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contents

3 Features

Risky Business or Risky Politics:
What Explains Investor-State Disputes?
Zoe Phillips Williams

6

Aron Broches and the Withdrawal of
Unilateral Offers of Consent to Investor-State
Arbitration
Matthew C. Porterfield

9

Opening the Door to Foreign Investment?
An Analysis of Bolivia's New Investment
Promotion Law
Martin Dietrich Brauch

13

News in Brief:

Opposition to investor-state arbitration in
TTIP grows; UNCITRAL approves draft
convention on transparency; Update on
Renco Group vs. Peru: Renco files memorial
on liability;

14

Awards and Decisions:

Renée Rose Levy de Levi v. Republic
of Peru; Emmis et al. v. Hungary; David
Minnotte and Robert Lewis v. Republic of
Poland

19

Resources and Events

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Risky Business or Risky Politics: What Explains Investor-State Disputes?

Zoe Phillips Williams

feature 1



International investment agreements (IIAs) were designed to protect private actors from the risks inherent in investing in foreign states. However, critics argue that the tables have turned; due to the increasing and expansive use of investor-state arbitration, what was once risky business for investors has become “risky politics” for states. At the same time, proponents of investor-state dispute settlement mechanisms claim that only a very narrow range of measures can be challenged under international arbitration and that worries about “regulatory chill” are unfounded.¹

The diversity of policy measures that have precipitated these conflicts demonstrates that the investment regime places obligations on states which may compete with domestic interests. While the curtailing of domestic “policy space” by IIAs has been widely proclaimed (and is, arguably, the explicit purpose of these agreements) the extent to which the regime actually impedes states in the normal course of regulating or reacting to crises remains a matter of debate.

While previous studies have focused on the proportion of cases won by the respondent as a measure of the impact on states,² this article argues that the types of policies and issue areas implicated in these disputes tell us a great deal about the effect of the regime on policy-making. This is particularly relevant given that investors may use the threat of arbitration to discourage states from enacting certain policies, and cases are often settled out of arbitration. Moreover, recent research has demonstrated that states experience a decline in foreign direct investment (FDI) inflows following an arbitration case, regardless of whether the tribunal rules in favour of the claimant or the respondent.³ Thus, arbitration cases may have an impact on the state, whether or not they win or lose.

This article, based on a larger research project⁴, provides some initial data to fill this gap in the literature: a statistical analysis of political and economic factors that contribute to the likelihood of an investor-state dispute; and a qualitative coding of measures which have resulted in arbitration cases. While there is a fair amount of scholarly work on the determinants of expropriation, we know less about the political and economic conditions under which the broader category of investor-state disputes take place.⁵ Disputes brought to arbitration often involve measures other than outright expropriation, and the conditions under which they occur may be different. Moreover,

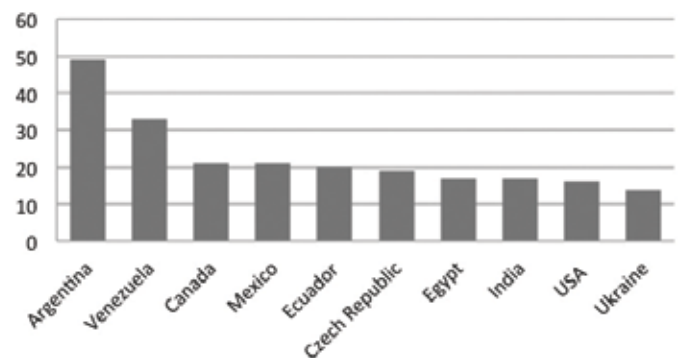
the relatively broad scope of protections found in many IIAs requires a more nuanced understanding of the causes of investor-state disputes under this regime.

In fact, these disputes are testament to the competing pressures globalization places on states. As interstate relations are increasingly legalized, states are bound by numerous international agreements, while at the same time continuing to be beholden to domestic interests. Ultimately, the most straightforward interpretation of these disputes is as instances of changing state preferences, in which states renege on a former commitment to respect the rights of foreign investors. However, this approach in turn assumes that policy-makers are fully aware of the implications of these treaties, and that the measures they pass are purposively anti-investor. Given the vague language of IIAs, and the varying interpretations by arbitration tribunals, it is likely that policymakers do not, at least at the outset, have a high level of awareness of the implications of the regime. This final point brings us to the limits of a quantitative analysis of the determinants of investor-state disputes—qualitative case studies may be necessary to tease out if and how investment concerns are brought into policy making decisions. However, the following provides some initial findings that can guide further research in this area.

Quantitative analysis: The conditions for investor-state disputes

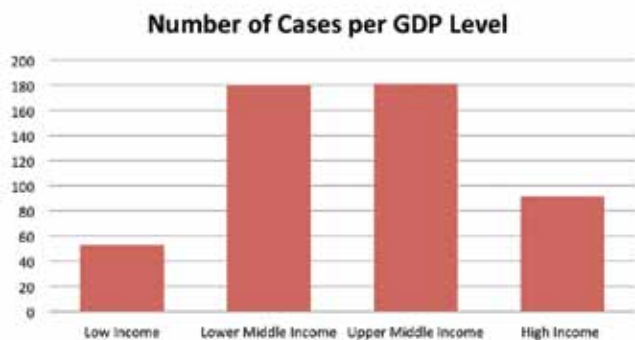
This study is based on a dataset of investor-state disputes from 1990-2012. All countries that have signed an IIA or free trade agreement with an investment chapter allowing for ISDS were included—147 in all. The most frequent respondent states are displayed in the chart below.

Frequent Respondent States



(Source: Own compilation)

These states are a mix of high-, low- and middle-income countries. However, in the entire sample of states that have been involved in at least one dispute, the mean GDP per capita is US\$8,885, which is squarely in the middle income range. The majority of cases involve oil, gas and mining (33 per cent); and electricity and other energy (16 per cent); with construction, telecommunications, finance, and agriculture also appearing among the top ten industries.



(Source: Own compilation)

A statistical analysis was carried out to test the effect of various economic and political variables on the likelihood of an arbitration case being filed in a given year. The incidence of an arbitration case in a given country-year serves as the dependent variable, and the dataset includes 538 arbitration cases. The independent variables and their hypothesized effect (derived from a review of relevant literature) on the likelihood of dispute are provided in the following table:

| Category | Indicator | Hypothesized Effect |
|-----------|--|---------------------|
| Economic | FDI inflows as % of GDP | Negative |
| | Total FDI stock | Positive |
| | GDP/Capita | Negative |
| | Economic crisis ⁶ | Positive |
| | Fuel exports as % GDP | Positive |
| Political | Democracy level ⁷ | Negative |
| | Veto players ⁸ | Negative |
| | Control of corruption | Negative |
| | Transition economy ⁹ | Positive |
| | Length of time incumbent has been in power | Negative |
| | Presidential system | Positive |
| Exposure | Leftist Incumbent ¹⁰ | Positive |
| | Treaties signed | Positive |
| | NAFTA ¹¹ | Positive |
| | Total FDI Stock | Positive |

The variables are grouped into categories of economic, political and exposure-related indicators. The latter refers to the exposure a state has to potential lawsuits, through the overall amount of FDI it hosts, and the number of treaties it has signed.

A panel logistic regression was used to test models based on the groupings of economic, political and exposure related variables.¹² The three models were tested separately, as well as a full model including all the variables. All variables were lagged one year to account for the length of time it takes for an investor to register a case.

Results

The economic variable of interest with the most significant impact on the likelihood of a dispute was simply the amount of overall FDI hosted by the state. As expected, the GDP per capita was negatively correlated with the likelihood of a dispute, but as can be seen from eyeballing the distribution of investor-state disputes, they are heavily concentrated in middle income countries. Also as predicted by the literature, fuel exports as a percentage of GDP was positively though

insignificantly related to the dependent variable. Interestingly, the economic crisis variable was negatively correlated with the likelihood of a dispute, suggesting, as some scholars have noted, that the disciplining effect of the market may induce more investor-friendly behaviour during times of crisis.¹³

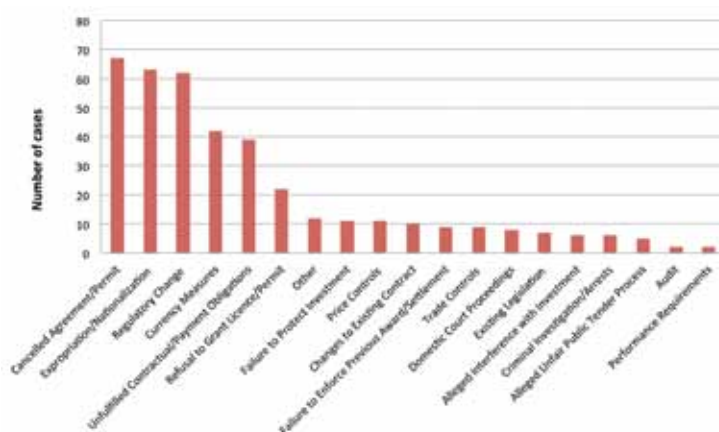
The models using political/institutional variables yielded further interesting results. As predicted, both the measurements for veto players and the control of corruption were negatively correlated with the dependent variable¹⁴, while transition economies were significantly more likely to be involved in investor state disputes. Countries with a presidential system were more likely to be engaged in an investor-state dispute, which may be related to the configuration of veto players in these systems. A leftist executive government positively, though insignificantly increased the likelihood of a dispute. Contrary to the predictions of the bulk of the literature on expropriation, a state's democracy score was positively and significantly associated with the likelihood of an arbitration case, though with only a weak effect. One possible explanation for this result is that democracies attract more FDI and thus have a greater likelihood of being involved in a dispute with an investor.¹⁵

Finally, the measures related to a state's "exposure" to the investment regime—NAFTA membership, number of IIAs signed, and as mentioned above, FDI stock—were all positively associated with the likelihood of a dispute. NAFTA membership had a particularly strong effect, implying that comparatively more investor-state disputes are filed under NAFTA than any other investment treaty even when overall investment levels are controlled for. This suggests that perhaps one of the biggest drivers of investor-state disputes is the investors themselves.

Qualitative analysis: Sources and categories of measures triggering investor-state disputes

Qualitative coding of the measures taken by states that prompted an investor to go to arbitration was also undertaken for 490 investment case.¹⁶ Information about these cases was drawn from a variety of sources, including the International Center for Settlement of Investment Disputes (ICSID) list of pending and concluded cases, the *Investment Arbitration Reporter* news service, and other online collections of case proceedings and awards. The dataset contains ICSID cases as well as those carried out under the rules of other forums. The information collected about the cases includes the industry of the investment; the outcome of the proceedings; the measure taken; and finally "object" and "source" of the measure. The former refers to the whether the measure was directed to a specific investor (for example the denial of an operating permit) or is more general, for example directed at all firms operating in a specific industry (such as the withdrawal of subsidies or the ban of a certain activity). The "source" of the measure refers to whether it was an administrative, legislative or judicial decision.

The results of the coding of the type of measure are displayed in the following chart.



