the Treaty protection, which is not the case*".

d. The fourth view

93. A fourth view held that umbrella clauses may form the basis for treaty claims, without transforming contractual claims into treaty claims. Such view is described and applied in the case *Toto Costruzioni v.*

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Lebanon, Decision on Jurisdiction of 11 September 2009, where the Tribunal held that (para 201): “That view best conforms with the unqualified commitment assumed by Lebanon to comply with ‘any other obligation it has assumed’ as well as with the fourth paragraph of the Preamble to the Treaty which confirms the importance of the ‘contractual protection’ of investments - again without further qualification”.

This position has been expressed by CRAWFORD (*Treaty and Contract in Investment Arbitration*, Arbitration International, 2008, 351 ff.), suggesting that an umbrella clause is operative and may form the basis for a substantive treaty claim, but “it does not convert a contractual claim into a treaty claim. On the one hand it provides, or at least may provide, a basis for a treaty claim even if the BIT in question contains not generic claims clause; on the other hand, the umbrella clause does not change the proper law of the contract or its legal incidents, including provisions for dispute settlement”.

94. **The Participants in the Rome Meeting of the Committee** have expressed a general agreement in favour of a strict interpretation of the UCs. A possible interpretation could be that this refers to “any breach” of “any obligations” which relate to the maintenance or the existence of the investment, whereby the clause is interpreted in such a way as to maintain the investment.

It was also said that not every single breach of the contract amounts to a breach of the treaty, but only these breaches that are paramount clear and correspond to the international standards of treatment of investments. This mechanism of suggesting tribunals to fully respect the choice made by the parties could reach a more reasonable solution.

In cases where a public entity (either a federal state or a public enterprise) is granted means of public power, it could be acting as an element of the State and the obligation under the treaty would be the same as for the State, so that there would be the obligation to act in integrity with the contract. In such cases the UC could justify that the public entity could go to treaty arbitration. In other words, in a case where a public entity has been granted prerogative powers, the investor could have a recourse to treaty arbitration if this entity has used public powers in a way that compromises the integrity of the investment.

D. The MFN Clause and the substantive and procedural rights of the investor

1. Definition and preliminary observations

95. The MFN Clause was defined by the International Law Commission as “*a treaty provision whereby a State undertakes the obligation towards another State to accord most-favoured nation treatment in an agreed sphere of relations*” (cf. Article 4 of the Draft Articles on Most-Favoured-Nation Clauses with Commentaries, Text adopted at its 30th Session, 1978). Although MFN has traditionally been linked to trade agreements, in the 1950s when the first BITs were concluded, its use became common also in the practice of international investment agreements. In particular, in the field of investment agreements MFN is generally identified as the provision according to which an investor from a party to an agreement, or its investment, would be treated by the other party “no less favorably” than an investor from any third country, or its investment, with respect to a given subject-matter. Therefore it could become crucial for guaranteeing the equality of competitive opportunities between investors of different countries, preventing discrimination against foreign investors on grounds of their nationality. The MFN is however connected and limited by the *eiusdem generis* principle, according to which the clause can only attract matters belonging to the same subject matter or the same category of subject matters it is related to.

96. MFN is a standard of treatment having its roots in international law and generally linked to the principle of the equality of States. In 1952 the ICJ expressed the view that the purpose of a MFN clause was to “*maintain at all times fundamental equality without discrimination among all of the countries concerned*” (*Case Concerning Rights of Nationals of the United States of America in Morocco, (France v. USA)*, Judgment of 27 August 1952).

97. One of the most controversial aspect of the MFN clause was focused on the issue whether it can be used to “*broaden the scope of an investor’s procedural and substantive rights*” beyond and in addition to the protection clauses already included in the agreement (cf. *Investor-State Disputes Arising From Investment Treaties: a Review*, UNCTAD Series on International Investment Policies for Development, 2005).

2. The MFN Clause in BITs, Free Trade Agreements and other multilateral instruments

98. When referred to investments the MFN Clauses essentially present the same basic structure and character. In the case *Renta 4 et al. v.*

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Russian Federation (cf. above para. 36) the Tribunal examined the substance of the MFN debate, observing that the treaty that contains the MFN clause is conventionally identified as “the basic treaty”, while the treaty invoked as evidence of a more favorable treatment is referred to as the “comparator treaty” (cf. above para. 77). The party (the investor) who claims to be entitled to a different treatment on the basis of the MFN Clause is a stranger to the comparator treaty and “*therefore [is] in no position to make any claim under it. The claim can arise only under the basic treaty.*”

99. The MFB clause, in the context of international investments, is reciprocal between the (State) Parties, unconditional and related to the whole lifetime of the investment. It will cover the various operations connected to the investment, namely operation, maintenance, use or sale or liquidation of an investment. In the operative, MFN clause is therefore characterized by its relative nature, lacking any *a priori* content and covering any discrimination by reason of nationality.

100. In most cases the MFN treatment is granted both to the investor and to the investment. This is the case of the NAFTA (Article 1103), the Norway 2007 Model BIT and of the German 2008 Model BIT, whose Article 3 first provides with regard to investments that “(1) *Neither Contracting State shall in its territory subject investments owned or controlled by investors of the other Contracting State to treatment less favorable than it accords to investments of its own investors or to investments of investors of any third State*” and then with regard to investors similarly provides that “(2) *Neither Contracting State shall in its territory subject investors of the other Contracting State, as regards their activity in connection with investments, to treatment less favorable than it accords to its own investors or to investors of any third State*”.

