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International and Domestic Law in Investment Disputes. The Case of ICSID

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1. Introduction

Investment relationships typically involve domestic law as well as international law. The host State's domestic law regulates a multitude of technical questions such as admission, licensing, labour relations, tax, foreign exchange and real estate. International law is relevant for such questions as the international minimum standard for the treatment of aliens, protection of foreign owned property, especially against illegal expropriations, interpretation of applicable treaties, especially bilateral investment treaties, State responsibility and, possibly, human rights. The dispute over the application of national or international standards with regard to the compensation of expropriated foreign owned property was one of the core issues in the debate surrounding the so-called new international economic order in the 1970s.[1]

The Convention on the Settlement of Investment Disputes between States and Nationals of Other States of March 18, 1965[2] is designed to provide a procedural framework for the settlement of investment disputes between host States and foreign investors. A settlement is to be achieved through either conciliation or arbitration. In most cases that have arisen to date, the parties have chosen arbitration. The Convention does not provide substantive rules for the resolution of investment disputes, but it does contain an Article on the law that an arbitral tribunal should apply to a dispute. Art. 42 provides:

[1] See esp. Art. 2(2)(c) of the Charter of Economic Rights and Duties of States. UNGA Res. 3281 (XXIX) of 12 Dec. 1974.

[2] In force: October 14, 1966. 4 ILM 532 (1965); öBGBl. 1971/357.

> (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.
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> (2) The Tribunal may not bring in a finding of *non liquet* on the ground of silence or obscurity of the law.
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> (3) The provisions of paragraphs (1) and (2) shall not prejudice the power of the Tribunal to decide a dispute *ex aequo et bono* if the parties so agree.

This provision is designed to combine flexibility, by granting maximum autonomy to the parties in choosing applicable rules, ensuring that the tribunal will find appropriate rules even in the absence of such a choice. The aim of flexibility is served by the first sentence of para. (1) on agreement by the parties and by para. (3) extending party autonomy to equitable principles.[3] The aim of certainty is served by the second sentence of para. (1), designating the host State's law in conjunction with international law as the applicable law in the absence of agreement, and by para. (2) prohibiting a finding of *non liquet* by the tribunal.

Art. 42 of the ICSID Convention only applies to the substantive law. It does not apply to questions of procedure or jurisdiction. The Convention and a set of Arbitration Rules adopted by ICSID's Administrative Council[4] regulate exhaustively the procedure of ICSID tribunals. Jurisdictional questions must be answered in conformity with the Convention's overall object and purpose in the light of general principles.[5]

A municipal court having to decide which system of law is applicable to a dispute is guided by the *lex fori*'s rules of private international law. Art. 42 is designed to give guidance to the ICSID tribunal in choosing the proper law. The tribunal's first task is to ascertain whether the parties have chosen a system of law or individual rules of law (Art. 42(1) first sentence). This choice may extend beyond legal rules *stricto sensu* to principles of equitable justice (Art. 42(3)). Only after determining that no agreement concerning applicable rules of law exists, may the tribunal resort to the residual rule refer to the law of the host State and to international law (Art. 42(1), second sentence). This method should provide the tribunal with sufficient authority to resolve

[3] On para. 3 of Art. 42 see *Schreuer*, Decisions *ex aequo et bono* under the ICSID Convention, 11 ICSID Review – Foreign Investment Law Journal 36 (1996).

[4] The most recent version of the Arbitration Rules is reproduced in 1 ICSID Reports 157.

[5] See esp. *SPP* v. *Egypt*, Decision on Jurisdiction, 14 April 1988, 3 ICSID Reports 140–143, 170, 177, 186.