(Source: Own compilation)

Some of these categories may require further elaboration. The category of regulatory change can be further broken down into the following:

- Ban of industrial activity (15 per cent of measures in this category)
 - Includes ban on wind farm expansion; nuclear phase-out; and fracking.
- Ban of specific substance (6 per cent of measures in this category)
- Change to or imposition of new taxes (39 per cent of measures in this category)
- Change to regulatory framework governing a specific industry (40 per cent of measures in this category)
 - Includes plain cigarette packaging; withdrawal of subsidies; pricing of utilities.

The currency measures category represents cases relating to currency devaluations or controls and includes measures taken during the Argentine financial crisis, which make up the majority in the category. Finally the category of failure to protect investment refers to investor claims regarding terrorist attacks; damage caused by protestors; squatters and thieves.

Specific measures, targeted at a single or small group of investors, made up 66 per cent of the measures coded, while 32 per cent were aimed at an entire industry or the general public. Two percent of the measures, corresponding to instances in which the investor claimed that the state failed to protect the investment were coded as “not applicable”.

Eighty-five percent of the measures were administrative decisions, originating either from the executive branch or other organizations affiliated with the state, including regulatory agencies and state-owned businesses. Legislative decisions made up 11 per cent of the measures coded, and 2 per cent were judicial decisions. Again, 2 per cent of the measures were coded as “not applicable” when a lack of action rather than a purposive measure triggered the dispute.

Conclusion

It is clear that the dynamics underlying expropriations play an important part in explaining conflicts under the broader category of investor-state disputes. As is suggested by the statistical analysis, when corruption or unilateral action by the executive are constrained, the likelihood of a dispute decreases. Moreover, transition economies, many of which experience high levels of corruption, are much more likely to be involved in conflicts with investors. However, outright expropriations make up 16 per cent of measures which trigger an arbitration process—far from the majority of all cases. In fact, regulatory changes have motivated investors to go to arbitration as often as expropriations.

Perhaps more telling are the sources and targets of the measures. The overwhelming majority are administrative decisions, with most also targeted at a specific investor. On the one hand this may ease the fears of critics of the investment protection regime—very few of the cases directly involve legislative decision-making. Of course, this cannot be understood to mean that all administrative decisions or targeted measures are divorced from public pressure or are not taken in the public interest. Moreover, the majority of disputes are related to investments in politically sensitive industries—oil, mining and gas; electricity and energy; construction (often of large infrastructure projects); and telecommunications are all generally related to the interests of the broader public. In the extractive industries especially, many decision-making

processes, although undertaken by the bureaucracy, involve substantial public participation during the application stage, and the rejection of projects due at least in part to public pressure has led to a number of cases.¹⁷

The concentration of disputes in middle income countries is also telling. This may be best explained by the fact that these countries host more FDI than the poorest countries, while also having lower levels of administrative capacity than developed countries. However, there may be additional factors at work here: these countries may in some cases be faced with strong domestic pressures that relate directly for FDI. For example, pressure to provide universal service for telecommunications and public utilities has led to the use of price controls as a developmental tool.¹⁸ While countries must treat foreign investors fairly, we also expect them to be responsive to the demands of their citizens. Finding a balance between the two may be difficult, especially if policymakers are unsure of the implications of IIAs, and when the strongest determinants of investor-state disputes appears to simply be the amount of investment hosted by a state.

Author

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Notes

- 1 See, for example, the European Commission's recent document “Incorrect claims about investor-state dispute settlement” <http://trade.ec.europa.eu/doclib/html/151790.htm>
- 2 Susan D Franck, “Development and Outcomes of Investment Treaty Arbitration” (2009): 1–56.
- 3 Todd Allee, Lincoln Hall, and South Wright Street, “Contingent Credibility : The Reputational Effects of Investment Treaty Disputes on Foreign Direct Investment” (2008).
- 4 This article presents the preliminary findings of the author's doctoral thesis. This work expands on the findings in of the large-N study with case studies in Canada, El Salvador and Hungary.
- 5 An exception to this is Nathan W. Freeman, “Domestic Institutions, Capacity Limitations, and Compliance Costs: Host Country Determinants of Investment Treaty Arbitrations, 1987–2007,” *International Interactions* 39, no. 1 (January 2013): 54–78.
- 6 Taken from the dataset on economic crisis by Reinhart and Rogoff . A binary variable that includes: currency crisis, inflation, stock market crisis, sovereign debt crisis and banking crisis.
- 7 As indicated by the Polity IV score, which awards countries a score from -10 (autocracy) to 10 (democracy).
- 8 Refers to the actors, usually within government, whose agreement or consent is required to alter the status quo See: Tsebelis, 2002. Indicator used developed by Witold Jerzy Henisz, “POLCON_2005 Codebook,” 2013.
- 9 State belonging to the former USSR.
- 10 A binary variable provided by the World Bank Database on Political Institutions.
- 11 Originally, other agreements with dispute settlement clauses such as the ECT and CAFTA were included, but had no effect on the dependent variable. They are however included in the variable for number of treaties signed.
- 12 This means that in fact, the dependent variable was a binary variable, coded 1 if at least one case was registered in a given year, and 0 otherwise. While this results in a loss of data for some years in which many cases were filed, it perhaps more representative when the goal is to understand the state's role in investor-state disputes, as one state measure often triggers a number of cases.
- 13 Nathan M. Jensen, Noel P. Johnston, and Chia-yi Lee, *Crisis and Contract Breach : The Domestic and International Determinants of Expropriation* (St Louis, 2013).
- 14 Higher scores are “better” for both variables.
- 15 The correlation between stock of FDI and the states' Polity scores is 0.17.
- 16 Sufficient information was not available for the remaining 48 cases which were included in the statistical analysis.
- 17 For example: *Bilcon of Delaware et al v. Canada*; *St Marys Cement v. Canada*.
- 18 Markus Krajewski, “The Impact of International Investment Agreements on Energy Regulation,” in *European Yearbook of International Economic Law (EYIEL) Vol. 3 (2012)*, ed. Christoph Herrmann and Jörg Philipp Terhechte, vol. 3 (Heidelberg: Springer-Verlag Berlin Heidelberg, 2012), 343–369.

Aron Broches and the Withdrawal of Unilateral Offers of Consent to Investor-State Arbitration

Matthew C. Porterfield

feature 2



During the last decade, a number of States have attempted to limit their exposure to investor-state arbitration under bilateral investment treaties (BITs) and other international investment agreements (IIAs). Several States have terminated BITs as they came up for renewal.¹ The effectiveness of BIT termination, however, is limited by the “survival clauses” that are frequently included in IIAs. These provisions state that even after the treaty is terminated it will continue to apply to investments that were made while the treaty was in force for an additional 10 or 15 years.

A few States—Ecuador, Venezuela and Bolivia²—have also withdrawn their consent to investor-state arbitration under the ICSID Convention³ by denouncing the Convention. Investor-State arbitration, like all arbitration, is predicated on the consent of the parties. In commercial arbitration the consent of both parties is typically provided in a single instrument in the form of an arbitration agreement. In contrast, with investor-State arbitration the State usually provides a unilateral offer of consent to arbitration in an IIA, which the investor “perfects” with its own consent by bringing a claim.⁴ According to Aron Broches, the “principal architect”⁵ of the ICSID Convention (and arguably the entire investor-state arbitration system), by denouncing the Convention, a State withdraws any unilateral offers of consent to arbitration under the Convention and prevents ICSID from asserting jurisdiction over new claims.⁶ Yet as with BIT termination, ICSID denunciation has its limits as a strategy for reducing exposure to investor-State arbitration given that most IIAs provide for alternatives to ICSID, such as the UNCITRAL Arbitration Rules.

Broches's writings, however, suggest an approach for States that are seeking to limit their exposure to investor-state arbitration that would address both the problems of survival clauses and alternatives to ICSID arbitration: withdrawal of unilateral offers of consent to non-ICSID arbitration. As discussed below, this approach would arguably preclude investors from bringing new claims under IIAs that provide for non-ICSID arbitration and that are either still in force or have applicable survival clauses.

State consent to arbitration under the ICSID convention

The investor-State arbitration system has its roots in the ICSID Convention, which still accounts for the majority of investor-State proceedings. The drafters of the Convention intended for it to serve primarily as a mechanism for addressing contractual disputes between foreign investors and host States, pre-dating as it did the first investor-state arbitration clause in a treaty by several years.⁷

The creation of a mechanism through which sovereigns would be subject to international claims by private investors was viewed as a significant departure from existing practice.⁸ Moreover, the issue of foreign investor rights had been the subject of contentious debate in the United Nations General Assembly, leading to the adoption in 1962 of the Resolution on Permanent Sovereignty over Natural Resources.⁹ Operating in this context, Broches, the World Bank's General Counsel at the time and who would later become ICSID's first Secretary-General, suggested that States be given significant flexibility in determining the disputes that they would submit to ICSID's jurisdiction. Broches proposed in an early working paper that the Convention provide for arbitration based on the consent of the parties to a dispute¹⁰ and stressed that the Convention would not involve “compulsory adjudication of disputes.”¹¹ Instead,

[it] would make available to foreign investors and host governments facilities for . . . arbitration of disputes between them. Use of these facilities would be entirely voluntary. No government and no investor would ever be under an obligation to go to . . . arbitration without having consented thereto.¹²

Although Broches conceived of ICSID's jurisdiction from the beginning as being rooted in the consent of States, the relatively low standard he initially proposed for establishing consent proved to be politically problematic. The working paper and a preliminary draft of the Convention would have permitted State consent to be implied under the doctrine of *forum prorogatum* if the State accepted ICSID's jurisdiction over a dispute submitted by an investor.¹³ The *forum prorogatum* provision, however, drew objections during a series of regional consultative meetings on the grounds that it could subject States to inappropriate pressure to accept the Centre's jurisdiction.¹⁴ Accordingly, the Convention in its final form dropped the *forum prorogatum* proposal, requiring instead that both parties explicitly consent in writing to ICSID's jurisdiction over a dispute.¹⁵

Withdrawal of treaty-based offers of consent to ICSID arbitration

Although the written consent of both parties is required under the ICSID Convention, it need not be provided simultaneously or in the same instrument, creating the potential for States to make unilateral offers of consent; for example, through domestic legislation. A question

was raised during the drafting of the Convention in 1965 concerning whether a State could withdraw such a unilateral offer of consent by denouncing the Convention before a claim had been submitted.¹⁶ Broches responded that a unilateral offer—

would not be binding on the State which had made it until it had been accepted by an investor. *If the State withdraws its unilateral statement [of consent] by denouncing the Convention before it has been accepted by any investor, no investor could later bring a claim before the Centre. If, however, the unilateral offer of the State has been accepted before the Denunciation of the Convention, then disputes arising between the State and the investor after the date of denunciation will still be within the jurisdiction of the Centre.*¹⁷

At the first annual meeting of ICSID's Administrative Council in 1967, Broches proposed that BITs provide for investor-State arbitration under the Convention.¹⁸ Over the next few years, States began including unilateral offers of consent to ICSID arbitration in treaties.¹⁹ Broches viewed these treaty-based offers as similarly subject to withdrawal prior to perfection by an investor:

[Investment] treaties evidence the consent of one party only, namely, the host State. Accordingly, until the investor has also signified his consent in writing, the prohibition against unilateral withdrawal of consent does not apply, that is to say, the host State's consent is revocable under the Convention.²⁰

Broches noted that revocation of an offer of consent provided in a treaty's arbitration clause could violate the treaty, potentially provoking the investor's home State to seek a retraction of the withdrawal of consent by the host State. Absent such a retraction, however, an attempt by the investor to institute an investor-state claim would be rejected by ICSID's Secretary-General or would face a jurisdictional objection from the host State if ICSID registered the claim.²¹

Broches's view that a State may avoid investor-state arbitration under a treaty by withdrawing its offer of consent to arbitration prior to its perfection by an investor rests upon the lack of an arbitration agreement establishing privity between the State and the investor. The duty to provide consent to arbitration is owed under international law to the other State party to the treaty, not to all potential investor-claimants. Accordingly, the issue of whether the withdrawal of the offer of consent violated the treaty could only be addressed through State-to-State proceedings.²²

Withdrawal of consent to non-ICSID investor-State arbitration

Broches first published his observations concerning the revocability of treaty-based offers of consent to ICSID arbitration in 1982. Over the next several years, it became an increasingly common practice for investment treaties to contain arbitration clauses that provide for

alternatives to ICSID—such as arbitration under the UNCITRAL rules—in order to accommodate participation in investment treaties by States that were not parties to the ICSID Convention.²³ Broches's analysis of the ability of States to revoke unilateral offers of consent to investor-state arbitration would presumably apply with equal force to these treaties.