101. In other cases the MFN treatment is accorded only to the investment, as in the case of the French 2006 Model BIT, whose Article 4 provides that “*Each Contracting Party shall apply ... to the nationals and companies of the other Party, with respect to their investments and activities related to the investments, a treatment not less favorable than that granted to its nationals or companies, or the treatment granted to the nationals or companies of the most favored nation, if the latter is more favorable*”, or in the case of the Colombia 2007 Model BIT (Article IV).

102. With regard to the activities covered by the MFN Clause, the standard of treatment is generally broad in order to cover all possible investment activities. It might use a rather general language, simply

referring to “*investment activities*” (as in the Japan-Mexico Free Trade Agreement, Article 59) or defining the various activities, making reference to “*the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments*” as in the NAFTA (Article 1103), or to the “[investment] *related activities including management, maintenance, use, enjoyment or disposal*”, as in the Energy Charter Treaty (Article 10.7), or “*establishment, acquisition, expansion, management, conduct, operation, liquidation, sale, transfer or other disposition of investments*”, as in Article 4 (Chapter 11) of the ASEAN.

103. With regard to the qualification of the “treatment” given by the States, which could be subject to the limits of the MFN Clause, it is generally understood that the provision applies only to “general treatment” and not to “individual practice”. It has been affirmed that “*freedom of contract prevails over MFN standard*” (Most Favoured-Nation Treatment, UNCTAD Series on issues in international investment agreements, 1999, p. 7). Furthermore the MFN standard implies a similarity in the field of operation where the treatment is accorded.

3. The exceptions to the MFN Treatment

104. There is a general understanding that exceptions to the MFN treatment are needed to reduce its very broad scope of application. The extent of the exceptions varies in the different treaties, but it is generally understood that they might apply in the field of social and labour activities, taxation, environmental protection, intellectual property rights, agriculture and air and maritime transportation.

In particular there are BITs that allow the contracting parties to derogate and exclude the application of the MFN standard for reasons of public order, public health or public morality (cf. the Energy Charter Treaty, whose Article 24, paras. 2 and 3, provides for exceptions to specific rules of the Treaty which are necessary “*to protect human, animal or plant life or health*” and “*for the protection of [a Contracting Party’s] essential security interests*”. It is to be noted that the exception based on national security reason is quite unusual in BITs. However the German Model BIT provides under Article 3, para. 2, that “*Measures that have to be taken for reasons of public security and order shall not be deemed treatment less favourable within the meaning of this Article*”.

105. Most investment agreements provide derogation to the MFN clause based on reciprocity, mostly with regard to taxation matters and intellectual property rights (cf. Canada Model BIT at Article 9, para. 4 “*In respect of intellectual property rights, a Party may derogate from Articles 3 and 4 in a manner that is consistent with the WTO*”).

Agreement”). However, particularly with regard to taxation, a recent case demonstrated that the mere wording “the provisions of the present agreement will not apply to taxation” is not sufficient to exclude all claims connected to taxation from the operation of a MFN (cf. *Renta 4 et al. v. Russian Federation*, above para 36, at para. 74). On the issue, cf. the ICSID awards *Encana v. Ecuador* (Decision on Jurisdiction of 27 February 2004) and *Duke Energy v. Ecuador* (Award of 18 August 2008) and most recently *Burlington Resources v. Ecuador* (cf. above para. 16).

106. Furthermore exceptions are provided in the case of regional economic integration organizations (also known as REIO Clause): this determines that the Member Countries of a REIO are allowed to derogate to the MFN treatment obligation. The German Model BIT provides that (Article 3, para. 3) “*Such treatment shall not relate to privileges which either Contracting State accords to investors of third States on account of its membership of, or association with, a customs or economic union, a common market or a free trade area*”.

4. The effect of MFN Clause to procedural or substantive right of investment protection

a. MFN treatment applied to substantive issues

107. The MFN standard in international law is traditionally linked to the treatment of foreign goods and persons (cf. GATS Agreement). When the substantive issues of non-discriminatory treatment are concerned, MFN clauses might concern various aspects of the investment mainly focused on how the host State treats foreign investors or investments. There are clauses which provide for the regular returns on the investment, or the transfer of payments, or for a non-discriminatory treatment as a consequence of expropriation/nationalization measures adopted by the host State, or for the coverage of particular events, like war or civil disturbance as in the case of some US BITs which might state “*Each Party shall accord national and most favoured nation treatment to covered investment as regards any measure relating to losses that investments suffer in its territory owing to war or other armed conflict, revolution, state of national emergency, insurrection, civil disturbance, or similar events*” (Article 4 of the 2000 US-Bolivia BIT).

108. Many ICSID cases dealt with the application of the MFN principle in relation to liability standards. Cf., for instance, the first known investment treaty arbitration *AAPL v. Sri Lanka* (cf. above para. 7) and later *CMS v. Argentina*, Award of 20 April 2005, *Lucchetti v. Peru* (cf.

above para. 20), *MTD v. Chile*, Award of 21 May 2004. The MFN issue appeared also in two NAFTA cases: *Pope & Talbot v. Canada*, Award on the Merits of Phase 2, 10 April 2001, and *ADF v. USA* (cf. above para. 18). The latter reconsidered the principle expressed in *Pope & Talbot* (“NAFTA investors and investments that would be denied access to the fairness elements untrammelled by the ‘egregious’ conduct threshold that Canada would graft onto Article 1105, would simply turn to Articles 1102 and 1103 for relief”, para 117), but eventually rejected claimant’s claim, excluding the subject matter from the scope of operation of NAFTA’s MFN Clause. In the 29 July 2008 Award in the case *Rumeli Telekom v. Kazakhstan*, the Tribunal declared that the host State was liable for a violation of the FET that the Tribunal had incorporated based on the MFN Clause in the Turkey-Kazakhstan BIT, deriving from the host State’s third-party BITs, particularly from the UK-Kazakhstan BIT.

