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Principles of International Investment Law

Second Edition

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reference to domestic law will, in itself, raise the question whether an international tribunal would, in view of its own legal basis and in light of the rules of international law applicable to aliens and foreign companies, invariably consider international rules irrelevant.[12]

The Permanent Court of International Justice, in the *Serbian Loans* case, pointed to the requirement that every contract must have a basis in a national legal order.[13] In light of that statement, tribunals have seen no reason to address the role of general rules of international law governing aliens.[14]

3. Stabilization clauses

Investment agreements are negotiated by the investor and the host state to allow for special rules between the two parties, separate from the general legislation of the host state. In principle, it will be the intention of both sides to create a legal framework that will last from the beginning to the end of their common project.

For the investor, a key concern will invariably be to safeguard the stability of the agreement. Applicable treaties between the host state and the investor's home state may provide for rules desiged to ensure or to promote stable contractual relations for their citizens—such as umbrella clauses—or a provision on fair and equitable treatment. However, such rules will not always be in place,[15] or they may not be as specific as desired by the investor. Against this background, an ongoing practice of including a stabilization clause in state-investor agreements has developed.[16] No single specific wording of such clauses has emerged and different types, with different functions and scope, have been drafted. In consequence, the significance and interpretation of each such clause will have to be assessed in light of its specific wording.

It is not surprising that investors have sought to negotiate stabilization clauses in particular with those states whose political and legal regime has in the past been subject to frequent changes or volatility. Governments of such states may have reason to agree to such clauses because they wish to attract foreign investment and because stability serves as an instrument to facilitate this goal.[17] For the host

[12] See p 288–93.

[13] PCIJ, Judgment No 14, Series A, No 20, 41: 'Any contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of some country.'

[14] See *Delagoa Bay Claim (UK v Portugal)*, Award, 24 July 1875, 28 RIAA 157; *Lena Goldfields v Soviet Union* (1930), (1950) 36 *Cornell LQ* 31, 42; *Aramco v Saudi Arabia* (1958) 27 ILR (1963) 117 and, on the relationship of international law with domestic law, *Ruler of Qatar v International Marine Oil Company* (1953) 20 ILR 534.

[15] For recent practice, see P Cameron, *International Energy Investment Law: The Pursuit of Stability* (2010) 233 et seq.

[16] *Amoco International Finance v Iran*, 15 Iran–US CTR 189, 239 (1987), observed that the term 'stabilization clause' normally refers to 'contract language which freezes the provisions of a national system of law chosen as the law of the contract as to the date of the contract in order to prevent the application to the contract of any future alterations of this system'.

[17] See also A Faruque, 'Validity and Efficiency of Stabilization Clauses: Legal Protection vs Fundamental Value' (2006) 23 *J Int'l Arbitration* 317, 335.

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country, a stabilization clause may be more attractive than a treaty, which requires lengthy international negotiations and ratification processes. Some states have introduced specific legislation which authorizes the executive branch to conclude a special contract stabilizing the actual agreement ('Legal Stability Agreement' (LSA)).[18]

A stabilization clause in the strongest sense would require the host state not to alter its general legal regime for the area addressed in the clause. Typically, however, the investor's concern will be limited to the stability of the individual agreement it has concluded with the host state. Thus, stabilization in the form of an intangibility clause[19] will provide that changes in the law of the host state will not apply to the investment contract. It is not uncommon for the contract to limit the scope of the stabilization clause to specific areas such as tax law.[20] Another version consists of so-called freezing clauses. These will incorporate into the agreement, as the applicable law, the law of the host state as it stands at a specified time, such as the law valid when the contract enters into force.[21]

A doctrinal issue that arises for stabilization clauses in general is whether they will bind the host state or whether the sovereignty of the state will operate to allow a change of the stabilization clause itself. No international tribunal has ruled that a stabilization clause is invalid or will have no legal effect.

In *AGIP v Congo*,[22] the Tribunal had to deal with a stabilization clause that ensured that changes in domestic law by the Congo would not affect certain parts of the contract (pertaining to the nature of the protected company) with AGIP. When, later on, the Congo nationalized the company, the Tribunal examined the compatibility of the nationalization decree with the stabilization clause from the viewpoint of international law (to which the contract explicitly referred). The Tribunal ruled:

> These stabilization clauses, which were freely entered into by the Government, do not affect the principle of its legislative and regulatory sovereignty since it retains both with respect to those, whether nationals of foreigners, with whom the Government has not entered into such undertakings, and that, in the present case, they are limited to rendering the modifications to the legislative regulatory provisions provided for the Agreement, unopposable to the other contracting party.
>
> ... It suffices to concentrate the examination of the compatibility of the nationalization with international law on the stabilization clauses. It is indeed in connection with these clauses that the principles of international law are used to complete the rules of Congolese law. The reference made to international law suffices to demonstrate the nationalization

[18] In *Duke Energy v Peru*, Award, 18 August 2008, the Tribunal had to interpret such an LSA; see also Cameron, n 15, 246 et seq on LSAs.

[19] Sometimes also called an inviolability clause; for examples see Cameron, n 15, 74.

[20] For examples, see Cameron, n 15, 70.

[21] In *Duke Energy v Peru*, Award, 18 August 2008, the Tribunal found that not only the text but also its interpretation was frozen.

[22] *AGIP v Congo*, Award, 30 November 1979.

carried out in the present case. It follows that the Government is obliged to compensate AGIP for the damage suffered by it as a result of the nationalization...[23]

In *LETCO v Liberia*,[24] the Tribunal explained:

> This clause, commonly referred to as a 'Stabilization Clause', is commonly found in long-term development contracts and... is meant to avoid the arbitrary actions of the contracting government. This clause must be respected, especially in this type of agreement. Otherwise, the contracting State may easily avoid its contractual obligations by legislation.[25]

In *Aminoil v Kuwait*,[26] the Tribunal concluded that a typical stabilization clause should not be presumed to imply that a state lost the right to expropriate a contract running for a period of 60 years. The Tribunal came to the conclusion that the main effect of a stabilization clause would lie in the calculation of the amount of compensation, provoking a sharp dissent from Arbitrator Fitzmaurice.

The ruling in *Amoco International Finance v Iran*[27] follows the *Aminoil* pattern to a considerable extent, but with a different view on this point in the Concurring Opinion of Judge Brower. The majority in the *Amoco* case also took the view that a typical stabilization clause in a contract should not be understood as a renunciation on the part of the host state of its right to expropriate a concession.

None of the cases discussed here had to apply an umbrella clause in an investment treaty, which is designed to protect an investor against violation of a contractual arrangement.

The premise of this jurisprudence (mostly not articulated) is the recognition that a state has the power to bind itself, from the viewpoint of an international tribunal, and that respect for the principle *pacta sunt servanda* as well as the principle of good faith will stand in the way of an attempt to ignore the contractual bond. Tribunals have differed in their views whether a violation of the stabilization clause will require specific performance of the contract[28] or whether the aggrieved party has a right to be compensated for its loss.[29]

Special questions will arise when a stabilization clause is included in a contract between an entity created by the state, such as a national company, and a foreign investor. Here, it will be relevant whether the national company has been given the power to bind the state or whether the foreign investor may rely on such a commitment on other grounds such as good faith; tribunals have not yet clarified the point.

In the oil and gas industry, it is not infrequent that stabilization is achieved by means other than a stabilization clause in the conventional sense. One technique here is that investment agreements provide that the national oil company, being the

[23] At paras 86–8.
[24] *LETCO v Liberia*, Award, 31 March 1989.
[25] 2 ICSID Reports 368. See also *MINE v Guinea*, Decision on Annulment, 22 December 1989, paras 6.33, 6.36; *CMS v Argentina*, Award, 12 May 2005, para 151.
[26] *Aminoil v Kuwait*, Award, 24 March 1982.
[27] *Amoco International Finance v Iran*, Award, 14 July 1987.
[28] *TOPCO v Libya*, Award, 19 January 1977.
[29] *LIAMCO v Libya*, Award, 12 April 1977, with an explicit recognition of *pacta sunt servanda*.

investor's contractual partner, will pay the tax for the foreign investor and that this will also be so in the event of a future change of domestic tax law.

4. Renegotiation/adaptation

As an alternative to preserving the sanctity and stability of a contract, the more recent trend has been to agree on a renegotiation clause. Such a clause may focus on economic equilibrium rather than on legal stability.[30] The following clause was, for instance, adopted in 1994 in the Model Exploration and Production Sharing Agreement of the Sheikdom of Qatar:

> Art. 34.12 Equilibrium of the Agreement
>
> Whereas the financial position of the Contractor has been based, under the Agreement, on the laws and regulations in force at the Effective Date, it is agreed that, if any future law, decree or regulation affects Contractor's financial position, and in particular if the customs duties exceed... percent during the term of the Agreement, both parties shall enter into negotiations, in good faith, in order to reach an equitable solution that maintains the economic equilibrium of this Agreement. Failing to reach agreement on such equitable solution, the matter may be referred by either Party to arbitration pursuant to Article 31.[31]

Difficulties will arise if the circumstances triggering the right to renegotiate, usually on the part of the investor, are not described in sufficient detail in the investment contract. Beyond the triggering clause, the parties have various choices for structuring the actual process of appropriate renegotiation. Adaptation of a contract based on automatically applicable criteria is rarely foreseen. Typically, renegotiation clauses rely on criteria that leave room for negotiation. Sometimes no criteria for the process of renegotiation are included.

Obviously, renegotiation clauses provide for more flexibility than a stabilization clause, but their practicability and usefulness are questionable. The concept of an 'economic equilibrium' remains to be defined in legal terms. Moreover, a duty to

[30] See also R Geiger, 'Unilateral Change of Economic Developments Agreements' (1974) 23 *ICLQ* 73; M Sornarajah, 'Supremacy of the Renegotiations Clause in International Contracts' (1988) 5 *J Int'l Arb* 113; W Peter, *Arbitration and Renegotiation of International Investment Agreements* (1995) 240; A Kolo and T Wälde, 'Renegotiation and Contract Adaptation in International Investment Projects' (2000) 1 *J World Investment & Trade* 5, 7; T Waelde and G Ndi, '"Stabilizing International Investment Commitments": International Law versus Contract Integration' (1996) 31 *Texas Int'l LJ* 228; J Salacuse, 'Renegotiating International Business Transactions: The Continuing Struggle of Life Against Form' (2001) 35 *Int'l Lawyer* 1507, 1519; J Gotanda, '"International Commercial Arbitration: Renegotiation and Adaptation Clauses in Investment Contracts", Revisited' (2003) 36 *Vanderbilt J Transn'l L* 1461; K Berger, 'Renegotiation and Adaptation in International Investment Contracts: The Role of Contracts Drafters and Arbitrators' (2003) 36 *Vanderbilt J Transn'l L* 1347, 1361; S Kröll, 'The Renegotiation and Adaptation in Investment Contracts' in N Horn, *Arbitrating Foreign Investment Disputes* (2004).

[31] The clause is reprinted in P Bernardini, 'The Renegotiation of Investment Contracts' (1998) 13 *ICSID Review-FILJ* 411, 416; for similar clauses and their significance, see also K Berger, 'Renegotiation and Adaptation of International Investment Contracts: The Role of Contract Drafters and Arbitrators' (2003) 36 *Vanderbilt J Transn'l L* 1347.

VI

Expropriation

The rules of international law governing the expropriation of alien property have long been of central concern to foreigners in general and to foreign investors in particular. Expropriation is the most severe form of interference with property. All expectations of the investor are destroyed if the investment is taken without adequate compensation.

On the level of customary international law, the minimum standard for the protection of aliens came to place limitations on the territorial sovereignty of the host state and to protect alien property. On the level of treaty law, all modern agreements on foreign investment contain specific provisions covering preconditions for and consequences of expropriation.

1. The right to expropriate

Consistent with the notion of territorial sovereignty, the classical rules of international law have accepted the host state's right to expropriate alien property in principle. Indeed, state practice has considered this right to be so fundamental that even modern investment treaties (often entitled agreements 'for the promotion and protection of foreign investment') respect this position. Treaty law typically addresses only the conditions and consequences of an expropriation, leaving the right to expropriate as such unaffected.[1]

Even clauses in agreements between the host state and the investor that freeze the applicable law for the period of the agreement ('stabilization clauses')[2] will not necessarily stand in the way of a lawful expropriation. The position is less clear if such an agreement explicitly excludes the right to expropriate. Except in extreme circumstances, an international tribunal will probably interpret such a clause in a literal manner. In practice, however, such far-reaching provisions have played no significant role.

[1] Some states (eg Ecuador, Peru) have in the past provided in their constitutions that their contractual agreements with foreign investors may not be changed by a unilateral act. But they have not gone as far as excluding the right to expropriate. Article 249 of the Constitution of Ecuador (1998) provided for all contracts relating to public services: 'The agreed contractual conditions cannot be modified unilaterally by law or other measures.' Article 62 of the 1993 Peruvian Constitution states: 'Through contract-laws, the State can establish guarantees and grant assurances. They may not be amended legislatively.'

[2] See pp 82 et seq.

2. The three branches of the law

Beyond the right of the host state to expropriate, international law on expropriation has developed three branches, which regulate the scope and conditions of the exercise of this power. The first one defines the interests that will be protected. This facet has not traditionally been in the forefront of academic and practical discussions but has received some prominence more recently. Most contemporary treaties, in their provisions dealing with expropriation, refer to 'investments'. Similarly, the jurisdiction of arbitral tribunals is typically restricted to disputes arising from 'investments'. Therefore, it is 'investments' as defined in these treaties that are protected.[3]

The second branch concerns the definition of an expropriation. While this matter raises no questions in cases of a formal expropriation, the issue may acquire a high degree of complexity when the host state interferes with the rights of the foreign owner without a formal taking of title. Indeed, in the practice of the past three decades, most cases relating to expropriation have turned on the controversy of whether or not a 'taking' had actually occurred. Matters of public health, the environment, or general changes in the regulatory system may prompt a state to regulate foreign investments. This has led to claims against the state on the basis that a regulatory taking or indirect expropriation has occurred. The elements of indirect expropriation are discussed below.[4]

The third branch of the law on expropriation relates to the conditions under which a state may expropriate alien property. The classical requirements for lawful expropriation are a public purpose, non-discrimination, as well as prompt, adequate, and effective compensation. In practice, the requirement of compensation has turned out to be the most controversial aspect. This issue is discussed in the next section.

3. The legality of the expropriation

It is today generally accepted that the legality of a measure of expropriation is conditioned on three (or four) requirements. These requirements are contained in most treaties. They are also seen to be part of customary international law. These requirements must be fulfilled cumulatively:

- The measure must serve a public purpose. Given the broad meaning of 'public purpose', it is not surprising that this requirement has rarely been questioned by the foreign investor. However, tribunals did address the significance of the term and its limits in some cases.[5]

[3] For the concept of an investment, see pp 60 et seq. See further p 248.

[4] See pp 101 et seq.

[5] See eg *ADC v Hungary*, Award, 2 October 2006, paras 429–33.

- The measure must not be arbitrary and discriminatory within the generally accepted meaning of the terms.
- Some treaties explicitly require that the procedure of expropriation must follow principles of due process.[6] Due process is an expression of the minimum standard under customary international law and of the requirement of fair and equitable treatment. Therefore, it is not clear whether such a clause, in the context of the rule on expropriation, adds an independent requirement for the legality of the expropriation.
- The expropriatory measure must be accompanied by prompt, adequate, and effective compensation. Adequate compensation is generally understood today to be equivalent to the market value of the expropriated investment.

Of these requirements for the legality of an expropriation, the measure of compensation has been by far the most controversial. In the period between roughly 1960 and 1990, the rules of customary law on compensation were at the centre of the debate on expropriation. They were discussed in the broader context of economic decolonization, the notion of 'Permanent Sovereignty over Natural Resources', and of the call for a new international economic order. Today, these fierce debates are over and nearly all expropriation cases before tribunals follow the treaty-based standard of compensation in accordance with the fair market value. In the terminology of the earlier decades this means 'full' or 'adequate' compensation. However, this does not mean that the amount of compensation is easy to determine. Especially in cases of foreign enterprises operating on the basis of complex contractual agreements, the task of valuation requires close cooperation of valuation experts and the legal profession.

Various methods may be employed to determine market value. The discounted cash flow method will often be a relevant yardstick, rather than book value or replacement value, in the case of a going concern that has already produced income. Before the point of reaching profitability, the liquidation value will be the more appropriate measure.[7]

A traditional issue that has never been entirely resolved concerns the consequences of an illegal expropriation. In the case of an indirect expropriation, illegality will be the rule, since there will be no compensation.

According to one school of thought, the measure of damages for an illegal expropriation is no different from compensation for a lawful taking. The better view is that an illegal expropriation will fall under the general rules of state responsibility, while this is not so in the case of a lawful expropriation accompanied by compensation. In the case of an illegal act the damages should, as far as possible, restore the situation that would have existed had the illegal act not been committed. By contrast, compensation for a lawful expropriation should represent the market value at the time of the taking. The result of these two methods can be markedly

[6] See eg the 2004 and 2012 US Model BITs, Art 6(1)(d).
[7] See pp 296–7.

different.[8] The difference will mainly concern the amount of lost profits. The issue of compensation and damages is discussed in more detail in Chapter X on the settlement of investment disputes.[9]

The requirement of 'prompt' compensation means 'without undue delay'.[10] The requirement of 'effective' compensation means that payment is to be made in a convertible currency.[11]

4. Direct and indirect expropriation

The difference between a direct or formal expropriation and an indirect expropriation turns on whether the legal title of the owner is affected by the measure in question. Today direct expropriations have become rare.[12] States are reluctant to jeopardize their investment climate by taking the drastic and conspicuous step of an open taking of foreign property. An official act that takes the title of the foreign investor's property will attract negative publicity and is likely to do lasting damage to the state's reputation as a venue for foreign investments.

As a consequence, indirect expropriations have gained in importance. An indirect expropriation leaves the investor's title untouched but deprives him of the possibility of utilizing the investment in a meaningful way. A typical feature of an indirect expropriation is that the state will deny the existence of an expropriation and will not contemplate the payment of compensation.

(a) Broad formulae: their substance and evolution

The contours of the definition of an indirect expropriation are not precisely drawn. An increasing number of arbitral cases and a growing body of literature on the subject have shed some light on the issue but the debate goes on.[13] In some recent decisions by the International Centre for Settlement of Investment Disputes (ICSID), tribunals have interpreted the concept of indirect expropriation narrowly and have preferred to find a violation of the standard of fair and equitable treatment.[14]

The concept of indirect expropriation as such was clearly recognized in the early case law of arbitral tribunals and of the Permanent Court of International Justice

[8] See eg D W Bowett, 'State Contracts with Aliens: Contemporary Developments on Compensation for Termination or Breach' (1988) 59 *BYIL* 47; *Case Concerning the Factory at Chorzów*, 1928, PCIJ, Series A, No 17, 47. For a full discussion, see I Marboe, 'Compensation and Damages in International Law, The Limits of "Fair Market Value"' (2006) 7 *J World Investment & Trade* 723.
[9] See pp 294–7.
[10] R Dolzer and M Stevens, *Bilateral Investment Treaties* (1995) 112.
[11] Dolzer and Stevens, n 11.
[12] But see *Funnekotter v Zimbabwe*, Award, 22 April 2009.
[13] See Y Fortier and S L Drymer, 'Indirect Expropriation in the Law of International Investment: I Know It When I See It, or Caveat Investor' (2004) 19 *ICSID Review-FILJ* 293.
[14] See pp 117 et seq.

(PCIJ) in the 1920s and 1930s.[15] Today it is generally accepted that certain types of measures affecting foreign property will be considered an expropriation, and require compensation, even though the owner retains the formal title. What was and remains contentious is drawing the line between non-compensable regulatory and other governmental activity and measures amounting to indirect, compensable expropriation. The issue is of equal importance to the host state, which may wish to broaden the range of non-compensable activities, and to the foreign investor, who will argue in favour of a broad understanding of the concept of indirect takings.

Bilateral and multilateral treaties and draft treaties typically contain a reference to indirect expropriation or to measures tantamount to expropriation. The Abs–Shawcross Draft Convention on Investment Abroad (1959) referred to 'measures against nationals of another Party to deprive them directly or indirectly of their property'. Essentially, the same wording appears in the 1967 Organisation for Economic Co-operation and Development (OECD) Draft Convention on the Protection of Foreign Property. The Draft United Nations Code of Conduct on Transnational Corporations referred to '[a]ny such taking of property whether direct or indirect'. The 1992 World Bank Guidelines on the Treatment of Foreign Direct Investment speaks of expropriation or 'measures which have similar effects'. Similarly, the 1998 OECD Draft for a Multilateral Agreement on Investment refers to 'measures having equivalent effect'. Another variation is contained in the North American Free Trade Agreement (NAFTA) of 1992, which speaks of 'a measure tantamount to nationalization or expropriation'. The 1994 Energy Charter Treaty similarly refers to 'a measure or measures having effect equivalent to nationalization or expropriation'.

Most current bilateral investment treaties contain similar language. The current French Model Treaty states: 'Neither Contracting Party shall take any measures of expropriation or nationalization or any other measures having the effect of dispossession, direct or indirect, of nationals or companies of the other Contracting Party of their investments.'[16] According to the German Model Treaty '[i]nvestments by investors of either Contracting State shall not directly or indirectly be expropriated, nationalized or subjected to any other measure the effects of which would be tantamount to expropriation or nationalization'.[17] The Model Treaty used by the United Kingdom provides that '[i]nvestments of nationals or companies of either Contracting Party shall not be nationalized, expropriated or subjected to measures having effect equivalent to nationalization or expropriation'.[18]

The 2004 and 2012 US Model BITs approach the issue in greater detail. After stating in Article 6(1) that '[n]either Party may expropriate or nationalize a covered investment either directly or indirectly through measures equivalent to expropriation or nationalization',[19] a special Annex B entitled 'Expropriation' adds:

[15] See *Norwegian Shipowners' Claims*, I RIAA 307 (1922); *Case Concerning Cert German Interests in Polish Upper Silesia*, 1926, PCIJ, Series A, No 7, 3.
[16] French Model Treaty, Art 6(2).
[17] German Model Treaty, Art 4(2).
[18] UK Model Treaty, Art 5(1).
[19] See US Model BITs, Art 6(1).