Investor-State arbitration requires the consent of the parties to the dispute regardless of which arbitration procedure is employed. Arbitration under the UNCITRAL Rules, for example, is only permitted “[w]here parties have agreed that disputes between them . . . shall be referred to arbitration under the UNCITRAL Arbitration Rules. . . .”²⁴

An investor must always perfect a State's treaty-based offer of consent in order to form an arbitration agreement that will provide the basis for an investor-state proceeding. If the State withdraws an offer of consent to arbitration before it is perfected, an investor cannot subsequently form an arbitration agreement by instituting a claim, regardless of which arbitration rules are invoked (ICSID, UNCITRAL, etc.) or whether the investor is attempting to assert rights under a survival clause or an IIA that is still in force.

As Broches recognized, the home State of the investor could employ whatever State-to-State procedures were available to challenge the legality of the withdrawal of consent. Whether a withdrawal of consent would be held to constitute a breach of the State's obligations would depend on the language of the relevant arbitration clause. Although some IIAs provide firm offers of consent to investor-State arbitration, others merely contemplate that the respondent State may provide its consent to arbitration at some point in the future.²⁵

Given that investment arbitrators are, at least in the first instance,²⁶ judges of their own jurisdiction, it would not be unreasonable to anticipate that some arbitrators may be reluctant to dismiss claims for lack of a valid arbitration agreement. States, however, may find a more receptive audience in domestic courts, where they could raise the absence of a valid arbitration agreement as a basis for opposing the enforcement of an award.²⁷

A State's withdrawal of a unilateral offer of consent to investor-State arbitration provided in an IIA could, of course, leave investors without a forum for asserting the substantive rights provided in the treaty. As the tribunal in *ICS v. Argentina* observed, however,

the default position under public international law is the absence of a forum before which to present claims . . . [a] finding of no jurisdiction should not therefore be treated as a defect in a treaty scheme that runs counter to its object and purpose in providing for substantive investment protection.²⁸

Conclusion

States could create a system of investor-State dispute settlement that would not be dependent on their

continuing consent to arbitration, *i.e.* a system in which international tribunals exercised compulsory jurisdiction over investor-state disputes and investors were directly vested with rights independent of the existence of an arbitration agreement. Thus far, however, they have not done so.

Instead, States continue to rely on the consent-based system that Broches viewed as necessary given the political sensitivity of permitting foreign investors to bring direct claims against sovereigns. This deferential approach to the jurisdiction of tribunals in investor-State proceedings provides States with the option of withdrawing their unilateral offers of consent before they are perfected. If investor-State tribunals were to assert jurisdiction based on withdrawn offers of consent, they would be exercising the type of compulsory jurisdiction that States, as Broches anticipated, have not been willing to confer on them.

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Notes

1 Since 2008, Venezuela, Ecuador, Bolivia, South Africa and Indonesia have each terminated one or more BITs. See United Nations Conference on Trade and Development, *International Investment Policymaking in Transition: Challenges and Opportunities of Treaty Renewal* at 2-3 (June 2013), available at http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d9_en.pdf; International Institute for Sustainable Development, *Indonesia terminates bilateral investment treaty with the Netherlands*, Investment Treaty News—News in Brief (May 14, 2014), available at <http://www.iisd.org/itn/2014/05/14/news-in-brief-15/>.

2 See ICSID News Release, *Venezuela Submits a Notice under Article 71 of the ICSID Convention* (January 26, 2012), available at <http://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=Announcements&pageName=Announcement100>; ICSID News Release, *Ecuador Submits a Notice under Article 71 of the ICSID Convention* (July 9, 2009), available at <https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=NewsReleases&pageName=Announcement20>; ICSID News Release, *Bolivia Submits a Notice under Article 71 of the ICSID Convention* (May 16, 2007), available at <https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=OpenPage&PageType=AnnouncementsFrame&FromPage=NewsReleases&pageName=Announcement3>.

3 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (opened for signature 18 March 1965, entered into force 14 October 1966) ("ICSID Convention"), available at https://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR_English-final.pdf.

4 Almost three-quarters of the investor-state disputes registered by ICSID have been based on consent provided in an IIA. The other cases were based on consent to arbitration provided either in a contract between the investor and the host-State (19%) or in the domestic law of the host-State (8%). *The ICSID Caseload—Statistics* (Issue 2014-1), at 10, available at <https://icsid.worldbank.org/ICSID/FrontServlet?requestType=ICSIDDocRH&actionVal=ShowDocument&CaseLoadStatistics=True&language=English51>.

5 Christoph H. Schreuer, *THE ICSID CONVENTION: A COMMENTARY* at 2 (2d ed. 2009).

6 See ICSID, CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES: DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, Vol. II-2, at 1010 (1968) (remarks of Mr. Broches). See also Christoph H. Schreuer, *THE ICSID CONVENTION: A COMMENTARY*, at 1280 (2d ed. 2009) ("An investor's attempt to accept a standing offer of consent by the host State that may exist under . . . a treaty after receipt of the notice of . . . denunciation . . . would not succeed.") Some commentators, however, contend that an unqualified offer of consent to ICSID arbitration in a treaty remains effective notwithstanding a State's denunciation of the Convention. See, e.g., Emmanuel Gaillard, *The Denunciation of the ICSID Convention*, NEW YORK LAW JOURNAL (June 26, 2007) ("where an unqualified consent exists [in an IIA] . . . the rights and obligations attached to this consent should not be affected by the denunciation of the ICSID Convention."), available at http://www.shearman.com/files/Publication/a4ce241f-83de-445d-a50a-b82ba12f89fc/Presentation/PublicationAttachment/ce3cbe9a-ca49-4eaa-b3f5-d0a26ba0680c/IA_NYLJ%20Denunciation%20ICSID%20Convention_040308_17.pdf.

7 See Agreement on Economic Cooperation between the Government of the Kingdom of the Netherlands and the Government of the Republic of Indonesia, Article 11 (signed at Djakarta, 7 July 1968), 799 U.N.T.S. 14, available at <https://treaties.un.org/doc/Publication/UNTS/Volume%20799/volume-799-I-11386-English.pdf>.

8 See Anne K. Hoffmann, *The Investor's Right to Waive Access to Protection under a Bilateral Investment Treaty*, 22 ICSID Review 69, 76-77 (2007) ("the right of private investors to sue foreign governments . . . was not only not anticipated, it was outright unthinkable for many of the scholars addressing this issue even in the early second half of the [20th] century.")

9 See Andreas F. Lowenfeld, *The ICSID Convention: Origins and Transformation*, 38 Ga. J. Int'l & Comp. L. 47, 48-49 (2009).

10 *Working Paper in the Form of a Draft Convention for the Resolution of Disputes between States and Nationals of Other States* (June 5, 1962), Article IV(1)(1) ("The jurisdiction of the Center . . . shall be based on consent"), in ICSID, CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES: DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, vol. II-1, at 19, 33 (1968) (hereinafter "Working Paper").

11 See *Paper Prepared by the General Counsel and Transmitted to the Members of the Committee of the Whole* (Feb. 18, 1963) in ICSID, CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES: DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, vol. II-1 at 74 (1968).

12 *Id.*

13 See *Working Paper, supra*, Article IV(1)(2) ("The consent of any party to a dispute to the jurisdiction of the Center may be evidenced by . . . the acceptance by such party of the jurisdiction of the Center in respect of a dispute submitted to it by another party.")

14 See Antonio R. Parra, *THE HISTORY OF ICSID* at 59, 71 (2012).

15 See ICSID Convention, Article 25(1) ("The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State . . . and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre") (emphasis added), available at https://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/CRR_English-final.pdf.

16 ICSID, CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES: DOCUMENTS CONCERNING THE ORIGIN AND THE FORMULATION OF THE CONVENTION, vol. II-2, at 1009-1010 (1968).

17 *Id.* at 1010 (emphasis added).

18 See Parra, *supra*, at 114, citing Administrative Council Proceedings, First Annual Meeting (Sept. 25, 1967), para. 11.

19 See Andrew Newcombe & Lluís Paradell, *LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT* at 43-44 (2009).

20 Aron Broches, *Bilateral Investment Protection Treaties and Arbitration of Investment Disputes*, in *THE ART OF ARBITRATION, LIBER AMICORUM PIETER SANDERS* 63, 68-69 (Jan C. Schultz & Albert Jan van den Berg eds., 1982), reprinted in Aron Broches, *SELECTED ESSAYS: WORLD BANK, ICSID, AND OTHER SUBJECTS OF PUBLIC AND PRIVATE INTERNATIONAL LAW* at 447, 453 (1995) (hereinafter "Broches, *Bilateral Investment Treaties*").

21 *Id.*

22 Broches similarly indicated that if a BIT requires a State provide its consent to arbitration at the request of an investor and the State refuses to do so, that refusal could only be challenged in state-to-state proceedings. See *id.* at 449-50.

23 See Parra, *supra*, at 199:

In the first half of the 1980s, as the circle of countries entering into BITs grew to include more non-parties to the ICSID Convention, BITs started to appear with provisions on the settlement of investment disputes referring to other forms of arbitration, mainly arbitration under the ICSID Additional Facility Rules or under the UNCITRAL Arbitration Rules.

24 UNCITRAL Arbitration Rules (2010), Article 1, paragraph 1, available at <http://www.uncitral.org/pdf/english/texts/arbitration/arb-rules-revised/arb-rules-revised-2010-e.pdf>. See also *id.* Article 3(3)(c) (requiring that the claimant identify the relevant arbitration agreement in its notice of arbitration).