109. In the ICSID case *Bayindir Insaat Turizm Ticaret Ve Sanayi v. Pakistan*, Award of 27 August 2009, the Arbitral Tribunal relied on the MFN provision contained in the Pakistan-Turkey BIT to import the Fear and Equitable Treatment (FET) standard found in other treaties signed by Pakistan, stating that “the basis for importing an FET obligation into the Treaty is provided by its MFN clause” (para. 164). The Tribunal stated that the ordinary meaning of the applicable MFN clause demonstrated that the contracting parties “did not intend to exclude the importation of a more favourable substantive standard of treatment accorded to the investors of third countries” (cf. paras. 156-157). Moreover, it noted that the fact that the FET provision referred to by the claimant pre-dates the MFN clause in the Pakistan-Turkey BIT does not appear to preclude the importation of an FET obligation from another BIT concluded by the respondent.

Moreover the Tribunal had to deal with an allegation of discrimination in violation of the MFN clause. On this issue, the Tribunal noted that the MFN clause is not limited to regulatory treatment but also applies to the manner in which a state concludes an investment contract and/or exercises its rights thereunder (para. 388, also referring to the 2005 Decision on Jurisdiction in the same case). The claimant had argued that, though there had been several other projects (some of which were run by foreign contractors) that had not been completed in time, the claimant was the only contractor to be expelled. The Tribunal dismissed the MFN claim because the claimant had failed to prove the “similarity of the situations” at the level of contractual terms and circumstances among the several projects (cf. para. 420). This requirement might be unproblematic, if the treaties involved concern the mutual promotion and protection.

b. MFN treatment applied to jurisdictional matters

110. As to procedural aspects of the application of the MFN standard, arbitral tribunals have been frequently faced with the issue of determining whether MFN clauses allow investors to rely on shorter waiting periods in third-country BITs or be granted to avoid the requirement to pursue local remedies for a limited time before initiating arbitration (mainly ICSID). Arbitral jurisprudence has generally accepted that investors circumvent this requirement, making recourse to more favourable provisions contained in third-party treaties.

111. The first and well known case where an ICSID arbitral tribunal has analyzed the MFN treatment in the matter of investments was *Maffezini v. Spain*, Decision on Objections to Jurisdiction of 25 January 2000. This became a landmark-case for all the following case-law. The basic assumption of the Tribunal was the following: “*if a third party treaty contains provisions for the settlement of disputes that are more favorable 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 favored nation clause as they are fully compatible with the ejusdem generis principle*” (cf. para. 56). The Tribunal observed however that “*It is clear, in any event, that 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*” (para. 63).

112. A MFN Clause was contained in the Germany-Argentina BIT, referred to in the ICSID case *Siemens v. Argentina* (Decision on Jurisdiction, 3 August 2004), where the Tribunal first noted that in the BIT concerned “*the formulation is narrower but ... the term ‘treatment’ and the phrase ‘activities related to the investments’ are sufficiently wide to include settlement of disputes*” (para. 103).

113. The danger of the s.c. “treaty shopping” (some authors also referred to the “cherry-picking” attitude of the investors) was considered with a certain criticism in the case *Plama v. Bulgaria* (ICSID, Decision on Jurisdiction, 8 February 2005). The Tribunal observed that “*Doubt may be further created by the scope of the dispute settlement provisions in the other BITs. A number of them refer to disputes arising out of the particular BIT*” and thus “[i]t appears to be difficult to interpret the MFN clause as importing into the particular BIT such specific language from other BITs” (para. 206). Moreover in the Tribunal’s view “[w]hen

concluding a multilateral or bilateral investment treaty with specific dispute resolution provisions, states cannot be expected to leave those provisions to future (partial) replacement by different dispute resolution provisions through the operation of an MFN provision, unless the States have explicitly agreed thereto” (para. 212). In this decision, the Tribunal also commented that the international law cases examined by the arbitrators to reach a decision in the *Maffezini* case, cf. above para. 111 (namely the *Case Concerning Rights of Nationals of United States of America in Morocco*, the *Anglo-Iranian Oil Co. Case*, and the *Ambatielos Claim*), “do not provide a conclusive answer to the question” (para. 217) of the extension of the MFN Clause. The Tribunal in *Plama* also denied that the purpose of the harmonization of dispute settlement provisions cannot be achieved by reliance on MFN provision (cf. para. 219).

However, the “harmonization effect” has been recognized by some authors, who confirmed that MFN clauses “multilateralize the bilateral inter-State treaty relationship and harmonize the protection of foreign investments in a specific host State” (cf. SHILL, *The Multilateralization of International Investment Law*, Cambridge, 2010).

114. A quite restrictive view has been expressed by the Arbitral Tribunal in the case *Wintershall Aktiengesellschaft v. Argentine*, ICSID Award (8 December 2008): “ordinarily and without more, the prospect of an investor selecting at will from an assorted variety of options provided in other treaties negotiated with other parties under different circumstances, dislodges the dispute resolution provision in the basic treaty itself – unless of course the MFN Clause in the basic treaty clearly and unambiguously indicates that it should be so interpreted: which is not so in the present case.” (para. 167).

