Finally, the most difficult subject, as discussed above, has concerned the quantum of compensation. Given the availability of the Security Account, the suggestion that 'appropriate compensation' called for something less than full compensation was not accepted. In a revolution by a poor country with no substantial assets, 'exceptional circumstances' might call for something less than full compensation or for stretched out payments.[70] That was not the case here. Just compensation seems to call for full value. For a going concern, i.e. a business that has a known market and a record of performance, full value is determined not by historical cost or replacement cost of physical assets, but on the basis of reasonable expectation of future earnings at the time of taking. There appears to be agreement with the goal stated in the *Chorzow Factory* case,[71] to place the prior owner in the position it would have been in had the taking not occurred, but there is skepticism about such methods as Discounted Cash Flow Analysis, i.e. the effort to establish present value on the basis of future earnings, because it requires speculation both about future earnings and about the interest or discount rate used.[72]

17.3 Bilateral Investment Treaties

(a) Introduction: The Spread of BITs

A striking illustration of the changing perception of the rules of international investment has been the growth—one could almost say explosion—of bilateral investment treaties or BITs. The first such treaty was concluded between the Federal Republic of Germany and Pakistan in 1959. Since then Germany has entered into over 100 BITs; France and Switzerland soon followed with similar programmes, and all the Western European states as well as the United States have made BITs an element of their foreign economic policy.[73] As of 2006, some 2,400–2,600 bilateral investment treaties were in effect, most between developed and developing countries but a substantial number between developing countries *inter se*.[74] Overall, at

[70] See the discussion in the *Chase Manhattan* case, Ch. 16, Sect. 16.3(b)(2), at n. 115; also the discussions throughout Ch. 15, esp. in Sect. 15.5, concerning the various resolutions of the UN General Assembly.

[71] See Ch. 15, Sect. 15.3(a), at nn. 17–19.

[72] See, in particular *Amoco International Finance Corporation v Iran*, 15 Iran-U.S. C.T.R. 189, esp. 258–260 (14 July 1987). In that case, concerning claimant's rights to exploit natural gas resources, the Tribunal wrote:

> One of the best settled rules of the law of international responsibility of States is that no reparation for speculative or uncertain damages can be awarded.

Note the contrast between this decision by Chamber Three, with the statement by Chamber Two two years later in *Phillips Petroleum*, at n. 61 *supra*.

[73] For a book-length study of BITs, including a history of their development, see Rudolf Dolzer and Margrete Stevens, *Bilateral Investment Treaties* (1995).

[74] It is difficult to arrive at a precise figure for the number of BITs, since some sources list all BITs signed, and others list only agreements for which ratifications have been completed

least 155 countries were parties to BITs, covering every continent. Just as the Latin American countries were slow to accept the ICSID Convention,[75] so they were slow to accept bilateral investment treaties. By the turn of the Millenium, however, nearly all the states of Latin America, including Cuba, had concluded one or more BITs.[76]

(b) The Content of BITs

Considering the large number of BITs in force, they are remarkably similar. BITs generally start with a preamble that recites the desire to promote greater economic cooperation between the parties, and to encourage the flow of private capital and create conditions conducive to such flow. The definitions article typically contains a broad definition of investment or covered investment, and makes clear, as in the ICSID Convention and also in the MIGA Convention,[77] that whether or not the investment is held by an entity incorporated in the host country, if it is owned or controlled by nationals of the other party, it is entitled to the protections afforded by the treaty.

1. *Admission of the Investment*

All the BITs appear to cover admission or entry into the host country. Some treaties, including all those entered into by the United States, require national treatment on conditions for entry, with the possibility of reserving certain sectors, such as airlines, telecommunications, and financial institutions from the national treatment undertaking. Those treaties that do not contain a national treatment requirement for entry typically provide that investments of the other contracting party will be admitted in accordance with each party's legislation, rules, and regulations.[78]

Some BITs, notably the recent treaties concluded by the United States, including the NAFTA, have introduced a new element into the international law of investment—a prohibition, or partial prohibition, of so-called performance requirements. The recent US BITs provide that neither Party shall mandate, as a condition for the establishment, acquisition, expansion, or operation of a covered investment any of six performance requirements:

and exchanged by both parties. The UNCTAD World Investment Report 2006 reports a total of 2,495 BITs as of year-end 2005; other sources place the number somewhat lower. The ICSID collection on its website ends in 1996.

[75] See Sect. 17.1(d) *supra*.

[76] For present purposes, the investment chapter of the North American Free Trade Agreement may be discussed together with BITs, though it has three parties, two developed and one developing. The substantive provisions of NAFTA Ch. 11 closely track the typical BITs, and tribunals interpreting BITs have drawn freely on decisions and awards in NAFTA cases.

[77] See Sects. 17.1 (ICSID) and 17.4 (MIGA).

[78] See e.g. the model Netherlands BIT, Article 2; the model Swiss BIT, Article 2(1); the model British BIT, Article 24(1), all reproduced in Annex I of Dolzer and Stevens, *Bilateral Investment Treaties*, n. 73 *supra*.

(a) to achieve a particular level or percentage of local content or to give a preference to products of services of domestic content or source;
(b) to limit imports in relation to a particular volume of production, exports, or foreign exchange earnings;
(c) to export a particular level or percentage of products or services;
(d) to limit sales in the Party's territory in relation to a particular volume or value of production, exports, or foreign exchange earnings;
(e) to transfer technology to a national company in the Party's territory; or
(f) to carry out a particular type, level or percentage of research and development in the party's territory.[79]

The standard American BITs provide that the prohibition on these performance requirements does not extend to conditions for receipt (or continued receipt) of an advantage, such as a subsidy, tax deferral, land grant, or similar benefit from the government. The North American Free Trade Agreement prohibits substantially the same performance requirements, but except for the requirement to export a given level or percentage of goods and the requirement to transfer technology, the prohibition applies whether or not it is a condition for an advantage.

2. *Fair and Equitable Treatment*

Whether or not the entry requires special permission, once an investment is admitted, it is entitled under virtually all the treaties to 'fair and equitable treatment' and 'full protection and security.' Until 2004, the United States BITs, including the Investment Chapter of the North American Free Trade Agreement, added 'as required by [or no less favourable than required by] international law'.[80] At a minimum, 'fair and equitable treatment' means no discrimination by nationality or origin, in respect of such matters as access to local courts and administrative bodies, applicable taxes, and

[79] Compare the limited steps on this subject taken in the Uruguay Round of Trade Negotiations, stimulated by the dispute about performance requirements between the United States and Canada, which led to the Agreement on Trade-Related Investment Measures (the TRIMs Agreement), Ch. 5, Sect. 5.6.

[80] One of the participants in the United States programme of drafting and negotiating BITs, pointed out that some of the earlier treaties of Friendship Commerce and Navigation had avoided reference to international law standards, apparently from fear on the part of the treaty drafters that, given the contemporary controversy over the content of international investment law, specific reference to international standards might undercut superior treaty language.

> The incorporation of international law in the BITs, [he continued] reflects a more optimistic view of its current state of health. The framers of the model BIT believed that reference to international law would add to, rather than detract from, the bundle of rights set forth in the treaty.

K. Scott Gudgeon, 'United States Bilateral Investment Treaties: Comments on their Origin, Purposes, and General Treatment Standards', 4 Int'l Tax & Business Law 105, 124–125 (1986).

administration of governmental regulations. But the reason for the clause, separate from the MFN and national treatment requirements, is to make clear that a minimum international standard of behaviour applies to treatment of foreign investment even if no discrimination can be shown. For instance, in the *Metalclad* case,[81] an arbitration under the North American Free Trade Agreement between a US-based firm and Mexico, the investor had received a permit from the national government to construct a facility for disposal of hazardous waste, and had spent 13 months and 20 million dollars constructing the plant when the local authorities announced that their permission was required and would not be forthcoming. The arbitral tribunal concluded:

> Mexico failed to assure a transparent and predictable framework for [the investor's] business planning and investment. The totality of these circumstances demonstrates a lack of orderly process and timely disposition in relation to an investor of a party acting in the expectation that it would be treated fairly and justly in accordance with the NAFTA.[82]

Accordingly, the Tribunal held that Mexico had violated the requirement of fair and equitable treatment in Article 1105 of the NAFTA.[83]

In July 2001, as all three state-Parties to the NAFTA found themselves in the role of defendant in investor-State claims and while several arbitrations under the investment chapter were in progress, the Free Trade Commission created by the NAFTA, i.e. the trade ministers of the three state-Parties, issued the following 'interpretation':

Minimum Standard of Treatment in Accordance with International Law

1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.
2. The concepts of 'fair and equitable treatment' and 'full protection and security' do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.

[81] *Metalclad Corporation v United Mexican States*, Final Award, 30 Aug 2000, ICSID Case No. ARB(AF)/97/1.

[82] Id. at para. 99.

[83] The tribunal in the *Metalclad* case also found the actions to constitute an indirect expropriation, as discussed in Sect. 17.3(b)(4) *infra*. The award was subsequently set aside in part by a court in British Columbia on the ground of excess of jurisdiction, after which the parties reached a settlement. See *United Mexican States v Metaclad Corp.*, 2001 BCSC 664 (2 May 2001).

> 3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).

Subsequent BITs concluded by the United States, as well as the U.S. prototype BIT, have repeated this formulation, thus apparently transforming the minimum standard of international law from the floor to the ceiling of what is required of host states, and creating a possible discrepancy between the treaties adopting this formula and the large number of BITs with the simpler formulation quoted above.[84] As of mid-year 2007, no court or arbitral tribunal had ruled on a claim involving the revised formulation, and in particular whether the effect of the revised formulation is to freeze the standard of '*customary* international law' at any particular date. Several NAFTA tribunals, however, have continued to refer to 'general principles of law' or comparable phrases, suggesting that in contrast to point (3) applicable to treaties, point (1) of the Interpretation or comparable provisions in BITs need not preclude developing concepts of international law from being considered as a source of law in investor/state controversies.[85]

3. *'Full protection and security'*

BITs seem to require the government of the host state not only not to attack the facilities or personnel of the investor, but to defend the investor or investment against others, including, for instance, rebel forces. In an ICSID arbitration initiated under the BIT between the United Kingdom and Sri Lanka, claimant asserted that its shrimp farm was destroyed during a military operation conducted by the security forces of Sri Lanka against installations reported to be used by local rebels. Following an evidentiary hearing, the tribunal was unable to conclude that the government security forces were themselves the actors of the destruction. But a majority of the tribunal did conclude that the governmental authorities failed to take the appropriate precautionary measures in view of fighting in the area.

> Therefore, and faced with the impossibility of obtaining conclusive evidence about what effectively caused the destruction of the farm premises during the period in which the entire area was out of bounds under the exclusive control of the

[84] For a sharp critique of this change by the former President of the World Court, see Stephen M. Schwebel, 'The United States 2004 Model Bilateral Investment Treaty: An Exercise in the Regressive Development of International Law,' in *Global Reflections on International Law, Commerce and Dispute Resolution* (ICC Publ. 693 2005). See also *Compañia de Aguas del Conquija S.A. and Vivendi Universal v Argentine Republic*, ICSID Case No. Arb/97/3, Award on Remand (20 Aug 2007) para. 7.4.7.: 'The Tribunal sees no basis for equating principles of international law with the minimum standard of treatment ... The language of the fair and equitable treatment provision suggests that one should ... look to contemporary principles of international law, not only to principles from almost a century ago.'