25 See Broches, *Bilateral Investment Treaties*, at 448-450. See also *Planet Mining Pty v. Republic of Indonesia, Decision on Jurisdiction*, ICSID Case No. ARB/12/14 and 12/40, para. 198 (Feb. 24, 2014) ("the Tribunal holds that . . . the Australia-Indonesia BIT contains no standing offer to arbitrate Planet's claims before ICSID. Planet is therefore only entitled to resort to ICSID arbitration if Indonesia's consent was given through a further act."), available at <http://www.italaw.com/sites/default/files/case-documents/italaw3104.pdf>.

26 See, e.g., UNCITRAL Arbitration Rules (2010), Article 23(1) ("The arbitral tribunal shall have the power to rule on its own jurisdiction . . .")

27 See Article V(1)(a) of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards ("New York Convention"), June 10, 1958, 21 U.S.T. 2517, 330 U.N.T.S. 3 ("Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked. . . if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that . . . the [arbitration] agreement is not valid . . ."), available at http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/XXI_1_e.pdf.

28 *ICS Inspection and Control Services Limited v. The Argentine Republic, Award on Jurisdiction*, UNCITRAL, PCA Case No. 2010-09, para. 281 (Feb. 10, 2012), available at <http://italaw.com/sites/default/files/case-documents/ita0416.pdf>.

Opening the Door to Foreign Investment? An Analysis of Bolivia's New Investment Promotion Law

Martin Dietrich Brauch

feature 3



On April 4, 2014, Bolivian President Evo Morales promulgated a law establishing the general legal and institutional framework to promote domestic and foreign investment in Bolivia, while contributing to socio-economic development. Enacting an investment promotion law is in line with the international trend to reform domestic regimes considering broader policy objectives, as reflected in the Investment Policy Framework for Sustainable Development published in 2012 by the United Nations Conference on Trade and Development (UNCTAD), and with Bolivia's revised investment policy. This note provides an overview and analysis of the main features of Bolivia's new law, within the context of the country's investment law and policy, and international trends.

From privatization to renationalization

Net foreign direct investment (FDI) inflows to Bolivia went from over US\$1 billion in the late 1990s, at the end of the wave of privatizations, to a negative US\$223 million in 2005, with investors leaving the country for fear of renationalizations. Despite the nationalizations that did follow and other steps taken by the government to reform its investment policy, FDI inflows to Bolivia have steadily increased, reaching an unprecedented peak of US\$1.75 billion in 2013 (CEPALSTAT, 2014).

On May 1, 2006, his 100th day in office, President Morales (reelected in 2009 for a second term to end in 2015) renationalized the oil and gas production chain. Other nationalizations followed in the energy, mining and telecommunications sectors (Bonneyfroy Miralles, 2014).

In 2007 Bolivia became the first State to withdraw from the convention establishing the International Centre for Settlement of Investment Disputes (ICSID), arguing that the widely-used forum for investor-State dispute settlement was biased towards investors (Diaz Balbuena, 2014).

In line with this policy, the 2009 Bolivian Constitution established that domestic investment has priority over foreign investment, and that foreign investors may not be treated more favourably than domestic investors. It subjects foreign investment to Bolivian jurisdiction, laws and authorities exclusively, and rejects diplomatic complaints as a means to obtain more favourable treatment. It appears unclear whether disputes would

nevertheless be permitted to be settled at the international level the international level, for example, in regional forums. Also of note, the Constitution rejects international arbitration as a means to settle disputes with foreign investors in the oil and gas sector.

Accordingly, the Bolivian Government launched a diplomatic task force to review its bilateral investment treaties (BITs), following the constitutional mandate to denounce and, if necessary, renegotiate all treaties that were contrary to the Constitution (AFP, 2010). According to a task force member, the new BITs would protect the interests of the people; balance public and social interests with private property and profits; account for indigenous, social, human and environmental rights; and promote socio-economic development (La Razón, 2011).

According to a May 2014 interview by Walter Clarems Endara Vera, Bolivian Vice-Minister of Foreign Trade and Integration, in 2006 Bolivia started to systematically refuse to renew every BIT that reached its expiration date. On May 6, 2013 the country collectively denounced all its remaining BITs (Orellana López & McDonagh, 2014).

As Bolivia denounced its BITs, it also advanced proposals to reform international dispute settlement in investment issues. The government has highlighted the need to overcome existing deficiencies in investor-State dispute settlement under investment treaties, including the one-way route of investment arbitration (in that only investors may initiate proceedings against a State), the lack of public access and transparency, the presumption of culpability against respondents, and the small universe of not necessarily impartial arbitrators (La Razón, 2011; ABI, 2014).

Overview and analysis of the investment promotion law

The latest development in restructuring Bolivia's investment regime was the promulgation of Law No. 516, the investment promotion law (*Ley de Promoción de Inversiones*—LPI). Resulting from a drafting process that included consultations with domestic private sector and diplomatic representatives, the law consolidates principles, protections, conditions and (to a lesser extent) incentives regarding domestic and foreign investment.

Principles (*Article 3*)

Sovereignty and dignity are the first principles mentioned by the LPI, which highlights the State's role in conducting social and economic planning, directing the economy and controlling its strategic sectors, to promote development, eliminate poverty and reduce economic, social and regional inequalities. "Strategic sectors" can be understood as those listed as strategic in the Constitution, including minerals, hydrocarbons, the electromagnetic spectrum, genetic resources, and water and energy sources (Constitution, Art. 348 (I) and (II)).

Other principles that must guide the investor-State relationship are the development of non-traditional sectors, industrialization, independence, mutual respect, equity, legal certainty and transparency. In addition, the LPI replicates the constitutional principle of prioritizing domestic over foreign investment, as a mechanism to strengthen the domestic market. Although the law does

not directly refer to sustainable development, it enlists the principle that investments “must guarantee the integral development of the activity in harmony and equilibrium with the Mother Earth, ensuring the sustainability of biodiversity.”

Treatment of investments

The LPI determines that the Ministry of Development Planning (*Ministerio de Planificación del Desarrollo—MPD*) will orient investments towards activities that promote economic and social development and create jobs (Art. 5(I)).

The State reserves itself the exclusive right to develop economic activities in strategic sectors (Arts. 6(I) and (II)). Only subject to the rights granted by the State may private investors develop economic activities in strategic sectors (Art. 6(III)). In case of a “mixed investment,” in which the State operates in association with a private party (whether domestic or foreign), the State must be a majority owner, with the right to control and direct the investment (Art. 16).

Apart from the protection of strategic sectors, the law does not restrict investment in any other economic sector, as long as they respect the State’s economic planning role and comply with Bolivian law (Art. 5(II)).

In short, the law formalizes and publicizes Bolivia’s strategic investment policy priorities, presents the role intended for private and foreign investment in the country’s development strategy and priorities, and sends a signal to investors and other relevant stakeholders, namely: investors are welcome, as long as they play by the rules dictated by the State, particularly in strategic sectors.

Conditions for investment

In a positive indication of Bolivia’s intent to prioritize investment with the potential for creating jobs and transferring skills, technology and know-how, the law demands that private investments contribute to economic and social development and strengthen economic independence (Art. 7). For example, technology transfers must factor in at least one of the following elements: building the capacity of Bolivian personnel, transferring cutting-edge equipment and machinery to Bolivian entities, or developing applied research that improves industrial processes or contributes to public well-being (Art. 14).

Investor obligations and performance requirements (Article 11)

The LPI provides that all investments must comply with domestic laws and regulations on labour, tax, customs, environmental and other matters. This is an important recognition, emphasized recently by UNCTAD, that “regulatory standards should not be lowered as a means to attract investment, or to compete for investment in a ‘regulatory race to the bottom’” (UNCTAD, 2012, Guideline 2.4.13).

However, the LPI could have gone further by endorsing or even incorporating international codes of conduct for foreign investors and standards of responsible investment; corporate accounting, disclosure and reporting;

governance; and social responsibility.

The LPI does not explicitly mention that investment must comply with internationally recognized core labour standards, such as the protections under the relevant conventions of the International Labour Organization (ILO). Neither does it refer to environmental impact assessments (EIA) requirements, environmental licensing procedures or international standards for environmental protection and against environmental dumping. However, a more in-depth analysis of Bolivian law would be required to determine whether these aspects are already covered by specific environmental and labour laws and regulations.

Freedom of transfers

The LPI guarantees that foreign investors may freely transfer abroad their net profits, the capital resulting from the liquidation of companies or from the sale of shares, dispute settlement awards, among other amounts, in freely convertible currency. Financial transfers to or out of Bolivia must be channelled through the Bolivian financial system, as well as registered with the country’s Central Bank, a requirement that did not exist under Law No. 1182 of 1990, the previous investment law. The LPI subjects the transfer to the investor’s compliance with the investor’s tax and other obligations under Bolivian law (Arts. 11, 13 and 15). Transfers must also be in line with the regulation on transfer prices, to be drafted by the Ministry of Economy and Public Finances within 90 days of the publication of the LPI (Art. 11(b) and First Transitory Provision).

However, missing from the LPI are provisions on the possibility to restrict transfers in cases of balance of payment and other macroeconomic crises, in recognition of the potential need for such prudential measures and to safeguard Bolivia’s right to control capital flows to mitigate such crises. For example, the LPI could have expressly reserved Bolivia’s right to restrict transfers in accordance with its laws, mentioning an illustrative list of restriction scenarios, such as the protection of the rights of creditors, criminal offences, compliance with judicial orders or administrative decisions, and the prevention of money laundering.

Investment incentives (Articles 21 to 23)

The LPI outlines very broadly how Bolivia will grant *general incentives*, applicable to all types of investment projects, and *specific incentives*, targeted to *preferential investments*, defined as those in strategic sectors, such as natural resources or activities that contribute to a change in the production matrix. The law defines incentives as fiscal or financial benefits or advantages granted by the State on a temporary basis (1 to 20 years) and other investment promotion policies, and may include tax reductions or exemptions and production stimuli.

The ministry that oversees the sector of a particular investment may submit a request for an incentive to the MPD, which evaluates the project, decides whether it qualifies as a preferential investment (in the case of specific incentives), and issues a recommendation to the Council of Ministers on whether the incentive should be granted. Upon request by a sectoral ministry, the MPD may also recommend suspending or cancelling an incentive in case of investor noncompliance with contractual obligations concerning the investment.

To be eligible to receive specific incentives, a project must factor in technology transfer and job creation, and must fall under one of the following categories (Art. 22):

- a) Value-added generating activities in the oil and gas, mining, energy or transportation sector;
- b) Value-added generating activities in the tourism, agroindustry or textile sector, with a high potential for innovation and human resource development; or
- c) Activities generating development poles and reducing regional socio-economic inequalities.

By allowing the government to condition incentives to specific obligations, the LPI explicitly provides for the use of performance requirements, which may help to promote the positive developmental contribution of investment.

Notably, requests for specific incentives to Bolivian investors have priority over requests for incentives to foreign investors in like circumstances (Art. 22(IV)). This discrimination is based on the country's development strategies, which prioritize domestic over foreign investment as a means to strengthen the domestic market. Specific measures prioritizing Bolivian vis-à-vis foreign investors in granting incentives to investments in the tourism sector might be considered to breach Bolivia's national treatment commitment for that sector under the World Trade Organization's General Agreement on Trade in Services (GATS). However, given that the LPI is vague on the criteria for specific incentives, assessing GATS compliance will depend on how each particular measure is designed.

