

# **Law and Practice of Investment Treaties**



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**Law and Practice of Investment Treaties**

Standards of Treatment

By

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## Authors' Preface

There have been significant developments in investment treaty law and practice over the past twenty years. Since 1990, the date of the first investor-state arbitral award under a modern investment treaty, the growth in the number of investment treaties and treaty disputes has been exponential. This book, drawing on the authors' academic and professional expertise, examines the origins and evolution of investment treaty law and practice, the law applicable to investment treaty disputes, and substantive investment law issues: standards of treatment and exceptions and defences to treaty obligations. Our aim is to provide a systematic, comprehensive and detailed statement of the law, along with applicable principles and policies, and to analyze critically investment treaty jurisprudence in the subject areas covered by the book.

The book is the product of extensive collaboration between the co-authors. Primary research and writing responsibilities were allocated as follows: Chapters 1, 3-8 and 10, Newcombe; and Chapters 2, 9 and 10, Paradell.

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## List of Abbreviations

### GENERAL

ACP	African, Caribbean and Pacific Group of States
ASEAN	Association of South East Asian Nations
BIT	Bilateral Investment Treaty
BLEU	Belgo-Luxembourg Economic Union
CAFTA-DR	Central America-Dominican Republic-United States Free Trade Agreement
DCF	Discounted Cash Flow
DSB	Dispute Settlement Body
EC	European Community
ECJ	European Court of Justice
ECT	Energy Charter Treaty
EU	European Union
FDI	Foreign Direct Investment
FCN	Treaty of Friendship, Commerce and Navigation
FIPA	Foreign Investment and Protection Agreement
FIRA	Foreign Investment Review Act
FTA	Free Trade Agreement
FTC	Free Trade Commission (NAFTA)
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
ICC	International Chamber of Commerce
ICCA	International Council for Commercial Arbitration
ICJ	International Court of Justice
ICSID	International Centre for Settlement of Investment Disputes

ICSID Convention	Convention on the Settlement of Investment Disputes between States and Nationals of Other States 1965
IGO	Intergovernmental Organization
IIA	International Investment Agreement
ILA	International Law Association
ILC	International Law Commission
IPPA	Investment Promotion and Protection Agreement
JSEPA	Japan-Singapore Economic Partnership Agreement
LCIA	London Court of International Arbitration
MAI	Draft Multilateral Agreement on Investment
MERCOSUR	Mercado Común del Sur (Common Market of the South)
MFN	Most-Favoured-Nation
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Co-operation and Development
PCIJ	Permanent Court of International Justice
SCC	Stockholm Chamber of Commerce
SLA	Softwood Lumber Agreement
SPS Agreement	Agreement on the Application of Sanitary and Phytosanitary Measures
TBT Agreement	Agreement on Technical Barriers to Trade
TRIMS Agreement	Agreement on Trade-Related Investment Measures
TRIPS Agreement	Agreement on Trade-Related Aspects of Intellectual Property Rights
UAE	United Arab Emirates
UN	United Nations
UNCITRAL	United Nations Commission on International Trade Law
UNCTC	United Nations Centre on Transnational Corporations
UNCTAD	United Nations Conference on Trade and Development
UNGA Res	United Nations General Assembly Resolution
UK	United Kingdom
US	United States
USD	United States Dollars
USSR	Union of Soviet Socialist Republics
Vienna Convention	Vienna Convention on the Law of Treaties 1969
WTO	World Trade Organization
WWI	World War I
WWII	World War II

JOURNALS, REPORTS AND TREATY SERIES

ABAJ	American Bar Association Journal
AULR	American University Law Review
AUILR	American University International Law Review
AIAJ	Asian International Arbitration Journal
AJIL	American Journal of International Law
AJIL Spec Supp	American Journal of International Law Special Supplement
AJCL	American Journal of Comparative Law
AI	Arbitration International
ARIA	American Review of International Arbitration
ASIL Proc	American Society of International Law Proceedings
AYIL	Asian Yearbook of International Law
BCICLR	Boston College International and Comparative Law Review
BLI	Business Law International
BYIL	British Yearbook of International Law
Can-USLJ	Canada-United States Law Journal
CBLJ	Canadian Business Law Journal
CLP	Current Legal Problems
CILJ	Cornell International Law Journal
CJIL	Chicago Journal of International Law
CJICL	Cardozo Journal of International and Comparative Law
CJTL	Columbia Journal of Transnational Law
CLQ	Cornell Law Quarterly
Con TS	Consolidated Treaty Series
CTS	Canadian Treaty Series
CYIL	Canadian Yearbook of International Law
EELR	European Environmental Law Review
EJIL	European Journal of International Law
ELJ	Energy Law Journal
ELR	Environmental Law Reporter
Foreign Aff	Foreign Affairs
Foreign Pol'y	Foreign Policy
FILJ	Fordham International Law Journal
FLR	Fordham Law Review
GYIL	German Yearbook of International Law
GGULR	Golden Gate University Law Review
GBDLJ	Global Business and Development Law Journal
GWJILE	George Washington Journal of International Law and Economics
HICLR	Hastings International and Comparative Law Review

HILJ	Harvard International Law Journal
IALR	International Arbitration Law Review
ICJ Rep	International Court of Justice Reports
ICLQ	International and Comparative Law Quarterly
ICLR	International Community Law Review
ICSID Rep	ICSID Reports
ICSID Rev	ICSID Review - Foreign Investment Law Journal
IFLR	International Financial Law Review
IALR	International Arbitration Law Review
IL	International Lawyer
ILF	International Law Forum
ILM	International Legal Materials
ILR	International Law Reports
ILSA JICL	ILSA Journal of International and Comparative Law
Iran-USCTR	Iran-United States Claims Tribunal Reports
ITBL	International Tax & Business Lawyer
IYBHR	Israel Yearbook on Human Rights
JAIL	Japanese Annual of International Law
JBL	Journal of Business Law
JCE	Journal of Comparative Economics
JDI	Journal de droit international
JENRL	Journal of Energy and Natural Resources Law
JILE	Journal of International Law and Economics
JIA	Journal of International Arbitration
JIEL	Journal of International Economic Law
JPL	Journal of Public Law (now Emory Law Journal)
JWI	Journal of World Investment (now JWIT)
JWIT	Journal of World Investment and Trade
JWT	Journal of World Trade
LCP	Law and Contemporary Problems
LNOJ	League of Nations Official Journal
LN Doc	League of Nations Documents
LNTS	League of Nations Treaty Series
LSI	Law & Social Inquiry
Marq LR	Marquette Law Review
Mich LR	Michigan Law Review
Minn LR	Minnesota Law Review
MJGT	Minnesota Journal of Global Trade
MJIL	Michigan Journal of International Law
NCLR	North Carolina Law Review
NILR	Netherlands International Law Review
NJILB	Northwestern Journal of International Law and Business
NYLJ	New York Law Journal
NYUJIL	New York University Journal of International Law

NYUELJ	New York University Environmental Law Journal
NYULQR	New York University Law Quarterly Review
NYULR	New York University Law Review
RDCADI	Recueil des cours de l' Académie de Droit International de La Haye
RIAA	Reports of International Arbitral Awards
RGD	Revue Générale de Droit
RGDIP	Revue Générale de Droit International Public
SJIL	Stanford Journal of International Law
TDM	Transnational Dispute Management
TILJ	Texas International Law Journal
UCDJILP	UC Davis Journal of International Law and Policy
UCDLR	UC Davis Law Review
UPJIEL	University of Pennsylvania Journal of International Economic Law
UTLJ	University of Toronto Law Journal
UKTS	United Kingdom Treaty Series
UNTS	United Nations Treaty Series
UST	United States Treaties
VJIL	Virginia Journal of International Law
VLR	Virginia Law Review
WCR	World Court Reports
WD	World Development
WILJ	Wisconsin International Law Journal
YJIL	Yale Journal of International Law
VJTL	Vanderbilt Journal of Transnational Law
YBCA	Yearbook of Commercial Arbitration
YBILC	Yearbook of the International Law Commission
YBUN	Yearbook of the United Nations
YWBA	Yearbook of World Affairs

FREQUENTLY CITED DRAFT CONVENTIONS AND OTHER INSTRUMENTS

1929 Draft Convention	<i>Convention on the Treatment of Foreigners</i>
1929 Harvard Draft	<i>Draft Convention on Responsibility of States for Damage done in their Territory to the Person or Property of Foreigners</i>
1961 Harvard Draft	<i>Draft Convention on the International Responsibility of States for Injuries to Aliens</i>
1967 Draft OECD Convention	<i>Draft Convention on the Protection of Foreign Property</i>

Abs-Shawcross Draft Convention	<i>Draft Convention on Investments Abroad</i>
Charter	<i>Charter of Economic Rights and Duties of States</i>
ICC Code	<i>International Code of Fair Treatment for Foreign Investment</i>
ILA Statute	<i>Draft Statutes of the Arbitral Tribunal for Foreign Investment and the Foreign Investment Court</i>
NIEO Declaration	<i>Declaration on the Establishment of a New International Economic Order</i>

NOTE ON REFERENCES TO BILATERAL  
INVESTMENT TREATIES

For ease of reference, specific bilateral investment treaties in this book are listed by referring to the two treaty parties in alphabetical order, followed by the date the treaty was signed (not the date of ratification). For example, the *Treaty between the United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment* (signed 14 November 1991, entered into force 20 October 1994) is referred to as Argentina-US (1991).

# Guide to Investment Treaty Resources

## INTERNATIONAL INVESTMENT AGREEMENTS AND INSTRUMENTS

International investment agreements and instruments are available in two print sources:

United Nations Conference on Trade and Development, *International Investment Instruments: A Compendium* (New York: United Nations, 1996) in three volumes.

International Centre for Settlement of Investment Disputes, *Investment Promotion and Protection Treaties*, looseleaf (New York: Oceana Publications, Inc., 1983) in ten volumes.

The United Nations Conference on Trade and Development (UNCTAD) website has two searchable electronic databases – a compilation of bilateral investment treaty texts and a compendium of international investment instruments. In addition, a number of commercially available databases including Kluwer Arbitration and Investment Claims have various treaty materials available online.

## INVESTMENT TREATY AWARDS AND DECISIONS

Investment treaty awards and decisions are reproduced in various print sources including ICSID Reports, ICSID Review-Foreign Investment Law Journal, International Law Reports and International Legal Materials.

Online access to current and past investment treaty awards and decisions, along with links to other materials and resources, is available through Professor Andrew Newcombe's Investment Treaty Arbitration website: <<http://ita.law.uvic.ca>>.

**OTHER RESOURCES**

A number of specialized websites provide access to current investment treaty decisions, awards and other materials, including links to further resources:

Digest of Investment Treaty Decisions and Awards: <<http://arbitration-icca.org>>

ICSID: <<http://icsid.worldbank.org>>

Investment Arbitration Reporter: <<http://iareporter.com>>

Investment Claims: <<http://investmentclaims.com>>

Investment Treaty Arbitration: <<http://ita.law.uvic.ca>>

Investment Treaty News: <<http://iisd.org/investment/itn>>

Kluwer Arbitration: <<http://kluwerarbitration.com>>

NAFTA Claims: <<http://naftaclaims.com>>

Transnational Dispute Management: <<http://transnational-dispute management.com>>

UNCTAD international investment agreement: <<http://unctad.org>>

## Chapter 1

# Historical Development of Investment Treaty Law

## INTRODUCTION

**§1.1 A unique treaty framework** The international legal framework governing foreign investment consists of a vast network of international investment agreements (IIAs)<sup>1</sup> supplemented by the general rules of international law. Although other international treaties interact with this network in important ways, IIAs are the primary public international law instruments governing the promotion and protection of foreign investment.<sup>2</sup> IIA texts differ in many important respects, but they are also remarkably similar in structure and content: most IIAs combine similar (sometimes identical) treaty-based standards of promotion and protection for foreign investment with an investor-state arbitration mechanism<sup>3</sup> that allows foreign investors to enforce

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1. The abbreviation IIAs is used throughout this text to refer to standalone bilateral investment treaties (BITs), bilateral and regional free trade agreements that include foreign investment obligations, such as the *North American Free Trade Agreement* (NAFTA), and sectoral treaties, such as the *Energy Charter Treaty* (ECT), that include investment obligations. The expression ‘investment treaties’ is sometimes used in the text instead of IIAs.
  2. The interaction between investment promotion and protection under IIAs and the rules imposed by other multilateral economic treaties is addressed throughout the text. Important interactions include market access for service suppliers under the *General Agreement on Trade in Services* (see *infra* Chapter 3 on establishment obligations), prohibitions on restrictions on transfers and convertibility under the International Monetary Fund’s *Articles of Agreement* (see *infra* Chapter 8 on transfer rights) and prohibitions on various types of performance requirements, including domestic content requirements, under the WTO’s *Agreement on Trade-Related Investment Measures* (see *infra* Chapter 8 on performance requirements).
  3. See generally J.G. Merrills, *International Dispute Settlement*, 4th edn (Cambridge: Cambridge University Press, 2005). On trends in international law regarding the access of private actors (individuals and corporations) to international dispute settlement see F. Orrego Vicuña, *International Dispute Settlement in an Evolving Global Society: Constitutionalization*,

these standards against host states.<sup>4</sup> The network of IIAs provides foreign investors with a powerful and dynamic method of international treaty enforcement. The purpose of this book is to provide a comprehensive explanation of the substantive standards of treatment that states must accord to foreign investors and investment under IIAs.<sup>5</sup>

The uniqueness of the current IIA network is a product of an historical evolution going as far back as the Middle Ages. Prior to the twentieth century, international standards of foreign investment and investor protection developed primarily through the related processes of diplomatic protection and claims commissions. In the late nineteenth and early twentieth centuries, as the world economy became increasingly internationalized, the limits of the diplomatic protection model became apparent, particularly as controversies arose between capital exporting and importing states regarding the customary international law minimum standard of treatment to be accorded to foreign investors and investments.<sup>6</sup> In the aftermath of

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*Accessibility, Privatization* (Cambridge: Cambridge University Press, 2004) [Orrego Vicuña, *International Dispute Settlement*], which describes treaties that provide individuals and corporate entities direct access to international courts and tribunals.

4. 'Host' state refers to the state in which a foreign investor or investment is located. 'Home' state refers to the state of which the investor is a national.
5. See *infra* Part V for an overview of the topics covered in this text. As noted in Part V, this book does not address threshold issues of the application of IIAs: to whom they apply (investors), to what they apply (investment), or when they apply (temporal application). Further, the book does not address jurisdictional or procedural issues related to investor-state arbitration or the consequences of breaches of IIA standards of treatment (reparations). A number of other texts consider these issues. See C. McLachlan, L. Shore & M. Weiniger, *International Investment Arbitration: Substantive Principles* (Oxford: Oxford University Press, 2007); R. Dolzer & C. Schreuer, *Principles of International Investment Law* (Oxford: Oxford University Press, 2008); K. Sauvants, ed., *Appeals Mechanism in International Investment Disputes* (Oxford: Oxford University Press, 2008); R.D. Bishop, J. Crawford & W.M. Reisman, *Foreign Investment Disputes: Cases, Materials and Commentary* (The Hague: Kluwer Law International, 2005); N. Rubins & N.S. Kinsella, *International Investment, Political Risk and Dispute Resolution* (Dobbs Ferry, NY: Oceana Publications Inc., 2005) and G. Van Harten, *Investment Treaty Arbitration and Public Law* (Oxford: Oxford University Press, 2007). There are also a number of new and forthcoming texts: P. Muchlinski, F. Ortino & C. Schreuer, *The Oxford Handbook of International Investment Law* (Oxford: Oxford University Press, 2008); A. Reinisch, ed., *Standards of Investment Protection* (Oxford: Oxford University Press, 2008); C. Dugan, D. Wallace, N. Rubins & B. Sabahi, *Investor-State Arbitration* (Oxford: Oxford University Press, 2008); Z. Douglas, *Investment Treaty Arbitration* (Cambridge: Cambridge University Press, forthcoming) and S. Ripinsky *et al.*, *Damages in International Law* (London: British Institute of International and Comparative Law, 2008).
6. Throughout this chapter, the term 'capital exporting' states refers to 'Western', 'developed' or 'industrialized' states – generally those that are now members of the Organization for Economic Co-operation and Development (OECD). The term 'capital importing' states refers to former colonies, 'developing' and 'newly-industrializing' states of Latin America, Asia and Africa. The terms 'capital importing' and 'capital exporting' states are generalizations and misleading in several respects. Many states are both capital importers and exporters. The categories are not static and states may become capital exporters or importers as political and economic circumstances change. Moreover, the capital exports in question are generally those of private

the Second World War (WWII), the process of international economic integration was rekindled, leading to the emergence of the contemporary investment treaty framework. It is crucial to consider this historical development in order to better understand current debates and contentious issues in investment treaty law.<sup>7</sup>

This chapter is divided into five parts. Part I delves into the historical origins of international investment law. Part II then explores developments in the post-WWII period, setting the background for Part III, which discusses the origins and development of IIAs. Part IV provides an overview of the current status of the IIA network. Part V discusses the basic structure of IIAs.

## I HISTORICAL ORIGINS OF INTERNATIONAL INVESTMENT LAW

**§1.2 Early history** There is no comprehensive history of the treatment of foreigners and their property under international law. However, historical records attest to the fact that early political communities routinely denied legal capacity and rights to those who originated from outside their community.<sup>8</sup> These ‘outsiders’, often known as aliens, from the Latin word *alius*, meaning ‘other’, were frequently treated as enemies, barbarians or outcasts. The treatment and the legal status of the alien has markedly improved from ancient times through the Middle Ages to the modern era. In his classic 1915 treatise, *The Diplomatic Protection of Citizens Abroad*, Edwin Borchard wrote that the ‘legal position of the alien has in the progress of time advanced from that of complete outlawry, in the days of the early Rome and the Germanic tribes, to that of the practical assimilation with nationals, at the present

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foreign investors, not the state itself as these expressions may wrongly suggest. Despite these conceptual limitations, the terms are useful since they reflect the tensions that have contributed to the development of the law governing relations between capital exporters and importers, as well as differing views about the nature and role of international investment law. As noted by Van Harten, *ibid.*, at 13-14, capital exporting states can be defined empirically as states whose outward foreign direct investment (FDI) stock exceeds their inward stock or whose outward stock exceeds USD100 billion. Based on data from the United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2005*, Annex Table B.2, Van Harten identifies 16 major capital exporters with outward stock of over USD100 billion. These are (ranked in order from the largest exporter): US, UK, Germany, France, Netherlands, Hong Kong, Switzerland, Japan, Canada, Spain, Italy, Belgium, Sweden, Luxembourg, Australia and Singapore. Capital importing states can be defined as states whose inward FDI exceeds outward FDI stocks by a ratio of at least 2 to 1. On this measure there are 111 capital importing states (Van Harten, *ibid.*, at 13). See UNCTAD’s annual *World Investment Report* for recent statistics on foreign investments flows.

7. Given the breadth of this topic and the varied state practice, only the most important historical developments are highlighted and citations to specialized works in the area are provided.
8. On the status of foreign nationals or aliens in international law see R. Arnold, ‘Aliens’, in R. Bernhardt, ed., *Encyclopedia of Public International Law*, Vol. I (Amsterdam: North-Holland Pub. Co, 1992) [*Encyclopedia*] at 102.

time.<sup>9</sup> These developments have continued through the twentieth and twenty-first centuries and are reflected in the current network of IIAs.

By the commencement of the modern era, international legal scholars considered that international law protected the rights of aliens to travel and trade.<sup>10</sup> Francisco de Vitoria argued that under international law foreigners had the right to travel, live and trade in foreign lands.<sup>11</sup> Hugo Grotius treated the status of foreigners under the category ‘Of Things That Belong To Men In Common’ and asserted a norm of non-discrimination in the treatment of foreigners.<sup>12</sup> However, Emmerich de Vattel was the first modern scholar to address the status of foreigners in detail. In *Law of Nations* (1758), Vattel argued that a state has the right to control and set conditions on the entry of foreigners.<sup>13</sup> Once admitted, foreigners are subject to local laws and the state is under a duty to protect foreigners in the same manner as its own subjects.<sup>14</sup> At the same time, however, foreigners retained their membership in their own state and were not ‘obliged to submit, like the subjects, to all the commands of the sovereign.’<sup>15</sup> In Vattel’s view, foreigners’ membership in their home state extended to their property, which remained part of the wealth of their home nation.<sup>16</sup> As a result, a state’s mistreatment of foreigners or their property was an injury to the foreigners’ home state.<sup>17</sup> This view eventually coalesced into the international legal principle of diplomatic protection.

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9. E.M. Borchard, *Diplomatic Protection of Citizens Abroad or The Law of International Claims* (New York: Banks Law Publishing Co., 1915) [Borchard, *Diplomatic Protection*] at 33.
  10. See generally H. Neufeld, *The International Protection of Private Creditors from the Treaties of Westphalia to the Congress of Vienna (1648-1815): A Contribution to the History of the Law of Nations* (Leiden: Sijthoff, 1971) at 47-55 for a summary of the views of early international law publicists on the economic interests of aliens.
  11. See F. de Vitoria, *De Indis et De Ivre Belli : Relectiones* (1696), E. Nys, ed., J.P. Bate, trans. (Washington, DC: Carnegie Institution of Washington, 1917), s. III. For a critical assessment of Vitoria’s work in the context of the colonial origins of international law and the Spanish conquest of the Americas, see A. Anghie, *Imperialism, Sovereignty, and the Making of International Law* (Cambridge: Cambridge University Press, 2005).
  12. See H. Grotius, *De Jure Belli Ac Pacis Libri Tres* (1625), J. B. Scott, ed., F.W. Kelsey, trans. (Oxford: Clarendon Press, 1925), Book II, Chapter II, XXII, where Grotius refers to most-favoured-nation treatment: ‘A common right by supposition relates to the acts which any people permits without distinction to foreigners; for if under such circumstances a single people is excluded, a wrong is done to it. Thus if foreigners are anywhere permitted to hunt, fish, snare birds, or gather pearls, to inherit by will, or sell property, and even to contract marriages in case there is no scarcity of women, such rights cannot be denied to one people alone, except on account of previous wrong-doing.’
  13. E. Vattel, *Law of Nations*, J. Chitty, trans. (Philadelphia: T.&J.W. Johnson & Co., 1858), Book II, Chapter VIII, §100.
  14. *Ibid.*, §104.
  15. *Ibid.*, §108.
  16. *Ibid.*, §109. For this reason, Vattel opposed the ‘droit d’aubaine’ or right of escheat, by which the property of foreigners passed to the host state at their death. See A.H. Roth, *The International Minimum Standard* (Leiden: Sijthoff, 1949) at 26-27 and Borchard, *Diplomatic Protection*, *supra* note 9 at 35-36.
  17. F.V. Garcia-Amador argues that while Vitoria and Grotius viewed foreigners’ rights as arising out of their status as members of the human race, and looked to nationality as a way to improve

**§1.3 Diplomatic protection** The exercise of diplomatic protection can be traced back to the Middle Ages, if not earlier.<sup>18</sup> The theory underlying the principle of diplomatic protection is that an injury to a state's national is an injury to the state itself, for which it may claim reparation from any responsible state.<sup>19</sup> Through the exercise of diplomatic protection, the home state makes a claim against the host state for an injury to the home state's national.<sup>20</sup> In the vernacular of international claims, a state 'espouses' the claim of its national. States exercised diplomatic protection throughout the eighteenth and nineteenth centuries, and by 1924 the Permanent Court of International Justice (PCIJ) recognized a state's right to exercise diplomatic protection over its nationals as an 'elementary principle of international law.'<sup>21</sup>

Although a comprehensive examination of the rules of diplomatic protection is beyond the scope of this book,<sup>22</sup> for present purposes, it is important to highlight

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their treatment, under Vattel's approach international legal rights and obligations arose as a result of nationality. See F.V. Garcia-Amador *The Changing Law of International Claims* (Dobbs Ferry, NY: Oceana Publications Inc., 1984) at 46.

18. See I. Brownlie, *Principles of Public International Law*, 6th edn (Oxford: Oxford University Press, 2003) [Brownlie, *Principles of Public International Law*] at 500. In addition to diplomatic protection, claims were also enforced through private means by obtaining letters of marque or reprisal from political authorities. See K.J. Partsch, 'Reprisals' in *Encyclopedia*, *supra* note 8, Vol. IV at 200.
19. Art. 1 of the International Law Commission's (ILC's) Articles on Diplomatic Protection adopted by the ILC's at its fifty-eighth session, in 2006, provides that 'diplomatic protection consists of the invocation by a State, through diplomatic action or other means of peaceful settlement, of the responsibility of another State for an injury caused by an internationally wrongful act of that State to a natural or legal person that is a national of the former State with a view to the implementation of such responsibility'. See 'Report on the work of its fifty-eighth session', in *Report of the International Law Commission*, UN GAOR, 61st Sess., Supp. No. 10, UN Doc A/61/10 (2006), at 16.
20. See *supra* note 4 on the terms 'home' and 'host' state.
21. The PCIJ affirmed the principle in *The Mavrommatis Palestine Concessions* (1924) PCIJ Ser. A, No. 2 at 12: 'It is an elementary principle of international law that a State is entitled to protect its subjects, when injured by acts contrary to international law committed by another state, from whom they have been unable to obtain satisfaction through the ordinary channels. By taking up the case of one of its subjects and by resorting to diplomatic action or international judicial proceedings on his behalf, a State is in reality asserting its own rights – its right to ensure, in the person of its subjects, respect for the rules of international law.' Also see *Panevezys-Saldutiskis Railway Case* (1939) PCIJ Ser. A/B, No. 76 at 14.
22. On diplomatic protection and international claims see Borchard, *Diplomatic Protection*, *supra* note 9; Garcia-Amador, *supra* note 17; C. Eagleton, *Responsibility of States in International Law* (New York: New York University Press, 1928); F.S. Dunn, *The Protection of Nationals: A Study in the Application of International Law* (Baltimore: The Johns Hopkins Press, 1932); A. Freeman, *The International Responsibility of States for Denial of Justice* (New York: Longmans, Green and Co. Ltd, 1938); C.F. Amerasinghe, *State Responsibility for Injuries to Aliens* (Oxford: Clarendon Press, 1967); R.B. Lillich, ed., *International Law of State Responsibility for Injuries to Aliens* (Charlottesville: University Press of Virginia, 1983) and C.F. Amerasinghe, *Diplomatic Protection* (Oxford: Oxford University Press, 2008). In addition, see the various reports of the ILC's and International Law Association (ILA) on diplomatic protection, *supra* note 19 and *infra* notes 23 and 24.

three issues related to the espousal of international claims. First, the state must bring the claim in accordance with the rules relating to international claims, including the nationality of claims. These rules determine the eligibility of persons for whom a state may espouse a claim and address issues such as whether continuous nationality is required from the time of injury to adjudication of the claim.<sup>23</sup> Second, state responsibility for injury to foreign nationals may not be invoked if ‘the rule of exhaustion of local remedies applies and any available and effective local remedy has not been exhausted.’<sup>24</sup> Before a state may exercise diplomatic protection, the foreign national must have sought redress in the host state’s domestic legal system. Finally, the right to exercise diplomatic protection is at the discretion of the espousing state.<sup>25</sup> A state may decide not to exercise protection for reasons unrelated to the merits of the claim, particularly if the state has other diplomatic, military or geo-political objectives that might be compromised by making a claim. As a result of this discretionary power, absent international treaty rights of action, a foreign investor has no control over the international claim-making process. As will be seen, IIAs provide a treaty-based right to bring claims through investor-state arbitration.<sup>26</sup> The extent to which elements of the

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23. The issue of nationality of claims has been the subject of extensive study and discussion by the ILA and the ILC. See *Report of the International Law Commission*, UN GAOR, 56th Sess., Supp. No. 10, UN Doc A/59/10 (2004), and F. Orrego Vicuña, *The Changing Law of Nationality of Claims*, Report for the International Law Association Committee on Diplomatic Protection of Persons and Property, 69th Conference, London 2000 at 631-645 [Orrego Vicuña, *The Changing Law of Nationality of Claims*]. Nationality issues have arisen in a series of IIA cases, including *The Loewen Group, Inc. and Raymond L. Loewen v. United States*; *Tokios Tokelès v. Ukraine* and *Waguih Elie George Siag and Clorinda Vecchi v. Egypt*.
24. Art. 44(b), International Law Commission’s Articles on Responsibility of States for Internationally Wrongful Acts, *Official Records of the General Assembly*, UN GAOR, 56th Sess., Supp. No. 10, UN Doc A/56/10 at 11; 2001 YBILC, Vol. II, Part Two. The Articles and commentary are reprinted in J. Crawford, *The International Law Commission’s Articles on State Responsibility: Introduction, Text, and Commentaries* (Cambridge: Cambridge University Press, 2002) [ILC’s Articles on State Responsibility]. The issue of exhaustion of local remedies has been the subject of extensive study and discussion by the ILA and the ILC’s. See *Report of the ILC’s*, 56th Session (2004), *ibid.*, and Articles on Diplomatic Protection, *supra* note 19. See also J. Kokott, *The Exhaustion of Local Remedies*, Report for the International Law Association Committee on Diplomatic Protection of Persons and Property, 69th Conference, London 2000 at 3-27. Treatises on exhaustion of local remedies include C.F. Amerasinghe, *Local Remedies in International Law*, 2nd edn (Cambridge: Cambridge University Press, 2004) and A.A. Cançado Trindade, *The Application of the Rule of Exhaustion of Local Remedies in International Law* (Cambridge: Cambridge University Press, 1983). For a discussion of the rule in the context of investor-state arbitrations, see W.S. Dodge, ‘National Courts and International Arbitration: Exhaustion of Remedies and Res Judicata Under Chapter 11 of NAFTA’ (2000) 23 HICLR 357.
25. ‘The State must be viewed as the sole judge to decide whether its protection will be granted, to what extent it will be granted, and when it will cease. It retains in this respect a discretionary power the exercise of which may be determined by considerations of a political or other nature, unrelated to the case.’ *Barcelona Traction, Light and Power Company Limited (Belgium v. Spain)* [1970] ICJ Rep 4 at para. 79.
26. See *infra* §1.31 *et seq.* regarding the development of investor-state arbitration.

international law relating to diplomatic protection, such as the rules relating to continuous nationality, are relevant to IIA claims remains unsettled.<sup>27</sup>

**§1.4 Dispute settlement by claims commissions and international arbitration** Early state practice on diplomatic protection took a number of forms. In addition to the diplomatic settlement of claims<sup>28</sup> and settlement through coercive means,<sup>29</sup> states established *ad hoc* commissions and arbitral tribunals to adjudicate specific claims or classes of claims involving a host state's treatment of foreign nationals and their property. This practice dates from the 1794 Treaty of Amity, Commerce and Navigation between Great Britain and United States (Jay Treaty),<sup>30</sup> which, among other things, established a commission to decide claims regarding the treatment of British and US nationals during and after the American Revolution.<sup>31</sup>

From 1840-1940 states established over sixty arbitral commissions to deal with disputes arising from injuries to foreign nationals.<sup>32</sup> In addition, there were various *ad hoc* tribunals established to deal with specific claims<sup>33</sup> and national prize courts that adjudicated claims regarding the capture of property at sea.<sup>34</sup> State practice and the decisions of these commissions and tribunals formed the nascent jurisprudence on state responsibility for injuries to aliens. Although these claims commissions, by hearing claims based on individual losses, were designed to protect the rights of individuals, they generally relied on a model of diplomatic protection, meaning that only states, and not individuals, were party

27. For an in-depth discussion of this issue, see Z. Douglas, 'Hybrid Foundations of Investment Treaty Arbitration' (2003) 74 BYIL 151.