[85] See Charles H. Brower, II, 'Why the FTC Notes of Interpretation Constitute a Partial Amendment of NAFTA Article 1105', 5 J. Int'l Arbitration News 2, 8–9 (Summer 2005).

government security force, the Tribunal considers the State's responsibility established...under international law.[86]

4. *Expropriation*

All of the Bilateral Investment Treaties (including as previously noted, Chapter Eleven of the NAFTA) contain provisions on expropriation, in closely parallel, if not identical wording. Expropriation is lawful and not inconsistent with the BITs if it (i) is carried out for a public purpose; (ii) is non-discriminatory; (iii) is carried out in accordance with due process; and (iv) is accompanied by payment of compensation—in some treaties qualified by the word 'just', in most other recent treaties by the traditional 'Hull formula'[87]—'prompt, adequate and effective'. Many of the treaties speak also of 'expropriation or nationalization', of 'expropriation direct or indirect', or 'expropriation through measures tantamount to expropriation' or variations of these terms.[88]

The reason for including 'direct or indirect', 'similar to', or 'tantamount to expropriation' is to confirm or establish that so-called 'creeping expropriation' is included within the provisions on expropriation. The use of these terms, however, has caused major controversy, particularly in disputes brought under the investment chapter of NAFTA, in which investors cite the expropriation text 'No Party [i.e. no host state] may directly or indirectly...take a measure tantamount to nationalization or expropriation' to challenge what the host state regards as an exercise of regulatory or police powers. Investors have argued, in effect, that they are not challenging the state's power to regulate, but if the regulation results in closing down or significantly impairing the investor's business, then compensation is required. The state Parties have replied that while they committed themselves not to expropriate except under the conditions set out in the treaty, they have not agreed to place their regulatory authorities—particularly in connection with management of the environment—under the treaty regime.

In the *Metalclad* case described in the preceding subsection, the NAFTA tribunal concluded that the deprivation of the right to operate the investor's hazardous waste disposal facility after it had been built constituted not only a failure to accord fair and equitable treatment under NAFTA Article 1105, but also expropriation under Article 1110. The Tribunal wrote:

> [E]xpropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with

[86] *Asian Agricultural Products Ltd. v Republic of Sri Lanka*, Award of 27 June 1990, paras. 85–66, repr. in 30 Int'l Legal Materials 577 (1991), 4 ICSID Rep. 246 (1997).

[87] See Ch. 15, Sect. 15.3(b).

[88] For samples of the variations, see Dolzer and Stevens, *Bilateral Investment Treaties*, n. 73 *supra*, 99–101.

the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.

By permitting or tolerating the conduct of [the local authority] in relation to Metalclad which the Tribunal has already held amounts to unfair and inequitable treatment breaching Article 1105 and by thus participating or acquiescing in the denial to Metalclad of the right to operate the landfill, notwithstanding the fact that the project was fully approved and endorsed by the federal government, Mexico must be held to have taken a measure tantamount to expropriation in violation of NAFTA Article 1110(1).[89]

In contrast, in the *Pope & Talbot* case,[90] another NAFTA panel hearing a claim by a US investor alleging unfair administration by the Canadian government of an export control regime in implementation of a trade agreement with the United States rejected the assertion that the allegations stated a claim under the expropriation article:

[T]he Tribunal concludes that the Investment's access to the U.S. market is a property interest subject to protection under Article 1110 and that the scope of that article does cover nondiscriminatory regulation that might be said to fall within an exercise of a state's so-called police powers. However, the Tribunal does not believe that those regulatory measures constitute an interference with the Investment's business activities substantial enough to be characterized as expropriation under international law. Finally, the Tribunal does not believe that the phrase 'measure tantamount to nationalization or expropriation' in Article 1110 broadens the ordinary concept of expropriation under international law to require compensation for measures affecting property interests without regard to the magnitude or severity of that effect.

...

The next question is whether the Export Control Regime has caused an expropriation of the Investor's investment, creeping or otherwise. Using the ordinary meaning of those terms under international law, the answer must be negative. First of all, there is no allegation that the investment has been nationalized or that the Regime is confiscatory. The Investor's (and the Investment's) Operations Controller testified at the hearing that the Investor remains in control of the investment, it directs the day-to-day operations of the investment, and no officers or employees of the investment have been detained by virtue of the Regime. Canada does not supervise the work of the officers or employees of the Investment, does not take any of the proceeds of company sales (apart from taxation), does not interfere with management or shareholders' activities, does not prevent the Investment from paying dividends to its shareholders, does not interfere with the appointment of directors or management and does not take any other actions ousting the Investor from full ownership and control of the Investment.

...

Even accepting (for the purpose of this analysis) the allegations of the Investor concerning diminished profits, the Tribunal concludes that the degree of interference

[89] *Metalclad*, Final Award, paras. 103–104.

[90] *Pope & Talbot Inc. v Government of Canada*, Interim Award, 26 June 2000.

with the Investment's operations due to the Export Control Regime does not rise to an expropriation (creeping or otherwise) within the meaning of Article 1110. While it may sometimes be uncertain whether a particular interference with business activities amounts to an expropriation, the test is whether that interference is sufficiently restrictive to support a conclusion that the property has been 'taken' from the owner. Thus, the *Harvard Draft* defines the standard as requiring interference that would 'justify an inference that the owner...will not be able to use, enjoy, or dispose of the property'... The *Restatement* in addressing the question whether regulation may be considered expropriation, speaks of 'action that is confiscatory, or that prevents, unreasonably interferes with, or unduly delays, effective enjoyment of an alien's property'.[91]

Indeed, at the hearing, the Investor's Counsel conceded, correctly, that under international law, expropriation requires a 'substantial deprivation'. The Export Control Regime has not restricted the Investment in ways that meet these standards.

As noted, the Investor expressly agreed that 'the Export Control Regime is a measure not covered by customary international law definitions or interpretations of the term expropriation'. It contends that NAFTA goes beyond those customary definitions and interpretations to adopt broader requirements that include under the purview of Article 1110 'measures of general application which have the effect of substantially interfering with the investments of investors of NAFTA Parties'. The Investor discerns this additional requirement because of the use of the phrase 'measure tantamount to...expropriation' in Article 1110.

The Tribunal is unable to accept the Investor's reading of Article 1110. 'Tantamount' means nothing more than equivalent. Something that is equivalent to something else cannot logically encompass more. No authority cited by the Investor supports a contrary conclusion.[92]

Again, in *S.D. Myers v Canada*,[93] another NAFTA Tribunal followed the *Pope & Talbot* decision in a case arising out of an alleged wrongful closure by the government of Canada of the border with the United States for disposal by the US investor of hazardous waste generated in Canada. The Tribunal found for the investor on its claim of failure to accord fair and equitable treatment and national treatment, but rejected the claim of expropriation:

The Tribunal accepts that, in legal theory, rights other than property rights may be 'expropriated' and that international law makes it appropriate for tribunals to examine the purpose and effect of governmental measures. The Interim Order and the Final Order were regulatory acts that imposed restrictions on [the Investor]. The general body of precedent usually does not treat regulatory action as amounting to expropriation. Regulatory conduct by public authorities is unlikely to be the subject of legitimate complaint under Article 1110 of the NAFTA, although the Tribunal does not rule out that possibility.

[91] Citing American Law Institute, *Restatement (Third) of the Foreign Relations Law of the United States*, §712, comment g.

[92] *Pope & Talbot*, Interim Award, paras. 97–104.

[93] *S. D. Myers, Inc. v Government of Canada*, Partial Award, 13 Nov 2000.

Expropriations tend to involve the deprivation of ownership rights; regulations a lesser interference. The distinction between expropriation and regulation screens out most potential cases of complaints concerning economic intervention by a state and reduces the risk that governments will be subject to claims as they go about their business of managing public affairs.

[The Investor] relied on the use of the word 'tantamount' in Article 1110(1) to extend the meaning of the expression 'tantamount to expropriation' beyond the customary scope of the term 'expropriation' under international law. The primary meaning of the word 'tantamount' given by the Oxford English Dictionary is 'equivalent'. Both words require a tribunal to look at the substance of what has occurred and not only at form. A tribunal should not be deterred by technical or facial considerations from reaching a conclusion that an expropriation or conduct tantamount to an expropriation has occurred. It must look at the real interests involved and the purpose and effect of the government measure.

The Tribunal agrees with the conclusion in the Interim Award of the *Pope & Talbot* Arbitral Tribunal that something that is 'equivalent' to something else cannot logically encompass more. In common with the *Pope & Talbot* Tribunal, this Tribunal considers that the drafters of the NAFTA intended the word 'tantamount' to embrace the concept of so-called 'creeping expropriation', rather than to expand the internationally accepted scope of the term expropriation.[94]

Later cases have generally, but not uniformly, followed the analysis in *Pope & Talbot*, declining to equate denial of fair and equitable treatment with expropriation. In *CMS Gas Transmission Company v Argentine Republic*,[95] for example, the Tribunal pointed out that while the value of Claimant's investment had been substantially impaired by actions of the Argentine government held to violate the standard of fair and equitable treatment, Claimant remained in full control of the investment and therefore expropriation could not be found. In *Fireman's Fund Insurance Company v United Mexican States*,[96] a case under Chapter Fourteen of the NAFTA (which excludes liability for violation of fair and equitable treatment but allows claims for expropriation), the Tribunal wrote:

While [Claimant] has clearly demonstrated injury–indeed loss of its investment–none of its claims, separately or in the aggregate, satisfy the concept of expropriation as understood in the NAFTA and in international law in general. [Claimant] undertook an investment that was risky both in terms of the economic conditions in Mexico at the time, and in terms of the specific financial institution that issued the [securities] that [it] purchased. The NAFTA, like other free trade agreements and bilateral investment treaties, does not provide insurance against the kinds of risks that Claimant assumed, and Chapter Fourteen addressed to cross-border investment in financial institutions, places further limits on the scope of investor-

[94] Id. at paras. 281–282, 285–286.

[95] ICSID Case No. ARB/03/8, Award of 12 May 2005, paras. 252–265. See also e.g. *LG&E Energy Corp. v Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability of 3 October 2006, paras. 198–200.

[96] ICSID Case No. ARB(AF)02/01, Award of 17 July 2006.

State arbitration. In rejecting the claim ... submitted to it in this arbitration, the Tribunal does not mean to suggest that Claimant was not subject to discriminatory and perhaps inequitable treatment by officials of the host State. It holds only that the evidence submitted to the Tribunal has not demonstrated a right to compensation under Article 1110 of the NAFTA, as incorporated by reference in Article 1401 of the NAFTA.[97]

In contrast, the Tribunal in *Siemens AG v Argentine Republic*[98] held that the termination by a series of measures of a concession contract concerning an immigration control and personal identification system 'culminated in expropriation' and was therefore subject to compensation pursuant to the expropriation provisions of the BIT.[99] Similarly, in *Tecnicas Medoambientales Tecmed S.A. v United Mexican States*,[100] a case arising under the BIT between Spain and Mexico, the Tribunal characterized the refusal of a local agency to renew a permit for a landfill operated by Claimant as a measure tantamount to an expropriation, even though legal ownership of the assets in question was not affected.