Positively, the law demands that ministries periodically assess whether investments that received general or specific incentives comply with the conditions under which the incentives were granted, based on expected economic results, and report on their assessment to the MPD (Art. 23).

However, the LPI lacks clear criteria for determining eligibility for incentives. The Organisation for Economic Co-operation and Development (OECD), UNCTAD and the World Bank, amongst others, have highlighted the importance of pre-determined, uniform, objective, clear and transparent criteria for granting investment incentives, for example, in terms of long-term costs and benefits (OECD, 2006; IC-WBG, 2010; UNCTAD, 2012, Guideline 2.4.14). While the sectoral ministries are responsible for monitoring the effectiveness of investments in achieving the desired objectives and their compliance with contract-based performance requirements, the LPI does not clarify how deeply or how often monitoring and reporting must occur. Furthermore, to the exception of the 20-year limit to incentives, no phase-out period seems to be embedded into the incentive structures, to promote self-sustainability and avoid granting incentives to non-viable investments. The implementing legislation should deal with these issues.

Investment promotion (Articles 24 and 25)

The MPD is mandated to promote investment within the framework of the LPI. It may request information from the sectoral ministries on preferential investment projects they have identified, on the monitoring of investments and on the incentives granted to projects in their respective sectors; it may also request investment-related information to any private or public entity. It must

evaluate the administrative procedures for establishing investments, and, where applicable, recommend their simplification. It may also recommend investment promotion laws and policies to the Council of Ministers.

Under the LPI, the MPD is in charge of promoting a culture of investment within the government. It is in a position to interact on investment matters with regulatory agencies (such as the Central Bank of Bolivia), and to bring cross-ministerial issues (facing the different sectoral ministries) to a high level of government (the Council of Ministers). However, its mandate could have been expanded or a new entity could be created with the mandate of an investment promotion agency (IPA), with explicit responsibility and accountability to assist investors in establishing, operating and developing their investments, in light of national policy objectives. The role of an IPA is wider than MPD's as it stands, in that it would be intended to be "the prime interface between Government and investors," and include functions such as "image building, targeting, facilitation, aftercare and advocacy" (UNCTAD, 2012, Guidelines 2.4.1 to 2.4.8).

However, the major disadvantages of the MPD's investment promotion mandate are the potential conflicts of interest arising from the MPD's role in monitoring investments and assessing their eligibility to incentives. Concentrating promotion and regulatory functions in the same entity is not desirable, as it could create opportunities for interference with investor affairs, rent-seeking behaviour and market distortions (IC-WBG, 2010). Granting incentives "should be the responsibility of an independent entity or ministry that does not have conflicting objectives or performance targets for investment attraction" (UNCTAD, 2012, Guideline 2.4.12).

Guidance on BIT negotiations

The LPI provides guidance to the (re)negotiation of BITs: all of them must now conform not only to the Constitution, but also to the LPI (First Additional Provision).

According to Vice-Minister Endara Vera, when Bolivia denounced its BITs, it invited the countries to negotiate new agreements once the LPI was promulgated. He stressed that Bolivia's new model BIT would focus more on investment promotion, as investment protection is already covered in both the Constitution and the LPI (Orellana López & McDonagh, 2014).

Dispute settlement in the LPI and the new conciliation and arbitration law

The LPI states that "disputes arising from the relationships between investors shall be settled in the manner and conditions established under laws and regulations in force" (Art. 26).

While the law is vague on dispute settlement, it mandates the Bolivian Ministry of Justice and Office of the Attorney-General to draft a new law on conciliation and arbitration within 90 days from the promulgation of the LPI (Third Transitory Provision), that is, by early July 2014. The new law is to include specific regulations for the settlement of investment disputes and must be in line with the LPI. Disputes arising before the new law is enacted are subject to Law No. 1770 of March 10, 1997, the current arbitration and conciliation law (*Ley de Arbitraje y Conciliación*).

For two days in early June, a working group formed by officials from the two bodies mandated with the drafting of the new law met to analyze proposed language, discuss relevant aspects and consolidate a first draft. According to Jorge Mercado, Director-General of Constitutional Development of the Ministry of Justice, the work has centered so far on creating a culture of peace in dispute settlement, generating legal and institutional conditions for their accessibility to the population, and ensuring compatibility of the new conciliation and arbitration law with international law (Bolivian Ministry of Justice, 2014). Moreover, according to the Office of the Attorney-General, the new law will reflect the Constitution, allowing international arbitration between private investors, but not in disputes involving the State or the strategic sectors under its control (Paredes, 2014).

Bolivian perceptions regarding the LPI

The LPI is perceived by critics to reflect the economic model established in the Constitution, in which the State directs economic planning and controls investment in strategic sectors, such as oil and gas. With its focus on the aspects of State control and regulation, the law is seen as failing to create clear and precise tax and other incentives for sectors not considered strategic, such as agriculture, and for small and medium enterprises (Azcuí, 2014; FEPC, 2014).

Economist Armando Méndez, former president of the Central Bank of Bolivia, argued that the law will hinder foreign investment: “The spirit of this law presupposes that foreign investors are desperate to enter Bolivia and don’t know the areas in which to invest, but that the Bolivian State does. Big and serious foreign investment will not come to Bolivia as a consequence of this law” (FEPC, 2014).

Others highlight that the effectiveness of the law depends on further legislation, such as the LPI regulation and the new conciliation and arbitration law. Some express doubts as to whether Bolivian courts could equitably settle disputes, such as those involving expropriation, and whether foreign investors would have sufficient incentives and legal certainty if disputes are to be settled in Bolivia (Chipana, 2013; Azcuí, 2014; Ochoa Urioste, 2014).

Concluding remarks

Along with the restructuring of its investment treaties, Bolivia took a major step in redesigning its domestic legal framework on investment by adopting the LPI. The law’s effectiveness in promoting foreign investment while ensuring the resulting socio-economic benefits will largely depend on further legislation to address uncertainties left by the LPI. The implementing legislation should detail how and what types of incentives will be granted. It should also provide how the MPD will be insulated from political pressures and corruption as it reconciles its investment promotion and regulatory functions. Importantly, the new conciliation and arbitration law should establish a clear approach for investment disputes. Ultimately, effectiveness will also depend on how closely and transparently the government and civil society will engage in foreign investment processes, and on how sectoral legislation will be implemented, such as the Law No. 535 of 2014 on Mining and Metallurgy (*Ley de Minería y Metalurgia*).

Finally, Bolivia’s criticism of the current dispute settlement system and the quest for alternatives are worthy of

note. The country’s bold stance on the matter—such as its withdrawal from ICSID and the non-renewal and renegotiation of its BITs—provides space for new thinking. Further developments at the national level, including in the context of dispute settlement options, could place the Bolivian Government in a prominent role as a proponent of alternatives to existing investor-State mechanisms.

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news in brief

UNCITRAL launches new transparency registry

The European Commission is being asked why investor-state arbitration provisions should be included in the Transatlantic Trade and Investment Partnership (TTIP), which has been under negotiation between the United States and European Union since July 2013.

On July 11th, Germany's upper parliament passed a resolution that highlights the "substantial risks" of investment arbitration, and asks the European Commission to explain why it would be necessary in the TTIP.

A group of 120 academics has also voiced its concern in a joint statement released in July 2014.¹ The statement takes aim at a recent online consultation organized by the Commission in which it invited the public to comment on its approach to investment protection and investor-state dispute settlement in the TTIP.

The group calls the consultation document "an extraordinary text," containing on the one hand "fierce ... criticism of the international investment treaty arbitration regime" while simultaneously seeming "content to entrust these same actors the vital constitutional task of weighing and balancing the right to regulate of sovereign states and the property rights of foreign investors."

In line with the German parliament, the academics ask the question: "why consider including investor-state arbitration in the TTIP at all?"

The group points out that investor-state arbitration was originally developed to protect foreign investment in countries with weak legal and judicial systems. But "it is difficult to argue realistically that investors have cause to worry about domestic legal systems on either side of the Atlantic."

Currently, nine EU member states have bilateral investment treaties with the US. As such, investment protection and arbitration provisions in the TTIP would add coverage to an additional 19 member states.

UNCITRAL approves draft convention on transparency

The United Nations Commission on International Trade Law (UNCITRAL) has approved a draft convention on transparency in treaty-based investor-state arbitration.

The draft convention comes on the heels of a package of rules agreed in July last year that aim to make investor-state arbitration more transparent. However, those rules will apply on a default basis only to UNCITRAL investor-state arbitrations conducted under investment treaties concluded after the new rules came into effect on April 1, 2014.

The new rules on transparency will only apply to treaties concluded before that date if the disputing parties or treaty parties agree on a case by case basis. As the UNCITRAL secretariat explains, the "purpose of the convention on transparency is to provide a mechanism for the application of the Rules on Transparency to arbitration cases arising under the almost 3,000 investment treaties concluded before 1 April 2014.

The draft convention will now be submitted to the United Nations General Assembly for final consideration and adoption at its 69th session this Fall.

Update on Renco Group vs. Peru: Renco files memorial on liability

On February 20, 2014, the U.S. investor The Renco Group, Inc. filed with ICSID a memorial on liability in arbitration proceedings against Peru under UNCITRAL rules.²

A Renco-led consortium acquired from Peru in 1997 the heavily polluted smelting and refining complex of La Oroya. The investor relied on assurances that the Peruvian Government would remediate existing soil contamination and assume liability for third-party claims for environmental damage.

A total of 22 personal injury lawsuits have been initiated on behalf of about 1,000 Peruvian citizens residing in the town of La Oroya, who allege harms arising from the operation of the complex. The lawsuits were consolidated in a U.S. federal court in St. Louis, Missouri. Renco initiated arbitration claiming that Peru, by refusing to honour its legal and contractual commitment to assume liability for the lawsuits and by subsequently adopting a "pattern of grossly arbitrary and unfair treatment" of the investor, violated the United States-Peru Trade Promotion Agreement (TPA).

In its memorial on liability, Renco first describes at length the factual background to the dispute, and affirms the tribunal's jurisdiction over the investor's treaty claim. It then elaborates on the arguments that Peru's conduct violated the TPA provisions on fair and equitable treatment (FET) (Article 10.5(1)) and national treatment (Article 10.3). Renco finally argues that Peru caused it to lose control over its investment, indirectly expropriating it (Article 10.7).

Accordingly, the investor's requests for relief include declarations that Peru breached its treaty obligations and expropriated Renco's investments. Renco requests compensation for material damages, but leaves their quantification to be determined in the course of the proceedings. It also requests an award of all costs incurred with the St. Louis lawsuits and with the arbitration proceeding itself.

An interesting claim, mentioned in the requests for relief but nowhere else in the memorials, is that for "compensation for moral damages arising from harm to Claimant's reputation," which Renco qualified as "a part of reparation of an international wrong as clearly established under the International Law Commission's Articles on State Responsibility Articles 31, 36 and 37" (paragraph 413).