28. The volume of diplomatic practice with respect to international claims increased substantially in the 19th century. US practice was collected in F. Wharton, *A Digest of the International Law of the United States* (Washington: Government Printing Office, 1886) and in J.B. Moore, *International Law Digest* (Washington: Government Printing Office, 1906) Vol. VII, both of which were official US government publications. In contrast, European state practice was less accessible and European publicists tended not to cite it. See I. Brownlie, *System of the Law of Nations, State Responsibility – Part I* (Oxford: Oxford University Press, 1986) [Brownlie, *System of the Law of Nations*] at 6.

29. See §1.5.

30. 19 Nov. 1794, 52 Cons TS 243, entered into force 28 Oct. 1795.

31. See B. Legum, 'The Innovation of Investor-State Arbitration Under NAFTA' (2002) 43 HILJ 534. The Jay Commissions issued over 500 awards. See A.M. Stuyt, *Survey of International Arbitrations, 1794-1989*, 3rd edn (Dordrecht: Martinus Nijhoff Publishers, 1990) at 2-3. Also see, D.M. Johnston, *The Historical Foundations of World Order: The Tower and the Arena* (Leiden: Martinus Nijhoff, 2008) at 636.

32. Brownlie, *Principles of Public International Law*, *supra* note 18 at 500. See also J.H. Ralston, *International Arbitration, from Athens to Locarno* (London: Oxford University Press, 1972) and Stuyt, *ibid.*

33. Several of these were established under the auspices of the Permanent Court of Arbitration. See Ralston, *ibid.*, and Stuyt, *ibid.*

34. See Halsbury, *et al.*, *The Principles and Practice of Prize Law* (London: Butterworths, 1914).

to the proceedings.<sup>35</sup> After the First World War (WWI), it became more common for agreements to provide that individual claimants could make claims directly.<sup>36</sup>

In addition to the mixed claims commissions of the nineteenth century, there were several direct investor-state arbitrations. One of the first was between *La Compagnie Universelle du Canal de Suez*, a Turkish company, and Egypt. In 1864, the company sought compensation from Egypt after a law was passed that disrupted a concession agreement to work on the Suez Canal. Although there was no arbitration clause in the original agreement, both parties agreed to use arbitration to resolve the dispute, and jointly agreed on Napoleon III as arbitrator.<sup>37</sup>

**§1.5 Use and abuse of diplomatic protection** The evolution and exercise of diplomatic protection should be viewed in its historical context. The espousal of claims developed in an era of colonialism and imperialism.<sup>38</sup> States exercised all possible means – political, economic and military – to protect their nationals' interests abroad. Reflecting on the development of the law of state responsibility for injuries to aliens, Henry Steiner and Detlev Vagts note that:

The growth of the law of state responsibility reflected the more intense identification of the individual (or later, the corporation) with his country that accompanied the nationalist trends of the 18th to early 20th centuries. That growth would not have taken place but for Western colonialism and economic imperialism which reached their zenith during this period. Transnational business operations centered in Europe, and later in the United States as well, penetrated Asia, Africa and Latin America. Thus security of the person and property of a national inevitably became a concern of his government. That concern manifested itself in the vigorous assertion of diplomatic protection and in the enhanced activity of arbitral tribunals. Often the arbitrations occurred under the pressure of actual or threatened military force by the aggrieved nations, particularly in Latin America.<sup>39</sup>

35. R. Dolzer, 'Mixed Claims Commissions' in *Encyclopedia*, *supra* note 8, Vol. III at 438.

36. Legum, *supra* note 31 at 533, notes that mixed arbitral tribunals were established to address claims by Allied nationals against Germany and the Iran-United States Claims Tribunal permitted direct claims. See *infra* §1.28 on the Iran-United States Claims Tribunal. On trends in international law to allow individual claims see Orrego Vicuña, *The Changing Law of Nationality of Claims*, *supra* note 23.

37. *Egypt v. Suez Canal Company* (Award, 1864) in Stuyt, *supra* note 31 at 471. For commentary, see Ch. Leben, 'La théorie du contrat d'Etat et l'évolution du droit international des investissements' (2003) 302 RDCADI 197 at 219. See Stuyt, *supra* note 31 at 472 *et seq.*, for lists of other early arbitrations between states and foreign entities. Also see E. Darby, *Modern Pacific Settlements Involving the Application of the Principle of International Arbitration* (London: Peace Society, 1904) on early international arbitrations and dispute resolution.

38. See Anghie, *supra* note 11. For another critical view of the law of state responsibility for injuries to aliens, see S.N. Guha Roy, 'Is the Law of Responsibility of States for Injuries to Aliens a Part of Universal International Law' (1961) 55 AJIL 863.

39. H.J. Steiner & D.F. Vagts, *Transnational Legal Problems: Materials and Text*, 2nd edn (Mineola, N.Y.: Foundation Press, 1976) at 357.

During the nineteenth and early twentieth centuries, the exercise of diplomatic protection by powerful states was often accompanied by ‘gun-boat diplomacy’ – the threat or the use of force to back up diplomatic protection claims.<sup>40</sup> At the time, the use of force in the exercise of diplomatic protection was not inconsistent with international law.<sup>41</sup> Despite the fact that the 1899 and 1907 *Hague Convention for the Pacific Settlement of International Disputes* (Hague Conventions) provided for state parties ‘to use their best efforts to ensure the pacific settlement of international differences,’<sup>42</sup> both the US and the European powers used force and threats of force on numerous occasions to back up and enforce claims of diplomatic protection.<sup>43</sup> For instance, between 1820 and 1914, Great Britain intervened in Latin America at least forty times to enforce British claims for injuries to its nationals and to restore order and protect property.<sup>44</sup> These claims were sometimes based on limited or erroneous evidence and frequently led to reprisals out of proportion to the injury suffered.<sup>45</sup>

Abuses, real and perceived, of diplomatic protection led Latin American states to resist its use, particularly in its more interventionist forms. This opposition solidified after armed English, German and Italian forces intervened in Venezuela in 1902 to enforce claims relating to state-issued bonds.<sup>46</sup> In reaction, Luis Drago, the Argentine foreign minister, authored a diplomatic note to the US in December 1902, arguing that the public debt of Latin American states should

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40. See D.R. Shea, *The Calvo Clause* (Minneapolis: University of Minnesota Press, 1955); M. Hood, *Gunboat Diplomacy 1895-1905* (London: George Allen & Unwin, 1975) and J. Cable, *Gunboat Diplomacy, 1919-1979: Political Applications of Limited Naval Force*, 2nd edn (London: Macmillan, 1981).

41. Moore, *supra* note 28, Vol. VII at 103-135.

42. Art. 1 of both conventions ((1898-1899) 187 Con TS at 410 and (1907) 205 Con TS at 233).

43. See the discussion of ‘nonamicable’ modes of redress and the practice of the US in Moore, *supra* note 28, §1089-§1099. Key incidents involving European powers include: French interventions in Mexico in 1838 and 1861 (see Shea, *supra* note 40 at 13); Great Britain threatening naval intervention in the 1836 Sicilian sulphur monopoly dispute (see J. Fawcett (1950) 27 BYIL 355); Italy sending a vessel to Colombia to rescue an Italian national in 1885 and later sending its fleet to enforce an arbitral award regarding the property of an Italian citizen (see W. Benedek, ‘Cerrutti Arbitrations’ in *Encyclopedia*, *supra* note 8, Vol. I at 555) and the embargo of Venezuelan ports by Great Britain, Germany and Italy in 1902-3 (see M. Silagi, ‘Preferential Claims Against Venezuela Arbitration’ in *Encyclopedia*, *supra* note 8, Vol. III at 1098). The US intervened in Dominican Republic in 1905 and 1916, Nicaragua in 1911 and Haiti in 1915 (K.J. Vandeveld, *United States Investment Treaties: Policy and Practice* (Boston: Kluwer Law and Taxation, 1992) [Vandeveld, *United States Investment Treaties*] at 8). As Vandeveld notes, US military intervention, while serving to protect US commercial interests, also reflected more general geopolitical considerations.

44. C. Lipson, *Standing Guard: Protecting Foreign Capital in the Nineteenth and Twentieth Centuries* (Berkeley: University of California Press, 1985) at 54.

45. Shea, *supra* note 40 at 12.

46. See Silagi, *supra* note 43 at 1098. On bond defaults and intervention, see Lipson, *supra* note 44 at 37-64. For a discussion of more recent attempts to enforce sovereign bond obligations through international arbitration, see M. Waibel, ‘Opening Pandora’s Box: Sovereign Bonds in International Arbitration’ (2007) 101 AJIL 711.

not give rise to a right of armed intervention.<sup>47</sup> This led to the development of the Drago Doctrine, which was incorporated into the *Hague Convention II of 1907 Respecting the Limitations of the Employment of Force for the Recovery of Contract Debts* (Drago-Porter Convention).<sup>48</sup> Under the Drago-Porter Convention, states agreed not to use armed force for the recovery of state debts unless there was a refusal to submit the claim to arbitration. Thus, even under the Drago-Porter Convention, and despite the general obligations in the Hague Conventions regarding pacific settlement of disputes, force remained a legal means of exercising diplomatic protection should a state fail to accept an offer of arbitration or accept any resulting award.<sup>49</sup> It was not until the *General Treaty for the Renunciation of War 1928* (Briand-Kellogg Pact) that international law prohibited the use of force and required states to resolve disputes only by pacific means.<sup>50</sup>

**§1.6 Colonial territories and extraterritorial jurisdiction** Much of the expansion of international trade and investment in the eighteenth, nineteenth and twentieth centuries occurred within colonial political and legal regimes. In this

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47. See D. Drago, 'State Loans in Their Relation to International Policy' (1907) 1 AJIL 692; E.M. Borchard, 'Limitations on Coercive Protection' (1927) 21 AJIL 303 [Borchard, 'Limitations'] and discussion in Shea, *supra* note 40 at 15.
48. *Hague Convention II of 1907 Respecting the Limitations of the Employment of Force for the Recovery of Contract Debts*, 18 Oct. 1907 [Drago-Porter Convention] in (1907) 205 Con. TS 250.
49. Lipson, *supra* note 44 at 74. As discussed in §1.8, Latin American states' general adherence to the Calvo Doctrine reflected an unwillingness to accept international arbitration. In addition, the Drago-Porter Convention, *ibid.*, only applied to intervention for the purpose of collecting on public debt obligations. It did not address interventions for other types of diplomatic claims. Most Latin American states entered reservations to the Drago-Porter Convention and only Mexico ratified it. See I. Brownlie, *International Law and the Use of Force by States* (London: Oxford University Press, 1963) [Brownlie, *International Law and the Use of Force by States*] at 23-25. Proposals made at the Inter-American Conference for the Maintenance of Peace in 1936 and the Eighth International Conference of American States in 1938 that the Drago Doctrine should be given treaty form were not adopted (Brownlie, *International Law and the Use of Force by States, ibid.*, at 226).
50. *General Treaty for the Renunciation of War 1928*, 94 LNTS 57. There was some debate over whether the Briand-Kellogg Pact prohibited armed force that did not amount to war. As of 1945, Art. 2(4), *Charter of the United Nations*, prohibits the threat or use of force. Various types of overt or covert interventions by Western states nevertheless continued, related in part to the protection of economic interests. The Roosevelt Corollary to the Monroe Doctrine authorized the use of force to collect private debts owed to US citizens. See A. Rappaport, *A History of American Diplomacy* (New York: Macmillan, 1975) at 223 *et seq.* Further, commentators have argued that interventions by Western states in Iran (1954), Guatemala (1954), Egypt (1956), Cuba (1961), British Guinea (1973), Brazil (1964), Dominican Republic (1965) and Chile (1973) may have been, or were at least in part, motivated by the desire to protect foreign economic interests. See A. Akinsanya, *Multinationals in a Changing Environment* (New York: Praeger Publishers, 1984) at 252-306 and *The Expropriation of Multinational Property in the Third World* (New York: Praeger Publishers, 1980). It should be noted that the USSR, China and other states with communist and socialist economies also intervened in the affairs of other states and that these interventions were arguably also motivated at least in part by economic reasons.

context, there was no need for colonists to have recourse to international law processes since colonial political and military power protected colonists and their property from local interference or control.<sup>51</sup> In addition, extraterritorial jurisdiction, which allowed foreign powers to apply their laws to their nationals in foreign states, was exercised under treaties.<sup>52</sup> In some cases, these regimes were imposed by force through treaties of capitulation. Extraterritorial jurisdiction in one form or another existed in China, Japan, Thailand, Iran, Egypt, Morocco, Turkey and other parts of the Ottoman Empire.<sup>53</sup> The existence of extraterritorial regimes in Asia and the Far East, but not in Latin America, explains why Latin American states are the source of almost all early jurisprudence and cases on diplomatic protection.<sup>54</sup>

**§1.7 The minimum standard of treatment** The expansion of trade and investment in the nineteenth and early twentieth centuries directed increased attention to the legal status of foreign nationals abroad and to the protection of their economic interests.<sup>55</sup> By the early 1900s, there was general agreement amongst international lawyers in Europe and the US that there existed a minimum standard of justice in the treatment of foreigners.<sup>56</sup> At the same time, an emerging body of international

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51. M. Sornarajah, *The International Law on Foreign Investment*, 2nd edn (Cambridge: Cambridge University Press, 2004) at 19-20.
52. See A. Heyking, 'L'exterritorialité et ses applications en Extrême-Orient' (1925) 7 RDCADI 237.
53. See Lipson, *supra* note 44 at 12-16, L.T. Lee, *Consular Law and Practice*, 2nd edn (Oxford: Clarendon Press, 1991) at 7-17 and R. Jennings & A. Watts eds., *Oppenheim's International Law*, 9th edn (London: Longman, 1992), §406 at 911.
54. Dunn, *supra* note 22 at 54.
55. In 1910, Elihu Root, then President of the American Society of International Law and former US Secretary of War and Secretary of State, noted: 'The great accumulation of capital in the money centres of the world, far in excess of the opportunities for home investment, has led to a great increase of international investment extending over the entire surface of the earth, and these investments have naturally been followed by citizens from the investing countries prosecuting and caring for the enterprises in the other countries where their investment are made.' E. Root, 'The Basis of Protection to Citizen's Residing Abroad' (1910) 4 AJIL 517 at 518-519.
56. See Brownlie, *System of the Law of Nations*, *supra* note 28 at 7 with respect to the emergence of German, French and English language treatises on the principle of state responsibility in the late nineteenth century and early twentieth century. The international standards of treatment applicable to the economic interests of foreign investors were still, however, nascent. International law treatises written in the early 1900s focus on issues such as denial of justice, equality before the law and mob violence, usually in the context of the rights of the individual. J. Westlake's treatise, *International Law* (Cambridge: Cambridge University Press, 1904) devoted an eight page chapter to 'The Protection of Subjects Abroad' and addressed denial of justice and contract claims. In the 1905 first edition of *International Law*, L. Oppenheim touched on the 'Protection to be Afforded to Foreigner's Person and Property' in one page and simply focused on the requirement for the host state to provide equality before the law. L. Oppenheim, *International Law* (London: Longmans, Green, and Co., 1905) at 376. G.G. Wilson, Professor of International Law at Harvard University addressed the treatment of aliens in two pages and focuses on the right to exclude and expel. With respect to property, he wrote: 'Rights of property and inheritance may be determined by local laws.' G.G. Wilson, *Handbook*

law on state responsibility for the treatment of aliens was developing through various commercial treaties,<sup>57</sup> state practice and the decisions of arbitral tribunals and mixed commissions.<sup>58</sup> Most of the practice and jurisprudence in this area related to injuries to individual foreigners arising from the denial of justice or acts of violence. Although the principles applying to the treatment of economic interests were less developed, there was a consensus amongst capital exporting states that expropriation of property required compensation.<sup>59</sup>

In the early twentieth century, the major powers and capital exporting states, including the US and the UK, took the position that foreign nationals and their property were entitled, under customary international law, to a minimum standard of treatment. This minimum standard was essentially similar to standards of justice and treatment accepted by ‘civilized states’, including the European states and the US.<sup>60</sup> The capital exporting states’ approach is reflected in Elihu Root’s 1910 address to the American Society of International Law:

Each country is bound to give to nationals of another country in its territory the benefit of the same laws, the same administration, the same protection, and the same redress for injury which it gives to its own citizen’s, and neither more nor less: provided the protection which the country gives to its own citizens conforms to the established standard of civilization.

There is a standard of justice, very simple, very fundamental, and of such general acceptance by all civilized countries as to form part of the international law of the world. A country is entitled to measure the standard of justice due an alien by the justice it accords its own citizens only when its system of law and administration conforms to this general standard. If any country’s system of law and administration does not conform to that standard of justice, although the people of the country may be content or compelled to live under it, no other country can be compelled to accept it as furnishing a satisfactory measure of treatment to its citizens.<sup>61</sup>

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*of International Law* (St Paul: West Publishing, 1910) at 145. C.C. Hyde primarily addressed denial of justice and mob violence. C.C. Hyde, *International Law: Chiefly as Interpreted and Applied by the United States* (Boston: Little, Brown and Company, 1922) at 491-496 and 516-524.

57. See Neufeld, *supra* note 10. On early friendship and commerce treaties, see *infra* §1.17.

58. See *supra* note 22 for the principal treatises.

59. See *infra* Chapter 7, §7.5.

60. The term was used almost exclusively to refer to Western or European states. Westlake, *supra* note 56 at 313, argued that these were rules ‘on which the people of European civilization are agreed that legal and administrative procedure ought to be based.’ E. Borchard, in ‘The “Minimum Standard” of the Treatment of Aliens’ (1939) 33 ASIL Proc 51 [Borchard, ‘Minimum Standard’] at 53, states that international law is ‘composed of the uniform practices of civilized states of the western world who gave birth and nourishment to international law.’ These rules included a minimum standard of due process and justice. See the discussion in Anghie, *supra* note 11 at 52 *et seq.*, on the civilized/uncivilized dichotomy.

61. Root, *supra* note 55 at 521-2. Interestingly, Root’s comments focus not only on the delicts of foreign states but also on the breach of international obligations by the US arising out of the mobbing and

**§1.8 The Calvo Doctrine** In response to assertions of a minimum standard of treatment, some states, particularly those in Latin America, endorsed a national treatment or equality of treatment standard. This position is most commonly associated with the Argentine jurist Carlos Calvo, who argued as early as 1868 against the exercise of diplomatic protection and the existence of a minimum standard of treatment. In Calvo's view, state equality required that there be no intervention, diplomatic or otherwise, in the internal affairs of other states, and that foreigners were not entitled to better treatment than host state nationals.<sup>62</sup> The Calvo Doctrine has three distinct elements: foreign nationals are entitled to no better treatment than host state nationals; the rights of foreign nationals are governed by host state law; and host state courts have exclusive jurisdiction over disputes involving foreign nationals.<sup>63</sup> The twin pillars of the Calvo Doctrine are the absolute equality of foreigners with nationals and the principle of non-intervention.<sup>64</sup> At its logical extreme, the doctrine would have abolished the principle of diplomatic protection<sup>65</sup> and the concept of the minimum standard of treatment.<sup>66</sup>

The Calvo Doctrine never attained the status of a principle of customary international law.<sup>67</sup> In the early twentieth century, capital exporting states maintained the view that international law requires a minimum standard of treatment. Capital importing states, however, continued to challenge the minimum standard of treatment, particularly with respect to compensation for expropriation. In 1917, the revolutionary government in Russia issued a decree abolishing all private property, including the property of foreign nationals.<sup>68</sup> Although Western states took the position that the decree violated international law, many of the claims

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lynching of Chinese, Italian and Mexican nationals in various US states between 1880 and 1901.

62. 'It is certain that aliens who establish themselves in a country have the same rights to protection as nationals, but they ought not to lay claim to a protection more extended.' C. Calvo, *Le droit international théorique et pratique*, 5th edn, 1896, Vol. VI at 231 as translated and quoted in Shea, *supra* note 40 at 18. From the Calvo Doctrine rose the Calvo Clause – a contractual clause by which a foreigner purports to waive any right to diplomatic protection vis-à-vis the host state. The clause attempts to ensure equality between foreigners and nationals. If effective, the foreigner, with respect to matters to which the contract applies, would waive any right to the protection of international law. In *North American Dredging Co. (1926)* IV RIAA 26, the US-Mexico Mixed Claims Commission held that a state is not bound by its own national's waiver of diplomatic protection, since the right of diplomatic protection belongs to the state. See Shea, *supra* note 40 at 210. See also M.R. Garcia-Mora, 'The Calvo Clause in Latin American Constitutions and International Law' (1950) 33 Marq L Rev 205 and K. Lipstein, 'The Place of the Calvo Clause in International Law' (1945) BYIL 130.
63. B.M. Cremades, 'Resurgence of the Calvo Doctrine in Latin America' (2006) 7 BLI 53 at 54.
64. Shea, *supra* note 40 at 19-29.
65. *Ibid.*, at 20.
66. The position of absolute equality between nationals and foreigners was formally adopted by Latin American states at the First International Conference of American States in 1889. See Shea, *supra* note 40 at 75.
67. See Shea, *ibid.*, at 20.
68. Lipson, *supra* note 44 at 66-70.

were never formally settled.<sup>69</sup> The Soviet nationalizations of private property were significant because they challenged the assumption that all states were committed to private property, a market economy and limited state control of the economy.<sup>70</sup> Prior to WWI, the need to protect private property had never been seriously challenged; however, after WWI, ideological divisions came to dominate.<sup>71</sup>

**§1.9 Early jurisprudence on the minimum standard of treatment** Despite the challenge posed by Russia and continued Latin American resistance to the minimum standard of treatment, the view that international law required a minimum standard of treatment was reaffirmed during the 1920s in several influential decisions of the US-Mexico General Claims Commission (the Commission). The US and Mexico established the Commission in 1923 to address claims by US citizens against Mexico and those of Mexican citizens against the US.<sup>72</sup> Commission decisions rejected Calvo's vision and affirmed the existence of the minimum standard of treatment.<sup>73</sup> For example, in *Harry Roberts*, the Commission stated that:

Roberts was given the same treatment as that given to all other persons.... Facts with respect to equality of treatment of aliens and nationals may be important in determining the merits of a complaint of mistreatment of an alien. But such equality is not the ultimate test of the propriety of the acts of authorities in the light of international law. That test is, broadly speaking, whether aliens are treated according to ordinary standards of civilization.<sup>74</sup>

In addition to decisions of the Commission, there were other important decisions in the 1920s that reaffirmed the view held by capital exporting states. In 1922, an arbitral tribunal established between Norway and the US declared that international law requires 'just compensation' for the taking of property rights.<sup>75</sup> The

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69. See A. Lowenfeld, *International Economic Law* (Oxford: Oxford University Press, 2002) at 392-393. The US recognized the Soviet government and the extraterritorial effect of Soviet expropriation decrees in the Litvinov Assignment Agreement. Under this Agreement, monies due to the former Russian government by US nationals were assigned to the US government, which in turn would use monies collected to pay off claims of the US and its nationals against the USSR. See J.W. Garner, 'Recognition by the United States of The Government of Soviet Russia' (1935) BYIL 171. France and Russia settled claims as recently as 1997. See P. Juillard & B. Stern, *Les emprunts russes: aspects juridiques* (Paris: Pedone, 2002).

70. Lipson, *supra* note 44 at 70.

71. *Ibid.*, at 73.

72. A.H. Feller, *The Mexican Claims Commissions: 1923-1934* (New York: Macmillan Company, 1935). A Special Claims Commission was also established to address claims arising out of revolutionary conditions in Mexico from 1910 to 1920.

73. Five decisions of the Commission are often cited to support the existence of the minimum standard of treatment: *Neer* (1926) IV RIAA 60, *Faulkner* (1927) 21 AJIL 349, *Harry Roberts* (1927) 21 AJIL 357, *Hopkins* (1927) 21 AJIL 160 and *Way* (1929) 23 AJIL 466. See also Roth, *supra* note 16 at 94-99. See *infra* Chapter 6 on the minimum standard of treatment.

74. *Harry Roberts*, *ibid.*, at 360-361.

75. 'Here it must be remembered that in the exercise of eminent domain the right of friendly alien property must always be respected. Those who ought not to take property without making just

tribunal ordered the US to pay compensation for its requisition of Norwegian ships during WWI.

These developments were further reinforced by judgments of the PCIJ. In *The Mavrommatis Palestine Concessions*, the PCIJ affirmed that diplomatic protection is an ‘elementary principle of international law.’<sup>76</sup> Two years later, in the *Case Concerning Certain German Interests in Polish Upper Silesia*, the PCIJ confirmed that vested rights of foreign nationals must be respected.<sup>77</sup> The PCIJ also held, in the 1928 *Case Concerning the Factory at Chorzów*, that an illegal seizure of property requires reparation.<sup>78</sup> These judgments reflected the view that states owe a duty to other states to treat foreign nationals and their property according to a minimum standard of treatment.

**§1.10 Efforts to codify treatment standards in the 1920s and 1930s** In 1924, the League of Nations established a Committee of Experts for the Progressive Codification of International Law.<sup>79</sup> The Committee reported in 1927, recommending that seven subjects were ripe for codification. On 27 September 1927, the Eighth Assembly of the League of Nations resolved to submit three topics to the First Conference for the Codification of International Law (the 1930 Codification Conference), including the ‘Responsibility of States for Damage done in their Territory to the Person or Property of Foreigners.’<sup>80</sup>

In anticipation of the 1930 Codification Conference, a number of organizations, including the Institute of International Law, Association de Droit International du Japon, the American Institute of International Law and the International Commission of Jurists instituted research projects on rules of international responsibility relating to injuries to foreigners.<sup>81</sup> The Harvard Law School undertook a program of research in international law for the purpose of preparing a draft international convention on each of the three topics to be discussed at the 1930 Codification Conference.<sup>82</sup> The reporter for responsibility of states, Edwin Borchard, prepared a *Draft Convention on Responsibility of States for Damage done in their Territory to the Person or Property of Foreigners* (1929 Harvard Draft).<sup>83</sup>

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compensation at the time or at least without due process of law must pay the penalty for their action.’ *Norwegian Shipowners’ Claims (Norway v. US)* (1922) 1 RIAA 307 at 332.

76. *Mavrommatis*, *supra* note 21.

77. See *Case Concerning Certain German Interests in Polish Upper Silesia (Germany v. Poland)* (1926) PCIJ Ser. A, No. 7 at 22 and 42.

78. *Case Concerning the Factory at Chorzów (Claim for Indemnity) (Germany v. Poland)* (1928) PCIJ Ser. A, No. 17 at 47. With respect to compensation for expropriation, see *infra* Chapter 7.

79. (1925) 5 LNOJ 143.

80. LNOJ Spec Supp 53 at 9. The other two topics were ‘Nationality’ and ‘Territorial Waters’.

81. These projects resulted in various draft codifications, which are reproduced at (1929) 23 AJIL Spec Supp at 219-239.

82. The drafts had no official status. According to the Director of Research, Manley Hudson, the preparation of the drafts ‘has been undertaken with the object of placing before the representatives of the various governments at the First Conference on Codification of International Law the collective views of a group of Americans specially interested in the development of international law.’ (1929) 23 AJIL Spec Supp at 9.

83. The 1929 Harvard Draft and commentary is reproduced at (1929) 23 AJIL Spec Supp at 133-218.

Divided opinion on standards of treatment, however, was evident at the 1930 Hague Conference, during its proceedings on codifying customary international law rules on the ‘Responsibility of States for Damage Caused in Their Territories to the Persons and Properties of Foreigners.’<sup>84</sup> Article 10 of the draft codification provides as follows:

As regards damage caused to the person or property of foreigners by a private person, the State is only responsible if the damage sustained by the foreigner results from the fact that the State has failed to take the measures which may reasonably be expected of it in the circumstances in order to prevent, remedy or inflict punishment for the damage.<sup>85</sup>

In voting on the article, seventeen states (mainly capital importing states) maintained the position that foreign nationals were only entitled to equality of treatment with nationals, while twenty-one states, including the capital exporting states, maintained the existence of a minimum standard of treatment.<sup>86</sup> Divided opinion on the issue of the minimum standard was a significant factor in the breakdown of the conference’s codification efforts in the area of state responsibility.<sup>87</sup> The final version of the codification was not adopted because it failed to receive the requisite support of two-thirds of the states at the conference.