(a) The determination of whether an action or series of actions by a Party, in a specific fact situation, constitutes an indirect expropriation, requires a case by case, fact-based inquiry that considers, among other factors: (i) the economic impact of the government action, although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred; (ii) the extent to which the government action interferes with distinct, reasonable investment-backed expectations; and (iii) the character of the government action.

(b) Except in rare circumstances, non-discriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations.[20]

Among the broader formulae proposed in general studies and drafts, some have received special attention in the decisions of arbitral tribunals and in academic writings. Harvard Professors Sohn and Baxter included in their 1961 Draft Convention on the International Responsibility of States for Injuries to Aliens, a version that is elaborate and contains specific categories of indirect takings:

> A taking of property includes not only an outright taking of property but also any such unreasonable interference with the use, enjoyment, or disposal of property as to justify an inference that the owner thereof will not be able to use, enjoy, or dispose of the proper y within a reasonable period of time after the inception of such interference.[21]

The 1986 *Restatement (Third) of the Foreign Relations Law of the United States* (§ 712) is much shorter and in its text only speaks of a 'taking'. Comment (g) refers to actions 'that have the effect of "taking" the property, in whole or in large part, outright or in stages ("creeping expropriation")'.

A United Nations Conference on Trade and Development (UNCTAD) study, prepared in 2000, uses different language and considers that 'measures short of physical takings may amount to takings in that they result in the effective loss of management, use or control, or a significant depreciation of the value, of the assets of a foreign investor'.[22]

In an early influential article Gordon Christie reviewed the then existing case law and pointed to certain recognized groups and categories of indirect takings, without an attempt to present a general formula.[23] Judge Rosalyn Higgins, in her 1982 Hague Lectures, questioned the usefulness of a distinction between non-compensable bona fide governmental regulation and 'taking' for a public purpose:

> Is this distinction intellectually viable? Is not the State in both cases (that is, either by a taking for a public purpose, or by regulating) purporting to act in the common good? And in each case has the owner of the property not suffered loss? Under international law standards,

[20] 2004 and 2012 US Model BITs, Annex B, para 4.
[21] L B Sohn and R R Baxter, 'Responsibility of States for Injuries to the Economic Interests of Aliens' (1961) 55 *AJIL* 545, 553 (Art 10(3)(a)). *ain*
[22] UNCTAD, *Series on Issues in International Investment Agreements: 'Taking of Property'* (2000) 4.
[23] G C Christie, 'What Constitutes a Taking of Property under International Law?' (1962) 38 *BYBIL* 307.

a regulation that amounted (by virtue of its scope and effect) to a taking, would need to be 'for a public purpose' (in the sense of a general, rather than for a private, interest). And just compensation would be due.[24]

It has been argued elsewhere that the international law of expropriation has essentially grown out of, and mirrored, parallel domestic laws.[25] As a consequence of this linkage, it appears plausible that measures that are, under the rules of key domestic laws, normally considered regulatory without requiring compensation, will not require compensation under international law either.

The importance of the effect of a measure for the question of whether an expropriation has occurred was highlighted by Reisman and Sloane:

> tribunals have increasingly accepted that expropriation must be analyzed in consequential rather than in formal terms. What matters is the effect of governmental conduct—whether malfeasance, misfeasance, or nonfeasance, or some combination of the three—on foreign property rights or control over an investment, not whether the state promulgates a formal decree or otherwise expressly proclaims its intent to expropriate. For purposes of state responsibility and the obligation to make adequate reparation, international law does not distinguish indirect from direct expropriations.[26] [Footnotes omitted]

In recent jurisprudence, the formula most often found is that an expropriation will be assumed in the event of a 'substantial deprivation' of an investment.[27]

The oscillating understanding of this approach may be illustrated in light of relevant jurisprudence.

(b) Judicial and arbitral practice: some illustrative cases

Cases decided by tribunals demonstrate the variety of scenarios in which the question of indirect expropriation may arise. Tribunals have had to adapt their focus of inquiry to these different circumstances; consequently, an emphasis on different aspects of the law should not necessarily be construed as an expression of inconsistency. Often, the facts of a case simply highlight only one specific factor and neglect of other possible factors does not result from oversight but from irrelevance to the specific circumstances. A short survey of cases may serve to demonstrate the diversity of factual bases and of the reasoning of tribunals.

The *Oscar Chinn* case[28] concerned the interests of a British shipping company in the Congo. In the aftermath of the economic crisis of 1929, the Belgian Government intervened in the shipping trade on the Congo River by reducing the prices charged by Mr Chinn's only competitor, the partly state-owned company

[24] R Higgins, 'The Taking of Property by the State: Recent Developments in International Law' (1982-III) 176 *Recueil des Cours* 259, 331.
[25] R Dolzer, 'Indirect Expropriation of Alien Property' (1986) 1 *ICSID Review-FILJ* 41.
[26] W M Reisman and R D Sloane, 'Indirect Expropriation and its Valuation in the BIT Generation' (2003) 74 *BYBIL* 115, 121.
[27] See eg *Société Générale v Dominican Republic*, Award, 19 September 2008, para 64; *Alpha Projectholding v Ukraine*, Award, 8 November 2010, para 408.
[28] *Oscar Chinn C se* (*UK v Belgium*), 12 December 1934, PCIJ, Series A/B, No 63, 4.

UNATRA. The government had also granted corresponding subsidies to UNATRA in order to keep the transport system on the Congo River viable. This made Oscan Chinn's business economically unsustainable. The PCIJ concluded that there was no taking. It said:

> The Court . . . is unable to see in his [Mr Chinn's] original position which was characterized by the possession of customers and the possibility of making a profit anything in the nature of a genuine vested right. Favourable business conditions and good-will are transient circumstances, subject to inevitable changes; . . . No enterprise . . . can escape from the chances and hazards resulting from general economic conditions.[29]

The arbitration in *Revere Copper v OPIC*[30] concerned a dispute arising from the insurance by the US Overseas Private Investment Corporation (OPIC)[31] of an investment made by the US claimant in Jamaica. Revere Copper had made substantial investments in the Jamaican bauxite mining sector. An agreement concluded in 1967 between RJA, the investor's local subsidiary, and the Jamaican Government fixed the taxes and royalties to be paid by RJA for a period of 25 years a d provided that no further taxes or financial burdens would be imposed on RJA by the Jamaican authorities. However, in 1972, the newly elected Jamaican Government announced far-reaching reform of the bauxite sector and, in 1974, increased the revenues to be paid by RJA so drastically that RJA ceased operating in 1975.

Revere Copper then sought recovery under its OPIC insurance contract, alleging that the measures adopted by the Jamaican Government amounted to an expropriation of Revere's investment. The General Terms and Conditions of the OPIC contract defined 'expropriatory action', inter alia, as: 'any action which . . . for a period of one year directly results in preventing . . . the Foreign Enterprise from exercising effective control over the use or disposition of substantial portion of its property or from constructing the project or operating the same.' Although there had been no direct interference with Revere's physical property, the majority of the Tribunal found that the repudiation of the guarantees given to Revere amounted to an action that had resulted in preventing the foreign enterprise from exercising effective control over the use or disposition of a substantial portion of its property:

> OPIC argues that RJA still has all the rights and property that it had before the events of 1974: it is in possession of the plant and other facilities; it has its Mining Lease; it can operate as it did before. This may be true in a formal sense but . . . we do not regard RJA's 'control' of the use and operation of its properties as any longer 'effective' in view of the destruction by Government actions of its contract rights.[32]

The Arbitral Tribunal came to this conclusion by emphasizing that 'control in a large industrial enterprise . . . is exercised by a continuous stream of decisions'[33] and

[29] At 27. [30] *Revere Copper v OPIC*, Award, 24 August 1978.
[31] On investment insurance and OPIC, see pp 228 et seq.
[32] *Revere Copper v OPIC*, 291–2.
[33] At 292.

and purpose of a measure, in reference to the role of the intent of a government, consideration of the issue of legitimate expectations of the investor, control over the investment, the need for regulatory measures, and the duration of a measure. These issues are discussed explicitly in some decisions, although they are not necessarily the key to a fully homogeneous theory that does justice to all existing arbitral decisions. But they will assist in a better understanding of individual decisions and general trends.

Not surprisingly, significant lacunae and open issues remain in the law governing indirect expropriation. Domestic courts have grappled with the same issues for far longer. Despite the benefit of constitutional texts and the homogeneity of their national legal systems, they have been unable to resolve all problems. Sometimes these courts have stated that broad formulae will not be helpful as guidelines for judicial reasoning.[79]

(c) Effect or intention?

The effect of the measure upon the economic benefit and value as well as upon the control over the investment is the key question when it comes to deciding whether an indirect expropriation has taken place. Whenever this effect is substantial and lasts for a significant period of time, it will be assumed prima facie that a taking of the property has occurred.[80]

Tribunals have accordingly based their decisions on economic considerations. Indirect expropriation was seen to exist if the measure constituted a deprivation of the economic use and enjoyment, 'as if the rights related thereto—such as the income or benefits... had ceased to exist',[81] or when 'the use or enjoyment of benefits related thereto is exacted or interfered with to a similar extent'.[82] Other formulae and phrases have also been used.[83]

[79] See eg *Andrus v Allard*, 444 US 51, 65; 100 S Ct 318 (1979):

> There is no abstract or fixed point at which judicial intervention under the Takings Clause becomes appropriate. Formulas and factors have been developed in a variety of settings. See *Penn Central*, above, at 123–8.
>
> Resolution of each case, however, ultimately calls as much for the exercise of judgment as for the application of logic.

[80] See eg *Norwegian Shipowners' Claims*, I RIAA 307 (1922); *Goetz v Burundi*, Award, 10 February 1999; *Middle East Cement v Egypt*, Award, 12 April 2002; *Metalclad Corp v Mexico*, Award, 30 August 2000; *CME v Czech Republic*, Partial Award, 13 September 2001.

[81] *TECMED v Mexico*, Award, 29 May 2003, para 115.

[82] At para 116.

[83] See Y Fortier and S L Drymer, 'Indirect Expropriation in the Law of International Investment: I Know It When I See It, or *Caveat Investor*' (2004) 19 *ICSID Revie FILJ* 293, 305:

> the required level of interference with such rights—has been variously described as: (1) *unreasonable*; (2) an interference that renders rights so *useless that they must be deemed to have been expropriated*; (3) an interference that deprives the investor of *fundamental rights of o nership*; (4) an interference that makes rights *practically useless*; (5) an interference *sufficiently restrictive* to warrant a conclusion that the property has been 'taken'; (6) an interference that deprives, in whole or in significant part, the *use or reasonably-to-be-expected economic benefit* of the property; (7) an interference that *radically deprives* the economical use and enjoyment of an investment, as if the rights related thereto had ceased to exist; (8) an interference that makes *any form of exploitation of the property disappear*...; (9) an interference such that the property can no longer be put to *reasonable use*.

In *RFCC v Morocco*,[84] the Tribunal stated that an indirect expropriation exists in cases where the measures have 'substantial effects of an intensity that reduces and/or removes the legitimate benefits related with the use of the rights targeted by the measure to an extent that they render their further possession useless'.[85]

Other decisions have in various wording and degrees also emphasized the effect of the measure.[86] The Tribunal in *CMS v Argentina*[87] found that no indirect expropriation had occurred when Argentina unilaterally suspended a previously agreed tariff adjustment scheme for the gas transport sector in the context of its economic and financial crisis. The US company CMS had argued, inter alia, that the suspension of the tariff adjustment formula amounted to an indirect expropriation of its investment in the Argentine gas transport sector. The Tribunal rejected this argument even though it admitted that the measures had an important effect on the claimant's business:

> The essential question is therefore to establish whether the enjoyment of the property has been effectively neutralized. The standard that a number of tribunals have applied in recent cases where indirect expropriation has been contended is that of substantial deprivation.... the investor is in control of the investment; the Government does not manage the day-to-day operations of the company; and the investor has full ownership and control of the investment.[88]

In *Telenor v Hungary*,[89] the investor held a telecom concession which was affected by a special levy on all telecommunications service providers. The Tribunal held that in order to constitute an expropriation, the conduct complained of must have a major adverse impact on the economic value of the investment.[90] The Tribunal said:

> the interference with the investor's rights must be such as substantially to deprive the investor of the economic value, use or enjoyment of its investment.[91]... In considering whether measures taken by government constitute expropriation the determinative factors are the intensity and duration of the economic deprivation suffered by the investor as the result of them.[92]

[84] *RFCC v Morocco*, Award, 22 December 2003.

[85] At para 69 (original in French: 'avoir des effets substantiels d'une intensité certaine qui réduisent et/ou font disparaître les bénéfices légitimement attendus de l'exploitation des droits objets de ladite mesure à un point tel qu'ils rendent la détention de ces droits inutile'). See also *LESI v Algeria*, Award, 12 November 2008, para 132; *Bayindir v Pakistan*, Award, 27 August 2009, para 459.

[86] *Tippetts, Abbett, McCarthy, Stratton v TAMS-AFFA Consulting Eng'rs of Iran*; *Biloune v Ghana*, Award on Jurisdiction, 27 October 1989; *Metalclad Corp v Mexico*, Award, 30 August 2000; *Wena v Egypt*, Award on Merits, 8 December 2000; *Santa Elena v Costa Rica*, Award, 17 February 2000; *CME v Czech Republic*, Partial Award, 13 September 2001; *Middle East Cement v Egypt*, Award, 12 April 2002; *Goetz v Burundi*, Award, 10 February 1999.

[87] *CMS v Argentina*, Award, 12 May 2005.

[88] At paras 262, 263. See also *Revere Copper v OPIC*, 56 ILR (1980) 258 and the cases discussed by G H Aldrich, 'What Constitutes a Compensable Taking of Property? The Decisions of the Iran–United States Claims Tribunal' (1994) 88 *AJIL* 585.

[89] *Telenor v Hungary*, Award, 13 September 2006.

[90] At para 64. [91] At para 65.

[92] At para 70. Footnote omitted.

assured, thereby safeguarding the very object and purpose of the protection sought by the treaty.

The Tribunal in *Tokios Tokelės v Ukraine*[127] explained that:

> one can reasonably infer that a diminution of 5% of the investment's value will not be enough for a finding of expropriation, while a diminution of 95% would likely be sufficient.

Azurix v Argentina[128] concerned breaches of a water concession by a province of Argentina. The Tribunal, although finding other breaches of the BIT, including fair and equitable treatment, denied the existence of an indirect expropriation, since the investor had retained control over the enterprise:

> the impact on the investment attributable to the Province's actions was not to the extent required to find that, in the aggregate, these actions amounted to an expropriation; Azurix did not lose the attributes of ownership, at all times continued to control ABA and its ownership of 90% of the shares was unaffected. No doubt the management of ABA was affected by the Province's actions, but not sufficiently for the Tribunal to find that Azurix's investment was expropriated.[129]

Similarly, in *LG&E v Argentina*[130] the host state had violated the terms of concessions for the distribution of gas. The Tribunal, although finding that other standards had been violated, denied the existence of an expropriation in view of the investor's continuing control:

> Ownership or enjoyment c n be said to be 'neutralized' where a party no longer is in control of the investment, or where it cannot direct the d y to-day operations of the investment. ... Interference with the investment's ability to carry on its business is not satisfied where the investment continues to operate, even if profits are diminished.[131]

Control is obviously an important aspect in the analysis of a taking. However, the continued exercise of control by the investor in itself is not necessarily the sole criterion. The issue becomes obvious when a host state substantially deprives the investor of the value of the investment leaving the investor with control of an entity that amounts to not much more than a shell of the former investment.

This illustrates the significance of a test which includes criteria other than control, such as economic use and benefit. Any attempt to define an indirect expropriation on the basis of one factor alone will not lead to a satisfactory result in all cases. In particular, an approach that looks exclusively at control over the overall investment is unable to contemplate the expropriation of specific rights enjoyed by the investor.

[127] *Tokios Tokelės v Ukraine*, Award, 26 July 2007, para 120.
[128] *Azurix v Argentina*, Award, 14 July 2006.
[129] At para 322.
[130] *LG&E v Argentina*, Decision on Liability, 3 October 2006.
[131] At paras 188, 191. Footnotes omitted.

(f) Partial expropriation

Some tribunals have accepted the possibility of an expropriation of particular rights that formed part of an overall business operation without looking at the issue of control over the entire investment.[132] In *Middle East Cement v Egypt*,[133] the investor had, inter alia, obtained an import licence for cement and had operated a ship. Egypt subsequently took measures that prevented the investor from operating its licence and seized and auctioned the ship. The investor raised a series of claims in respect of which it alleged expropriation. These included but went beyond the import licence and ownership of the ship. The Tribunal looked at these claims separately and determined in respect of each whether an expropriation had taken place. It found that the licence qualified as an investment and that the measures that prevented the exercise of the rights under it amounted to an expropriation.[134] The Tribunal examined separately whether an expropriation of the ship had occurred and gave an affirmative answer.[135] Several other claims of expropriation in respect of other rights were also examined but denied for a variety of reasons.[136] Therefore, *Middle East Cement* demonstrates that it is possible separately to expropriate specific rights enjoyed by the investor regardless of control over the overall investment.

In *Eureko v Poland*,[137] the investor had acquired a minority share in a privatized insurance company. A related agreement granted the investor the right to acquire further shares thereby gaining majority control of the company. The right to acquire the additional shares was subsequently withdrawn by the state. The original investment remained unaffected. The Tribunal found that the right to acquire further shares constituted 'assets', which were separately capable of expropriation.[138] It follows from this decision that even where control over the basic investment remains unaffected, the taking of specific rights related to the basic investment may amount to an expropriation.[139]

In *Grand River v United States*[140] the Tribunal suggested that under the rules of the NAFTA, only an expropriation of the investment as a whole will fall under the rules of the Treaty. This view of the NAFTA (and the law of expropriation in general) is too narrow; indeed, it appears from the case law discussed in the decision[141] that the Tribunal may have failed to distinguish between the questions of the definition of a taking and the extent to which an investment may have been expropriated.

[132] *Waste Management v Mexico*, Award, 30 April 2004, paras 141, 147; *EnCana v Ecuador*, Award, 3 February 2006, paras 172 83. For an extensive discussion, see U Kriebaum, 'Partial Expropriation' (2007) 8 *J World Investment & Trade* 69.
[133] *Middle East Cement v Egypt*, Award, 12 April 2002.
[134] At paras 101, 105, 107, 127.
[135] At paras 138, 144.
[136] At paras 152–6, 163–5.
[137] *Eureko v Poland*, Partial Award, 19 August 2005.
[138] At paras 239 41.
[139] See U Kriebaum, 'Partial Expropriation' (2007) 8 *J World Investment & Trade* 69.
[140] *Grand River v United States*, Award, 12 January 2011, para 146.
[141] At paras 148 et seq.

(h) Duration of a measure

The duration of a governmental measure affecting the interests of a foreign investor is important for the assessment of whether an expropriation has occurred.[173] The Iran–US Claims Tribunal has ruled that the appointment of a temporary m nager by the host state against the will of the foreign investor will constitute a taking if the consequential deprivation is not 'merely ephemeral'.[174]

Investment tribunals have also laid emphasis on the duration of the measure in question.[175] In *SD Myers v Canada*,[176] the Tribunal said:

> An exptopriation usually amount to a lasting removal of the ability of an owner to make use of its economic rights although it may be that, in some contexts and circumstances, it would be appropriate to view a deprivation as amounting to an expropriation, even if it were partial or temporary.[177]

In the event, the Tribunal found that the measure had lasted for 18 months only and that this limited effect did not amount to an expropriation.[178]

In *Wena Hotels v Egypt*,[179] the Tribunal found that the seizure of the investor's hotel lasting for nearly a year was not 'ephemer l' but amounted to an expropri-ation.[180] In its subsequent Decision on Interpretation[181] the *Wena* Tribun l said:

> It is true that the Original Tribunal did not explicitly state that such expropriation totally and permanently deprived Wena of its fundamental rights of ownership. However, in assessing the weight of the actions described above, there was no doubt in the Tribunal's mind that the deprivation of Wena's fundamental rights of ownership was so profound that the expropriation was indeed a total and permanent one.[182]

LG&E v Argentina also ruled that the duration of the measure had to be taken into account.[183] The Tribunal found that, as a rule, only an interference that is permanent will lead to an expropriation:

> Similarly, one must consider the duration of the measure as it relates to the degree of interference with the investor's ownership rights. Generally, the expropriation must be permanent, that is to say, it cannot have a temporary nature, unless the investment's successful development depends on the realization of certain activities at specific moments that may not endure variations.[184]

The Tribunal concluded:

> Thus, the effect of the Argentine State's actions has not been permanent on the value of the Claimants' shares, and Claimants' investment has not ceased to exist. Without a permanent, severe deprivation of LG&E's rights with regard to its investment, or almost complete deprivation of the value of LG&E's investment, the Tribunal concludes that these circum stances do not constitute expropriation.[185]

(i) Creeping expropriation

The rules on protection of foreign investments must not be circumvented by way of splitting a measure amounting to an indirect expropriation into a series of cumulative steps which, taken together, have the same effect on the foreign owner. Therefore, it has long been accepted that an expropriation may occur 'outright or in stages'.[186] Thus, the term 'creeping expropriation' describes a taking through a series of acts.[187] A study by UNCTAD referred in this context to 'a slow and incremental encroachment on one or more of the ownership rights of a foreign investor that diminishes the value of its investment'.[188]

Practice has recognized the phenomenon of creeping expropriation on a number of occasions.[189] The Tribunal in *Generation Ukraine v Ukraine*[190] explained creeping expropriation as follows:

> Creeping expropriation is a form of indirect expropriation with a distinctive temporal quality in the sense that it encapsulates the situation whereby a series of acts attributable to the State *over a period of time* culminate in the expropriatory taking of such property.... A plea of creeping expropriation must proceed on the basis that the investment existed at a particular point in time and that subsequent acts attributable to the State have eroded the investor's rights to its investment to an extent that is violative of the relevant international standard of protection against expropriation.[191]

[173] See G C Christie, 'What Constitutes a Taking of Property under International Law?' (1962) *BYBIL* 307; J Wagner, 'International Investment, Expropriation and Environmental Protection' (1999) 29 *Golden Gate University L Rev* 465; W M Reisman and R D Sloane, 'Indirect Expropriation and its Valuation in the BIT Generation' (2003) 74 *BYBIL* 115.