According to the tribunal's Procedural Order No. 1 of August 22, 2013, assuming Peru has not raised an objection as a preliminary question under Article 10.20(4) of the TPA, Peru's counter-memorial on liability, including any counterclaims or jurisdictional objections, will be due on August 21, 2014.

Notes

¹ Statement of Concern about Planned Provisions on Investment Protection and Investor-State Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership (TTIP), http://www.kent.ac.uk/law/isds_treaty_consultation.html

² *The Renco Group, Inc. v. The Republic of Peru*, ICSID Case No. UNCT/13/1, Claimant's memorial on liability

awards & decisions

Majority clears Peru of any wrongdoing in relation to close down of French-owned bank; dissenting arbitrator says that majority misconstrued facts and law

Renée Rose Levy de Levi v. Republic of Peru, ICSID Case No. ARB/10/17, Award and Dissenting Opinion
Diana Rosert

A majority has rejected a claim by *Renée Rose Levy*, a French investor in the Peruvian banking sector, who reportedly sought US\$7 billion in damages.¹

In an award dated February 26, 2014, the tribunal established jurisdiction, but was divided over the merits of the claimant's allegations. While two arbitrators—Rodrigo Oreamuno and Bernard Hanotiau—found no wrongdoing by Peru, the third arbitrator strongly disagreed with the majority decision. Joaquin Morales Godoy, the claimant's nominee, considered that the tribunal should have rendered a merits and damages award in favour of Ms. Levy.

An annulment proceeding was registered on May 20, 2014 at Ms. Levy's request. Meanwhile, US\$50 billion are said to be at stake in another pending ICSID proceeding that involves the same claimant.²

Background

Ms. Levy alleged that Peru and its state organs subjected Banco Nuevo Mundo (BNM), a French-owned bank in Peru in which she held shares, to arbitrary and illegal treatment that eventually involved the liquidation of the bank and amounted to indirect expropriation. Ms. Levy claimed that Peru's acts and omissions violated fair and equitable treatment (FET), full protection and security and national treatment obligations stipulated in the France-Peru BIT.

The dispute revolved around an emergency regime for financial institutions put in place by Peru in 2000 to facilitate the restructuring of the banking sector through interventions by an oversight agency for banking, SBS. It was undisputed that BNM was subjected to this regime, pronounced insolvent and dissolved. In essence, the claimant argued that Peru, acting through SBS, caused BNM's bankruptcy instead of helping the bank to overcome temporary illiquidity.

The majority came to the conclusion that the bank's bad accounting and management practices, which it deemed to be in breach of Peru's banking regulations, were the actual reason for BNM's misfortune and that the state agency's actions were justified. In his dissenting opinion, the third arbitrator stated that his "colleagues have construed the facts and the law to dismiss Claimant's complaint" and that the majority's legal analysis was "inaccurate and inconsistent."

Tribunal confirms French nationality and other jurisdictional requirements

Peru pleaded for the tribunal to dismiss jurisdiction, arguing that Ms. Levy acquired her shares in BNM from her father at a time when the bank was already insolvent and allegedly without value. Peru also pointed out that the claimant held no interest in the bank when the actions in dispute took place. The respondent alleged that the transfer of rights from father to daughter constituted "abuse of process," arguing that its sole purpose was to "manufacture" jurisdiction over the dispute. According to the respondent, the tribunal would infringe upon the discretion of Peru and its regulatory agency in enacting banking laws and regulations if it were to assume jurisdiction.

The tribunal rejected all of the Peru's jurisdictional objections, confirming that the Levy family's investment in BNM was in

accordance with requirements set out in the BIT and the ICSID Convention. It determined that the claimant was a national of France and that the ICSID Convention, as well as the BIT, protected indirect minority interests such as Ms. Levy's. The tribunal stated that "shares may be assigned at any time with no effect on the rights of the assignee." It added that it was irrelevant whether the claimant had paid for the transfer of rights and that the insolvency did not "in itself" turn the investment valueless.

However, the tribunal decided that Ms. Levy had not proven that she was allowed to represent BNM in the proceedings and, therefore, only Ms. Levy could be accepted as a claimant, not BNM. The tribunal further determined that the respondent had not substantiated bad faith on the part of the claimant or that the transfer was undertaken to create jurisdiction. The tribunal concluded by stating that it was not precluded from examining state actions or actions of state organs in light of international law standards even if the respondent stated that these acts complied with national laws.

Majority finds no breach of fair and equitable treatment

Ms. Levy asserted that Peru violated the investor's legitimate expectations and failed to guarantee legal stability, while also acting in a discriminatory and arbitrary manner. The majority ruled that Peru did not breach the fair and equitable standard with regard to any of the claimant's allegations; the third arbitrator disagreed with this conclusion.

The claimant founded its legitimate expectations on a 1992 operating license issued by SBS to BNM. However, in the opinion of the majority, the claimant was "wrong" in assuming that this created legitimate expectations of return on investment. The majority considered that return on investment rested on the ability of BNM's management.

The majority then rejected the claimant's assertion that Peru lacked transparency when it enacted the emergency regime, because BNM was not invited to alleged "consultations" between Peru and major banks. The majority explained that the decree was published in Peru's official gazette a day after the said meeting and the latter therefore served merely to inform but not consult the largest banks. In addition, it remarked that Peru was under no obligation to involve stakeholders in its regulatory activity.

The claimant also complained that "abrupt and disproportionate" withdrawals of state-owned companies' funds from BNM destabilized it and that the Ministry of Economy and Finance abstained from measures to "neutralize" these withdrawals. Rather, the majority considered that the events and their impact demonstrated the failure of the bank—not of the respondent—and identified several occasions in which SBS informed the bank about vulnerabilities in this respect and recommended risk mitigation. Ms. Levy further criticized SBS for failing to take action when false rumors about BNM's financial situation endangered the bank. However, the majority concluded that SBS was not guilty of negligence, because a financial panic was "very difficult to control," and SBS had only limited possibilities at its disposal and they came with the risk of adverse effects.

With regard to the refusal of Peru's Central Reserve Bank (BCR) to give BNM a temporary loan, the majority held that no "absolute certainty" of approval could have been expected, particularly because it was considered "evident" that BNM lacked sufficient collateral. Furthermore, Ms. Levy alleged that the state agency's intervention impaired BNM's loan portfolio. However, the majority determined that SBS actions were in order and the claimant's expectations were unsubstantiated

given BNM's accounting irregularities and million dollar losses reported in SBS inspection reports and an audit report by PwC. The majority also noted that SBS was eventually able to recover about US\$161 million "for the benefit of BNM's depositors and creditors" rather spoke in favour of the respondent's intervention in SBS.

While the claimant saw the zero valuation of BNM's equity as a coercion attempt by SBS, the majority confirmed that SBS was empowered to determine the real capital value of BNM, and no indications of arbitrary or illegal practice had been demonstrated. It then explained that the banking laws required that a bank had to be liquidated following an intervention by SBS. The majority recalled that SBS's decision to dissolve BNM was based on an audit by PwC that supported the existence of insolvency and was thus justified. The majority inferred that the liquidation of the bank could not have been a threat, since in any event BNM would have been liquidated so as to comply with banking laws. Overall, the actions of SBS could not be described as taken in bad faith, the majority determined.

The majority also dismissed the accusation that SBS disregarded domestic judicial decisions and thereby failed to guarantee legal stability, stating that the chain of events suggested by Ms. Levy was "unsound," since some events allegedly in contempt with court rulings occurred before such rulings were even rendered.

Dissenting opinion finds Peru liable for FET breach

While disagreeing with the majority's decision in all respects, the third arbitrator focused his analysis on Peru's violations of the FET standard, which he deemed to have occurred.

For example, he considered that the non-invitation of BNM to Peru's meeting with banks spurred a "loss of confidence" in BNM and resulted in reduced interbank lending by the other invited banks. In his opinion, this was "more than a mistake by the State," because it had serious repercussion for BNM. With regard to withdrawals of public deposits, he came to the conclusion that through its actions and omissions "the State aggravated BNM's illiquidity situation." He also contested that the fear of adverse effects was a valid excuse for SBS's inaction in the face of a financial panic. Furthermore, Mr. Godoy believed that it was "certain" that the BCR loan would be approved, since BNM had provided sufficient collateral. He criticized that BCR did not provide other—in other words 'the real'—reasons for the rejection of the loan, which manifested a violation of the investor's legitimate expectations.

He also emphasized that SBS's actions related to the intervention and the dissolution of BNM "do not meet the minimum requirements of proportionality, reasonability, and predictability." In his opinion, the recovery of some US\$161 million cast doubt on the respondent's assertion that the bank was insolvent; he suggested that this even disproved the insolvency thesis. The dissenting arbitrator saw it as proven that SBS was responsible for an "arbitrary act" which caused BNM's losses and created an "insolvency situation that actually did not exist." Moreover, he opined that the majority showed "unawareness" of Peruvian banking law, because the co-arbitrators failed to see that the emergency regime constituted a substantial change in the legal framework, for instance suspending rehabilitation proceedings for banks by shareholders and creditors available under previously applicable banking law. He therefore considered the emergency regime to be contrary to the claimant's legitimate expectations. Finally, as concerned legal stability, Mr. Godoy determined that SBS had violated some court orders and therefore "infringed" upon the standard.

Full protection and security: majority sees no denial of justice

Ms. Levy contended that she was denied justice because no administrative remedies existed against some of SBS's measures. She also alleged that SBS disobeyed court judgments—a claim that the majority had already dealt with and dismissed in the FET context.

At the outset, the majority agreed with Ms. Levy that the full protection and security standard went beyond the protection of physical security, and also encompassed investor rights more generally. Yet, the majority rejected this claim, finding that the "Peruvian judicial system does provide remedies to protect the rights of persons subject to its jurisdiction in this area." It explained that although administrative remedies did not exist, BNM shareholders submitted various claims against SBS to domestic courts and that judgments were delivered in those cases. As such, the majority concluded that the claimant had access to judicial remedies and "received due process."

The majority also found that the claimant's allegations concerning a 2006 court decision in favour of SBS—that it was arbitrary, ignored the arguments of BNM shareholders and manifested the government's interference in judicial decision-making—were unjustified.

Majority finds lack of evidence to support a breach of national treatment

The claimant identified specific banks and brought examples of government action towards them, which in its view evidenced less favorable treatment for BNM. The majority decided that before it could determine whether other banks were treated more favorably, it first needed to assess whether "like circumstances" existed between BNM and the banks that the claimant suggested for the comparison. The majority considered that being a bank was not by itself a sufficient criterion for comparability, and that the "segment [of a bank] and the number of individuals affected, its market share, and other similar factors" needed to be taken into account.

The majority deemed that in terms of loans and deposits BNM was not comparable to the second largest bank of Peru; neither was it comparable to a bank that had a similar market share, but affected a larger group of individual depositors as opposed to corporate depositors.

Ultimately, the majority rejected the claimant's allegation with regard to national treatment, considering it impossible to verify whether the treatment afforded to other banks was "different" and if so, why it was different. The majority was inclined to believe that "when there was a different treatment, this was due to the existence of justifiable circumstances," because in its view insufficient evidence existed to prove otherwise.