**§1.11 Convention on the Treatment of Foreigners** In addition to the codification efforts at the 1930 Codification Conference, states also attempted to conclude a *Convention on the Treatment of Foreigners* (1929 Draft Convention), in the late 1920s and early 1930s, under the auspices of the League of Nations.<sup>88</sup> A diplomatic conference – the International Conference on the Treatment of Foreigners – was held in Paris in late 1929 with forty-seven states participating.<sup>89</sup> The origin for the conference lay in Article 23 of the *Covenant of the League of Nations*,

84. See S. Rosenne, *League of Nations Conference for the Codification of International Law (1930)* (Dobbs Ferry, NY: Oceana Publications Inc., 1975), Vol. II at 423-702 for a collection of the documents relating to this topic. See also S. Rosenne, *League of Nations Committee of Experts for the Progressive Codification of International Law (1925-1928)* (Dobbs Ferry, NY: Oceana Publications Inc., 1972), Vol. 2 at 118 for the Report of the Sub-Committee of Experts by Guerrero, Rapporteur and Wang Chung-Hui. For commentary, see G.H. Hackworth, ‘Responsibility of States for Damage Caused in Their Territories to the Persons and Properties of Foreigners’ (1930) 24 AJIL 500 and E. Borchard, ‘Responsibility of States at the Hague Codification Conference’ (1930) 24 AJIL 517 [Borchard, ‘Responsibility of States’].

85. See Hackworth, *ibid.*, at 513-514; Borchard, ‘Responsibility of States’, *ibid.*, at 533-537 and Roth, *supra* note 16 at 68-80.

86. See Hackworth, *ibid.*, at 514 and Roth, *ibid.*, at 74.

87. J.W. Cutler, ‘The Treatment of Foreigners in Relation to the Draft Convention and Conference of 1929’ (1933) 27 AJIL 225 at 230.

88. The text of the 1929 Draft Convention is reproduced in *International Conference on the Treatment of Foreigners, Preparatory Documents*, L.N. Doc. C.36.M. 21.1929.II. The conference proceedings are reproduced in L.N. Doc. C.97.M. 23.1930.II. For commentary see A.K. Kuhn, ‘The International Conference on the Treatment of Foreigners’ (1930) 24 AJIL 570 and Cutler, *ibid.*

89. See *Final Protocol of the First Session of the Conference on the Treatment of Foreigners* (Paris, 5 Dec. 1929), (1930) 11 LNOJ 171.

under which states undertook to ‘secure and maintain equitable treatment for the commerce of all members of the League.’<sup>90</sup> At the World Economic Conference in Geneva in 1927, the International Chamber of Commerce (ICC) had submitted a report on the treatment of foreigners, recommending that the Council of the League hold a diplomatic conference.<sup>91</sup> The Council entrusted the Economic Committee of the League of Nations to prepare a draft convention to serve as a basis for discussions at the conference.<sup>92</sup>

The twenty-nine articles of the draft convention were far-reaching.<sup>93</sup> They accorded foreigners equality with nationals (national treatment) in almost all respects, including the right of establishment, freedom in relation to fiscal matters, freedom to travel, carry on a business and engage in all occupations, and the ability to exercise civil, judicial and succession rights.<sup>94</sup> The conference, however, revealed significant differences of opinion between capital exporting and importing states on the principle of equality. The report of the President of the Conference, M. Devèze, highlighted that:

... after three weeks’ discussion, the draft Convention has been so profoundly modified and its essential provisions so attenuated that the delegations with liberal tendencies stated their intention of not signing a convention which, in their view, would have constituted, not the progress they wished to achieve, but, on the contrary, a retrograde step as compared with the present situation.<sup>95</sup>

**§1.12 Seventh International Conference of American States** Overwhelming Latin American support for the equality of treatment standard was also evident a few years later at the Seventh International Conference of American States in Montevideo, where states concluded the 1933 *Convention on the Rights and Duties of States* (Montevideo Convention).<sup>96</sup> Article 9 of the Montevideo Convention provides, in part, that: ‘Nationals and foreigners are under the same protection of the law and the national authorities and the foreigners may not claim rights other or more extensive than those of the nationals.’ The Convention was

90. *Covenant of the League of Nations*, 28 Jun. 1919 (1920) 1 LNOJ 3 (entered into force 10 Jan. 1920).

91. Kuhn, *supra* note 88 at 571.

92. *Ibid.*

93. See *Work of the International Conference on the Treatment of Foreigners: Report by M. Devèze, President of the Conference*, Geneva, 14 Jan. 1930, L.N. Doc. C.10.1930.II [Report by M. Devèze].

94. The draft convention also provided a number of exceptions to the national treatment obligation, for example, the exclusion of certain professions (lawyers and stockbrokers), government contracts, exploitation of minerals and hydraulic power and limitation on ownership of land and business for national security purposes. National treatment extended to foreign companies (Art. 16(8)).

95. Report by M. Devèze, *supra* note 93.

96. *Convention on the Rights and Duties of States*, 26 Dec. 1933, 165 LNTS 19 (1933) (entered into force 26 Dec. 1924).

adopted, but with reservations deposited by the US and other capital exporting states.<sup>97</sup>

**§1.13 The Hull Rule** The disagreement between capital exporting and importing states over the minimum standard of treatment came to a head in an exchange of correspondence between Mexico and the US in 1938 regarding the standard of compensation for expropriation. The US insisted on the Hull Rule, named after US Secretary of State Cordell Hull, who, in response to the expropriation of American-held oil interests by Mexico in 1938,<sup>98</sup> argued that ‘adequate, effective and prompt payment for the properties seized’<sup>99</sup> was required under international law. By contrast, Mexico argued that, in the case of general and impersonal expropriation for the purpose of redistribution of land, it was only required to pay compensation in accordance with its national laws. In Mexico’s view, international law distinguished between expropriations resulting from a ‘modification of the juridical organization and which affect equally all the inhabitants of the state and those otherwise decreed in specific cases and which affect interests known in advance and individually determined.’<sup>100</sup> General social reforms imposed no international obligation to provide immediate compensation, as foreigners were only entitled to the same treatment as Mexican citizens.<sup>101</sup> Thus, although the Hull Rule focuses on the required standard of compensation under international law, the actual dispute between Mexico and the US that gave rise to the articulation of the rule concerned the types of measures affecting property that are compensable under international law. The standard of compensation for expropriation continued to be a source of significant disagreement in the post-WWII era.

## II POST-WWII DEVELOPMENTS

**§1.14 Decolonization and nationalizations** Disputes over the treatment of foreign investment increased and intensified after WWII as the process of decolonization resulted in colonial territories becoming states. Many of these newly independent states, along with the Eastern European communist states, adopted socialist economic policies, including large scale nationalizations of key sectors of their economies.<sup>102</sup> Notable examples include the nationalizations of major

97. For a discussion of Art. 9, see Borchard, ‘Minimum Standard’, *supra* note 60 at 69.

98. See J.L. Kunz, ‘The Mexican Expropriations’ (1940) 17 NYULQR 327.

99. US Secretary of State to Mexican Ambassador, 22 Aug. 1938, reproduced in ‘Mexico-United States: Expropriation by Mexico of Agrarian Properties Owned by American Citizens’ (1938) 33 AJIL Supp at 191-201.

100. Mexican Minister of Foreign Affairs to US Ambassador, 1 Sep. 1938, *supra* note 99 at 201-207.

101. See discussion by Lowenfeld, *supra* note 69 at 397-403.

102. See I. Foighel, *Nationalization: A Study in the Protection of Alien Property in International Law* (London: Stevens & Sons Limited, 1957); G. White, *Nationalisation of Foreign Property* (London: Stevens & Sons Limited, 1961); R.B. Lillich, ed., *The Valuation of Nationalized Property in International Law* (Charlottesville: University Press of Virginia, 1972); M. Sornarajah, *The Pursuit of Nationalized Property* (Dordrecht: Martinus Nijhoff Publishers,

industries in Eastern European states, China, Cuba, and Latin America (Argentina, Bolivia, Brazil, Chile, Guatemala and Peru); the Indonesian nationalization of Dutch properties; the Egyptian nationalization of the Suez Canal; and the nationalizations of the oil industry throughout the Middle East and Northern Africa (Algeria, Iran, Iraq, Libya, Kuwait and Saudi Arabia).<sup>103</sup> The foreign investment disputes that ensued focused on two principal issues: the extent to which acquired rights, including natural resource concessions granted by colonial powers, were to be respected; and the standard of compensation for the expropriation of those acquired rights. In a series of cases, newly independent and developing states asserted that, upon independence, states were entitled to review concession agreements that had been granted by colonial powers, and, furthermore, maintained that compensation for the expropriation of property would be based on national laws.<sup>104</sup>

**§1.15 The Havana Charter and the International Trade Organization** The post-WWII political and economic climate stimulated a series of initiatives with the goal of establishing a multilateral legal framework for investment.<sup>105</sup> The first attempt arose during the negotiations for the proposed International Trade Organization (ITO), an institution intended as the third pillar of the new international financial system alongside the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (the World Bank).<sup>106</sup> The initial US proposal for the ITO contained no investment provisions. This reflected the US preference for bilateral commercial treaties with high standards of protection, rather than a multilateral agreement that reflected the ‘lowest common denominator of protection.’<sup>107</sup> During the ITO negotiations, articles on investment protection with provisions for national treatment, most-favoured-nation (MFN) treatment and just compensation for expropriation were introduced. States, however, were unable to agree on the standards.<sup>108</sup> As a result, the final draft of the

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1986) and A.A. Akinsanya, *The Expropriation of Multinational Property in the Third World*, *supra* note 50.

103. See Lowenfeld, *supra* note 69 at 405. In the period from 1960 to 1977, there were on average ninety-eight cases of expropriation of foreign property a year. See F.N. Burton & H. Inoue, ‘Expropriation of Foreign-Owned Firms in Developing Countries: A Cross National Analysis’ (1984) 18 JWTL 396 at 397.

104. See *infra* §1.23.

105. For a comprehensive bibliography of works on multilateral approaches to foreign investment current to the early 1990s, see (1992) 7 ICSID Rev 504. See, in particular, the review of international instruments by F. Tschofen, ‘Multilateral Approaches to the Treatment of Foreign Investment’ (1992) 7 ICSID Rev 384.

106. On the investment aspects of the IMF and World Bank, see T.L. Brewer & S. Young, *The Multilateral Investment System and Multinational Enterprises* (Oxford: Oxford University Press, 1998) at 70-73. The role of the IMF *Articles of Agreement* with respect to transfer of funds is addressed at Chapter 8, §8.3.

107. C. Wilcox, *A Charter for World Trade* (New York: Macmillan, 1949) at 146.

108. See Brewer & Young, *supra* note 106 at 66-68.

*Havana Charter for the International Trade Organization* (Havana Charter)<sup>109</sup> only briefly addressed the issue of investment protection by providing a prohibition on ‘unreasonable or unjustifiable action’ and permitting the ITO to make recommendations for bilateral or multilateral investment agreements.<sup>110</sup> The Havana Charter never came into force and the ITO was never established, chiefly because the US Senate would not approve US ratification.<sup>111</sup> As a result, the *General Agreement on Tariffs and Trade* (GATT),<sup>112</sup> which had been negotiated to liberalize trade, was applied provisionally without an overarching ITO framework.<sup>113</sup> Thus, although international trade and investment are economically intertwined,<sup>114</sup> the absence of investment from the purview of the GATT meant that after 1947, international investment and trade law developed independently of one another.

**§1.16 Non-governmental initiatives to create a multilateral legal framework for investment** From the 1940s to the early 1960s there were four important non-governmental initiatives designed to create a multilateral legal framework for foreign investment. In 1949, the ICC proposed an *International Code of Fair Treatment for Foreign Investment* (ICC Code).<sup>115</sup> The ICC Code reflected high standards of treatment for foreign investment by providing national treatment and MFN treatment for investments, prohibiting restrictions on transfers of funds, ensuring ‘fair compensation according to international law’ in the event of expropriation, and providing binding state-to-state dispute resolution before the ICC

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109. *Havana Charter for an International Trade Organization*, 24 Mar. 1948, UN Conference on Trade and Employment, U.N. Doc. E/CONF.2/78, Sales No. 1948.II.D.4.
110. Art. 11(1)(b) of the Havana Charter provides: ‘No Member shall take unreasonable or unjustifiable action within its territory injurious to the rights or interests of nationals of other Members in the enterprise, skills, capital, arts or technology which they have supplied.’ Art. 11(2) provides, in part, that: ‘The Organization may, in such collaboration with other inter-governmental organizations as may be appropriate: (a) make recommendations for and promote bilateral or multilateral agreements on measures designed: (i) to assure just and equitable treatment for the enterprise, skills, capital, arts and technology brought from one Member country to another...’
111. J.H. Jackson, *The World Trading System Law and Policy of International Economic Relations*, 2nd edn (Cambridge, MA: MIT Press, 1997) at 38.
112. *General Agreement on Tariffs and Trade*, 30 Oct. 1947, 55 UNTS 814 (applied provisionally as from 1 Jan. 1948 pursuant to the Protocol of Provisional Application).
113. Jackson, *supra* note 111 at 39.
114. Where there are import barriers, a producer may decide to set up a local subsidiary to produce goods locally, thereby ‘jumping’ the trade barrier. In many cases, trade and investment are substitutes. Whether a producer decides to engage in trade or investment will depend on both economic factors and the regulatory environment, including the comparative legal barriers to trade and investment. See M. Trebilcock & R. Howse, *The Regulation of International Trade*, 3rd edn (London: Routledge, 2005) at 439-446.
115. International Chamber of Commerce, *International Code of Fair Treatment of Foreign Investment*, ICC Pub. No. 129 (Paris: Lecraw Press, 1948), reprinted in UNCTAD, *International Investment Instruments: A Compendium*, Vol. 3 (New York: United Nations, 1996) [IIA Compendium] at 273. The compendium is available online on the UNCTAD website.

International Court of Arbitration. States were reticent to accept such a broad ranging investment regime and the ICC Code was never adopted.

The next initiative was the International Law Association (ILA) *Draft Statutes of the Arbitral Tribunal for Foreign Investment and the Foreign Investment Court* (ILA Statute).<sup>116</sup> The purpose of the proposed tribunal and court was to provide an impartial forum for the resolution of foreign investment disputes rather than to establish specific standards of treatment for foreign investment. States never adopted the ILA Statute.

Although the ICC Code and the ILA Statute were not adopted, the initiatives were significant in signaling both a conceptual and semantic change from the traditional notions of protection of aliens and their property. Instead of state responsibility for injuries to aliens and their property, the primary concern had become the protection of foreign investment with the object of promoting economic development.<sup>117</sup> The change reflected a shift in emphasis from the protection of private property as an end in itself to a policy of promoting conditions upon which the private foreign investment necessary for economic development could occur. This shift from the language of property to investment took place at the same time that newly independent states were beginning to challenge the system of acquired rights (concessions, contracts and other forms of tangible and intangible property) and could be seen as an attempt to regroup the protection of private property in the language of international economic development.<sup>118</sup> This conceptual and semantic change would be reflected in future developments in the international legal framework for investment.

The third non-governmental initiative was the 1959 *Draft Convention on Investments Abroad* (Abs-Shawcross Draft Convention).<sup>119</sup> The Draft Convention was prepared under the leadership of Hermann Abs, the Director-General of Deutsche Bank, and Lord Shawcross, former Attorney General of the UK. The draft had its origins partly in a 1957 draft document entitled the *International*

116. Reprinted in *IIA Compendium, ibid.*, at 259.

117. For example, the preamble to the ICC Code, *supra* note 115, notes that ‘an ample flow of private investments is essential to the economic and industrial growth of their countries and to the welfare of their peoples ...’

118. See T. Wälde, ‘The Specific Nature of Investment Arbitration – Report of the Director of Studies of the English-speaking Section of the Centre,’ *New Aspects of International Investment Law*, eds P. Khan & T. Wälde (Leiden: Martinus Nijhoff Publishers, 2007) at 43.

119. *IIA Compendium, supra* note 115, Vol. 5 at 395. The draft was first published in (1960) 9 JPL 116. See also H. Shawcross, ‘The Problems of Foreign Investment in International Law’ (1961) 102 RDCADI 334 and Chapter 8 of G. Schwarzenberger, *Foreign Investments and International Law* (New York: Frederick A. Praeger, 1969) for a history of and commentary on the Abs-Shawcross Draft Convention. For contemporary discussions of proposals for multilateral foreign investment protection, see A.S. Miller, ‘Protection of Private Foreign Investment by Multilateral Convention’ (1959) 53 AJIL 371; R. Gardner, ‘International Measures for the Promotion and Protection of Foreign Investment’ (1959) ASIL Proc 255; A.A. Fatouros, ‘An International Code to Protect Private Investment-Proposals and Perspectives’ (1961) 14 UTLJ 77; E. Snyder, ‘Protection of Private Foreign Investment: Examination and Appraisal’ (1961) 10 ICLQ 469 and D.A.V. Boyle, ‘Some Proposals for a World Investment Convention’ (1961) JBL 18 and 155.

*Convention for the Mutual Protection of Private Property Rights in Foreign Countries*, published by a group of German business people called the Society to Advance the Protection of Foreign Investments.<sup>120</sup> The Abs-Shawcross Draft Convention provided for a minimum standard of treatment (defined as ‘fair and equitable treatment’),<sup>121</sup> protection against ‘unreasonable or discriminatory measures,’ observance of undertakings, and ‘just and effective’ compensation for expropriation. Importantly, the Abs-Shawcross Draft Convention was the first instrument that expressly provided for direct investor-state arbitration.<sup>122</sup>

Two years later, the 1961 *Draft Convention on the International Responsibility of States for Injuries to Aliens*<sup>123</sup> (1961 Harvard Draft) was prepared by Louis Sohn and Richard Baxter at the request of the UN Secretariat in an attempt to codify the international law on state responsibility. The 1961 Harvard Draft is an updated version of the 1929 Harvard Draft.<sup>124</sup> Early drafts of the 1961 Harvard Draft were presented to the International Law Commission (ILC).<sup>125</sup> The draft has been cited by a number of IIA tribunals as an authoritative statement of certain aspects of the minimum standard of treatment.<sup>126</sup>

**§1.17 Bilateral and regional initiatives** In the post-WWII era, several states, including the UK, US and Japan, entered into bilateral treaties on commerce and navigation.<sup>127</sup> These treaties were often called Treaties of Friendship, Commerce

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120. This document is also known as the *Köln Draft Convention*. See Tschofen, *supra* note 105 at 389.
121. See *infra* Chapter 6, §6.14, for a discussion of early treaty practice on fair and equitable treatment.
122. Art. VII states that nationals may make claims for a breach of the convention before an arbitral tribunal established under the convention provided the state had consented to the arbitral jurisdiction through a special agreement or unilateral declaration.
123. (1961) 55 AJIL 545. The text of the 1961 Harvard Draft is accompanied by extensive commentary.
124. See *supra* §1.10.
125. (1961) 55 AJIL 545 at 546.
126. The Harvard Draft has been cited in several cases in the context of expropriation: *Saluka Investments BV v. Czech Republic* (Partial Award, 17 Mar. 2006) at paras 256-257; *Pope & Talbot Inc v. Canada* (Interim Award, 26 Jun. 2000) at para. 102; *Wena Hotels Limited v. Egypt* (Award, 8 Dec. 2000) at note 242, as well as in *United Parcel Service America Inc v. Canada* (Award on Jurisdiction, 22 Nov. 2002) at paras 90-91 on the issue of anti-competitive behaviour, and in *Mondev International Ltd. v. United States* (Award, 11 Oct. 2002) at footnote 57 on fair and equitable treatment. See also *The Loewen Group, Inc. and Raymond L. v. United States* (Award, 26 Jun. 2003) at para. 167 and *Tokios Tokelés Group, Inc. and Raymond L. v. Ukraine* (Award, 29 Apr. 2004) at para. 92. In *United Parcel Service, ibid.* at paras 89-89, the tribunal characterized it as ‘something of a high water mark in the statement of the law for the protection of aliens.’
127. See generally D. Blumenwitz, ‘Treaties of Friendship, Commerce and Navigation’ in *Encyclopedia, supra* note 8, Vol. IV at 953. For British treaty practice, see G. Schwarzenberger, *Foreign Investments and International Law, supra* note 119. For US practice, see R.R. Wilson, *United States Commercial Treaties and International Law* (New Orleans: Hauser Press, 1960) and H. Walker, Jr. ‘Treaties for the Encouragement and Protection of Foreign Investment: Present United States Practice’ (1956) 5 AJCL 229. For Japanese practice, see L. Jerold Adams,

and Navigation, or FCN treaties.<sup>128</sup> Although traditionally the focus of FCN treaties had been to promote trade and commercial relationships,<sup>129</sup> in the post-WWII era the investment protection function of these treaties came to dominate.<sup>130</sup> FCN treaties, designed to facilitate post-war reconstruction in Europe, provided significant investment protections.<sup>131</sup> In addition, the implementation of the GATT in 1947 reduced the need for trade provisions in FCN treaties amongst GATT Contracting Parties.<sup>132</sup> In Europe the most significant development was the creation of the common market in 1957.<sup>133</sup>

One of the earliest post-war examples of a regional initiative was the Ninth International Conference of American States (1948), which adopted the *Economic Agreement of Bogotá*.<sup>134</sup> The Agreement was signed by twenty Latin American states, but never entered into force. Although certain provisions of the *Economic Agreement of Bogotá* could be viewed as providing for a minimum standard of treatment,<sup>135</sup> many Latin American states made reservations providing that standards of treatment were governed by the state constitution.<sup>136</sup>

In 1961, the then twenty Member States of the Organization for Economic Co-operation and Development (OECD) liberalized capital transfers and investment

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'Japanese Treaty Patterns' (1972) 12 *Asian Survey* 242 and L. Jerod Adams, *Theory, Law and Policy of Contemporary Japanese Treaties* (New York: Oceana Publications Inc., 1974).

128. From 1946 to 1966, the US entered into twenty-one FCN treaties. Two of the treaties were subject to proceedings before the International Court of Justice: *Military and Paramilitary Activities In and Against Nicaragua (Nicaragua v. US)* [1984] ICJ Rep 392 and [1986] ICJ Rep 14, and *Elettronica Sicula S.p.A. (ELSI) (US v. Italy)* [1989] ICJ Rep 15 [ELSI].
129. The US entered into numerous FCNs with Latin American, Asian and African states in the nineteenth century. See Wilson, *supra* note 127, and Vandevelde, *United States Investment Treaties*, *supra* note 43.
130. Vandevelde, *ibid.*, at 15-16 and K.J. Vandevelde, 'A Brief History of International Investment Agreements' (2005) 12 UCDJILP [Vandevelde, 'A Brief History'] at 162.
131. In 1956 Herman Walker, Jr., a former advisor on commercial treaties for the US State Department wrote that the 'FCN treaty as a whole is an investment treaty'. H. Walker, Jr. 'Treaties for the Encouragement and Protection of Foreign Investment: Present United States Practice' (1956) 5 *AJCL* 229 at 244-245.
132. See Wilson, *supra* note 127. Post-WWII US FCN treaties generally provided national and MFN treatment, the rights of foreign nationals to enter and stay in the host state, guarantees regarding freedom of conscience, fair and/or equitable treatment, a constant protection guarantee, compensation for expropriation, transfer of funds and freedom of navigation. Disputes regarding the interpretation or application of the treaties were to be resolved by the ICJ. Vandevelde, 'A Brief History', *supra* note 130 at 17.
133. P. Craig and G. De Búrca, *EU Law: Texts, Cases, and Materials*, 3rd edn (Oxford; New York: Oxford University Press, 2002) [EU Law] at 11-12.
134. Organization of American States Treaty Series No. 21, available on the OAS website.
135. In particular, Art. 25 provides: 'Los Estados no tomarán acción discriminatoria contra las inversiones por virtud de la cual la privación de los derechos de propiedad legalmente adquiridos por empresas o capitales extranjeros se lleve a cabo por causas o en condiciones diferentes a aquellas que la Constitución o las leyes de cada país establezcan para la expropiación de propiedades nacionales. Toda expropiación estará acompañada del pago del justo precio en forma oportuna, adecuada y efectiva.'
136. See Brownlie, *International Law and the Use of Force by States*, *supra* note 49. See C.G. Fenwick, 'The Ninth International Conference of American States' (1948) 42 *AJIL* 562.

in major service industries through codes on the liberalization of capital movements and current invisible operations.<sup>137</sup>

**§1.18 Increasing resort to international arbitration post-WWII** In the post-WWII era, the use of international arbitration to resolve foreign investment disputes significantly increased.<sup>138</sup> The assertion of economic sovereignty by capital importing states and the implementation of socialist economic policies in the 1950s augmented the risks for foreign investment of expropriations, nationalizations, the imposition of new regulatory controls, and breaches of contract.<sup>139</sup> Although many developing countries viewed international arbitration with distrust,<sup>140</sup> foreign investors generally preferred it to submitting disputes to local courts where decisions might be affected by bias, corruption and inefficiency. Investors began to use various contractual mechanisms, including stabilization, choice of law and international arbitration clauses in order to mitigate political risks.<sup>141</sup> Other risk management mechanisms, such as political risk insurance, also began to be available at this time.<sup>142</sup>

Many international arbitrations in the period immediately after WWII were the result of the cancellation or nationalizations of oil concessions.<sup>143</sup> In these

137. The codes are legally binding on OECD Member States under the convention on the *Organisation for Economic Co-operation and Development* (14 Dec. 1960), 888 UNTS 179 (entered into force 30 Sep. 1961). As of 1 May 2008, thirty states have ratified the Convention. See *infra* Chapter 8, §8.4, for discussion of the codes on the liberalisation of capital movements and current invisible operations.

138. Prior to WWII, almost all arbitral tribunals or mixed commissions created to address foreign investment claims were established by agreement between the home and host state *after* a dispute had arisen. For example, see *The Jaffa-Jerusalem Railway Arbitration*, reproduced in S. Rosenne, 'The Jaffa-Jerusalem Railway Arbitration (1922)' (1998) 28 IYBHR 239. Also see M.R. Reynolds, 'The Jaffa-Jerusalem Railway Company Arbitration 1922' (1991) 57 Arbitration 42. There were a number of arbitrations arising out of concession agreements made in the 1920s between Western companies and the Soviet Union. See V.V. Veeder, 'Lloyd George, Lenin and Cannibals: The Harriman Arbitration' (2000) 16 AI 115 and V.V. Veeder, 'The 1921-1923 North Sakhalin Concession Agreement: The 1925 Court Decisions Between the US Company Sinclair Exploration and the Soviet Government' (2002) 18 AI 185. Also see the award in the *Lena Goldfields Arbitration* and commentary by A. Nussbaum in (1950) 36 CLQ 31 and V.V. Veeder, 'The *Lena Goldfields* Arbitration: The Historical Roots of Three Ideas' (1998) 47 ICLQ 747. See also S.M. Schwebel & J.G. Wetter, 'Some Little Known Cases on Concessions' reprinted in S.M. Schwebel, *Justice in International Law* (Cambridge: Grotius Publications/Cambridge University Press, 1994) at 436.

139. See generally Rubins & Kinsella, *supra* note 5.

140. See J. Paulsson, 'Third World Participation in International Investment Arbitration' (1987) 2 ICSID Rev 19 and A.A. Shalakany, 'Arbitration and the Third World: A Plea for Reassessing Bias under the Specter of Neoliberalism' (2000) 41 HILJ 419.

141. See Rubins & Kinsella, *supra* note 5 at 43-68 and Sornarajah, *supra* note 51 at 404-415.

142. See *infra* §1.29.

143. See *Petroleum Development Ltd. v. The Sheikh of Abu Dhabi* (1951) 18 ILR 144; *Ruler of Qatar v. International Marine Oil Co.* (1953) 20 ILR 534; *Saudi Arabia v. Arabian American Oil Co. (ARAMCO)* (1963) 27 ILR 117; *Sapphire International Petroleums Ltd. v. National Iranian Oil Co.* (1963) 35 ILR 136; *BP Exploration Company Ltd. v. Libya* (1979) 53 ILR

arbitrations, tribunals had to consider the applicable law and the extent to which the proper law of the contract included general principles of international law, such as the observance of commitments in good faith and respect for acquired rights.<sup>144</sup> The cases gave rise to a continuing debate in international law regarding the extent to which state responsibility arises for a breach of a contract between a foreign national and a host state.<sup>145</sup>

**§1.19 New York Convention** The increased use of international arbitration to settle foreign investment and commercial disputes exposed the practical difficulties involved in enforcing international arbitral awards. A key development in the evolving international legal framework for international arbitration was the conclusion and widespread ratification of the *1958 New York Convention on the Recognition of Foreign Arbitral Awards* (the New York Convention),<sup>146</sup> which provides for the recognition and enforcement of foreign arbitral awards and limits the grounds upon which local courts may refuse to recognize and enforce awards.<sup>147</sup> Importantly, the New York Convention makes respect of arbitration agreements a treaty obligation. Although the New York Convention provides the foundation for international arbitration, it does not address the issue of state immunity; thus, even if a foreign investor obtains a favourable arbitral award and seeks to enforce it against state assets located in another state, the assets may be

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297; *Texaco Overseas Petroleum Co. (TOPCO) and Californian Asiatic Oil Co. v. Libya* (1977) 104 JDI 350 (French original), (1979) 53 ILR 389 (English translation); *Libyan American Oil Co. (LIAMCO) v. Libya* (1981) 20 ILM 1; *Kuwait v. American Independent Oil Company (AMINOIL)* (1982) 21 ILM 976; *Elf Aquitaine Iran v. NIOC* (1982) 11 YCA 112. For commentary on the cases and further sources see Lowenfeld, *supra* note 69 at 416-431 and D.W. Bowett. 'State contracts with aliens: contemporary developments on compensation for termination or breach' (1988) 59 BYIL 49-74. For a critical assessment of the arbitral treatment of state contracts, see Anghie, *supra* note 11 at 226-244.

144. See Lowenfeld, *supra* note 69 at 417-430 and Paulsson, *supra* note 140. See *infra* Chapter 2 for discussion of applicable law in IIAs.