[I]t is understood [the Tribunal wrote], that the measures adopted by a State, whether regulatory or not, are an indirect *de facto* expropriation if they are irreversible and permanent and if the assets or rights subject to such measures have been affected in such a way that "...any form of exploitation thereof ..." has disappeared ... Under international law, the owner is also deprived of property where the use or enjoyment of benefits related hereto or interfered with to a similar extent...so long as the deprivation is not temporary. The government's intention is less important that the effects of the measures on the owner of the assets or on the benefits arising from such assets affected by the measures; and the form of the deprivation measure is less important that its actual effects.[101]

It seems clear from the cases here excerpted and others that expropriation as governed by the BITs is defined by the deprivation to the investor, not by the gain to the host state. Thus destruction of the investor's property may come within the definition of expropriation if the actions are attributable to the host state, even if the state does not acquire the property in question.[102] Further, intangible rights, such as the right to import or export a given product or to participate in a given industry, may be subject to the constraints on expropriation set out in the BITs. However, a regulation of temporary duration, or a regulation that reduces the profitability of an investment but does not shut it down completely and leaves the investor in

[97] Id.
[98] ICSID Case No. ARB/02/8, Award of 8 Feb 2007.
[99] Id. at paras. 271, 273.
[100] ICSID Case No. ARB (AF)/00/2, Award of 29 May 2003.
[101] Id. at para. 116.
[102] For a recent decision of an ICSID tribunal, not under a BIT but under the ICSID Convention, declining to attribute to the government destruction of the claimant's property by local populations, see *Tradex Hellas S.A. v Republic of Albania*, Award of 29 Apr 1999, 14 ICSID Review-Foreign Investment L.J. 197 (1999).

control, will generally not be seen as an expropriation, even when it gives rise to liability on the part of the host state for violation of the national treatment and fair and equitable treatment clauses.[103]

5. *Compensation*

The subject of compensation, as discussed in Chapters 15 and 16, has been at the centre of the debate about the rights and responsibilities related to foreign direct investment. Since virtually all statements of the law recognize the right of host states to expropriate or nationalize, subject to stated conditions, and since the requirement of public purpose is generally a tautology because it is the state that has acted for what it considers its benefit, the critical question has been whether compensation is due to the investor, and if so, how much, in what form, and in what period of time.[104]

Most, though not all BITs adopt the 'Hull formula' for compensation for takings; many of the BITs—notably the German and the American treaties—elaborate at least somewhat on the meaning of 'prompt', 'effective', and 'adequate'. *Adequacy* is typically defined as 'market value' or 'fair market value' before the expropriation took place, and is supposed to exclude any change in value occurring because the plan to expropriate had become known before the actual taking. The object is spelled out most clearly in the BIT between Japan and China of 1988.[105] Article 5(3) states:

> The compensation...shall be such as to place the nationals and companies [of the other Contracting Party] in the same financial position as that in which the nationals and companies would have been if expropriation, nationalization or any other measures the effects of which would be similar to expropriation or nationalization...had not been taken. Such compensation shall be paid without delay. It shall be effectively realizable and freely transferable at the exchange rate

[103] See e.g. *Corn Products v United Mexican States*, ICSID Case No. ARB (AF)/04/1 (2008).

[104] The statement in the text leaves out the issue of non-discrimination, which is generally stated to be a requirement of 'lawful' expropriation. In fact, while discrimination is often an element in claims brought under Bilateral Investment Treaties, it seems that if compensation is paid equal to the economic loss of the claimant, determined as discussed hereafter, the issue of discrimination does not call for additional compensation. If compensation is not paid, a finding of discrimination may lead to increased compensation. See *ADC v Hungary*, discussed at n. 121 *infra*.

As for 'public purpose', it might not be met if the dictator of a host state expropriated a mansion for his own use; so long as the stated object of an expropriation or other violation is to benefit the national interest, no other nation, and no court or arbitral tribunal, would undertake to examine a taking on this ground. Accordingly, public purpose has not figured prominently in international claims. Accord, *Restatement (Third) of the Foreign Relations Law of the United States*, § 712, comment e. This statement, too, is drawn into question by the *ADC* case, in which the Tribunal asked the respondent state to explain the public purpose of the expropriation, and was not satisfied with the answer.

[105] Agreement Concerning the Encouragement and Reciprocal Protection of Investment, done at Beijing, 27 Aug 1998, repr. in English in 28 Int'l Legal Materials 575 (1989).

in effect on the date used for the determination of the amount of compensation.

Prompt need not mean immediate. Indeed it is generally contemplated in the BITs that there may be disputes about the amount of compensation, and provision is made for resolution of those disputes, as described below.[106] But 'prompt' means that interest shall accrue from the date of the expropriation and shall be included in any agreement, or any arbitral award, concerning the amount of compensation. Some agreements, including the United States model agreement, state that interest shall be paid at a 'commercially reasonable rate' for the currency (assuming it is freely usable) in which the compensation is paid. Some other BITs refer expressly to the London Interbank rate (LIBOR). Still other BITs say nothing about interest or provide for interest but say nothing about the rate.[107]

The question has arisen whether bonds of the taking state calling for payment over time meet the requirement of prompt compensation. None of the BITs expressly addresses this question, and no case is known that addresses it in connection with a BIT. The answer should be that if the bonds are marketable and bear interest realistically related to market rates, they meet the requirements of the Hull formula. This was the answer given by the French Conseil Constitutionnel in upholding the compensation through negotiable interest-bearing 15-year bonds offered by the French government as compensation (otherwise just) for nationalizing several major French companies.[108] The challenge by the former owners was not brought under international law, but under Article 17 of the Declaration of the Rights of Man and the Citizen of 1789, incorporated by reference into the French Constitution of 1958, which provides that property can be taken only 'on condition of a just and prior indemnification'.[109] In this context 'prior' and 'prompt' would seem to call for the same interpretation.

Effective means in a form usable by the investor. The currency of payment must be freely usable or convertible into a freely usable currency, without restrictions on transfer. As discussed above, marketable bonds are

[106] An Agreed Minute of the Japan–China treaty reads:

> The term 'without delay' referred to in the provisions of paragraph 3 of Article 5 of the Agreement shall not exclude a reasonable period of time necessary for deciding the amount, way of payment and so on.

[107] For various provisions concerning interest, see Dolzer and Stevens, *Bilateral Investment Treaties*, n. 73 *supra*, 113–114. Whether the interest is to be simple or compound is not stated in any of the treaties. In the past, arbitral tribunals have generally awarded simple interest only, unless the delay in payment is exceptionally long, but more recently some tribunals have been receptive to requests for award of compound interest.

[108] Conseil Constitutionnel, Decision No. 81–132 DC of 16 Jan 1982, *Journal Officiel*, 17 Jan 1982, 299. For a summary of the other challenges to the nationalizations by the newly elected government of President Mitterand, none of which involved foreign-owned companies, see Andreas F. Lowenfeld, *International Private Investment*, 203–205 (2nd edn., 1982).

[109] For the complete text of Article 17, see Ch. 15, Sect. 15.1, n. 2.

acceptable, provided their actual value, as contrasted with their nominal value, is equal to the compensation determined to be payable. Thus if ten-year bonds issued by Patria are selling in the market at a 10 per cent discount and compensation for SUNATCO's property is set at 5 million dollars equal to 20 million pesos, adequate and effective compensation would be 22.2 million pesos face value of Patria's bonds.

The most difficult problem—with or without BITs—is how to establish 'market value', 'fair market value', or 'genuine value' all of which are essentially synonymous, or even 'just compensation,' which usually is as well.[110] If the value of the investment can be defined—for instance if the shares of the entity in question have been traded on a stock exchange, the price of the shares on the relevant date may be used to determine the market value of the investment. If the investment is unique—for instance a mine or a large manufacturing entity—it may be hard to find comparable assets or a hypothetical willing buyer, and thus establishment of market value may be difficult. The BITs generally do not give guidance for such cases, but if the enterprise has a record of earnings over a representative period, negotiators or a disputes panel may attempt to establish *going concern value*, i.e. the present value of the expected future earnings.[111] When an investment is expropriated or destroyed before it has been able to establish an earnings experience, or when it has failed to make a profit in the period prior to the expropriation or destruction, arbitral tribunals tend to be skeptical about claims of prospective earnings, and to found their awards rather on the actual funds invested in the enterprise. In the *Metalclad* case previously discussed,[112] the Tribunal, drawing on various precedents from arbitrations in ICSID and elsewhere as well as in the Iran–United States Claims Tribunal, awarded the amount actually invested by the investor, less certain costs allocated by the investor in part to the waste disposal facility in question but disallowed by the Tribunal.[113]

[110] 'Just compensation' is the term used in the Fifth Amendment to the United States Constitution, and in decisions of the US Supreme Court. In *United States v Cors*, 337 U.S. 325, 332 (1949), the Supreme Court wrote:

> The Court in its construction of the constitutional provision has been careful not to reduce the concept of just compensation to a formula. The political ethics reflected in the Fifth Amendment reject confiscation as a measure of justice. But the Amendment does not contain any definite standard by which the measure of 'just compensation is to be determined'.

In *United States v Commodities Trading Corp.*, 339 U.S. 121, 123 (1950) the Court wrote:

> Fair market value has normally been accepted as a just standard. But when market value has been too difficult to find, or when its application would result in manifest injustice to owner or public, courts have fashioned or applied other standards.

[111] For a discussion of this method, often termed 'discounted cash flow analysis', see e.g. Brower and Brueschke, *The Iran–United States Claims Tribunal*, n. 30 *supra*, 575–583 and sources there cited.

[112] See Sect. 17.3(b)(2) at n. 81 *supra*.

[113] *Metalclad*, Final Award, paras. 113–26.

It is worth noting that the BITs set out the criteria for compensation only in respect to expropriation or measures tantamount to expropriation. No comparable criteria are set out in any of the treaties for breach of the obligations to accord national treatment, most-favoured-nation treatment, full protection and security, or fair and equitable treatment. Arbitral tribunals that have found a violation of one or more of these provisions have in effect borrowed from the provisions and precedents concerned with expropriations.

In *American Agricultural Products Ltd. v Republic of Sri Lanka*,[114] in which the claim concerned damages for breach of the obligation to provide full protection and security to an enterprise that had not yet had a record of earnings, the Tribunal based its award solely on the investor's tangible assets, rejecting claims for intangible assets, loss of crops to be harvested in the future, or expected profits.[115]

In *Metalclad*, where both denial of fair and equitable treatment and expropriation were found, the Tribunal held that compensation under both provisions would be the same, since both violations involved the complete frustration of the operation and loss of the investment.[116]

In *S.D. Myers*, where the claim of expropriation was rejected but breach of the national treatment and fair and equitable treatment obligations was established, the Tribunal wrote:

> By not identifying any particular methodology for the assessment of compensation in cases not involving expropriation, the Tribunal considers that the drafters of the NAFTA intended to leave it open to tribunals to determine a measure of compensation appropriate to the specific circumstances of the case, taking into account the principles of both international law and the provisions of the NAFTA. In some non-expropriation cases a tribunal might think it appropriate to adopt the 'fair market value' standard; in other cases it might not. In this case the Tribunal considers that the application of the fair market value standard is not a logical, appropriate or practicable measure of the compensation to be awarded.[117]

There being no relevant provisions of the NAFTA other than those contained in Article 1110, the Tribunal turned for guidance to international law, specifically the *Chorzow Factory* case,[118] as well as the *Draft Articles on State Responsibility* then being considered by the International Law Commission.[119] The Tribunal convened another hearing to determine, on the basis of detailed evidence concerning contracts that could not be carried

[114] See Sect. 17.3(b)(3).

[115] *AAPL v Sri Lanka*, Award of 27 June 1990, paras. 88–108.

[116] *Metalclad*, Final Award, para. 113.

[117] *S.D. Myers v Canada*, First Partial Award, paras. 309–317 (13 Nov 2000).

[118] Ch. 15, Sect. 15.3(a).