[174] See *Tippetts, Abbett, McCarthy, Stratton v TAMS AFFA Consulting Eng'rs of Iran*, 6 Iran–US CTR 219, 225 (1984); *Phelps Dodge Corp v Iran*, 10 Iran US CTR 121 (1986); *James M Saghi, Michael R Saghi, and Allan J Saghi v Iran*, 14 Itan US CTR 3 (1988).

[175] *TECMED v Mexico*, Award, 29 May 2003, para 116; *Generation Ukraine v Ukraine*, Award, 16 September 2003, para 20.32; *Azurix v Argentina*, Award, 14 July 2006, para 313: 'How much time is needed must be judged by the specific circumstances of each case.'

[176] *S D Myers v Canada*, First Partial Award, 13 November 2000.

[177] At para 283.

[178] At para 287.

[179] *Wena Hotels v Egypt*, Award, 8 December 2000.

[180] At para 99.

[181] *Wena Hotels v Egypt*, Decision on Interpretation, 31 October 2005.

[182] At para 120.

[183] *LG&E v Argentina*, Decision on Liability, 3 October 2006.

[184] At para 193.

[185] At para 200.

[186] See American Law Institute, *Restatement (Third) of the Foreign Relations Law of the United States*, Vol 1 (1987), § 712; G C Christie, 'What Constitutes a Taking of Property under International Law?' (1962) 38 *BYBIL* 307.

[187] The term 'creeping expropriation' has also occasionally been used interchangeably with the term 'indirect expropriation'.

[188] UNCTAD, *Series on Issues in International Investment Agreements: 'Taking of Property'* (2000) 11–12.

[189] See also *Biloune v Ghana*, 95 ILR (1994) 184, 209; *TECMED v Mexico*, Award, 29 May 2003, para 144; cf also Art 15 of the ILC Articles on State Responsibility in J Crawford, *The International Law Commission's Articles on State Responsibility* (2002) 141; *Santa Elena v Costa Rica*, Award, 17 February 2000, para 76; *Azurix v Argentina*, Award, 14 July 2006, para 313.

[190] *Generation Ukraine v Ukraine*, Award, 16 September 2003; also *Rumeli v Kazakhstan*, Award, 29 July 2008.

[191] At paras 20.22, 20.26.

The decision in *Tradex v Albania*[192] emphasized the cumulative effect of the measures in question:

> While the... Award has come to the conclusion that none of the single decisions and events alleged by Tradex to constitute an expropriation can indeed be qualified by the Tribunal as expropriation, it might still be possible that, and the Tribunal, therefore, has to examine and evaluate hereafter whether the combination of the decisions and events can be qualified as expropriation of Tradex' foreign investment in a long, step-by-step process by Albania.[193]

In *Siemens v Argentina*,[194] the host state had taken a series of adverse measures, including postponements and suspensions of the investor's profitable activities, fruitless renegotiations, and ultimately cancellation of the project. The Tribunal found that this had amounted to an expropriation and described creeping expropriation in the following terms:

> By definition, creeping expropriation refers to a process, to steps that eventually have the effect of an expropriation. If the process stops before it reaches that point, then expropriation would not occur. This does not necessarily mean that no adverse effects would have occurred. Obviously, each step must have an adverse effect but by itself may not be significant or considered an illegal act. The last step in a creeping expropriation that tilts the balance is similar to the straw that breaks the camel's back. The preceding straws may not have had a perceptible effect but are part of the process that led to the break.[195]

Professor Reisman and R D Sloane have rightly pointed out that the issue must sometimes be seen in retrospect:

> Discrete acts, analyzed in isolation rather than in the context of the overall flow of events, may, whether legal or not in themselves, seem innocuous vis-à-vis a potential expropriation. Some may not be expropriatory in themselves. Only, in retrospect will it become evident that those acts comprised part of an accretion of deleterious acts and omissions, which in the aggregate expropriated the foreign investor's property rights.... Because of their gradual and cumulative nature, creeping expropriations also render it problematic, perhaps even arbitrary, to identify a single interference (or failure to act where a duty requires it) as the 'moment of expropriation'.[196]

5. Expropriation of contractual rights

'The taking away or destruction of rights acquired, transmitted, and defined by a contract is as much a wrong, entitling the sufferer to redress, as the taking away or destruction of tangible property.' This principle, stated in 1903 by a member of the

[192] *Tradex v Albania*, Award, 29 April 1999.
[193] At para 191.
[194] *Siemens v Argentina*, Award, 6 February 2007.
[195] At para 263.
[196] W M Reisman and R D Sloane, 'Indirect Expropriation and its Valuation in the BIT Generation' (2003) 74 *BYBIL* 115, 123–5.

US–Venezuela Mixed Claims Commission in the *Rudloff* case,[197] was followed in 1922 by the Permanent Court of Arbitration in the *Norwegian Shipowners* case[198] and also by the PCIJ in 1926 in the *Chorzów Factory* case.[199] Cases decided in investment arbitrations[200] and by the Iran–US Claims Tribunal[201] have confirmed this position.

In *Amoco International Finance Corp v Iran* the Iran–US Claims Tribunal held that expropriation may extend to any right that can be the object of a commercial transaction.[202] The Arbitral Tribunal in *Tokios Tokelės v Ukraine* stated that all business operations associated with the physical property of the investors are covered by the term 'investment', including contractual rights.[203]

In the modern investment context, many investment decisions are accompanied and protected by specific investment agreements with the host state, often covering matters such as taxation, customs regulations, the right and duty to sell at a certain price to the host state, or pricing issues. These agreements form the legal and financial foundations of the investment, and the business decisions based upon them may collapse in their absence. Thus, it is understandable that practically all investment treaties state that contracts are covered by the term 'investment'.[204] In turn, provisions dealing with expropriation in these treaties refer to 'investments'. It follows that contracts are protected against expropriation. The Tribunal in *Siemens v Argentina*,[205] applying the BIT between Argentina and Germany, said:

[197] American–Venezuelan Mixed Claims Commission, *Rudloff Case*, Decision on Merits, IX RIAA 244, 250 (1959).
[198] Permanent Court of Arbitration, *Norwegian Shipowners' Claim* (*Norway v United States*), 13 October 1922, I RIAA 307 (1948). The arbitrators held that by requisitioning ships that were to be built for Norwegian citizens, the US Government also expropriated the underlying construction contracts.
[199] *Case Concerning Certain German Interests in Polish Upper Silesia*, 1926, PCIJ, Series A, No 7, 3.
[200] See *SPP v Egypt*, Award, 20 May 1992, paras 164–7; *Wena Hotels v Egypt*, Award, 8 December 2000, para 98; *CME v Czech Republic*, Partial Award, 13 September 2001, para 591; *Impregilo v Pakistan*, Decision on Jurisdiction, 22 April 2005, para 274; *Eureko v Poland*, Partial Award, 19 August 2005, para 241; *Bayindir v Pakistan*, Decision on Jurisdiction, 14 November 2005, para 255; *Azurix v Argentina*, Award, 14 July 2006, para 314; *Inmaris v Ukraine*, Decision on Jurisdiction, 8 March 2010, para 66: contracts may lead to 'a claim of money' even if the agreement is fictious.
[201] Article IV-2 of the Treaty of Amity between Iran and the USA (1955) protects not only 'property' but also 'interests in property'. According to the tribunal in *Phillips Petroleum Company v Iran*, the term 'interest in property' was 'included at the insistence of the United States for the stated purpose of ensuring that contract rights in the petroleum industry would be protected by the treaty in the same way as would the older type of property represented by a petroleum concession' (see *Phillips Petroleum Company v Iran*, Award, 29 June 1989, para 105).
[202] *Amoco International Finance Corp v Iran*, Award, 14 July 1987, para 108.
[203] *Tokios Tokelės v Ukraine*, Decision on Jurisdiction, 29 April 2004, paras 92–3.
[204] See eg Energy Charter Treaty, Art 1(6)(f): 'any right conferred by law or contract'. See also NAFTA, Art 1139. See R Dolzer and M Stevens, *Bilateral Investment Treaties* (1994); G Sacerdoti, 'Bilateral Treaties and Multilateral Instruments on Investment Protection' (1997) 269 *Collected Courses of the Hague Academy of International Law* 251, 381; R Higgins, 'The Taking of Property by the State: Recent Developments in International Law' (1982-III) 176 *Collected Courses of the Hague Academy of International Law* 263, 271; UNCTAD, *Series on Issues in International Investment Agreements: 'Taking of Property'* (2000) 36.
[205] *Siemens v Argentina*, Award, 6 February 2007.

The Contract falls under the definition of 'investments' under the Treaty and Article 4(2) refers to expropriation or nationalization of investments. Therefore, the State parties recognized that an investment in terms of the Treaty may be expropriated. There is nothing unusual in this regard. There is a long judicial practice that recognizes that expropriation is not limited to tangible property.[206]

Not every failure by a government to perform a contract amounts to an expropriation even if the violation leads to a loss of rights under the contract. A simple breach of contract at the hands of the state is not an expropriation.[207] Tribunals have found that the determining factor is whether the state acted in an official, governmental capacity.[208]

In the *Jalapa Railroad* case before the American Mexican Claims Commission (1948),[209] the decisive issue was whether the nullification of a contractual clause by the Mexican Government was 'effected arbitrarily by means of a governmental power illegal under international law'. In *Consortium RFCC v Morocco*, the Tribunal differentiated between the mere exercise of a right and an action by the host state 'in a public capacity' and placed emphasis on whether a law or a governmental decree had been passed or a judgment executed.[210]

Other tribunals have held similarly that mere breaches of contract or defects in its performance would not amount to an expropriation. What was needed was an act of public authority.[211] In *Siemens v Argentina*,[212] the Tribunal, in the course of its discussion of expropriation, found that a state party to a contract would breach the applicable treaty only if its behaviour went beyond that which an ordinary contracting party could adopt.[213] The Tribunal said:

for the State to incur international responsibility it must act as such, it must use its public authority. The actions of the State have to be based on its 'superior governmental power'. It is not a matter of being disappointed in the performance of the State in the execution of a contract but rather of interference in the contract execution through governmental action.[214]

[206] At para 267. The Tribunal relied on the *Norwegian Shipowners* and *Chorzów Factory* cases.
[207] For detailed discussion, see S M Schwebel, 'On Whether the Breach by a State of a Contract with an Alien is a Breach of International Law' in *International Law at the Time of its Codification, Essays in Honour of Roberto Ago, III* (1987) 401.
[208] See also the American Law Institute, *Restatement (Third) of the Foreign Relations Law of the United States*, Vol 2 (1986), p 201: 'a state is responsible for such a repudiation or breach only . . . if it is akin to an expropriation in that the contract is repudiated or breached for governmental rather than commercial reasons.'
[209] American Mexican Claims Commission, *Jalapa Railroad and Power Co*, 8 Whiteman Digest of International Law (1976) 908–9.
[210] *RFCC v Morocco*, Award, 22 December 2003, paras 60–2, 65–9, 85–9.
[211] *Impregilo v Pakistan*, Decision on Jurisdiction, 22 April 2005, para 281; *Bayindir v Pakistan*, Decision on Jurisdiction, 14 November 2005, para 257; *Azurix v Argentina*, Award, 14 July 2006, para 315.
[212] *Siemens v Argentina*, Award, 6 February 2007.
[213] At para 248.
[214] At para 253.

In particular, tribunals have held that failure to pay a debt under a contract does not amount to an expropriation.[215] *Waste Management v Mexico*[216] concerned a concession for waste disposal. The Tribunal found that the mere non-payment by the city of Acapulco of amounts due under the concession agreement did not amount to an expropriation.[217] It found that the state's failure to pay bills, did not amount to an 'outright repudiation of the transaction' and did not purport to terminate the contact. Only a decree or executive act or an exercise of legislative public authority could amount to an expropriation:

> The mere non-performance of a contractual obligation is not to be equated with a taking of property, nor (unless accompanied by other elements) is it tantamount to expropriation. Any private party can fail to perform its contracts, whereas nationalization and expropriation are inherently governmental acts.[218] . . .
>
> The Tribunal concludes that it is one thing to expropriate a right under a contract and another to fail to comply with the contract. Non-compliance by a government with contractual obligations is nor the same thing as, or equivalent or tantamount to, an expropriation.[219]

While these considerations are clearly helpful, they do not exhaust the subject. Indeed, the *Waste Management* tribunal itself recognized, without elaboration, that 'one could envisage conduct tantamount to an expropriation which consisted of acts and omissions not specifically or exclusively governmental'.[220] An analysis that is consistent with the approach generally valid for all acts of expropriation would not focus exclusively on the existence of formal governmental acts or the purported intentions of the government but would also contemplate other relevant factors.[221]

[215] *SGS v Philippines*, Decision on Jurisdiction, 29 January 2004, para 161.
[216] *Waste Management v Mexico*, Award, 30 April 2004.
[217] At paras 159–74.
[218] At para 174.
[219] At para 175. Also *Bureau Veritas v Paraguay*, Award, 29 May 2009.
[220] At para 175.
[221] See *Alpha v Ukraine*, Award, 8 November 2010, para 412; see further p 230.

from the terms of the applicable investment treaty and not from any set of expectations investors may have or claim to have.[95]

In *Saluka v Czech Republic*[96] an ailing bank in which the claimants had invested was taken over by a competitor that had received financial assistance from the state for the purpose of the takeover. By contrast, the bank had not received similar aid when the claimants attempted to negotiate the conditions to maintain the viability of the bank. The Tribunal found that there was a violation of FET and described the requirements of the FET standard in terms of consistency, transparency, and reasonableness:

> A foreign investor whose interests are protected under the Treaty is entitled to expect that the [host state] will not act in a way that is manifestly inconsistent, non-transparent, unreasonable (*i.e.* unrelated to some rational policy), or discriminatory (*i.e.* based on unjustifiable distinctions).[97]

The NAFTA case, *Waste Management v Mexico*,[98] arose from a failed concession for the disposal of waste that involved a number of grievances, including the municipality's failure to pay its bills, failure to honour exclusivity of services, difficulties with a line of credit agreement, and proceedings before the Mexican courts. The Tribunal summarized its position on the FET standard in Article 1105 of the NAFTA in the following terms:

> the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.[99]

Discrimination against foreigners has been regarded as an important indicator of failure to grant fair and equitable treatment.[100] Awards have also included the standard of 'improper and discreditable'[101] or 'unreasonable conduct',[102] or have referred to international or comparative standards.[103]

[95] At para 67.
[96] *Saluka v Czech Republic*, Partial Award, 17 March 2006.
[97] At para 309.
[98] *Waste Management v Mexico*, Final Award, 30 April 2004.
[99] At para 98. On the facts of the particular case, the Tribunal found that this standard had not been violated. At para 140.
[100] *Loewen v United States*, Award, 26 June 2003, para 135; *Waste Management v Mexico*, Final Award, 30 April 2004, para 98; *MTD v Chile*, Award, 25 May 2004, para 109. But see *Grand River v United States*, Award, 12 January 2011, para 209.
[101] *Mondev v United States*, Award, 11 October 2002, para 127; *Loewen v United States*, Award, 26 June 2003, para 133 (in reference to *Mondev*).
[102] *Saluka v Czech Republic*, Partial Award, 17 March 2006, para 309.
[103] *SD Myers v Canada*, First Partial Award, 13 November 2000, para 264.

(h) Specific applications of the fair and equitable treatment standard

Broad definitions or descriptions are not the only way to gauge the meaning of an elusive concept such as FET. Another method is to identify typical factual situations to which this principle has been applied.[104] An examination of the practice of tribunals demonstrates that several principles can be identified which are embraced by the standard of fair and equitable treatment. The cases discussed below clearly speak to the central role of stability, transparency, and the investor's legitimate expectations for the current understanding of the FET standard. Other contexts in which the standard has been applied concern compliance with contractual obligations, procedural propriety and due process, acting in good faith, and freedom from coercion and harassment.[105]

aa. Stability and the protection of the investor's legitimate expectations

The investor's legitimate expectations are based on the host state's legal framework and on any undertakings and representations made explicitly or implicitly by the host state.[106] The legal framework on which the investor is entitled to rely consists of legislation and treaties, assurances contained in decrees, licences, and similar executive statements, as well as contractual undertakings. Specific representations play a central role in the creation of legitimate expectations. Undertakings and representations made explicitly or implicitly by the host state are the strongest basis for legitimate expectations. A reversal of assurances by the host state that have led to legitimate expectations will violate the principle of fair and equitable treatment.[107]

Tribunals have emphasized that the legitimate expectations of the investor will be grounded in the legal order of the host state as it stands at the time the investor acquires the investment.[108] *GAMI v Mexico* ruled categorically: 'NAFTA arbitrations have no mandate to evaluate laws and regulations that predate the decision of

[104] See also K Yannaca-Small, 'Fair and Equitable Treatment Standard' in K Yannaca-Small (ed), *Arbitration under International Investment Agreements* (2010) 393–407; S W Schill, 'Fair and Equitable Treatment, the Rule of Law, and Comparative Public Law' in S W Schill (ed), *International Investment Law and Comparative Public Law* (2010) 159–70.
[105] For decisions adopting similar categories for the analysis of the FET standard, see: *Biwater Gauff v Tanzania*, Award, 24 July 2008, para 602; *Rumeli v Kazakhstan*, Award, 29 July 2008, para 609; *Siag v Egypt*, Award, 1 June 2009, para 450; *Bayindir v Pakistan*, Award, 27 August 2009, para 178; *Lemire v Ukraine*, Decision on Jurisdiction and Liability, 14 January 2010, para 284; *Paushok v Mongolia*, Award, 28 April 2011, para 253.
[106] For early discussions of the relevance of the concept of legitimate expectations in foreign investment law, see R Dolzer, 'New Foundations of the Law of Expropriation of Alien Property' (1981) 75 *AJIL* 553; G Burdeau, 'Droit international et contrats d' Etat' (1982) *Annuaire francaise de droit international* 454, 470.
[107] See also W M Reisman and M H Arsanjani, 'The Question of Unilateral Governmental Statements as Applicable Law in Investment Disputes' (2004) 19 *ICSID Review-FILJ* 328; S Vasciannie, 'The Fair and Equitable Treatment Standard in International Investment Law and Practice' (1999) 70 *BYBIL* 99, 146–7; T W Wälde, 'Energy Charter Treaty-based Investment Arbitration' (2004) 5 *J World Investment* 387.
[108] C Schreuer and U Kriebaum, 'At What Time Must Legitimate Expectations Exist?' in J Werner and A H Ali (eds), *A Liber Amicorum: Thomas Wälde. Law Beyond Conventional Thought* (2009) 265.

state had consciously and overtly breached Eureko's basic expectations.[123] Therefore, the Tribunal had no hesitation in concluding that the FET standard of the Netherlands-Poland BIT had been violated by the respondent.[124]

Other tribunals have similarly found that the FET principle involved the government's obligation not to frustrate the investor's legitimate expectations by arbitrarily changing the legal framework under which the investment had been made.[125] According to one view, the investor's legitimate expectations will be seriously reduced if there is general instability in the political conditions of the country concerned.[126]

Legitimate expectations are not subjective hopes and perceptions; rather, they must be based on objectively verifiable facts. Expectations are protected only if they are legitimate and reasonable in the circumstances. The Tribunal in *Suez v Argentina*[127] said:

> one must not look single-mindedly at the Claimants' subjective expectations. The Tribunal must rather examine them from an objective and reasonable point of view.[128]

More recently, tribunals have increasingly emphasized that the requirement of stability is not absolute and does not affect the state's right to exercise its sovereign power to legislate and to adapt its legal system to changing circumstances.[129] What matters is whether measures exceed normal regulatory powers and fundamentally modify the regulatory framework for the investment beyond an acceptable margin of change.[130] In other words, 'changes to general legislation, in the absence of specific stabilization promises to the foreign investor, reflect a legitimate exercise of the host state's governmental powers that are not prevented by a BIT's fair and equitable treatment standard'.[131] The Tribunal in *EDF v Romania*[132] stated in this respect:

[123] At paras 231, 232.

[124] At para 234.

[125] *CME v Czech Republic*, Partial Award, 13 September 2001, para 611; *Bayindir v Pakistan*, Decision on Jurisdiction, 14 November 2005, paras 231–2; *LG&E v Argentina*, Decision on Liability, 3 October 2006, para 131; *PSEG v Turkey*, Award, 19 January 2007, paras 240–56; *Enron v Argentina*, Award, 22 May 2007, paras 260–2; *Sempra v Argentina*, Award, 28 September 2007, paras 300, 303; *National Grid v Argentina*, Award, 3 November 2008, paras 178–9; *Alpha v Ukraine*, Award, 8 November 2010, para 420; *Lemire v Ukraine*, Decision on Jurisdiction and Liability, 14 January 2010, para 267; Award, 28 March 2011, paras 68–73.

[126] *Bayindir v Pakistan*, Award, 27 August 2009, paras 192–7. See also U Kriebaum, 'The Relevance of Economic and Political Conditions for the Protection under Investment Treaties' (2011) 10 *Law and Practice of International Courts and Tribunals* 383.

[127] *Suez v Argentina*, Decision on Liability, 30 July 2010.

[128] At para 209.

[129] *Parkerings v Lithuania*, Award, 11 September 2007, paras 327–38; *BG Group v Argentina*, Final Award, 24 December 2007, paras 292–310; *Plama v Bulgaria*, Award, 27 August 2008, para 219; *Continental Casualty v Argentina*, Award, 5 September 2008, paras 258–61; *AES v Hungary*, Award, 23 September 2010, paras 9.3.27–9.3.35; *Paushok v Mongolia*, Award, 28 April 2011, para 302; *Impregilo v Argentina*, Award, 21 June 2011, paras 290–1; *El Paso v Argentina*, Award, 31 October 2011, paras 344–52, 365–74.