145. See P. Weil, 'Problèmes relatifs aux contrats passés entre un Etat et un particulier' (1969) 128 (III) RDCADI 95; P. Weil, 'Droit international et contrats d'Etat' in D. Bardonnet *et al.* eds., *Mélanges offerts à Paul Reuter: le droit international: unité et diversité*, (Paris: Pedone, 1981) at 549; S.J. Toope, *Mixed International Arbitration: Studies in Arbitration between States and Private Persons* (Cambridge: Grotius, 1990); T.E. Carbonneau, ed., *Lex Mercatoria and Arbitration: A Discussion of the New Merchant Law* (Dobbs Ferry, N.Y.: Transnational Juris Publications, 1990) and Sornarajah, *supra* note 51 at 416-433. This issue has also arisen under IIA provisions providing for the observance of undertakings. See *infra* Chapter 9.

146. *Convention on the Recognition and Enforcement of Foreign Arbitral Awards*, 10 Jun. 1958, 330 UNTS 38 (entered into force 7 Jun. 1959).

147. A.J. van den Berg, *The New York Arbitration Convention of 1958: Towards a Uniform Judicial Interpretation* (Boston: Kluwer Law and Taxation, 1981) and E. Gaillard & J. Savage, eds, *Fouchard, Gaillard, Goldman on International Commercial Arbitration* (The Hague; Boston: Kluwer Law International, 1999) at 966-997. See the *Yearbook of Commercial Arbitration* for discussion of court decisions applying the Convention. As of 10 May 2008, there were 142 parties to the New York Convention.

subject to immunity from execution under the law of the state where the asset is located.

**§1.20 Permanent Sovereignty Over Natural Resources** Confronted with the legacy of colonialism and continued foreign control over resources, throughout the 1950s developing states sought to affirm their economic independence. One avenue for the assertion of economic independence was through the United Nations General Assembly, which in 1952, passed the first of seven resolutions on Permanent Sovereignty Over Natural Resources.<sup>148</sup> In the late 1950s the UN Commission on Permanent Sovereignty over Natural Resources was established to study the question of national control over resources. In 1962, the General Assembly passed Resolution 1803, which declares that the ‘right of peoples and nations to permanent sovereignty over their natural wealth and resources must be exercised in the interest of their national development and of the well-being of the people of the State concerned.’<sup>149</sup> The Resolution reaffirmed that the admission of foreign investment was subject to the authorization, restriction or prohibition of the state.<sup>150</sup> Once admitted, however, foreign investment was to be treated in accordance with national and international law.<sup>151</sup> Paragraph 4 of the Resolution addresses expropriation as follows:

Nationalization, expropriation or requisitioning shall be based on grounds or reasons of public utility, security or the national interest which are recognized as overriding purely individual or private interests, both domestic and foreign. In such cases the owner shall be paid appropriate compensation, in accordance with the rules in force in the State taking such measures in the exercise of its sovereignty and in accordance with international law. In any case where the question of compensation gives rise to a controversy, the national jurisdiction of the State taking such measures shall be exhausted. However, upon agreement by sovereign States and other parties concerned, settlement of the dispute should be made through arbitration or international adjudication.

Paragraph 4 affirms that appropriate compensation *shall* be paid for expropriation, thereby confirming the customary international law requirement of compensation

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148. GA Res. 626 (VII), (1952) YBUN at 387.

149. GA Res 1803, 14 Dec. 1962, *reprinted in* (1963) 2 ILM 223. The resolution was passed by eighty-seven votes in favour, two against (France and South Africa) and twelve abstentions (Communist states, Ghana and Burma). For a discussion of the drafting of the resolution, see S.M. Schwebel, ‘The Story of the UN’s Declaration on Permanent Sovereignty Over Natural Resources’ (1963) 49 ABAJ 463 *reprinted in* Schwebel, *Justice in International Law*, *supra* note 138 and K. Gess, ‘Permanent Sovereignty Over Natural Resources’ (1974) 13 ICLQ 398. For a critical commentary on the resolution and K. Gess’ article, see A. Anghie, *Imperialism, Sovereignty and the Making of International Law* (Cambridge: Cambridge University Press, 2005) at 216-220.

150. *Ibid.*, at para. 2.

151. *Ibid.*, at para. 3.

for expropriation.<sup>152</sup> The US had proposed that appropriate compensation be defined as ‘prompt adequate and effective compensation,’ but this proposal was withdrawn because it lacked support. An amendment by the USSR proposing that national law ought to govern the standard of compensation was defeated.<sup>153</sup> Thus, the reference to ‘appropriate compensation,’ without elaboration, was a compromise between the US position and the position of states advocating a national treatment standard.

Resolution 1803 also provides that ‘foreign investment agreements freely entered into by or between sovereign States shall be observed in good faith,’ but does not expressly address foreign investment contracts entered into before a state had acquired independence.

**§1.21 International Centre for Settlement of Investment Disputes** The establishment in 1965 of the International Centre for Settlement of Investment Disputes (ICSID) under the auspices of the World Bank was the next important step in the creation of the international legal framework for foreign investment protection.<sup>154</sup> Discussions on the standard of investment protection in multilateral fora, including the United Nations, had revealed the divided state of opinion on substantive standards. In 1961, Aron Broches, General Counsel of the World Bank, proposed creating a mechanism for the impartial settlement of international investment disputes, rather than seeking agreement on substantive standards of treatment.<sup>155</sup> The ICSID was the result, and was designed to provide a neutral forum for the settlement of investment disputes<sup>156</sup> with the desired consequence of creating ‘an atmosphere of mutual confidence and thus stimulating a larger flow of private international capital into those countries which wish to attract it.’<sup>157</sup> Ibrahim

152. It should be noted, however, that the preamble to the resolution expressly provides that ‘nothing in paragraph 4 below in any way prejudices the position of any Member State on any aspect of the question of the rights and obligations of successor States and Governments in respect of property acquired before the accession to complete sovereignty of countries formerly under colonial rule.’

153. See Lowenfeld, *supra* note 69 at 408; Gess, *supra* note 149 at 420-429 and Schwebel, *supra* note 149 at 465-466.

154. *Convention on the Settlement of Investment Disputes between States and Nationals of Other States*, 18 Mar. 1965, (1965) 4 ILM 524. The convention is commonly called the ICSID or Washington Convention. As of 4 Nov. 2007, 155 states have signed and 143 have ratified the ICSID Convention. For legal commentary on the Convention and references to other sources see: C. Schreuer, *The ICSID Convention: A Commentary* (Cambridge: Cambridge University Press, 2001) [Schreuer, *ICSID Commentary*]; E. Gaillard, *La Jurisprudence du CIRDI* (Paris, Pedone, 2004); L. Reed, J. Paulsson & N. Blackaby, *Guide to ICSID Arbitration* (The Hague: Kluwer Law, 2004); and S. Manciaux, *Investissements étrangers et arbitrage entre Etats et ressortissants d’autres Etats, Trente années d’activité du CIRDI* (Paris: Litec, 2004). The ICSID website contains an extensive bibliography of works on the ICSID.

155. E. Lauterpacht, foreword in Schreuer, *ICSID Commentary*, *ibid.*, at xi.

156. I.F.I. Shihata, *Towards a Greater Depoliticization of Investment Disputes: The Roles of ICSID and MIGA* (Washington: ICSID, 1993).

157. Report of the Executive Directors of the International Bank for Reconstruction and Development on the Convention of the Settlement of Investment Disputes between States and

Shihata noted in his well-known article, 'Towards a Greater Depoliticization of Investment Disputes,' that the ICSID provides:

A forum for conflict resolution in a framework that carefully balances the interests and requirements of all the parties involved, and attempts in particular to 'depoliticize' the settlement of investment disputes.<sup>158</sup>

The ICSID is not a permanent arbitral tribunal; rather it provides a legal and organizational framework for the arbitration of disputes between Contracting States and investors who qualify as nationals of other Contracting States. The ICSID Convention makes the agreement to arbitrate an investment dispute before the ICSID a treaty obligation. Thus, an arbitration agreement providing for ICSID proceedings engages the state's international responsibility. The ICSID allows investment disputes to be arbitrated without interference from domestic political or judicial organs in the same manner as a dispute between states can be made subject to international adjudication by an international court or tribunal.

Arbitration under the ICSID is subject to four conditions: (1) the parties must have agreed to submit their dispute to dispute settlement under the ICSID; (2) the dispute must be between a Contracting State to the ICSID (or a subdivision or agency of that state) and the national of another Contracting State; (3) the dispute must be a legal dispute; and (4) the dispute must arise directly out of an investment made in the host Contracting State.<sup>159</sup> The ICSID Convention provides that, where the parties have consented to ICSID arbitration, the consent operates to exclude any other forum or remedy.<sup>160</sup> In particular, states may not exercise diplomatic protection once a claim has been submitted to the ICSID, except where there is a failure to comply with an award.<sup>161</sup> In addition, where a state has consented to arbitration, it cannot withdraw consent unilaterally nor, require that there be an exhaustion of local remedies unless this has been made an express condition of its consent to arbitration.<sup>162</sup>

One of the purposes of the ICSID is to 'delocalise' disputes by making ICSID arbitration and awards subject solely to the ICSID Convention, rather than national law. This does not mean that national law is irrelevant to the resolution of disputes under ICSID arbitration.<sup>163</sup> Rather, the substantive law applicable to the investment dispute will largely depend on the relationship between the host state and the investor in question (e.g., the dispute might arise out of a contract,

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Nationals of Other States, 1 ICSID Rep 23 [Report of the Executive Directors on the Convention].

158. I.F.I. Shihata, 'Towards a Greater Depoliticization of Investment Disputes' (1986) 1 ICSID Rev 1. Shihata became the Secretary General of the ICSID in 1983, serving in that role and as General Counsel of the World Bank until 1998.

159. The conditions for the jurisdiction of ICSID are set out in Art. 25(1) of the ICSID Convention. See *supra* note 154 for commentary on the jurisdiction of ICSID tribunals.

160. Art. 26, *ibid.*

161. Art. 27, *ibid.*

162. Art. 25(1) and 26, *ibid.*

163. See *infra* Chapter 2 for a discussion of applicable law in the context of IIAs.

foreign investment code or an IIA).<sup>164</sup> However, the ICSID Convention provisions govern the conduct of the arbitration. Awards made by ICSID tribunals are binding on the parties and can only be annulled by an *ad hoc* committee established under the ICSID Convention.<sup>165</sup> This is designed to prevent national courts from reviewing the merits of ICSID awards.

Another important innovation under the ICSID Convention is the definition of ‘nationals of another Contracting State.’ Under the principles of diplomatic protection in customary international law, states espouse the claims of their nationals.<sup>166</sup> In the foreign investment context, however, local laws may require that a foreign investment be made using a locally incorporated company, which is technically the national of the host state. The ICSID Convention addresses this issue by providing that the host state can agree to treat legal entities created under its jurisdiction as nationals of another party if those entities are under foreign control.<sup>167</sup> As a result, a locally incorporated company controlled by foreign investors can begin ICSID arbitration against the state in which it is incorporated, even though technically the company is not a foreign national.

In 1978, ICSID created an Additional Facility that allows the ICSID Secretariat to administer arbitration proceedings where one of the parties is not a Contracting State to the ICSID Convention or a national of a Contracting State.<sup>168</sup> The Additional Facility allows the ICSID Secretariat to administer arbitrations not otherwise falling within the purview of the ICSID Convention. An important difference between arbitrations under the ICSID Rules and the Additional Facility Rules is that national laws, rather than the ICSID Convention, apply to the enforcement of awards made under the Additional Facility Rules. Article 19 of the Additional Facility Rules provides that arbitration proceedings are to be held only in states that are parties to the New York Convention. Many IIAs now provide for arbitrations under the both the ICSID Arbitration Rules and the Additional Facility Rules.

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164. Art. 42(1), ICSID Convention provides that: ‘The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable.’

165. See Art. 50, *ibid.* On annulment, see *supra* note 154 for commentary, and E. Gaillard & Y. Banifatemi, eds, *Annulment of ICSID Awards*, IAI International Arbitration Series No.1 (New York: Juris Publishing, 2004). If an award is annulled, the claimant may still resubmit the claim. A number of IIA awards have been subject to annulment proceedings, including: *CMS Gas Transmission Company v. Argentina*; *Compañía de Aguas del Aconquija, & Compagnie Générale des Eaux v. Argentina*; *Consortium R.F.C.C. v. Morocco*; *Empresas Lucchetti, S.A. and Lucchetti Peru, S.A. v. Peru*; *Mr. Patrick Mitchell v. Congo*; *MTD Equity Sdn. Bhd. & MTD Chile S.A. v. Chile*; and *Wena Hotels Limited v. Egypt*.

166. See *supra* §1.3 for a discussion of diplomatic protection.

167. Art. 25(1), *supra* note 154.

168. Rules Governing the Additional Facility for the Administration of Proceedings By the Secretariat of the International Centre for Settlement of Investment Disputes. The original rules are published in 1 ICSID Reports 213. The rules were revised effective 1 Jan. 2003.

**§1.22 OECD Convention on the Protection of Foreign Property** In 1962 the OECD released the *Draft Convention on the Protection of Foreign Property*,<sup>169</sup> which was revised and approved by the OECD in 1967 (1967 Draft OECD Convention).<sup>170</sup> Given the membership of the OECD,<sup>171</sup> it is not surprising that the 1967 Draft Convention generally reflects the views of the major capital exporting states on the minimum standard of treatment. The 1967 OECD Council Resolution approving the Draft Convention highlights that it ‘embodies recognised principles relating to the protection of foreign property’ and that it ‘will be a useful document in the preparation of agreements on the protection of foreign investment.’<sup>172</sup> The 1967 Draft OECD Convention sets out the minimum standards of treatment as follows:

Each Party shall at all times ensure fair and equitable treatment to the property of the nationals of the other Parties. It shall accord within its territory the most constant protection and security to such property and shall not in any way impair the management, maintenance, use, enjoyment or disposal thereof by unreasonable or discriminatory measures. The fact that certain nationals of any State are accorded treatment more favourable than that provided for in this Convention shall not be regarded as discriminatory against nationals of a Party by reason only of the fact that such treatment is not accorded to the latter.<sup>173</sup>

With respect to compensation for expropriation, the 1967 Draft OECD Convention reflects the Hull Rule requirement for prompt, adequate and effective compensation. Taking of property is to be:

... accompanied by provision for the payment of just compensation. Such compensation shall represent the genuine value of the property affected, shall be paid without undue delay, and shall be transferable to the extent necessary to make it effective for the national entitled thereto.<sup>174</sup>

Although the 1967 Draft OECD Convention failed to gain sufficient support among OECD countries for adoption as a multilateral convention,<sup>175</sup> its substantive provisions have served as an important model for bilateral investment treaties (BITs).<sup>176</sup> It should be noted that the 1967 Draft OECD Convention, although

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169. (1963) 2 ILM 241.

170. (1968) 7 ILM 117.

171. *Supra* note 137.

172. Resolution of the OECD Council, 12 Oct. 1967, (1968) 7 ILM 117.

173. Art. 1(a), *ibid.*, at 119. See *infra* Chapter 6, §6.4 *et seq.*, on the development of the minimum standard of treatment.

174. Art. 3, *ibid.*

175. This was due, in part, to the reluctance of some less developed members, including Greece, Portugal and Turkey, to be bound by the provisions. See, UNCTC, *Bilateral Investment Treaties* (New York: United Nations, 1988) (Doc. No. ST/CTC/65) at 7.

176. R. Dolzer & M. Stevens, *Bilateral Investment Treaties* (The Hague: Martinus Nijhoff Publishers, 1995) at 2.

setting out a mechanism for investor-state arbitration, conditions arbitration on a separate declaration of consent to arbitral jurisdiction by the state.<sup>177</sup>

**§1.23 Charter of Economic Rights and Duties of States** Throughout the late 1960s and 1970s, developing states sought to reconstruct the legal framework for international economic relations. In the UN, these efforts culminated in a series of General Assembly resolutions, including the 1974 *Declaration on the Establishment of a New International Economic Order* (NIEO Declaration) and the 1974 *Charter of Economic Rights and Duties of States* (Charter).<sup>178</sup> The NIEO Declaration asserts that the international economic system, including neo-colonialism and the inequitable distribution of income, are obstacles to developing states. While reaffirming the principle of permanent sovereignty over resources and economic activities, it sets out principles for a new system of economic relations, including such items as: terms of trade for raw materials and primary commodities; the reform of the international monetary system; the financing of development; the transfer of technology; and the regulation of transnational corporations.

The Charter elaborates on the principles in the NIEO Declaration and contains specific measures concerning foreign investment.<sup>179</sup> It affirms the right

177. See Art. 7, 1967 Draft OECD Convention, *supra* note 170.

178. 'General Assembly Resolution on Permanent Sovereignty over Natural Resources', GA Res 3171, 17 Dec. 1973, (1974) 13 ILM 238; 'Declaration on the Establishment of a New International Economic Order', GA Res 3201, 1 May 1974, (1974) 13 ILM 715; 'Charter of Economic Rights and Duties of States', GA Res 3281, 12 Dec. 1974, (1975) 14 ILM 251. For commentary, see M. Bedjaoui, *Towards a New International Economic Order* (New York: Holmes & Meier, 1979); I. Brownlie, 'Legal Status of Natural Resources In International Law (Some Aspects)' (1979) 162 RDCADI 245 [Brownlie, 'Legal Status of Natural Resources'] and N. Schrijver, *Sovereignty Over Natural Resources: Balancing Rights and Duties* (Cambridge: Cambridge University Press, 1997). See *supra* §1.20 on the 1962 Resolution 1803.

179. Section 2.2 of the Charter provides:

1. Every State has and shall freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities.
2. Each State has the right:
  - a. To regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities. No State shall be compelled to grant preferential treatment to foreign investment;
  - b. To regulate and supervise the activities of transnational corporations within its national jurisdiction and take measures to ensure that such activities comply with its laws, rules and regulations and conform with its economic and social policies. Transnational corporations shall not intervene in the internal affairs of a host State. Every State should, with full regard for its sovereign rights, co-operate with other States in the exercise of the right set forth in this subparagraph;
  - c. To nationalize, expropriate or transfer ownership of foreign property in which case appropriate compensation should be paid by the State adopting such measures, taking into account its relevant laws and regulations and all circumstances that the State considers pertinent. In any case where the questions of compensation give rise to a controversy, it shall be settled under the domestic law of the nationalizing State and by its tribunals, unless it is freely and mutually agreed by all States concerned that other

of states to regulate foreign investment within their jurisdictions and provides that no state can be compelled to grant 'preferential treatment' to foreign investment.<sup>180</sup> The Charter also states that transnational corporations are not to intervene in the internal affairs of states and affirms the right of states to regulate transnational corporations. Simultaneously, the Charter encourages states to co-operate in regulating the activities of transnational corporations.<sup>181</sup> In contrast to the 1962 General Assembly Resolution 1803 on Permanent Sovereignty over National Resources, which recognized that there is an international law standard of compensation for expropriation ('appropriate compensation'),<sup>182</sup> the Charter provides that compensation for expropriation is to be determined in accordance with national laws and omits any reference to international law or a minimum international standard in determining compensation.<sup>183</sup>

The Charter, like the NIEO Declaration, was an assertion of national sovereignty by developing states. Although the Charter was adopted by an overwhelming majority as a result of the numerical preponderance of developing states in the General Assembly, most developed states either voted against its adoption or abstained from voting.<sup>184</sup> In his influential arbitral award, *Texaco Overseas Petroleum Co. (TOPCO) and Californian Asiatic Oil Co. v. Libya*,<sup>185</sup> René-Jean Dupuy observed that although the 1962 Resolution 1803 on Permanent Sovereignty over Natural Resources was assented to 'by a great many states representing not only all geographic areas but also all economic systems,'<sup>186</sup> the NIEO resolutions – 3171, 3201 and 3281<sup>187</sup> – were supported 'by a majority of states but not any of the developed countries with market economies which carry on the largest part of international trade.'<sup>188</sup>

Although the Charter and NIEO Declaration were strong political and programmatic statements, as General Assembly resolutions, they have no binding force and did not purport to be restatements of existing law. Further, they had little long-term impact on state practice relating to foreign investment protection.

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peaceful means be sought on the basis of the sovereign equality of States and in accordance with the principle of free choice of means.

180. Subparagraph (a) was approved by 113 states and opposed by ten. Four states abstained from voting. See (1975) 14 ILM 251 at 264.
181. Subparagraph (b) was approved by 119 states and opposed by four. Six states abstained from voting. *Ibid.*
182. See *supra* §1.20.
183. Subparagraph (c) was approved by 104 states and opposed by sixteen. Six states abstained from voting. *Ibid.*
184. The Charter was adopted by a vote of 120 in favour to six against with ten abstentions. *Supra* note 180 at 251. Belgium, Denmark, Federal Republic of Germany, Luxembourg, UK and US voted against the Charter. Austria, Canada, France, Ireland, Israel, Italy, Japan, The Netherlands, Norway and Spain abstained from voting.
185. *Texaco Overseas Petroleum Co. (TOPCO) and Californian Asiatic Oil Co. v. Libya* (1977) 104 JDI 350 (French original), (1979) 53 ILR 389 (English translation).
186. *Ibid.*, 53 ILR at 487, para. 84.
187. *Supra* note 178.
188. *Supra* note 185, 53 ILR at 491, para. 86.

During the following decades, developing states entered into IIAs to promote and protect investments on terms that departed significantly from the principles reflected in the Charter and the NIEO Declaration.<sup>189</sup>

**§1.24 Draft UN Code of Conduct on Transnational Corporations** One of the clear objectives of the NIEO Declaration and the Charter was more stringent regulation of multinational enterprises.<sup>190</sup> In 1974, the UN Economic and Social Council established the Commission on Transnational Corporations, the primary purpose of which was to draft a Code of Conduct on Transnational Corporations (TNC Code of Conduct).<sup>191</sup> From the earliest discussions, disagreement emerged between capital exporting and importing states as to whether the Code would only apply to the conduct of transnational corporations or whether it would extend also to the treatment of TNCs by host states. In 1980, the Economic and Social Council decided the Code would address both issues.<sup>192</sup> For the next ten years the drafting of the Code's substantive provisions was characterized by continued disagreements over its content, inclusion of references to the minimum standard of treatment and compensation for expropriation, and its legal status.<sup>193</sup> Negotiations were suspended in 1992.<sup>194</sup>

**§1.25 OECD Declaration on International Investment and Multinational Enterprises** The 1976 *OECD Declaration on International Investment and Multinational Enterprises* (OECD Declaration)<sup>195</sup> was a response by OECD member states to the NIEO Declaration and Charter and the draft TNC Code of Conduct.<sup>196</sup> The OECD Declaration highlights the importance of international investment to economic development, commits the OECD states to national treatment of foreign enterprises,<sup>197</sup> and includes the *OECD Guidelines on Multinational Enterprises* (the Guidelines). In the OECD Declaration, the OECD

189. T. Wälde, 'A Requiem for the "New International Economic Order": The Rise and Fall in International Economic Law and a Post-Mortem with Timeless Significance,' in G.L.G. Hafner *et al.*, eds, *Liber Amicorum Professor Siedl-Hohenfeldern*, (The Hague: Kluwer Law International, 1998) 771.

190. *Supra* note 178.

191. See P. Muchlinski, *Multinational Enterprises and the Law*, 2nd edn (Oxford: Oxford University Press, 2007) [Muchlinski (2007)] at 660 and W. Spröte, 'Negotiations on a United Nations Code of Conduct for Transnational Corporations' (1990) 33 GYIL 331.

192. See P. Muchlinski, *Multinational Enterprises and the Law* (Cambridge, Mass: Blackwell Publishers, 1995) [Muchlinski (1995)] at 593.

193. The draft code is available in (1984) 23 ILM 626.

194. Muchlinski (1995), *supra* note 192 at 661. The last draft of the text of the code is dated 31 May 1990. In addition to the draft code, in 1977 the International Labour Organization adopted the *Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy* setting out principles with respect to employment, training, conditions of work and life and industrial relations (1978) 17 ILM 422. See Muchlinski (1995), *ibid.*, at 473-506.

195. The *OECD Declaration and Decisions on International Investment and Multinational Enterprises*, DAF/IME(2000)20, available on the OECD website.

196. Muchlinski (2007), *supra* note 191 at 658.

197. See *infra* Chapter 4, §4.6 *et seq.*, with respect to the OECD National Treatment Instrument.

states recommend that multinational enterprises operating in or from their territories observe the Guidelines. The Guidelines provide voluntary principles and standards for responsible business conduct and encourage 'the positive contributions which multinational enterprises can make towards economic and social progress.'<sup>198</sup> The Guidelines set out standards for multinational enterprises in areas including disclosure, employment, environment, corruption, consumers, science and technology, competition and taxation. The Guidelines affirm that states have the right to regulate multinational corporations, subject to international law standards, although they do not elaborate on the content of those standards.<sup>199</sup>

**§1.26 Lump sum agreements and national claims commissions** A lump sum agreement is a settlement agreement whereby claimant and respondent states agree to settle claims through lump sum compensation. The claimant state then distributes the lump sum settlement amongst its nationals who have made claims, typically by establishing special domestic tribunals or claims commissions to adjudicate the merits of its nationals' claims.<sup>200</sup> In the past sixty years, states have concluded more than 200 lump sum agreements,<sup>201</sup> making them the primary method for settling international claims concerning the treatment of nationals and their property.<sup>202</sup> Lump sum agreements have been popular because they provide for a final settlement of claims between states and thus resolve the diplomatic, political and economic frictions caused by outstanding claims, while at the same time allowing states to avoid binding dispute settlement mechanisms and adjudication of the merits of any particular claim.

Despite the extensive practice involving lump sum agreements, there is a division of opinion on the jurisprudential significance of lump sum agreements.<sup>203</sup> Do lump sum agreements simply reflect negotiated resolutions of claims motivated by extra-legal considerations, or do they represent a source of customary

198. Para. 2. The original guidelines are reproduced at (1976) 15 ILM 967. The Guidelines have been reviewed four times since 1976 and were last updated in 2000. See OECD, *The OECD Guidelines for Multinational Enterprises: Text, Commentary and Clarification*, 31 Oct. 2001, DAF/IME/WPG(2000)15/FINAL.

199. Para. 8 of the Guidelines provides: 'Governments adhering to the Guidelines set them forth with the understanding that they will fulfil their responsibilities to treat enterprises equitably and in accordance with international law and with their contractual obligations.'

200. The US has been a predominant practitioner in this area. The United States Foreign Claims Settlement Commission and predecessor US agencies have adjudicated more than 660,000 claims under forty-three claims programs. See online: <<http://usdoj.gov/fcsc>>.

201. See R.B. Lillich, 'Lump Sum Agreements' in *Encyclopedia, supra* note 8, Vol. III at 268.

202. D.J. Bederman, *Lump Sum Agreements and Diplomatic Protection*, Report for the International Law Association Committee on Diplomatic Protection of Persons and Property, 70th Conference, New Delhi 2002.

203. See R.B. Lillich & B. H. Weston, *International Claims: Their Settlement by Lump Sum Agreements* (Charlottesville: University Press of Virginia, 1975); R.B. Lillich & B.H. Weston, *International Claims: Contemporary European Practice* (Charlottesville, VA: University Press of Virginia, 1982); B. H. Weston, R.B. Lillich & D.J. Bederman, *International Claims: Their Settlement by Lump Sum Agreements, 1975-1995* (New York: Transnational Publishers, 1999); and D.J. Bederman, *Lump Sum Agreements and Diplomatic Protection, ibid.*

international law reflecting legal determinations of claims? With respect to the admissibility of claims and claims involving state responsibility, there has been significant uniformity between the practices under lump sum agreements, the results of claims commissions and customary international law. Thus, although lump sum agreements are clearly influenced by extra-legal considerations, the international law relating to diplomatic protection and state responsibility has had a significant impact on the agreements and claims commission practice.<sup>204</sup>

One of the most controversial issues regarding lump sum agreements is the jurisprudential significance of the standard of compensation for expropriation. On the one hand, since most lump sum agreements provide for less than full compensation for large scale nationalizations, some international publicists argue that state practice supports the position that only partial compensation is required for large scale nationalizations.<sup>205</sup> On the other hand, others argue that it is difficult to generalize about the standard of compensation because different views on the amount of compensation for an expropriation may simply reflect different views of the merits of specific claims.<sup>206</sup> Further, settlements are often driven by political objectives and may not reflect general rules on standards of compensation.

**§1.27 Investment disputes before the International Court of Justice** Despite the intense conflict over the past sixty years regarding the standards that apply to foreign investment under customary international law, the International Court of Justice (ICJ) has played a minimal role in resolving foreign investment disputes and in the development of jurisprudence on substantive standards of foreign investment protection. Since the Court's creation in 1945, only six foreign investment related cases have been brought before it.<sup>207</sup> In three of these cases the ICJ held that it did not have jurisdiction to deal with the complaint, while the fourth

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204. See R.J. Bettauer, 'International Claims: Their Settlement by Lump Sum Agreements, 1975-1995. (Review)' (2000) 94 AJIL 810. In his ILA report, *supra* note 202, Professor Bederman puts the position as follows: 'The jurisprudential significance of lump sum settlement lies not in their discount of the face value of claims, but, rather, in the substantive rules they articulate for such matters as claimant eligibility, attribution of State conduct, the nature of compensable claims, and the general standard and modalities of prompt, adequate and affective compensation.'

205. See discussion in Professor Bederman's ILA Report, *ibid.*

206. *Ibid.*

207. As of 1 Jun. 2008.

was denied on the merits. The fifth (*Ahmadou Sadio Diallo*)<sup>208</sup> and sixth (*Pulp Mills on the River Uruguay*)<sup>209</sup> claims are currently before the Court.

The first investment dispute before the ICJ was the 1952 *Anglo-Iranian Co. Case*,<sup>210</sup> which arose out of Iran's nationalization of its oil industry in 1951. The Court held that it lacked jurisdiction because Iran's 1930 declaration accepting the jurisdiction of the Court did not apply to treaties made prior to the declaration. The second dispute, the *Case of Certain Norwegian Loans*,<sup>211</sup> involved a claim by France that Norway had breached its obligations under a series of state bonds. Here the Court also held that it did not have jurisdiction based on the scope of Norway's declaration accepting the jurisdiction of the Court.