[119] Article 31 in the final (2001) version of the ILC Articles on State Responsibility cited in full in n. 171 *infra*. Article 31, entitled 'Reparation', in turn draws on the *Chorzow Factory* case:

out, projections of contracts that the investor might have won, the impact of possible competition from new entrants, and the costs to the investor of carrying out the contracts that it had had to forego, all designed to arrive at the loss by the investor of 'net income stream'.[120]

Generally, as discussed in the next section, arbitral tribunals hearing investor-state disputes pursuant to a BIT have searched for a way to compensate the investor for its losses, but to distinguish between risks that should be borne by the investor, including legitimate regulation, and to avoid awarding consequential damages or compensation based on expectation of future profits not supported by clear showing of 'going concern value'. Some recent cases have moved in the opposite direction, emphasizing the distinction between lawful and unlawful expropriation, and resorting to customary international law beyond the scope of the BITs.

In *ADC Affiliate Limited and ADC & ADMC Management Limited v Republic of Hungary*,[121] an ICSID arbitration arising out of an alleged expropriation of an investment in the expansion and management of the Budapest Airport, the Tribunal went a significant step further in exploring the legal basis, or rather the absence of legal basis, for the expropriation. The Respondent State had not only taken Claimants' property without compensation, but, as the Tribunal found, the expropriation had breached all the conditions that could justify a state taking of a foreign-owned investment. The taking was unlawful because:

(a) the taking was not in the public interest;
(b) it did not comply with due process, in particular, the Claimants were denied of '*fair and equitable treatment*' specified in Article 3(1) of the BIT and the Respondent failed to provide '*full security and protection*' to the Claimants' investment under Article 3(2) of the BIT;
(c) the taking was discriminatory; and
(d) the taking was not accompanied by the payment of just compensation.[122]

The BIT in question contained a provision stating: 'The amount of compensation must correspond to the market value of the expropriated investments *at the moment of the expropriation*'. The Respondent State, having failed to persuade the Tribunal of any of its substantive defences, contended that the quoted provision constituted the *lex specialis* to be applied by the Tribunal in determining the appropriate compensation. The Tribunal, however, held that the BIT pertained to *lawful* expropriation, whose provisions would,

1. The Responsible State is under an obligation to make full reparation for the injury caused by the internationally wrongful act.

2. Injury includes any damage, whether material or moral, caused by the internationally wrongful act of a State.

[120] *S.D. Myers v Canada*, Second Partial Award, Oct 2002.

[121] ICSID Case No. ARB/03/16, Award of 2 Oct 2006.

[122] Id. at para. 476.

if applicable, prevail over rules of customary international law (citing e.g. *Phillips Petroleum Co. v Iran*[123]). The BIT did not, however, address the standard of compensation payable in the case of an *unlawful* expropriation. For that standard the Tribunal referred back to the *Chorzow Factory* case, in particular to the famous passage calling for wiping out all the consequences of the illegal act, and for re-establishing the situation 'which would, in all probability, have existed if that act had not been committed'.[124]

The issue was significant in the *ADC* case because, unlike most expropriation cases and particularly those arising out of the Iranian revolution, the value of the property had increased very substantially between the taking and the award. The Tribunal assumed that this would have occurred as well had Claimants remained in control, on the basis that air travel generally and travel to and from Hungary in particular kept growing. Accordingly the Tribunal, in application of what it saw as the customary international law, ruled that in absence of restitution, which was clearly impossible, compensation should be based not on the value at the 'moment of the expropriation', but on the value at the time of the award. The result, based on the value of the expropriated investments as of the date of the award, estimated by use of the Discounted Cash Flow method, was an award of damages of US $76.2 million, compared to an initial investment by Claimants of US $16.765 million.[125] Thus in counterpoint to the debate summarized in Section 17.3(e), which questions whether the vast expansion of Bilateral Investment Treaties has ripened to a customary international law protecting foreign investors, the Tribunal in the *ADC* case, consisting of three very experienced arbitrators,[126] concluded that customary law extended beyond the limits of the typical BIT and reflected the expansive (though not inevitable) reading of what the Permanent Court of International Justice had written in the 1920s.[127]

In sum, the Bilateral Investment Treaties reflect a turn away from the search for 'appropriate compensation', and a return to the earlier standards reflected in the Hull formula. In principle, that formula is easy to understand—an effort to put the investor in the position in which it would

[123] Discussed in Sect. 17.2(c)(5) *supra*.

[124] *Chorzow Factory* case, P.C.I.J. Series A, No. 17, at 47. A longer excerpt, as well as discussion of varying interpretations of the effect of the case, appears in Ch. 15, Sect. 15.3(a).

[125] Since the calculation was based on the value of the expropriated investments as of the date of the award, no pre-award interest was awarded. The Tribunal ruled that post-award interest would be awarded, compounded monthly until payment, but Hungary appears to have promptly made the required payment.

[126] The Panel consisted of a long-time American Judge on the Iran–US Claims Tribunal (Brower), a leading Dutch international arbitrator and author (van den Berg), and as President, an English Queen's Counsel and former chairman of the Hong Kong International Arbitration Centre (Kaplan).

[127] For a somewhat similar recent decision under a BIT awarding full value plus consequential damages but not loss of future profits for what the Tribunal found to be an unlawful expropriation, see *Siemens AG v Argentine Republic*, n. 98 *supra*.

have been had the expropriation or other breach not taken place. Working out the details has never been easy, either under classical international law or under the regime of the BITs.

6. *Dispute Settlement*

As shown in Chapter 15, one of the prime goals of the New International Economic Order was to establish the principle, previously advocated by Calvo and others, that disputes between a foreign investor and a host state be submitted exclusively to the courts or administrative tribunals of the host state. The ICSID Convention negotiated in the early 1960s offered an alternative to this principle; the Bilateral Investment Treaties reject this principle completely and explicitly. Every modern BIT makes provision for settlement of disputes between the investor and the host state.[128] The ICSID Convention, it will be recalled, requires consent by the parties to arbitration under a particular investment agreement or in respect to a particular dispute, but provides that the consent once given may not be withdrawn.[129] The BITs go a significant step further, by providing in nearly all of the treaties that the host state gives its consent to arbitration of any investment dispute subject of the treaty, generally by reference to the rules or arbitral institutions provided for in the treaty. If the treaty provides for arbitration pursuant to the ICSID Convention, the consent given in the BIT satisfies the requirement of Article 25(1) of that Convention; if the treaty provides for arbitration under the UNCITRAL rules or under some other set of rules, the consent by the state satisfies those rules as well as the requirements of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention).[130]

The most common reference in the BITs is to arbitration under the auspices of International Centre for the Settlement of Investment Disputes (ICSID), provided both the host state and the home state of the investor are parties.[131] Many recent BITs provide also for alternatives to ICSID arbitration, in particular for arbitration pursuant to the UNCITRAL rules, but in some treaties also for arbitration under the auspices of the International Chamber of Commerce or under purely *ad hoc* arbitration if agreed by the parties to the dispute. The recent American treaties, as well as the NAFTA,

[128] Dolzer and Stevens, in *Bilateral Investment Treaties*, n. 73 *supra*, 129, write 'Virtually all modern treaties provide for the arbitral settlement of investment disputes', but they do not mention any treaty that does not so provide and the present author has not found any.

[129] See Sect. 17.1, n. 6, discussing Article 25(1) of the ICSID Convention.

[130] The United States model BIT recites the above explicitly; it is clearly implied in most other BITs. For various versions of the consent, see Dolzer and Stevens, *Bilateral Investment Treaties*, n. 73 *supra*, 131–136.

[131] Nearly all developed states, with the exception of Canada, are parties to the ICSID Convention. If the host is not a party to the ICSID Convention or has signed but not yet ratified the Convention, some of the BITs provide for arbitration under the ICSID Additional Facility. See Sect. 17.1, n. 19 *supra*.

provide for a choice by the investor between arbitration under UNCITRAL rules and under ICSID (or the Additional Facility); the British model treaty also provides options, but subject to agreement of the disputing parties, with arbitration under the UNCITRAL rules called for in the absence of agreement.[132]

It may be asked on what basis the choice is made among the various options for dispute settlement, either by the claimant (investor) alone or by the two disputing parties jointly. Some parties or their counsel prefer the discipline and fixed fee schedule of institutional arbitration. Others prefer the greater freedom of *ad hoc* arbitration without scrutiny by an institution. No jurisprudential answer can be given, and no prediction that one forum for arbitration is advantageous for one side or the other. The present writer's experience is that differences among the various arbitral rules and institutions are significant at the initial stage, concerning fees, deposits, schedules, and appointment of arbitrators, and at the enforcement stage if that becomes necessary.[133] The process of determining facts, ruling on evidence, choosing the applicable law and construing that law depends on the arbitrators and counsel, not on differences in the rules.[134]

Arbitral proceedings under BITs and the NAFTA are confidential, and participation by non-governmental organizations or other *amici curiae* has usually not been permitted.[135] ICSID awards are published in the ICSID Review and are made available on ICSID's website. Most other awards based on disputes under BITs have also been published, and arbitral tribunals hearing investment disputes have freely considered other awards

[132] UNCITRAL arbitration proceeds without supervision by an institution such as ICSID, the ICC, the London Court of International Arbitration, or the American Arbitration Association. Each of these institutions may be designated as appointing authority to choose the presiding arbitrator (or sole arbitrator) in the absence of agreement by the parties. In the NAFTA, the Secretary-General of ICSID is designated as the appointing authority. When no appointing authority is designated in an agreement, the UNCITRAL rules provide that the Secretary-General of the Permanent Court of Arbitration at The Hague may be requested to designate the appointing authority.

[133] Under Article 54 of the ICSID Convention (but not under the Additional Facility) awards are directly enforceable in all Contracting States as if they were a final judgment of a court of the state where enforcement is sought. Other awards, whether under UNCITRAL rules or under the rules of an arbitral institution, are generally entitled to enforcement under the New York Convention, i.e. under the same conditions as a foreign arbitral award, subject to a limited number of defences. For an account of the difficulty in enforcing ICSID awards in national courts, see Edward Baldwin, Mark Kantor and Michael Noran, 'Limits to Enforcement of ICSID Awards', 23 J. Int'l Arbitration 1 (2006).

[134] For a discussion of the choices made by counsel, which recently have greatly favoured ICSID, see Barry Appleton, 'Comparing ICSID and *ad hoc* Treaty Arbitration', 2 Global Arbitration Review: The International Journal of Public and Private Arbitration, Issue 2, at 11 (2007).

[135] But neither Article 44 of the ICSID Convention nor the UNCITRAL Arbitration Rules exclude submission of *amicus curiae* briefs, and in *Aguas Provinciales de Santa Fe S.A. v Argentine Republic*, ICSID Case No. ARB/03/17, Order in Response to a Petition for Participation as *amicus curiae*, 17 March 2006, the tribunal laid out specific conditions for the admission of such briefs on issues of public interest by suitable, independent, nongovernmental parties.

made under treaties similar to the one before them. Thus a substantial body of decisions on investor–state disputes under BITs has been building up. Arbitral tribunals have also relied on awards and judgments not arising from BITs but involving disputes between investors or their governments and host states. It may fairly be said that dispute resolution under BITs both draws on and contributes to the corpus of international law.

(c) BITs and Jurisdiction: The MFN Question

Virtually all BITs contain most-favoured-nation clauses, modeled on the tradition of such clauses in international trade,[136] and designed to guarantee treatment to foreign investors of the treaty partner at least equal to the treatment granted to foreign investors of any other country.[137] In some treaties, the MFN provision is subject to specific exclusions, in some it expressly extends to 'all matters,' in still others the clause is neither expressly all-inclusive nor expressly limited.[138] In a number of ICSID arbitrations brought pursuant to BITs, claimants have sought to take advantage of MFN clauses to get around provisions in the dispute resolution clauses requiring resort to national jurisdiction of the host country as a condition precedent to jurisdiction of an international forum. Host countries have contended that MFN clauses concern substantive matters, not procedural matters such as dispute settlement.