[130] *El Paso v Argentina*, Award, 31 October 2011, para 402.

[131] *Total v Argentina*, Decision on Liability, 27 December 2010, para 164. See also paras 113–24, 309, 312, 429.

[132] *EDF v Romania*, Award, 8 October 2009.

> The idea that legitimate expectations, and therefore FET, imply the stability of the legal and business framework, may not be correct if stated in an overly-broad and unqualified formulation. The FET might then mean the virtual freezing of the legal regulation of economic activities, in contrast with the State's normal regulatory power and the evolutionary character of economic life. Except where specific promises or representations are made by the State to the investor, the latter may not rely on a bilateral investment treaty as a kind of insurance policy against the risk of any changes in the host State's legal and economic framework. Such expectation would be neither legitimate nor reasonable.[133]

In deciding between the investor's right to stability and the state's right to regulate, some tribunals have weighed the investor's legitimate expectations against the state's duty to act in the public interest.[134]

Particularly important in the creation of legitimate expectations are specific assurances and representations made by the host state in order to induce investors to make investments.[135] But even here some tribunals have found that mere political statements were not capable of creating reasonable expectations.[136]

bb. Transparency

Transparency is closely related to protection of the investor's legitimate expectations. Transparency means that the legal framework for the investor's operations is readily apparent and that any decisions affecting the investor can be traced to that legal framework.[137]

There is authority to the effect that transparency and the investor's legitimate expectations are protected even without a treaty guarantee of FET. In *SPP v Egypt*[138] the respondent contended that certain acts of Egyptian officials, upon which the claimants relied, were null and void because they were in conflict with the inalienable nature of the public domain and because they were not taken pursuant to the procedures prescribed by Egyptian law. The Tribunal rejected this argument and emphasized that the investor was entitled to rely on the official representations of the government:

[133] At para 217.

[134] *Saluka v Czech Republic*, Partial Award, 17 March 2006, para 306; *Total v Argentina*, Decision on Liability, 27 December 2010, paras 123, 309. For an instance where a tribunal found misuse of regulatory powers, see *Vivendi v Argentina*, Award, 20 August 2007, para 7.4.24.

[135] *Kardassopoulos v Georgia*, Decision on Jurisdiction, 6 July 2007, para 191; *Parkerings v Lithuania*, Award, 11 September 2007, para 331; *Sempra v Argentina*, Award, 28 September 2007, paras 298, 299; *OKO Pankki v Estonia*, Award, 19 November 2007, paras 247–8, 263; *Duke Energy v Ecuador*, Award, 18 August 2008, paras 359–64; *Continental Casualty v Argentina*, Award, 5 September 2008, paras 258–61; *Total v Argentina*, Decision on Liability, 27 December 2010, paras 119–20, 309.

[136] *Continental Casualty v Argentina*, Award, 5 September 2008, para 261(i); *El Paso v Argentina*, Award, 31 October 2011, paras 375–9, 392–5.

[137] UNCTAD Series on issues in international investment agreements, 'Fair and Equitable Treatment' (1999) 51; S W Schill, 'Fair and Equitable Treatment, the Rule of Law, and Comparative Public Law' in S W Schill (ed), *International Investment Law and Comparative Public Law* (2010) 168–9.

[138] *SPP v Egypt*, Award, 20 May 1992.

the FET standard.[187] They cited special circumstances relating to the complexity of the issues[188] or to the political situation in the country concerned.[189]

Denial of justice is traditionally associated with the administration of justice by domestic courts[190] but investment tribunals have accepted that the procedural guarantees inherent in the FET standard extend to the activities of the host state's administrative authorities.[191] On the other hand, the requirement to afford fair procedure on the basis of the FET standard does not extend to a state entity's management of its contractual relationship with the investor.[192]

In *Thunderbird v Mexico*[193] the Tribunal held that the standards of due process and procedural fairness applicable in administrative proceedings are lower than in a judicial process. In the particular case it found no violation of the FET standard, explaining that the claimant had been given full opportunity to be heard and to present evidence and that the proceedings were subject to judicial review by the courts.[194]

ee. Good faith

As explained above, good faith is a broad principle that is one of the foundations of international law in general and of foreign investment law in particular.[195] Arbitral tribunals have confirmed that good faith is inherent in FET.[196] It is 'the common guiding beacon' to the obligation under BITs; it is 'at the heart of the concept of FET', and 'permeates the whole approach' to investor protection.[197] The Tribunal in *Tecmed*,[198] interpreting a BIT provision on FET, said:

> The Arbitral Tribunal finds that the commitment of fair and equitable treatment... is an expression and part of the *bona fide* principle recognized in international law...[199]

The FET standard in general, and the obligation to act in good faith in particular, include the obligation not to inflict damage upon an investment purposefully.[200] The Tribunal in *Waste Management*[201] found that the obligation to act in good faith was a basic obligation under the FET standard as contained in Article 1105 of

[187] *Frontier Petroleum v Czech Republic*, Final Award, 12 November 2010, paras 289–96, 334.
[188] *Jan de Nul v Egypt*, Award, 6 November 2008, paras 202–4.
[189] *Toto v Lebanon*, Decision on Jurisdiction, 11 September 2009, para 165.
[190] *Grand River Enterprises v United States*, Award, 12 January 2011, paras 222–36.
[191] *Rumeli v Kazakhstan*, 29 July 2008, para 623; *Chemtura v Canada*, Award, 2 August 2010, paras 211–24; *AES v Hungary*, Award, 23 September 2010, paras 9.3.36–9.3.73.
[192] *Bayindir v Pakistan*, Award, 27 August 2009, paras 343–8.
[193] *Thunderbird v Mexico*, Award, 26 January 2006.
[194] At paras 197–201.
[195] See pp 18, 132, 142 et seq.
[196] *Genin v Estonia*, Award, 25 June 2001, para 367: 'Acts that would violate this minimum standard [of fair and equitable treatment] would include... subjective bad faith.'
[197] *Sempra v Argentina*, Award, 28 September 2007, paras 297–99.
[198] *Tecmed v Mexico*, Award, 29 May 2003.
[199] At para 153, quoting I Brownlie, *Principles of Public International Law* (1989) 19.
[200] *Vivendi v Argentina*, Award, 20 August 2007, para 7.4.39.
[201] *Waste Management v Mexico*, Final Award, 30 April 2004.

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the NAFTA. In particular, a deliberate conspiracy by government authorities to defeat the investment would violate this principle:

> The Tribunal has no doubt that a deliberate conspiracy—that is to say, a conscious combination of various agencies of government without justification to defeat the purposes of an investment agreement—would constitute a breach of Article 1105(1). A basic obligation of the State under Article 1105(1) is to act in good faith and form, and not deliberately to set out to destroy or frustrate the investment by improper means.[202]

In *Bayindir v Pakistan*[203] the investor claimed that its expulsion was based on local favouritism and on bad faith, since the reasons given by the government did not correspond to its actual motivation.[204] The Tribunal in its Decision on Jurisdiction found that 'the allegedly unfair motives of expulsion, if proven, are capable of founding a fair and equitable treatment claim under the BIT'.[205]

In *Saluka v Czech Republic*[206] the Tribunal also gave a central role to the requirement of good faith in its description of FET:

> A foreign investor protected by the Treaty may in any case properly expect that the Czech Republic implements its policies *bona fide* by conduct that is, as far as it affects the investors' investment, reasonably justifiable by public policies and that such conduct does not manifestly violate the requirements of consistency, transparency, even-handedness and non-discrimination.[207]

In *Chemtura v Canada*[208] the claimants had complained about a special review of their product, claiming that the investigation had been in bad faith. The Tribunal, after examining the circumstances in some detail, concluded that the special review had been launched out of legitimate regulatory concerns and in accordance with Canada's international commitments.

In *Frontier Petroleum v Czech Republic*[209] the Tribunal gave the following description of violations of the good faith principle:

> Bad faith action by the host state includes the use of legal instruments for purposes other than those for which they were created. It also includes a conspiracy by state organs to inflict damage upon or to defeat the investment, the termination of the investment for reasons other than the one put forth by the government, and expulsion of an investment based on local favouritism. Reliance by a government on its internal structures to excuse non-compliance with contractual obligations would also be contrary to good faith.[210]

It follows from these authorities that action in bad faith against the investor would be a violation of FET. Bad faith action by the host state includes the use of legal

[202] At para 138.
[203] *Bayindir v Pakistan*, Decision on Jurisdiction, 14 November 2005.
[204] At paras 242, 243.
[205] At para 250.
[206] *Saluka v Czech Republic*, Partial Award, 17 March 2006.
[207] At para 307.
[208] *Chemtura v Canada*, Award, 2 August 2010, paras 143–8, 158, 184.
[209] *Frontier Petroleum v Czech Republic*, Final Award, 12 November 2010.
[210] At para 300. Footnotes omitted.

instruments for purposes other than those for which they were created. It also includes a conspiracy by state organs to inflict damage upon or to defeat the investment.

A related but different question is whether every violation of the standard of FET requires bad faith. Put differently, is it a valid defence for the host state to argue that, although its actions may have caused harm to the investor, those actions were bona fide and hence could not have violated the FET standard? Arbitral practice clearly indicates that the FET standard may be violated, even if no *mala fides* is involved.[211] For instance, the Tribunal in *Mondev*[212] said:

> To the modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith.[213]

The Award in *Occidental*[214] expresses the same idea. In the context of transparency and consistency as part of the FET standard the Tribunal said:

> this is an objective requirement that does not depend on whether the Respondent has proceeded in good faith or not.[215]

In *CMS v Argentina*[216] the Tribunal, after finding that FET was inseparable from stability and predictability, stated:

> The Tribunal believes this is an objective requirement unrelated to whether the Respondent has had any deliberate intention or bad faith in adopting the measures in question. Of course, such intention and bad faith can aggravate the situation but are not an essential element of the standard.[217]

Similarly, the Tribunal in *El Paso v Argentina*[218] said that 'a violation can be found even if there is a mere objective disregard of the rights enjoyed by the investor under the FET standard, and that such a violation does not require subjective bad faith on the part of the State'.[219]

Other tribunals have consistently adopted the same approach.[220]

[211] The only contrary indication would be a dictum in *Genin v Estonia*, Award, 25 June 2001, para 371: 'any procedural irregularity that may have been present would have to amount to bad faith, a willful disregard of due process of law or an extreme insufficiency of action.' However, this passage does not relate to fair and equitable treatment but to the standard of arbitrary and discriminatory measures in Art II(3)(b) of the Estonia-US BIT.

[212] *Mondev v United States*, Award, 11 October 2002.

[213] At para 116.

[214] *Occidental v Ecuador*, Award, 1 July 2004.

[215] At para 186.

[216] *CMS v Argentina*, Award, 12 May 2005.

[217] At para 280. This passage was quoted approvingly in *Vivendi v Argentina*, Award, 20 August 2007, para 7.4.12.

[218] *El Paso v Argentina*, Award, 31 October 2011.

[219] At para 372.

[220] *Tecmed v Mexico*, Award, 29 May 2003, para 153; *Loewen v United States*, Award, 26 June 2003, para 132; *Azurix v Argentina*, Award, 14 July 2006, para 372; *LG&E v Argentina*, Decision on Liability, 3 October 2006, para 129; *PSEG v Turkey*, Award, 19 January 2007, paras 245–6; *Siemens v Argentina*, Award, 6 February 2007, para 299; *Enron v Argentina*, Award, 22 May 2007, para 263;

ff. Freedom from coercion and harassment

The FET standard also applies in situations of coercion and harassment directed at the investor. In *Pope & Talbot v Canada*[221] SLD, a government regulatory authority, had launched a 'verification review' against the investor that was confrontational and aggressive. The Tribunal held that this investigation was 'more like combat than cooperative regulation'.[222] It found that these actions by the regulatory authority were 'threats and misrepresentation', 'burdensome and confrontational', and hence a violation of the FET standard.[223]

In *Tecmed v Mexico*,[224] an unlimited licence for the operation of a landfill had been replaced by a licence of limited duration. The Tribunal applied a provision in the BIT between Mexico and Spain guaranteeing FET according to international law. The Tribunal found that the denial of the permit's renewal was designed to force the investor to relocate to another site, bearing the costs and risks of a new business. The Tribunal said:

> Under such circumstances, such pressure involves forms of coercion that may be considered inconsistent with the fair and equitable treatment to be given to international investments under Article 4(1) of the Agreement and objectionable from the perspective of international law.[225]

In *Total v Argentina*[226] the investor had been forced to accept conditions much less favourable that originally agreed, including an arrangement under which it had to surrender receivables in exchange for shares. The Tribunal stated:

> This scheme must be considered as a kind of forced, inequitable, debt-for-equity swap, not due to unfavourable market conditions or a company's crisis (as is usually the premise of such swaps in the private market), but due to governmental policy and conduct by Argentina. As such, in the view of the Tribunal it represents a clear breach of the fair and equitable treatment obligation of the BIT for which Argentina is liable to pay damages.[227]

Desert Line v Yemen[228] concerned contracts for the construction of asphalt roads. A dispute between the parties involved armed threats and arrest of some the investor's personnel. Local arbitration resulted in an award of certain sums to the claimant who was, however, subsequently forced to accept a much reduced amount in a settlement agreement. The Tribunal found that the settlement agreement had been imposed upon the claimant under physical and financial duress. It said:

Duke Energy v Ecuador, Award, 18 August 2008, para 341; *National Grid v Argentina*, Award, 3 November 2008, para 173; *Jan de Nul v Egypt*, Award, 6 November 2008, para 185; *Bayindir v Pakistan*, Award, 27 August 2009, para 181; *RSM v Grenada*, Award, 10 December 2010, para 7.2.24.

[221] *Pope & Talbot v Canada*, Award on Merits, 10 April 2001, paras 156–81.
[222] At para 181.
[223] *Pope & Talbot v Canada*, Award on Damages, 31 May 2002, paras 67–9.
[224] *Tecmed v Mexico*, Award, 29 May 2003.
[225] At para 163. Footnote omitted.
[226] *Total v Argentina*, Decision on Liability, 27 December 2010.
[227] At para 338.
[228] *Desert Line v Yemen*, Award, 6 February 2008, paras 151–94.

the subjection of the Claimant's employees, family members, and equipment to arrest and armed interference, as well as the subsequent peremptory 'advice' that it was 'in [his] interest' to accept that the amount awarded be amputated by half, falls well short of minimum standards of international law and cannot be the result of an authentic fair and equitable negotiation.[229]

In the resulting award, the Tribunal took the unusual step of awarding not only damages for the violation of the FET standard but additionally awarded moral damages in the amount of US$1 million.

In a number of cases tribunals have found that the investors' allegations were not proven. These include complaints of a campaign to punish the investor for publishing material critical to the regime,[230] of aggressive tax inspections,[231] and generally of coercion and harassment.[232]

(i) Conclusion

As demonstrated above, tribunals have applied the FET standard to a number of typical fact situations and have now developed considerable case law in this area. The categories outlined above by no means exhaust the possibilities of the FET standard. With the progression of arbitral practice, tribunals are likely to develop these categories further and to add new ones.

Meeting the investor's central legitimate concerns of legal consistency, stability, and predictability remains a major, but not the only, ingredient of an investment-friendly climate in which the host state in turn can reasonably expect to attract foreign investment. Thus, no inconsistency between the interests of the host state and those of the investor in regard to the creation of a stable legal framework of the host state will be diagnosed. Built upon this joint perspective of host state and investor which informs the agreement laid down in an investment treaty, the standard of fair and equitable treatment will nevertheless not be understood to amount to a stabilization clause but will leave a measure of governmental space for regulation. Presumably, the degree of freedom generally considered appropriate in domestic legal orders will not be affected. Nevertheless, it is true that in effect the standard will narrow the discretionary space available to the host state. But it is also true, in principle, that this specific sort of limitation is indeed necessary to attract foreign investment and to make it viable in practice.

2. Full protection and security

(a) Concept

At first sight, the traditional notion of 'full protection and security' is amorphous and not readily amenable to operational applicability. However, as is the case for

[229] At para 179.
[230] *Tokios Tokelès v Ukraine*, Award, 26 July 2007, paras 123, 137.
[231] *AMTO v Ukraine*, Award, 26 March 2008, para 96.
[232] *EDF v Romania*, Award, 8 October 2009, para 300.

other standards contained in BITs, arbitral jurisprudence has gradually refined the understanding of the term. This is true both in light of the specificity of the particular wording of various treaty clauses providing protection and in regard to the particular issues falling under this concept.

Treaty practice has relied on different formulations and patterns. Whereas the traditional version (found in a series of US FCN treaties going back to the nineteenth century)[233] relies on the classical version of a guarantee which provides for 'full protection and security', other treaties have deleted the word 'full'. Another variation ensures 'protection in accordance with fair and equitable treatment'. A simple approach is restricted to the granting of 'protection' (and not 'security'), and yet another wording relies on the promise of 'legal security'. Other phrases and combinations will also be found.

These different wordings have to be applied chiefly to three different settings. In a number of earlier cases, the acts which had harmed the foreign interest were those of insurgents or rioting groups. In a second group of cases, the governmental police authorities or military units were involved. Thirdly, more recent cases have addressed governmental regulatory acts which disturb the legal stability surrounding the investor's business.

The breadth of the clause raises issues of delimitation in relation to the scope of other treaty clauses, for instance fair and equitable treatment or the umbrella clause. Especially when it comes to protection against the application of laws affecting the security and protection of the investment, the standard may acquire special importance if the treaty does not contain other clauses with a broad scope.

Some tribunals have equated the standards of full protection and security with fair and equitable treatment.[234] Other tribunals have found that the two standards were separate.[235]

(b) Standard of liability

There is broad consensus that the standard does not provide absolute protection against physical or legal infringement. In terms of the law of state responsibility, the host state is not placed under an obligation of strict liability to prevent such violations. Rather, it is generally accepted that the host state will have to exercise 'due diligence' and will have to take such measures to protect the foreign investment as are reasonable under the circumstances.[236]

[233] See R Wilson, *The International Law Standard in Treaties of the United States* (1952) 92–3; K Vandevelde, 'The Bilateral Investment Treaty Programme of the United States' (1988) 21 *Cornell Int'l LJ* 203, 204.

[234] *Wena Hotels v Egypt*, Award, 8 December 2000, paras 84–95; *Occidental v Ecuador*, Award, 1 July 2004, para 187; *PSEG v Turkey*, Award, 19 January 2007, paras 257–9; *National Grid v Argentina*, Award, 3 November 2008, paras 187, 189.

[235] *National Grid v Argentina*, Award, 3 November 2008, paras 187–90; *Jan de Nul v Egypt*, Award, 6 November 2008, para 269; *Azurix v Argentina*, Award, 14 July 2006, para 407. The analysis in *Suez v Argentina*, Decision on Liability, 30 July 2010, paras 165–7 on this point is ambivalent.

[236] R Dolzer and M Stevens, *Bilateral Investment Treaties* (1995) 61; see *Elettronica Sicula SpA (ELSI) (US v Italy)*, ICJ Reports (1989) 15, para 108; *AAPL v Sri Lanka*, Award, 27 June 1990, para

At the same time, the standard would be eviscerated and downgraded to a meaningless requirement if it were assumed—as was the case in *LESI v Algeria*[237]—that it accords no more protection than clauses on national treatment or most-favoured-nation treatment. Lack of resources to take appropriate action will not serve as an excuse for the host state.[238] Whenever state organs themselves act in violation of the standard, or significantly contribute to such action, no issues of attribution or due diligence will arise because the state will then be held directly responsible.

The standard will not be violated if a state exercises its right to legislate and regulate and thereby takes reasonable measures under the circumstances.[239] Recognition of a state's police power will not in itself lead to different conclusions; the existence of this power is consumed in the sovereign right to regulate, within the boundaries of international law, and does not in itself justify more far-reaching measures affecting the rights of the investor.[240]

(c) Protection against physical violence and harassment

The duty to grant physical protection and security may operate in relation to encroachment by state organs or in relation to private acts. Violence by state organs was under review in *AAPL v Sri Lanka*,[241] a case in which security forces had destroyed the investment in the course of a counter-insurgency operation. The Tribunal reviewed all circumstances and held that these actions were unwarranted and excessive.

In *Wena Hotels v Egypt*,[242] the Tribunal found Egypt liable under the standard because employees of a state entity had seized the hotel in question and because the police authorities had been aware of the seizure and had not acted to protect the investor before or after the invasive action.

In *AMT v Zaire*,[243] the host country was held liable under a protection and security clause in the applicable BIT after incidents of looting by elements of the armed forces.

In *Eureko v Poland*,[244] there was an allegation of harassment of the investor's senior representatives. The Tribunal found that there was no violation of the standard since there was no evidence that the state had authored or instigated

53; *TECMED v Mexico*, Award, 29 May 2003, para 177; *Noble Ventures v Romania*, Award, 12 October 2005, para 164; *Saluka v Czech Republic*, Partial Award, 17 March 2006, para 484; *Suez v Argentina*, Decision on Liability, 30 July 2010, para 158.

237 *LESI v Algeria*, Award, 12 November 2008, para 174; the BIT applicable to that case required '*protection et securité constantes, pleines et entieres*'.

238 But see the differentiated analysis in *Pantechniki v Albania*, Award, 30 July 2009, paras 71–84.

239 *AES v Hungary*, Award, 23 September 2010, para 13.3.2.

240 See *Suez v Argentina*, Decision on Liability, 30 July 2010, paras 148–50.

241 *AAPL v Sri Lanka*, Award, 27 June 1990, paras 45 et seq, 78 et seq.

242 *Wena Hotels v Egypt*, Award, 8 December 2000, para 84.

243 *AMT v Zaire*, Award, 21 February 1997, paras 6.02 et seq. See also *Saluka v Czech Republic*, Partial Award, 17 March 2006, para 483.

244 *Eureko v Poland*, Partial Award, 19 August 2005, paras 236–7.

these acts. However, the position might have been different had such actions occurred repeatedly without protective measures on the part of the state.

