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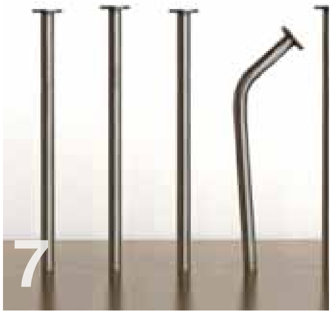
State Liability for Regulatory Change: How International Investment Rules are Overriding Domestic Law by Lise Johnson and Oleksandr Volkov



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feature 1

State Liability for Regulatory Change: How International Investment Rules are Overriding Domestic Law

Lise Johnson and Oleksandr Volkov

With governments around the world pushing efforts to negotiate and approve mega-investment treaties, it is important to be clear on just what these investment treaties do and do not mean. One issue that is increasingly apparent is that investment treaties are not merely tools to provide protections against abusive regimes and egregious conduct, but are mechanisms through which a small and typically powerful set of private actors can change the substantive content of the law outside the normal domestic legislative and judicial frameworks.

Some might counter that contention. Indeed, the European Commission recently issued a statement enthusiastically supporting investment treaties and investor-state dispute settlement, and labeling as flatly "untrue!" concerns that investor-state dispute settlement "subverts democracy," "takes place behind closed doors," "undermines public choices" and is handled by "a small clique of lawyers".[1] But, evidence from decisions regarding state liability for regulatory change shows something different.

This article, which draws from a more detailed study, compares U.S. domestic law and international treaty rules on state liability for regulatory changes. It shows that arbitral tribunals have interpreted investment treaty rules in a manner far more favorable to the interests of investors than the approaches adopted in U.S. courts.[2]

Investor-state arbitration and state liability for regulatory change

When are states liable for regulatory change that hurts the profitability or value of an investment? The answer to that question in domestic law reflects lawmakers' decisions regarding how to appropriately balance public and private interests, and has very real implications for a government's willingness and ability to introduce, monitor, and enforce measures that regulate private conduct in order to serve broader public goals. Arbitral tribunals interpreting and applying investment treaties, however, are issuing decisions that override those domestic choices.

These tensions between domestic law and international investment treaties are particularly evident when looking at the issue of state liability for changes in the general legal framework that impact an existing investor-state contract or quasi-contractual relationship, such as a permit, license or authorization issued by the government to a private entity. On this issue, arbitral tribunals have stated that one core obligation in investment treaties—the fair and equitable treatment (FET) obligation—protects the "legitimate expectations" of investors made at the time of the investment;[3] and if the legal framework governing the investment changes in a way that was not anticipated or foreseen by the investor at the time of making the investment, then the investor should be compensated for the cost of complying with those changes.[4] This means that if a new law is adopted, or an existing law is revoked or interpreted or applied in a new way,[5] those changes can trigger state liability. Various tribunals have refined and arguably softened that rule of "legitimate expectations," stating that investment treaties do not generally act to freeze the law *unless* those changes are contrary to a specific commitment made by the state.[6] For those tribunals, the key to whether they will require governments to compensate investors for regulatory change is their view of what constitutes a "specific commitment" to refrain from making such changes.

In a number of cases decided to date, tribunals have interpreted the concept of a "specific commitment" broadly. In cases such as *EDFI v. Argentina,*[7] *Enron v. Argentina,*[8] *LG&E v. Argentina*[9] and *Occidental v. Ecuador* (2004),[10] the tribunals have found provisions in general domestic laws and regulations to constitute non-revocable commitments. The commitment, they have thus concluded, need not be so "specific."[11] Tribunals have also bound governments to "promises" they have found or inferred from statements by government officials and representatives of state-owned enterprises, positions taken by agencies, and even illegal contracts or deals involving procedural or other irregularities.[12]

How this differs from domestic law—example of the gap between tribunal decisions and U.S. courts

Notably, the broad rule that governments should compensate investors for changes in the general regulatory framework that impact their expectations and profitability as well as the narrower interpretation that governments are only liable to compensate for regulatory change that is inconsistent with a "specific commitment" given by a state to an investor, both privilege private rights over governmental regulatory freedom in a way that is inconsistent with domestic rules, such as those of the United States.

Comparing investment arbitration decisions regarding liability for regulatory change with U.S. case law addressing similar factual circumstances, for instance, illustrates that U.S. law takes a much narrower view of private rights. U.S. cases addressing the precise issue of state liability for regulatory change impacting investor-state contracts and quasi-contracts show that:[13]

– The general rule is that the state *will not* be liable to private parties for economic harms suffered as a result of general regulatory change; and

– The government may in certain cases have to compensate an investor for losses suffered as a result of general regulatory changes that impact a contractual or quasi-contractual relationship with the government, *but, due to strict application of the doctrine of "unmistakability" and related rules, the government is largely shielded against liability in these cases.*

More specifically, under U.S. law and its doctrine of "unmistakability," liability will only be found when an official or entity with the (1) *actual* authority to make a promise regarding future regulatory treatment, (2) makes that promise in a clear and *unmistakable* way and (3) in a manner *fully consistent with relevant procedural requirements* for entering into investor-state contracts, and (4) does so with the *intent* to bind itself to that *particular commitment regarding future regulatory treatment.*

Case law has elaborated upon each of these requirements. On the requirement of actual authority, for instance, courts have explained that even if a government entity has authority to set tariffs for water use, that does not mean that it also has the authority to give up or restrict its sovereign power to set those tariffs.[14] The power to set rates is not the same as the power to promise to freeze or stabilize them, and for an agency to exercise the latter power it must have been clearly delegated that ability. Notably, the doctrine of estoppel is largely unavailable under U.S. law to protect investors in cases of mistaken reliance on promises made by government actors that exceeded the bounds of their authority.[15]

The requirement of intent has also been interpreted in a way that shields the government from liability. Courts have concluded, for example, that clear intent to induce investment by promising a certain type of regulatory treatment is different from and does not establish intent to induce investment by promising *continued* enjoyment of that regulatory treatment.[16]

Similarly, any alleged promise by the government to compensate an investor for the effect of a sovereign act must be "unmistakable." This requirement acts as a "rule of strict construction that presumes that the government, in making an agreement regarding its regulation of a private party, has not promised to restrain future use of its sovereign power, unless the intent to do so appears unmistakably clear in the agreement."[17] In one case illustrating the force of this rule, the Supreme Court found that a promise in a legislative act to "forever exempt" a water services system from taxes did not unmistakably establish a promise to never "exercise the reserved power of amending or repealing [that] act."[18] The Supreme Court reasoned that the "utmost" that could be said was that when the legislature passed the law "forever" exempting the water system from taxes it had no intent "to withdraw the exemption from taxation; not that the power reserved would never be exerted … if in the judgment of the legislature the public interests required that to be done."[19]

In addition to having to comply with substantive legal requirements, promises made by government entities to waive or compensate for regulatory change must also strictly comply with applicable procedural rules designed to prevent impropriety in the contracting process. Agreements concluded with the U.S. government in violation of those rules have traditionally been declared void *ab initio*. No actual collusion or fraud need be shown.[20]

There is notable divergence between international investment tribunals' and U.S. courts' respective assessments of the scope of enforceable "commitments" and government liability for interference with those undertakings. Both arbitral tribunals and U.S courts declare deference to sovereign acts of general applicability; both also recognize that governments do not have unbounded authority to exercise their sovereign power to the detriment of investor-state contracts. Nevertheless, they differ in terms of the respective tests they apply to determine whether the government promised *not* to exercise its authority or to provide compensation for future regulatory changes.[21]

Key points of distinction between the two systems include tribunals' apparent willingness to find implied enforceable and non-revocable commitments against regulatory change, and to hold governments to particular undertakings that, under domestic law, may not be legally binding on either the government or the investor due to substantive or procedural failings. Similarly, tribunals have read ambiguity in the contract in favor of affirming, rather than rejecting, the existence of a commitment to waive future use of sovereign power. The *Enron* tribunal, for instance, stated that if the legal framework existing at the time "was intended to be transitory[,] it should have also been clearly advised to prospective investors."[22] Likewise, the *EDFI* tribunal asserted that if Argentina had not intended to bear the risk of loss for future regulatory changes, it "could have said so" in its contract.[23] Both cases required the states to explicitly reserve future exercises of sovereign power, and thus stand in stark opposition to the U.S. unmistakability cases, which will only enforce promises to refrain from future exercises of sovereign power if there is mutuality of intent behind the promises and the commitments themselves are clearly expressed.

Another area of divergence relates to how a finding of unmistakability or a specific commitment can be impacted by the purpose or type of regulatory action that it purports to freeze. With respect to the purpose of the regulatory action, the early U.S. cases indicate that courts strictly applied the "unmistakability" test when applying a more relaxed rule could have threatened development of the new nation and its efforts to construct and operate crucial infrastructure. Likewise, courts today appear reluctant to find "unmistakable" promises of legal stability where the existence and enforcement of such promises would hinder the government's ability to respond to crises, react to matters of public interest, and address harms caused or negative externalities imposed by private actors once the problems are discovered.

U.S. courts also appear to base the strictness with which they apply the "unmistakability" test on the type of action at issue, evidencing heightened concern regarding interfering with the government's exercise of its taxation powers. By contrast, in international investor-state arbitration, neither the purpose nor type of the regulatory action at issue has seemed to impact the level of scrutiny tribunals have applied to determine whether the government had in fact guaranteed to waive its powers. Indeed, tribunals have found implied promises of stability that barred government action taken in response to financial crises and through the exercise of fiscal policy.

Finally, a fifth area of divergence is in the relevance U.S. courts and investment tribunals respectively assign to the temporal scope of the alleged commitment. In U.S. decisions, courts have emphasized that a commitment to accord a specific form of treatment does not imply a commitment to accord that treatment over the life of the contract. The *degree* of the waiver seems to affect scrutiny of the "unmistakable" nature of government guarantees that purport to restrict the authority of future administrations to respond to changing constituents, policies, and circumstances. Indeed, a number of cases finding no "unmistakable" promise of regulatory stability involved alleged promises that purported to last for decades, if not indefinitely.[24]

Decisions by investment tribunals to date reflect less unease with strictly enforcing long-term promises. In a number of cases, a framework established in law has been interpreted to be a framework that persists over time. Tribunals have also further elevated the importance of stability and of maintaining promises in accordance with their original terms by awarding lost profits over the originally foreseen life of intended deals and in accordance with the legal regimes applying to those arrangements at the time of their conclusion.[25]

How this impacts and overrides domestic law

In short, U.S. domestic rules regarding government flexibility to change the applicable regulatory framework differ from rules being developed and applied by investment tribunals.[26] The question this raises is whether tribunals will apply these rules on "specific commitments" to such domestic jurisdictions that take a different view of limits on sovereign powers.

The answer appears to be "yes". Through this approach, tribunals have evidenced that they view investment treaties and, more specifically, the FET obligation, as implicitly creating a new category of investor rights that the investors would not have received under the relevant contracts/quasi-contracts or the domestic legal frameworks governing those instruments.