The *Barcelona Traction* case (1970)<sup>212</sup> was also one where the ICJ ultimately determined it did not have jurisdiction, but it remains both a controversial and important decision respecting international investment law. Belgium alleged that the acts and omissions of the Spanish courts in placing Barcelona Traction into bankruptcy constituted a denial of justice and an expropriation of the Barcelona Traction shares held by Belgian nationals. Spain objected to the ICJ's jurisdiction on the basis that Barcelona Traction was incorporated in Canada and that Belgium was not entitled to exercise diplomatic protection on behalf of a Canadian company, even if owned by Belgian shareholders. In a much criticized judgment,<sup>213</sup> a majority of the

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208. *Ahmadou Sadio Diallo (Republic of Guinea v. Democratic Republic of the Congo)*. The case arose out of the 1995 expulsion of Mr. Diallo from Zaire (the predecessor to the Democratic Republic of the Congo (DRC)). Mr. Diallo was the shareholder in several companies doing business in the DRC and incorporated in the DRC. In its Judgment on Preliminary Objections of 24 May 2007, the ICJ held that Guinea could not exercise diplomatic protection 'by substitution' on behalf of two private limited liability companies created under DRC law but held that Guinea had standing to bring a claim on behalf of Mr. Diallo as an individual and as majority shareholder (para. 65). At para. 61, the Court affirmed that: 'only the State of nationality may exercise diplomatic protection on behalf of the company when its rights are injured by a wrongful act of another State. In determining whether a company possesses independent and distinct legal personality, international law looks to the rules of the relevant domestic law.'
209. In *Pulp Mills on the River Uruguay (Argentina v. Uruguay)*, Argentina has brought a claim against Uruguay alleging that the government of Uruguay unilaterally authorized the construction of two pulp mills along the River Uruguay, without the compulsory notification and consultation required under the Statute of the River Uruguay signed by both states in 1975. Argentina claims that the mills would have a deleterious effect on the biodiversity of the river and constitute a health hazard to the residents of the area. The pulp mills are to be built by two different foreign investors.
210. *Anglo-Iranian Oil Co. Case (UK v. Iran)*, [1952] ICJ Rep 93.
211. *Case of Certain Norwegian Loans (France v. Norway)*, [1957] ICJ Rep 9.
212. *Supra* note 25. For a fascinating discussion of the political and legal context of the case, see J. Brooks, 'Annals of Finance – Privateer' *The New Yorker*, 21 and 28 May 1979. Also see F.A. Mann, 'Protection of Shareholders' Interests in the Light of the Barcelona Traction Case' in F.A. Mann, *Further Studies in International Law* (Oxford: Clarendon Press, 1990) at 217.
213. See F.A. Mann, 'The Protection of Shareholders' Interests in Light of the Barcelona Traction Case' (1973) 67 AJIL 259; R.B. Lillich, 'Two Perspectives on the Barcelona Traction Case: The Rigidity of Barcelona' (1971) 65 AJIL 522; R. Higgins, 'Aspects of the Case Concerning

Court held that ‘where it is a question of an unlawful act committed against a company representing foreign capital, the general rule of international law authorizes the national State of the company alone to make a claim.’<sup>214</sup> As a result, Canada, not Belgium, was the proper party to bring a claim before the Court. This, however, was not possible as the Court did not have jurisdiction for disputes between Canada and Spain. In determining that it did not have jurisdiction, the Court highlighted that there had been an ‘intense conflict of systems and interests’<sup>215</sup> concerning the protection of foreign investment and that states ‘ever more frequently’<sup>216</sup> were providing foreign investment protection through bilateral and multilateral agreements. It noted that no such instrument was in force between Belgium and Spain.<sup>217</sup> By making these statements the ICJ signalled that progressive developments in international investment law would mainly be treaty-based.

The only case involving foreign investment that the ICJ has addressed on the merits to date is the *Elettronica Sicula S.p.A. (ELSI)* case (1982).<sup>218</sup> This case was brought under the 1948 Italy-US *Treaty of Friendship, Commerce and Navigation* (FCN), which provided for ICJ jurisdiction for disputes arising under the treaty.<sup>219</sup> Elettronica Sicula S.p.A. (ELSI) produced electronic components in Italy and was a subsidiary of two American corporations. ELSI’s board of directors decided to shut down operations and liquidate ELSI to minimize ongoing losses. In order to protect employment, the local mayor issued a requisition order under which the town took temporary control of ELSI’s factory. ELSI appealed this order and subsequently made a bankruptcy petition. The requisition order was later annulled by the Italian courts and the trustee in bankruptcy brought a suit for damages, arguing that the requisition order had caused the bankruptcy. In the case before the ICJ, the US claimed that the requisition, and the delay in overturning it, interfered with the American corporations’ management and control of ELSI, as well as their interests in it, and causing the bankruptcy. The ICJ, however, found that

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the Barcelona Traction, Light and Power Company, Ltd.’ (1970) 11 VJIL 327; F. Orrego Vicuña, ‘Changing Approaches to the Nationality of Claims in the Context of Diplomatic Protection and International Dispute Settlement’ (2000) 15 ICSID Rev 340; and Orrego Vicuña, *The Changing Law of Nationality of Claims*, *supra* note 23.

214. *Supra* note 25 at para. 88.

215. *Ibid.*, at para. 89.

216. *Ibid.*, at para. 90.

217. *Ibid.*

218. *Supra* note 128. The decision was made by a Chamber of the ICJ consisting of Judges Ruda, Oda, Ago, Schwebel and Jennings. For commentary on the case see: F.A. Mann, ‘Foreign Investment in the International Court of Justice: The *ELSI* Case’ (1992) 86 AJIL 92; S.D. Murphy, ‘The *ELSI* Case: An Investment Dispute at the International Court of Justice’ (1991) 16 YJIL 391 and K.J. Hamrock, ‘The *ELSI* Case: Toward an International Definition of ‘Arbitrary Conduct’, (1992) TILJ 837.

219. The factory was owned by ELSI, an Italian company, which was in turn wholly owned by two US corporations. The US claimed that Italy had breached the 1948 Italy-US FCN Treaty, a 1951 Supplementary Agreement to the FCN Treaty and customary international law. Art. I of the Supplementary Agreement provided protection against ‘arbitrary or discriminatory measures ... resulting particularly in: (a) preventing ... effective control and management of enterprises ... or, (b) impairing ... other legally acquired rights and interests ...’.

ELSI's bankruptcy was caused not by the requisition order, but rather by the company's precarious financial situation. The Court denied the US's claim that Italy's actions were covered by the FCN Treaty as the mayor's order did not cause or trigger the bankruptcy. It also denied the US's claim that ELSI's shareholders were deprived of their rights to dispose of property, holding that the mayor's action was not the cause of the property loss.<sup>220</sup> Of particular importance with respect to the minimum standard of treatment, the Court addressed the meaning of 'arbitrariness' in international law.<sup>221</sup>

The majority judgment in *ELSI* largely avoided the issue of whether the US was entitled to bring the claim under the FCN Treaty and proceeded on the basis that the property protected under the treaty was not ELSI's plant and equipment (its property), but ELSI itself (the company).<sup>222</sup> In his Separate Opinion, Judge Oda addressed the treaty rights afforded to US nationals with respect to shareholdings in Italian companies. In his view, the treaty did not augment the rights of shareholders and the US shareholders of ELSI could only claim those rights guaranteed to them as shareholders under Italian law.<sup>223</sup> In contrast, in his Dissenting Opinion, Judge Schwebel stated that the treaty protected shareholders' rights. In his view, the treaty's guarantees with respect to the organization, control and management of corporations protected the US shareholders' interests in ELSI.<sup>224</sup>

In its jurisprudence the ICJ has addressed few of the controversial legal issues relating to foreign investment, such as the responsibility of states to foreign investors under customary international law and the standard of compensation for the expropriation of foreign investment. The *Barcelona Traction* and *ELSI* cases, however, highlighted some of the procedural and substantive inadequacies with the diplomatic protection model in safeguarding shareholder interests. These uncertainties and inadequacies may have provided compelling rationales for the development of IIAs. The *Barcelona Traction* case demonstrated

220. See Hamrock, 'The *ELSI* Case: Toward an International Definition of 'Arbitrary Conduct' *supra* note 218 for a discussion of the case.

221. See *infra* Chapter 6, §6.9.

222. *Supra* note 128 at 64, para. 106. The issue of shareholder's rights in *ELSI* is discussed in V. Lowe, 'Shareholders' Rights to Control and Manage: From *Barcelona Traction* to *ELSI*,' in N. Ando, E. McWhinney & R. Wolfrum, eds, *Liber Amicorum Judge Shigeru Oda* (The Hague: Kluwer Law International, 2002).

223. *Supra* note 128 at 87-88.

224. Judge Schwebel noted: 'it was maintained that the Treaty was essentially irrelevant to the claims of the United States in this case, since the measures taken by Italy (notably, the requisition of ELSI's plant and equipment) directly affected not nationals or corporations of the United States but an Italian corporation, ELSI, whose shares happened to be owned by United States corporations whose rights as shareholders were largely outside the scope of the protection afforded by the Treaty. The Chamber did not accept this argument. Nor did it accept the contention that the right to organize, control and manage a corporation was limited to the founding of a Company and the election of its directors and did not include its continuing management; nor that the right to control and manage was unaffected by the requisition of that corporation's plant and equipment.' *Supra* note 128 at 94-95. See also *ibid.*, at 100: 'the foreign investor shall enjoy the benefits of the Treaty and its Supplement, whether he invests in a corporation of his or the other party's nationality.'

that, depending on the place of incorporation of the investment vehicle, a home state may be unable to espouse the claims of its nationals. In addition, the Court signalled that clarification of the law in the area of foreign investment would need to be treaty-based given the intense conflict in the area. The opposing opinions of Judges Oda and Schwebel in *ELSI* highlighted the need for IIAs to address the extent to which investors holding shares in a corporation incorporated in a host state are entitled to claim for breaches of an IIA where the state measures in question are directed at the locally incorporated company. Finally, both *Barcelona Traction* and *ELSI* demonstrated that the diplomatic protection model was slow and cumbersome.<sup>225</sup>

**§1.28 Iran-US Claims Tribunal** The Iran-United States Claims Tribunal was established in 1981 to address claims by US and Iranian nationals arising out of the 1979 Iranian revolution.<sup>226</sup> This tribunal was the first international tribunal since WWII to consider a large number of investment claims. Its decisions have contributed substantially to international jurisprudence on state responsibility for injuries to foreigners.<sup>227</sup> Not surprisingly, the tribunal's jurisprudence has been cited extensively by investment treaty tribunals.<sup>228</sup>

**§1.29 Foreign investment insurance** Foreign investment insurance developed in the post-WWII era to provide foreign investors a mechanism to manage the inherent political risks of investing abroad.<sup>229</sup> National agencies were established by many capital exporting states to provide foreign investment insurance against political risks, including expropriation, restrictions on transfer of funds and political

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225. The events giving rise to *Barcelona Traction* occurred between 1948 and 1952. Belgium's first ICJ application was filed in 1958. The final court judgment was delivered in 1970. The events giving rise to *ELSI* began in 1968. The US application to the ICJ was made in 1987 and the Chamber of the ICJ formed to deal with the case delivered its judgment in 1989.

226. The tribunal was established under the Claims Settlement Declaration, 19 Jan. 1981 (1981) 1 Iran-US CTR 9. See generally G.H. Aldrich, *The Jurisprudence of the Iran-United States Claims Tribunal* (Oxford: Clarendon Press, 1996); C.N. Brower & J.D. Brueschke, *The Iran-United States Claims Tribunal* (The Hague: Martinus Nijhoff Publishers, 1998); D. Caron & J. Crook, *The Iran-United States Claims Tribunal and the Process of International Claims Resolution: A Study by the Panel on State Responsibility of the American Society of International Law* (Ardsley, New York: Transnational, 2000) and C. Gibson & C. Drahozal, *The Iran-U.S. Claims Tribunal at 25: The Cases Everyone Needs to Know for Investor-State and International Arbitration* (Oxford: Oxford University Press, 2007).

227. As of 11 Jul. 2007, the tribunal had made final awards, decisions or orders in 3,936 cases. See Office of the Secretary-General of the Iran-United States Claims Tribunal, Communiqué, 25 Apr. 2008, No. 08/2.

228. See C. Gibson & C. Drahozal, 'Iran-United States Claims Tribunal Precedent in Investor-State Arbitration' (2006) 23 JIA 521.

229. See generally Chapter 3, 'Investment Insurance', in Rubins & Kinsella, *supra* note 5. Most private and public foreign investment insurers are members of the International Union of Credit & Investment Insurers (Berne Union). See online: <<http://berneunion.org.uk>>.

violence.<sup>230</sup> In 1985, the *Multilateral Investment Guarantee Agency* (MIGA) was created under the auspices of the World Bank to encourage foreign direct investment (FDI) flows between Member States and less developed countries by providing foreign investment insurance, technical assistance and policy advice.<sup>231</sup>

Foreign investment insurance mechanisms interact with investment treaty law in three important ways. First, in deciding whether to offer investment guarantees, insurers will look to whether a state has signed an IIA. In some cases, the existence of an IIA may be a precondition for providing political risk insurance.<sup>232</sup> For example, MIGA's Operational Regulations provide that, in considering the investment conditions of a host state for the purposes of assessing risks, an 'investment will be regarded as having adequate legal protection if it is protected under the terms of a bilateral investment treaty between the Host Country and the Home Country of the investor.'<sup>233</sup> Second, IIAs often provide for subrogation in investment treaty claims, thereby allowing the insurer who has paid a claim under a foreign investment policy to take up an investor's treaty claim.<sup>234</sup> Third, foreign investment insurance regularly covers risks such as expropriation and restrictions on transfers. A claims determination concerning foreign investment insurance, although based on the terms of a specific insurance contract, may address questions of state responsibility, such as attribution of responsibility or the types of conduct amounting to expropriation in international law.<sup>235</sup> Although foreign investment claim

230. As of 1992, the US, German and Japanese state agencies accounted for over 80% of national political risk insurance. See M.D. Rowat, 'Multilateral Approaches to Improving the Investment Climate of Developing Countries: The Cases of ICSID and MIGA' (1992) 22 HILJ 103 at 119 as quoted by Rubins & Kinsella, *supra* note 5 at 70. The US government's program is run by the Overseas Private Insurance Corporation (OPIC). Japan's insurer is Nippon Export and Investment Insurance (NEXI). In Germany, foreign investment insurance was formally provided through Treuarbeit. In early 2003, the German Government appointed a consortium formed by PricewaterhouseCoopers and Euler Hermes to manage its investment guarantee scheme. See Rubins & Kinsella, *ibid.*, at 94.

231. *Convention Establishing the Multilateral Investment Guarantee Agency* (1985) 24 ILM 1605 [MIGA Convention]. As of 28 Apr. 2008, MIGA had 172 members. Online: <miga.org>. For commentary, see P. Chatterjee, 'The Convention Establishing the Multilateral Investment Guarantee Scheme' (1987) 36 ICLQ 76 and I.F.I. Shihata, *MIGA and Foreign Investment: Origins, Operations, Policies, and Basic Documents of the Multilateral Investment Guarantee Agency* (Dordrecht: Martinus Nijhoff Publishers, 1988).

232. See UNCTAD, *supra* note 175 at 4.

233. Para. 3.16, MIGA, Operational Regulations, as amended by the Board of Directors through 27 Aug. 2002.

234. Subrogation agreements may also appear in separate agreements. For example, the US has investment guarantee agreements with a number of states that provide the right of OPIC to make a claim against the state where it has paid out on a political risk insurance policy. For example, see US-Poland Investment Guaranty Agreement, dated 13 Oct. 1989, TIAS 12039. In addition, MIGA is empowered to enter into investment guarantee agreements with states. See Art. 23(b)(ii), MIGA Convention, *supra* note 231.

235. For example, V.R. Koven, 'Expropriation and the "Jurisprudence" of OPIC' (1981) 22 HILJ 269. OPIC publishes its Memoranda of Determinations on its website.

determinations are based on contractual obligations, IIA tribunals have referred to claims determinations for guidance on legal issues arising under IIAs.<sup>236</sup>

### III INTERNATIONAL INVESTMENT AGREEMENTS

**§1.30 The origins of international investment agreements**<sup>237</sup> The development of IIAs was primarily a response to the uncertainties and inadequacies of the customary international law of state responsibility for injuries to aliens and their property.<sup>238</sup> In addition, capital exporting states sought to obtain better market access commitments from capital importing states for investors and investment, and to obtain progressive development in the standards of investment protection. As already noted, although there were early efforts to create an international framework for foreign investment, disagreement between capital exporting and importing states about standards of treatment for foreign investors derailed the conclusion of a multilateral treaty. As a result, capital exporting states began concluding BITs dedicated to foreign investment promotion and protection.<sup>239</sup>

Prior to the development of the investment-focused BITs, treaty-based investment protection was available under some general economic treaties. As discussed above, after WWII numerous states, including the US and the UK, entered into FCN treaties that focused on the protection of property rights and the business interests of foreigners.<sup>240</sup> For example, the 1956 *Treaty of Friendship, Commerce and Navigation* between Nicaragua and the US, although not formally called a BIT, essentially served the same function – the treaty’s preamble highlights the contribution to be made by ‘mutually beneficial investments’ between the two states. Indeed, the 1956 Nicaragua-US FCN Treaty might be considered as providing

236. For example, several IIA tribunals, in discussing the meaning of expropriation in international law, have referred to the determination made in the arbitration *In the Matter of Revere Copper and Brass, Inc. and Overseas Private Investment Corporation* (Award, 24 Aug. 1978) 17 ILM 1321 and 56 ILR 258.

237. For a bibliography of articles on books on BITs current to 1996, see the ICSID website. An earlier version of this bibliography is available in (1992) 7 ICSID Rev 497.

238. See UNCTC, *supra* note 175 at 1.

239. For an overview of treaty practice, see the following three comprehensive studies: UNCTC, *ibid.*; UNCTAD, *Bilateral Investment Treaties in the Mid-1990s* (New York and Geneva: United Nations, 1998) (Doc. No. UNCTAD/ITE/IIT/7) and UNCTAD, *Bilateral Investment Treaties 1995-2006* (New York and Geneva: United Nations, 2007) (Doc. No. UNCTAD/ITE/IIT/2006/5). Also see the overview of BIT practice as of 1995 by Dolzer & Stevens, *supra* note 176. For the texts of specific BITs see the compilation of investment treaties in ICSID, *Investment Promotion and Protection Treaties*, looseleaf (Dobbs Ferry, New York: Oceana Publications Inc., 1983) [*Investment Protection Treaties*]. UNCTAD also has two comprehensive online databases on its website: one for BITs and one for other investment instruments.

240. See *infra* §1.17.

more comprehensive substantive standards of investment protection than many of the early European BITs.

Germany is commonly cited as the first state to develop a BIT program and to sign the first BIT, with Pakistan, in 1959.<sup>241</sup> The *Treaty between the Federal Republic of Germany and Pakistan for the Promotion and Protection of Investments* (Germany-Pakistan (1959)) contains many of the substantive provisions that have become common in subsequent BITs. The term investment is defined broadly.<sup>242</sup> The contracting states undertake a general obligation to encourage foreign investment, although the right of admission is determined by national law. The parties are obliged to refrain from discrimination based on the nationality of the investor and there is to be no discrimination against investment activities. Investments are to enjoy protection and security.<sup>243</sup> Provision is made for compensation due in the event of an expropriation and a right of subrogation may be exercised where the investor has been compensated under an insurance arrangement. There are guarantees on the transfer of capital and investment returns, as well as a general guarantee that the state will observe any obligation it has undertaken. Finally, the BIT provides for state-to-state dispute settlement before the ICJ if the parties agree, or if they do not agree, to an arbitration tribunal upon the request of either party.<sup>244</sup> This recourse to state-to-state arbitration before a three person arbitral tribunal, as an alternative to ICJ jurisdiction, represents one of the major differences between early post-WWII agreements such as the Nicaragua-US FCN and the BITs that were developed in the early 1960s.

Germany's efforts to conclude BITs were quickly followed by other capital exporting states: Switzerland in 1961,<sup>245</sup> The Netherlands in 1963,<sup>246</sup> Italy<sup>247</sup> and

241. On the development of German BITs, see J. Alenfeld, *Die Investitionsförderungsverträge der Bundesrepublik Deutschland* (Frankfurt, Antenäum Verlag, 1970) as cited in UNCTC, *supra* note 175 at iii. For a more recent discussion, see J. Karl, 'The Promotion and Protection of German Foreign Investment Abroad' (1996) 11 ICSID Rev 1.

242. A letter dated the same day as the BIT clarifies that the coverage of the BIT applies only to 'investments' that have been specifically approved by government agencies. See documents in *Investment Protection Treaties*, *supra* note 239.

243. Later German BITs included provisions on national treatment and MFN treatment. See Germany-Liberia (1961).

244. Art. 11(2), Germany-Pakistan (1959).

245. The first Swiss BIT was Switzerland-Tunisia (1961). On the Swiss BIT program, see Gattiker, 'Behandlung und Rolle von Auslandsinvestitionen im modernen Völkerrecht' (1981) 27 *Schweizerisches Jahrbuch für internationales Recht* 25; N. Huu-Tru, 'Le Réseau suisse d'accords bilatéraux d'encouragement et de protection des investissements' (1988) 92 *RGDIP* 577; M. Kraft, 'Les accords bilatéraux sur la protection des investissements conclus par la Suisse', in D. Dicke, ed., *Foreign Investment in the Present and a New International Economic Order* (Fribourg: University Press, 1987) at 72 and J. Liebeskind, 'The Legal Framework of Swiss International Trade and Investments, Part I: Promotion' (2006) *JWIT* 331. Part II on Protection is published in the subsequent issue at 469.

246. Netherlands-Tunisia (1963). M. Bos, 'The Protection of Foreign Investments in Dutch Court and Treaty Practice,' in H.F. van Panhuys, W.P. Heere *et al.*, eds, *International Law in The Netherlands* (Alphen aan den Rijn: Sijthoff & Noordhoff; Dobbs Ferry, NY: Oceana Publications, 1978-1980), Vol. 3 at 221.

247. Guinea-Italy (1964).

the Belgo-Luxembourg Economic Union (BLEU)<sup>248</sup> in 1964, Sweden<sup>249</sup> and Denmark<sup>250</sup> in 1965, Norway in 1966,<sup>251</sup> France in 1972,<sup>252</sup> the UK in 1975,<sup>253</sup> Austria in 1976<sup>254</sup> and Japan in 1977.<sup>255</sup> BITs in this period were generally quite short – approximately five to six pages and focused on core protections such as national treatment, MFN treatment, a general minimum standard of treatment, compensation for expropriation and rights to transfer capital and returns. Many of the BITs in this period were based on the 1962 and 1967 OECD Draft Conventions.

A characteristic of BITs during this period was the asymmetrical economic and political relationship that existed between capital exporting and importing states. Although the obligations on the state parties to BITs were formally reciprocal, BITs were developed by capital exporting states to protect the economic interests of their nationals abroad. Until Romania began concluding BITs with developing states in 1978,<sup>256</sup> the Iraq-Kuwait (1964) was the only one that did not fall within the developed-developing state paradigm.<sup>257</sup> It is also noteworthy that several major developing states did not conclude BITs until much later.

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248. BLEU-Tunisia (1964). See W. Van de Voorde, 'Belgian Bilateral Investment Treaties as a Means for Promoting and Protecting Foreign Investment' (1991) 44 *Studia Diplomatica* 87.
249. Côte d'Ivoire-Sweden (1965).
250. Denmark-Madagascar (1965).
251. Madagascar-Norway (1966).
252. France-Tunisia (1972). See P. Juillard, 'Les conventions bilatérales d'investissements conclues par la France' (1979) 106 *JDI* 274; 'Les conventions bilatérales d'investissement conclues par la France avec des pays n'appartenant pas à la zone franc' (1982) 28 *Annuaire Français de Droit International* 760; 'Le réseau français des conventions bilatérales d'investissement: à la recherche d'un droit perdu?' (1987) 13 *Droit et Pratique du Commerce International* 9 and 'La Convention entre la France et la Roumanie sur l'encouragement, la protection et la garantie réciproque des investissements' (1988) 22 *Revue Roumaine d'Etudes Internationales* 211.
253. Egypt-UK (1975). On the UK BIT program, see F.A. Mann, 'British Treaties for the Promotion and Protection of Investments' (1981) 52 *BYIL* 241 and E. Denza & S. Brooks, 'Investment Protection Treaties: United Kingdom Experience' (1987) 36 *ICLQ* 910.
254. Austria-Czechoslovakia (1974). For a description of Austrian BIT practice, see Maschke, 'Investitionsabkommen' (1986) 37 *Österreichische Zeitschrift für öffentliches Recht und Völkerrecht* 201 and H.H. Haschek, 'Austrian Foreign Investments and Investment Protection Agreements', in D. Dicke, ed., *Foreign Investment in the Present and a New International Economic Order*, *supra* note 245 at 3.
255. Egypt-Japan (1977). On Japanese BITs, see Y. Matsui, 'Japan's International Legal Policy for the Protection of Foreign Investment' (1989) 32 *JAIL* 1 and S. Yanase, 'Bilateral Investment Treaties of Japan and Resolution of Disputes with Respect to Foreign Direct Investment', in ICCA Congress Series No. 11 (The Hague: Kluwer, 2003) at 426.
256. Romania concluded a BIT with Pakistan in 1978 and one with Sudan in 1979.
257. The one other exception is the 1970 Agreement on Investment and Free Movement of Arab Capital Among Arab Countries. See discussion in T. Pollan, *Legal Framework for the Admission of FDI* (Utrecht: Eleven International Publishing, 2006) at 146.

China, for example, did not conclude its first BIT until 1982;<sup>258</sup> Brazil<sup>259</sup> and India<sup>260</sup> not until 1994.

**§1.31 The advent of treaty-based investor-state arbitration in BITs** The traditional form of consent to arbitration between a foreign investor and a host state was through an arbitration clause in a contract, such as a natural resource concession or a foreign investment agreement.<sup>261</sup> During discussions of the 1965 ICSID Convention it was recognized that states could consent to arbitrate future disputes by making an offer to arbitrate in a foreign investment code or law, or by means of a treaty. The investor would accept this offer to arbitrate by submitting a claim.<sup>262</sup> Therefore, unlike the typical form of consent to international arbitration through an arbitration clause in a contract, investor-state arbitration under a foreign investment law or IIA can occur where there is no pre-existing formal contractual relationship between the foreign investor and the state. Because the consent to arbitration does not occur in an investment contract or concession, this form of arbitration has been referred to as ‘arbitration without privity.’<sup>263</sup> In this form of arbitration, the claimant’s acceptance of the offer to arbitrate in a foreign investment law or treaty will normally occur upon submission of a request for arbitration.

Until 1968, BITs only provided for state-to-state dispute resolution through the establishment of an arbitral tribunal or submission of the dispute to the ICJ. It appears that the first BIT that expressly incorporates provisions for investor-state arbitration, though with qualifications, is Indonesia-Netherlands (1968).<sup>264</sup>

258. China-Sweden (1982). See note in (1985) 24 ILM 537 on China’s BIT program. For a discussion of early Chinese BIT practice, see L. Shishi, ‘Bilateral Investment Promotion and Protection Agreements: Practice of the People’s Republic of China,’ in *International Law and Development*, eds de Waart *et al.* (Dordrecht: Martinus Nijhoff, 1988) at 163-84 and Mo, ‘Some Aspects of the Australia-China Investment Protection Treaty’ (1991) 25 JWTL 43. See *infra* §1.42 for more recent developments.

259. Brazil-Chile (1994).

260. India-UK (1994). See §1.43 for further discussion.

261. See *supra* §1.18.

262. See Schreuer, *ICSID Commentary*, *supra* note 154 at paras 257-8. The possibility of unilateral state consent to arbitration was specifically contemplated in the Report of the Executive Directors on the Convention (*supra* note 157) noting that the consent of both parties need not be expressed in a single instrument and that a host state ‘might in its investment promotion legislation offer to submit disputes arising out of certain classes of investments to the jurisdiction of the Centre, and the investor might give his consent by accepting the offer in writing.’ (1 ICSID Rep at 28). See also the definition of ‘date of consent’ in ICSID Arbitration Rule 2(3) which highlights that acts of consent may occur at different times.

263. J. Paulsson, ‘Arbitration Without Privity’ (1995) 10 ICSID Rev 232. For an in-depth discussion of the nature of investment treaty arbitration see Douglas, *supra* note 27, and the various texts referenced *supra* note 5.

264. The effect of the ICSID investor-state arbitration clause in this BIT is, however, unclear. Art. 11 of Indonesia-Netherlands (1968) provides that: ‘The Contracting Party in the territory of which a national of the other Contracting Party makes or intends to make an investment, shall assent to any demand on the part of such national and any such national shall comply

In 1969, ICSID published a series of model BIT arbitration clauses for use in BITs.<sup>265</sup>

Chad-Italy (1969) appears to be the first BIT that provides for investor-state arbitration with unqualified state consent.<sup>266</sup> This BIT, rather than Germany-Pakistan (1959), marks the true beginning of modern BIT practice because it combines substantive investment promotion and protection obligations with binding investor-state arbitration to address alleged breaches of those obligations.

The validity of a unilateral arbitration clause ('arbitration without privity') was first upheld in 1985 in *SPP v. Egypt*.<sup>267</sup> In this case, an ICSID tribunal found that

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with any request of the former Contracting Party, to submit, for conciliation or arbitration, to the Centre established by the Convention of Washington of 18 Mar. 1965, any dispute that may arise in connection with the investment'. [Emphasis added.] The effect of the article is unclear. On one hand, it could be viewed as a binding offer to the investor to arbitrate. On the other hand, it could be viewed as a binding obligation on the state to agree to arbitrate if an investment dispute arises. Under this interpretation, if the state fails to assent to a demand to arbitration, this failure could be subject to state-to-state arbitration under Art. 22, which provides that disputes 'shall be submitted' to arbitration. The provision is also unusual because it provides that the investor 'shall comply' with a request for arbitration. It is difficult to see how this provision could be enforced. If the investor failed to consent to arbitration, the host state could proceed with state-to-state arbitration, but it is unclear how a private party's failure to consent to arbitration could be attributable to its home state.