Other cases have concerned private violence.[245] In the *ELSI* case,[246] a Chamber of the ICJ applied a provision in an FCN treaty that granted 'the most constant protection and security'. One charge by the claimants was that the Italian authorities had allowed workers to occupy the factory. The Court found that the response of the Italian authorities had been adequate under the circumstances.[247] The Court stated that 'The reference in Article V to the provision of "constant protection and security" cannot be construed as the giving of a warranty that property shall never in any circumstances be occupied or disturbed'.[248]

In *Tecmed v Mexico*,[249] the claimant alleged that the Mexican authorities had not acted efficiently against 'social demonstrations' and disturbances at the site of the landfill under dispute. The Tribunal applied a treaty provision guaranteeing 'full protection and security to the investments... in accordance with International Law'. It found that there was not sufficient evidence to prove that the Mexican authorities had encouraged, fostered, or contributed to the actions in question and that there was no evidence that the authorities had not reacted reasonably.[250]

Similarly, *Noble Ventures v Romania*[251] involved demonstrations and protests by employees. The relevant treaty provision stipulated that the 'Investment shall... enjoy full protection and security'. The Tribunal rejected the claim, finding that it was difficult to identify any specific failure on the part of Romania to exercise due diligence in protecting the claimant.[252]

(d) Legal protection

There is also authority to the effect that the principle of full protection and security reaches beyond physical violence and requires legal protection for the investor.[253] Some treaties explicitly provide for 'full protection and legal security'.[254] However, case law supports the view that the usual formula of 'full protection and security' also provides protection against infringements of the investor's rights.

In the *ELSI* case,[255] the guarantee of 'the most constant protection and security' was also the basis for a complaint concerning the time taken (16 months) for a decision on an appeal against an order requisitioning the factory. The ICJ's

245 See also *Eastern Sugar v Czech Republic*, Partial Award, 27 March 2007, para 203.

246 *Elettronica Sicula SpA (ELSI) (US v Italy)*, ICJ Reports (1989) 15.

247 At paras 105–8.

248 At para 108.

249 *TECMED v Mexico*, Award, 29 May 2003.

250 At paras 175–7.

251 *Noble Ventures Inc v Romania*, Award, 12 October 2005.

252 At paras 164–6.

253 See *CSOB v Slovakia*, Award, 29 December 2004, para 170; *National Grid v Argentina*, Award, 3 November 2008, paras 187–90; *Frontier Petroleum v Czech Republic*, Final Award, 12 November 2010, paras 260–73; *Total v Argentina*, Decision on Liability, 27 December 2010, para 343.

254 See eg Art 4(1) of the Germany-Argentina BIT of 9 April 1991 ('*plena protección y seguridad jurídica*').

255 *Elettronica Sicula SpA (ELSI) (US v Italy)*, ICJ Reports (1989) 15.

Chamber examined this argument and found that the time taken, though undoubtedly long, did not violate the treaty standard in view of other procedural safeguards under Italian law.[256]

In *CME v Czech Republic*,[257] a regulatory authority had created a legal situation that enabled the investor's local partner to terminate the contract on which the investment depended. The Tribunal said that 'The host State is obligated to ensure that neither by amendment of its laws nor by actions of its administrative bodies is the agreed and approved security and protection of the foreign investor's investment withdrawn or devalued'.[258]

The tribunal in *Lauder v Czech Republic*, however, denied a violation of the standard on the basis of the same facts. It reached the result that the only duty of the host state under the 'protection and security' clause had been to grant the investor access to its judicial system.[259]

In *Azurix v Argentina*,[260] the Tribunal confirmed that 'full protection and security may be breached even if no physical violence or damage occurs':[261]

> The cases referred to above show that full protection and security was understood to go beyond protection and security ensured by the police. It is not only a matter of physical security; the stability afforded by a secure investment environment is as important from an investor's point of view. The tribunal is aware that in recent free trade agreements signed by the United States, for instance, with Uruguay, full protection and security is understood to be limited to the level of police protection required under customary international law. However, when the terms 'protection and security' are qualified by 'full' and no other adjective or explanation, they extend, in their ordinary meaning, the content of this standard beyond physical security.[262]

In *Siemens v Argentina*,[263] the Tribunal derived additional authority for the proposition that 'full protection and security' goes beyond physical security and extends to legal protection from the fact that the applicable BIT's definition of investment also applied to intangible assets:

> As a general matter and based on the definition of investment, which includes tangible and intangible assets, the Tribunal considers that the obligation to provide full protection and security is wider than 'physical' protection and security. It is difficult to understand how the physical security of an intangible asset would be achieved.[264]

In *Vivendi v Argentina*,[265] the Tribunal had to apply a clause requiring 'full protection and security in accordance with the principle of fair and equitable

[256] At para 109.
[257] *CME v Czech Republic*, Partial Award, 13 September 2001, para 613.
[258] At para 613.
[259] *Lauder v Czech Republic*, Award, 3 September 2001, para 314.
[260] *Azurix v Argentina*, Award, 14 July 2006.
[261] At para 406.
[262] At para 408.
[263] *Siemens v Argentina*, Award, 6 February 2007.
[264] At para 303.
[265] *Vivendi v Argentina*, Award, 20 August 2007.

treatment'. The Tribunal found that the scope of such a provision is not limited to safeguarding 'physical possession or the legally protected terms of the operation of the investment'.[266]

Sempra v Argentina[267] recognized that the standard has traditionally developed in the context of physical protection of the investment, but that exceptionally a broader interpretation would be possible.

The investor may also have to take active measures to protect the investment. In *GEA v Ukraine*,[268] the claimant argued that the host state should have initiated proceedings to inquire into a theft of the claimant's property. The Tribunal rejected the claim because the claimant itself had not brought a criminal complaint.

Biwater Gauff v Tanzania[269] confirmed that the guarantee of 'full security' extends to actions both of the host state and of third parties.[270] Due diligence is not observed in the case of failure 'to take reasonable, precautionary and preventive action' to protect an investment.[271] Full protection implies 'a State's guarantee to stability in a secure environment, both physical, commercial and legal'.[272]

Some tribunals have denied the applicability of this standard to legal protection. According to *Suez v Argentina*,[273] the concept of 'full protection and security' would not cover issues of legal security. The Tribunal assumed, as did *Rumeli v Kazakhstan*,[274] that the traditional interpretation given to this term stands in the way of an understanding that would extend to a broader construction; without further explanation, the *Suez* Tribunal also stated that this view is supported by a textual method of interpretation.[275]

In this context it is doubtful whether it is useful to distinguish 'full protection and security' from 'protection and security' and to assume that the absence of the word 'full' means that the standard must be given a narrower meaning which extends to physical security only.[276]

The Tribunal in *Parkerings v Lithuania*[277] ruled that 'full protection and security' not only requires the prevention of damage, but also requires the host state 'to restore the previous situation' and 'to punish the author of the injury'.

[266] At para 7.4.15. Cited approvingly in *AES v Hungary*, Award, 23 September 2010, para 13.3.2.
[267] *Sempra v Argentina*, Award, 28 September 2007, para 323.
[268] *GEA v Ukraine*, Award, 31 March 2011, para 247.
[269] *Biwater Gauff v Tanzania*, Award, 24 July 2008.
[270] At para 730.
[271] At para 725.
[272] At para 729.
[273] *Suez v Argentina*, Decision on Liability, 30 July 2010, paras 158–73.
[274] *Rumeli v Kazakhstan*, Award, 29 July 2008, para 668. See also *BG Group v Argentina*, Final Award, 24 December 2007, paras 323–8.
[275] At para 171.
[276] See *Parkerings v Lithuania*, Award, 11 September 2007, para 354. But see also the discussion in *Suez v Argentina*, Decision on Liability, 30 July 2010, paras 161 et seq, in particular para 169.
[277] *Parkerings v Lithuania*, Award, 11 September 2007, para 355.

(e) Relationship to customary international law

Some treaty provisions on protection and security tie the standard to general international law ('full protection and security in accordance with international law'), parallel to the practice on fair and equitable treatment. Other treaties refer to protection and security and to treatment in accordance with international law as separate standards, suggesting that the two are not identical.

The question remains whether an unqualified reference to 'full protection and security' provides an autonomous treaty standard or merely serves to incorporate customary law. To clarify the issue for purposes of the NAFTA, the three parties have stated in a Note of Interpretation that the provision on full protection and security in Article 1105(1) embodies customary law,[278] as they also did in regard to fair and equitable treatment. In other words, the NAFTA parties assume that the standard reflects those requirements embodied in the concept of the minimum standard on the level of general international law as applied to aliens.[279]

In the *ELSI* case, the ICJ suggested that the standard 'may go further' than general international law,[280] even though the clause in the relevant treaty contained a reference to international law ('full protection and security required by international law'). By contrast, some tribunals have expressed the view that this standard is no more than the traditional obligation to protect aliens under customary international law.[281]

3. The umbrella clause

(a) Meaning and origin

An umbrella clause is a provision in an investment protection treaty that guarantees the observance of obligations assumed by the host state vis-à-vis the investor. These clauses are referred to as 'umbrella clauses' because they bring contractual and other commitments under the treaty's protective umbrella. At times they are also referred to as 'observance of undertakings clauses'.[282] The most contentious issue in relation to clauses of this kind is whether, and in what circumstances, they place contracts between the host state and the investor under the treaty's protection. A typical umbrella clause in a contemporary version is Article 2(2) of the British Model Treaty: 'Each Contracting Party shall observe any obligation it may

[278] NAFTA Free Trade Commission, Interpretative Note of 31 July 2001, cited in *Mondev v United States*, Award, 11 October 2002, para 101.

[279] See pp 136 et seq.

[280] *Elettronica Sicula SpA (ELSI) (US v Italy)*, ICJ Reports (1989) 15, para 111.

[281] *Noble Ventures v Romania*, Award, 12 October 2005, para 164; *El Paso v Argentina*, Award, 31 October 2011, para 522.

[282] For a general overview, see K Yannaca-Small, 'What About This "Umbrella Clause"' in K Yannaca-Small (ed), *Arbitration Under International Investment Agreements* (2010) 479.

have entered into with regard to investments of nationals or companies of the other Contracting Party.'

The German Model Treaty contains a similar clause in Article 8(2). Many, but by no means all, BITs contain clauses of this type. The ECT offers such a clause in Article 10(1),[283] but the NAFTA does not contain an umbrella clause.

The wording of umbrella clauses in investment treaties is not uniform. A general discussion must allow for the variation in language of these clauses and the resulting differences in interpretation. Some treaties follow the British model quoted above, whereas other treaties use more detailed wording. The investment protection treaty concluded between France and Hong Kong in 1995 states in Article III:

> Without prejudice to the provisions of this Agreement, each Contracting Party shall observe any particular obligation it may have entered into with regard to investments of investors of the other Contracting Party, including provisions more favourable than those of this Agreement.

A provision that addresses the future legal order of the host state is not an umbrella clause properly speaking:

> Each contracting Party shall create and maintain in its territory a legal framework apt to guarantee to investors the continuity of legal treatment, including the compliance, in good faith, of all undertakings assumed with regard to each specific investor.[284]

Umbrella clauses are by no means of recent vintage.[285] The BIT between Germany and Pakistan of 1959—the first modern investment treaty—already contained a clause of the same kind as the current German Model Treaty. In 1959, the German Government informed the German Parliament about the effect of an umbrella clause: 'The violation of such an obligation [of an investment agreement] accordingly will also amount to a violation of the international legal obligation contained in the present Treaty.'[286]

The historical-legal context in which the origin of the clause must be assessed pertains to the post-1945 controversies about the status of investment agreements as contracts subject to the domestic laws of the host state or, alternatively, as undertakings on the level of international law.[287] In 1929, the PCIJ ruled in the *Serbian Loans* case that '[a]ny contract which is not a contract between States in

[283] ECT, Art 10(1), last sentence: 'Each Contracting Party shall observe any obligation it has entered into with an Investor or an Investment of an Investor of any other Contracting Party.'

[284] BIT between Italy and Jordan, Art 2(4). See *Salini v Jordan*, Decision on Jurisdiction, 29 November 2004, para 126.

[285] For discussion on the origin of the clause, see A Sinclair, '"The Origins of the Umbrella Clause": The International Law of Investment Protection' (2004) 4 *Arbitration International* 411.

[286] Translation by the authors. For the original German text, see J Alenfeld, *Die Investitionsförderungsverträge der Bundesrepublik Deutschland* (1971) 97, note 180.

[287] See eg F A Mann, 'State Contracts and State Responsibility' (1960) 54 *AJIL* 572; R Jennings, 'State Contracts in International Law' (1961) 37 *BYBIL* 156; S Schwebel, 'International Protection of Contractual Agreements' (1959) *ASIL Proceedings* 273; A Verdross, 'Protection of Private Property under Quasi-International Agreements' (1959) *Nederlands Tijdschrift voor Internationaal Recht* 355; C Hyde, 'Economic Development Agreements' (1962-I) 105 *Receuil des Cours de l'Académie de droit international* 267.

their capacity as subjects of international law is based on the municipal law of some country'.[288]

Contract claims may be put under the protection of a treaty and be referred to international adjudication. This point is made in Oppenheim's *International Law* in the following words:

> It is doubtful whether a breach by a state of its contractual obligations with aliens constitutes *per se* a breach of an international obligation, unless there is some such additional element as denial of justice, or expropriation, or breach of treaty, in which case it is that additional element which will constitute the basis for the state's international responsibility. However, either by virtue of a term in the contract itself or of an agreement between the state and the alien, or by virtue of an agreement between the state allegedly in breach of its contractual obligations and the state of which the alien is a national, disputes as to compliance with the terms of contracts may be referred to an internationally composed tribunal, applying, at least in part, international law.[289]

After 1945, projects for large-scale foreign investments prompted the question whether guarantees given under the domestic law of the host state provided sufficient legal stability to justify the required expenditures for such projects. Umbrella clauses were seen as a bridge between private contractual arrangements, the domestic law of the host state, and public international law allowing for more investor security. One effect of these clauses is to blur the distinction between investment arbitration and commercial arbitration.

An umbrella clause in a treaty protects a contract that an investor has entered into with the host state and is an expression of the maxim *pacta sunt servanda*. It follows that in the presence of an umbrella clause a breach by the host country of an investment contract with the foreign investor constitutes a violation of the treaty and can be raised in international arbitration.

Until 2003, the umbrella clause received little attention in academic discussion or arbitral practice, although it was often reflected in treaties. Those few authors who drew attention to the clause essentially shared the German view of the purpose of the clause as a means to elevate violations of investment contracts to the level of international law.[290] However, this phase of unanimity came to an end with the

[288] Judgment, No 14, PCIJ, Series A, No 20, 41; see also *Noble Ventures v Romania*, Award, 12 October 2005, para 53: 'The Tribunal recalls the well established rule of general international law that in normal circumstances per se a breach of a contract by the State does not give rise to direct international responsibility on the part of the State.'

[289] R Jennings and A Watts, *Oppenheim's International Law*, 9th edn (1996), vol 1, 927. Footnotes omitted.

[290] See eg P Weil, 'Problèmes relatifs aux contrats passés entre un Etat et un particulier' (1969) 128 *Recueil des Cours de l'Académie de droit international* 130; F A Mann, 'British Treaties for the Promotion and Protection of Investments' (1981) *BYBIL* 241, 246; R Dolzer and M Stevens, *Bilateral Investment Treaties* (1995) 81; I Shihata, 'Applicable Law in International Arbitration: Specific Aspects in Case of the Involvement of State Parties' in I Shihata and D Wolfensohn (eds), *The World Bank in a Changing World. Selected Essays and Lectures*, vol II (1995) 601; more recently, see C Schreuer, 'Travelling the BIT-Route—Of Waiting Periods, Umbrella Clauses and Forks in the Road' (2004) 5 *J World Investment and Trade* 231, 250.

arbitral decision in *SGS v Pakistan* in 2003[291] which departed fundamentally from the conventional understanding of the clause. Ever since this ruling, the purpose, meaning, and scope of the clause have caused controversy and given rise to disturbingly divergent lines of jurisprudence.

(b) Effective application of umbrella clauses

One line of decisions gives full effect to umbrella clauses. This practice is best represented by *Noble Ventures v Romania*[292] where the Tribunal had to interpret and apply the following clause in Article II(2)(c) of the BIT between the United States and Romania: 'Each party shall observe any obligation it may have entered into with regard to investments.' The US claimant in this case argued, inter alia, that Romania had breached the umbrella clause by failing to abide by its contractual obligation to renegotiate the debts of a formerly state-owned company acquired by the investor. The Tribunal insisted on the specificity of each umbrella clause, distinguishing earlier cases on this basis. The ruling emphasized that the wording obviously referred to investment contracts.[293] Consistent with Article 31 of the VCLT, it emphasized the object and purpose of investment treaties.[294] In the view of the Tribunal:

> two States may include in a bilateral investment treaty a provision to the effect that, in the interest of achieving the objects and goals of the treaty, the host State may incur international responsibility by reason of a breach of its contractual obligations towards the private investor of the other Party, the breach of contract being thus 'internationalized', i.e. assimilated to a breach of the treaty.[295]
>
> ... [I]n including Art. II(2)(c) in the BIT, the Parties had as their aim to equate contractual obligations governed by municipal law to international treaty obligations as established in the BIT.
>
> By reason therefore of the inclusion of Art. II(2)(c) in the BIT, the Tribunal therefore considers the Claimant's claims of breach of contract on the basis that any such breach constitutes a breach of the BIT.[296]

In the event, the Tribunal found that Romania had not violated its contractual obligation, and the Tribunal left open the question whether the wide scope of an umbrella clause has to be narrowed in some way.[297]

The *Noble Ventures* Tribunal was not the first to accord a broad or full scope to the clause. In *SGS v Philippines*,[298] the Tribunal, in its Decision on Jurisdiction,

[291] *SGS v Pakistan*, Decision on Jurisdiction, 6 August 2003.

[292] *Noble Ventures v Romania*, Award, 12 October 2005.

[293] At para 51.

[294] At para 52.

[295] At para 64. See also at para 85: 'where the acts of a governmental agency are to be attributed to the State for the purposes of applying an umbrella clause, such as Art. II(2)(c) of the BIT, breaches of a contract into which the State has entered are capable of constituting a breach of international law *by virtue of the breach of the umbrella clause*.' Emphasis in original.

[296] At paras 61, 62.

[297] At para 61.

[298] *SGS v Philippines*, Decision on Jurisdiction, 29 January 2004.

also ruled that in the presence of an umbrella clause in the Philippines-Swiss BIT, a violation of an investment agreement will lead to a violation of the investment treaty: 'Article X(2) [the umbrella clause] means what it says.'[299] The Tribunal stated:

Article X(2) makes it a breach of the BIT for the host State to fail to observe binding commitments, including contractual commitments, which it has assumed with regard to specific investments. But it does not convert the issue of the *extent* or *content* of such obligations into an issue of international law. That issue (in the present case, the issue of how much is payable for services provided under the CISS Agreement) is still governed by the investment agreement.[300]

However, *SGS v Philippines* did not carry this approach to its logical conclusion. Instead the Tribunal assumed that, due to the existence of a forum selection clause in favour of the courts of the host state, the Philippine courts were to rule on the obligations contained in the investment contract.[301]

In *Eureko v Poland*[302] the Tribunal had to rule on the umbrella clause in Article 3.5 of the treaty between the Netherlands and Poland. The Tribunal considered the ordinary meaning, the context of the clause, and the maxim of *effet utile*. It concluded that breaches by Poland of its obligations under the contracts could be breaches of the BIT's umbrella clause, even if they did not violate the BIT's other standards.[303] The Tribunal said:

The plain meaning—the 'ordinary meaning'—of a provision prescribing that a State 'shall observe any obligation it may have entered into' with regard to certain foreign investment is not obscure. The phrase, 'shall observe' is imperative and categorical. 'Any' obligations is capacious; it means not only obligations of a certain type, but 'any'—that is to say, all—obligations entered into with regard to investments of investors of the other Contracting Party.... The context of Article 3.5 [the umbrella clause] is a Treaty whose object and purpose is 'the encouragement and reciprocal protection of investment', a treaty which contains specific provisions designed to accomplish that end, of which Article 3.5 is one. It is a cardinal rule of the interpretation of treaties that each and every operative clause of a treaty is to be interpreted as meaningful rather than meaningless.[304]

In the event, the Tribunal found that Poland had violated its obligations arising from a privatization scheme vis-à-vis the investor.

[299] At para 119.
[300] At para 128. Emphasis in original.
[301] At para 155:

> The Philippine courts are available to hear SGS's contract claim. Until the question of the scope or extent of the Respondent's obligation to pay is clarified—whether by agreement between the parties or by proceedings in the Philippine courts as provided for in Article 12 of the CISS Agreement—a decision by this Tribunal on SGS's claim to payment would be premature.

For a critical review, see C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (2004) *Law & Practice of Int'l Courts and Tribunals* 1, 11.
[302] *Eureko v Poland*, Partial Award, 19 August 2005; for a critical review, see Z Douglas, 'Nothing if not Critical for Investment Treaty Arbitration: *Occidental*, *Eureko* and *Methanex*' (2006) 22 *Arbitration International* 27.
[303] At para 250.
[304] At paras 246, 248.

In *SGS v Paraguay* the claim was for unpaid bills under a contract between the investor and the state for the pre-shipment inspection of goods. The BIT between Switzerland and Paraguay provided in Article 11 that '[e]ither Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party'. The Tribunal rejected a restrictive interpretation of this umbrella clause based either on the nature of the contract or on the nature of its breach. It said:

Article 11 does not exclude commercial contracts of the State from its scope. Likewise, Article 11 does not state that its constant guarantee of observance of such commitments may be breached only through actions that a commercial counterparty cannot take, through abuses of state power, or through exertions of undue government influence.[305]

... Article 11 requires the 'observance' of commitments. Also as a matter of the ordinary meaning of the term, a failure to meet one's obligations under a contract is clearly a failure to 'observe' one's commitments. There is nothing in Article 11 that states or implies that a government will only fail to observe its commitments if it abuses its sovereign authority.[306]

In a number of other decisions tribunals similarly gave full effect to umbrella clauses and confirmed that, by virtue of such a clause, failure by the host state to meet obligations assumed in relation to investments amounted to a breach of the treaty.[307]

(c) Restrictive application of umbrella clauses

In a series of other cases tribunals have imposed various limitations on the application of the umbrella clause.[308] In *SGS v Pakistan*[309] the Swiss claimant had concluded a contract with Pakistan on pre-shipment inspection services with a forum selection clause for Pakistani courts. When Pakistan unilaterally terminated the contract, the claimant started proceedings at the International Centre for Settlement of Investment Disputes (ICSID) under the BIT between Pakistan and Switzerland. The BIT contained the following clause: 'Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party.'