Tribunals have thus attached "new legal consequences" to pre-existing contractual or quasi-contractual relationships between investors and states, retroactively changing the rights and obligations of those actors.[27] Domestic delineations of private property rights are thus vulnerable to being overridden by arbitral tribunals with their own interpretation of what rights economic actors have been given under investment treaties.

> "U.S. domestic rules regarding government flexibility to change the applicable regulatory framework differ from rules being developed and applied by investment tribunals."

Reining in claims seeking damages for regulatory change?

Because there is no system of binding precedent in international investment law, the fact that tribunals have taken certain approaches to "specific commitments" in the past does not mean that they will continue to do so in the future. Thus, future tribunals could soften the rule that has been applied in the past, and look to domestic law when defining the scope of property rights investors claim were harmed by conduct breaching the investment treaty. But there is no guarantee that tribunals will do so. Investment treaties give private arbitrators significant powers of interpretation, and other international treaties (i.e., the New York Convention and the ICSID Convention) largely insulate tribunals from formal or informal checks on their power. Even where the state parties to the treaty take a common and consistent position on their view of the meaning of a given treaty provision, that is no guarantee that the tribunals will follow those states' mutually-agreed positions;[28] and where tribunals issue an interpretation with which states disagree, there are few, if any, mechanisms through which states can set tribunals back on the correct path.[29]

Moreover, through past case law, tribunals are sending signals to investors about how investment treaties can be used to challenge regulatory change. One of many examples of how investors are picking up these signals is *Eli Lilly v. Canada*, a dispute in which the investor is challenging rulings of Canadian courts interpreting Canadian intellectual property law, arguing that those judicial decisions improperly changed the host country's legal regime in violation of the investor's "legitimate expectations."[30] Similarly, in *Guaracachi v. Bolivia*, the investor argues that the host country breached the FET obligation when it "effected a fundamental change to the regulatory regime that attracted" the investor's investment.[31] Of course, not all claims will succeed. But if leading law firms are signing these filings, this illustrates that at least some experts believe these claims have enough legal merit to launch a costly case.

The conclusion this produces is that investment treaties—as they are being used by investors and applied by some tribunals—are not merely instruments to protect foreign investors against outrageous and discriminatory conduct by host states, but to expand the rights that investors have, and to do so in a way that shifts the risk of regulatory change from the investor to the government.

Author

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Notes

1 See European Commission, Incorrect Claims about Investor-State Dispute Settlement, Oct. 3, 2013, available at http://trade.ec.europa.eu/doclib/docs/2013/october/tradoc_151790.pdf.

2 This essay draws from the following longer paper: Lise Johnson and Oleksandr Volkov, Investor-State Contracts, Host-State "Commitments" and the Myth of Stability in International Law, 24 Am. Rev. of Int'l Arb. 361 (2013)

3 Técnicas Medioambientales Tecmed, S.A. v. United Mexican States, ICSID Case No. ARB(AF)/00/2, Award, May 29, 2003, para. 154.

4 For example, this reading of the meaning of the fair and equitable treatment obligation as protecting against unforeseeable changes in the law was taken by Professor Rudolf Dolzer in his presentation at the VCC's Spring Speaker Series on March 14, 2013, at Columbia University. See also, e.g., Suez, Sociedad General de Aguas de Barcelona S.A. and InterAgua Servicios Integrales del Agua S.A. v. Argentine Republic, ICSID Case No. ARB/03/17, Decision on Liability, July 30, 2010, para. 207; Total v. Argentina, ICSID Case No. ARB/04/1, Decision on Liability, Dec. 27, 2010, para. 122.

5 Occidental Exploration and Production Company v. Ecuador, LCIA Case No. UN 3467, Final Award, July 1, 2004.

6 See, e.g., AES v. Hungary, ICSID Case No. ARB/07/22, Award, Sept. 23, 2010, para. 9.3.34.

7 EDFI v. Argentina, ICSID Case No. ARB/03/23 Award, June 11, 2012.

8 Enron v. Argentina, ICSID Case No. ARB/01/3, Award, May 22, 2007.

9 LG&E v. Argentina, ICSID Case No. ARB/02/1, Decision on Liability, Oct. 3, 2006.

10 Occidental Exploration and Production Company v. Ecuador, LCIA Case No. UN 3467, Final Award, July 1, 2004.

11 See also, e.g., M. Kinnear, "The Continuous Development of the Fair and Equitable Treatment Standard," in A. Bjorklund, I. Laird, S. Ripinsky (eds.), INVESTMENT TREATY LAW, CURRENT ISSUES III (2009), at 228 ("The weight of authority suggests that an undertaking or promise need not be directed specifically to the investor and that reliance on publicly announced representations or well known market conditions is a sufficient foundation for investor expectations.").

12 See, e.g., Kardassopoulos v. Georgia, ICSID Case No. ARB/05/18, Award, March 3, 2010.

13 These cases are reviewed in detail in Lise Johnson & Oleksandr Volkov, Investor-State Contracts, Host-State "Commitments" and the Myth of Stability in International Law, 24 Am. Rev. of Int'l Arb. 361 (2013).

14 See, e.g., Home Telephone & Telegraph v. Los Angeles, 211 U.S. 265 (1908).

15 See Johnson & Volkov at pp. 400-401; Fed. Crop Ins. Corp. v. Merrill, 332 U.S. 380, 384 (1947). Even where actual authority is established, estoppel claims against the government still place a heavy burden on the plaintiff to succeed. The general rule under U.S. federal law is that for equitable estoppel to apply against the government, a plaintiff must establish the basic elements of an estoppel claim, and show that the government engaged in affirmative and egregious misconduct. See, e.g., Sanz v. U.S. Sec. Ins. Co., 328 F.3d 1314 (11th Cir. 2003). Courts have also said that the equitable estoppel doctrine will only be applied against the government if doing so is necessary to avoid a serious injustice that would outweigh the damages to the public interest. See, e.g., Bolt v. United States, 944 F.2d 603, 609 (9th Cir. 1991). U.S. states similarly restrict estoppel claims against the government. See, e.g., Greece Town Mall, L.P. v. New York, 964 N.Y.S.2d 277 (April 25, 2013) (addressing the issue under New York state law); DRFP, LLC v. Republica Bolivariana de Venezuela, Case No. 2:04-CV-00793 (S.D. Ohio, May 14, 2013) (addressing the issue in a case against Venezuela addressing a contract governed by the law of Ohio).

16 See, e.g., Suess v. United States, 535 F.3d 1348, 1362 (Fed. Cir. 2008).

17 Alan R. Burch, Purchasing the Right to Govern: *Winstar* and the Need to Reconceptualize the Law of Regulatory Agreements, 88 Ky. L.J. 245, 248 (2000).

18 Covington v. Kentucky, 173 U.S. 231, 238-239 (1899).

19 Id. at 238-39.

20 Alan I. Saltman, The Government's Liability for Actions of its Agents that Are Not Specifically Authorized: The Continuing Influence of *Merrill* and *Richmond*, 32 Public Contract L.J. 775, 796 (2003).

21 *Cf.* Glamis Gold Ltd. v. United States, NAFTA/UNCITRAL Ad hoc, Award, para 800-02 (June 8, 2009) (finding no "specific inducements" the repudiation of which could potentially give rise to a breach of NAFTA Article 1105); para 22 & n.24 (noting that although it viewed a repudiation of specific assurance as potentially giving rise to liability under the NAFTA, it would take no position on the "type or nature of repudiation measures that would be necessary to violate international obligations").

22 Enron Corp. v. Argentina, *supra* note 7, para 137.

23 *See* EDFI v. Argentina, *supra* note 6, para 960.

24 *See, e.g.,* Bridge Proprietors v. Hoboken Co., 68 U.S. (1 Wall.) 116 (1883); Rogers Park Water v. Fergus, 180 U.S. 624 (1901); Century Exploration New Orleans, LLC v. United States, 110 Fed. Cl. 148, 172 (Fed. Cl. 2013) ("[N]othing in plaintiffs' lease can be read to provide static treatment for their activities in perpetuity.").

25 *See, e.g.,* Occidental Petroleum Corp. v. Ecuador, ICSID Case No. ARB/06/11, Award, Oct. 5, 2012, pp. 185-221, 308.

26 While our research has focused on US law, preliminary analysis of the laws of other countries (e.g., India, Japan, and Canada) appears that other jurisdictions also take a view that is narrower than investment tribunals' regarding the existence of purported promises by governments to restrict their abilities to take future regulatory action.

27 See, e.g., Quantum Entertainment Ltd. v. US Dept. of Interior, 714 F.3d 1338 (Ct. App. DC. 2013) (upholding finding that contract was "null and void" at the time it was entered into and that subsequent enforcement of that contract was impermissible retroactive change in the legal consequences of the deal).

28 This can be easily seen by comparing states' positions in briefs and non-disputing party filings with tribunals' decisions. Briefs are regularly disclosed by the parties to the NAFTA and CAFTA.

29 Some treaties have a mechanism making clear that if states agree to and issue interpretations reflecting their understanding of the agreement, those interpretations will be binding on tribunals. A well-known example of this is Article 1131 of the NAFTA.

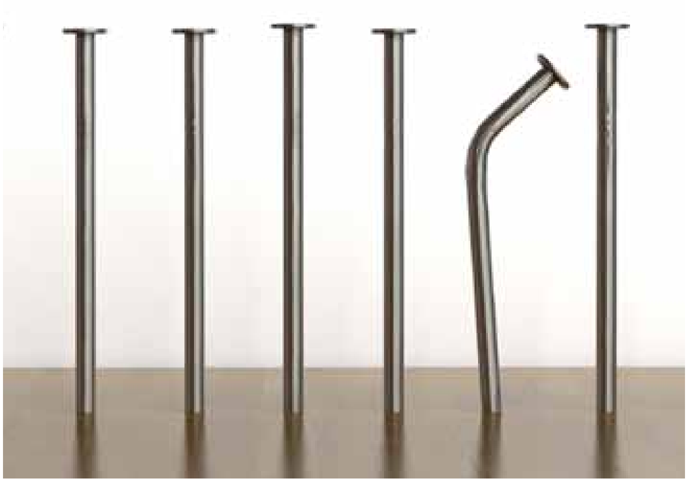
30 Eli Lilly and Co. v. Canada, Notice of Arbitration, Sept. 12, 2013, para 82-84 (filed by Covington & Burling LLP and Gowling Lafleur Henderson LLP).

31 Guaracachi v. Bolivia, Claimants' Post-Hearing Brief, May 31, 2013, para 116 (filed by Freshfields Bruckhaus Deringer).

The Boom in Parallel Claims in Investment Treaty Arbitration

Gus Van Harten

feature 2



Investment treaty arbitrators have adopted a *de facto* policy of favouring parallel claims by declining to yield to contractually-agreed dispute settlement provisions. In 12 cases decided before June 2010, tribunals awarded at least US$1.2 billion against states after taking jurisdiction over an investor claim in spite of an exclusive jurisdiction clause in a relevant contract.[1] The policy is widespread among tribunals but appears out of step with judicial restraint based on principles of party autonomy, sanctity of contract, or the avoidance of parallel proceedings.