265. See *Model Clauses Relating to the Convention on the Settlement of Investment Disputes Designed for Use in Bilateral Investment Agreements* (Sep. 1969) (1969) 8 ILM 1341.

266. Art. VII, Chad-Italy (1969), provides: 'Tout différend relative aux investissements faisant l'objet du présent Accord, qui pourrait surgir entre l'une des Parties contractantes (ou l'une quelconque des institutions ou organisations relevant de ladite Partie ou contrôlée par ladite Partie) et une personne physique ou morale ayant la nationalité de l'autre Partie, est soumis à la juridiction du Centre International pour le Règlement des Différends Relatifs aux Investissements, conformément à la Convention Internationale de Washington du 18 mars 1965. Toute contestation et tout différend entre les deux Parties contractantes, portant sur l'interprétation ou sur l'application du présent Accord sont réglés par la voie diplomatique.' Also see Art. VII, Côte d'Ivoire-Italy (1969), which provides a slightly different formulation: 'Tout différend concernant les investissements, objet du présent accord, qui s'élèverait entre un Etat contractant (ou n'importe quelle institution ou organisation dépendantes ou contrôlées par le même Etat) et une personne physique ou morale, ayant la nationalité de l'autre Etat, sera réglé par la voie diplomatique. Si un différend ne peut être réglé de cette façon il sera soumis à la juridiction du Centre international pour le règlement des différends relatifs aux investissements, conformément à la Convention internationale de Washington du 18 mars 1965. Toute contestation ou tout différend entre les deux Etats, portant sur l'interprétation ou l'application du présent accord, seront réglés par la voie diplomatique.' Art. X, Belgium-Indonesia (1970), provides consent in very clear language: 'Each Contracting Party hereby irrevocably and anticipatory gives its consent to submit to conciliation and arbitration any dispute relating to a measure contrary to this Agreement, pursuant to the Convention of Washington of 18 March 1965, at the initiative of a national or legal person of the other Contracting Party, who considers himself to have been affected by such a measure. This consent implies renunciation of the requirement that the internal administrative or judicial resorts should be exhausted.'

267. *Southern Pacific Properties (Middle East) Limited v. Egypt* (Decision on Jurisdiction, 27 Nov. 1985) 3 ICSID Rep 112.

Egypt's foreign investment law provided consent for ICSID arbitration and that, as a result of the investor's notification of acceptance,<sup>268</sup> the tribunal had jurisdiction over the dispute. Five years later, in 1990, an arbitral tribunal established under the investor-state arbitration provisions of Sri Lanka-UK (1980) issued the first ICSID award where jurisdiction was based on an arbitration clause in a BIT.<sup>269</sup> Investment treaty arbitration had begun and, in that case, it had proven to be successful for the foreign investor.

**§1.32 BITs – the 1970s and 1980s** States entered into only a small number of BITs through the 1970s – by 1979 states had entered into approximately 100 BITs.<sup>270</sup> As discussed above, the early 1970s were characterized by differences in views among capital exporting and importing states about the standards of treatment for foreign investment, as evidenced by the NIEO Declaration and the *Charter of Economic Rights and Duties of States*. Thus, capital importing states had little interest in, or perceived need for, BITs. Although oil-importing developing states suffered balance-of-payments deficits on current accounts as a result of the combined effect of rising import prices and falling commodity prices,<sup>271</sup> recycled petrodollars in the form of bank loans provided large amounts of capital for most developing states' industrialization and infrastructure programs. As a result, however, developing states' external debt ballooned.<sup>272</sup> By the early 1980s many developing states were unable to service their debt levels and defaulted.<sup>273</sup>

Other major capital exporting states became engaged in negotiating BITs through the 1970s and 1980s.<sup>274</sup> A significant development was the US BIT program.<sup>275</sup> Prior to the 1980s the US had relied on its FCN treaties as its primary

268. The investor had sent a letter to Egyptian authorities expressly accepting ICSID jurisdiction over the dispute. See *ibid.*, at 120.

269. *Asian Agricultural Products Ltd (AAPL) v. Sri Lanka* (Final Award, 27 Jun. 1990).

270. Between 1970 and 1974, thirty-nine BITs were concluded. Between 1975 and 1979, sixty BITs were concluded. The numbers are determined by collating results from both the UNCTAD and ICSID databases.

271. UNCTC, *supra* note 175 at 1.

272. External debt in Latin America quadrupled from USD75 billion in 1975 to USD315 billion in 1983. See Institute of Latin American Studies, *The Debt Crisis in Latin America* (Stockholm: Nalkas Gruppen, 1986) at 69.

273. See J. Amuzegar, 'Dealing with Debt' (1987) 68 *Foreign Pol'y* 140; S. Britain, 'A Very Painful World Adjustment' (1983) 61 *Foreign Aff* 541 and P. Kucynski, 'Latin American Debt' (1982) 61 *Foreign Aff* 344.

274. UNCTC, *supra* note 175 at 7.

275. On the US BIT program, see generally Vandavelde, *United States Investment Treaties*, *supra* note 43. Also see J.E. Pattison, 'The United States-Egypt Bilateral Investment Treaty: A Prototype for Future Negotiation' (1983) 16 *CILQ* 305; P.M. Robin, 'The BIT Won't Bite: The American Bilateral Investment Treaty Program' (1984) 33 *AULR Rev* 931; P.B. Gann, 'The U.S. Bilateral Investment Treaty Program' (1985) 21 *SJIL* 373; S. Gudgeon, 'US Bilateral Investment Treaties: Comments on Their Origins, Purposes and General Treatment Standards' (1986) 4 *ITBL* 111; K.J. Vandavelde, 'The Bilateral Investment Treaty Program of the United States' (1988) 21 *CILQ* 201; K.J. Vandavelde, 'U.S. Bilateral Investment Treaties: The Second Wave' (1993) 14 *MJIL* 621; K.J. Vandavelde, 'Of Politics and Markets:

means of investment protection.<sup>276</sup> In the 1970s, the US business community began lobbying the US government to conclude BITs as a means to provide to US investors protections similar to those available to investors from other capital exporting states.<sup>277</sup> The US government began its BIT program in 1977.<sup>278</sup> The primary purpose of the US program was to create a legal framework with high standards of investment protection. A secondary purpose was to depoliticize investment disputes.<sup>279</sup> The US BIT program, however, was not expressly designed to promote foreign investment, since US labour organizations generally opposed promoting outward investment flows.<sup>280</sup> Nevertheless, from the beginning, US BITs provided entry and establishment rights.<sup>281</sup> The US developed a model BIT in 1982 and concluded its first BIT with Egypt that same year. The US model BIT changed throughout the 1980s as the text was refined.<sup>282</sup>

By 1987, 265 BITs had been concluded, the majority of which continued to be between developed and developing states.<sup>283</sup> Developed states concluded BITs with over seventy developing states worldwide, the majority of which were in Africa and South-East Asia.<sup>284</sup> China signed its first BIT in 1982.<sup>285</sup> The 1980s also saw newly-industrializing states conclude BITs with other developing states.<sup>286</sup>

**§1.33 BITs – the 1990s** The end of the 1980s and the 1990s witnessed an exponential growth in the conclusion of international investment and trade treaties. BITs quintupled during the 1990s.<sup>287</sup> Importantly, BITs were being concluded

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the Shifting Ideology of the BITs' (1993) ITBL 159; K.J. Vandeveld, 'The Political Economy of a Bilateral Investment Treaty' (1998) 92 AJIL 621; K.J. Vandeveld, 'The Economics of Bilateral Investment Treaties' (2000) 41 HILJ 469; and Vandeveld, 'A Brief History', *supra* note 130.

276. Between 1946 and 1966, the US entered into twenty-one FCNs. Vandeveld, *United States Investment Treaties*, *supra* note 43 at 19.

277. Vandeveld, *United States Investment Treaties*, *ibid.*, noting that the US business groups including the International Chamber of Commerce and the State Department's Advisory Committee on Transnational Enterprises recommended that the State Department commence a BIT program.

278. Vandeveld, *United States Investment Treaties*, *ibid.*, at 19-22.

279. See the description of the Hickenlooper Amendment to the United States Foreign Assistance Act, denial of preferential trade treatment under the US Trade Act of 1974 and opposition to international financial assistance by international financial institutions. Akinsanya, *supra* note 50 at 284-300 and Vandeveld, *United States Investment Treaties*, *ibid.*, at 13-14 and 22-28.

280. Vandeveld, *United States Investment Treaties*, *ibid.*, at 22.

281. *Ibid.*, at 72.

282. *Ibid.*, at 29-43.

283. UNCTC, *supra* note 175 at 6.

284. *Ibid.*

285. *Ibid.*, at 39.

286. By 1987, twelve of the 265 BITs had been concluded between developing states. *Ibid.*, at 6.

287. UNCTAD Press Release, 'Bilateral Investment Treaties Quintupled During the 1990s', 15 Dec. 2000, TAD/INF/2877. The press release notes that there were 1857 BITs by the end of the 1990s, up from 385 at the end of the 1980s.

between non-industrialized states.<sup>288</sup> By the end of the 1990s, 1857 BITs had been concluded.<sup>289</sup> Several industrializing states, including India,<sup>290</sup> Argentina, Brazil and Chile signed their first BITs,<sup>291</sup> and OECD states such as Canada<sup>292</sup> and Australia<sup>293</sup> followed the US in creating BIT programs.

The explosion in IIA practice had two major causes.<sup>294</sup> First, there was an increased political commitment by governments in both developed and developing states to economic liberalism and the freer international flow of goods, services and investment. The economic success of the several Asian economies, which had promoted private investment and export production, was viewed as discrediting import substitution policies that had been the dominant economic development model in the immediate post-WWII era. IIAs were regarded as aiding the flow of the investment required for development. The positive economic development role to be played by IIAs was reinforced by the Washington Consensus – a consensus between the IMF, the World Bank and the US Treasury on the policies for developing states' economic development and stabilization.<sup>295</sup> The pillars of the Washington Consensus were fiscal austerity, privatization and market liberalization. The original 1989 consensus included the promotion of FDI and the enforcement of property rights.<sup>296</sup>

The second main cause of the BIT boom was the lack of developing state alternatives to FDI. International lending and aid, both important sources of development financing in the 1970s and early 1980s, became increasingly scarce. Lending was curtailed as developing state indebtedness and defaults increased. The economic recession of the early 1980s in developed states also contributed to

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288. By the end of the 1990s, 833 of the total of 1857 were between developing states and states in transition. *Ibid.*

289. *Ibid.*

290. India's first BIT was India-UK (1994). India had signed an exchange of notes with Germany in 1964 with respect to investment. See *Investment Protection Treaties*, *supra* note 239.

291. Argentina's first BIT was with Italy in 1990. Brazil's first BIT was with Portugal in 1994. Chile's first BIT was with Argentina in 1991. Brazil has not ratified any of its BITs.

292. Canada signed its first BIT in 1989 with the former Soviet Union. Canada calls its BITs Foreign Investment Promotion and Protection Agreements (FIPAs). On Canadian FIPAs, see R.K. Paterson, 'Canadian Investment Promotion and Protection Treaties' (1991) 29 *CYIL* 373 and J. MacIlroy, 'Canada's New Foreign Investment Protection and Promotion Agreement: Two Steps Forward, One Step Back?' (2004) 5 *JWI* 621.

293. Australia signed its first BIT in 1988, with China. See P.T.B. Kohona, 'Investment Protection Agreements: An Australian Perspective' (1987) 21 *JWTL* 79 and P. Turner, M. Mangan & A. Baykitch 'Investment Treaty Arbitration: An Australian Perspective' (2007) 24 *JIA* 103.

294. Vandevelde, 'A Brief History' *supra* note 130 at 177. See also Vandevelde, *supra* note 275; J. Salacuse & N. Sullivan, 'Do BITs Really Work? An Evaluation of Bilateral Investment Treaties and their Grand Bargain' (2006) *HILJ* 67 and Van Harten, *supra* note 5 at 38-44.

295. The term 'Washington Consensus' is attributed to economist John Williamson. See 'What Washington Means by Policy Reform' in J. Williamson, ed., *Latin American Adjustment: How Much Has Happened?* (Washington: Institute for International Economics, 1990). For a critical commentary on the Washington Consensus, see J.E. Stiglitz, *Globalization and Its Discontents* (New York: W.W. Norton, 2002).

296. Williamson, *ibid.*

a declining willingness to increase official aid, which forced developing states to look to FDI as a means of encouraging economic development.

The competition for FDI coupled with an increasing acceptance of liberal economic policies provided the fertile ground for the conclusion of IIAs. IIAs proliferated at the same time as FDI to developing states expanded.<sup>297</sup>

**§1.34 World Bank Guidelines** In 1992 the World Bank issued its *Guidelines on the Treatment of Foreign Direct Investment* (the Guidelines), which emphasized the importance and benefits of FDI and set out the policy for and legal framework governing FDI.<sup>298</sup> The Guidelines were part of the World Bank's wider work on the role of good governance in economic development and the Bank's promotion of the importance of the legal framework for economic development.<sup>299</sup> The Guidelines were created not as binding rules but as part of the evolution of generally acceptable international standards, complementing, but not substituting for, BITs. They are based on the general premise that 'equal treatment of investors in similar circumstances and free competition among them are prerequisites of a positive investment environment.'<sup>300</sup> The Guidelines identify a set of best practices with respect to admission, treatment, expropriation, contracts, the prevention and control of corrupt business practices, the promotion of accountability and transparency in dealings with foreign investors, and settlement of disputes. IIA tribunals have subsequently occasionally referred to the Guidelines in interpreting IIA obligations.<sup>301</sup>

297. In 1982, FDI inflows were USD59 billion and total FDI inward stock amounted to USD0.647 trillion. In 2005, FDI inflows amounted to USD916 billion and total FDI inward stock amounted to USD10.13 trillion. Inflows peaked in 2000 at USD1.4 trillion (United Nations Conference on Trade and Development, *World Investment Report 2006* (New York and Geneva: United Nations, 2006) at xvi and 9 [WIR 2006]). In the 1990's, developing states increased their share of FDI inflows from USD34 billion in 1990 (17% of global inflows) to USD149 billion in 1997 (37% of global inflows). See *World Investment Report 1998: Trends and Determinants – Overview* (New York and Geneva: United Nations, 1998) at 1-12. Of the USD916 billion world FDI inflows in 2005, inflows to developed states were USD542 billion (59%) and inflows to developing state were USD334 billion (36%). The share of South-East Europe (SEE) and the Commonwealth of Independent States (CIS) was 4%. There have been significant increases in FDI outflows from developing states, which totaled USD133 billion – or 17% of world outflows – in 2005 (WIR 2006, *ibid.*, at xvi). For current FDI statistics, see UNCTAD's annual *World Investment Report*.

298. Foreword, *World Bank Guidelines on the Treatment of Foreign Direct Investment*, in World Bank, *Legal Framework for the Treatment of Foreign Investment* (Washington DC: The World Bank, 1992). The Guidelines are reprinted in (1992) 31 ILM 1379. See, generally, I.F.I. Shihata, *Legal Treatment of Foreign Investment: The World Bank Guidelines* (Washington DC: The World Bank, 1993) and C. Wendrich, 'The World Bank Guidelines as a Foundation for a Global Investment Treaty: A Problem-Oriented Approach' (2005) 2 TDM.

299. See World Bank, *Governance and Development* (Washington DC: The World Bank, 1992).

300. Guideline I(3), *supra* note 298.

301. See *Fedax N.V. v. Venezuela* (Decision of the Tribunal on Objections to Jurisdiction, 11 Jul. 1997) at para. 35; *Mr. Patrick Mitchell v. Congo* (Decision on the Application for Annulment of the Award, 1 Nov. 2006) at para. 33; and *CME Czech Republic B.V. v. Czech Republic* (Final Award, 14 Mar. 2003) at para. 161.

**§1.35 Developments in Latin America** Throughout the 1960s and 1970s, Latin American states maintained their general opposition to the minimum standard of treatment and supported the NIEO *Declaration and the Charter of Economic Rights and Duties of States*. Latin American states remained uncomfortable with international investment arbitration, with no Latin American state becoming a party to the ICSID Convention in the 1960s or 1970s. The general approach to foreign investment in Latin America in the 1970s is reflected in Decision 24 of the Andean Common Market (ANCOM) – the *Andean Investment Code*.<sup>302</sup> The Code provided for stringent regulation of foreign investment and incorporated the Calvo Doctrine by providing that Member States would not accord foreign investors more favourable treatment than national investors<sup>303</sup> and that states would not enter into investment instruments limiting the jurisdiction of national courts over investment disputes.<sup>304</sup> In the 1980s, however, Latin American states began liberalizing their foreign investment policies, and in 1987 and 1991 there was a substantial liberalization of the treatment of foreign investment as a result of two Andean Group Commission decisions.<sup>305</sup> By the 1990s, Latin American states were signing BITs *en masse*<sup>306</sup> and began to accede to the ICSID Convention<sup>307</sup> leaving behind the Calvo Doctrine and resistance to the minimum standards of treatment as well as to international adjudication of investment disputes.<sup>308</sup>

The Common Market of the Southern Cone was established in 1991 by Argentina, Brazil, Paraguay and Uruguay under the *Treaty of Asunción* (MERCOSUR).<sup>309</sup> In 1994, the MERCOSUR Council approved the Colonia

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302. ANCOM was created in 1969 by Bolivia, Chile, Ecuador and Peru under the *Cartegena Agreement*. Venezuela joined in 1973 and Chile withdrew in 1976. The *Andean Investment Code* originally appeared in 1970 (1972) 11 ILM 126 and was amended in 1976 (1977) 16 ILM 138. See L. Valdez, 'The Andean Foreign Investment Code: An Analysis' (1972) 7 JILE 1.

303. See Muchlinski (2007), *supra* note 191 at 575-577 and Rubins & Kinsella, *supra* note 5 at 158.

304. Arts. 50 and 51 (1977) 16 ILM 138.

305. See *Andean Group: Commission Decision 220 Replacing Decision 24, the Common Foreign Investment and Technology Licensing Code* (1988) 27 ILM 974 and *Andean Group: Commission Decision 291 (Common Code for the Treatment of Foreign Capital and on Trademarks, Patents, Licenses and Royalties)* (1991) 30 ILM 1283.

306. There were a handful of early BITs between European and Latin American states, namely, Colombia-Germany (1965); Costa Rica-Switzerland (1965); Ecuador-Switzerland (1968); El Salvador-France (1978); Paraguay-UK (1981); Belize-UK (1982); Costa Rica-UK (1982) and Panama-US (1982). Argentina, Chile and Brazil did not conclude their first BITs until the 1990s (see *supra* note 291).

307. The first Latin American country to ratify the ICSID Convention was El Salvador in 1984. Significant numbers ratified in the 1990s.

308. P. Peters & N. Schrijver, 'Latin America and International Regulation of Foreign Investment: Changing Perceptions' (1992) 39 NILR 368.

309. The treaty is *reprinted in* (1991) 30 ILM 1041.

Protocol,<sup>310</sup> which provides BIT-like protections to nationals of MERCOSUR,<sup>311</sup> and the Buenos Aires Protocol, which provides similar protections to non-nationals.<sup>312</sup> However, neither of these protocols has entered into force. The *Group of Three Treaty* (between Colombia, Mexico and Venezuela), concluded in 1994, is a comprehensive free trade agreement (FTA) that, like the *North American Free Trade Agreement* (NAFTA),<sup>313</sup> has a chapter on investment.<sup>314</sup> In addition, Chile entered into an FTA with an investment chapter with Canada in 1996. Other agreements that included investment chapters have been completed in the 2000s.<sup>315</sup>

More recently, IIA claims and awards against Latin American states, and the renewed interest in nationalizing energy industries, have led some Latin American states to reconsider their commitment to investor-state arbitration under IIAs.<sup>316</sup>

310. See N. Rubins, 'Investment Arbitration in Brazil' (2003) 4 *JWI* 1071.

311. *Colonia Protocol on the Reciprocal Promotion and Protection of Investments within MERCOSUR*, signed on 17 Jan. 1994.

312. *Buenos Aires Protocol on the Promotion and Protection of Investments Made by Countries that are not Parties to MERCOSUR*, signed on 8 Aug. 1994. As of 1 Jun. 2008 neither protocol was in force.

313. *North American Free Trade Agreement Between the Government of Canada, the Government of Mexico and the Government of the United States*, 17 Dec. 1992, CTS 1994 No. 2; (1993) 32 *ILM* 289 (Chapters 1-9), 32 *ILM* 605 (Chapters 10-22) (entered into force 1 Jan. 1994) [NAFTA].

314. *Treaty on Free Trade Between the Republic of Colombia, the Republic of Venezuela and the United Mexican States*, signed on 13 Jun. 1994 available online: <<http://sice.oas.org>>. Chapter XVII covers investment and provides similar protections as in other modern BITs.

315. US FTAs with Latin American states include Central America-Dominican Republic-US FTA (CAFTA-DR) (2004); Chile-US FTA (2003); Colombia-US FTA (2006); Panama-US FTA (2007) and Peru-US FTA (2006).

316. Prominent manifestations of this concern are Bolivia's notice of denunciation of the ICSID Convention in May 2007 and Ecuador's notification to ICSID in Dec. 2007 that it will not consent to investment disputes regarding natural resources. See ICSID website. Further, the constitutionality of IIAs has been questioned in some countries. See, H. Rosatti, 'Los Tratados Bilaterales de Inversión, el Arbitraje Internacional Obligatorio y el Sistema Constitucional Argentino' (2003) *La Ley* 1; and C.S. Fayt, *La Constitución Nacional y los Tribunales Internacionales de Arbitraje* (Buenos Aires: La Ley, 2007). In Bolivia, the laws approving several BITs were challenged before the Constitutional Tribunal which dismissed the application on the basis that the constitutionality of treaties in Bolivia can only subject to an *ex ante* review (before approval) and not to an *ex post* review. See *Wilson Beimar Magne Hinojosa, Diputado Nacional contra Eduardo Rodríguez Veltzé, Presidente Constitucional de la República de Bolivia, y otro* (Sentencia TC 0031/2006, 10 May 2006). The constitutionality of NAFTA Chapter 11 has been questioned in Canada before the provincial superior court. The Ontario Court of Appeal rejected the challenge in 2006 (see *Council of Canadians et al. v. Attorney General of Canada*, Ontario Court of Appeal (Judgment, 30 Nov. 2006)).

**§1.36 Developments in Africa, Middle East and Asia** Many African, Middle Eastern and Asian states were early signatories to BITs. As already noted, these early BITs were generally based on model agreements prepared by capital exporting states. In the early 1980s, the Asian-African Legal Consultative Organization (AALCO)<sup>317</sup> published three draft BITs, which provided different models of investment liberalization and protection.<sup>318</sup> In 1980, the *United treaties Agreement for the Investment of Arab Capital in the Arab States* was signed creating an Arab Investment Court.<sup>319</sup> A number of other regional investment have been concluded in the Middle East and Africa.<sup>320</sup> In addition, the European Economic Community (EEC) and certain African, Caribbean and Pacific (ACP) states concluded the *Lomé III and Lomé IV Conventions*, both of which had sections addressing investment.<sup>321</sup> In 2007, the Common Market for Eastern and Southern Africa (COMESA) adopted an *Investment Agreement for the COMESA Common Investment Area*.<sup>322</sup>

In 1987, the Association of South East Asian Nations (ASEAN) created the *Agreement for the Promotion and Protection of Investments* (ASEAN Investment Agreement) applicable to ASEAN investors.<sup>323</sup> The ASEAN Investment Agreement was amended by the Jakarta Protocol in 1996. In 1998, the *Framework Agreement on the ASEAN Investment Area* (Framework Agreement) was concluded. The aim

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317. AALCO was formed in 1956, a tangible outcome of the 1955 Bandung Conference, which forged the non-aligned movement (see <aalco.int>). The question of promotion and protection of investments was first discussed at the Jakarta Session held in Apr. 1980, in the context of regional co-operation in the field of industry among the countries of the Asian-African region. At this time, the AALCO was called Asian African Legal Consultative Committee.
318. Model A provides the highest standards of investment protection. Model B provides for more restrictive investment promotion and protection provisions. Model C provides protection similar to Model A but the protections apply to specific types of investments. The models are reprinted in (1984) 23 ILM 237. Online: <<http://aalco.int>>.
319. The first Arab Investment Court decision is *Tanmiah v. Tunisia*, 12 Oct. 2004. For a discussion of the case, see W. Ben Hamida, 'The First Arab Investment Court Decision' (2006) 7 JWIT 699. For a discussion of BITs with Arab states, see R.T. Greig, C. Annacker & R. Ziadé 'How Bilateral Investment Treaties Can Protect Foreign Investors in the Arab World or Arab Investors Abroad' (2008) 25 JIA 257.
320. These treaties include the *Agreement on Promotion, Protection and Guarantee of Investments Among Member States of the Organisation of Islamic Conference* (1981) and the *Community Investment Code of the Economic Community of the Great Lakes Countries* (1982) (See UNCTAD IIA Compendium Vol. 9, Nos 38 and 39).
321. *Third ACP-EEC Convention* of 8 Dec. 1984 [Lomé III] (1985) 24 ILM 571 and *Fourth ACP-EEC Convention* of 15 Dec. 1989 [Lomé IV] (1990) 29 ILM 783. Lomé III and Lomé IV provide for investor-state arbitration in limited circumstances. For a discussion of the investment provisions in the Lomé Conventions see J. Paulsson, *supra* note 263 at 241-246.
322. *Investment Agreement for the COMESA Common Investment Area*, adopted at the Twelfth Summit of COMESA Authority of Heads of State and Government, held in Nairobi, Kenya, 22-23 May 2007.
323. (1988) 27 ILM 612. The ASEAN Investment Agreement was considered in *Yaung Chi Oo Trading Pte. Ltd. v. Myanmar* (Award, 31 Mar. 2003).

of the Framework Agreement is to create an ASEAN Investment Area by 2010 where all ASEAN investors would benefit from national treatment.<sup>324</sup>

**§1.37 North American Free Trade Agreement** A significant development in the 1990s was the conclusion of the NAFTA in 1992.<sup>325</sup> The NAFTA is a comprehensive free trade agreement between Canada, Mexico and the US covering, among other things, goods, services, government procurement and investment. Chapter Eleven, the investment chapter, was unique at the time because of the breadth of its coverage and its provision for investor-state arbitration between an OECD Member State and nationals of another OECD Member State. Although the investor-state arbitration provisions were originally included in NAFTA at US insistence in order to protect US investors in Mexico, a number of high profile claims have been made against the US and Canada. Over forty-five claims have been commenced under NAFTA Chapter Eleven,<sup>326</sup> resulting in a series of important IIA orders, decisions and awards addressing procedural and jurisdictional issues, as well as the substantive scope of investment protections.<sup>327</sup> NAFTA investment practice and jurisprudence is considered in detail in subsequent chapters.

**§1.38 Energy Charter Treaty** The *Energy Charter Treaty* (ECT) was concluded in 1994 and covers multilateral co-operation in the areas of energy transit, trade, investments, environmental protection and energy efficiency.<sup>328</sup> The ECT's

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324. For a discussion of the ASEAN investment protection framework and more generally for developments in Asia, see J. Savage, 'Investment Treaty Arbitration and Asia: Survey and Comment' (2005) 1 AIAJ 3 and 'Investment Treaty Arbitration and Asia: Recent Developments in 2005 and 2006' (2007) 3 AIAJ 1.
325. NAFTA, *supra* note 313.
326. Documents relating to NAFTA claims are available on the official Canadian, Mexican and US NAFTA websites and [naftaclaims.org](http://naftaclaims.org).
327. For a comprehensive negotiating history of Chapter Eleven and analysis of Chapter Eleven jurisprudence, see M. Kinnear, A.K. Bjorklund & J. Hannaford, *Investment Disputes Under NAFTA: An Annotated Guide to NAFTA Chapter 11* (The Netherlands: Kluwer Law International, 2006); H.C. Alvarez, 'Arbitration under the North American Free Trade Agreement' (1999) 16 AI 393; C. Brower, II, 'Investor-State Disputes Under NAFTA: The Empire Strikes Back' (2001) 40 CJTL 43; J.C. Thomas, 'A Reply to Professor Brower' (2002) 40 CJTL 433; C. Brower, II, 'Beware the Jabberwock: A Reply to Mr. Thomas' (2002) 40 CJTL 465; G.A. Alvarez & W.W. Park, 'The New Face of Investment Arbitration: NAFTA Chapter 11' (2003) 28 YJIL 365; C.H. Brower, II, 'Structure, Legitimacy, and NAFTA's Investment Chapter.' (2003) 36 VJTL 37; J. Coe, 'Taking Stock of NAFTA Chapter 11 in Its Tenth Year: An Interim Sketch of Selected Themes, Issues, and Methods' (2003) VJTL 36. Also see the collection of papers in L.R. Dawson, ed., *Whose Rights?: The NAFTA Chapter 11 Debate* (Ottawa: Centre for Trade Policy and Law, 2002) and T. Weiler, ed., *NAFTA Investment Law and Arbitration: Past Issues, Current Practice, Future Prospects* (Ardsey: Transnational Publishers, 2004).
328. The treaty, reprinted at (1995) 34 ILM 360, was concluded in 1994 and entered into force in 1998. As of 1 Jun. 2008, forty-six states and the EC have ratified the ECT, including most European states. Australia, Belarus, Iceland, Norway and Russia have signed the treaty but not yet ratified it. A number of other states, including Canada, China, a number of Middle Eastern states and the US are observers. See online <<http://encharter.org>>. For background

investment protection provisions are similar to those found in other BITs, although they only apply to investments in the energy sector. To date, eighteen investor-state claims have been commenced under the ECT, resulting in a number of awards.<sup>329</sup>

**§1.39 World Trade Organization** The World Trade Organization (WTO) was established on 1 January 1998 as a result of the Uruguay Round trade negotiations.<sup>330</sup> Under pre-WTO GATT law, the GATT applied only to a limited number of trade-related investment measures (TRIMs), primarily those that link foreign investment to a requirement to use domestic goods.<sup>331</sup> During the Uruguay Round (1986-1994), the US pushed for greater discipline on TRIMs and sought a code that would further liberalize market access for investment.<sup>332</sup> The majority of the GATT members, however, rejected this proposal, preferring to clarify the types of measures that breached the existing GATT obligations.<sup>333</sup> The accord attained as part of the Uruguay Round, *Agreement on Trade-Related Investment Measures* (TRIMS Agreement),<sup>334</sup> reaffirms that WTO Members may not apply investment measures that are inconsistent with GATT national treatment obligations or that otherwise violate the general prohibition on quantitative restrictions on imports and exports of goods.