115. In the recent case *Tza Yap Shum v. Peru* (cf. above para. 64), the Tribunal refused to permit the claimant to invoke the MFN clause in the China-Peru BIT, in order to establish a jurisdictional basis for the dispute. The Tribunal argued that “Since the Contracting Parties specifically established the possibility of submitting “other matters” to ICSID arbitration and since they have established specifically such occurrence in the wording of the BIT, we, the Tribunal, conclude that it is our duty to give the BIT wording the meaning it was really intended. As a result, the Tribunal hereby determines that the specific wording of Article 8(3) should prevail over the general wording of the MFN clause in Article 3 and Claimant's arguments on the contrary must be dismissed” (cf. para. 216).

116. In the case *Renta 4 et al. v. Russia* (cf. above para. 36), under the Arbitration Institute of the Stockholm Chamber of Commerce, the

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Tribunal accepted the general proposition that MFN clauses may extend the tribunal's jurisdiction beyond the scope of the underlying treaty's jurisdictional clause. However the Tribunal by majority ultimately decided that the specific MFN clause in the Spain-Union Soviet Socialist Republics BIT could not be read to enlarge the competence of the Tribunal.

117. A positive solution as to the extension of the MFN Clause was expressed by the Tribunal in the case *Gas Natural v. Argentine*, Decision on Preliminary Questions on Jurisdiction (17 June 2005): “*the issue of applying a general most-favored-nation clause to the dispute resolution provisions of bilateral investment treaties is not free from doubt*”. The Tribunal declared to be “*satisfied, however, that the terms of the BIT between Spain and Argentina show that dispute resolution was included within the scope of most-favored-nation treatment, and that our analysis ... is consistent with the current thinking as expressed in other recent arbitral awards. We remain persuaded that assurance of independent international arbitration is an important – perhaps the most important – element in investor protection. Unless it appears clearly that the state parties to a BIT or the parties to a particular investment agreement settled on a different method for resolution of disputes that may arise, most-favored-nation provisions in BITs should be understood to be applicable to dispute settlement*” (para. 49).

Similarly in the case *Suez v. Argentine*, Decision on Jurisdiction (3 August 2006), the Tribunal observed that: “*after an analysis of the substantive provisions of the BITs in question, the Tribunal finds no basis for distinguishing dispute settlement matters from any other matters covered by a bilateral investment treaty*”. The Tribunal concluded that Claimants InterAguas and AGBAR, “*relying on Article IV of the Argentina-Spain BIT ... may invoke the more favorable treatment afforded in the Argentina-France BIT and may therefore bring an international arbitration without the necessity of first having recourse to the local courts of Argentina*” (paras. 59 and 68).

118. It has to be noted that the more recent practice of the States in negotiating BITs seems to be critical towards the application of the MFN Clause to dispute settlement. The 2007 Norway Model BIT introduced a clear provision stating: “*For greater certainty, treatment referred to in paragraph [1] does not encompass dispute resolution mechanisms provided for in this Agreement or other International Agreements*” (Article 4, para. 3).

The Participants to the Rome Meeting of the Committee expressed a preference for a more restrictive use of the MFN clause. There was a general agreement as to the fact that the MFN clause refers to “treatment”, but strong doubts as to whether the MFN clause also encompasses dispute settlement solutions (reference to the *Maffezini* and *Daimler* cases). If the treatment is deemed to include access to arbitration or the extension of an UC, it is necessary to stick to the provisions of the treaty, from which the obligations originate. Thus, an investor could not invoke an UC which is not provided for in a treaty.

In assessing the MFN status of treatment, a prior interpretation of the treaty should therefore be made in order to ascertain the intention of the States.

Doubts were raised as to whether an investor could invoke a MFN clause for a treaty which is not an investment treaty.

E. The Fair & Equitable Treatment (FET)

1. Definition and preliminary observations

119. Originated as a treaty clause containing a declaration of principles, the Fair and Equitable Standard (FET) is one of the key standards of investment protection. According to this provision foreign investments are granted by the host State a treatment in compliance to a minimum standard of fairness, irrespective of the standards the host State applies to domestic investment under its national law. It has been noted that an unfair and non-equitable treatment by the host State towards the investor, determining the impairment of his property rights or his capacity to develop the investment, might be considered a new type of expropriation (BRONFMAN, *Fair and Equitable Treatment: an Evolving Standard*, Max Planck YUNL, 2006, p. 609 ff.)

FET has been frequently invoked in investment disputes with a remarkable relevance in the arbitration practice. A great number of claims have been successfully grounded on the violation of FET by the host State for a broad range of measures. The problematic issue in applying the FET standard is the broadness of the clause interpretation, determining limits of application of the FET. Therefore arbitral tribunals have been frequently involved in determining “*whether the obligation to grant ‘fair and equitable treatment’ is synonymous with the minimum standard of treatment of foreign investment required under customary international law, or whether it means something different – albeit with some overlap*” (*Identifying Core Elements in Investment Agreements in the APEC Region*, UNCTAD Series on International Investment Policies for Development, 2008).