These observations emerged from a study of arbitrator decision-making under investment treaties outlined more fully in a book by the author.[2] The study revealed a tendency of arbitrators to favour parallel claims in spite of treaty language that supported restraint due to the role of another forum. The *de facto* policy has important implications besides the obvious benefit to the investor-state arbitration industry that grew alongside the boom in treaty claims since the late 1990s. Fundamentally, it expanded arbitrator power and prospects for investor compensation and state liability, while revealing how the growth of investor-state arbitration has depended on expansive legal interpretations by arbitrators.

Overlap between contract and treaty-based disputes

Investment treaty arbitration is deeply intertwined with contract-based adjudication. It emerged from the study that approximately two-thirds of investment treaty cases appeared to involve a contract—presumably with its own dispute settlement clause—that related to the dispute brought before the treaty arbitrators.[3] In light of this overlap, it was asked whether the treaty arbitrators stayed or delayed their own proceedings in deference to a contractually-agreed forum. Restraint might not be appropriate in all such cases. Yet, in these circumstances, principles of party autonomy and sanctity of contract provided a basis for arbitrators to: (a) allow other forums to play the primary role in resolving a dispute; and (b) limit their own role to providing a check against sovereign interference in the contract-based forum. In spite of this, investment treaty tribunals overwhelmingly declined to show restraint in the face of a contract-based forum.

Rejection of restraint

On the specific issue of exclusive jurisdiction clauses, the earliest example of restraint, from 2000, was *Vivendi (No 1)* in which the tribunal declined to hear an investor's claim because it related closely to a concession contract that contained its own exclusive jurisdiction clause.[4] The tribunal decided that the claimant had to submit the dispute first to the contract-agreed forum and that, if the claimant was unsatisfied with the outcome, then the claimant would be limited to a claim of denial of justice under the treaty.[5] Thus, the tribunal decided implicitly that investment treaties do not provide a general alternative venue for investors involved in contractual disputes, where the investors have agreed previously to resolve such disputes in another forum.

Had the decision in *Vivendi (No 1)* been accepted widely by later tribunals, it would have constituted investment treaty arbitration as a supplement to contract-based adjudication. Instead, the decision was overridden by an International Centre for Settlement of Investment Dispute (ICSID) annulment committee of three World Bank-appointed arbitrators, two of whom—Yves Fortier and James Crawford—became mainstays in investment treaty arbitration.[6] According to the annulment committee, the original tribunal's decision amounted to a manifest excess of powers under the ICSID Convention because the original tribunal:[7]

- looked beyond the claimant's framing of the treaty claim in order to evaluate for itself whether the claim involved issues of contractual performance or non-performance,

- stayed its proceedings upon finding that the underlying dispute was a matter of contract and that the contractual forum was the more appropriate forum,

- declined to analyse in detail specific treaty standards until after the claimant had resorted to the contractual forum, and

- signalled that the treaty would not offer relief for the claimant unless the respondent state denied justice to the claimant in the contract-based forum.

This annulment heralded the current *de facto* policy in favour of parallel claims under investment treaties despite the role of contract-based forums.[8] Remarkably, the *Vivendi (No 1)* annulment committee overrode the original tribunal in a situation where the annulment committee was itself supposed to be deferring to the original tribunal.[9] In essence, the original tribunal was said to have exceeded its power manifestly because it showed restraint.

After the annulment in *Vivendi (No 1)* in 2002, there were few examples of restraint linked to the role of a contract-based forum.[10] Rather, in 30 of 36 cases where this specific legal issue was found to have arisen, the tribunal allowed a treaty claim to proceed in the face of a contractually-agreed venue.[11]

Arbitrators justified this favouring of parallel claims in various ways. For instance, in *Vivendi (No 1)*, the annulment committee emphasized the distinction between formal causes of action rather than factual similarities between disputes in order to distinguish treaty from contractual claims.[12] Other tribunals took a similar approach that sidelined exclusive jurisdiction clauses.[13] For example, the *Siemens* tribunal stated that "[t]he dispute *as formulated by the Claimant* is a dispute under the Treaty…. The Tribunal simply has to be satisfied that, if the Claimant's allegations would be proven correct, then the Tribunal has jurisdiction to consider them."[14] In *Eureko v Poland*, the tribunal allowed an investor's claim to proceed under the treaty in spite of an exclusive jurisdiction clause, stating that the investor "advances claims for breach of Treaty… [and] every one of those claims must be heard and judged by this Tribunal."[15]

This hands-off approach solidified a shift in power to claimants because, in effect, the arbitrators chose not to evaluate for themselves whether the investor's complaints against the state, though presented as treaty claims, in fact fell within the scope of a contractual dispute resolution clause. Similarly, arbitrators adopted an interpretive presumption—put forward also by the *Vivendi (No 1)* annulment committee—that an exclusive jurisdiction clause must rule out investment treaty arbitration specifically if it is to preclude a treaty claim.[16] In other words, it was insufficient for such clauses to designate the contract-based forum to the exclusion of other forums generally. Adopting this presumption, arbitrators faced with a general waiver clause typically did not show restraint based on party autonomy, sanctity of contract, or other considerations.[17]

Arbitrators also facilitated parallel treaty claims by applying different thresholds to decide whether a claim related to the treaty or a contract. In *Sempra*, the tribunal decided that the contract-based forum had exclusive carriage over disputes that were "purely" contract-related, whereas the investment treaty tribunal could hear any disputes "relating to" the interpretation of the treaty.[18] According to the tribunal, if it did not characterize disputes based on this test of contractual purity, then "the contract would nullify the provisions of the treaty."[19] As such, the tribunal de-emphasized party autonomy and sanctity of contract in a situation where these principles appeared clearly to support restraint.

In other cases, arbitrators allowed the investor's claim to proceed by distinguishing one or more parties in the treaty arbitration from the parties to the contractual relationship or proceedings.[20] For example, in *National Grid*, the tribunal emphasized that the company that brought the treaty claim was different from the company that signed the concession contract, although the former owned the latter.[21] By this approach, a company could avoid an exclusive jurisdiction clause and bring a treaty claim simply by having a subsidiary negotiate the contract and litigate the contractual dispute.

Thus, investment treaty arbitrators erected a series of legal obstacles for states seeking to uphold their position under an exclusive jurisdiction clause. In doing so, they veered from alternative options that might invoke concepts of comity, *forum non conveniens*, or flexible versions of *lis pendens*. This created a major hurdle to the effectiveness of contractual dispute resolution clauses and allowed claimants and tribunals to distinguish almost any investment treaty claim from an underlying contractual relationship. In turn, it helped to fuel the boom in treaty arbitrations.

> "Investment treaty tribunals overwhelmingly declined to show restraint in the face of a contract based forum."

Treaty-based requirements also side-stepped

On another track, tribunals in many cases declined to give effect to treaty provisions that supported restraint to avoid parallel proceedings. First, most arbitrators took a soft approach to wait periods under an investment treaty by allowing an investor claim to proceed even though the claimant had not waited the required period before bringing a treaty claim. In 14 of 19 cases where this issue appeared to arise, the tribunal allowed the treaty claim to proceed.[22]

Tribunals justified this position on various rationales, including that the treaty was not sufficiently clear and precise,[23] that the issue raised by the wait period was insignificant because the tribunal would have allowed the claim to be re-submitted in due course,[24] that imposing the wait period would have little effect other than to increase any damages owed by the state,[25] that the respondent state's obligation to provide most-favoured-nation treatment extended to dispute settlement processes such that wait periods were removed or shortened for all claimants,[26] or that giving effect to a wait period would nullify the treaty's role to provide access to international arbitration regardless of whether an investor resorted to other remedies.[27] Many of these rationales are highly debatable, at least, and they indicate how arbitrators usually chose to expand their role in the face of treaty provisions that appeared precisely to constrain it.

Incidentally, such arcane legal interpretations by arbitrators could sow the seed for a monumental harvest, such as in *Occidental (No 2)* where the tribunal awarded over US$2.3 billion (including pre-award interest) against Ecuador after allowing the claim to proceed in spite of a treaty-based wait period. The tribunal reasoned that it would have been futile for the investor, during the wait period, to have continued to pursue a negotiated solution; paradoxically, on the same facts, the tribunal also concluded that Ecuador had acted disproportionately by terminating a contract with the claimant instead of continuing to negotiate.[28] In this case and others, arbitrators framed wait periods as an option instead of a prerequisite for treaty claims. In doing so, they put aside an apparent precondition for the state's consent to arbitrate under the treaty.[29]

Arbitrators took a similarly expansive position when faced with a fork-in-the-road clause in a treaty. Such clauses require claimants to choose between bringing a claim under the treaty or resorting to another forum such as domestic courts or a contract-based forum. In all but two of 17 relevant cases the tribunal did not bar an investor claim although it was subject to a fork-in-the-road clause that appeared not to have been satisfied by the claimant.[30]

Conclusion

Remarkably, had tribunals taken a general position of restraint in these contexts—especially out of respect for contract-based forums—then investor claims under the treaties in many cases, perhaps most, would have had to wait for a resolution in another forum. As mentioned at the outset, in cases in which the tribunal did not show restraint—although the claim appeared to relate to a contract with a dispute settlement clause that had been agreed previously by the claimant or a related entity—states were ordered to pay at least US$1.2 billion overall.[31] This amount would rise to US$3.5 billion if one included the award in *Occidental v Ecuador (No 2)*.[32] It is not for nothing that investment treaty arbitration has boomed, based partly on the *de facto* policy choices of for-profit arbitrators.

Author

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Notes

1 Below n 34.

2 The study and methodology are reported in *Sovereign Choices and Sovereign Constraints: Judicial Restraint in Investment Treaty Arbitration* (Oxford University Press, 2013). The findings noted here were based on content analyses of investment treaty awards decided and publicly-available by cut-offs ranging from May 2010 to October 2012.

3 Ibid, 122-4.

4 *Vivendi v Argentina (No 1)* (Award, 21 November 2000), p 2-3 and 28.

5 Ibid, p 28-9.

6 *Vivendi v Argentina (No 1)* (Annulment decision, 3 July 2002). See above n 2, 135-47, for a more elaborate analysis of the decision.

7 Ibid, para 86-7 and 115.

8 See also *Wena Hotels v Egypt* (Award, 8 December 2000) para 331-2.

9 This is based on the limited grounds for annulment under the ICSID Convention, article 52(1); e.g. *MCI Power v Ecuador* (Annulment decision, 19 October 2009) para 49.

10 Five examples of restraint, comparable to the original decision in *Vivendi (No 1)*, emerged from the study: *SGS v Philippines* (Award, 29 January 2004) para 155 and 170 (note 95); *Joy Mining v Egypt* (Award, 6 August 2004) para 81 and 89-94; *Salini v Jordan* (Award, 9 November 2004) para 70, 76, and 100-1; *SGS v Pakistan* (Award, 6 August 2003) para 177; and *Bureau Veritas v Paraguay* (Award, 29 May 2009) para 159 and 161. Another example emerged from incidental related searches after the cut-off for content analysis on this issue: *Paushok v Mongolia* (Award, 28 April 2011) para 557. These include examples of abstention (declining or staying jurisdiction) and in-built restraint (interpreting a particular standard restrictively) due to the role of a contract-based forum.