The Tribunal found that the proper mode of interpretation was a restrictive one (*in dubio mitius*).[310] The Tribunal made no reference to the modes of interpretation laid down in Article 31 of the VCLT which does not in its wording embrace

[305] *SGS v Paraguay*, Decision on Jurisdiction, 12 February 2010, para 168.
[306] *SGS v Paraguay*, Award, 10 February 2012, para 91.
[307] *LG&E v Argentina*, Decision on Liability, 3 October 2006, paras 164–75; *Siemens v Argentina*, Award, 6 February 2007, paras 196–206; *Plama v Bulgaria*, Award, 27 August 2008, paras 185–7; *Duke Energy v Ecuador*, Award, 18 August 2008, paras 314–25; *AMTO v Ukraine*, Award, 26 March 2008, paras 109–12.
[308] For a critical evaluation, see S W Schill, 'Umbrella Clauses as Public Law Concepts in Comparative Perspective' in S W Schill (ed), *International Investment Law and Comparative Public Law* (2010) 317.
[309] *SGS v Pakistan*, Decision on Jurisdiction, 6 August 2003.
[310] At para 171.

this maxim. In light of this interpretative approach, the Tribunal concluded that any other understanding would have a far-reaching impact on the sovereignty of the host state which could not be presumed in the absence of a clear expression of a corresponding will by the parties.[311]

The Tribunal presented four arguments in support of this position. First, the conventional view would also cover non-contractual obligations arising under the laws of the host state, including the smallest types of commitment, and would lead to a flood of lawsuits before international tribunals.[312] Secondly, the conventional view would make other guarantees contained in investment treaties superfluous because even a violation of a small obligation would allow a lawsuit.[313] Thirdly, the Tribunal considered that the location of the umbrella clause not in the substantive guarantees but towards the end of the treaty spoke against a far-reaching obligation.[314] And, fourthly, it pointed out that the forum selection in investment agreements would, under the conventional view, not be binding for the investor whereas the host state would be bound to honour such clauses.[315] The Tribunal did not refer to the distinction between 'commercial acts' and 'sovereign acts'.

The Tribunal denied that its position would deprive an umbrella clause of its meaning. It pointed out that the clause would be relevant in the context of implementation of the investment treaty in the domestic legal order or if the host state failed to participate in international proceedings to which it had agreed earlier.[316]

This decision was widely criticized.[317] The sharpest criticism came from the Tribunal in *SGS v Philippines*,[318] but commentators also pointed to weaknesses of the decision.[319] The most vulnerable aspect of the decision is the lack of any attempt to ground the method of interpretation in the accepted canons embodied in Article 31 of the VCLT.

For a while it seemed as though *SGS v Pakistan* would remain an isolated decision. But the decision has also found a measure of support.[320] In 2006, two nearly identical decisions—in *El Paso v Argentina*[321] and in *Pan America v*

[311] At paras 167, 168. [312] At paras 166, 168. [313] At para 168.
[314] At para 169. [315] At para 168. [316] At para 172.
[317] The Government of Switzerland took the unusual step of expressing its disapproval and concern over the decision in a letter of 1 October 2003 to the Deputy Secretary-General of ICSID.
[318] *SGS v Philippines*, Decision on Jurisdiction, 29 January 2004, para 125: 'Not only are the reasons given by the Tribunal in *SGS v Pakistan* unconvincing: the Tribunal failed to give any clear meaning to the "umbrella clause".' See also *Eureko v Poland*, Partial Award, 19 August 2005, para 257.
[319] S A Alexandrov, 'Breaches of Contract and Breaches of Treaty, The Jurisdiction of Treaty-based Arbitration Tribunals to Decide Breach of Contract Claims in *SGS v Pakistan* and *SGS v Philippines*' (2004) 5 *J World Investment and Trade* 555, 569; C Schreuer 'Travelling the BIT-Route—Of Waiting Periods, Umbrella Clauses and Forks in the Road' (2004) *J World Investment and Trade* 231, 253; T Wälde, 'The "Umbrella Clause" in Investment Arbitration—A Comment on Original Intentions and Recent Cases' (2005) 6 *J World Investment and Trade* 183, 225; E Gaillard, *La jurisprudence du CIRDI* (2004) 834.
[320] See eg *Toto Costruzioni Generali v Lebanon*, Decision on Jurisdiction, 11 September 2009, paras 187–202.
[321] *El Paso Energy v Argentina*, Decision on Jurisdiction, 27 April 2006.

Argentina[322]—explicitly supported the first and second arguments set out in *SGS v Pakistan* (flood of lawsuits, overreach because of wider scope than other treaty guarantees).[323] But unlike *SGS v Pakistan*, the Tribunals then introduced the distinction between the state as a merchant and the state as a sovereign. It concluded, with a broad brush, that investment arbitration will cover only disputes concerning investment agreements or state contracts in which the state is involved 'as a sovereign' but not mere commercial contracts.[324] The Tribunal in *El Paso* sought to establish a balance between the interests of the host state and those of the investor:

> This Tribunal considers that a balanced interpretation is needed, taking into account both State sovereignty and the State's responsibility to create an adapted and evolutionary framework for the development of economic activities, and the necessity to protect foreign investment and its continuing flow.[325]

Thus, the decisions in *El Paso* and in *Pan American* did not restrict the scope of the umbrella clause as drastically as *SGS v Pakistan*. They accept that obligations in investment agreements are covered by the clause to the extent that they bind the state in its sovereign capacity. Essentially, the two decisions seem to echo the French concept of *contrat administratif*.[326]

The distinction between different types of investment agreement was subsequently rejected in the Award in *Siemens v Argentina*[327] where the Tribunal stated that:

> The Tribunal does not subscribe to the view of the Respondent that investment agreements should be distinguished from concession agreements of an administrative nature. Such distinction has no basis in Article 7(2) of the Treaty which refers to 'any obligations', or in the definition of 'investment' in the Treaty. Any agreement related to an investment that qualifies as such under the Treaty would be part of the obligations covered under the umbrella clause.[328]

Another approach to limiting the effect of the umbrella clause does not look at the nature of the affected contract but at the nature or magnitude of its violation. The

[322] *Pan America/BP v Argentina*, Decision on Preliminary Objections, 27 July 2006; two out of the three arbitrators were the same as in the *El Paso* decision.
[323] See *El Paso Energy v Argentina*, Decision on Jurisdiction, 27 April 2006, paras 72–4; *Pan America/BP v Argentina*, Decision on Preliminary Objections, 27 July 2006, paras 101–3.
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[325] *El Paso Energy v Argentina*, Decision on Jurisdiction, 27 April 2006, para 70.
[326] This position is contrary to the position taken by arbitrator René-Jean Dupuy in *Texaco v Libya*, 53 ILR (1979) 389, para 72 who had held that the theory of administrative contracts had no place in international law. See also *ARAMCO v Saudi Arabia*, 27 ILR (1963) 117, 164.
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Tribunal in *CMS v Argentina* referred to the distinction between governmental and commercial actions and the significance of the interference with the contract:

> the tribunal believes the Respondent is correct in arguing that not all contract breaches result in breaches of the treaty. The standard of protection of the treaty will be engaged only when there is a specific breach of treaty rights and obligations or a violation of contract rights protected under the treaty. Purely commercial aspects of a contract might not be protected by the treaty in some situations, but the protection is likely to be available when there is significant interference by governments or public agencies with the rights of the investor.[329]

Similarly, in *Sempra v Argentina*[330] the Tribunal held that ordinary commercial breaches of a contract would not violate the umbrella clause in the Argentina-US BIT. Only a breach in the exercise of a sovereign state function or power but not the conduct of an ordinary contract party could effect a breach. In the particular case, the Tribunal found that the sweeping changes that Argentina had introduced were not ordinary contractual breaches but had been brought about in exercise of the state's public function. Therefore, it concluded that breaches of the obligations in question had resulted in a breach of the umbrella clause.[331]

An examination of the current strands of jurisprudence shows clearly conflicting positions. The survey of the jurisprudence interpreting the umbrella clause indicates that the understanding of the rule remains in a state of flux. However, a terminological observation and a comment on the discussion of the substance of the clause are appropriate at this stage. The terminological point concerns the distinction between 'treaty claims' and 'contract claims', introduced by the *Vivendi* Annulment Committee and subsequently often relied upon by tribunals.[332] While the simplicity of the distinction may have seemed helpful for analytical purposes at the outset, the current position of jurisprudence on the umbrella clause suggests that the contrasting of 'treaty claims' and 'contract claims' does not facilitate an understanding of the scope of the clause. The crucial point lies in recognition that certain (or all) types of violations of contracts between the state and the investor will, in the presence of an umbrella clause, amount to a violation of the investment treaty.

States entering into an investment treaty are free to fashion the scope of the treaty and the guarantees granted therein. If the parties choose to extend the scope of the agreement beyond the confines of the classical understanding of an investment treaty and also cover, to some extent, operations previously deemed 'commercial' or 'contractual' in nature, conventional terminology cannot stand in the

[329] *CMS v Argentina*, Award, 12 May 2005, para 299.
[330] *Sempra v Argentina*, Award, 28 September 2007.
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> In a case where the essential basis of a claim brought before an international tribunal is a breach of contract, the tribunal will give effect to any valid choice of forum clause in the contract. . . . On the other hand, where the fundamental basis of the claim is a treaty laying down an independent standard by which the conduct of the parties is to be judged, the existence of an exclusive jurisdiction clause in a contract between the claimant and the respondent state cannot operate as a bar to the application of the treaty standard.

Generally on the distinction between treaty claims and contract claims, see pp 261, 268, 272, 275–8.

way of the parties' intentions. For this reason, any attempt to define the scope of the umbrella clause by reference to abstract concepts such as 'sovereign acts', 'commercial acts', or '*contrats administratifs*' will carry no methodological power of persuasion when it comes to interpreting and applying the clause. Ultimately, no justification exists for ignoring or revising the canons of interpretation laid down in Article 31 of the VCLT. References to conventional terminological distinctions or to categories of a specific domestic legal order have no place within this canon.

(d) Umbrella clauses and privity of contract

In principle, contracts to which an umbrella clause is to apply would be between the disputing parties, that is, a state and a foreign investor. But in some cases the disputing parties and the parties to the contract on which the investor relies for the purposes of the umbrella clause are not identical. On the host state's side, the party to the contract may be a state entity or a territorial subdivision rather than the state itself. On the investor's side, the party to the contract may not be the foreign investor itself but its subsidiary in the host state. In these situations, the question arises whether an umbrella clause will protect a contract that is not directly between the host state and the investor.[333]

Noble Ventures v Romania[334] concerned a contract between the claimant and the Romanian 'State Ownership Fund', a separate legal entity. The Tribunal reached the conclusion that the contractual conduct of the Fund had to be attributed to the Romanian Government in view of the grant of governmental power to the Fund. The Tribunal found that, for the purposes of attribution, the distinction between commercial acts and sovereign acts had no relevance.[335] It followed that the umbrella clause was applicable to the contract. The Tribunal said:

> where the acts of a governmental agency are to be attributed to the State for the purposes of applying an umbrella clause, such as Art. II(2)(c) of the BIT, breaches of a contract into which the State has entered are capable of constituting a breach of international law *by virtue of the breach of the umbrella clause.*[336]

In a series of other decisions, tribunals found that the umbrella clause was inapplicable where the state had not contracted in its own name.[337] In *Impregilo v Pakistan*,[338] the contracts had been concluded not with Pakistan directly but with the Pakistan Water and Power Development Authority. The claimant wanted to benefit from an umbrella clause in a third country BIT by way of an MFN clause contained in the BIT between Italy and Pakistan. The Tribunal found that

[333] See N Gallus, 'An Umbrella just for Two? BIT Obligations Observance Clauses and the Parties to a Contract' (2008) 24 *Arbitration International* 157.
[334] *Noble Ventures v Romania*, Award, 12 October 2005.
[335] At para 82.
[336] At para 85. Emphasis in original.
[337] *Azurix v Argentina*, Award, 14 July 2006, paras 52, 384; *AMTO v Ukraine*, Award, 26 March 2008, paras 109–12; *EDF v Romania*, Award, 8 October 2009, paras 317, 318; *Hamester v Ghana*, Award, 18 June 2010, paras 339–50.
[338] *Impregilo v Pakistan*, Decision on Jurisdiction, 22 April 2005.

contracts concluded by a separate entity of Pakistan would not be protected by an umbrella clause.[339] A similar problem arises on the investor's side when it operates through a local company that enters into a contract. The question then arises whether the foreign investor may rely on the umbrella clause in relation to a contract to which it is not a party. The ECT in Article 10(1) gives an affirmative answer to this question by referring to 'any obligations it has entered into with an Investor *or an Investment of an Investor*'.[340]

Most BITs do not contain a clarification of this kind. The practice of tribunals is divided on whether foreign investors are entitled to protection under umbrella clauses for claims arising from the contracts of their local subsidiaries. Some tribunals have allowed claims of this nature.

In *Continental Casualty v Argentina*,[341] the investor's local subsidiary, CNA, had entered into a number of contracts with Argentina. The claimant invoked the umbrella clause in respect of these contracts[342] and the Tribunal left no doubt that the umbrella clause covered contracts concluded by the investor's subsidiary. The Tribunal stated, with respect to obligations covered by the umbrella clause in Article II(2)(c) of the Argentina-US BIT:

> provided that these obligations have been entered 'with regard' to investments, they may have been entered with persons or entities other than foreign investors themselves, so that an undertaking by the host State with a subsidiary such as CNA is not in principle excluded.[343]

Other tribunals have similarly extended the effect of umbrella clauses to contracts entered into by local subsidiaries of the foreign investors.[344]

In another group of cases, tribunals have concluded that successful invocation of the umbrella clause requires that the contract is directly with the foreign investor and not with its local subsidiary.[345] In *Azurix v Argentina*,[346] a concession agreement had been concluded between a province of Argentina and the subsidiary of Azurix ABA. The Tribunal recalled that Azurix and the respondent had no contractual relationship: the obligations undertaken in the concession contract

[339] At para 223.

[340] Emphasis added. The Reader's Guide to the ECT offers the following explanation: 'This provision covers any contract that a host country has concluded with a subsidiary of the foreign investor in the host country, or a contract between the host country and the parent company of the subsidiary.' See also *AMTO v Ukraine*, Award, 26 March 2008, para 110.

[341] *Continental Casualty v Argentina*, Award, 5 September 2008.

[342] At para 288.

[343] At para 297. See also para 98.

[344] *CMS v Argentina*, Award, 12 May 2005, paras 296–303; *Enron v Argentina*, Award, 22 May 2007, paras 269–77. The ad hoc Committee declined to annul this part of the Award: Decision on Annulment, 30 July 2010, paras 317–46; *Sempra v Argentina*, Award, 28 September 2007, paras 308–14; *Duke Energy v Ecuador*, Award, 18 August 2008, paras 314–25.

[345] *Siemens v Argentina*, Award, 6 February 2007, paras 204–6; *BG Group v Argentina*, Final Award, 24 December 2007, paras 206–15, 361–6; *El Paso v Argentina*, Award, 31 October 2011, paras 531–8.

[346] *Azurix v Argentina*, Award, 14 July 2006.

were undertaken by the province, not Argentina, in favour of ABA, not Azurix.[347] The Tribunal said:

> there is no undertaking to be honored by Argentina to Azurix other than the obligations under the BIT. Even if for argument's sake, it would be possible under Article II(2)(c) [the umbrella clause] to hold Argentina responsible for the alleged breaches of the Concession Agreement by the Province, it was ABA and not Azurix which was the party to this Agreement.[348]

In *CMS v Argentina*, the claimant was a minority shareholder in a local company TGN. The Tribunal had allowed the application of the umbrella clause with respect to a licence obtained by TGN.[349] In proceedings for the Award's annulment, the ad hoc Committee noted that under Argentinian law the obligations of Argentina under the licence were obligations to TGN, not to CMS.[350] The Committee annulled the part of the Award dealing with the umbrella clause for failure to state reasons. In the Committee's view it was 'quite unclear how the Tribunal arrived at its conclusion that CMS could enforce the obligations of Argentina to TGN'.[351]

(e) Umbrella clauses and unilateral acts

In the discussion of umbrella clauses, attention is mostly centred on contracts between the host state and the investor. However, states may assume obligations not only by way of contracts but also through unilateral declarations such as legislation and executive acts.[352] Case law indicates that umbrella clauses are not restricted to contractual obligations but are capable of protecting obligations of the host state assumed unilaterally through legislation or executive acts.[353]

Tribunals have recognized, in principle, that umbrella clauses in which states undertake to observe obligations with regard to investments cover unilateral undertakings.[354] *LG&E v Argentina*,[355] involved an umbrella clause referring to the observance of 'any obligation it may have entered into with regard to investments'.[356] The case concerned the abrogation of rights granted to investors under a Gas Law and its implementing regulations. The Tribunal found that this legislation contained 'obligations' in the sense of the umbrella clause:

[347] At para 52. [348] At para 384.

[349] *CMS v Argentina*, Award, 12 May 2005, paras 296–303.

[350] *CMS v Argentina*, Decision on Annulment, 25 September 2007.

[351] At para 96.

[352] W M Reisman and M H Arsanjani, 'The Question of Unilateral Governmental Statements as Applicable Law in Investment Disputes' (2004) 19 *ICSID Review-FILJ* 328.

[353] See M C Gritón Salias, 'Do Umbrella Clauses Apply to Unilateral Undertakings?' in C Binder, U Kriebaum, A Reinisch, and S Wittich (eds), *International Investment Law for the 21st Century* (2009) 490.

[354] *Enron v Argentina*, Award, 22 May 2007, paras 269–77; see also Decision on Annulment, 30 July 2010, paras 317–46; *Noble Energy v Ecuador*, Decision on Jurisdiction, 5 March 2008, paras 154–7; *Plama v Bulgaria*, Award, 27 August 2008, paras 185–7.

[355] *LG&E v Argentina*, Decision on Liability, 3 October 2006, paras 169–75.

[356] BIT between Argentina and the United States, Art II(2)(c).

These laws and regulations became obligations within the meaning of Article II(2)(c), by virtue of targeting foreign investors and applying specifically to their investments, that gave rise to liability under the umbrella clause.[357]

Some tribunals have read limitations into the clauses on the basis of the specific wording of umbrella clauses. A reference to obligations with regard to 'specific investments' was seen to exclude general legal obligations arising from legislative measures.[358] Other tribunals have found that the words 'entered into' contained in an umbrella clause could only be read as restricting the clause to contractual undertakings.[359] In *Noble Ventures v Romania*[360] the Tribunal said:

> The employment of the notion 'entered into' indicates that specific commitments are referred to and not general commitments, for example by way of legislative acts. This is also the reason why Art. II(2)(c) would be very much an empty base unless understood as referring to contracts.[361]

4. Access to justice, fair procedure, and denial of justice

The 2004 and 2012 US Model BITs in Article 5(2)(a) state that the FET standard includes the obligation 'not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world'. It would appear that even without such a specific reference, these principles are still covered, at least in part, by the requirement of full protection and security[362] and by the rule on fair and equitable treatment.[363] Also, it is plausible to assume that the US approach refers to the relevant rules of customary law.

The standard will cover proceedings before the courts of the host state. However, depending on the wording of the treaty, it may also find application in the conduct of a party during arbitration proceedings, in particular if a party ignores a previous agreement to arbitrate.[364] Generally, the principle of denial of justice applies to actions of all branches of a government.[365] An international tribunal will decide

[357] At para 175.
[358] *SGS v Philippines*, Decision on Jurisdiction, 29 January 2004, para 121.
[359] *CMS v Argentina*, Decision on Annulment, 25 September 2007, para 95(a) and (b). See also *Continental Casualty v Argentina*, Award, 5 September 2008, paras 297–303.
[360] *Noble Ventures v Romania*, Award, 12 October 2005.
[361] At para 51.
[362] See pp 160 et seq.
[363] See pp 130 et seq.
[364] In *Waste Management v Mexico*, Final Award, 30 April 2004, paras 118–40, one issue was that a Mexican city refused to advance funds to cover the cost of local arbitration and the claimant then withdrew the case. The Tribunal ruled that the refusal of payment did not amount to a wrongful act.
[365] See *Petrobart v Kyrgyz Republic*, Award, 29 March 2005, pp 75–7. This case involved the improper intervention of the government in judicial proceedings. Due process and procedural fairness are not required for strictly internal governmental matters; see *Bayindir v Pakistan*, Award, 27 August 2009, paras 338 et seq.

independently whether the principle has been respected and will in this respect not be bound by the position of a domestic court.[366]

The principles of access to justice, fair procedure, and the prohibition of denial of justice relate to three stages of the judicial process: the right to bring a claim, the right of both parties to fair treatment during the proceedings, and the right to an appropriate decision at the end of the process and its enforcement. In *Azinian v Mexico*,[367] the Tribunal summarized these criteria in the following terms:

> A denial of justice could be pleaded if the relevant courts refuse to entertain a suit, if they subject it to undue delay, or if they administer justice in a seriously inadequate way.... There is a fourth type of denial of justice, namely the clear and malicious misapplication of the law.[368]

The principles of international law that apply during all phases set forth a broad framework which national rules have to respect. Essentially, these principles operate as the expression of an international standard that requires the establishment of a decent and civilized system of justice as reflected in accepted international and national practice. Thus, the concept of the minimum standard of international law[369] has a substantive and a procedural side. So far, most issues of procedural propriety have in practice been reviewed under the standard of fair and equitable treatment, as discussed above.[370]

In *Duke Energy v Ecuador*,[371] the Tribunal considered that the duty to provide effective access to justice 'seeks to implement and form part of the more general guarantee against denial of justice'.[372] The case was brought by an investor who had concluded an arbitration agreement with a local Peruvian company subject to local law. In arbitration proceedings initiated by the investor in this local setting, the local arbitral tribunal had upheld a jurisdictional objection by the state, and the claimant did not challenge this award. The Tribunal did not agree with the claimant that Peru's conduct had failed to provide effective means to assert a claim.[373]

[366] See *Feldman v Mexico*, Award, 16 December 2002, para 140; *Himpurna v Indonesia*, XXV ICCA YB Commercial Arbitration 109, 181. Tribunals have not yet spelled out in detail under what circumstances the misapplication of domestic law may lead to international responsibility; see *Waste Management v Mexico*, Award, 30 April 2004, paras 129 et seq. As to the decision of lower courts, it is widely assumed that their rulings will not be considered to amount to an internationally wrongful act as long as a reasonable opportunity exists for the foreigner for appropriate review; see *Ambatielos Claim*, ICJ Reports (1953) 10; *Loewen v United States*, Award, 26 June 2003, para 154.
[367] *Azinian v Mexico*, Award, 1 November 1999.
[368] At paras 102, 103. See also *Mondev v United States*, Award, 11 October 2002, paras 126–7; *Parkerings v Lithuania*, Award, 11 September 2007, para 317.
[369] See p 3.
[370] See pp 154–6.
[371] *Duke Energy v Ecuador*, Award, 18 August 2008, para 391.
[372] At para 391.
[373] At paras 390–403.