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120. In relation to the meaning and content of the FET, the opinion of Dr. Mann expressed in 1981 is well known and was repeatedly commented by other authors: “the term ‘fair and equitable treatment’ envisages conduct far beyond a minimum standard and affords protection to a greater extent and according to a much more objective standard than any previously employed form of words. A tribunal would not be concerned with a minimum, maximum or average standard. It will have to decide whether in all circumstances the conduct in issue is fair and equitable or unfair and inequitable. ... The terms are to be understood and applied independently and autonomously.” (MANN, *British Treaties for the Promotion and Protection of Investments*, BYIL 52, 1981, p. 241). In general on the FET clause cf. JUILLARD, *L'évolution des sources du droit des investissements*, RCADI, 250, 1994, 11 ff.; SACERDOTI, *Bilateral Treaties and Multilateral Instruments on Investment Protection*, cf. above fn. n. 2; YANNACA-SMALL, *Fair and Equitable Treatment Standard in International Investment Law*, OECD, Working Papers on International Investment, 2004/3; TUDOR, *The Fair and Equitable Standard in the International Law of Foreign Investment*, Oxford, 2008; DOLZER, SCHREUER, *Principles of International Investment Law*, cf. above para. 37.

2. FET in the multilateral instruments, Free Trade Agreements and in BITs

121. The first reference to the FET is found in Article 11 (2) of the 1948 Havana Charter for an International Trade Organization, assessing that foreign investments should be assured “just and equitable treatment”.

The FET clause is included in the 1985 Convention establishing the MIGA (Article 12 (d)), establishing that “*In guaranteeing an investment, the Agency shall satisfy itself as to: ... the investment conditions in the host country, including the availability of fair and equitable treatment and legal protection for the investment*”.

The Section III of the World Bank Guidelines on the Treatment of Foreign Direct Investment also provides that “*2. Each State will extend to investments established in its territory by nationals of any other State fair and equitable treatment according to the standards recommended in these Guidelines*”.

Article 10 of the 1994 Energy Charter Treaty provides that “*(1) 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”.

122. Article 1105 (1) of the NAFTA requires the State parties to “*accord investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment”.*

The ASEAN Comprehensive Investment Agreement of 2009, includes a rather wide provision concerning the FET, requesting the Contracting States to guarantee that “*1. Each Member State shall accord to covered investments of investors of any other Member State, fair and equitable treatment and full protection and security. 2. For greater certainty: (a) fair and equitable treatment requires each Member State not to deny justice in any legal or administrative proceedings in accordance with the principle of due process; and (b) full protection and security requires each Member State to take such measures as may be reasonably necessary to ensure the protection and security of the covered investments”.*

123. At the bilateral level, Article 5 of 2004 Canada Model BIT provides that “*1. Each Party shall accord to covered investments treatment in accordance with the customary international law minimum standard of treatment of aliens, including fair and equitable treatment and full protection and security. 2. The concepts of ‘fair and equitable treatment’ and ‘full protection and security’ in paragraph 1 do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens”.*

Article 5 of 2007 Norway Model BIT provides that “*Each Party shall accord to investors of the other Party, and their investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security”.*

The German Model BIT introduced in 2008 among the general provisions concerning the admission and protection of investments states that (Article 2 (2)): “*Each Contracting State shall in its territory in every case accord investments by investors of the other Contracting State fair and equitable treatment as well as full protection under this Treaty”.*

Article 5 of the 2012 US Model BIT reads as follows: “*1. Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security”.*

3. Different language of the FET clauses

124. The practice of bilateral treaties has evidenced different approaches to dealing with the FET standard. In its 2008 Report concerning the investment agreements in the APEC (Asia-Pacific Economic Cooperation) Region, UNCTAD emphasizes the different drafting of the FET clauses depending on the existence of a link between the wording “fair and equitable treatment” and a more general reference to “treatment under international law”.

It has been noted that some treaties (only a few BITs, however) simply do not include any FET standard. This has important consequences for the investor who will have a reduced protection against unfair measures possibly adopted by the host State and will only claim for the violation of the minimum standard of treatment as prescribed by customary international law for the aliens. Cf. BRONFMAN, *Fair and Equitable Treatment: an Evolving Standard*, above para. 119.

Some BITs do not contain any reference to international law, simply providing that each contracting party shall accord to investments of the other contracting party “a fair and equitable treatment”. A slight variation (although rare) of this type of clause is when the BIT simply refers to “equitable” treatment, without mentioning the “fairness” of the treatment. Cf. Article 2 of the 2002 Lebanon-Malaysia BIT and Article III of the 1991 Indonesia-Norway BIT (“equitable and reasonable”).

125. The NAFTA FET clause inserted in Article 1105 (cf. above para. 122) is an example of a clear connection between the principle of FET and international law, when requiring the Contracting Parties to grant “treatment in accordance with international law, including fair and equitable treatment”. In the interpretation given in the NAFTA system it has been noted that this does not mean that investments should be given treatment beyond what is required under international law minimum standard of treatment. Cf. the FET clause contained in Article 7, (A) of the 2005 Model International Agreement on Investment for Sustainable Development (intended as a basis for bilateral, regional and multilateral negotiations and agreements) “*Each Party shall accord to investors or their investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security*”.

126. This issue has been recently analyzed by two arbitral tribunals, reaching different conclusions. In the ICSID case (UNCITRAL) *Glamis Gold v. United States*, Award of 8 June 2009, the Arbitral Tribunal was

involved with the interpretation of FET as provided in Article 1105 NAFTA. The Tribunal stated that (para. 615) “[t]he customary international law minimum standard of treatment is just that, a minimum standard. It is meant to serve as a floor, an absolute bottom, below which conduct is not accepted by the international community”. The Tribunal moreover affirmed that “The fair and equitable treatment promised by Article 1105 is not dynamic; it cannot vary between nations as thus the protection afforded would have no minimum”. Then the Tribunal in order to identify possible parameters for the FET standard made reference to the decision in the 15 October 1926 *Neer* case (*Neer v. Mexico*, 4 R. Int’l Arb. Awards, 1926) (para. 616): “The fundamentals of the *Neer* standard thus still apply today: to violate the customary international law minimum standard of treatment codified in article 1105 of the NAFTA, an act must be sufficiently egregious and shocking – a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons – so as to fall below accepted international standards and constitute a breach of article 1105(1). The Tribunal notes that one aspect of evolution from *Neer* that is generally agreed upon is that bad faith is not required to find a violation of the fair and equitable treatment standard, but its presence is conclusive evidence of such”.