11 Above n 2, 135-6.

12 Above n 7 above, para 101.

13 e.g. *IBM v Ecuador* (Award, 22 December 2003) para 69; *Sempra v Argentina* (Award, 11 May 2005) para 121; *Desert Line Products v Yemen* (Award, 6 February 2008) para 134-6.

14 *Siemens v Argentina* (Award, 3 August 2004) para 180 [emphasis added].

15 *Eureko v Poland* (Award, 19 August 2005) para 113.

16 Above n 7, para 76-9.

17 e.g. *TSA Spectrum v Argentina* (Award, 19 December 2008) para 58; *SGS v Paraguay* (Award, 10 February 2012) para 180.

18 *Sempra v Argentina* (Award, 11 May 2005) para 123.

19 Ibid.

20 e.g. *Nykomb v Latvia* (Award, 16 December 2003) p 9; *RDC v Guatemala* (Award, 18 May 2010) para 130-1.

21 *National Grid v Argentina* (Award, 20 June 2006) para 169.

22 For a list of the cases, see above n 2, 148 (note 171).

23 *Gas Natural v Argentina* (Award, 17 June 2005) para 30.

24 *Ethyl v Canada* (Award, 24 June 1998) para 84-5.

25 *Link Trading v Moldova* (Award, 16 February 2001) para 8.6.4.

26 *Maffezini v Spain* (Award, 25 January 2000) para 21-3.

27 *PSEG v Turkey* (Award, 4 June 2004) para 161-2.

28 The tribunal also appeared to conclude that the claimant had waited the required period. *Occidental v Ecuador* (No 2) (Award, 9 September 2008) para 92-4; *Occidental v Ecuador (No 2)* (Award, 5 October 2012) para 432-6.

29 *Republic of Argentina v. BG Group PLC* (DC Cir, January 17, 2012) p 17 (where the court set aside the award due to the claimant's failure to satisfy the treaty's wait period).

30 For a list of the cases, see above n 2, 149 (note 181).

31 This reflects amounts awarded in known awards with publicly-available materials up to June 2010 and does not incorporate awards of pre-award interest in most cases, amounts paid by states to settle claims, or annulment outcomes: *Siemens v Argentina; National Grid v Argentina; Azurix v Argentina; Sempra v Argentina; CMS v Argentina; Vivendi v Argentina (No 2); Enron v Argentina; LG&E v Argentina; Rumeli Telekom v Kazakhstan; Nykomb v Latvia; PSEG v Turkey; Desert Line Projects v Yemen.* In other relevant cases, an order for compensation was apparently still pending or not public or the case apparently settled after a decision on jurisdiction. Above n 2, 156 (note 219).

32 Above n 29.

Proposed Changes to the Investment Dispute-Resolution System: A South American Perspective

Hildegard Rondón de Sansó

feature 3

The system of international investment arbitration suffers from serious flaws. In South America, more than other regions, these failings are apparent from direct experience. Although South America does not attract the most foreign direct investment, the region has historically encountered the largest number investment-treaty arbitrations. This is in spite of the fact that we are ruled by democratically elected governments, with well-established institutions and laws.

Perhaps because so many countries in the region have faced multiple international investment arbitrations based on multi-million dollar claims for compensations, a number of alternatives to the current system of investment dispute resolution have been proposed by governments, multilateral institutions and academics. While these proposals are not only applicable to South America, the region has been particularly active in identifying solutions or alternatives. This brief article summarizes some of those alternatives.

Mandatory periods of amicable settlement and mediation before arbitration

This proposal, which has been discussed in academic and government forums, involves the development of contractual, treaty or other legal provisions whereby the investor and state, once a dispute has arisen, will be required to enter an initial period of amicable settlement and mediation before being allowed to move to arbitration.[1] This would require demonstrating that communication denoting the existence of a dispute has been exchanged between the investor and host state, which would form the basis for starting the amicable settlement phase of the dispute resolution process. If the period of amicable settlement is unsuccessful, the parties must then begin a formal process of mediation for a specified period of time. Only after this second phase has concluded can the parties submit the dispute for arbitration.

In an effort to try and avoid the present situation, where many arbitration tribunals allow claimants to avoid pre-arbitration requirements in investment treaties that demand amicable settlement or the use of local remedies, with the excuse that it would be "futile" or that it is a matter of admissibility and not of jurisdiction, the implementation of this proposal would expressly indicate—in specific instruments—that the phases prior to arbitration *must* be properly concluded.
The advantage of this proposal is that it creates conditions for parties to communicate, negotiate and seek mediated solutions with each other, in an effort to resolve the dispute at a low cost. However, the disadvantage is, if negotiation and mediation are not successful, the disputing parties incur into additional time and costs.

Resolution of disputes by local tribunals

This proposal, which some governments consider viable, has two variants:

a) A special foreign investment jurisdiction. This would entail the establishment of specialised administrative courts, made up of judges specialised in investment law, trade law, administrative law and administrative disputes, business accounting, and political sociology.

b) A system of associated judges. Here, investors would be permitted to appoint a jurist of high prestige to join the sitting judge and therefore be part of the competent national court.[2] This proposal might require legal reforms in some countries. Due to the local nature of the tribunals, it is likely that one of the requirements of the associated judges would be to have a license to practice law in the host country. However, as investment disputes are likely to be solved based on international investment agreements, which have the dual nature of national and international law (i.e. having been ratified by the legislative branches of the states), some adjustment to national law could be made to allow the possibility of appointing foreign lawyers that meet the other requirements of associated judges.[3]

The advantage of this proposal is that the investor might lose its fear of a lack of impartiality on the part of local judges, as the tribunals will be partially constituted with jurists selected and appointed by them. Likewise a decision by a national tribunal will be easier to accept by the state for purposes of voluntary enforcement. For states the advantage is that the disputes will be solved in their territories, in their jurisdiction and through their procedures. However, the disadvantage of this option is that it may be perceived by foreign investors as lacking the neutral and international edge that is apparently valued in the current system.

Creation of a regional investment tribunal

A regional investment tribunal could be formed, for example, under the Union of South American Nations (UNASUR: Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Guyana, Paraguay, Peru, Surinam, Uruguay, and Venezuela); the Bolivarian Alliance for the Peoples of Our Americas (ALBA: Antigua and Barbados, Bolivia, Cuba, Dominica, Ecuador, Honduras, Nicaragua, San Vicente and the Grenadines, and Venezuela); or Southern Common Market (MERCOSUR: Argentina, Brazil, Paraguay, Uruguay, and Venezuela).

To be established by a treaty, such a public institutional undertaking could serve the interests of states and investors. Likewise, by establishing new arbitration rules, it could provide improved legitimacy, predictability and transparency, compared to the arbitration rules linked to the World Bank's International Centre for Settlement of Investment Disputes (ICSID) and United Nation Commission on International Trade Law (UNCITRAL).

It has also been proposed that the treaty establish a roster of judges which would be assigned randomly to cases, thus moving away from the system of party-appointed arbitrators.[4] Judges could be nominated for a specific period and cases be assigned in accordance with internal rules. Of course, the persons nominated to an investment tribunal will have to meet certain ethical and professional requirements, including sufficient knowledge of international investment law. This structure would help inspire confidence in the level of competence of judges among investors, and satisfy states by providing permanence, transparency and predictability within the framework for resolving disputes.

The parties to a dispute will have the option of accepting or refusing to resolve conflicts using these permanent investment tribunals. Consent could be given via treaties, laws, notifications or the presentation of a dispute, as is currently the case.

States that agree to create permanent investment tribunals can finance them as is done at the World Trade Organization or other permanent regional tribunals. Some of the funds will be used to pay the salaries of judges. In fact, states may favourably compare the costs of financing permanent tribunals with the amounts paid in investment arbitration costs and fees.

These tribunals will probably compete with with existing dispute resolution options, such as ICSID and UNCITRAL, which feature in most investment treaties. But over time, and as the reputation of these new tribunals grows, they will be capable of attracting further cases. Moreover, with future treaties, states would be able to formally grant consent to submit disputes to tribunals alone or as an alternative.[5]

Currently, there are 21 international investment agreements between the UNASUR countries. Thus, were South America to create a South American Court on Foreign Investments, the court could immediately have jurisdiction to disputes pertaining more than 20 international investment agreements, provided the relevant countries mutually grant consent.

This option has the advantage of creating a neutral and permanent international centre for investment dispute resolution. The disadvantage is that the centre would have to be created, structured, supplied and qualified, and even then it may not attract many cases. However, the experience of the first years of ICSID is a useful example. With few staff, its first years were mainly educational, dedicated to technical qualifications and publications, among other things. A permanent foreign investment court would assume the role of a qualifying, informational, and decision-making body.

Currently this is the proposal that appears to have received the most support in the South American diplomatic arena, and one that possibly would be best suited to provide a neutral, professional and stable forum for investment dispute resolution.[6]

Designation of first instance to national tribunals and second instance to two or three appeal courts in different South American countries

This option, conceived by the author,[7] involves a combination of some of the earlier proposals and therefore carries the same advantages and disadvantages. For example, the disputes could be settled by a local court composed by associated 'partner' judges. The appeal could be submitted before a specially created international tribunal or before the highest judicial forum (to be identified in the relevant treaty) in a third country.

The advantage of this proposal is that it could provide legitimacy to the adjudicators, stability to the court, consistency on its decisions, and neutrality of the court, all of which could reduce the cost of the litigation. An intermediate method is to enable the possibility—via the same treaties in which this appeal method is established—that courts that recognise these appeals may be made up of associate judges in conjunction with sitting judges.

The important point is that due to the crisis of the international system of settlement of investment disputes, creativeness is required in order to arrive at alternatives that offer fairness and are supportive of sustainable social and economic development.

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Notes

1 *How to Prevent and Manage Investor-State Disputes: Lessons from Peru*, Best Practices in Investment for Development Series (United Nations, New York and Geneva, 2011) page 32.

2 Corte Plena de la entonces Corte Suprema de Justicia de Venezuela, caso "Apertura Petrolera" de fecha 17 de agosto de 1999, voto salvado.

3 Hildegard Rondón de Sansó, *Aspectos Jurídicos Fundamentales del Arbitraje Internacional de Inversión*, page 102, (2011).

4 Karsten Nowrot, *International Investment Law and the Republic of Ecuador: from arbitral bilateralism to judicial regionalism,* Beitrträge zum Transnationalen Wirtschafsrecht, Mayo de 2010, page 46.