In *SGS v Paraguay* the claim was for unpaid bills under a contract between the investor and the state for the pre-shipment inspection of goods. The BIT between Switzerland and Paraguay provided in Article 11 that '[e]ither Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party'. The Tribunal rejected a restrictive interpretation of this umbrella clause based either on the nature of the contract or on the nature of its breach. It said:

> Article 11 does not exclude commercial contracts of the State from its scope. Likewise, Article 11 does not state that its constant guarantee of observance of such commitments may be breached only through actions that a commercial counterparty cannot take, through abuses of state power, or through exertions of undue government influence.[305]
>
> ... Article 11 requires the 'observance' of commitments. Also as a matter of the ordinary meaning of the term, a failure to meet one's obligations under a contract is clearly a failure to 'observe' one's commitments. There is nothing in Article 11 that states or implies that a government will only fail to observe its commitments if it abuses its sovereign authority.[306]

In a number of other decisions tribunals similarly gave full effect to umbrella clauses and confirmed that, by virtue of such a clause, failure by the host state to meet obligations assumed in relation to investments amounted to a breach of the treaty.[307]

(c) Restrictive application of umbrella clauses

In a series of other cases tribunals have imposed various limitations on the application of the umbrella clause.[308] In *SGS v Pakistan*[309] the Swiss claimant had concluded a contract with Pakistan on pre-shipment inspection services with a forum selection clause for Pakistani courts. When Pakistan unilaterally terminated the contract, the claimant started proceedings at the International Centre for Settlement of Investment Disputes (ICSID) under the BIT between Pakistan and Switzerland. The BIT contained the following clause: 'Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party.'

The Tribunal found that the proper mode of interpretation was a restrictive one (*in dubio mitius*).[310] The Tribunal made no reference to the modes of interpretation laid down in Article 31 of the VCLT which does not in its wording embrace

[305] *SGS v Paraguay*, Decision on Jurisdiction, 12 February 2010, para 168.

[306] *SGS v Paraguay*, Award, 10 February 2012, para 91.

[307] *LG&E v Argentina*, Decision on Liability, 3 October 2006, paras 164–75; *Siemens v Argentina*, Award, 6 February 2007, paras 196–206; *Plama v Bulgaria*, Award, 27 August 2008, paras 185–7; *Duke Energy v Ecuador*, Award, 18 August 2008, paras 314–25; *AMTO v Ukraine*, Award, 26 March 2008, paras 109–12.

[308] For a critical evaluation, see S W Schill, 'Umbrella Clauses as Public Law Concepts in Comparative Perspective' in S W Schill (ed), *International Investment Law and Comparative Public Law* (2010) 317.

[309] *SGS v Pakistan*, Decision on Jurisdiction, 6 August 2003.

[310] At para 171.

this maxim. In light of this interpretative approach, the Tribunal concluded that any other understanding would have a far-reaching impact on the sovereignty of the host state which could not be presumed in the absence of a clear expression of a corresponding will by the parties.[311]

The Tribunal presented four arguments in support of this position. First, the conventional view would also cover non-contractual obligations arising under the laws of the host state, including the smallest types of commitment, and would lead to a flood of lawsuits before international tribunals.[312] Secondly, the conventional view would make other guarantees contained in investment treaties superfluous because even a violation of a small obligation would allow a lawsuit.[313] Thirdly, the Tribunal considered that the location of the umbrella clause not in the substantive guarantees but towards the end of the treaty spoke against a far-reaching obligation.[314] And, fourthly, it pointed out that the forum selection in investment agreements would, under the conventional view, not be binding for the investor whereas the host state would be bound to honour such clauses.[315] The Tribunal did not refer to the distinction between 'commercial acts' and 'sovereign acts'.

The Tribunal denied that its position would deprive an umbrella clause of its meaning. It pointed out that the clause would be relevant in the context of implementation of the investment treaty in the domestic legal order or if the host state failed to participate in international proceedings to which it had agreed earlier.[316]

This decision was widely criticized.[317] The sharpest criticism came from the Tribunal in *SGS v Philippines*,[318] but commentators also pointed to weaknesses of the decision.[319] The most vulnerable aspect of the decision is the lack of any attempt to ground the method of interpretation in the accepted canons embodied in Article 31 of the VCLT.

For a while it seemed as though *SGS v Pakistan* would remain an isolated decision. But the decision has also found a measure of support.[320] In 2006, two nearly identical decisions—in *El Paso v Argentina*[321] and in *Pan America v*

[311] At paras 167, 168. [312] At paras 166, 168. [313] At para 168.
[314] At para 169. [315] At para 168. [316] At para 172.
[317] The Government of Switzerland took the unusual step of expressing its disapproval and concern over the decision in a letter of 1 October 2003 to the Deputy Secretary-General of ICSID.
[318] *SGS v Philippines*, Decision on Jurisdiction, 29 January 2004, para 125: 'Not only are the reasons given by the Tribunal in *SGS v Pakistan* unconvincing: the Tribunal failed to give any clear meaning to the "umbrella clause".' See also *Eureko v Poland*, Partial Award, 19 August 2005, para 257.
[319] S A Alexandrov, 'Breaches of Contract and Breaches of Treaty, The Jurisdiction of Treaty-based Arbitration Tribunals to Decide Breach of Contract Claims in *SGS v Pakistan* and *SGS v Philippines*' (2004) 5 *J World Investment and Trade* 555, 569; C Schreuer 'Travelling the BIT-Route—Of Waiting Periods, Umbrella Clauses and Forks in the Road' (2004) *J World Investment and Trade* 231, 253; T Wälde, 'The "Umbrella Clause" in Investment Arbitration—A Comment on Original Intentions and Recent Cases' (2005) 6 *J World Investment and Trade* 183, 225; E Gaillard, *La jurisprudence du CIRDI* (2004) 834.
[320] See eg *Toto Costruzioni Generali v Lebanon*, Decision on Jurisdiction, 11 September 2009, paras 187–202.
[321] *El Paso Energy v Argentina*, Decision on Jurisdiction, 27 April 2006.

Argentina[322]—explicitly supported the first and second arguments set out in *SGS v Pakistan* (flood of lawsuits, overreach because of wider scope than other treaty guarantees).[323] But unlike *SGS v Pakistan*, the Tribunals then introduced the distinction between the state as a merchant and the state as a sovereign. It concluded, with a broad brush, that investment arbitration will cover only disputes concerning investment agreements or state contracts in which the state is involved 'as a sovereign' but not mere commercial contracts.[324] The Tribunal in *El Paso* sought to establish a balance between the interests of the host state and those of the investor:

> This Tribunal considers that a balanced interpretation is needed, taking into account both State sovereignty and the State's responsibility to create an adapted and evolutionary framework for the development of economic activities, and the necessity to protect foreign investment and its continuing flow.[325]

Thus, the decisions in *El Paso* and in *Pan American* did not restrict the scope of the umbrella clause as drastically as *SGS v Pakistan*. They accept that obligations in investment agreements are covered by the clause to the extent that they bind the state in its sovereign capacity. Essentially, the two decisions seem to echo the French concept of *contrat administratif*.[326]

The distinction between different types of investment agreement was subsequently rejected in the Award in *Siemens v Argentina*[327] where the Tribunal stated that:

> The Tribunal does not subscribe to the view of the Respondent that investment agreements should be distinguished from concession agreements of an administrative nature. Such distinction has no basis in Article 7(2) of the Treaty which refers to 'any obligations', or in the definition of 'investment' in the Treaty. Any agreement related to an investment that qualifies as such under the Treaty would be part of the obligations covered under the umbrella clause.[328]

Another approach to limiting the effect of the umbrella clause does not look at the nature of the affected contract but at the nature or magnitude of its violation. The

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[326] This position is contrary to the position taken by arbitrator René-Jean Dupuy in *Texaco v Libya*, 53 ILR (1979) 389, para 72 who had held that the theory of administrative contracts had no place in international law. See also *ARAMCO v Saudi Arabia*, 27 ILR (1963) 117, 164.

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[330] *Sempra v Argentina*, Award, 28 September 2007.
[331] At paras 305–14.
[332] *Vivendi v Argentina*, Decision on Annulment, 3 July 2002, paras 98, 101:

> In a case where the essential basis of a claim brought before an international tribunal is a breach of contract, the tribunal will give effect to any valid choice of forum clause in the contract. . . . On the other hand, where the fundamental basis of the claim is a treaty laying down an independent standard by which the conduct of the parties is to be judged, the existence of an exclusive jurisdiction clause in a contract between the claimant and the respondent state cannot operate as a bar to the application of the treaty standard.

Generally on the distinction between treaty claims and contract claims, see pp 261, 268, 272, 275–8.

way of the parties' intentions. For this reason, any attempt to define the scope of the umbrella clause by reference to abstract concepts such as 'sovereign acts', 'commercial acts', or '*contrats administratifs*' will carry no methodological power of persuasion when it comes to interpreting and applying the clause. Ultimately, no justification exists for ignoring or revising the canons of interpretation laid down in Article 31 of the VCLT. References to conventional terminological distinctions or to categories of a specific domestic legal order have no place within this canon.

(d) Umbrella clauses and privity of contract

In principle, contracts to which an umbrella clause is to apply would be between the disputing parties, that is, a state and a foreign investor. But in some cases the disputing parties and the parties to the contract on which the investor relies for the purposes of the umbrella clause are not identical. On the host state's side, the party to the contract may be a state entity or a territorial subdivision rather than the state itself. On the investor's side, the party to the contract may not be the foreign investor itself but its subsidiary in the host state. In these situations, the question arises whether an umbrella clause will protect a contract that is not directly between the host state and the investor.[333]

Noble Ventures v Romania[334] concerned a contract between the claimant and the Romanian 'State Ownership Fund', a separate legal entity. The Tribunal reached the conclusion that the contractual conduct of the Fund had to be attributed to the Romanian Government in view of the grant of governmental power to the Fund. The Tribunal found that, for the purposes of attribution, the distinction between commercial acts and sovereign acts had no relevance.[335] It followed that the umbrella clause was applicable to the contract. The Tribunal said:

> where the acts of a governmental agency are to be attributed to the State for the purposes of applying an umbrella clause, such as Art. II(2)(c) of the BIT, breaches of a contract into which the State has entered are capable of constituting a breach of international law *by virtue of the breach of the umbrella clause.*[336]

In a series of other decisions, tribunals found that the umbrella clause was inapplicable where the state had not contracted in its own name.[337] In *Impregilo v Pakistan*,[338] the contracts had been concluded not with Pakistan directly but with the Pakistan Water and Power Development Authority. The claimant wanted to benefit from an umbrella clause in a third country BIT by way of an MFN clause contained in the BIT between Italy and Pakistan. The Tribunal found that

[333] See N Gallus, 'An Umbrella just for Two? BIT Obligations Observance Clauses and the Parties to a Contract' (2008) 24 *Arbitration International* 157.

[334] *Noble Ventures v Romania*, Award, 12 October 2005.

[335] At para 82.

[336] At para 85. Emphasis in original.

[337] *Azurix v Argentina*, Award, 14 July 2006, paras 52, 384; *AMTO v Ukraine*, Award, 26 March 2008, paras 109–12; *EDF v Romania*, Award, 8 October 2009, paras 317, 318; *Hamester v Ghana*, Award, 18 June 2010, paras 339–50.

[338] *Impregilo v Pakistan*, Decision on Jurisdiction, 22 April 2005.

that the fundamental basis of the claim before them was the same as before the domestic courts[167]

CMS v Argentina[168] addressed the fork-in-the-road provision in the Argentina-US BIT. Argentina argued that the investor had taken the fork in the road since the local company, TGN, in which the investor held shares, had appealed a judicial decision to the Federal Supreme Court and had sought other administrative remedies.[169]

The Tribunal rejected Argentina's contention. It pointed out that the appeal had been taken by the local company TGN rather than by the foreign investor. Also, the steps taken consisted only of defensive and reactive actions. Most importantly, the subject matter in the domestic proceedings was not the same as the one in the ICSID arbitration. TGN's claims concerned the contractual arrangements under a licence while those of CMS concerned treaty rights.[170] The Tribunal said:

> 80. Decisions of several ICSID tribunals have held that as contractual claims are different from treaty claims, even if there had been or there currently was a recourse to the local courts for breach of contract, this would not have prevented submission of the treaty claims to arbitration. This Tribunal is persuaded that with even more reason this view applies to the instant dispute, since no submission has been made by CMS to local courts and since, even if TGN had done so—which is not the case—, this would not result in triggering the 'fork in the road' provision against CMS. Both the parties and the causes of action under separate instruments are different.

cc. An attempt at amicable settlement

A common condition in treaties providing for investor-state arbitration is that an amicable settlement must first be attempted through consultations or negotiations. This requirement is subject to certain time limits ranging from 3 to 12 months. If no settlement is reached within that period the claimant may proceed to arbitration. A typical waiting period under BITs would be six months. The NAFTA (Arts 1118–20) also prescribes a waiting period of six months after the events giving rise to the claim.[171] Article 26(2) of the ECT offers consent to arbitration if the dispute cannot be settled within three months from the date on which either party requested amicable settlement.[172] National legislation offering consent to arbitration may similarly provide for waiting periods.[173]

Argentina, Decision on Jurisdiction, 14 January 2004, paras 95–8; *Occidental v Ecuador*, Award, 1 July 2004, paras 37–63; *LG&E v Argentina*, Decision on Jurisdiction, 30 April 2004, paras 75, 76; *Champion Trading v Egypt*, Decision on Jurisdiction, 21 October 2003, sec 3.4.3; *Pan American v Argentina*, Decision on Preliminary Objections, 27 July 2006, paras 155–7; *Toto v Lebanon*, Decision on Jurisdiction, 11 September 2009, paras 203–17; *Victor Pey Casado v Chile*, Award, 8 May 2008, paras 467–98; *Total v Argentina*, Decision on Liability, 27 December 2010, paras 442–3.

167 *Pantechniki v Albania*, Award, 30 July 2009, paras 53–67.

168 *CMS v Argentina*, Decision on Jurisdiction, 17 July 2003, paras 77–82.

169 At para 77.

170 At paras 78–82.

171 *Metalclad v Mexico*, Award, 30 August 2000, paras 64–9.

172 *Petrobart v Kyrgyz Republic*, Award, 29 March 2005, sec VIII.7.

173 *Tradex v Albania*, Decision on Jurisdiction, 24 December 1996, 5 ICSID Reports 47, 60–1.

The reaction of tribunals to these provisions requiring an attempt at amicable settlement before the institution of arbitration has not been uniform.[174] In the majority of cases the tribunals found that the claimants had complied with these waiting periods before proceeding to arbitration.[175] In other cases the tribunals found that non-compliance with the waiting periods did not affect their jurisdiction.[176]

In *Biwater Gauff v Tanzania*, the UK-Tanzania BIT provided for a six-month period for settlement. There had been attempts to resolve the dispute but the six-month period had not yet elapsed when the Request for Arbitration was filed. The Tribunal held that this did not preclude it from proceeding. It said:

> this six-month period is procedural and directory in nature, rather than jurisdictional and mandatory. Its underlying purpose is to facilitate opportunities for amicable settlement. Its purpose is not to impede or obstruct arbitration proceedings, where such settlement is not possible. Non-compliance with the six month period, therefore, does not preclude this Arbitral Tribunal from proceeding. If it did so, the provision would have curious effects, including:
>
> - preventing the prosecution of a claim, and forcing the claimant to do nothing until six months have elapsed, even where further negotiations are obviously futile, or settlement obviously impossible for any reason;
> - forcing the claimant to recommence an arbitration started too soon, even if the six-month period has elapsed by the time the Arbitral Tribunal considers the matter.[177]

174 For the practice of the ICJ see *Military and Paramilitary Activities in and against Nicaragua (Nicaragua v United States)*, Judgment (Jurisdiction and Admissibility), 26 November 1984, ICJ Reports (1984) 427–9 and *Case Concerning Application of the International Convention on the Elimination of all forms of Racial Discrimination (Georgia v Russia)*, Judgment, 1 April 2011, paras 115–84.

175 *Salini v Morocco*, Decision on Jurisdiction, 23 July 2001, paras 15–23; *CMS v Argentina*, Decision on Jurisdiction, 17 July 2003, paras 121–3; *Generation Ukraine v Ukraine*, Award, 16 September 2003, paras 14.1–14.6; *Azurix v Argentina*, Decision on Jurisdiction, 8 December 2003, para 55; *Tokios Tokelés v Ukraine*, Decision on Jurisdiction, 29 April 2004, paras 101–7; *LG&E v Argentina*, Decision on Jurisdiction, 30 April 2004, para 80; *MTD v Chile*, Award, 25 May 2004, para 96; *Occidental v Ecuador*, Award, 1 July 2004, para 7; *Siemens v Argentina*, Decision on Jurisdiction, 3 August 2004, paras 163–73; *LESI—DIPENTA v Algérie*, Award, 10 January 2005, paras 32, 33; *AES Corp v Argentina*, Decision on Jurisdiction, 26 April 2005, paras 62–71; *Continental Casualty v Argentina*, Decision on Jurisdiction, 22 February 2006, para 6; *Berschader v Russia*, Award, 21 April 2006, paras 98–104; *El Paso v Argentina*, Decision on Jurisdiction, 27 April 2006, para 38; *Pan American v Argentina*, Decision on Preliminary Objections, 27 July 2006, paras 39, 41; *AMTO v Ukraine*, Award, 26 March 2008, paras 50, 53, 57–8; *Occidental v Ecuador*, Decision on Jurisdiction, 9 September 2008, paras 90–5; *AFT v Slovakia*, Award, 5 March 2011, paras 200–12.

176 In *Ethyl Corp v Canada*, Decision on Jurisdiction, 24 June 1998, paras 76–88, the Tribunal dismissed the objection based on the six-month provision since further negotiations would have been pointless. In *Lauder v Czech Republic*, Final Award, 3 September 2001, para 187, the Tribunal found that the waiting period of six months was not a jurisdictional provision. In *SGS v Pakistan*, Decision on Jurisdiction, 6 August 2003, para 184, the Tribunal found that the waiting period was procedural rather than jurisdictional and that negotiations would have been futile. Similarly in *Bayindir v Pakistan*, Decision on Jurisdiction, 14 November 2005, paras 88–103, the Tribunal found that a requirement to give notice of the dispute for the purpose of reaching a negotiated settlement was not a precondition for jurisdiction.

177 *Biwater Gauff v Tanzania*, Award, 24 July 2008, paras 338–50 at 343.

Other tribunals have reached the opposite conclusion.[178] In *Burlington Resources v Ecuador*, the BIT between Ecuador and the United States provided for consultation and negotiation in the event of a dispute. ICSID arbitration would become available six months after the dispute had arisen. The Tribunal found that the claimant had only informed the respondent of the dispute with its submission of the dispute to ICSID arbitration. It followed that the claim was inadmissible:

> by imposing upon investors an obligation to voice their disagreement at least six months prior to the submission of an investment dispute to arbitration, the Treaty effectively accords host States the right to be informed about the dispute at least six months before it is submitted to arbitration. The purpose of this right is to grant the host State an *opportunity* to redress the problem before the investor submits the dispute to arbitration. In this case, Claimant has deprived the host State of that opportunity. That suffices to defeat jurisdiction.[179]

It would seem that the decisive question is whether there was a promising opportunity for a settlement. There is little point in declining jurisdiction and sending the parties back to the negotiating table if negotiations are obviously futile. Even if the institution of arbitration was premature, the waiting period will often have expired by the time the tribunal is ready to make a decision on jurisdiction. Under these circumstances, declining jurisdiction and compelling the claimant to start the proceedings anew would be uneconomical. An alternative way to deal with non-compliance with a waiting period is a suspension of proceedings to allow additional time for negotiations if these appear promising.

(h) The applicability of MFN clauses to dispute settlement

An MFN clause contained in a treaty will extend the better treatment granted to a third state or its nationals to a beneficiary of the treaty.[180] Most BITs and some other treaties for the protection of investments[181] contain MFN clauses. Some of these MFN clauses will specify to which parts of the treaty they apply. For instance, the MFN clause may specify that it includes, or that it excludes, dispute settlement.[182] But most MFN clauses are worded in a general way and typically refer only to the treatment of investments.[183]

This has led to the question of whether the effect of MFN clauses extends to the provisions on dispute settlement in these treaties. Put differently, is it possible to

[178] *Goetz v Burundi*, Award, 10 February 1999, paras 90–3; *Enron v Argentina*, Decision on Jurisdiction, 14 January 2004, para 88; *Wintershall v Argentina*, Award, 8 December 2008, paras 133–57; *Murphy v Ecuador*, Award, 15 December 2010, paras 90–157.