127. In the NAFTA-UNCITRAL case *Merrill&Ring Forestry v. Canada*, Award of 31 March 2010, the Tribunal was also called to determine the meaning of the FET clause contained in Article 1105 NAFTA in relation to the minimum standard granted by international law. In this perspective the *Neer* case was again quoted, although in a more critical manner. In its conclusion on the issue the Tribunal observed that (para. 213): “the applicable minimum standard of treatment of investors is found in customary international law and that, except for cases of safety and due process, broader than that defined in the *Neer* case and its progeny. Specifically this standard provides for the fair and equitable treatment of alien investors within the confines of reasonableness. The protection does not go beyond that required by customary law, as the FTC has emphasized. Nor, however, should protected treatment fall short of the customary law standard”.

128. Also in the US BITs, the FET clause is generally linked to international law: cf. among the others the US-Argentina BIT (Article II): “2. a) Investment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that required by international law”.

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The 2004 Japan-United Mexican States for the Strengthening of the Economic Partnership, in relation to the general treatment accorded to investments, provides that (Article 60) “*Each Party shall accord to investments of investors of the other Party treatment in accordance with international law, including fair and equitable treatment and full protection and security*”.

4. The core elements of the FET standard according to the arbitral case-law

129. Although considering all the differences in the drafting of the FET clause in BITs, arbitral tribunals have often gone beyond the discussion whether FET corresponds to the minimum standard protection granted by international law, and have identified some core elements distinguishable in the FET standard. These elements are hereby analyzed with reference to the most recent arbitral practice.

a) Due process

130. The violation of this basic principle of law determines an international wrongful act of denial of justice. The denial of justice can be interpreted on the basis of customary international law. The breach of such obligation might be attributed to the host State judiciary or even to the executive. This requirement is considered to be so fundamental that in the practice of US BIT and FTA is specifically indicated.

131. The due process principle has been coped with in various ICSID cases. Among them cf. *Bayindir Insaat Turizm Ticaret Ve Sanayi v. Pakistan* (cf. above para. 109). The Tribunal stated that it agreed “*with Bayindir when it identifies the different factors which emerge from decisions of investment tribunals as forming part of the FET standard. These comprise the obligation to act transparently and grant due process*” (para. 178).

132. In the ICSID case *Toto Costruzioni v. Lebanon* (cf. above para. 93), the Tribunal denied its jurisdiction over the investor’s claim of delays in two lawsuits before the *Conseil d’Etat* as breach of the fair and equitable standard provision in the Italy–Lebanon BIT as the claimant had not satisfied a *prima facie* case. The Arbitral Tribunal affirmed that (para. 164): “*Moreover, a state can only be held liable for denial of justice when it has not remedied this denial domestically. As summarized by Jan Paulsson: ‘States are held to an obligation to provide a fair and efficient system of justice, not to an undertaking that there will never be an instance of judicial misconduct. National responsibility for denial of*

justice occurs only when the system as a whole has been tested and the initial delict has remained uncorrected... The very definition of denial of justice encompasses the notion of exhaustion of local remedies. There can be no denial of justice before exhaustion” (the Tribunal was quoting PAULSSON, *Denial of justice in International Law*, 2005, 306).

b) Non-discrimination and arbitrariness

133. The principle of non-discrimination/arbitrariness was affirmed by the ICJ in the *Elettronica Sicula (ELSI)* case (*United States v. Italy*, 20 July 1989) “*Arbitrariness is not so much something opposed to a rule of law, as something opposed to the rule of law ... It is a wilful disregard of due process of law, an act which shocks, or at least surprises, a sense of juridical propriety*” (para. 128).

In the ICSID case *Lemire v. Ukraine* (cf. above para. 71), the Tribunal affirmed that “*Discrimination, in the words of pertinent precedents, requires more than different treatment. To amount to discrimination, a case must be treated differently from similar cases without justification; a measure must be ‘discriminatory and expose[s] the claimant to sectional or racial prejudice’; or a measure must ‘target[ed] Claimant’s investments specifically as foreign investments’*” (para. 261).

As to arbitrariness, in the same case *Lemire v. Ukraine*, the Tribunal confirmed that (para. 262) “*Arbitrariness has been described as ‘founded on prejudice or preference rather than on reason or fact’; ‘...contrary to the law because...[it] shocks, or at least surprises, a sense of juridical propriety’; or ‘wilful disregard of due process of law, an act which shocks, or at least surprises a sense of judicial propriety’; or conduct which ‘manifestly violate[s] the requirements of consistency, transparency, even-handedness and non-discrimination’*”. The Tribunal also made reference to the definition of “arbitrary” measure given by Schreuer (who acted as expert in the ICSID Case *EDF (Services) Limited v. Romania* (cf. above para. 71), and was quoted by the Tribunal at para. 262 of the Award): “*a. a measure that inflicts damage on the investor without serving any apparent legitimate purpose; b. a measure that is not based on legal standards but on discretion, prejudice or personal preference; c. a measure taken for reasons that are different from those put forward by the decision maker; d. a measure taken in wilful disregard of due process and proper procedure.*” The Tribunal then affirmed that (para. 263): “*Summing up, the underlying notion of arbitrariness is that prejudice, preference or bias is substituted for the rule of law*”.