5 Omar E. Garcia-Bolivar. 2012. "*Has the time arrived for permanent investment tribunals*?" International Investment Law http://works.bepress.com/omar_garcia_bolivar/15

6 Vid, Protocolo Constitutivo del Centro de Mediación y Arbitraje de la Unión de Naciones Suramericanas "UNASUR" en materia de inversiones, http://www.unasursg.org/uploads/4f/d0/4fd027384196e5e0073e36cf76cffc6d/Protocolo-constitutivo-Centro-de-Mediacion-y-Arbitraje-en-materia-de-inversion.pdf

7 Vid Hildegard Rondón de Sansó, *Vías sustitutivas del arbitraje internacional de inversión (Alternative ways to international investment Arbitration) Quinto Día, 8 de junio de 2012* http://www.quintodia.net/pais/2473/vias-sustitutivas-del-arbitraje-internacional-de-inversion

Australia changes position on investor-state arbitration in free trade agreement with Korea

The Australian government has agreed to investor-state arbitration in the investment chapter of a free trade agreement with Korea, abandoning the position of the previous government which had made a decision not to sign up to such commitments.

The deal, signed in December but not yet public, concludes negotiations that began in 2009.

The previous Labor-led coalition committed to rejecting investor-state dispute resolution in 2011. The government justified the policy on the basis of not allowing "greater rights" to foreign investors and maintaining its "ability to impose laws that do not discriminate between domestic and foreign businesses" to protect the public interest.

That position hardened when Philip Morris, the tobacco company, sued Australia under the Hong Kong-Australia bilateral investment treaty over legislation that limits branding of tobacco products.

However, the new Liberal-National coalition has said it would take a more flexible approach to investor-state arbitration, considering it on a case-by-case basis.

In the new agreement with Korea, the Australian government said that it "has ensured the inclusion of appropriate carve-outs and safeguards in important areas such as public welfare, health and the environment." The text of the agreement was not public as ITN was going to press, so it was not possible to verify the nature of those carve-outs and safeguards.

Investor-state arbitration has proven divisive in the Trans Pacific Partnership Agreement (TPP)—the mega regional trade and investment agreement that is currently under negotiation. Australia has not confirmed whether it would sign on to investor-state in the TPP, preferring instead to keep its options open.

European Commission goes on the offensive to promote investment treaties

In recent months the European Commission—the executive body of the European Union—has released a number of documents that seek to drum up support for investment treaties.

In October it published a fact-sheet titled *Incorrect claims about investor-state dispute settlement*, which seeks to refute common concerns about investment arbitration.[1]

For instance, in response to the claim that investor-state dispute settlement "subverts democracy by allowing companies to go outside national legal systems," the Commission responds "Untrue!" While not exactly responding to that claim, the Commission points out that an "investor may not want to bring an action against the host country in that country's courts because they might be biased or lack independence," or "might not be able to access the local courts in the host country."

A factsheet published in November, however, acknowledges that the investment protection provisions in international treaties have "imperfections." *Investment protection and investor-state dispute settlement in EU agreements* identifies two areas where improvements are needed: to investment protection rules, and how the investor-state dispute settlement system operates.[2]

The Commission identifies the "main concern is that the current investment protection rules may be abused to prevent countries from making legitimate policy choices." It points to Philip Morris' case against Australia, and Vattenfall's case against Germany, as examples that raise this concern.

The factsheet goes on to outline how the Commission is responding to these concerns by better defining investment protection rules and the procedures that guide arbitrators.

With respect to investment protection rules, the Commission says that EU agreements preserve states' right to regulate. For example, on indirect expropriation, "the right of the state to regulate should prevail over the economic impact of those measures on the investor." On fair and equitable treatment—which is frequently invoked by claimants—the EU's agreements will "set out precisely which actions are not allowed."

Turning to dispute settlement, the Commission seeks to discourage frivolous claims, such as by setting rules that encourage tribunals to settle such cases quickly and ordering the claimant to pay for legal costs. In response to concerns about the independence of arbitrators, the EU has established a new code of conduct. It is also aiming to set up an appellate mechanism "to ensure consistency and increase the legitimacy of the system by subjecting awards to review."

The Commission seeks to show how these approaches have been put into practice in a third document on the EU-Canada free trade agreement, which was concluded last October.[3] Under headings like "How is the right to regulate protected in the investment chapter?" and "Investor state dispute settlement in CETA: main achievements," the Commission outlines where it believes that progressive moves have been made to improve international investment rules in that agreement.

Ecuador sets up a commission to audit its bilateral investment treaties

Ecuador announced in October 2012 that it had established a commission to audit 26 of its bilateral investment treaties. A similar type of commission examined Ecuador's external debt in 2008, and its conclusions ultimately prombted the country to default on US$3.2 billion in global bonds.

The commission has been tasked with determining whether Ecuador's BITs compromise sovereignty and are beneficial to the country. Ecuador's Foreign Minister, Ricardo Patino, said the purpose of the commission is to "discover things that in the past did too much damage to Ecuador."

Ecuador has been a respondent in at least 26 investment treaty arbitrations—the third highest after Argentina and Venezuela. It has also been on the receiving end of the largest damages award in investment treaty history, having been ordered in September 2012 to pay US$1.77 billion in damages to Occidental Petroleum Corporation. Ecuador initiated annulment proceedings in that case earlier this year.

Similar to Bolivia and Venezuela, Ecuador has also given notice of its withdrawal from the ICSID Convention.

The commission includes lawyers, academic and lobbyists from a variety of Latin American countries. It has been given 8 months to produce its report.

Notes

1 http://trade.ec.europa.eu/doclib/docs/2013/october/tradoc_151790.pdf

2 http://trade.ec.europa.eu/doclib/docs/2013/november/tradoc_151916.pdf

3 http://trade.ec.europa.eu/doclib/docs/2013/november/tradoc_151918.pdf

awards & decisions

Libya ordered to pay US$935 million to Kuwaiti company for cancelled investment project; jurisdiction established under Unified Agreement for the Investment of Arab Capital

Mohamed Abdulmohsen Al-Kharafi & Sons Co. v. Libya and others, Final Arbitral Award

Diana Rosert

A tribunal has ordered Libya to pay US$935 million in a dispute over a land-leasing contract for a tourism project—marking the second-largest known investment treaty award to date.

The March 22, 2013, award upheld the tribunal's jurisdiction and ruled Libya responsible for breaches of contract, national law and the Unified Agreement for the Investment of Arab Capital in the Arab States (Unified Agreement). Libya's nominee to the tribunal, Justice Mohamed El-Kamoudi El-Hafi, refused to sign the award.

Background

In 2006, the Libyan Ministry of Tourism approved an investment project proposed by Al-Kharafi & Sons Co. for the construction and operation of a tourism complex. Shortly after, the Kuwaiti company signed a 90-year land-leasing contract with the Tourism Development Authority, comprised of 24 hectares of state-owned land in Tajura, a city in the Tripoli district. The project was to start in 2007, but construction work never commenced. The Ministry of Economy annulled the project approval in 2010; as a result, the land-leasing contract was also invalidated.

Al-Kharafi & Sons Co. launched its claim against Libya and several authorities in 2011, with two main complaints. Firstly, the claimant asserted that the Tourism Development Authority did not hand over the property "free of occupancies and persons" as required by the contract, and that the Libyan State, through various authorities, was responsible for delaying construction. Secondly, the claimant alleged that annulment of the approval and the cancellation of the land-lease contract were both illegal. Considering that these acts and omissions constituted breaches and caused damages, the claimant demanded compensation from the Libya state.

A tribunal was instituted under the Unified Agreement under consideration of the arbitration clause contained in the land-leasing contract.

Background on the Unified Agreement

Libya and Kuwait ratified the Unified Agreement, to which many other Arab League members have acceded, in 1982. Besides capital liberalisation and protection provisions, the Agreement provides that disputes, including those between state parties and Arab investors, shall be settled through conciliation, arbitration or by the Arab Investment Court established for that purpose. The Agreement also states that the two disputing parties "may agree to resort to arbitration" if they cannot agree on conciliation; if the decision of a conciliation is not rendered within the required time or is not unanimously accepted by the parties. Notably, this is commonly considered not to provide the signatory states' advance consent to arbitration.[1]

Tribunal assumes jurisdiction on basis of land-leasing contract and the Unified Agreement

The claimant argued that it had access to arbitration under the Unified Agreement by virtue of the arbitration clause contained in the land-leasing contract which referred to the Unified Agreement. The contract determined that disputes between the parties "arising from the interpretation or performance of the present contract during its validity period … shall be settled amicably" and, if this failed, "the dispute shall be referred to arbitration pursuant to the provisions of the Unified Agreement."

The tribunal deemed that the wording of the contract clause established consent to arbitration under the Unified Agreement. "A fortiori, the two parties explicitly chose to resort to arbitration as provided for in Article (29) of the contract," the tribunal reasoned.

Challenging jurisdiction under the Unified Agreement, Libya maintained that the project did not involve the transfer of Arab capital from Kuwait to Libya and therefore the "substantive scope for the application of this Agreement is not fulfilled ipso facto." Aside from the undisputed fact that the construction works on the tourist complex never began, Libya pointed out that the claimant failed to deposit 10% of the established value of the investment project in a Libyan bank account as requested by the General Authority. While the claimant was able to show that it had paid 0.1% of the value to the Authority, Libya contended that was not a proof for the existence of an Arab investment.

Nonetheless, the tribunal determined that the Kuwaiti company's payment of 0.1% of the investment value constituted a transfer of Arab capital, and the tribunal saw no legal obligation for the claimant to pay 10% at a minimum.

Libya also objected to the tribunal's jurisdiction arguing that the case fell outside of the limited scope of the arbitration clause contained in the contract. In its view, the clause excluded disputes relating to non-performance, cancellation of the contract and "anything arising after its expiry and any disputes related to compensation claims for any damages." It stated that "arbitration is a special judicial system arising from the will of the parties to resort thereto … this leads to conclude that the present claim does not fall within the jurisdiction of the arbitration Tribunal."

Addressing this objection, the tribunal deemed that it was competent to rule on the "scope of extension of the arbitration clause" so as to cover the annulment of the contract and compensation for damages. Since it had already determined that the Unified Agreement applied to the dispute, the tribunal considered that the arbitration rules stated therein applied to the case, including Article 2.6 of the Unified Agreement's Annex, which states that the "arbitral panel shall decide all matters related to its jurisdiction and shall determine its own procedure." The tribunal interpreted this as giving it competence to rule on its own competence as well as the extension of scope of the contract clause.

Another jurisdictional objection related to the contract's requirement of amicable settlement prior to arbitration. Libya contended that the claimant did not make serious efforts to fulfill it and asserted that the arbitration was therefore filed prematurely, while the claimant argued that it had attempted to settle the dispute amicably. The tribunal found that both parties "made amicable endeavors," and since all endeavors failed, the claimant was permitted to file the arbitration.

Given that only the Tourism Development Authority was a signatory of the contract, Libya argued that the contract provisions could not be invoked against the

Libyan government and the other authorities. Granting the claimant's request to extend the arbitration clause to non-signatories of the contract, the tribunal determined that "the intervention of multiple government bodies and public institutions as well as ministries in the contract performance or termination" gave the contract a "governmental character." However, it declined to include the Libyan Investment Authority as a disputing party, considering that, unlike the others, this institution was not involved in the dispute.