[179] *Burlington Resources v Ecuador*, Decision on Jurisdiction, 2 June 2010, paras 312–18, 332–40 at para 315. Emphasis in original.

[180] See also R Dolzer and T Myers, 'After *Tecmed:* Most-Favored-Nation Clauses in Investment Protection Agreements' (2004) 19 *ICSID Review-FILJ* 49.

[181] See NAFTA, Art 1103; ECT, Art 10(7).

[182] The UK Model BIT confirms 'for the avoidance of doubt' that MFN treatment applies to a list of Articles that include the settlement of investor-state disputes. The BIT between Austria and Kazakhstan specifically includes dispute settlement in its MFN clause.

[183] Generally on MFN clauses, see Chapter VII.9.

avoid the conditions and limitations attached to consent to arbitration in a treaty by relying on an MFN clause in the treaty provided the respondent state has entered into a treaty with a third state that contains a consent clause without these conditions and limitations? Or even more radically, if the treaty containing the MFN clause does not offer consent to arbitration, is it possible to rely on consent to arbitration in a treaty of the respondent state with a third party?

In *Maffezini v Spain*[184] the consent clause in the Argentina-Spain BIT required resort to the host state's domestic courts for 18 months before the institution of arbitration. That BIT contained the following MFN clause: 'In all matters subject to this Agreement, this treatment shall not be less favorable than that extended by each Party to the investments made in its territory by investors of a third country.'

On the basis of that clause, the Argentinian claimant relied on the Chile-Spain BIT which does not contain the requirement to seek redress in the host state's courts for 18 months. The Tribunal undertook a detailed analysis of the applicability of MFN clauses to dispute settlement arrangements[185] and concluded:

> the most favored nation clause included in the Argentine-Spain BIT embraces the dispute settlement provisions of this treaty. . . . the Tribunal concludes that Claimant had the right to submit the instant dispute to arbitration without first accessing the Spanish courts.[186]

At the same time, the *Maffezini* Tribunal warned against exaggerated expectations attached to the operation of MFN clauses and distinguished between the legitimate extension of rights and benefits and disruptive treaty-shopping.[187] In particular, the MFN clause should not override public policy considerations that the contracting parties had in mind as fundamental conditions for their acceptance of the agreement.[188]

Subsequent decisions dealing with the application of MFN clauses to the requirement to seek a settlement in domestic courts for 18 months have mostly adopted the same solution.[189] The tribunals confirmed that the claimants were entitled to rely on the MFN clause in the applicable treaty to invoke the more favourable dispute settlement clause of another treaty that did not contain the 18-month rule.[190] At the same time these tribunals expressed their conviction that arbitration was an important part of the protection of foreign investors and that MFN clauses

[184] *Maffezini v Spain*, Decision on Jurisdiction, 25 January 2000.

[185] At paras 38–64.

[186] At para 64.

[187] At para 63.

[188] At para 62.

[189] For notable exceptions, see *Wintershall v Argentina*, Award, 8 December 2008, paras 158–97; *ICS Inspection v Argentina*, Award, 10 February 2012, paras 243–327.

[190] *Siemens v Argentina*, Decision on Jurisdiction, 3 August 2004, paras 94–110; *Gas Natural SDG, SA v Argentina*, Decision on Jurisdiction, 17 June 2005, paras 24–31, 41–9; *Suez, Sociedad General de Aguas de Barcelona SA, and InterAguas Servicios Integrales del Agua SA v Argentina*, Decision on Jurisdiction, 16 May 2006, paras 52–66; *National Grid plc v Argentina*, Decision on Jurisdiction, 20 June 2006, paras 53–94; *Suez, Sociedad General de Aguas de Barcelona SA, and Vivendi Universal SA v Argentina and AWG Group Ltd v Argentina*, Decision on Jurisdiction, 3 August 2006, paras 52–68; *Impregilo v Argentina*, Award, 21 June 2011, paras 51–109; *Hochtief v Argentina*, Decision on Jurisdiction, 24 October 2011.

In the absence of such an agreement, it provides for the application of the host state's law and international law:

Article 42

(1) 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.

Both the UNCITRAL Rules (Art 35(1)) and the ICC Rules (Art 21(1)) state that a tribunal will apply the law designated by the parties. If there is no choice of law clause, the UNCITRAL Rules refer to 'the law which it determines to be appropriate' and to 'any usage of trade applicable to the transaction' which the tribunal shall take into account (Art 35(3)). For ICC proceedings, its Rules provide in such a case that the Tribunal 'shall apply the rules of law which it determines to be appropriate' (Art 21(1)) and that the Tribunal 'shall take account of the provisions of the contract, if any, between the parties and of any relevant trade usages' (Art 21(2)). Many of the treaty provisions that offer investor-state arbitration, such as the NAFTA, the ECT, and some BITs, also contain provisions on applicable law. By taking up the offer of arbitration, the investor also accepts the choice of law clause contained in the treaty's dispute settlement provision. In this way, the treaty's provision on applicable law becomes part of the arbitration agreement. In other words, the clause on applicable law in the treaty becomes a choice of law agreed by the parties to the arbitration.[301]

Some clauses in treaties governing the applicable law in investment disputes refer exclusively to international law. For instance, Chapter 11, Section B of the NAFTA, dealing with the settlement of investor-state disputes, refers only to international law including the NAFTA itself:

Article 1131: Governing law

1. A Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law.[302]

Similarly, the ECT's provision on investor-state dispute settlement provides:

Article 26 Settlement of disputes between an investor and a contracting party

...

(6) A tribunal established under paragraph (4) shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law.[303]

[301] A R Parra, 'Provisions on the Settlement of Investment Disputes in Modern Investment Laws, Bilateral Investment Treaties and Multilateral Instruments on Investment' (1997) 12 *ICSID Review-FILJ* 287, 332; P Peters, 'Dispute Settlement Arrangements in Investment Treaties' (1991) 22 *Netherlands Yearbook of Int'l L* 91, 147–8 (1991); I F I Shihata and A R Parra, 'The Experience of the International Centre for Settlement of Investment Disputes' (1999) 14 *ICSID Review-FILJ* 299, 336. See also the analysis in *Antoine Goetz v Burundi*, Award, 10 February 1999, para 94 and in *Siemens v Argentina*, Award, 6 February 2007, para 76.

[302] 32 ILM 605, 645 (1993).

[303] 34 ILM 360, 400 (1995).

A number of BITs also merely refer to international law including the substantive rules of the BIT itself.[304]

Other BITs, in provisions dealing with applicable law, combine the host state's domestic law with international law. A frequently used formula lists: (a) the host state's law; (b) the BIT itself as well as other treaties; (c) any contract relating to the investment; and (d) general international law. In *Antoine Goetz v Burundi*[305] the relevant Belgium-Burundi BIT contained a provision on applicable law of this type. The Tribunal found that it had to apply a combination of domestic law and international law.[306] The Tribunal made the following general statement:

> a complementary relationship must be allowed to prevail. That the Tribunal must apply Burundian law is beyond doubt, since this last is also cited in the first place by the relevant provision of the Belgium-Burundi investment treaty. As regards international law, its application is obligatory for two reasons. First, because, according to the indications furnished to the Tribunal by the claimants, Burundian law seems to incorporate international law and thus to render it directly applicable; . . . Furthermore, because the Republic of Burundi is bound by the international law obligations which it freely assumed under the Treaty for the protection of investments . . .[307]

The Tribunal then stated that an application of international law and of domestic law might lead to different results. The Tribunal first undertook an analysis of the dispute from the perspective of the law of Burundi. This analysis led to the conclusion that under the law of Burundi the actions in question were legal.[308] The Tribunal then examined the same issue from the perspective of international law, in particular in light of the BIT. This examination led to the result that the legality of the measures taken by Burundi depended on the payment of adequate and effective compensation which was still outstanding.[309]

A slightly different provision on applicable law that combines host state law and international law may be found in the BIT between Argentina and Spain:

> The Arbitral Tribunal shall decide the dispute in accordance with the provisions of this Agreement, the terms of other Agreements concluded between the parties, the law of the Contracting Party in whose territory the investment was made, including its rules on conflict of laws, and general principles of international law.[310]

That treaty provision was applicable in *Maffezini v Spain*[311] where the subject of the dispute was the construction of a chemical plant. The Tribunal did not enter into a theoretical discussion on the law applicable to the case before it; it applied

[304] For a detailed list of examples, see E Gaillard and Y Banifatemi, 'The Meaning of "and" in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process' (2003) 18 *ICSID Review-FILJ* 375, 377.

[305] *Antoine Goetz v Burundi*, Award, 10 February 1999.

[306] At para 95.

[307] At para 98.

[308] At paras 100–19.

[309] At paras 120–33.

[310] Argentina-Spain BIT, Art 10(5).

[311] *Maffezini v Spain*, Award, 13 November 2000.

international law to some questions and host state law to other questions. For instance, on the issue of whether Spain was responsible for the actions of a state entity the Tribunal relied on the international law of state responsibility for the question of attribution[312] and on the Spanish Law on Public Administration and Common Administrative Procedure to elucidate the structure and functions of the entity.[313] Having reached an affirmative reply on attribution, it then applied the BIT.[314] On the issue of an environmental impact assessment, the Tribunal applied international law,[315] Spanish legislation,[316] a European Community directive,[317] and the BIT.[318] To the question of whether a contract had been perfected between the investor and the state entity, the Tribunal applied the Spanish Civil Code and the Spanish Commercial Code together with authoritative commentaries.[319] On the issue of a statute of limitation under Spanish legislation, the Tribunal found that it did not apply to claims filed under the ICSID Convention.[320]

Not all BITs contain provisions on applicable law. Where jurisdiction is based on a BIT that does not contain a provision on governing law, tribunals have sometimes construed such a choice from the BIT's invocation.

In *AAPL v Sri Lanka*,[321] jurisdiction was based on the BIT between Sri Lanka and the United Kingdom. This BIT did not contain a provision on applicable law. The Tribunal found that by arguing their case on the basis of the BIT, the parties had expressed their choice of the BIT as the applicable law as 'both Parties acted in a manner that demonstrates their mutual agreement to consider the provisions of the Sri Lanka/UK Bilateral Investment Treaty as being the primary source of the applicable legal rules'.[322]

The Tribunal in *AAPL v Sri Lanka* went on to state that the BIT was not a closed legal system but had to be seen in a wider juridical context. This wider juridical context, as well as the parties' submissions, led it to apply customary international law as well as domestic law.[323] Other tribunals have similarly found that in cases involving disputes under BITs the primary source of law had to be the BIT itself and other rules of international law.[324]

In the absence of an agreement on the governing law, Article 42 of the ICSID Convention provides that the tribunal apply host state law and applicable rules of international law. Most tribunals applying this provision examined the issues before

[312] At paras 50, 52, 57, 77, 83. [313] At paras 47–9. [314] At para 83.
[315] At para 67. [316] At paras 68, 69. [317] At para 69.
[318] At para 71. [319] At paras 89, 90.
[320] At paras 92, 93. For a similar methodology on applicable law, see also *BG Group v Argentina*, Final Award, 24 December 2007, paras 89–103; *National Grid v Argentina*, Award, 3 November 2008, paras 81–90.
[321] *AAPL v Sri Lanka*, Award, 27 June 1990.
[322] At para 20.
[323] At paras 18–24.
[324] *Wena Hotels v Egypt*, Award, 8 December 2000, paras 78, 79; *ADC v Hungary*, Award, 2 October 2006, paras 288–91; *LG&E v Argentina*, Decision on Liability, 3 October 2006, paras 85, 97–8; *Saipem v Bangladesh*, Award, 30 June 2009, para 99; *Bayindir v Pakistan*, Award, 27 August 2009, paras 109, 110.

them under both systems of law.[325] In some cases the tribunals were simply content to find that both systems of law reached the same result.[326]

A widely held theory on the relationship of international law to host state law under the second sentence of Article 42(1) is the doctrine of the supplemental and corrective function of international law vis-à-vis domestic law.[327] The ad hoc Committee in *Amco v Indonesia* described this doctrine as follows:

> Article 42(1) of the Convention authorizes an ICSID tribunal to apply rules of international law only to fill up lacunae in the applicable domestic law and to ensure precedence to international law norms where the rules of the applicable domestic law are in collision with such norms.[328]

It is questionable whether this doctrine accurately reflects reality. Tribunals have given international law more than a mere ancillary or subsidiary role. The Tribunal in the resubmitted case of *Amco v Indonesia* called this a distinction without a difference:

> 40. This Tribunal notes that Article 42(1) refers to the application of host-state law and international law. If there are no relevant host-state laws on a particular matter, a search must be made for the relevant international laws. And, where there are applicable host-state laws, they must be checked against international laws, which will prevail in case of conflict. Thus international law is fully applicable and to classify its role as 'only' 'supplemental and corrective' seems a distinction without a difference.[329]

Under the residual rule of Article 42(1) of the ICSID Convention both legal systems, that is international law and host state law, have a role to play.[330] In *CMS v Argentina* the Tribunal said:

> there is here a close interaction between the legislation and the regulations governing the gas privatization, the License and international law, as embodied both in the Treaty and in

[325] But see *SOABI v Senegal*, Award, 25 February 1988, paras 5.02 et seq where the Tribunal restricted itself to the application of Senegalese law.

[326] *Adriano Gardella v Côte d'Ivoire*, Award, 29 August 1977, para 4.3; *Benvenuti & Bonfant v Congo*, Award, 15 August 1980, para 4.64; *Klöckner v Cameroon*, Award, 21 October 1983, 2 ICSID Reports 9, at p 63; *Amco v Indonesia*, Award, 20 November 1984, paras 147–8, 188, 201, 245–50, 265–8, 281; *Duke Energy v Peru*, Award, 18 August 2008, paras 144–61; *Aguaytia v Peru*, Award, 11 December 2008, paras 71–4.

[327] *Klöckner v Cameroon*, Decision on Annulment, 3 May 1985, para 69; *LETCO v Liberia*, Award, 31 March 1986, 2 ICSID Reports 343, at 358–9; *Amco v Indonesia*, Resubmitted Case: Award, 5 June 1990, para 38; *SPP v Egypt*, Award, 20 May 1992, para 84; *Autopista v Venezuela*, Award, 23 September 2003, paras 101–5.

[328] *Amco v Indonesia*, Decision on Annulment, 16 May 1986, para 20.

[329] *Amco v Indonesia*, Resubmitted Case: Award, 5 June 1990, para 40.

[330] See E Gaillard and Y Banifatemi, 'The Meaning of "and" in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process' (2003) 18 *ICSID Review-FILJ* 375, 403–11; R Dolzer, 'Contemporary Law of Foreign Investment: Revisiting the Status of International Law' in C Binder, U Kriebaum, A Reinisch, and S Wittich (eds), *International Investment Law for the 21st Century* (2009) 818; Z Douglas, *The International Law of Investment Claims* (2009) 39–133.

customary international law. All of these rules are inseparable and will, to the extent justified, be applied by the Tribunal.[331]

It is only where there is a conflict between the host state's law and international law that a tribunal has to make a decision on precedence. The Tribunal in *LG&E v Argentina* emphasized that ultimately international law is controlling: 'International law overrides domestic law when there is a contradiction since a State cannot justify non-compliance of its international obligations by asserting the provisions of its domestic law.'[332]

In non-ICSID arbitration between investors and host states, tribunals also apply a combination of international law and host state law. The UNCITRAL Arbitration Rules refer the tribunal to the law designated by the parties. In the absence of a choice of law, the tribunal is to apply the law which it determines to be appropriate.[333]

In *Occidental v Ecuador* the arbitration was conducted under the UNCITRAL Rules of 1976. The Tribunal listed a mix of sources of law under host state law and under international law:

> The dispute in the present case is related to various sources of applicable law. It is first related to the Contract . . . ; it is next related to Ecuadorian tax legislation; this is followed by specific Decisions adopted by the Andean Community and issues that arise under the law of the WTO. In particular the dispute is related to the rights and obligations of the parties under the Treaty [ie the US-Ecuador BIT] and international law.[334]

Therefore, in most cases the applicable substantive law in investment arbitration combines international law and host state law. This is so whether or not the parties have made a choice of law that combines international law with host state law. In the majority of cases tribunals have, in fact, applied both systems of law. Where there was a contradiction between the two, international law had to prevail. It is left to the tribunals to identify the various issues before them to which international law or host state law is to apply.

(l) Remedies

aa. Restitution and satisfaction

Under the international law of state responsibility, reparation for a wrongful act takes the form of restitution, compensation, or satisfaction.[335] In investment

[331] *CMS v Argentina*, Award, 12 May 2005, para 117. See also *Wena v Egypt*, Decision on Annulment, 5 February 2002, paras 37–40; *Azurix v Argentina*, Award, 14 July 2006, para 67; *LG&E v Argentina*, Decision on Liability, 3 October 2006, paras 82–99; *Enron v Argentina*, Award, 22 May 2007, paras 203–9; *Tokios Tokelės v Ukraine*, Award, 26 July 2007, paras 138–45; *Sempra v Argentina*, Award, 28 September 2007, paras 231–40.

[332] *LG&E v Argentina*, Decision on Liability, 3 October 2006, para 94. See also *CDSE v Costa Rica*, Award, 17 February 2000, paras 64, 65; *Duke Energy v Peru*, Decision on Jurisdiction, 1 February 2006, para 162.

[333] UNCITRAL Arbitration Rules 2010, Art 35(1).

[334] *Occidental v Ecuador*, Final Award, 1 July 2004, para 93. See also *Eastern Sugar v Czech Republic*, Partial Award, 27 March 2007, paras 191–7.

[335] Articles on Responsibility of States for Internationally Wrongful Acts adopted by the ILC in 2001, Art 34. J Crawford, *The International Law Commission's Articles on State Responsibility* (2002) 211.

the case-law elaborated by international arbitral tribunals strongly suggests that in assessing the liability due for losses incurred the interest becomes an integral part of the compensation itself, and should run consequently from the date when the State's international responsibility became engaged[363]

In the case of compensation, interest is normally due from the date of the expropriation, although that date may be difficult to determine with indirect or creeping expropriations. The appropriate date will be the day when the investor definitely lost control over the investment.

The rate of interest may be calculated on the basis of the legal interest rate in an applicable legal system or on an inter-bank rate such as the London Interbank Offered Rate (LIBOR).[364]

The practice of tribunals shows a trend towards compounding interest, that is, interest is capitalized at certain intervals and will then itself bear interest. While some tribunals have rejected compound interest,[365] it has been accepted in the majority of recent decisions.[366]

(m) Costs

The costs of major investment arbitrations can be considerable and may run into millions of dollars for complex cases.[367] The costs consist of three elements: the charges for the use of the facilities and expenses of ICSID[368] or other arbitration institution, the fees and expenses of the arbitrators, and the expenses incurred by

[363] *AAPL v Sri Lanka*, Award, 27 June 1990, para 114. See also *SPP v Egypt*, Award, 20 May 1992, para 234; *Metalclad Corp v United Mexican States*, Award, 30 August 2000, para 128.

[364] *PSEG v Turkey*, Award, 19 January 2007, para 348; *Sempra v Argentina*, Award, 28 September 2007, paras 483–6; *Rumeli Telekom v Kazakhstan*, Award, 29 July 2008, para 818; *National Grid v Argentina*, Award, 3 November 2008, para 291; *Siag v Egypt*, Award, 1 June 2009, paras 594–8.

[365] *CME v Czech Republic*, Final Award, 14 March 2003, paras 642–7; *Autopista v Venezuela*, Award, 23 September 2003, paras 393–7; *Eastern Sugar v Czech Republic*, Partial Award, 27 March 2007, para 374; *Duke Energy v Ecuador*, Award, 18 August 2008, para 473.

[366] *Atlantic Triton v Guinea*, Award, 21 April 1986, 3 ICSID Reports 13, at 33, 43; *Compania del Desarrollo de Santa Elena SA v Costa Rica*, Award, 17 February 2000, paras 104, 105; *Metalclad v Mexico*, Award, 30 August 2000, para 128; *Maffezini v Spain*, Award, 13 November 2000, para 96; *Wena Hotels v Egypt*, Award, 8 December 2000, para 129; *Middle East Cement v Egypt*, Award, 12 April 2002, para 174; *Pope & Talbot v Canada*, Award in Respect of Damages, 31 May 2002, para 90; *Tecmed v United Mexican States*, Award, 29 May 2003, para 196; *MTD v Chile*, Award, 25 May 2004, para 253(4); *Azurix v Argentina*, Award, 14 July 2006, paras 439–40; *ADC v Hungary*, Award, 2 October 2006, para 522; *PSEG v Turkey*, Award, 19 January 2007, para 348; *Enron v Argentina*, Award, 22 May, 2007, paras 451–2; *Compañía de Aguas del Aconquija, SA & Vivendi Universal v Argentina*, Award, 20 August 2007, paras 9.1.1–9.2.8; *BG Group v Argentina*, Final Award, 24 December 2007, paras 456–7; *Sempra v Argentina*, Award, 28 September 2007, paras 483–6; *OKO Pankki v Estonia*, Award, 19 November 2007, paras 343–56; *Continental Casualty v Argentina*, Award, 5 September 2008, paras 306–16; *Funnekotter v Zimbabwe*, Award, 22 April 2009, paras 141–6; *Siag v Egypt*, Award, 1 June 2009, paras 594–8; *Impregilo v Argentina*, Award, 21 June 2011, paras 382–4.

[367] Eg in *PSEG v Turkey*, the total amount of costs claimed was US$20,851,636.62. See Award, 19 January 2007, para 352. The Award in *Libananco v Turkey*, 2 September 2011, paras 558–9, seems to have set a record with combined costs for both parties at US$60 million.

[368] The details are set out in ICSID's Administrative and Financial Regulations at <http://www.worldbank.org/icsid/basicdoc/partC.htm> as well as in a Schedule of Fees at <http://www.worldbank.org/icsid/schedule/fees.pdfsee>.