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c) Due diligence

134. This obligation is also known as “obligation of vigilance”. It has been analyzed in some arbitral disputes, but often in connection to the principles of standard of full protection and security.

d) Legitimate expectations: transparency, consistent conduct

135. These basic requirements for the investor’s operation in the host State are strictly connected. Transparency should guarantee that the legal framework for the investment in the host State is stable and predictable to the investor and any measures undertaken by the host State can be reconnected to the legal order that was opened to the investor. As it has been noted, this legal framework “*consist[s] of legislation and treaties, of assurances contained in decrees, licences and similar executive assurances as well as in contractual undertakings ...*”. Under this issue the FET standard implies the protection of the investor’s right to plan and establish the investment, having duly examined the law order of the host State (DOLZER, SCHREUER, *Principles of international investment law*, cf. above para. 37). Problems might also arise due to inconsistent positions taken by the State, such as the reversal of assurances.

In the case *GAMI v. Mexico*, UNCITRAL-NAFTA Award of 15 November 2004, on the interpretation of Article 1105, the Ad-Hoc Arbitral Tribunal stated (paras. 92 ff): “*The challenging task for this Tribunal is to apply these abstractions. It is necessary first to enquire how they relate to compliance with national law. To repeat: NAFTA arbitrators have no mandate to evaluate laws and regulations that predate the decision of a foreigner to invest*”. Other precedent NAFTA disputes are *Metalclad v. United Mexican States*, ICSID Award of 30 August 2000, *Waste Management v. United Mexican States* (cf. above para. 18).

136. The issue of transparency has been afforded in various ICSID cases, among others the most recent cases are: *Plama*, Award of 12 November 2008, *Siag & Clorinda Vecchi v. The Arab Republic of Egypt*, Award of 1 June 2009; *Lemire v. Ukraine* (cf. above para. 71). In the latter case, the Tribunal observed (para. 284) “*The FET standard defined in the BIT is an autonomous treaty standard, whose precise meaning must be established on a case-by-case basis. It requires an action or omission by the State which violates a certain threshold of propriety, causing harm to the investor, and with a causal link between action or omission and harm. The threshold must be defined by the Tribunal, on the basis of the wording of Article II.3 of the BIT, and bearing in mind a*

number of factors, including among others the following: - whether the State has failed to offer a stable and predictable legal framework; ... - whether there is an absence of transparency in the legal procedure or in the actions of the State”.

e) Good faith

137. This element of the FET standard is commonly recognized as a general principle of law, requiring the parties to act honestly and fairly with each other. In the ICSID case *Siag and Clorinda Vecchi v. The Arab Republic of Egypt* (cf. above para. 136), the Tribunal affirmed (para. 450): “*The general, if not cardinal, principle of customary international law that States must act in good faith is thus a useful yardstick by which to measure the Fair and Equitable standard*”.

Similarly, in the ICSID case *Rumeli Telekom v. Kazakhstan* (cf. above para. 108) confirmed by the Ad Hoc Committee with Decision of 25 March 2010, the Tribunal affirmed that: “*The parties rightly agree that the fair and equitable treatment standard encompasses inter alia the following concrete principles: ... - the State is obliged to act in good faith*” (para. 609).

F. Expropriations, Indirect Expropriations, Regulatory Measures

The topic of Regulatory Measures has been selected by the Rapporteur and the Commission for preliminary examination in order to study a stimulating issue which appears capable of offering interesting points for a general discussion and, consequently, obtaining advice and directions for the future work.

138. The analysis of the topic proposed here does not intend to rediscuss the traditional rules of treaty law and/or customary law concerning expropriations, nationalizations, and generally speaking, the takings of foreign property. For the purpose of this Section of the Presentation, these traditional rules are taken as granted and considered as accepted. The choice is made in order to better focus on the peculiarity of the measures that are the object of the examination.

139. Thus, the traditional rules taken here for granted, can be summarized as follows: a) Foreign property may not be expropriated except for: (i) public purpose, (ii) a non-discriminatory basis, (iii) in accordance with due process of law, and (iv) against compensation. b) The compensation has to be: (i) prompt, (ii) adequate, and (iii) effective.

140. According to these traditional rules, the term expropriation is usually comprehensive also of nationalizations, for which no specific rules are provided. Moreover, expropriations may be direct or indirect, the latter including any measures having equivalent effect to an

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expropriation (cf. HIGGINS, *The Taking of Property by the State: Recent Developments in International Law*, RCADI, 1982, 259 ff.; ORREGO VICUÑA, *Regulatory Authority and Legitimate Expectations: Balancing the Rights of the State and the Individual under International Law in a Global Society*, Int. Law Forum, 2003, 188 ff.). Examples of these traditional solutions can be found in numerous BITs and in the Draft MAI of 1998 (cf. YANNACA-SMALL, *Indirect Expropriation' and the 'Right to Regulate' in International Investment Law*, in *International Investment Law: A Changing Landscape*, OCSE, 2005; REINISCH, KNAHR, *International Investment Law in Context*, 2008).

In application of the above rules and solutions, the s.c. regulatory measures have been generally considered as a sort of indirect or creeping expropriations.