The tribunal further established that the land-leasing contract was a private law contract governed by the Libyan Civil Code, national laws on the Promotion of Foreign Capital Investment (Libyan Investment Law) and the Unified Agreement.

Libyan defendants found to have frustrated claimant's project execution

With respect to the merits, the first contentious issue was whether the Tourism Development Authority had handed over the land to the claimant according to the terms of the contract. The contract signed by both parties stipulated that the tourism authority "undertakes to hand over … the plot of land free of any occupancies and persons, guarantees that there are no physical or legal impediments preventing the initiation of the project execution or operation during the usufruct period immediately upon the signature of this contract, and permit it to take physical possession thereof for the purpose of establishing the project."

According to the claimant, the tourism authority failed to fulfill this contractual obligation, because other persons and businesses occupied the land and impeded the execution of the project from the outset. The claimant asserted that during several attempts to take over the land and build a fence, it was assaulted by municipal guards and other occupants. It alleged that the tourism authority was aware of these obstacles, but refrained from evacuating the land. Instead the authority demanded that the claimant stall the project until the issues were resolved and offered an alternative plot of land.

However, according to Libya, the claimant took over the site in 2007 "free of any occupancies or impediments." It maintained that Al-Kharafi & Sons Co. was responsible for the delays due to its failure, among other things, to provide the authorities with final project designs, deposit 10% of the project value on a Libyan bank account, and apply for permits.

The tribunal found that "all the data and facts established" confirmed the claimant's allegations that the land was not "free of occupancies," and that Libyan authorities prevented it from starting the project. The tribunal also concluded that the claimant did not cause any "self-inflicted obstacles." Indeed, it held that Libya's offer to provide the Kuwaiti company with alternative land was "further proof of the Defendants' failure." The tribunal therefore ruled that Libya breached a primary obligation of the leasing contract, as well as the Libyan Civil Code that required it to adhere to such obligations. Furthermore, the tribunal noted that the case involved "administrative corruption." Even if not "organized or deliberated" by the Libyan state, Libya had committed "gross negligence and disregard of investment rules."

Decision to annul project considered to have led to "confiscation, liquidation, freezing and control of the investment"

The tribunal went on to consider the claimant's assertion that the annulment of the project approval by the Ministry of Economy was an "illegal act" in violation of various Libyan laws and provisions of the Unified Agreement.

Libya argued that the ministry cancelled the approval due to a four-year delay in construction. It maintained that the step was taken in accordance with national laws as well as the contract, which in Article 24 expressly stated the authority's right to terminate the contract if the project was not executed in time.

Meanwhile, the claimant argued that the "real reason" behind the annulment was that Libya neglected its obligation to hand over the land free of occupants.

The tribunal ruled that the annulment constituted a second serious violation of Libya's obligations. While recalling that all evidence confirmed that Libya was responsible for the delay, it disproved Libya's factual allegations concerning the claimant's faults one by one. Examining liability under different law, it found that the annulment was "an arbitrary decision" that led to confiscation, liquidation and freezing of project which was prohibited by Libyan Investment Law and Article 9(1) of the Unified Agreement. The tribunal decided that the Libyan authorities were liable for those breaches and obliged to pay compensation according to the Libyan Civil Code.

US$935 awarded for lost profits, moral damages, and material losses and expenses

The tribunal ordered Libya to pay US$5 million for value of losses and expenses suffered by the Kuwaiti company, US$30 million for moral damages and US$900 million for "lost profits resulting from real and certain lost opportunities."

It is noteworthy that, in the course of the proceeding, the claimant increased the compensation claim to more than US$2 billion covering lost future profits for 83 years, corresponding to the length of the revoked land-leasing contract. Originally, Al-Kharafi & Sons Co. had claimed US$55 million which it amended to US$1,144,930 billion in September 2012. Libya maintained that the company "incurred damages, if any, due to its own faults" and considered the compensation claim to be "characterized by corruption."

Compensation for moral damages to claimant's reputation awarded

The claimant demanded US$50 million in moral damages, in addition to US$5 million for material losses and expenses related to the opening of an office in Tripoli. It argued that it should receive this "merely symbolic" amount because the cancellation of the project damaged its high national and international reputation.

The Libyan defendants contested that moral damages had not occurred and pointed out that the claimant had not submitted proofs in this regard.

Ultimately, the tribunal decided that compensation for moral damages was permitted under Libyan law and that the claimant was entitled to it. It considered that the claimant suffered moral damages "to its reputation in the stock market, as well as in the business and construction markets in Kuwait and around the world."

The tribunal's decision on moral damages is an outlier in the field of investment arbitration. Moral damages claims have been raised in other investment treaty arbitrations, but tribunals commonly placed strict conditions on the validity of such claims. For instance, in *Rompetrol v. Romania*, the tribunal considered that moral damages were "subject to the usual rules of proof."[2] It eventually rejected the claimant's demand of US$46 million for moral damages "for loss of reputation and creditworthiness." The tribunal in *Arif v. Moldova*[3] dismissed a moral damages claim of €5 million, holding that the "different actions did not reach a level of gravity and intensity" sufficient to justify it.

US$2 billion considered "sound and convincing" estimation of future lost profits

The company's claim of US$2 billion for lost profits was based on four reports that Ernst & Young, Prime Global (Khaled El-Ghannam), Habib Khalil El-Masri and Ahmad Ghatour & Partners prepared on the claimant's request and based on documents submitted by it.

Libya asserted that the reports lacked credibility because they were based solely on data and information provided by the claimant, which were not independently verified. Libya did not, however, present its own expert estimations.

Firstly, the tribunal determined that the Libyan Civil Code (Article 224), supported by Libyan Supreme Court rulings, covered compensation for lost profits. It deemed that the UNIDROIT Principles of International Commercial Contracts confirmed that it had discretion to decide on such issues. It then interpreted the Libyan law on compensation for damages, concluding that the lost profit claim was valid only if damages resulted from opportunities that were "real and certain."

Secondly, the tribunal found that the submitted reports on lost profits were "scientific and unbiased reports" by firms with good reputations. The tribunal noted that Libya's criticism of the reports was not on "the same level of expertise," since it had not submitted own expert reports disproving any of the findings.

Based on those conclusions, the tribunal decided that the reports with estimations ranging from US$1.7 to 2.6 billion were "sound and convincing." Two of the experts that had drafted reports, Khaled El-Ghannam and Habib Khalil El-Masri, confirmed during a hearing that the amounts were "certain lost profits" and constituted a "minimum" of what the claimant "would have otherwise certainly realized in the normal conditions currently prevailing in Libya."

However, instead of awarding the arithmetic average of US$2.1 billion, the tribunal decided to reduce the amount of compensation for lost profits, "by virtue of its discretionary power," to US$900 million. In light of the Libyan revolution, the tribunal noted that "this arbitration will serve as an incentive to government agencies" and "reassure the Arab investors."

Lost profit claims are not unusual in treaty or commercial arbitration, yet the amount awarded in under the circumstances of the present case appears to be distinct. For example, in a seminal case, *PSEG v. Turkey,* the tribunal declined to grant the claimants compensation for future lost profits of US$223.742 million for a power plant project that was not constructed.[4] The *PSEG* award recalled that other investment tribunals were also hesitant to award lost profits for not established businesses that, consequently, lacked historical evidence for profits.

The tribunal is composed of Dr. Abdel Hamid El-Ahdab (presiding arbitrator), Dr. Ibrahim Fawzi (claimant's nominee) and Justice Mohamed El-Kamoudi El-Hafi (respondent's nominee).

The award is available at http://www.italaw.com/sites/default/files/case-documents/italaw1554.pdf

ICSID tribunal finds Venezuela liable for not negotiating market value compensation for takings in good faith; other claims rejected *ConocoPhillips Petrozuata B.V., ConocoPhillips Hamaca B.V. and ConocoPhillips Gulf of Paria B.V. v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/07/30, Decision on Jurisdiction and Merits*

Diana Rosert

A tribunal has issued a decision on jurisdiction and merits in a claim by subsidiaries of the U.S. energy company ConocoPhillips against Venezuela some 5 years after the case was registered at ICSID.
The tribunal's September 3, 2013, ruling unanimously dismisses parts of ConocoPhillips' claims, both on jurisdiction and merits. However, Judge Kenneth Keith and L. Yves Fortier found a breach of the expropriation provision contained in the Netherlands-Venezuela BIT, while the third arbitrator, Prof. Georges Abi-Saab, dissented from the majority finding. The majority's decision on damages is forthcoming.

Background

ConocoPhillips' claims relate to its interests in three on- and off-shore oil projects in Venezuela: the Petrozuata Project, the Hamaca Project and the Corocoro Project. The Dutch incorporated subsidiaries of ConocoPhillips, which are the claimants in this case, invoke provisions of the Netherlands-Venezuela BIT, while the claims of the US parent company are based on the Venezuelan Law on the Promotion and Protection of Investments (Investment Law).

ConocoPhillips alleged that Venezuela violated fair and equitable treatment (FET) obligations and committed an unlawful expropriation. These complaints are linked to changes to the fiscal regime that applied to the oil projects, as well as migration and nationalization laws that involved a partial transfer of the claimants' rights to the national oil company, PdVSA, in order to establish mixed companies in the oil sector.

Negotiations between Venezuela and ConocoPhillips took place regarding the terms of the transfer, compensation, and the claimants' participation in the new mixed companies. However, after failing to reach an agreement after four months, the period foreseen in the nationalization decree for that purpose, Venezuela nationalized ConocoPhillips' interests in the three projects. The amount owed in compensation, and other related issues, remained unsettled.

Against this background, ConocoPhillips originally claimed damages amounting to some US$30 billion, while Venezuela insisted that "the claims […] should be dismissed in their entirety."

Although not addressed in the tribunal's decision, it is noteworthy that Venezuela terminated its BIT with the Netherlands in 2008 and withdrew from the ICSID Convention in 2012.

No jurisdiction over ConocoPhillips' claims under Venezuelan Investment Law

The tribunal dismissed the claims of the U.S. parent company with respect to its "loss of future tax credits" for lack of jurisdiction under Venezuela's Investment Law. Controversy surrounded the question whether Article 22 of the Investment Law conferred jurisdiction to the ICSID tribunal.

The article in question refers to disputes arising between an international investor from a contracting party of a BIT with Venezuela, as well as to disputes under ICSID, which was understood by the claimants as containing Venezuela's unilateral consent to ICSID arbitration, an assertion that Venezuela contested.

The tribunal concluded that "Venezuela has not consented to ICSID jurisdiction by enacting that provision." Given this decision, the tribunal did not further assess Venezuela's contention that ConocoPhillips was not an "international investor" in the sense of Article 22. The tribunal continued by addressing only the Dutch claimants' claims based on the BIT.