Ironically, the first case to raise the issue was not an instance of an investor from a developed country claiming against a developing country, but the reverse. In *Maffezini v Kingdom of Spain*,[139] an Argentine private investor in Spain claimed that Spanish authorities had interfered with his rights in a chemical products joint venture with a Spanish public entity in breach of the BIT between Argentina and Spain. Following notice of a dispute and negotiations over a six-month period, Claimant initiated arbitration under the ICSID Arbitration Rules. The BIT between Argentina and Spain provides that unless the disputing parties agree otherwise, a dispute under the treaty shall be submitted to the national jurisdiction of the state Party in whose territory the investment was made. Arbitration under ICSID (or UNCITRAL) may be initiated only if no decision has been rendered by the national courts within 18 months of submission or if a decision is rendered but the dispute continues. The claimant did not resort to local courts, asserting that pursuant to the MFN clause in the Argentina-Spain

[136] See Ch. 3, Sect. 3.3(b).

[137] Recall the rather loose nod to MFN in regard to foreign investment contained in the abortive Havana Charter of 1948, Ch. 15, Sect. 15.4(a).

[138] See Dolzer and Stevens, *Bilateral Investment Treaties*, n. 73 *supra*, for a selection of such clauses; also OECD, Directorate for Financial and Enterprise Affairs, *Most-Favoured-Nation Treatment in International Investment Law*, 3–8 (Sep 2004).

[139] ICSID Case No. ARB/97/7, Decision on Jurisdiction of 25 Jan 2000, reprinted in 16 ICSID Review–Foreign Investment L.J. 212 (2001).

BIT,[140] he was entitled to the advantages contained in the BIT between Chile and Spain, which also provided for ICSID arbitration, but without any requirement for prior resort to national courts.

The Tribunal upheld Claimant's contention, rejecting the argument on behalf of Spain that the MFN clause applied only to substantive matters, not to matters of procedure:

> Notwithstanding the fact that the basic treaty containing the [MFN] clause does not refer expressly to dispute settlement as covered by the most-favoured-nation clause, the Tribunal considers that there are good reasons to conclude that today dispute settlement arrangements are inextricably related to the protection of foreign investors, as they are also related to the protection of traders under treaties of commerce.
>
> ...
>
> From the above considerations it can be concluded that if a third-party treaty contains provisions for settlement of disputes that are more favourable to the protection of the investor's rights and interests than those in the basic treaty, such provisions may be extended to the beneficiary of the most favored nation clause....
>
> ...
>
> Accordingly, the Tribunal affirms the jurisdiction of the Centre and its own competence in this case in respect to this aspect of the challenge made by the Kingdom of Spain.[141]

Most but not all subsequent cases raising the issue of whether a MFN clause can override a restrictive jurisdiction clause have followed the result in *Maffezini,* but with some differences in the reasoning.[142] In *Gas Natural SDG, S.A. v The Argentine Republic,* one of the many cases arising from the economic crisis in Argentina in 2001–2003 (see Ch. 20, Sect. 20.17), the Tribunal was confronted with the same treaty as in the *Maffezzini* case, but with the parties reversed. A Spanish private company claimed under the Argentina–Spain BIT, and sought to avoid the resort to national jurisdiction clause in reliance on the MFN clause and the United States–Argentina BIT, which contained no requirement of prior resort to national jurisdiction. The

[140] Article IV(2) of the BIT reads (in translation):

> In all matters governed by the present Agreement, such treatment shall not be less favorable than that accorded by each Party to investments made in the territory to investors of Third States.

[141] *Maffezini,* Decision on Jurisdiction, paras. 54, 56, 64.

[142] See e.g. *Siemens A.G. v Argentine Republic,* ICSID Case No. ARB/02/8, Decision on Jurisdiction of 3 Aug 2004; *Camuzzi International S.A. v Argentine Republic,* ICSID Case No. ARB/03/7. *Republica Argentina* Decision on Jurisdiction of 10 June 2005; *Suez, Sociedad General de Aguas de Barcelona S.A. (AGBAR) v Argentine Republic,* ICSID Case No. ARB/03/17, Decision on Jurisdiction of 16 May 2006; *Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal S.A. and Auglian Wafer Group (AWD) v Argentine Republic,* ICSID Case No. ARB/03/19, Decision on Jurisdiction of August 3, 2006; *MTD Equity Sdn* and *MTD Chile S.A. in Republic of Chile,* ICSID Case No. ARB/01/7, Award of 25 May 2004.

Tribunal considered that 'the critical issue is whether or not the dispute settlement provisions of bilateral investment treaties constitute part of the bundle of protections granted to foreign investors by most states'. Reviewing the history, part of the ICSID Convention and subsequently the wave of BITs between developed and developing countries, the Tribunal concluded that:

> a crucial element – indeed perhaps the most crucial element – has been the provision for independent international arbitration.... [S]uch provisions are universally required – by opponents as well as by proponents – as essential to a regime of protection of foreign direct investment.[143]

The Tribunal wrote that the issue is not free from doubt, but supported its conclusion also by reference to the phrase 'all matters governed by the present Agreement' in the MFN clause.[144] It concluded that:

> Unless it appears clearly that the state parties to a BIT or the parties to a particular investment agreement settled on a different method for resolution of disputes that may arise, most-favoured-nation provisions in BITs should be understood to be applicable to dispute settlement.[145]

Two cases decided at approximately the same time as *Gas Natural* viewed the issue differently. *Salini Construction S.p.A. and Italstrade v Hashemite Kingdom of Jordan*,[146] grew out of a dispute between two Italian construction companies and the kingdom of Jordan over claims under a construction contract. The Tribunal drew a distinction between contractual claims and treaty claims, pointing to a detailed dispute settlement clause in the investment agreement and the general condition of the construction contract. The Tribunal held that only the treaty claims were governed by the consent to ICSID arbitration in the BIT between Italy and Jordan, and accordingly that it did not have jurisdiction over the contract claims. Claimants contended that the distinction between treaty and contract claims was suspended by the MFN provision in the BIT, and that BITs concluded by Jordan with the United States and the United Kingdom entitled investors to refer to ICSID *any* dispute arising from their construction contracts. The Tribunal rejected that argument, pointing out that in contrast to the clause in the *Maffezini* case, the MFN clause in the Italy–Jordan treaty did not refer to 'all matters covered by the agreement' but that on the contrary the disputes clause excluded from ICSID jurisdiction contractual disputes between an investor and an entity of a State party.[147] Beyond that, however, the *Salini* tribunal wrote:

[143] *Gas Natural*, Decision on Jurisdiction, ICSID Case No. AR13/03/10 (17 June 2005) para. 29. (The present writer served as President of the *Gas Natural* Tribunal.)
[144] See n. 138 *supra*.
[145] Id. at para. 49.
[146] ICSID Case No. ARB/02/13, Decision on Jurisdiction of 29 Nov 2004.
[147] *Salini* Decision, para. 118.

The current Tribunal shares the concerns that have been expressed in numerous quarters with regard to the solution adopted in the *Maffezini* case. Its fear is that the precautions taken by authors of the award may in practice prove difficult to apply, thereby adding more uncertainties to the risk of 'treaty shopping.'[148]

Plama Consortium Ltd v Republic of Bulgaria[149] was a claim pursuant to the European Energy Charter Treaty, [150] a multilateral treaty comparable to a BIT in that its purpose is to promote foreign direct investment in countries with energy resources, and to provide certain rights of entry as well as protection to foreign investors. Claimant, a company organized under the laws of Cyprus, had purchased a Belgian company that owned an oil refinery in Bulgaria, and alleged in its request for arbitration that expectations had been impaired by actions of the Bulgarian government. Claimant asserted jurisdiction under a BIT between Cyprus and Bulgaria. The BIT, however, provided for arbitration of disputes relating to expropriation only with regard to the amount of compensation, and only after the merits of the claims of the investor had been checked through regular administrative proceedings of the host country. In contrast to the clauses in the Argentine BITs addressed in *Maffezini*, *Siemens*, and *Gas Natural*, which contemplated ICSID jurisdiction following first resort to local courts or expiry of 18 months, the Cyprus–Bulgaria BIT made no provision at all for jurisdiction of a dispute on the merits by an ICSID tribunal. Nevertheless, Claimant asserted that it was entitled by virtue of the MFN clause in the Cyprus–Bulgaria treaty to the benefits of a BIT between Bulgaria and Finland, which provided generally for ICSID jurisdiction of investor–state disputes. The Tribunal was not moved. Rejecting Claimant's effort, it wrote:

It is one thing to add to the treatment provided in one treaty more favourable treatment provided elsewhere. It is quite another thing to replace a procedure specifically negotiated by the parties with an entirely different mechanism.[151]

It is easy to distinguish the *Plama* decision from *Maffezini* and the decisions that have followed it, both because the MFN clause did not cover 'all matters', as most of the BITs concluded by Argentina did,[152] and because, as pointed out by the Tribunal, sustaining ICSID jurisdiction in *Plama* via the MFN clause would have required a greater leap than in any of the

[148] Id. at para. 115.

[149] ICSID Case No. ARB/03/24, Decision on Jurisdiction of 8 Feb 2005.

[150] European Energy Charter Treaty, signed 17 Dec 1994, 2080 U.N.T.S. 100, repr. in 34 Int'l Legal Materials 360 (1995).

[151] *Plama* Decision on Jurisdiction, para. 209. The decision also addressed jurisdiction of a claim under the European Energy Charter Treaty, but the discussion of that issue is not here pertinent.

[152] Article 3(11) of the Cyprus–Bulgaria BIT reads:

Each Contracting Party shall apply to the investments in its territory by investors of the other Contracting Party a treatment which is not less favourable than that accorded to investments by investors of third states.

other cases. Moreover, the evidence in the *Plama* case showed that following Communist rule in Bulgaria the parties themselves were negotiating to expand the scope of the BIT. But the Tribunal in the *Plama* case wanted to make a more general point:

Nowadays [it wrote], arbitration is the generally accepted avenue for resolving disputes between investors and states. Yet that phenomenon does not take away the basic prerequisites for arbitration: an agreement of the parties to arbitrate. It is a well established principle, both in domestic and in international law, that such an agreement should be clear and unambiguous.

...

A clause reading 'a treatment which is not less favorable than that accorded to investments by investors of third states'...creates doubt whether the reference to the other documents...clearly and unambiguously includes a reference to the dispute settlement provision concerned in those BITs.[153]

The Tribunal concluded by setting out its principle:

A MFN provision in a basic treaty does not incorporate by reference dispute settlements in whole or in part set forth in another treaty, unless the MFN provision in the basic treaty leaves us doubt that the Contracting Parties intended to incorporate them.[154]

Responding to *Plama*, the tribunal in the two *Suez Water* cases[155] rejected this view, which, it said, seems to hark back to earlier attitudes of mistrust toward arbitration:

This Tribunal [it wrote] does not share this sentiment...[I]t believes that dispute resolution provisions are subject to interpretation like any other provisions of a treaty, neither more restrictive nor more liberal.[156]

Conclusion

On one level, the decisions discussed above can be reconciled by reading the relevant MFN clauses and the relevant dispute settlement clauses with care. The Spain–Argentina bilateral investment agreement, for example, contains a broad MFN clause, and the dispute provisions, though detailed, are not limited to particular contracts, as in *Salini*, or to unusual limitations, as in *Plama*. On another level, the almost contemporaneous statements in *Gas Natural* at note 143 and in *Plama* at note 149 both issued by experienced arbitrators, are striking in their different perspectives.[157] It

[153] *Plama* Decision on Jurisdiction , paras. 198, 200.