In contrast, the claimant's appointee, Mr. Godoy, was convinced that the majority's conclusion that the other banks were not comparable was false. In his opinion, the allegation that Peru breached national treatment was "appropriate."

Majority considers allegation of indirect expropriation "not true"

Based on the same facts, Ms. Levy claimed that the actions of SBS amounted to "creeping expropriation," that the expropriation lacked a public interest or necessity purpose and that Peru should pay compensation for damages. Ms. Levy also asked the tribunal to assess the proportionality between Peru's intent and effects of the interference on the investor's legitimate expectations.

However, the majority ruled that the intervention into BNM and its dissolution constituted “legitimate acts of ‘police power’” and were not an expropriation. In the majority’s opinion, Peru’s intention was to help rather than to harm BNM, whereas it attributed the responsibility for the bank’s collapse to “bad banking practices” and negligence on the part of BNM managers. Contrary to this, the dissenting arbitrator found that it was solely due to the acts of the state and state organs that the claimant incurred damages, because BNM was not insolvent to begin with.

Mr. Godoy stated that the tribunal should have found Peru liable for treaty breaches and made an award on damages.

All claims for damages denied; full arbitration costs allocated to the claimant

Since none of the claimant’s allegations had been upheld, the majority also rejected all claims for damages. It decided that the claimant should bear its own costs as well as the full costs for ICSID proceedings and arbitrator fees. The majority reasoned that this cost allocation was “fair and appropriate” in light of the finding that the bank was itself responsible for the bankruptcy and that bank officials had been negligent. The third arbitrator, however, saw no reason why Ms. Levy should pay the entire arbitration costs, emphasizing that the claimant had won on jurisdiction.

The tribunal was composed of Rodrigo Oreamuno (presiding arbitrator), Joaquin Morales Godoy (claimant’s nominee) and Bernard Hanotiau (respondent’s nominee).

The award is available at <http://www.italaw.com/sites/default/files/case-documents/italaw3109.pdf>

The dissenting opinion of Joaquin Morales Godoy is available at <http://www.italaw.com/sites/default/files/case-documents/italaw3111.pdf>

Claims against Hungary dismissed as investors had no property rights capable of expropriation

Emmis et al. v. Hungary, ICSID Case No. ARB/12/2, Award Martin Dietrich Brauch

In an award dated April 16, 2014, an ICSID tribunal dismissed expropriation claims by three broadcasting companies against Hungary. The tribunal considered that, after the expiration of the Hungarian broadcasting license they held from 1997 until 2009, the investors no longer had any valuable assets that Hungary could have taken.

Background

In 1997 the Hungarian Radio and Television Broadcasting Board (ORTT) launched a tender process for rights to broadcast two nationwide commercial FM radio frequencies. The successful bidder of one of them was Sláger Rádió Műsorszolgáltató Zrt. (Sláger), a Hungarian company wholly-owned by Dutch companies Emmis International Holding, B.V. and Emmis Radio Operating, B.V. (Emmis) and Swiss-controlled Hungarian company MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. (MEM).

Sláger and ORTT concluded a broadcasting agreement on November 18, 1997. Pursuant to Hungary’s Media Law then in force, a radio license could be issued for seven years and renewed only once at the broadcaster’s request, without tender, for an additional five years. Accordingly, on November 18, 2004 Sláger’s license was extended until November 18, 2009. Although there were several disputes regarding fines ORTT levied against Sláger for infringement of its broadcasting

obligations, all of them were settled, and Sláger enjoyed the full term of the agreement.

In June 2009 ORTT initiated a new call for tenders to award the frequency then held by Sláger once its license expired in November. Sláger submitted a bid, but was not successful. Emmis and MEM claimed that the tendering process was irregular, unlawful and politically influenced, and that ORTT should have disqualified the prevailing bidder based on conflicts of interest, an unfeasible business plan and lack of broadcasting experience in Hungary.

The investors unsuccessfully sought injunctions in Hungarian courts to prevent ORTT from executing a broadcasting agreement with the winning bidder. Later, they sought a court declaration that the agreement was unlawful. They obtained it from the Metropolitan Court of First Instance and the Court of Appeals, but the Hungarian Supreme Court finally declared that ORTT’s conduct was lawful.

The arbitration proceedings

In October 2011 Emmis and MEM initiated ICSID arbitration against Hungary based on the Netherlands-Hungary BIT and the Switzerland-Hungary BIT, claiming that Hungary had unlawfully expropriated their investment in the Sláger license, among other claims. In a decision issued on March 11, 2013, the arbitral tribunal dismissed all non-expropriation claims, ruling that its jurisdiction was limited to expropriation. After a hearing on Hungary’s jurisdictional objections to the remaining claims, the tribunal finally decided on them in an award of April 16, 2014.

Did the investors have rights capable of expropriation?

In the present award, the tribunal considered whether the investors had property rights capable of expropriation in 2009. For such determination, it turned to the law of the host State, Hungary, evaluating the evidence presented by the parties, including the opinion of Hungarian law experts, and giving weight to the determinations of domestic courts on how Hungarian law should be understood and applied.

It found that “it is an essential attribute of a proprietary right that it be an asset capable of ownership, valuation and alienation,” before analyzing the sources of property rights arguably held by the investors.

First, the investors argued that the 1997 broadcasting agreement had granted them property rights in respect of the 2009 tender. However, based on evidence of Hungarian law, the tribunal considered that under the 1997 agreement ORTT had no obligation toward the investors regarding the period after November 18, 2009 that could constitute valuable assets capable of expropriation.

Second, the investors claimed that their participation in the 2009 tender granted them an incumbent advantage that was to be regarded as a property right. The tribunal concluded that ORTT was not obliged by Hungarian law to accord an incumbent advantage to the investors, a conclusion supported by both expert opinion and Hungarian court decisions issued at the time.

The tribunal considered that these two conclusions were corroborated by the investors’ own conduct. In their filings with the regulatory authorities in the United States and in Hungary, the investors had expressly declared that they did not attach a value to the broadcasting license after November 2009, given the lack of a renewal expectancy beyond the 12-year period. In addition, they had lobbied in 2008 for an

amendment to the Media Law to permit the renewal of their licenses without tender beyond 2009; however, the amendment was held unconstitutional by the Hungarian Supreme Court. Both examples demonstrated, as the tribunal acknowledged, that the investors did not expect to have rights to the frequency after the expiration of the license.

Third, according to the investors, their participation in the 2009 tender granted Sláger four additional rights: the right to a properly established tender procedure, the right to a timely tender, the right to a fair and objective tender evaluation in accordance with transparent scoring criteria; and the right not to compete against unqualified or improperly qualified bidders. The investors' case was that, had ORTT complied with these rights, Sláger should have been declared the winning bidder.

While the tribunal recognized the existence and importance of those rights, it considered that they did not constitute valuable proprietary assets belonging to the investors. First, the rights were more like due process rights held by all bidders, while property rights are held by their owner to the exclusion of others. Second, they were rights regarding participation in a process to determine whether the investors would acquire ownership rather than rights that could be "freely sold and bought, and thus ha[ve] a monetary value" (using the words the Amoco case before the Iran-US Claims Tribunal). The tribunal also invoked the holding in *Waste Management II* that "[n]on-compliance by a government with contractual obligations is not the same thing as, or equivalent or tantamount to, an expropriation."

In conclusion, the tribunal held that the only property right ever held by the investors capable of expropriation was the broadcasting right under the 1997 agreement, which was a right of limited duration that expired in 2009. No other investor rights having met the requirement of a property right that could have been expropriated, the tribunal dismissed the investors' claims for lack of jurisdiction.

An itch to assess a breach of fair and equitable treatment?

The "Factual Background" section of the award referenced a joint statement issued on November 18, 2009 by the ambassadors to Hungary of nine States, condemning "non-transparent behaviour affecting [foreign] investors in such areas as public utilities, broadcasting, and elements of the nation's transportation infrastructure" in Hungary, and suggesting that "[p]assing, implementing and enforcing new anti-corruption legislation could be an important factor in helping meet the aspirations of Hungary's citizens for renewed economic growth, and prosperity" (paragraph 42).

While irrelevant to the tribunal's deliberations on jurisdiction, the mention to the joint statement could be a sign of the tribunal's eagerness to assess whether Hungary breached the fair and equitable treatment standard in its treatment of the investors in the 2009 tender.

Having stressed that both applicable BITs only allow arbitration in cases of expropriation claims, the tribunal reasoned that: "[h]ad the Tribunal been granted a broader jurisdiction, it would have been possible to determine whether Claimants' investments in Sláger would benefit from, for example, the Treaties' fair and equitable treatment standard when it came to adjudging the Respondent's conduct of the [2009] bid" (emphasis added, paragraph 144).

The tribunal was composed of Prof. Campbell McLachlan (president), Hon. Marc Lalonde (claimant's appointee) and Mr. J. Christopher Thomas (respondent's appointee).

The award is available at: <http://www.italaw.com/sites/default/files/case-documents/italaw3143.pdf>. Earlier decisions in this case are available at: <http://www.italaw.com/cases/384>.

ICSID-AF tribunal upholds jurisdiction, dismisses all claims by medical technology minority investors in Poland *David Minnotte and Robert Lewis v. Republic of Poland, ICSID Case No. ARB(AF)/10/1* **Matthew Levine**

A London-seated ICSID-Additional Facility arbitration tribunal has rejected all claims brought against Poland by two American investors. The claimants had a minority stake in a medical technology enterprise that went bankrupt after being investigated by tax authorities for financial wrongdoing.

The tribunal found jurisdiction under a 1990 U.S.-Poland economic relations treaty.

Background

The claimants' business partner Zygmunt Nizioł established Laboratorium Frakcjonowania Osocza Sp. z o.o. (LFO) to carry out a Polish Ministry of Health tender to build and operate the country's first blood plasma fractionation plant

After considerable negotiations which concluded in 1997, LFO secured a US\$34,651,000 loan from a domestic banking consortium. A significant aspect of these negotiations was the State Treasury's provision to the banking consortium of a surety for up to 60% of the loan's value.

During this same period, Nizioł on behalf of LFO negotiated an agreement with the claimants, David Minnotte and Robert Lewis, which resulted in each holding 16.5% of the shares in LFO. During the arbitration, there was significant disagreement between the claimants and the respondent on the details of this capitalization phase.

In 1998, LFO was the subject of an inspection by Polish tax authorities in relation to, *inter alia*, the amount of LFO's shareholders' financial contributions and the way in which LFO spent those funds. Subsequently, the Ministry of Finance wrote to the banking consortium and requested that the loan payment be suspended pending certain conditions.

Following extensive exchanges between Poland and the consortium lead, the loan agreement was terminated in 2001. Ultimately, LFO defaulted on the loan and declared bankruptcy in 2006, by which time the total owing was US\$22,746,309.12. Poland partially reimbursed the banking consortium per the terms of the surety.

Arbitration process witnesses complicated and legally tenuous business relationships

Following the constitution of the tribunal, the claimants requested an interim order that Poland suspend criminal proceedings against and take immediate steps to ensure that no arrest warrants would be issued against Messrs Minnotte and Lewis; a similar request was also made in relation to Mr Nizioł. After a hearing via videoconference, the tribunal rejected these requests but decided to nevertheless organize the proceedings outside Europe.