In addition to the TRIMS Agreement, the Uruguay Round produced the *General Agreement on Trade in Services* (GATS), which liberalizes trade in services. The GATS includes a commitment with respect to commercial presence, essentially creating rights for foreign investors to invest in service sectors covered

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on the ECT, see T. Wälde, ed., *The Energy Charter Treaty: An East-West Gateway for Investment and Trade* (London: Kluwer Law, 1996); R. Happ, 'Dispute Settlement under the Energy Charter Treaty' (2003) 45 GYIL 331; T. Wälde, 'Energy Charter Treaty-based Investment Arbitration – Controversial Issues' (2004) 5 JWIT 373 and C. Ribeiro, *Investment Arbitration and the Energy Charter Treaty* (New York: Juris, 2007). See also P. Cameron, *International Energy Investment Law* (Oxford: Oxford University Press, forthcoming).

329. As of 14 Jun. 2008, the Energy Charter Secretariat listed eighteen ECT investor-state dispute settlement cases on its website. Thirteen of the cases were pending, two had been settled by the parties and in three cases tribunals had made a final award. The three final awards are: *Nykomb Synergetics Technology Holding AB v. Latvia* (Award, 16 Dec. 2003); *Petrobart Limited v. Kyrgyz Republic* (Award, 29 Mar. 2005) and *Limited Liability Company Amtov v. Ukraine* (Award, 26 Mar. 2008). In addition, there are two decisions on jurisdiction: *Plama Consortium Limited v. Bulgaria* (Decision on Jurisdiction, 8 Feb. 2005) and *Ioannis Kardassopoulos v. Georgia* (Decision on Jurisdiction, 6 Jul. 2007).
330. See *The Legal Texts: Results of the Uruguay Round of Multilateral Trade Negotiations* (Cambridge: Cambridge University Press, 1994) [Legal Texts].
331. See *infra* Chapter 8, §8.15.
332. See T. Stewart, 'Trade Related Investment Measures' in T. Stewart, ed., *The GATT Uruguay Round: A Negotiating History* (Boston: Kluwer Law International, 1994) at 2348. See also *infra* Chapter 8, §8.15.
333. P. Civello, 'The TRIMS Agreement: A Failed Attempt at Investment Liberalization' (1999) 8 MJGT 97.
334. *Agreement on Trade-Related Investment Measures*, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, reproduced in Legal Texts, *supra* note 330.

by GATS commitments.<sup>335</sup> For this reason, the GATS can be considered as being the first multilateral investment liberalization treaty.

**§1.40 Multilateral Agreement on Investment (MAI)** Although states have been willing to create a network of IIAs in a piece-meal way, states have been unable to agree on investment issues at a multilateral level. Following the failure to obtain investment protection in the Uruguay Round agreements, the US promoted negotiations for a *Multilateral Agreement on Investment* (MAI) within the OECD. The strategy was to conclude a multilateral agreement with high standards of protection amongst OECD members and other willing states, and then to open the agreement to other states.<sup>336</sup> Negotiations for the MAI were conducted by OECD Member States between 1995 and 1998.<sup>337</sup> However, MAI negotiations were commenced at the same time that several NAFTA investment claims attained a high public profile. This and disagreements between the negotiating states on a broad range of issues, as well as concerns raised by non-governmental organizations (NGOs) about the procedural and substantive protections afforded by investment treaties, resulted in the abandonment of the draft MAI.<sup>338</sup>

**§1.41 WTO Working Group on the Relationship between Trade and Investment and the Doha Declaration** As a result of the 1996 WTO Singapore Declaration, a Working Group on the Relationship between Trade and Investment (Working Group) was established, which began studying the nexus between trade and investment. The abandonment of the MAI negotiations in 1998 led to renewed interest amongst some states to provide the WTO a role in international investment rules. In the 2001 *Doha Declaration*, WTO members recognized ‘the case for a multilateral framework to secure transparent, stable and predictable conditions for long-term cross-border investment.’<sup>339</sup> The Declaration directed the Working Group to focus on several investment issues,<sup>340</sup> with the formal decision on the

335. See *infra* Chapter 3, §3.14.

336. For commentary see J.W. Salacuse, ‘Towards a Global Treaty on Foreign Investment: The Search for a Grand Bargain’ in N. Horn, ed., *Arbitrating Foreign Investment Disputes* (The Hague: Kluwer Law International, 2004) at 51.

337. The Multilateral Agreement on Investment: Draft Consolidated Text, DAF/MAI(98)7/REV1; The Multilateral Agreement on Investment: Commentary to the Consolidated Text, DAF/MAI(98)8/REV1. See also the database containing documents from the negotiations, online: <<http://www1.oecd.org/daf/mai/index.htm>>.

338. See S. Picciotto, ‘Linkages in International Investment Regulation: The Antinomies of the Draft Multilateral Agreement on Investment’ (1998) UPJIEL 731; R. Geiger, ‘Towards a Multilateral Agreement on Investment’ (1998) 31 CILQ 467; C. Schittecatte, ‘The Politics of the MAI – On the Social Opposition of the MAI and its Role in the Demise of the Negotiations’ (2000) 1 JWI 329; J. Kurtz, ‘A General Investment Agreement in the WTO? Lessons from Chapter 11 of NAFTA and the OECD Multilateral Agreement on Investment’ (2002) 23 UPJIEL 713 and P. Sauve ‘Multilateral Rules on Investment: Is Forward Movement Possible’ (2006) 9 JIEL 325.

339. Para. 20, *Doha Declaration*, 14 Nov. 2001, 41 ILM 746 [*Doha Declaration*].

340. These were scope and definition; transparency; non-discrimination; modalities for pre-establishment commitments based on a GATS-type, positive list approach; development

beginning of negotiations on a possible text to be taken at the next WTO Ministerial Conference in 2003. In the lead-up to the 2003 Ministerial Conference, developing state members opposed negotiation of the ‘Singapore Issues’ (trade and investment, trade and competition, transparency in government procurement and trade facilitation).<sup>341</sup> Disagreement between WTO members on including investment in the Doha Round is seen as a major factor in the breakdown of the Doha negotiations. At the 2003 Ministerial Conference, the EC Trade Commissioner agreed to drop investment from the Doha agenda, a decision later supported by the US. As a result, there is unlikely to be any comprehensive discussion of investment disciplines within the WTO in the foreseeable future.<sup>342</sup>

**§1.42 Chinese IIAs** Although China did not enter its first BIT until 1982,<sup>343</sup> over the past twenty five years, China has signed a significant number of BITs. With over 120 BITs, it ranks only second to Germany in the numbers of BITs concluded.<sup>344</sup> Although China is the largest recipient of FDI among developing economies,<sup>345</sup> it has increasingly become a major source of FDI, with significant Chinese investment in Africa and Asia.<sup>346</sup> Since 1998, Chinese BIT policy has increasingly addressed the protection of Chinese overseas FDI.<sup>347</sup> Importantly, beginning with Barbados-China (1998), China changed its practice of limiting investor-state arbitration to disputes concerning the amount of compensation resulting from expropriation and consented generally to the arbitration of IIA disputes.<sup>348</sup> Current Chinese BIT practice is reflected in China’s BITs with The Netherlands (2001) and Germany (2003). Unlike early Chinese BITs, which provided for significant limitations in substantive and procedural protections,<sup>349</sup> China’s most recent BITs provide

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provisions; exceptions and balance-of-payments safeguards; consultation; and the settlement of disputes between members (*Doha Declaration, ibid.*, at para. 22).

341. See M. Trebilcock & R. Howse, *The Regulation of International Trade*, 3rd edn (London: Routledge, 2005) at 498.

342. *Ibid.*, at 461.

343. China-Sweden (1982).

344. UNCTAD, *Recent Developments in international investment agreement, IIA Monitor No. 3 (2007)*, UNCTAD/WEB/ITE/IIA/2007/6 [IIA Monitor No. 3 (2007)] at 2. Germany ranks first with BITs concluded (134), followed by China (120) and Switzerland (114).

345. UNCTAD, *World Investment Report 2007* (United Nations: Geneva: 2007) [WIR 2007] at 41.

346. WIR 2007, *ibid.*, at 41-44.

347. See C. Congyan, ‘Outward Foreign Direct Investment Protection and the Effectiveness of Chinese BIT Practice’ (2006) 7 JWIT 621. See also Savage, *supra* note 324; A. Chen ‘Should the Four Great Safeguards in Sino-Foreign Bits Be Hastily Dismantled – Comments on Provisions Concerning Dispute Settlement in Model U.S. and Canada Bits’ (2006) 7 JWIT 899; S. Schill, ‘Tearing Down the Great Wall: The New Generation Investment Treaties of the People’s Republic of China’ (2007) 15 CJICL 73; P. Turner, ‘Investor-State Arbitration’ in M. Moser, ed., *Managing Business Disputes in Today’s China: Duelling with Dragons* (Hague: Kluwer Law International, 2007) and W. Shan & N. Gallagher, *Chinese Investment Treaties: Policies and Practice* (Oxford: Oxford University Press, forthcoming).

348. See Congyan, *ibid.*, at 638.

349. Older Chinese BITs limit (i) the scope of national treatment to treatment in accordance with domestic laws and regulations; (ii) transfer rights; and (iii) recourse to investor-state

substantive and procedural protections generally similar to capital exporting state BITs.<sup>350</sup> China has also begun to conclude free trade agreements with wide-ranging procedural and substantive investment obligations.<sup>351</sup>

**§1.43 Indian IIAs** The US proposed concluding an FCN Treaty with India shortly after Indian independence in 1947.<sup>352</sup> These talks floundered because of India's inward looking economic policy, a policy that continued until the 1980s.<sup>353</sup> Between 1988 and 1991, India began to embrace the prescriptions of economic liberalization.<sup>354</sup> This policy change led to the rapid development an IIA program. India signed the MIGA Convention in 1992. In 1993, it signed a *Third-Generation Cooperation Agreement on Partnership and Development* with the EU, which called for the development of India's IIAs. India signed its first IIA with the UK in 1994.<sup>355</sup> As of December 2006, India had signed sixty-one IIAs, of which forty-nine were ratified, and was in negotiations with forty-one other countries.<sup>356</sup> In addition, India has entered into economic co-operation agreements that contain investment chapters.<sup>357</sup> All of India's IIAs adopt the principle of direct investor-state arbitration.

## IV CURRENT STATUS OF THE NETWORK OF IIAS

**§1.44 The expanding network of IIAs** The current international legal framework governing foreign investment consists of a network of over 2800 IIAs.<sup>358</sup> By the end of 2006, this network comprised some 2573 BITs<sup>359</sup> (of which 75% had

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arbitration to the determination of compensation for expropriation. Congyan, *ibid.*, at 638.

350. There are some important exceptions. For example, national treatment does not apply to existing non-conforming measures and the investor must have exhausted a domestic administrative review procedure before submission of the claim (see *China-Netherlands (2001)*). For a comparison of older and newer model Chinese BITs see articles cited *supra* at note 347.

351. See Chapter 11 (Investment), *China-New Zealand Free Trade Agreement (2008)*.

352. See D. Krishan, 'India and International Investment Laws' in B. Patel, ed., *India and International Law* Vol. 2 (London: Brill, 2008) 277.

353. *Ibid.*, at 291-294.

354. *Ibid.*, at 294-295.

355. *Ibid.*, at 297. India based its model BIT upon a not very significant adaptation of the UK Model BIT. The UK Model BIT, in turn, was created in the mid-1970s and was based on the 1967 Draft OECD Convention, the ICSID Convention and German and Swiss BIT practice. See, for example, *Egypt-UK (1975)*.

356. Krishan, *supra* note 352 at 298. India has since signed an IIA with China. Negotiations with the US and Canada are ongoing.

357. See *India-Singapore Comprehensive Economic Co-operation Agreement (2005)*.

358. Note by the UNCTAD Secretariat, 'International Investment Rulemaking', 22 May 2007, TD/B/COM.2/EM.21/2 [International Investment Rulemaking]. For earlier statistics see UNCTAD, *World Investment Report 2006* (Geneva: United Nations, 2006) at xix. Current statistics are available on the UNCTAD webpage on IIAs.

359. International Investment Rulemaking, *ibid.* at 3.

entered into force<sup>360</sup>) and 241 bilateral or trilateral free trade and investments agreements.<sup>361</sup> The network also includes a number of important regional and sectoral agreements that include investment protection provisions, notably NAFTA, the ECT and the *Framework Agreement on the ASEAN Investment Area*.<sup>362</sup> In addition, there is a network of 2,651 double taxation treaties.<sup>363</sup>

Although historically BITs developed in an asymmetrical context in which developing states exported capital and developed states imported capital, in recent years developing states have been concluding IIAs between themselves. In 1990, there were 42 BITs between developing states. This number jumped to 679 by the end of 2006 – 26% of existing BITs.<sup>364</sup> Further, there were over 90 south-south free trade and investment agreements by the end of 2006.<sup>365</sup> This reflects the economic reality that developing states are increasingly capital exporters.<sup>366</sup> As a result, there is a global, decentralized and overlapping network of IIAs that protect foreign investment.<sup>367</sup>

**§1.45 The increase in investor-state arbitrations** Despite the fact that investor-state arbitration provisions had been included in IIAs since 1968, until 1990 there were no reported IIA arbitrations. The first reported IIA award was *Asian Agricultural Products Ltd v. Sri Lanka (AALP)* a claim under the Sri Lanka-UK BIT arising from the destruction of a shrimp farm by Sri Lankan security forces.<sup>368</sup> The tribunal ultimately awarded the investor USD460,000 in damages for the destruction of the farm. The *AAPL* award was followed by an award against Poland in 1995 that is not publicly available,<sup>369</sup> an award against Zaire in 1997 under the

360. UNCTAD, 'The Entry into Force of Bilateral Investment Agreements (BITs),' IIA Monitor No. 3 (2006), UNCTAD/WEB/ITE/IIA/2006/9.

361. International Investment Rulemaking, *supra* note 358 at 4.

362. Others include the Colonia and Buenos Aires Investment Protocols of MERCOSUR; the *Unified Agreement for the Investment of Arab Capital in the Arab States*; and the *Agreement on Promotion, Protection and Guarantee of Investments Among Member States of the Organisation of Islamic Conference*. See *infra* §§1.35 to 1.38.

363. International Investment Rulemaking, *supra* note 358 at 3. On double taxation treaties see, UNCTAD, *Taxation*, UNCTAD Series on issues in international investment agreements (New York and Geneva: United Nations, 2000) (UNCTAD/ITE/IIT/16). Also see the OECD's extensive publications and analysis of taxation treaties.

364. International Investment Rulemaking, *supra* note 358 at 6. Also see UNCTAD, *Recent Developments in International Investment Agreements*, IIA Monitor No. 2 (2005) (New York and Geneva: United Nations, 2005) at 4.

365. *Ibid.*

366. There have been significant increases in FDI outflows from developing states, which totaled USD133 billion – or 17% of world outflows – in 2005.

367. International Investment Rulemaking, *supra* note 358 at 6.

368. *Asian Agricultural Products Ltd (AAPL) v. Sri Lanka* (Final Award, 27 Jun. 1990).

369. *Saar Papier Vertriebs GmbH v. Poland*. See Investment Law and Policy Weekly News Bulletin, 5 Jan. 2004.

US-Zaire BIT,<sup>370</sup> and a decision on jurisdiction under Netherlands-Venezuela (1991).<sup>371</sup>

According to UNCTAD, by the end of 2007, there were 290 known IIA arbitrations, the majority of which had been commenced under BITs.<sup>372</sup> Over two-thirds of the claims have been filed since 2001<sup>373</sup> – 182 of these claims were filed with ICSID,<sup>374</sup> 80 under the UNCITRAL Rules and 14 under the Stockholm Chamber Commerce Rules.<sup>375</sup> The remaining claims were filed under other international and regional arbitral rules.<sup>376</sup> Of the ICSID claims, 46 have been brought against Argentina, 44 of which relate to the measures taken by Argentina in the early 2000s to address its economic crisis.<sup>377</sup> Recent studies have begun to empirically analyze trends in IIA awards.<sup>378</sup>

**§1.46 IIA jurisprudence** The growing body of IIA arbitration decisions has created a specialized body of jurisprudence. Although there is no formal doctrine

370. *American Manufacturing & Trading, Inc. v. Zaire* (Final Award, 21 Feb. 1997).

371. *Fedax N.V. v. Venezuela* (Decision of the Tribunal on Objections to Jurisdiction, 11 Jul. 1997).

372. See UNCTAD, *Latest Developments in Investor-State Dispute Settlement*, IIA Monitor No. 1 (2008), UNCATD/WEB/ITE/IIA/2008/3 [IIA Monitor No. 1 (2008)]. For earlier reports, see International Investment Rulemaking, *supra* note 358 at 5 and UNCTAD, 'Investor State Disputes Arising from Investment Treaties: A Review', UNCTAD/ITE/IIT/2005/4. [UNCTAD, 'Investor-State Disputes']. A 2007 International Institute for Sustainable Development report highlights, however, that the number of non-ICSID IIA claims may be significantly higher since claims may proceed under arbitration rules that require no public disclosure. See L.E. Peterson 'Investment Treaty News: 2006 – A Year in Review' (Winnipeg: IISD, 2007).

373. *Supra* note 358.

374. See International Investment Rulemaking, *supra* note 358 at 5. Also see UNCTAD, 'Investor-State Disputes', *supra* note 372 at 4.

375. IIA Monitor No. 1 (2008), *supra* note 372. The UNCITRAL Arbitration Rules were adopted by the United Nations Commission on International Trade Law in 1976 as a comprehensive set of procedural rules to govern international commercial arbitrations. For commentary on the rules in the context of foreign investment see D. Caron, *The UNCITRAL Arbitration Rules: A Commentary* (Oxford: Oxford University Press, 2006) and S. Baker & M. Davis, *The UNCITRAL Arbitration Rules in Practice: The Experience of the Iran-United States Claims Tribunal* (Deventer: Kluwer Law and Taxation Publishers, 1992). Despite their widespread use, there is concern that the 30 year old UNCITRAL Rules need to be updated to reflect developments and changes in international arbitral practice. UNCITRAL is considering revisions to the rules. See UNCITRAL, Secretariat Note, 'Settlement of commercial disputes: Revisions of the UNCITRAL Arbitration Rules' (20 Jul. 2006) A/CN.9/WG.II/WP.143. UNCITRAL commissioned Jan Paulsson and Georgios Petrochilos to report on recommendations for revisions. See J. Paulsson & G. Petrochilos, 'Revisions of the UNCITRAL Rules' (2006), available on the UNCITRAL website.

376. IIA Monitor No. 1 (2008), *supra* note 372.

377. IIA Monitor No. 1 (2008), *ibid.* For a summary of events see J.F. Hornbeck, 'The Argentine Financial Crisis: A Chronology of Events' US Congressional Research Service Report No. RS21130, 31 Jan. 2002.

378. See S.D. Franck, 'Empirically Evaluating Claims About Investment Treaty Arbitration' (2007) 86 NCLR 1 and 'Empiricism and International Law: Insights from Investment Treaty Dispute Resolution' (2008) 48 VJIL 767. Also see Van Harten, *supra* note 5 at 30-34.

of *stare decisis* or precedent in public international law,<sup>379</sup> in practice IIA tribunals refer to and rely on previous IIAs awards and decisions to support their interpretation of IIAs.<sup>380</sup> The tribunal in *ADC Affiliate Limited and ADC & ADMC Management Limited v. Hungary*, noted:

The Parties to the present case have also debated the relevance of international case law relating to expropriation. It is true that arbitral awards do not constitute binding precedent. It is also true that a number of cases are fact-driven and that the findings in those cases cannot be transposed in and of themselves to other cases. It is further true that a number of cases are based on treaties that differ from the present BIT in certain respects. However, cautious reliance on certain principles developed in a number of those cases, as persuasive authority, may advance the body of law, which in turn may serve predictability in the interest of both investors and host States.<sup>381</sup>

A recent empirical study on the incidence of citation to previous awards highlights that the jurisprudence has been facilitated by: the publication and ready availability of IIA awards and decisions; the similarity between provisions amongst IIAs; and the comparatively small number of arbitrators many of whom sit on multiple cases.<sup>382</sup> As noted by a leading IIA practitioner and arbitrator:

That a special jurisprudence is developing from the leading awards in the domain of investment arbitration can only be denied by those determined to close their eyes.<sup>383</sup>

The existence of a growing body of IIA case law has not necessarily resulted in a consistent jurisprudence. As will be explored throughout this book, there are

379. Art. 59, *Statute of the International Court of Justice* provides that '[t]he decision of the Court has no binding force except between the parties and in respect of that particular case.' Art. 38 states that judicial decisions constitute only 'subsidiary means for the determination of rules of law.' See A. Zimmermann *et al.*, eds, *Statute of the International Court of Justice: A Commentary* (Oxford: Oxford University Press, 2006) at 1244. Art. 53 of the ICSID Convention provides that the '[t]he award shall be binding on the parties,' which has been interpreted 'as excluding the applicability of the principle of binding precedent to successive ICSID cases.' C. Schreuer, *ICSID Commentary*, *supra* note 154 at 1082. See *infra* Chapter 2, §2.23.

380. See J. Commission, 'Precedent in Investment Treaty Arbitration: A Citation Analysis of a Developing Jurisprudence' (2007) 24 JIA 129 for an in-depth survey of this phenomenon. For statements by tribunals on the use of previous IIA awards and decisions see *CMS Gas Transmission Company v. Argentina* (Decision of the Tribunal on Objections to Jurisdiction, 17 Jul. 2003); *El Paso Energy International Company v. Argentina* (Decision on Jurisdiction, 27 Apr. 2006); *Suez, Sociedad General de Aguas de Barcelona S.A., and InterAgua Servicios Integrales del Agua S.A. v. Argentina*, (Decision on Jurisdiction, 16 May 2006); and *Jan de Nul N.V., Dredging International N.V. v. Egypt* (Decision on Jurisdiction, 16 Jun. 2006). Also see *infra* T. Cheng, 'Precedent and Control in Investment Treaty Arbitration' (2007) 30 FILJ 1014. See *infra* Chapter 2, §2.23 on the use of precedent in IIA arbitrations.

381. Award of the Tribunal, 2 Oct. 2006, at para. 293.

382. *Ibid.*, at 136 *et seq.*

383. J. Paulsson, 'International Arbitration and the Generation of Legal Norms: Treaty Arbitration and International Law,' in ICCA Congress Series No. 13 (The Hague: Kluwer, 2007).

inconsistencies in the IIA case law. One of the purposes of this book is to examine critically the emerging jurisprudence and, where possible, provide a statement of applicable principles.

**§1.47 Renegotiation and new model IIAs** The rapid developments in IIA practice and jurisprudence has led states to renegotiate older IIAs and to develop new model IIAs to address issues of concern.<sup>384</sup> By June 2007, a total of 109 BITs had been renegotiated. Germany, the state that initiated the first BIT program, led this development with thirteen renegotiated BITs, followed by China and Morocco with twelve renegotiated BITs each.<sup>385</sup>

The experience of the US and Canada as respondents in NAFTA investment arbitrations has led these states to create new Model BITs that clarify the scope and meaning of investment obligations, including the minimum standard of treatment, expropriation and MFN treatment. The new model treaties also address various issues related to investor-state arbitration, including the ability of non-disputing parties to participate in the proceedings.<sup>386</sup> The Canadian (2003),<sup>387</sup> US (2004)<sup>388</sup> and Norwegian (2007)<sup>389</sup> Model BITs, along with the investment chapters in recent free trade and investment agreements,<sup>390</sup> suggest that the IIA regime is continuing to evolve.<sup>391</sup>

384. See UNCTAD, *Investor-State Dispute Settlement and Impact on Investment Rulemaking*, UNCTAD/ITE/IIA/2007/3 (United Nations, Geneva, 2007) [UNCTAD, *Investor-State Dispute Settlement and Impact on Investment Rulemaking*] for a discussion of the impact of IIA arbitrations on IIA practice.

385. IIA Monitor No. 3 (2007), *supra* note 344.

386. UNCTAD, *Investor-State Dispute Settlement and Impact on Investment Rulemaking*, *supra* note 384.

387. See J. MacIlroy, *supra* note 292.

388. For commentary see G.A. Alvarez & W.W. Park, *supra* note 327; C.H. Brower, II, 'Investor-State Arbitration, and the Law of State Immunity' (2005) 20 AUILR 907; J. Coe Jr., 'The State of Investor-State Arbitration-Some Reflections on Professor Brower's Search for Sensible Principles' (2005) 20 AUILR 931; W.S. Dodge, 'Investor-State Dispute Settlement Between Developed Countries: Reflections on the Australia-United States Free Trade Agreement' (2006) 39 VJTL 1; D. Gantz, 'The Evolution of FTA Investment Provisions: From NAFTA to the United States-Chile Free Trade Agreement' (2004) 19 AUILR 679; B. Legum, 'Lesson Learned from the NAFTA: The New Generation of U.S. Investment Treaty Arbitration Provisions' (2004) 19 ICSID Rev 344 and S.M. Schwebel, 'The United States 2004 Model Bilateral Investment Treaty: An Exercise in the Regressive Development of International Law,' in G. Aksen *et al.*, eds, *Reflections on International Law, Commerce and Dispute Resolution, Liber Americorum in honour of Robert Briner*, (Paris: International Chamber of Commerce, 2005) 815.

389. The 2007 Norwegian Model BIT and commentary is available on <<http://ita.law.uvic.ca>>.

390. For example, see Chapter 6 (Investment), *India-Singapore Comprehensive Economic Co-operation Agreement* (2005) and Chapter 11 (Investment), *China-New Zealand Free Trade Agreement* (2008).

391. For an overview of developments in IIA practice in the context of sustainable development, see A. Newcombe, 'Sustainable Development and Investment Treaty Law' (2007) 8 JWIT 357.

**§1.48 Investment promotion effects of IIAs** Although there is little commentary or jurisprudence on legal obligations arising from promotion clauses in IIAs,<sup>392</sup> there is a growing body of literature on the effects of IIAs on FDI flows. Given the rate at which states have concluded BITs, it is perhaps surprising that the empirical literature is inconclusive on the extent to which BITs result in increased FDI. Commentators have highlighted the polarized views of ‘Treaty Protagonists’ and ‘Market Protagonists.’<sup>393</sup> ‘Treaty Protagonists’ argue that IIAs attract FDI, while ‘Market Protagonists’ suggest that market factors are determinative. The 2003 UNCTAD World Investment Report (WIR) concluded – with a ‘Market Protagonist’ argument – that ‘BITs play a minor role in influencing global FDI flows.’<sup>394</sup> The WIR nevertheless highlights, with a ‘Treaty Protagonist’ argument, the ‘enabling’ function of IIAs in allowing a state’s economic determinants to assert themselves:

The policy framework is at best enabling, having by itself little or no effect on FDI flows. It has to be complemented by economic determinants that attract FDI, especially market size and growth, skills, abundant competitive resources and good infrastructure. As a rule, IIAs tend to make the regulatory framework more transparent, stable, predictable and secure – that is, they allow the economic determinants to assert themselves. And when IIAs reduce obstacles to FDI and the economic determinants are right, they can lead to more FDI. But it is difficult to identify the specific impact of the policy framework on FDI flows, given the interaction and relative importance of individual determinants.<sup>395</sup>

Although later studies provide support for a more robust relationship between IIAs and FDI levels,<sup>396</sup> the existence of a causal relationship and the strength of that

392. See *infra* Chapter 3, §3.6.

393. S. Franck, ‘Foreign Direct Investment, Investment Treaty Arbitration and the Rule of Law’ (2005) 19 *Pacific McGeorge GBDLJ* 337.

394. UNCTAD, *World Investment Report 2003* (UNCTAD: Geneva, 2003) at 89 [WIR 2003]. This conclusion is based on a 1998 aggregate statistical analysis conducted by UNCTAD. See also M. Hallward-Driemeier, ‘Do Bilateral Investment Treaties Attract Foreign Direct Investment? Only a Bit ... and They Could Bite’, World Bank Policy Research Working Paper Series No. 3121. Online: <<http://ssrn.com/abstract=636541>>; S. Rose-Ackerman & J. Tobin, ‘Foreign Direct Investment and the Business Environment in Developing Countries: The Impact of Bilateral Investment Treaties’, Yale Law & Economics Research Paper No. 293, May 2, 2005. Online: <http://ssrn.com/abstract=557121> [Rose-Ackerman & Tobin, ‘Foreign Direct Investment’]; and J.W. Yackee, ‘Sacrificing Sovereignty: Bilateral Investment Treaties, International Arbitration, and the Quest for Capital’ (2006) USC CLEO Research Paper No. C06-15. Online: <<http://ssrn.com/abstract=950567>>. Also see R. Bubb & S. Rose-Ackerman, ‘BITs and Bargains: Strategic Aspects of Bilateral and Multilateral Regulation of Foreign Investment’ (2007) 27 *IRLE* 291.