[154] Id. at para. 223.

[155] *Aguas Provinciales de Santa Fe S.A. v Argentine Republic*, ICSID Case No. ARB/03/17, n. 142 *supra* and ICSID Case No. ARB/03/19.

[156] ICSID Case No. ARB/03/17, para. 64. and Case No. ARB/03/19, para. 66.

[157] The *Plama* decision was rendered shortly before the decision in *Gas Natural*, but the latter Tribunal had finished its deliberations and settled on its award before the *Plama* decisions became publicly available. Thus neither Tribunal had occasion to respond to the other.

is possible that since these decisions all concern jurisdiction of the tribunals, some uniformity may be achieved through the annulment procedure pursuant to Article 52 of the ICSID Convention. As of mid-year 2007, the issue remained controversial, and hotly contested.[158]

(d) Defences

1. *Measures of General Application*

Whereas the types of expropriations described in Chapter 15—the Russian Revolution, the Mexican Revolution, and the changes following World War II—were part of major political and social transformation, the claims presented pursuant to the ICSID Convention and BITs (including NAFTA) have for the most part involved measures applied to particular investors or investments. Would the criteria adopted by ICSID tribunals in interpreting and applying BITs be the same when the measures giving rise to the claim were not directed to particular claimants but were part of a general response by the government of the host state to a national emergency? This question became acute in connection with the financial and social crisis in Argentina in the period 2000–2003.[159]

In the early 1990s the government of Argentina under President Carlos Menem embarked on a massive programme of privatization of state-owned industries, particularly in the public utilities sector—water, natural gas, telecommunications, electric power and the like. The major source of the capital was to consist of foreign direct investment. To this end, the government concluded more than fifty BITs. It committed itself by law to maintain parity of the new Argentine peso with the US dollar through the operation of a so-called currency board,[160] and to maintain convertibility of the peso at one-to-one without restrictions on remittances. For regulated industries such as transmission and distribution of natural gas, the respective tenders and investment agreements provided for tariffs tied to the United States Producer Price Index, i.e. the promise of regular rate increases in line with international price movements.

For a time, the programme launched by President Menem had great success. Over $10 billion in foreign direct investment flowed into Argentina, exports increased by 12 per cent per year, inflation was halted, and the country's standard of living improved substantially. By the end of the

[158] For a thoughtful discussion, also concluding that consensus will have to wait for further cases, see Dana H. Freyer and David Herlihy, 'Most-Favored-Nation Treatment and Dispute Settlement in Investment Arbitration: Just How "Favored" is "Most Favored"'?, 20 ICSID Review – Foreign Investment L.J. 58 (2005).

[159] The origins and consequences of the Argentine crisis are set out in detail in Ch. 20, Sects. 20.16 and 20.17 in the context of exploration of the international monetary system and regional crises. Only a brief summary is presented here, to put the questions raised in this section in context.

[160] See Ch. 20, Sect. 20.16 n. 144.

decade, however, the policy could not be sustained, and the economy collapsed. In a brief period, four presidents had to resign, Argentina defaulted on massive foreign debt, convertibility was abandoned, and the peso was permitted to float (like a rock, it was said). Emergency decrees were issued, revised, rescinded, and reissued. With respect to the foreign companies that had invested in Argentina, dollar deposits were frozen, agreements to adjust tariffs were suspended, and the shares in the Argentine companies that constituted the foreign companies' investments lost much of their value.

More than fifty claims were filed with ICSID pursuant to Bilateral Investment Treaties between Argentina and various developed countries. The claims differed in detail, depending on the specific investment agreements and franchises, but nearly all alleged expropriation, failure to grant fair and equitable treatment, arbitrary or discriminatory measures, failure to provide full protection and security, and breach of the so-called 'umbrella clause' in many of the BITs.[161] As of mid-year 2007, some of the arbitrations had been settled, and some were involved in various jurisdictional disputes.[162] Two cases arising under the same BIT between Argentina and the United States and based on essentially the same facts turned in significant measure on the response of the tribunals to the issue here raised.[163]

Both CMS Gas Transmission Company and LG&E Energy Corporation established in their separate arbitrations that their investments in the privatized utilities had lost a great deal of their value as a result of the measures taken by the Argentine government in response to the financial and social crisis. Their rates had not been adjusted as required by the investment agreements; their dollar assets had been frozen, and their revenues had been 'pesified', i.e. converted to the local currency no longer at par with the dollar. Both claimants asserted expropriation, failure to accord fair and equitable treatment, arbitrary and discriminatory action, and breach of the 'umbrella clause'.

Both tribunals were careful to state that they did not have jurisdiction over measures of general economic policy adopted by the government of Argentina, and could not pass judgment on whether they were right or wrong. Both rejected, however, the defence that the claims did not present an 'investment dispute' and held that they did have jurisdiction to examine whether specific measures affecting the respective claimants' investment, or measures of general economic application having a direct bearing on such investment had been adopted in violation of legally binding commitments

[161] The 'umbrella clause' (Art. II(2)(c) in the Argentina–United States Treaty) states 'each Party shall observe any obligation it may have entered into with regard to investments'.

[162] See Sect. 17.3(c) *supra*.

[163] *CMS Gas Transmission Company v Argentine Republic*, ICSID Case No. ARB/01/8, Award of 12 May 2005; *LG&E Energy Corp. v Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability of 3 Oct 2006.

made to the investor in treaties, legislation or contracts.[164] Accordingly, the tribunals examined specific guarantees to the claimants of the right to tariffs calculated in dollars, the right to adjustment of their tariffs in accordance with a United States index, and the right not to have their licences amended without their consent, and both tribunals held that each of these guarantees had been violated.

Both tribunals concluded that the measures complained of 'did in fact entirely transform and alter the legal and business environment under which the investment was decided and made', and accordingly violated the standard of fair and equitable treatment set out in the Argentina–United States BIT.[165] It was not necessary, as the *CMS Gas* tribunal stated, to relate that conclusion to any finding of deliberate intention or bad faith. Both tribunals rejected claims based on arbitrary action, but both held that in abrogating the guarantees given in the investment agreements, Argentina had violated the umbrella clause.[166] Both tribunals found that there had been no expropriation, essentially on the grounds set forth in the *Pope & Talbot* and *S.D. Myers* cases summarized in Sect. 17.3(b)(4) *supra*. The investors had remained in control of their business or their shares—albeit that the business or the shares had lost a great portion of their value. The term 'tantamount to nationalization or expropriation' however, did not broaden the concept of expropriation in international law.[167]

On the basis of these decisions as well as of numerous others, including those discussed in subsection (c) above, it seems clear that claims by investors against a host government, when asserting specific losses or economic injury, will be regarded as raising 'investment disputes' within the meaning of the ICSID Convention. Furthermore, the failure by a Claimant to establish that it was the intended target of the challenged measures will not, without more, provide a defence or excuse to the host state. As discussed hereafter, however, measures such as those taken by the Argentine authorities, in combination with a plea of *force majeure* or necessity, might avoid liability under a BIT.

[164] *CMS Gas* Award, para. 124, quoting from Decision on Jurisdiction of 17 July 2003, para. 33, *LG&E*, Decision on Jurisdiction of 30 April 2004, paras. 67–68.

[165] The quoted phrase comes from *CMS Gas* Award, para. 275. To the same effect in *LG&E* Decision on Liability, paras. 132–139.

[166] The *LG&E* tribunal differed from the *CMS Gas* tribunal in that it did find discrimination, on the ground that gas distribution companies were treated more unfavourably than other public utility companies such as the electricity and water distribution companies. *LG&E* Decision, paras. 147–148. The tribunal did not find discrimination based on nationality.

[167] *CMS Gas* Award, paras. 263–265; *LG&E* Decision, paras. 198–200. For a contrary holding, see *Siemens AG v Argentine Republic*, discussed in Sect. 17.3(b)(4) at n. 98.

2. *The Defence of Necessity*

Pleading in the alternative, Argentina argued that if the tribunals should find that it had breached the Treaty, it should be exempt from liability by reason of the existence of a state of necessity or state of emergency, that is the severe economic social and political crisis in which the country found itself. In raising this defence, Argentina relied both on customary law, as codified in the International Law Commission's Draft Articles on State Responsibility, and on Article XI of the Argentina–US BIT, which provides:

> This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of peace or security, or the Protection of its own essential security interests.

On this issue, the *CMS Gas* and *LG&E* tribunals came out on opposite sides. Claimant in *CMS* argued that the BIT was designed precisely to protect the interests of investors at a time of economic difficulties or other circumstances leading to adverse measures by the host government. The tribunal agreed. There might be a situation of total collapse, in which case the Treaty would not impose liability. 'The question is, however, how grave those economic difficulties might be.'

> A severe crisis cannot necessarily be equated with a situation of total collapse. And in the absence of such profoundly serious conditions it is plainly clear that the Treaty will prevail over a plea of necessity.
>
> ...
>
> The tribunal is convinced that the Argentine crisis was severe but did not result in total economic and social collapse. When the Argentine crisis is compared to other contemporary crises affecting countries in different regions of the world it may be noted that such other crises have not led to the derogation of international contractual or treaty obligations. Renegotiation, adaptation and postponement have occurred but the essence of the international obligations has been kept intact.[168]

The *LG&E* tribunal, viewing the same facts, came to the opposite conclusion.

> In the judgment of the Tribunal, [it wrote] from 1 December 2001 until 26 April 2003, Argentina was in a period of crisis during which it was necessary to enact measures to maintain public order and protect its essential security interests.... Thus, Argentina is excused under Article XI from liability for any breaches of the Treaty [between those dates].[169]

[168] *CMS Gas* Award, paras. 354, 355.

[169] For the significance of the starting date, see Ch. 20, Sect. 20.15(d). The significance of the end of the crisis as found by the Tribunal is not quite clear. On 27 April 2003, Argentina held what was supposed to be a primary election. Former President Menem finished first but with only 24 per cent of the votes. Facing a run-off with the second place candidate, Nestor

The *LG&E* Tribunal described the Argentine crisis in considerable detail, pointing out that the country's gross domestic product, private competition, domestic prices and assets values all fell sharply in the last quarter of 2001, while unemployment and poverty were rising rapidly, with unemployment at 25 per cent and almost half the population living below the poverty line. 'Facing increased pressure to provide social services and security to the masses of indigent and poor people, the Government was forced to decrease its per capita spending on social services by 74 per cent.'

Writing 16 months after the *CMS* award was issued (but without referring to that award in this context), the *LG&E* tribunal rejected the notion that Article XI is only applicable in circumstances amounting to military action or war:

> To conclude that such a severe economic crisis could not constitute an essential security interest is to diminish the havoc that the economy can create on the lives of an entire population and the ability of the Government to lead. When a State's economic foundation is under siege, the severity of the problem can equal that of any military invasion.[170]

Both tribunals referred to customary international law, and both looked for exposition of that law to the International Law Commission's Draft Articles on State Responsibility.[171] The *LG&E* tribunal looked first to the Treaty, and then referred to the Draft Articles to support its conclusion. The *CMS Gas* tribunal, in contrast, looked first to customary law, and then used its reading of the Draft Articles to inform its construction of the Treaty. Going back to the explanation of Article 42(1) of the ICSID Convention by Aron Broches, the principal drafter and proponent of the Convention,[172] the approach of the *LG&E* tribunal on this issue seems correct. Construing the Treaty should come first. The fact that a 'codification' of the customary law on this issue is easy to find, and that that codification has been endorsed by the International Court of Justice in an unrelated case,[173] does not, in this writer's view, give customary law status superior

Kirchner, Menem withdrew, and Kirchner won by default. Kirchner assumed the presidency on 25 May 2003, but apparently the Tribunal thought the emergency ended with the primary election.