Notably, claimants in three other arbitrations against Venezuela—*Mobil, Cemex and Tidewater*—had also attempted to establish jurisdiction on the ambiguous wording of Article 22, but the respective tribunals ruled against them.[5]

Jurisdiction over BIT claims accepted despite allegations of treaty abuse

Venezuela also raised objections concerning the tribunal's jurisdiction under the BIT, asserting that the U.S. company established its three Dutch subsidiaries and transferred ownership to them solely to gain access to ICSID. In support of its argument, Venezuela alleged that the restructuring took place only after some of the disputed measures had occurred, meaning that "the Dutch claimants were not in existence or had not been inserted into the corporate chain of ownership" at that time. Venezuela also cited other ICSID cases that addressed "abuse of the corporate form and blatant treaty or forum shopping."

In response, the claimants asserted that "no principle of law" prohibited a restructuring "to benefit from the protection of another country's laws" and countered that it was carried out "before the changes were made in the tax law and before the investments were confiscated."

The tribunal confirmed that access to ICSID was "the only business purpose" of the restructuring, but it rejected Venezuela's objections. In its view, it was decisive that "the transfers of ownership in 2005 and 2006 did not attempt to transfer any right or claim arising under ICSID or a BIT from one owner to another." According to the tribunal, no ICSID or BIT claim existed or was "in prospect" at that time. The tribunal further stated that ConocoPhillips' continued expenditure on the projects after the restructuring was a "very weighty" factor speaking against treaty abuse.

It then decided that jurisdiction only existed over claims related to measures that entered into force after the restructuring of the respective projects. Accordingly, all three subsidiaries were allowed to claim breaches in respect of an income tax increase in 2007, the expropriation, and migration of interests. However, the tribunal determined that ConocoPhillips Hamaca could make no claim concerning an increase of the extraction tax in 2006 which entered into force before the restructuring of the Hamaca project took place.

Finding that the BIT's definition of investment was "written in broad terms," the tribunal briefly rejected Venezuela's contention that the investments of two companies, ConocoPhillips Hamaca and Gulf of Paria, were not covered by the BIT's investment definition, because they allegedly constituted indirect investments owned through intermediaries.

FET obligation in BIT considered not applicable to claims relating to tax measures

While ConocoPhillips claimed that several tax measures taken by Venezuela breached FET obligations, some contentions surrounded the question whether, in the first place, such matters fell within the scope of the FET provision expressed in Article 3 of the BIT. Article 4 of the BIT specifically addressed "taxes, fees, charges, and ... fiscal deductions and exemptions" but provided for non-discriminatory treatment, in the absence of FET. Assessing the interaction between the two articles at length, the tribunal concluded that ConocoPhillips' taxation claims were not covered by the FET provision. The disputed fiscal measures, understood to encompass royalties, were found to be subject to Article 4 exclusively. Given that ConocoPhillips did not claim breaches of the latter, the tribunal did not consider the issue any further.

Majority finds breach of expropriation provision in respect of "good faith" negotiations and "market value compensation"

At the outset, the tribunal noted that ConocoPhillips did not call into question "the Respondent's sovereign prerogative to nationalize," yet alleged that the expropriation was unlawful in that it breached conditions for expropriation set out in Article 6 of the BIT. Venezuela, in response, maintained the nationalization's lawfulness and denied liability.

Following a condition established in the BIT's Article 6(b), the tribunal assessed whether Venezuela's taking of assets breached an "undertaking" or "promise" that it allegedly made to the claimants in respect of taxation. It deemed that the claimants did not provide evidence of the existence of such a promise. Instead of substantiating "express stabilization commitments" or "fiscal guarantees," ConocoPhillips invoked "legitimate expectations." However, since the tribunal had ruled out the availability of FET provisions with respect to fiscal claims, it reasoned that the taking was not unlawful in the sense of Article 6(b).

The tribunal also dismissed ConocoPhillips' claims that Venezuela's measures between 2004 and 2007, including changes to the fiscal regime, constituted a single unlawful taking that should make it necessary for the tribunal to calculate compensation based on the value of assets under the original royalty and income tax rate regime. Recalling that such measures were outside of the scope of FET and were not in breach of the Article applicable to taxation, the tribunal decided that they were not relevant for the determination of quantum.

However, the tribunal found that Venezuela breached condition 6(c) of the expropriation provision in that it failed to negotiate in good faith with claimants over market-value compensation. Venezuela required oil companies, including the claimants, to migrate to mixed contracts or relinquish their rights in the projects. The terms of the transfer and the amount of compensation were to be negotiated between Venezuela and the claimants within a fixed period of four months. No agreement was reached within or after the period and the compensation issue remained unresolved, while the claimants' assets were fully nationalised in 2007. Venezuela maintained that "ConocoPhillips refused to participate in the negotiation process in any meaningful manner," while it made attempts to discuss "reasonable compensation." Contrary to this, the claimants alleged that the amounts of compensation offered by Venezuela during negotiations were "far below" the fair market value prescribed by the BIT and rather corresponded to the assets' book value which was deemed not to be an "adequate" standard of compensation.

Taking into consideration the accounts of two key witnesses for both sides, former President of ConocoPhillips Latin America, Mr. Lyons, and former Vice-Minister of Hydrocarbons, Dr. Mommer, the tribunal inferred that during meetings and through letters to Venezuelan ministers and officials, ConocoPhillips raised critical issues with respect to fair and book market valuation of assets that Venezuela indeed failed to respond to. For this reason it determined that "Venezuela at that time was not negotiating in good faith by reference to the standard of "market value" set out in the BIT." The tribunal also considered the fact that Venezuela did not make compensation offers for Corocoro, the third project.

Addressing a crucial issue for the amount of compensation, it determined that the valuation date for the assets should be the date of the award and not, as demanded by Venezuela, the date of the taking. Presumably, the latter would have led to lower compensation. The determination of quantum as well as the allocation of costs and expenses was postponed to a later stage.

The tribunal is composed of Judge Kenneth Keith (presiding arbitrator), L. Yves Fortier (claimants' nominee) and Prof. Georges Abi-Saab (respondent's nominee).

The award is available at http://italaw.com/sites/default/files/case-documents/italaw1569.pdf

Claim against Romania dismissed for lack of jurisdiction; claimants failed to abide by domestic litigation requirement

Ömer Dede and Serdar Elhüseyni v. Romania, ICSID Case No. ARB/10/22

Maria Antonieta Merino

In a decision dated September 5, 2013, a Turkish claimants' case before an ICSID tribunal was dismissed for failing to first pursue the dispute before Romanian's domestic courts.

Background

The claimants, Ömer Dede and Serdar Elhüseyni, acquired a 55% share in SC IMUM SA, a producer of agricultural equipment. As a condition of the share purchase agreement, the claimants were required to provide guarantees securing the performance of certain investment obligations.

Subsequent to the share purchase agreement, the Romanian Authority for Privatization and Management of State Ownership ordered an inspection of the company. Alleging non-fulfillment of several obligations relating to the share purchase agreement, the authority requested that the claimants' shares be transferred to its name. Soon afterwards, the company declared bankruptcy.

The claimants contended that the confiscation of their shares amounted to an illegal expropriation in violation of the 1996 version Romania-Turkey BIT (two versions of the Romania-Turkey BIT exist, and the claimants' relied on the earlier version).

Recourse to domestic courts deemed a pre-condition to accessing arbitration

Romania argued that the tribunal lacked jurisdiction over the dispute based on Articles 6(2) and 6(4) of the BIT, which require a good-faith attempt at amiable settlement and recourse to local courts, respectively.

However, the claimants attempted to draw a distinction between types of arbitrable disputes based on the use of different terms in the BIT. While Article 6(1) refers to "investment disputes," Article 6(2) refers to "any dispute" arising out of an investment. Considering this distinction, the claimants asserted that the investor could directly raise an "investment dispute" and submit it to ICSID, while the precondition to arbitration exists applies to "any dispute," which encompasses a broader category of controversies than the defined term "investment disputes."

The tribunal rejected this line of reasoning. It determined that the BIT does not comprise any additional category of controversy other than an "investment dispute" defined as "involving either (i) the interpretation or application of any investment authorization or (ii) the breach of any right conferred by the BIT." In both cases the definition of an "investment dispute" does not provide the investor the right to submit a dispute directly to ICSID.

Moreover, the tribunal confirmed that the entitlement to arbitrate is subject to express conditions of either exhaustion of local remedies or submission to local courts for a minimum of a year.

Tribunal rejects satisfaction of jurisdictional preconditions

Alternatively, the claimants asserted that even if the BIT contained jurisdictional preconditions, these were satisfied. However, in this case the tribunal determined that the claimants neither exhausted local remedies, nor litigated the dispute in local courts for a year.

Regarding the exhaustion of local remedies, the tribunal noted that the claimants could have sought relief through one of two general courses of action under Romanian law: (1) actions to obtain performance and (2) action whereby claimants could have sought termination of the SPA and compensation for damages. Yet the claimants did not pursue either course.

Failures on futility and MFN arguments

In cases where claimants have failed to abide by pre-arbitration requirements, it is common for them argue that: a) the most-favoured nation provision allows them to 'borrow' from third-party treaties that do not contain such requirements; or that litigating in local courts would be futile. However, neither of those arguments was raised by the claimants; a fact noted by the tribunal.

The scope of the tribunal's decision

Although the parties raised other arguments, the tribunal determined that since it lacked competence over the dispute, it was unnecessary and unwise to give its opinion on matters not pertinent to its conclusion.

Referring to the Article 48(3) of the ICSID Convention, which provides that the award shall deal with "every question submitted," the tribunal reasoned that this does not mean that it should comment on arguments that will have no effect on the award. Conversely, the tribunal expressed its disagreement with awards that addressed issues unnecessarily, considering such decisions inappropriate and needless.

Costs

None of the factors that justify cost allocation (such as unreasonable argument, exaggerated claim, or obstructionist tactics) was present in the arbitration, and the tribunal considered both parties conducted themselves in a way that furthered procedural efficiency.

Consequently, the tribunal concluded each side should bear its own legal expenses, and the costs of the arbitration should be divided on an equal basis.

The tribunal is composed of Professor William W. Park (President), Professor Brigitte Stern (respondent's appointee) and Dr. Nicolas Herzog (claimant's appointee).

The award is available here: http://italaw.com/sites/default/files/case-documents/italaw5010.pdf

UNCITRAL tribunal declines jurisdiction in claim against Kazakhstan due to a lack of valid agreement to arbitration
Ruby Roz Agricol LLP v. The Republic of Kazakhstan, Ad hoc Tribunal (UNCITRAL)
Marina Ruete

An UNCITRAL tribunal declined jurisdiction on August 1st, 2013, in a dispute between a poultry company and the Republic of Kazakhstan, having determined that there was no valid agreement to arbitrate.

The claimant, Ruby Roz Agricol LLP, had sought US$214,705,778 in damages.
Background

The Kazakh State Investment Agency entered into an investment agreement with the claimant in 1999. Owned at the time by Mr. Badaoui and his wife, the investment was encouraged by tax concessions and other preferences.