395. WIR 2003, *ibid.* at 91.

396. J. Salacuse & N. Sullivan, ‘Do BITs Really Work: An Evaluation of Bilateral Investment Treaties and their Grand Bargain’ (2005) 46 *HJIL* 67; E. Neumayer & L. Spess, ‘Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?’ (2005) 33 *WD* 1567; P. Egger & M. Pfaffermayr, ‘The Impact of Bilateral Investment Treaties on

relationship remain disputed.<sup>397</sup> For example, despite the fact that Brazil has ratified neither a BIT nor the ICSID Convention, it was the largest recipient of FDI in South America in 2005.<sup>398</sup> Nevertheless, even if empirical evidence of a causal relationship is inconclusive, there remains strong competitive pressure for developing states to enter into IIAs and thereby signal to foreign investors that an enabling environment for foreign investment exists.<sup>399</sup> In addition, firms from developing states are increasingly investing abroad, providing an incentive for these states to enter into IIAs to protect their nationals' FDI. This trend will likely continue as more developing states become FDI exporters.<sup>400</sup>

**§1.49 Critiques of IIAs** Criticisms of IIAs by NGOs and academics are wide ranging.<sup>401</sup> Some liken IIAs to a neo-imperialist regime designed to protect multinational capital,<sup>402</sup> or a form of global economic constitutionalism that subverts democratic decision making.<sup>403</sup> Other critics re-assert the Calvo Doctrine and reject the development of international standards and adjudication in the area of investment. There are also focused legal critiques about the scope of investment guarantees and the investor-state arbitration process.<sup>404</sup> These critiques typically

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Foreign Direct Investment' (2004) 32 JCE 788 and S. Kim, 'Bilateral Investment Treaties, Political Risk, and Foreign Direct Investment' (2006), online: <<http://ssrn.com/abstract=909760>>.

397. S. Rose-Ackerman & J. Tobin, 'When BITS Have Some Bite: the Political-Economic Environment for Bilateral Investment Treaties' (2006), online: <[http://law.yale.edu/documents/pdf/When\\_BITS\\_Have\\_Some\\_Bite.doc](http://law.yale.edu/documents/pdf/When_BITS_Have_Some_Bite.doc)> [Rose-Ackerman & Tobin, 'When BITS Have Some Bite']. The authors find, in contrast to their earlier paper, *supra* note 394, that there is a positive relationship between BITS and FDI. However, the marginal impact of BITS decreases as the number of BITS worldwide grows. The study also highlights the importance of the political, economic and institutional features of the host state.
398. WIR 2006, *supra* note 297 at 69.
399. Z. Elkins, A. Guzman & B. Simmons, 'Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000', UC Berkeley Public Law Research Paper No. 578961, online: <<http://ssrn.com/abstract=578961>>. On the motivations for signing IIAs, see A. Guzman, 'Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of BITS' (1998) 38 VJIL 639 and L. Swenson, 'Why Do Developing Countries Sign BITS' (2005) UCDJILP 131.
400. See IIA Monitor No. 3 (2007), *supra* note 344 at 4, highlighting that as of Jun. 2007, 27% of BITS are between developing states. See also WIR 2006, *supra* note 297 at 228 highlighting the expansion of FDI from developing states.
401. See J. Atik, 'Legitimacy, Transparency and NGO Participation in the NAFTA Chapter 11 Process' in T. Weiler, ed., *supra* note 327 at 135, for an overview of the concerns and issues. Also see M. Sornarajah, 'A Coming Crisis: Expansionary Trends in Investment Treaty Arbitration' in K. Sauvant, ed., *supra* note 5 at 39 and Van Harten, *supra* note 5.
402. S. Gill, 'Globalisation, Market Civilisation, and Disciplinary Neoliberalism' (1995) 24 Millennium 399 and K. Jayasuriya, 'Globalization, Sovereignty, and the Rule of Law: From Political to Economic Constitutionalism' (2001) 8 Constellations 442.
403. See D. Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (New York: Cambridge University Press, 2008).
404. The International Institute for Sustainable Development (IISD) has published a number of reports on the IIA regime raising concerns about IIAs. IISD's early work focused primarily on NAFTA investment obligations. For example, see H. Mann, *Private Rights, Public*

highlight three core concerns.<sup>405</sup> The first is that investment liberalization and treatment standards are too wide and indeterminate and their interpretation has been too expansive and pro-investment. The second broad critique focuses on the process of investor-state arbitration.<sup>406</sup> It is argued that investor-state arbitration is an inappropriate mechanism for what are, in essence, public regulatory disputes. Some critics recommend the wholesale replacement of investor-state arbitration with an international investment court. Alternatively, it has been suggested that an appeal mechanism should be developed to review IIA awards.<sup>407</sup> Still other critics focus on how arbitration rules and practices need to be changed to make the investor-state arbitration process more transparent and to address conflicts of interest. The third broad critique concerns the asymmetry of obligations in IIAs.<sup>408</sup> IIAs impose obligations on host states with respect to investments and investors; there are no corresponding international obligations imposed on foreign investors in the operation of investments, or on the investors' home state to require that its nationals comply with standards of conduct in their operations abroad. These criticisms are typically linked to debates about corporate social responsibility and whether international economic actors have international obligations.<sup>409</sup>

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*Problems* (Winnipeg: International Institute for Sustainable Development, 2001). Its more recent work focuses more generally on investment and sustainable development including the proposal of a *Model International Agreement on Investment for Sustainable Development*. See online: <<http://iisd.org/investment>>.

405. See generally, Atik, *supra* note 401 and Van Harten, *supra* note 5. For a very critical perspective on IIAs, see S. Anderson & S. Grusky, *Challenging Corporate Investor Rule* (Washington, DC: Institute for Policy Studies and Food and Water Watch, Apr. 2007). For a recent paper highlighting a number of concerns with IIAs, see H. Mann, 'International Investment Agreements, Business and Human Rights: Key Issues and Opportunities' (Feb. 2008), online: <<http://reports-and-materials.org/IISD-Ruggie-Feb-2008.pdf>>.
406. See generally Van Harten, *supra* note 5 for an in-depth analysis of the use of arbitration as a regulatory dispute settlement mechanism between foreign investors and states.
407. For a discussion of this issue see K. Sauvant, *supra* note 5; K. Yannaca-Small, 'Improving The System Of Investor-State Dispute Settlement: An Overview' OECD Working Papers On International Investment Number 2006/1; D. Gantz, 'An Appellate Mechanism for Review of Arbitral Decisions in Investor-State Disputes: Prospects and Challenges' (2006) 39 VJTL 49; S. Franck, 'The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions' (2005) 73 FLR 1521 and S. Franck, 'Integrating Investment Treaty Conflict and Dispute Systems Design' (2007) 92 Minn LR 161.
408. See, for example, IISD's work on a *Model International Agreement on Investment for Sustainable Development*, *supra* note 404.
409. The question whether multinational enterprises have human rights responsibilities has been particularly controversial and is the subject of debate. See *UN Norms on the Responsibilities of Transnational Enterprises and Other Business Enterprises with regard to Human Rights* ECOSOC, Sub-Commission on Promotion and Protection of Human Rights, UN Doc E/CN.4/Sub.2/2003/12/Rev.2 (2003). For a detailed account of the provenance of the norms see D. Weissbrodt & M. Kruger, 'UN Norms on the Responsibilities of Transnational Corporation and Other Business Entities with Regard to Human Rights' (2003) 97 AJIL 901. The norms have been controversial and the ECOSOC has not accepted them. A special representative, John Ruggie, has been appointed to study the matter. See *Report of the Special Representative of the Secretary-General on the Issue of Human Rights and Transnational Corporations and Other Business Entities* (Apr. 2008) UN Doc. A/HRC/8/5. Other recent initiatives include the Global

## V STRUCTURE AND SCOPE OF APPLICATION OF IIAS

**§1.50 The structure of IIAs** IIAs have a recognizable look, starting from their titles, which tend to be similar, and continuing with their structure and content. BITs in particular are often named alike. For example a common title is ‘Treaty between [one contracting party] and [the other contracting party] concerning the encouragement and reciprocal protection of investment.’<sup>410</sup> Preambles are also often similar, providing a short statement of purposes such as ‘desiring’ to promote greater economic co-operation, ‘recognising’ that an agreement on the treatment of investment will stimulate the flow of private investment, and ‘agreeing’ in this context on the importance of a stable framework for investment.<sup>411</sup> The actual content of IIAs also follows a pattern.<sup>412</sup> It typically includes: (i) initial provisions establishing the scope of coverage of the IIA defining who are the ‘investors’ and what are the ‘investments’ benefiting from treaty protections, as well as often defining the notion of territory of the contracting parties, so that investments made in that territory of a contracting party by investors of another contracting party qualify as protected ‘foreign’ investments; (ii) clauses establishing the substantive protections accorded to those investors and/or investments; (iii) dispute resolution mechanisms both for disputes between the contracting parties and between an investor of a contracting party and another contracting party (investor-state arbitration); (iv) provisions on subrogation and on the preservation of more favourable rules to the investors (the preservation of rights clause);<sup>413</sup> and (v) final provisions on entry into force and termination. The following sections briefly highlight some of the above issues as an introduction to the substantive protections analysis addressed in this book.<sup>414</sup>

**§1.51 The scope of application – investment** IIAs usually provide a definition of what constitutes an investment protected by the treaty in their initial clauses. Definitions are broad, often referring to ‘every kind of asset’<sup>415</sup> or ‘every kind of investment in the territory,’<sup>416</sup> and then adding a specific non-exhaustive list of

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Compact, which the UN Secretary General launched in 2000, and the Principles for Responsible Investment launched in 2005. See A. Newcombe, *supra* note 391. See *infra* Chapter 2, §2.25, and Chapter 6, §6.11, on human rights in the IIA context.

410. For example, 1994 US Model BIT.

411. *Ibid.* On the interpretive issues that arise from IIA titles and preambular language, see *infra* Chapter 2, §2.29, Chapter 3, §3.5, and Chapter 6, §6.20 and §6.30.

412. For an overview of IIA practice, see the three comprehensive studies cited *supra* note 239

413. See *infra* Chapter 6, §6.48, and Chapter 9, §9.28.

414. The sections below are developed on the basis of the introductory work to IIAs in N. Blackaby & L. Paradell, ‘Investment Treaty Arbitration’ in *Bernstein’s Handbook of Arbitration Practice* (London: Sweet & Maxwell, 2003) part 10.

415. Art. 1(a), UK-USSR (now UK-Russia) (1989), and Art. 1(6), ECT.

416. Art. I(1)(a), Argentina-US (1991).

examples. Typical in this respect is UK-USSR (1989), which provides in Article 1(a):

the term 'investment' means every kind of asset and in particular, though not exclusively, includes:

- (i) movable and immovable property and any other related property rights such as mortgages;
- (ii) shares in, and stock, bonds and debentures of, and any other form of participation in, a company or business enterprise;
- (iii) claims to money, and claims to performance under contract having a financial value;
- (iv) intellectual property rights, technical processes, know-how and any other benefit or advantage attached to a business;
- (v) rights, conferred by law or under contract, to undertake any commercial activity, including the search for, or the cultivation, extraction or exploitation of natural resources.

With small variations, similar definitions bringing into the scope of treaties almost all possible forms of investment are found in most IIAs. These definitions cover direct, as well as indirect, investments and modern contractual and other transactions having economic value.<sup>417</sup> This is confirmed by decisions of tribunals in IIA arbitrations. In *Fedax N.V. v. Venezuela*, for example, the tribunal found that promissory notes issued by Venezuela, and acquired by the claimant from the original holder in the secondary market by way of endorsement, were an investment under Netherlands-Venezuela (1991).<sup>418</sup> The tribunal engaged in an extensive analysis of the notion of investment under IIAs, which it refused to limit to the classic forms of direct investment, i.e., 'the laying out of money or property in business ventures, so that it may produce a revenue or income,' as argued by the respondent state. Further, another ICSID tribunal has found that transactions that, taken into isolation might not qualify as investments, may nevertheless be so considered if the overall operation of which they are part, or to which they are connected, constitutes an investment.<sup>419</sup>

While extensive, the notion of investments obviously has limitations. In 1985, for example, the ICSID Secretary-General refused to register a case on the basis that the dispute related to a mere commercial sale and could not be qualified

417. See A. Parra, 'The Scope of New Investment Laws and International Instruments,' in R. Pritchard, ed., *Economic Development, Foreign Investment and the Law* (The Hague: Kluwer, 1996) at 35. UNCTAD, *Scope and Definition*, UNCTAD Series on issues in international investment agreements (New York and Geneva: United Nations, 1999) UNCTAD/ITE/IIT/11 (Vol. II).

418. *Fedax N.V. v. Venezuela* (Decision on Jurisdiction, 11 Jul. 1997) at para. 19 *et seq.* The definition contained in the applicable BIT was substantially the same as the one quoted above.

419. *Československá Obchodní Banka, A.S. v. Slovak Republic* (Decision of the Tribunal on Objections to Jurisdiction, 24 May 1999) at para. 72 *et seq.*

as an investment.<sup>420</sup> Another example is the award declining jurisdiction in *Mihaly International Corporation v. Sri Lanka*. There the tribunal found that expenses incurred in preparation for obtaining a public contract, including sums spent in planning the financial and economic modeling necessary for the negotiation and finalization of the contract, were not an investment under the applicable BIT. The tribunal attached great importance to the fact that the respondent state had taken care to point out, throughout the negotiations, that these created no rights and obligations between the parties.<sup>421</sup> Thus, the claimant had not acquired any asset, right or interest that could fall within the notion of investment. It remains to be seen whether a different conclusion could be reached in different circumstances, for example where expectations are raised or not adequately averted by a negotiating state.

An investment is protected under a treaty, obviously, only if made by a covered investor. The point is clear and thus very few treaties provide this expressly. The exception are US BITs which provide that they apply to investments ‘owned or controlled directly or indirectly’ by covered investors.<sup>422</sup> While the principle is incontrovertible, its practical application, i.e., determining whether a particular investment can be regarded as belonging to a given investor, may be a difficult question in certain circumstances. In *Philippe Gruslin v. Malaysia*, for example, the question arose whether investors in an investment fund that held foreign shares could actually be said to own or control an investment in the territory of the foreign state where the shares were traded, so as to benefit from the BIT between that state

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420. ICSID 1985 Annual Report at 6. It is important to distinguish between the meaning of investment for the purposes of ICSID jurisdiction under Art. 25, ICSID Convention, and the definition of investment for the purposes of an IIA. It is argued that the fact that an asset qualifies as an investment under the IIA in question does not necessarily mean that it qualifies as an investment for the purposes of the ICSID Convention. Further, there is conflicting ICSID jurisprudence on the meaning of investment under the ICSID convention. In *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Morocco* (Decision on Jurisdiction, 23 Jul. 2001) the tribunal set out a test based on: (i) the existence of contributions in capital or otherwise; (ii) a certain duration; (iii) an element of risk; and added that ‘the contribution to the economic development of the host state of the investment as an additional condition’ for there being an investment for the purposes of the ICSID Convention (para. 52). In contrast, in *L.E.S.I. S.p.A. et ASTALDI S.p.A. v. Algeria* (Decision, 12 Jul. 2006) another ICSID tribunal found that there is no requirement under the ICSID Convention for the investment to promote economic development (para. 72). The *ad hoc* annulment committee in *Mr. Patrick Mitchell v. Congo* (Decision on the Application for the Annulment of the Award, 1 Nov. 2006) followed *Salini* and stated that the ‘existence of a contribution to the economic development of the host State as an essential – although not sufficient – characteristic’ of an investment for the purposes of the ICSID Convention (para. 33). For discussion of Art. 25, ICSID Convention, see Schreuer and other reference sources, *supra* note 154 at 82 *et seq.* For an analysis of the conflicting ICSID jurisprudence, see D. Krishan, ‘A Notion of ICSID Investment’ in T. Weiler, ed., *Investment Treaty Arbitration: A Debate and Discussion* (New York: Juris, 2008).

421. *Mihaly International Corporation v. Sri Lanka* (Award, 15 Mar. 2002) at paras 58-61.

422. See Art. I(1)(a), Argentina-US (1991).

and the investor's state.<sup>423</sup> The question was difficult. Formally, investment funds do not 'own' investments but just 'manage' them on behalf of their unit-holders which, on the other hand, cannot be said to control them in any meaningful (perhaps proprietary) way. Further, the case had huge potential implications. A decision favourable to the investor could have opened the door to innumerable BIT claims brought by countless disappointed partakers of investment funds, pension funds, or investment savings accounts. Ultimately the tribunal declined jurisdiction on other grounds, leaving the question unanswered.

**§1.52 The scope of application – investors** IIAs typically include also a provision specifying the requirements of nationality, location, place of incorporation, etc., for a person or entity making an investment to be protected by, and thus to be able to rely on, the IIA. Together with the definition of 'investment,' this is usually found in the initial article of the treaty which, *inter alia*, defines who are the 'investors' or 'nationals' benefiting from treaty protections. Although in this, as well as in other issues, treaties vary substantially, the following provision of Bolivia-Netherlands (1992) is quite representative:

For the purposes of the present agreement:

[ ... ]

- (b) the term 'nationals' shall comprise with regard to either Contracting Party:
  - (i) natural persons having the nationality of that Contracting Party in accordance with its laws;
  - (ii) without prejudice to the provisions of (iii) hereafter, legal persons constituted in accordance with the law of that Contracting Party;
  - (iii) legal persons controlled directly or indirectly, by nationals of that contracting Party, but constituted in accordance with the law of the other Contracting Party.

Natural persons that are nationals of a state party to the IIA, and entities incorporated or constituted under the laws of such state, are thus able to rely on the treaty against the other state party to it. Some IIAs add the requirement that entities also have their seat and/or actually carry out business in the relevant state.<sup>424</sup>

Most IIA may be relied upon either by the entity that makes the investment directly or, when this is a separate host state entity, by the direct or indirect foreign controller of that entity, or the controlled entity itself. In this way, the obligation frequently imposed by host states on foreign investors to incorporate

423. *Philippe Gruslin v. Malaysia* (Award, 27 Nov. 2000).

424. See Art 1(b), Argentina-Netherlands (1992): 'the term "investor" shall comprise with regard to either Contracting Party: .... (ii) ... legal persons constituted under the law of that Contracting Party and actually doing business under the laws in force in any part of the territory of that Contracting Party in which a place of effective management is situated; and (iii) legal persons, wherever located, controlled, directly or indirectly, by nationals of that Contracting Party.'

a local entity as a vehicle for their investment does not weaken the effectiveness of the IIA, which can still be relied upon by the controlling foreign investor, or its local subsidiary. Some treaties go further, and encompass investing entities *wherever located* which are directly or indirectly controlled by investors of a state party to the IIA.<sup>425</sup> Control, under international law, is a flexible and broad concept, referring not only to majority shareholding, but also to other ‘reasonable’ criteria such as managerial responsibility, voting rights, nationality of board members, etc.<sup>426</sup>

In permitting to look behind strict formal criteria, to determine an entity’s ‘nationality’ on the basis of where control or ownership is located, these IIA provisions may extend treaty coverage more vastly than it would appear at first sight. The complexities of some corporate organizations and investment vehicles may effectively allow companies to claim several foreign nationalities. Some IIAs appear to restrain this laxity by specifying that their protections extend to ‘effectively’ controlling entities.<sup>427</sup> The question arises whether a similar effective control test may be read into treaty provisions on foreign control, even absent explicit language. There is still no reported case law on this point. Nor is there a clear indication of the criteria that may be used in defining the required level of control.<sup>428</sup> IIA tribunals so far have been flexible and willing to uphold the rights of any legitimate investor under an applicable treaty, including where the investor is an intermediate company in the investment structure.<sup>429</sup> Some tribunals have expressed concern that this allows for ‘treaty shopping,’ i.e., it permits claimants to select as the ‘investor’ a company in the investment structure (or even constitute a new company, often a ‘shell’) simply to benefit from the provisions of a particular IIA.<sup>430</sup>

425. See, *ibid.* In any case, the foreign shareholder of a host state or third country entity would normally be able to invoke the treaty at least in relation to its participation in that entity, assuming that participation qualifies as a protected investment. See *CMS Gas Transmission Company v. Argentina* (Decision of the Tribunal on Objections to Jurisdiction, 17 Jul. 2003).

426. *Aguas del Tunari, S.A. v. Bolivia* (Decision on Respondent’s Objections to Jurisdiction, 21 Oct. 2005) at paras 225 *et seq.*; *Autopista Concesionaria de Venezuela, C.A. v. Venezuela* (Decision on Jurisdiction, 27 Sep. 2001) [*Autopista*] at paras 110-125; and *Vacuum Salt Products Ltd. v. Ghana* (Award 16 Feb. 1994) at paras 38 *et seq.*

427. See Art. 1(2), Argentina-France (1991), which reads: ‘The term “investors” means: ... c) legal persons effectively controlled directly or indirectly by nationals of one of the contracting Parties, or by legal persons having their seat on the territory of one of the contracting Parties and constituted in conformity with its legislation’ (authors’ translation from French original).

428. In a non-IIA case, an ICSID tribunal has refused the notion of effective control, suggesting instead that any reasonable criteria of control is valid under international law. The tribunal seemed to suggest, however, that a more restrictive approach could be applied in certain circumstances to prevent abuse by ‘corporations of convenience exerting a purely fictional control for jurisdictional purposes.’ See *Autopista*, *supra* note 426 at paras 110-125.

429. *Ibid.*

430. See *Saluka Investments BV v. Czech Republic* (Partial Award, 17 Mar. 2006) at para. 240: ‘The Tribunal has some sympathy for the argument that a company which has no real connection with a State Party to a BIT, and which is in reality a mere shell company controlled by another

**§1.53 Dispute settlement** A few early IIAs do not provide any direct right of investor action at all,<sup>431</sup> or they limit access to arbitration to certain specific treaty breaches, such as issues of expropriation and repatriation of profits.<sup>432</sup> The great majority of IIAs, however, do provide aggrieved investors with a direct right to resort to arbitration with regard to any disputes arising from alleged treaty breaches or more generally with regard to investments.

Some treaties contain the so-called ‘fork in the road’ provision, that is, the stipulation that if the investor submits a dispute to the local courts of the host state, or to any other agreed dispute settlement procedures, it loses the right to submit it to arbitration. This provision is, for example, contained in Article VII(2) and (3), Argentina-US (1991):

In the event of an investment dispute, the parties to the dispute should initially seek a resolution through consultation and negotiation. If the dispute cannot be settled amicably, the national or company concerned may choose to submit the dispute for resolution:

- (a) to the courts or administrative tribunals of the Party that is a party to the dispute; or
- (b) in accordance with any applicable, previously agreed dispute-settlement procedures; or
- (c) in accordance with the terms of paragraph 3.

Provided that the national or company concerned has not submitted the dispute for resolution under ... (a) or (b) [above] and that six months have elapsed from the date on which the dispute arose, the national or company concerned may choose to consent in writing to the submission of the dispute for settlement by binding arbitration ...

The case law seems to suggest that IIA arbitration would not be precluded by the submission to domestic courts of grievances, framed as breaches of contract, arising out of the same host state acts,<sup>433</sup> in order to constitute a ‘fork in the road’ choice, it would seem to be required that the court action raised the same IIA

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company which is not constituted under the laws of that state, should not be entitled to invoke the provisions of that BIT. Such a possibility lends itself to abuses of the arbitral procedure, and to practices of “treaty shopping” which can share many of the disadvantages of the widely criticized practice of “forum shopping”. Although the tribunal found that Saluka fell within the broad definition of ‘investor’ provided by Czechoslovakia- Netherlands (1991), the tribunal’s expression of ‘sympathy’ is a hallmark of the increasing concern displayed by IIA tribunals about ‘treaty shopping’ by claimants. See also the dissenting opinion of the President of the tribunal in *Tokios Tokelès v. Ukraine* (Decision on Jurisdiction, 29 Apr. 2004) and *The Rompetrol Group N.V. v. Romania* (Decision on Respondent’s Preliminary Objections on Jurisdiction and Admissibility, 18 Apr. 2008) at paras 79 *et seq.*

431. See Germany-Pakistan (1959).

432. See Art. 8(1), UK-USSR (1989).

433. *Compañía de Aguas del Aconquija, S.A. & Compagnie Générale des Eaux v. Argentina* (Award, 21 Nov. 2000) at para. 55.

claims, e.g., breach of ‘fair and equitable’ treatment or no expropriation without compensation, that are the subject of the IIA arbitration.<sup>434</sup>

A similar approach has been applied to the question of whether the investor may be held to have waived its right to resort to IIA arbitration, simply by agreeing, in a contract with the host state, to a dispute resolution clause providing for local or other international remedies. Tribunals have held that as long as the arbitration claims allege a cause of action under the treaty, they are not subject to the jurisdiction of the local courts as provided by the contract.<sup>435</sup>

Typically IIA dispute resolution clauses establish the conditions that must be fulfilled before such arbitration pursuant to the IIA can be commenced. These can vary widely from treaty to treaty but typically include a negotiation or consultation period, usually between three months and six months from the date when the dispute arose or was formally notified by the investor to the host state authorities. For example, Article 9, Bolivia-Netherlands (1992) provides, in the relevant part, as follows:

For the purpose of resolving disputes that may arise from investments between one Contracting Party and a national of the other Party to the present Agreement, consultation will be held with a view to settling amicably the conflict between the parties to the dispute.

If a dispute cannot be settled within a period of six months from the date on which the interested national shall have formally notified it, the dispute shall, at the request of the interested national, be submitted to an arbitral tribunal.

Usually there are no required formalities to be followed either in the notification or eventual ensuing negotiations.<sup>436</sup> As a matter of practice the negotiating periods are triggered by letters to the authorities of the host state (e.g., the Head of State and Government and the Minister in charge of foreign investment) notifying the existence of the dispute, a basic summary of its nature and a request to commence negotiations (the so-called ‘trigger’ letter). Upon expiry of the negotiation period, the arbitration may be instituted. In *Ronald S. Lauder v. Czech Republic*, the tribunal rejected a formalistic approach to the negotiation period requirement of the applicable BIT. The tribunal found that, provided the host state had an opportunity

434. See *Eudoro Armando Olguín v. Paraguay* (Award, 26 Jul. 2001) at para. 30.

435. For the first decision on this point, see *Lanco International Inc. v. Argentina* (Preliminary Decision on the Jurisdiction of the Arbitral Tribunal, 8 Dec. 1998) at paras 31 *et seq.* There is abundant case law in this regard. See *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Morocco* (Decision on Jurisdiction, 23 Jul. 2001) at paras 59-63; *CMS Gas Transmission Company v. Argentina* (Decision of the Tribunal on Objections to Jurisdiction, 17 Jul. 2003) at paras 72 and 76; *Azurix Corp v. Argentina* (Decision on Jurisdiction, 8 Dec. 2003) at paras 76-77, and generally paras 75-85; *SGS Société Générale de Surveillance S.A. v. Pakistan* (Decision of the Tribunal on Objections to Jurisdiction, 6 Aug. 2003) at para. 154; *Impregilo S.p.A. v. Pakistan* (Decision on Jurisdiction, 22 Apr. 2005) at paras 286-290; and *Eureko B.V. v. Poland* (Partial Award, 19 Aug. 2005) at paras 92-114. On the admissibility issues that arise in umbrella clause claims see *infra* Chapter 9, §9.24-9.25.

436. See, however, Art. 9.1, BLEU-Venezuela (1998), providing for a ‘sufficiently detailed memorandum to be presented by the investors to the state with its formal notification of the dispute.

to engage in negotiations, the investor could initiate arbitration without waiting until the end of the negotiation period.<sup>437</sup>

Some IIAs require the aggrieved investor to make use of host state courts and only subsequently, if the courts do not issue a decision within the specified period of time, or the decision is rendered but the dispute subsists, the investor is entitled to resort to arbitration. This sort of provision has been by-passed in a number of cases on the basis of most-favoured-nation arguments,<sup>438</sup> and in one case on the basis of the host state measures arguably foreclosing local remedies.<sup>439</sup>

IIAs often present the investor with a choice of dispute resolution mechanisms. This choice usually includes more than one type of arbitration, alongside local court litigation and other agreed dispute settlement procedures. By way of example, Article IX, Azerbaijan-US (1997), provides:

- (2) A national or company that is a party to an investment dispute may submit the dispute for resolution under one of the following alternatives:
  - (a) to the courts of administrative tribunals of the Party that is a party to the dispute; or
  - (b) in accordance with any applicable, previously agreed dispute-settlement procedures; or
  - (c) in accordance with the terms of paragraph 3.
- (3) Provided that the national or company concerned has not submitted the dispute for resolution under paragraph 2 (a) or (b), and that three months have elapsed from the date on which the dispute arose, the national or company concerned may submit the dispute for settlement by binding arbitration:
  - (i) to the Centre, if the Centre is available; or
  - (ii) to the Additional Facility of the Centre, if the Centre is not available; or
  - (iii) in accordance with the UNCITRAL Arbitration Rules; or
  - (iv) if agreed by both parties to the dispute, to any other arbitration institution or in accordance with any other arbitration rules.

The institutional form of arbitration, i.e., arbitration under the auspices of an arbitration institution that assists in the initiation of the arbitration, constitution of the tribunal and subsequent proceedings, most frequently mentioned in investment treaties is ICSID arbitration (sometimes referred to just as 'ICSID' or 'the Centre'). In order for ICSID arbitration to be available, the host State and the investor's state must be parties to the ICSID Convention. If only one of the states

437. *Ronald S. Lauder v. Czech Republic* (Final Award, 3 Sep. 2001 at para. 187. See also *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Pakistan* (Decision on Jurisdiction 14 Nov. 2005) at paras 88-103) Cf. *Antoine Goetz et consorts v. Burundi* (Award, 10 Feb. 1999) at paras 91-93; *Generation Ukraine, Inc. v. Ukraine* (Award, 16 Sep. 2003) at paras 14.1-14.6 and *Western NIS Enterprise Fund v. Ukraine* (Order, 16 May 2006).

438. See *infra* Chapter 5, Part III.

439. *BG Group Plc. v. Argentina* (Final Award, 24 Dec. 2007) at paras 147-157.

is party to the Convention, then the ICSID Additional Facility is available, and sometimes also offered in investment treaties as an option.<sup>440</sup> Two other forms of institutional arbitration are also often mentioned. These are arbitration under the International Chamber of Commerce Rules of Arbitration (usually abbreviated ‘ICC Arbitration’), and arbitration under the Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce (principally in investment treaties implicating Eastern European countries). Alongside institutional arbitration, investment treaties usually provide also for the possibility of *ad hoc* arbitration, i.e., arbitration without an administering institution. The most common form of *ad hoc* arbitration is arbitration under the 1976 Arbitration Rules of the United Nations Commission on International Trade Law (UNCITRAL), which are designed for *ad hoc* or non-institutional proceedings.

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440. See *supra* §1.21.