[170] *LG&E* Decision, para. 238.

[171] International Law Commission, *Articles on Responsibility of States for Internationally Wrongful Acts*, approved by UN General Assembly, 56 UN GAOR, Supp. No. 10, 43, UN Doc. A/56/10 (2001), UN Doc. A/RES/56/83 (12 Dec 2001), conveniently available with commentary in James Crawford, *The International Law Commission's Articles on State Responsibility* (2002).

[172] See Sect. 17.1(c) *supra*.

[173] See *Gabčikovo-Nagymaros Project (Hungary/Slovakia)*, I.C.J. Reports 1997, 7, para. 51:

> The Court considers...that the state of necessity is a ground recognized by customary international law for precluding the wrongfulness of an act not in conformity with an international obligation.

to the treaty on which the claim is based. It turned out, however, that the hierarchy did not matter. Each tribunal interpreted the relevant provision in the Draft Articles as consistent with its interpretation of the Treaty.

Article 25 of the Draft Articles, entitled *Necessity*, reads as follows:

1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:
   (a) is the only means for the State to safeguard an essential interest against a grave and imminent peril; and
   (b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.
2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:
   (a) the international obligation in question excludes the possibility of invoking necessity; or
   (b) the State has contributed to the situation of necessity.

The *CMS Gas* tribunal focused on the word 'only' in subsection 1(a), and concluded that it meant that the defence would be available only if the situation had left no other option open to the state than the measures it took.[174] Were the measures taken by successive Argentine governments the only way for the state to safeguard its interests? The tribunal thought this was debatable. What about dollarization of the economy, granting direct subsidies to the affected population or industries, 'and many others'?[175] Thus while elements of necessity are partially present here and there, the tribunal wrote, it could not be concluded that all such elements were present: 'This in itself leads to the inevitable conclusion that the requirements of necessity under customary international law have not been fully met so as to preclude the wrongfulness of the acts.'[176] Having satisfied itself that customary international law did not call for recognizing the necessity defence in this case, the tribunal could comfortably proceed to its analysis of the treaty as quoted above, i.e. that the object and purpose of the Treaty would be defeated if emergencies short of total collapse deprived investors of the Treaty's protection.

In the actual case, the Court rejected the plea. For a review of other sources dealing with the necessity defence, as well as an in-depth discussion of the cases here discussed, see August Reinisch, 'Necessity in International Investment Arbitration – An Unnecessary Split of Opinions in Recent ICSID Cases?' 3 Trade Dispute Management (TDM), Issue 5 (Dec 2006).

[174] *CMS Gas* Award, paras. 323–324, and again para. 356. Note that Article 25 is written in double negative. The defence 'may not be invoked... unless...'.

[175] Id. at para. 323.

[176] Id. at para. 331.

For the *LG&E* tribunal, the key to Article 25 of the Draft Articles was the evidence. It agreed that Article 25 requires that for the necessity defence to be applicable, the challenged action must be the only means available to protect an essential interest. But, the tribunal found that:

> The essential interests of the Argentine State were threatened in December 2001.... Although there may have been a number of ways to draft the economic recovery plan, the evidence before the Tribunal demonstrates that an across-the-board response was necessary, and the tariffs on public utilities had to be addressed....
>
> While this analysis concerning Article 25 of the Draft Articles on State Responsibility alone does not establish Argentina's defense, it supports the Tribunal's analysis with regard to the meaning of Article XI [of the Treaty].[177]

As to the suggestion, with reference to subsection 2(b) of Article 25 that the Argentine government contributed to the situation of necessity, 'there is no serious evidence in the record...'.[178]

Conclusion

The law on this issue is evidently not settled, and perhaps the sample here presented is too small to draw any firm conclusions.[179] It may be said, however, that the defence of necessity or emergency is available both under the typical BIT and under customary law as presently understood, and further, that tribunals applying BITs or similar agreements will look to the ILC Articles on State Responsibility for exposition of the customary law even when the claimant is a private actor.

Emergencies falling short of military threats may justify resort to the necessity defence, but the threshold is high. The differences in outcome of the two cases here discussed may be explained by the differences in setting that threshold. Neither of the tribunals accepted the proposition that the issue of necessity is one permitting self-judging by the state asserting the defence.[180] But the suggestion by the *CMS* tribunal that the choice among remedial measures, once a situation of crisis is established, is subject to review in an international arbitration seems, to this writer, unpersuasive, and unlikely to be followed by other tribunals.

[177] *LG&E* Decision, paras. 257- 258.

[178] Id. at paras. 256, 257.

[179] It is striking that one of the arbitrators, Judge Francisco Rezek of Brazil, was a member of both tribunals, each time nominated by Argentina.

[180] In the Model BIT published by the US State Department in 2004, the article corresponding to Article XI of the Argentina–US Treaty reads:

> Nothing in this Treaty shall be construed :
>
> ...
>
> 2. to preclude a Party from applying *measures that it considers necessary* for the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests (emphasis added).

(e) BITs and International Law

Given the large web of BITs covering every continent and countries from the First, the Second, and the Third World, a fair inference might be drawn that, taken together, the Bilateral Investment Treaties are now evidence of customary international law, applicable even when a given situation or controversy is not explicitly governed by a treaty.[181] Some writers strongly resist such an inference, arguing that any given BIT merely constitutes a *lex specialis* between the parties.[182] The argument is that to create or evidence customary law, states not only need to follow a certain practice, but need to do so from a sense of legal obligation (*opinio juris*).[183] Professor Guzman, for instance, writes:

> [S]igning a BIT offers an LDC an advantage in the competition for foreign investment. That BITs have been signed in large numbers merely demonstrates the magnitude of the perceived benefits associated with the dynamic inconsistency problem. Thus, if countries have signed BITs out of economic motives, the treaties should not be interpreted as evidence of customary international law. It is equally plausible that BITs represent a permissible derogation from the existing rules of customary law and that countries have pursued the treaties because it is in their economic interest to do so. This means that BITs offer no evidence concerning the rules of customary international law that govern compensation for appropriations.[184]

F. A. Mann, in contrast, writing well before the BITs had reached the level of acceptance that they reached in the last decade of the twentieth

[181] The word 'situation' is used to indicate that the issue need not arise only in the context of a dispute, but may, for instance, be raised if the government of Patria is considering a measure that might be inconsistent with international law, but not with any given treaty to which Patria is a party.

[182] See e.g. Bernard Kishoiyian, 'The Utility of Bilateral Investment Treaties in the Formulation of Customary International Law', 14 Northwestern J. Int'l L. & Business 327 (1994).

[183] Compare *Restatement (Third) of Foreign Relations Law*, n. 91 *supra*, § 102(2):

> Customary international law results from a general and consistent practice of states followed by them from a sense of legal obligation.

Comment *c*, on *opinio juris*, adds:

> For a practice of states to become a rule of customary international law it must appear that the states follow the practice from a sense of legal obligation (*opinio juris sive necessitatis*); a practice that is generally followed but which states feel legally free to disregard does not contribute to customary law. A practice initially followed by states as a matter of courtesy or habit may become law when states generally come to believe that they are under a legal obligation to comply with it. It is often difficult to determine when that transformation into law has taken place. Explicit evidence of a sense of legal obligation (e.g. by official statements) is not necessary; *opinio juris* may be inferred from acts or omissions.

See also the discussion of customary law in Ch. 15, Sect. 15.4 (b) at n. 49.

[184] Andrew T. Guzman, 'Why LDCs Sign Treaties that Hurt Them: Explaining the Popularity of Bilateral Investment Treaties', 38 Virginia J. Int'l L. 639, 686–667 (1998). By 'dynamic inconsistency' the author means a situation in which a preferred course of action cannot be undertaken without the establishment of some commitment mechanism; since contracts between a developing country host state and a foreign investor do not give a sufficient assurance to the investor, the host state is led to agree to a BIT. Id. at 658–660.

century, argued that by concluding BITs in large numbers, the developing countries that in the 1960s and 1970s had rejected the classical view of international law must have had a change of view:

> Is it possible for a State to reject the rule according to which alien property may be expropriated only on certain terms long believed to be required by customary international law, yet to accept it for the purpose of these treaties?[185]

To this writer, the debate need not be answered conclusively. There can be no doubt that bilateral investment treaties are relevant to the development of the international law of international investment:

- If Patria, a host country, is considering a given investment, existing or proposed, it should take its own and others' BITs into account, even if the investor in question is not from a contracting state with which Patria has concluded a BIT.
- Courts and arbitral tribunals, whether national or international, may rely on the common principles in the bilateral investment treaties.
- In adjudicating under a given BIT, courts and arbitral tribunals may, and indeed will be expected to, take into account decisions of other courts and tribunals that have heard disputes under comparable treaties.

Suppose Patria has entered into BITs with Xandia, Tertia, and Quarta, but not with Quinta. However, Patria has joined the ICSID Convention, and has consented to ICSID arbitration of disputes that may arise in connection with an investment agreement with Supranational Corporation [SUNATCO], a corporation organized and existing under the laws of Quinta. A dispute arises and is submitted to an ICSID Tribunal. In the present writer's view, the arbitrators should take into account all the obligations undertaken by Patria in its BITs with Xandia *et al.*, as evidence of Patria's understanding of international law, for the purpose of applying Article 42 of the ICSID Convention.[186] Patria should be given the opportunity to explain why it had not concluded a treaty with Quinta, but unless the explanation is compelling that a different standard of treatment of investors from Quinta

[185] F. A. Mann, 'British Treaties for the Promotion and Protection of Investment', 52 British Y.B. Int'l L. 241, 249 (1981). Dr Mann answered his question as follows:

> The paramount duty of States imposed by international law is to observe and act in accordance with the requirements of good faith. From this point of view it follows that, where these treaties express a duty which customary international law imposes or is widely believed to impose, they give very strong support to the existence of such a duty and preclude the Contracting States from denying its existence.

Id. at 249–250.

[186] Article 42, as discussed in Sect. 17.1(c) reads in the pertinent part:

> 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.

was contemplated and communicated to the government of Quinta and to SUNATCO, the failure to conclude an agreement with Quinta applicable to the dispute should not be decisive. In contrast, if Patria has consistently declined to conclude a BIT with any country, the argument in favour of applying the principle set out in the BITs, while not excluded, is significantly weaker.[187]

It is important in this discussion to distinguish between the *common principles* that may be said to have ripened into customary international law, and *particular provisions* of BITs that even if widely utilized are applicable only between the treaty partners or investors entitled to the benefits of the treaty in question. For example, an agreement to arbitrate under a particular set of rules, or a prohibition of specified performance requirements would not be regarded as general principles, but would depend on the applicability and text of a given treaty. But the understanding that international law is applicable to the relation between host states and foreign investors, that expropriation must be for a public purpose and must be accompanied by just compensation, and that disputes between foreign investors and host states should be subjected to impartial adjudication or arbitration are general principles, and do not depend on the wording or indeed on the existence of any given treaty.

17.4 THE MULTILATERAL INVESTMENT GUARANTEE AGENCY (MIGA)

(a) Introduction

In the early 1980s, the staff of the World Bank, urged by its new President, A. W. Clausen of the United States, launched a project for a Bank-sponsored multinational agency that would 'enhance the flow of developing countries of capital and technology for productive purposes' by improving the conditions for direct foreign investment and reducing—and insuring against—the political risks of such investment.[188] The promoters of MIGA had two purposes in mind. One, of course, was to create a multilateral investment guarantee agency linked in some way to the World Bank. Beyond this, by involving all member states of the World Bank in serious debate and infor-

[187] Not many countries fit into the category of states that have not entered into any modern bilateral investment treaties. Libya, Myanmar (Burma), and Suriname had concluded no BITs as of year-end 2006. Among developed countries, Ireland appears to be the only one that has not concluded a BIT. It is, however, a party to several treaties of Friendship, Commerce and Navigation, which contain some of the same guarantees in less detail.