The tribunal ultimately observed that "[T]he full facts underlying this claim may never be known, but it is evident that the Claimants relied to a remarkable degree upon their trust in their Polish associates, and in particular Mr Nizioł." The tribunal even wondered if the claimants "...trusted too much, and perhaps overestimated the extent to which their previous commercial

successes demonstrated a level of business acumen sufficient to overcome the obstacles of operating in a foreign country, in a foreign language, and within a foreign legal and administrative system.”

Jurisdiction not affected by Poland's fraud-related objections

The tribunal found that it had jurisdiction under the “Treaty between the United States of America and the Republic of Poland concerning Business and Economic Relations” of March 21, 1990. (The tribunal referred to the Treaty as ‘the BIT’ and this usage is adopted in the following.)

Poland objected to the tribunal’s jurisdiction on the grounds that LFO’s conduct, and by extension the claimants’ investment in LFO, was characterized by fraud, deceit and bad faith.

The tribunal observed that the “[the BIT] does not define an ‘investment’ in terms that explicitly require the investment to be made in accordance with the host State’s law.” But that “it is now generally accepted that investments made on the basis of fraudulent conduct cannot benefit from BIT protection; and this is a principle that is independent of the effect of any express requirement in a BIT that the investment be made in accordance with the host State’s law.”

The tribunal proceeded to find that “[T]here may be circumstances where fraud is so manifest, and so closely connected to facts (such as the making of an investment) which form the basis of a tribunal’s jurisdiction as to warrant a dismissal of claims in *limine* for want of jurisdiction. This situation is, however, likely to be exceptional; and it is not the situation in the present case.”

Tribunal finds that fraud and deceit claims may also be relevant at the merit stage

The tribunal considered whether, having found the claims within its jurisdiction and admissible, they should be dismissed on the merits because of the respondent’s allegations of fraud and deceit.

The tribunal decided that the particular allegations should not entirely deprive the claimants of coverage under the U.S.-Poland BIT. Rather, it considered whether the facts underlying those allegations justified some or all of the State’s conduct towards the claimants’ investment.

Tribunal rejects three theories of indirect expropriation

The tribunal considered three alleged instances of expropriation and found in all three cases that the facts and evidence did not support the claimants’ position.

First, the claimants alleged that Poland pressured Kredyt Bank as organizer of the banking consortium to cease funding LFO’s line of credit, which forced the failure of the LFO project. The tribunal found “no evidence that indicates that the Respondent’s dealings with Kredyt Bank were motivated by anything other than a legitimate concern to protect its position as a guarantor and fulfil its responsibilities as an accountable user of public funds.”

Second, the claimants argued that Poland’s failure to supply plasma for testing purposes caused delays, which led to the failure of the project. The tribunal found that “the [relevant] express terms ... cannot be construed as requiring the Respondent to deliver plasma for the purposes of pre-production testing, either on demand or by any given date.” The tribunal further observed that while Poland maintained a domestic monopoly on the supply of plasma, LFO remained

free to import plasma from foreign markets at this stage of the project.

Third, the claimants alleged that a strategic investor in the LFO project had been pressured or induced by authorities to divest itself. The tribunal found that there was insufficient evidence to reach this conclusion.

No violation of fair & equitable treatment obligation

The claimant advanced five separate circumstances that it believed had violated its legitimate expectation to fair and equitable treatment under the BIT. The tribunal stated that “the State must be shown to have acted delinquent in some way or other if it is to be held to have violated that standard. It is not enough that a claimant should find itself in an unfortunate position”

In the first scenario, the tribunal concluded that the claimants had not shown that “they had any legitimate expectations that were defeated by the conduct of the Respondent.”

In the remaining scenarios, the tribunal found that, notwithstanding the claimants’ legitimate expectations, “the Claimants have not made out their claim that the Respondent acted in a manner that was unfair or inequitable.”

Costs borne by claimants

The tribunal ordered the claimants to bear all of the arbitration costs and Poland’s reasonable legal fees. It identified three factors informing this decision: the claimants had failed to establish any breach of the treaty; the claimants had placed “a good deal of weight ... on inferences drawn from circumstantial evidence”; and Poland had had the burden of refuting the claimants’ arguments.

The tribunal was composed of Maurice Mendelson (claimants’ nominee), Eduardo Silva Romero (Poland’s nominee), and Vaughan Lowe (President).

The award is available at: <http://www.italaw.com/sites/default/files/case-documents/italaw3192.pdf>

Notes

¹ Sidley Austin LLP, Representative Engagements in Investor-State Arbitrations. Retrieved from <http://www.sidley.com/Recent-Investor-State-Arbitrations/>

² *Renée Rose Levy and Gremcitel S.A. v. Republic of Peru*, ICSID Case No. ARB/11/17. For the amount in dispute, see Sidley Austin LLP, Representative Engagements in Investor-State Arbitrations. Retrieved from <http://www.sidley.com/Recent-Investor-State-Arbitrations/>

resources and events

Resources

World Investment Report 2014

United Nations Conference on Trade and Sustainable Development, June 2014

UNCTAD's *The World Investment Report* is an annual publication that focuses on trends in foreign direct investment (FDI) worldwide, at the regional and country levels and emerging measures to improve its contribution to development. The 2014 report shows that FDI inflows increased by 9 percent in 2013 to US\$1.45 trillion. Developing countries increased their global share of FDI inflows to a record level of 54 percent, and developing Asia now attracts more inward FDI than either the EU or the United States. As investors, developing and transition countries have been steadily increasing their investments abroad and last year they accounted for a record 39 per cent of global FDI outflows—up from just 12 per cent in the early 2000s. Because United Nations member States and other stakeholders are currently negotiating a post-2015 development framework—the Sustainable Development Goals (SDGs)—this year's report focuses on how private finance can be mobilized for investment in sustainable development sectors, such as climate change adaptation, infrastructure development, food security, health, and education. The report is available here: <http://unctad-worldinvestmentforum.org/about-wif-2014/world-investment-report-2014/>

International Law and Developing Countries: Essays in Honour of Kamal Hossain

Edited by Sharif Bhuiyan, Philippe Sands and Nico Schrijver, Brill, February 2014

This book celebrates Kamal Hossain's lifelong and significant contribution to the development of international law and the cause of developing countries. It brings together an interview with Hossain by the editors, and thirteen essays written in his honour by scholars representing a wide spectrum of expertise in international law. The interview provides an introduction to the rich and varied life of a statesman, a drafter of his country's constitution, and an acclaimed constitutional and international lawyer. The subjects covered in the essays include the new international economic order, human rights, counter-terrorism, climate change, oil and gas law, arbitration, law of the sea, international trade law and judicial reform. These essays offer important perspectives on the issues addressed. More information is available here: <http://www.brill.com/products/book/international-law-and-developing-countries>

The Right to Regulate in International Investment Law

Catharine Titi, Hart Publishing, June 2014

Since the inception of the international investment law system, investment promotion and protection have been the *raison d'être* of investment treaties and States have confined their policy space in order to attract foreign investment and protect their investors abroad. Languishing in relative obscurity until recently, the right to regulate has gradually come to the spotlight as a key component of negotiations on new generation investment agreements around the globe. States and regional organisations, including, notably, the European Union and the United States, have started to examine ways in which to safeguard their regulatory power and guide—and delimit—the interpretive power of arbitral tribunals, by reserving their right to pursue specific public policy objectives. This book explores the status quo of the right to regulate, in order to offer an appraisal and a reference tool for treaty makers, thus contributing to a better understanding of the concept and the broader discourse on how to enhance the investment law system's legitimacy. More information is available here: <http://www.hartpub.co.uk/BookDetails.aspx?ISBN=9781849466110>

The Foundations of International Investment Law: Bringing Theory into Practice

Edited by Zachary Douglas, Joost Pauwelyn, and Jorge E. Viñuales, Oxford University Press, May 2014

International investment law is one of the fastest growing areas of international law. It has led to the signing of thousands of agreements, mostly in the form of investment contracts and bilateral investment treaties. Also, in the last two decades,

there has been an exponential growth in the number of disputes being resolved by investment arbitration tribunals. Yet the legal principles at the basis of international investment law and arbitration remain in a state of flux. Perhaps the best illustration of this phenomenon is the wide disagreement among investment tribunals on some of the core concepts underpinning the regime, such as investment, property, regulatory powers, scope of jurisdiction, applicable law, or the interactions with other areas of international law. The purpose of this book is to revisit these conceptual foundations in order to shed light on the practice of international investment law. The first part of the book focuses on the 'infrastructure' of the investment regime or, more specifically, on the structural arrangements that have been developed to manage foreign investment transactions and the potential disputes arising from them. The second part of the book identifies the common conceptual bases of an array of seemingly unconnected practical problems in order to clarify the main stakes and offer balanced solutions. The third part addresses the main sources of 'regime stress' as well as the main legal mechanisms available to manage such challenges to the operation of the regime. More information is available here: <http://ukcatalogue.oup.com/product/9780199685387.do>

Events 2014

September 1-2

ARBITRATION OF ENERGY DISPUTES: NEW CHALLENGES, Danish Institute of Arbitration, Copenhagen, Denmark, <http://www.voldgiftsinstitutet.dk/dk/Menu/ENERGY+CONFERENCE/Program>

September 4-5

SWEDISH ARBITRATION DAYS 2014 - EXPERTS IN INTERNATIONAL ARBITRATION, The Swedish Arbitration Association, Stockholm, Sweden, <http://swedisharbitration.se/event/swedish-arbitration-days-2014/>

October 13-16

WORLD INVESTMENT FORUM 2014: INVESTING IN SUSTAINABLE DEVELOPMENT, UNCTAD, Geneva, Switzerland, <http://unctad-worldinvestmentforum.org/>

October 20-24

INTERGOVERNMENTAL FORUM ON MINING, MINERALS, METALS AND SUSTAINABLE DEVELOPMENT, UNCTAD, Geneva, Switzerland, <http://unctad.org/en/Pages/MeetingDetails.aspx?meetingid=492>

November 12-13

RAISING THE BAR: HOME COUNTRY EFFORTS TO REGULATE FOREIGN INVESTMENT FOR SUSTAINABLE DEVELOPMENT, Columbia University, New York, United States, <http://ccsi.columbia.edu/2014/01/01/raising-the-bar-home-country-efforts-to-regulate-foreign-investment-for-sustainable-development/>

December 8-9

THE POLITICAL ECONOMY OF INTERNATIONAL INVESTMENT AGREEMENTS, GERMAN DEVELOPMENT INSTITUTE AND INTERNATIONAL INVESTMENT INITIATIVE OF THE WORLD TRADE INSTITUTE, Bonn, Germany, <http://www.die-gdi.de/veranstaltungen/international-investment-agreements/>

Events 2015

March 9-14

EXECUTIVE TRAINING PROGRAM ON SUSTAINABLE INVESTMENTS IN AGRICULTURE, Columbia University, New York, United States, <http://ccsi.columbia.edu/2012/03/16/agtraining/>



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