The company later became embroiled in a political dispute between President Nursultan Nazarbayev and his former son-in-law, Rakhat Aliyev. Kazakhstan asserted that the company was forcefully sold to Kassem Omar, a businessman with connections with Mr. Aliyev, while Ruby Roz alleged unlawful interference from the government as part of a reprisal against Mr. Aliyev. Intimidations continued during the proceedings, frustrating the presence of witnesses during hearings.

Consent to arbitration lapses after foreign investment law is repealed

The tribunal's decision on jurisdiction focused whether there was a valid agreement to arbitrate in Kazakhstan's domestic legislation and an investment contract.

The claimant argued that Kazakhstan's earlier foreign investment law – it was repealed in 2003 and replaced with a new law -- contains Kazakhstan´s standing offer of consent to international arbitration.

While Kazakhstan's new investment law does not include a standing offer to arbitrate investment disputes, the claimant argued it could rely on the repealed investment law given its stabilization clause.

Specifically, Article 6 of the old investment law provided that, in the case of changes in legislation or international treaties, foreign investments will be treated in accordance with the legislation in force at the time of the investment for a period of ten years.

In Kazakhstan's opinion, the old investment law, as a piece of domestic legislation, could be amended or repealed as the government wishes. In the case the tribunal considered that the stabilization clause survived the 2003 repeal, Kazakhstan offered the alternate argument that the ten-year period had, in any case, already expired.

The tribunal agreed with Kazakhstan's position, concluding that the offer of consent lapsed together with the repeal of the foreign investment law. It also pointed out that the right to arbitration needed the claimant´s written consent and this occurred only in June 2010.

Notably, the tribunal disagreed with the ICSID tribunal in *Rumeli Teleko & Telsim Mobil v. Kazakhstan*, which decided that the claimant had an "accrued right" to arbitrate under the same foreign investment law, and took the repealed law as a basis for its jurisdiction.

Ruby Roz is not a *"foreign investor"*

Kazakhstan also argued that the repealed foreign investment law and the investment agreement provided consent to arbitration only in the case of disputes with a foreign investor, which Ruby Roz was not. On this point the tribunal also agreed, finding that Ruby Roz was not incorporated under the laws of a foreign jurisdiction.

On the base that the stabilization period expired and the claimant was not a foreign investor, the tribunal decided there was no valid agreement to arbitrate and, consequently, that it lacked jurisdiction.

On the issue of costs, the tribunal drew up a separate procedural order with its decision on the arbitration costs and invited the parties to submit comments.

The tribunal is composed of Mr. Alan Redfurn (president), Mr. Bruno Boesch (respondent´s appointee), and Mr. Joseph Neuhaus (claimant´s appointee).

The decision is available here: http://www.italaw.com/sites/default/files/case-documents/italaw1558.pdf

Notes

1 As Walid Ben Hamida puts it, arbitration under the Unified Agreement is "subordinated to an agreement between the parties." See Walid Ben Hamida (2006), The First Arab Investment Court Decision, Journal of World Investment & Trade, Vol. 6, Issue 5, pp. 699-721 (p. 709).

2 *The Rompetrol Group N.V. v. Romania*, ICSID Case No. ARB/06/3, Award.

3 *Mr. Franck Charles Arif v. Republic of Moldova, ICSID Case No. ARB/11/23,* Award.

4 *PSEG Global Inc. and Konya Ilgin Elektrik Uretim ve Ticaret Limited Sirketi v. Turkey*, ICSID Case No. ARB/02/5, Award.

5 *Mobil Corporation et al. v. Venezuela*, ICSID Case No. ARB/07/27, Decision on Jurisdiction; *CEMEX Caracas Investments B.V. et al. v. Venezuela*, ICSID Case No. ARB/08/15, Decision on Jurisdiction; *Tidewater Inc. et al. v. Venezuela*, ICSID Case No. ARB/10/5, Decision on Jurisdiction.

resources and events

Resources

United Kingdom Assessment of the Costs and Benefits of Investment Protection Treaties

United Kingdom Department for Business, Innovation and Skills, November 2013

Three new reports commissioned by the Government of the United Kingdom examine the cost and benefits of investment treaties for the UK. The first report develops an analytical framework to assess costs and benefits of investment treaties. The second and third reports apply the framework to EU-China and EU-US agreements. The authors recommend that the UK government should consider either excluding the investment protection chapter from the EU-US free trade agreement altogether; or retaining investment protection provisions but excluding an investor state dispute settlement mechanism. The second option would not affect the "already negligible" benefits of an investment protection treaty while largely removing the costs of the treaty to the UK. According to the authors, those costs include the prospect of successful investment treaty claims, international investors gaining more rights under investment treaties than under UK domestic law, and the political cost associated with high-profile claims from US investors and, to a lesser extent, reduced scope to decide policy.

Analytical framework for assessing costs and benefits of investment protection treaties is available here: https://www.gov.uk/government/publications/analytical-framework-for-assessment-costs-and-benefits-of-investment-protection-treaties

Costs and benefits of an EU-China Investment Protection Treaty is available here: https://www.gov.uk/government/publications/costs-and-benefits-to-the-uk-of-an-eu-us-investment-protection-treaty

Costs and benefits of an EU-US Investment Protection Treaty is available here: https://www.gov.uk/government/publications/costs-and-benefits-to-the-uk-of-an-eu-us-investment-protection-treaty

How to Use Law to Make Foreign Investment Work for Sustainable Development

International Institute for Environment and Development, November 2013

This handbook shows how government officials and civil society organisations in low and middle-income countries can use legal tools to ensure foreign investments contribute to sustainable development. The book focuses on investments in agriculture and the extractive industries—mining, oil and gas. It covers the variety of legal arenas that can influence the outcomes of investments—from investment treaties, extractive industry legislation, land tenure, human rights norms, environmental legislation and tax law—including arrangements to fight tax avoidance. The book covers four main ways in which government and civil society can use legal tools to promote sustainable development: aligning public policies and decisions on investment with a strategic vision of sustainable development based on local and national aspirations; ensuring a fair economic deal; taking social and environmental considerations seriously; and balancing investment protection with competing policy goals. Available here: http://www.iied.org/how-use-law-make-foreign-investment-work-for-sustainable-development

Investment Law within International Law: Integrationist Perspectives

Cambridge University Press, December 2013

Developments within various sub-fields of international law influence international investment law, but changes in investment law also have an impact on the evolution of other fields within international law. Through contributions from leading scholars and practitioners, this book analyses specific links between investment law and other sub-fields of international law, such as the law on armed conflict, human rights, sustainable development, trade, development and EU law. In particular, this book scrutinizes how concepts, principles and rules developed in the context of such sub-fields could inform the content of investment law. Solutions aimed at resolving problems in other settings may provide instructive examples for addressing current problems in the field of investment law, and vice versa. The underlying question is whether key sub-fields of public international law, notably international investment law, are open to cross-fertilisation, or, whether they are evolving further into self-contained regimes. Available here: http://www.cambridge.org/gb/academic/subjects/law/arbitration-dispute-resolution-and-mediation/investment-law-within-international-law-integrationist-perspectives

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Events 2014

January 31
ASA ANNUAL CONFERENCE - 10 YEARS OF SWISS RULES OF INTERNATIONAL ARBITRATION, Swiss Arbitration Association, Basel, Switzerland, http://www.arbitration-ch.org/pages/en/asa-events/details/37.asa-annual-conference.html#.UothWmSxOFc

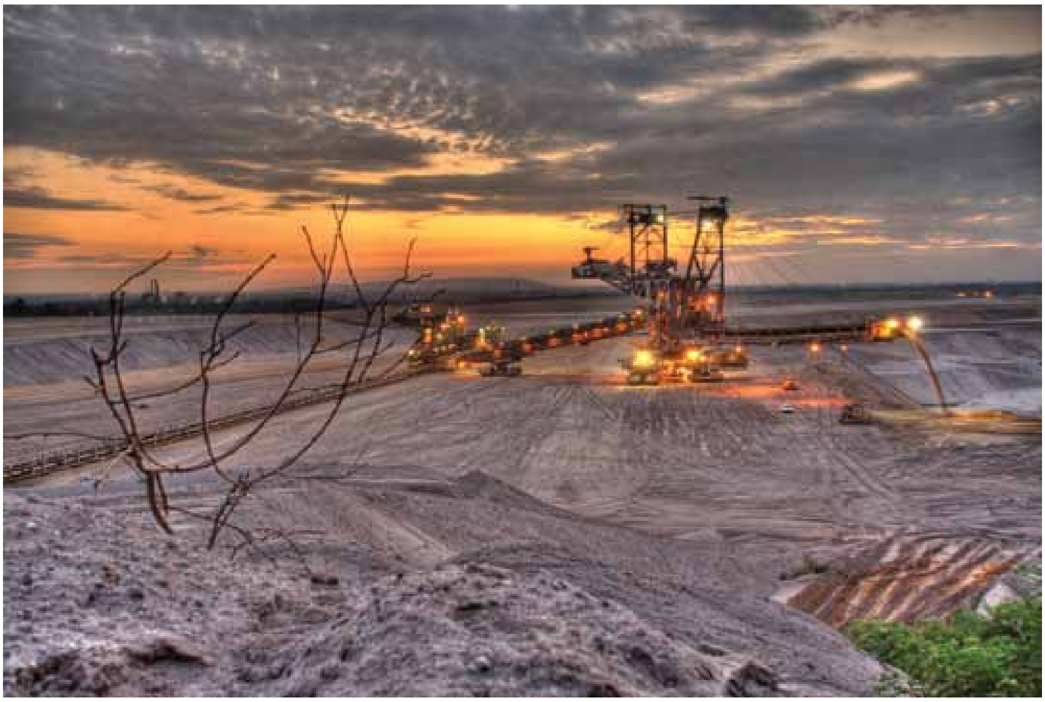
March 17 - 21
MULTI-YEAR EXPERT MEETING ON INVESTMENT, INNOVATION AND ENTREPRENEURSHIP FOR PRODUCTIVE CAPACITY-BUILDING AND SUSTAINABLE DEVELOPMENT, UNCTAD, Geneva, Switzerland, http://unctad.org/en/pages/meetingdetails.aspx?meetingid=427

March 21 - 23
ASA ARBITRATION PRACTICE SEMINAR, Swiss Arbitration Association, Tremezzo, Lago Di Como, Italy, http://www.arbitration-ch.org/pages/en/asa-events/details/72.asa-arbitration-practice-seminar.html#.uotiomsxofc

March 26 - 28
10TH ANNIVERSARY CONFERENCE OF THE ASIA PACIFIC REGIONAL ARBITRATION GROUP, Aprag, Melbourne, Australia, http://apragmelbourne2014.org/

April 24 - 25
PUBLIC SYMPOSIUM WITH CIVIL SOCIETY, Unctad, Geneva, Switzerland, http://unctad.org/en/pages/meetingdetails.aspx?meetingid=433

June 16 - 20
FIFTIETH ANNIVERSARY OF UNCTAD, Geneva, Switzerland, http://unctad.org/en/pages/meetingdetails.aspx?meetingid=437



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