141. The following examples demonstrate the above conclusion and deserve to be considered:

- a) ICSID case *SPP v. Egypt*, Award of 20 May 1992, where full compensation was awarded to the investor, notwithstanding that the breach of contract was determined by cultural and environmental reasons. However, loss of gain was not awarded for the period subsequent to the entry into force of the UNESCO Convention on the protection of the cultural heritage;
- b) ICSID case *Santa Elena v. Costa Rica*, Award of 17 February 2000, where full compensation was awarded to the investor in a case of breach determined by environmental reasons;
- c) ICSID case *Metalclad v. Mexico* (cf. above para. 135), where the full compensation was awarded in a case of breach determined by the denial of an authorization by local government notwithstanding the assurances given by the federal government and the denial was caused by the environmental and public health reasons;
- d) ICSID Addition Facility case *Tecmed v. Mexico*, Award of 29 May 2003, where a NAFTA Tribunal found that the revocation of a license for the operation of a landfill represented an indirect expropriation, and the revocation was due to environmental and public health reasons.

142. A trend in favor of differentiate regulatory measures from indirect or creeping expropriations started around 2004, qualifying as such measures adopted by public authorities in order to protect legitimate public welfare objectives, *i.e.* public health, safety and environment, and

excluding compensation for the consequences of such measures on foreign investments.

In this respect, the Energy Charter Treaty of 1996 may be worth recalling as an international precedent for the importance given, in its Article 19, to the environmental aspects of the research and development of natural resources and for the statement, in its Article 18, that each State “*continues to hold the rights to ... regulate the environmental and safety aspects of the [energy resources] exploration, and development*” (cf. WALDE, *Energy Charter Treaty-Based Investment Arbitration: Controversial Issues*, JWIT, 2004).

143. The new developments mentioned above have been especially evidenced by the 2004 US and Canadian Model BIT. The 2004 US Model has been the object of different evaluations and criticisms (cf. for a comprehensive and critical examination, SCHWEBEL, *The United States 2004 Model Bilateral Investment Treaty: an Exercise in the Regressive Development of International Law*, above para. 51), but it appears of undoubted importance for the specific topic of Regulatory Measures.

Actually, Annex B to the Model BIT, - clarifying Article 6 devoted to expropriations – contains a final statement according to which “*Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations*”. The 2012 US Model BIT provides that “*3. The Parties recognize that each Party retains the right to exercise discretion with respect to regulatory, compliance, investigatory, and prosecutorial matters, and to make decisions regarding the allocation of resources to enforcement with respect to other environmental matters determined to have higher priorities. Accordingly, the Parties understand that a Party is in compliance with paragraph 2 where a course of action or inaction reflects a reasonable exercise of such discretion, or results from a bona fide decision regarding the allocation of resources*”.

144. The same solutions, even with identical formulations, are contained in the Annex B to the Canadian Model BIT also of 2004 and in the Annex 10-C to CAFTA-DR (CAFTA-Dominican Republic) also of 2004 (cf. MCILROY, *Canada's new foreign investment protection and promotion agreement. Two steps forward, one step back?*, above para. 51; EDSALL, *Indirect expropriation under NAFTA and DR-CAFTA: potential inconsistencies in the treatment of State public welfare regulations*, 86 *Boston University Law Review*, 2006, 931; NEWCOMBE, *The Boundaries of Regulatory Expropriation in International Law*, 20 *ICSID Rev.*, 2005).

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It has to be noted that the appendix relating to expropriation is maintained in identical terms in the US Model of 2012.

The arbitral Award of 3 August 2005, in the case *Methanex v. United States*, conducted according to the UNCITRAL Rules and under NAFTA, appears to have followed the new approach. The Tribunal found that “*As a matter of general international law, a non-discriminatory regulation for public purpose, which is enacted in accordance with due process.....is not deemed expropriatory and compensable unless specific commitments had been given by the regulatory government to the then putative foreign investor...*”. Similar construction and conclusion has been adopted by another UNCITRAL tribunal in the case *Saluka v. Czech Republic* (cf. above fn. n. 4), considering that, according to customary international law, a State does not commit an expropriation and is not liable to pay compensation “*when it adopts general regulations that are commonly accepted as within the police power of State*”.

The point which remains open for debate is whether the public purpose alone, as declared by the public authorities, would be sufficient for considering legitimate ad adopted regulatory measure and thus depriving the foreign investor of any compensation. In the ICSID case *Azurix v. Argentina*, Award of 14 July 2006, the Tribunal found that the public purpose alone would not be sufficient and would not automatically deprive the investor of any compensation.

145. **Most Participants to the Rome Meeting of the Committee** have expressed their preference for not differentiating anymore between the concepts of nationalization, expropriations and creeping expropriation, but to treat them as part of the one and same category, identified as taking of property. The general rule of international responsibility should then apply to them.

Furthermore, reference to the 1992 Guidelines of the World Bank was suggested. In the Guidelines, nationalizations are mentioned as having a different regime from expropriations. Expropriation, unlike nationalization, is an individual measure where special policy grounds come into play. Therefore it was suggested by some participants that the differentiation be kept, but this did not find an unanimous consent as the majority of Participants did not find such differentiation useful.

Provided that there is an obligation to avoid imposing arbitrary measures or use of threats against the investor, it was also suggested that there should be an obligation to renegotiate in case of fundamental economic changes in the host State, especially for long-term contracts. The refusal

to renegotiate will constitute a breach of the contract, and penalties can be applied.

A **Participant** expressed the desire to maintain the difference between expropriations and regulatory expropriations (reference was made to the *Burlington* case). Regulatory expropriations, which are admitted by the BITs since 2004 and which are repeated in the most recent BITs, do not constitute expropriations. In case of protection of human health and human rights, the measures adopted should be considered in themselves as justified without compensation for the investor.