[188] For a detailed history of the often difficult negotiations that led to the creation of MIGA, see Ibrahim Shihata, *MIGA and Foreign Investment: Origins, Operations, Policies and Basic Documents of the Multilateral Investment Guarantee Agency* (1988).

mation exchange, the sponsors of MIGA sought to change the 'investment climate' in developing countries.

The 1970s had been the decade of the New International Economic Order.[189] In the five years preceding the first consideration of MIGA in 1983 by the Executive Directors of the World Bank, i.e. 1978–82, 42 expropriations had taken place in 24 countries of Africa, Latin America, and Asia.[190] At the same time, the debt crisis of many developing countries had severely slowed down commercial bank lending, and had further undermined confidence among potential investors in the developing world.[191] MIGA would be a vehicle, it was hoped, for turning these trends around. This could be achieved by a combination of technical assistance to developing countries that sought to attract foreign investment—what kind of laws, infrastructure, and attitudes would be useful—and by establishing an institution whose common purpose would be clear, but where the developing countries, i.e. the potential host countries, would have an equal say with the developed countries.

Thus MIGA could serve as an honest broker, 'guiding all concerned parties', as its brochure stated,[192] 'toward a common definition of fairness and equitable treatment'. In addition to investment guarantees and insurance, MIGA's Legal and Claims Department could provide legal advice and guidance to parties involved in investment disputes, not necessarily covered by an investment guarantee issued by MIGA.[193]

The World Bank's Board of Governors approved the MIGA Convention in the fall of 1985, but it took two and a half more years before the minimum number of states in each category—five from Category One, the developed states, and fifteen from Category Two, the developing states—had deposited their instruments of ratification.[194] As of mid-year 2007, MIGA had 23 industrial and 147 developing country members.

(b) Covered Risks

Eligible investors can purchase insurance against risks of inconvertibility of local currency; expropriation; breach of contract; and war and civil disturbance, including politically motivated acts of sabotage or terrorism.[195]

[189] See Ch. 15, Sect. 15.5(b).

[190] See Multinational Investment Guarantee Agency, *The First Ten Years*, 3 (1998).

[191] See Ch. 20, Sects. 20.1–20.4.

[192] MIGA, *The First Ten Years*, n. 190 *supra*, 6.

[193] See MIGA Convention Article 23(b), which under the heading 'Investment Promotion' provides that the Agency shall 'encourage the amicable settlement of disputes between investors and host countries', without reference to MIGA insurance.

[194] *Convention Establishing the Multilateral Investment Guarantee Agency*, done at Seoul, 11 Oct 1985, entered into force 12 April 1988, 1988 T.I.A.S. 12089, 1508 U.N.T.S. 99. The requirements for entry into force appear in Article 61.

[195] MIGA Convention, Article 11.

To be an eligible investor, a person must be a national of a member country other than the host country, a corporation organized or established in such a country, or, if it is incorporated in the host country, a corporation the majority of whose capital is owned by nationals of member countries.[196] Two interesting additional classes of investors are stated to be eligible for coverage by MIGA. *First*, state-owned enterprises are eligible if they operate on a commercial basis. Thus, for instance, the Norwegian Statoil, the Mexican Pemex, and numerous enterprises of the People's Republic of China, would qualify as investors if they undertook a project in another eligible country. *Second*, upon agreement of the host country and the investor, the MIGA Board may extend eligibility to an investor (natural or juridical) from the host country that seeks to engage in so-called 'round-tripping'—i.e. to invest assets left abroad back to the host country, thus reversing prior capital flight.[197]

Eligible projects can include new investments as well as expansion, modernization, restructuring, and privatization of existing investments, and in some circumstances loans made or guaranteed by holders of equity in the enterprise in question.[198]

(c) MIGA and International Law

If the practice of states and international organizations is evidence of prevailing thinking about international law, the MIGA Convention—adhered to by more than 150 states—developed and developing—makes several contributions to international law and to the receptivity of foreign direct investment loosely referred to as investment climate. Not only does it state explicitly the objective 'to encourage the flow of investment for productive purposes among member countries, and in particular to developing member countries' (Art. 2),[199] Article 12 concerning investments eligible for a MIGA guarantee states, in paragraph (d):

> In guaranteeing an investment, the Agency shall satisfy itself as to
>
> . . .
>
> (iv) the investment conditions in the host country, including the availability of fair and equitable treatment and legal protection for the investment.

[196] This provision, which acknowledges the requirement in many states that corporations must be locally incorporated but then looks to ownership and control, is similar to Article 25(2)(b) of the ICSID Convention, discussed in Sect. 17.1(b).

[197] MIGA Convention, Article 13.

[198] Id. at Article 12.

[199] Contrast this commitment of 1988 with the very different tone and substance of the excerpt from the Charter of Economic Rights and Duties of States of 1974, reproduced in Ch. 15, Sect. 15.5(b) at n. 68.

A promise of the host country addressed only to the particular investment is not sufficient. The Agency must be satisfied with the 'investment conditions'.[200] Turning the sentence around, if Patria fails to accord fair and equitable treatment for one investment, it cannot count on approval of a MIGA investment guarantee for another investment.

Further, Article 23, which is directed to Investment Promotion, i.e. not explicitly to issuance of investment guarantees, states in section (b):

> The Agency also shall:
> (i) encourage the amicable settlement of disputes between investors and host countries;
> (ii) endeavor to conclude agreements with developing member countries, and in particular with prospective host countries, which will assure that the Agency, with respect to investment guaranteed by it, has treatment at least as favorable as that agreed by the member concerned for the most favored investment guarantee agency or State in an agreement relating to investment, such agreements to be approved by special majority of the Board; and
> (iii) promote and facilitate the conclusion of agreements, among its members, on the promotion and protection of investments.

Thus, far from maintaining the traditional neutrality of international agencies toward investment in developing countries, the MIGA Convention requires the agency to encourage developing countries to enter into Bilateral Investment Treaties; to join the ICSID Convention, or to adopt other indicia of an investor-friendly legal regime. The official Commentary to the MIGA Convention confirms that in case no protection is assured under the laws of a host country or a BIT, the Agency will issue a guarantee only after it reaches agreement with the host country pursuant to Article 23(b)(ii), in which case investments guaranteed by the host country will receive MFN treatment.[201]

Finally, as pointed out in the preceding section, there has been and continues to be a debate about the contours of *expropriation*, which requires compensation (and almost always triggers an investment guarantee if one is applicable), and regulation, which does not call for compensation and generally does not engage international law unless it is discriminatory or violates fair and equitable treatment. The MIGA Convention adopts a fairly broad definition of 'expropriation and similar measures', and makes

[200] See Shihata, *MIGA and Foreign Investment*, n. 188 *supra*, 222–223.

[201] *Commentary on the Convention Establishing Multilateral Investment Guarantee Agency*, republished in Shihata, *MIGA and Foreign Investment*, n. 188 *supra*, at Appendix 3 and on MIGA's Website, paras. 21 and 44, Article 44. Agreements under Article 23(b)(ii) require approval of the MIGA board by a special majority.

clear that the focus is on the loss to the investor, not on the gain to the host government:

> any legislative action or administrative action or omission attributable to the host government which has the effect of depriving the holder of a guarantee of his ownership or control of, or a substantial benefit from, his investment, with the exception of non-discriminatory measures of general application which the governments normally take for the purpose of regulating economic activity in their territories.[202]

Breach of contract is in some ways more difficult, because it is clear that neither MIGA nor traditional international law is concerned with commercial risks, and it is not always clear whether a contract with a government or governmental agency is repudiated for commercial or 'sovereign' purposes. MIGA's solution is not to attempt to distinguish among the motives of the host government, but to link the scope of its coverage to the remedies available to the holder of a guarantee. Thus MIGA will cover any repudiation or breach by the host government of a contract with the holder of a guarantee, when (a) the holder of a guarantee does not have recourse to a judicial or arbitral forum to determine the claim of repudiation or breach, (b) a decision by such forum is not rendered within such reasonable period of time as shall be prescribed in the contracts of guarantee pursuant to the Agency's regulations, or (c) such a decision cannot be enforced.[203]

The regulations define the reasonable period as not less than two years, and define judicial or arbitral forum as 'any competent court or arbitral tribunal which is independent from the executive branch of the host government, acts judicially, and is authorized to make a final and binding decision'.[204]

There can be little doubt that these various provisions, and their broad acceptance by countries all around the globe, reflect and contribute to a relatively warm investment climate. The more difficult and controversial question is whether these provisions, along with similar provisions in a great many BITs, and in regional agreements such as the NAFTA, reflect and contribute to the international *law* of international investment. One could take the position that MIGA clauses, like provisions of specific bilateral investment treaties, bind only the parties to those arrangements, and that states subscribing to them do so on the basis of a particular

[202] MIGA Convention, Article 11(a)(ii). The Commentary adds in para. 14 that the definition would encompass measures attributable to the host government such as nationalization, confiscation, sequestration, seizure, attachment, and freezing of assets. It would include measures by the executive, but not measures taken by judicial bodies in exercise of their functions.

[203] MIGA Convention, Article 11(a)(iii).

[204] MIGA Operational Regulations, Sects. 1.42, 1.43.

calculation of advantage, not from any sense of obligation.[205] A more sophisticated understanding, in the view of the present author, would regard the MIGA Convention, even more than the web of bilateral (and in the case of NAFTA trilateral) agreements as evidence of state practice and of a growing consensus that may well be regarded, not just by writers, but by courts, arbitral tribunals, and governments as laws. It is fair to add that if one regards these commitments as law, very little breach occurred in the last two decades of the twentieth century, as compared with the preceding three decades.[206]

SUMMARY

The corpus of international law concerning international investment, and in particular the relation between host countries and foreign investors, greatly expanded in the last quarter of the twentieth century. Two major treaties sponsored by the World Bank have endeavoured—with considerable success—to improve the investment climate and to encourage transborder investment as a vehicle for economic growth. Over a thousand bilateral investment treaties have provided specific protections and guarantees for foreign investors, and—one may fairly say—have contributed to prevailing customary international law. The pace and content of international arbitration of investment disputes has vastly increased, notably in the hundreds of decisions rendered over more than a decade by the Iran–United States Claims Tribunal, but also in arbitrations under ICSID, BITs, and NAFTA. The resolution of disputes under international law directly between foreign investors and host states has become firmly established.

The law that emerges from this rich load of sources—treaties, statutes, scholarly writing, and arbitral awards—is not wholly uniform. No body of law is monolithic, and certainly one would not expect complete consensus on the subject of international investment, inevitably intertwined with history, economics, and politics—local and international. But there has been a substantial shift from the time when the United States Supreme Court issued the famous statement quoted at the beginning of this Part. In 1964, the Supreme Court could fairly write of the law concerning expropriation 'There are few if any issues on which opinions are so divided.' That statement, it is submitted, could not be made at the beginning of the third millennium.

[205] This is the position, for example, of Prof. Andrew Guzman, in 'Why LDCs Sign Treaties that Hurt Them', n. 184 *supra*, writing specifically about BITs but more generally about the growing mass of instruments setting down definitions and guides to behaviour concerning investments.

[206] But as this volume went to press in mid-year 2007, developments in Bolivia, Venezuela, and perhaps other countries of Latin America (see n. 20 *supra*) suggested caution in using the statement in the text as a basis for predicting the future.