

Global Reflections on
**International Law,
Commerce and
Dispute Resolution**

Liber Amicorum in honour of Robert Briner

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Investment Arbitration under the ICSID Convention and BITs

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I. Introduction

Measures of investment protection have developed over the years in various forms and based on various legal sources. Also, the scope of such measures has evolved with the passing of time. At national level, States wishing to attract foreign investment have enacted investment laws offering certain incentives and assurances,¹ while industrialized States have established insurance systems to cover the risks incurred by their nationals' investments abroad.² At international level, the protection of foreign investments in the nineteen sixties relied essentially on the diplomatic protection afforded by each State to its own nationals.³ Attempts to introduce multilateral conventions in the field, such as the OECD's 1962 Draft Convention on the Protection of Foreign Property, revised and reissued in 1967, failed to obtain sufficient support.⁴

The most significant product of the 1960s in this field was the 1965 Washington Convention on the Settlement of Investment Disputes between States and Nationals of other States (the ICSID Convention).⁵ Sponsored by the World Bank, this Convention has established a legal framework for the settlement of investment disputes through an arbitration process administered by the International Centre for Settlement of Investment Disputes ('ICSID'). Under the ICSID Convention the private investor has *locus standi* to sue the State for breach of its obligations under the investment contract containing an ICSID clause or under the treaty on which ICSID jurisdiction is founded.

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1 e.g. the *codes des investissements* of African States, formerly French colonies.

2 e.g. OPIC in the USA, HERMES in Germany, the Export Credit Guarantee Department in the UK, COFACE in France and SACE in Italy.

3 As diplomatic protection depends very much on the political relations between the two States involved, this has often led to the private party's claims being ignored or the dispute being politicized.

4 The current OECD initiative for a Multilateral Agreement on Investment is meant to provide a comprehensive framework for investment.

5 In March 2005, the number of Contracting States to the ICSID Convention stood at 142.

The most important characteristic of the ICSID Convention is that it creates a self-sufficient legal framework, independent of all other legal systems, national or international. Under the Convention, a private investor may bring a claim against the host State without the assistance of its own State, while enjoying equal treatment in the proceedings.⁶

Although the ICSID Convention has helped to depoliticize investment disputes, it has given rise to a certain number of problems traditionally associated with arbitrations involving States. The first of these—characteristic of legal systems derived from the Napoleonic code—is the capacity of a State or a State-owned entity to validly stipulate an arbitration clause.⁷ A development has however occurred here with the recognition that, since State immunity can be waived explicitly or implicitly, whenever a State voluntarily accepts an arbitration clause in a contract it may be deemed to have waived its immunity from jurisdiction. The ICSID Convention removes any residual doubts by providing that: 'When the parties have given their consent, no party may withdraw its consent unilaterally.' (Article 25(1))

Another critical issue is the choice of the applicable law. In the nineteen sixties and seventies, States' insistence on the application of their own laws was confronted with requests by foreign investors' to denationalize the contract by making it subject to a-national rules of law. Article 42(1) of the ICSID Convention strikes a fair balance between these opposite positions by putting the emphasis first on the parties' choice, failing which both the host State's law and international law will be applicable.⁸

Enforcement of an award against a State has always been a crucial aspect of investment arbitration. The ICSID Convention provides a fundamental rule in this respect by establishing that each Contracting State must recognize an award as binding and enforce the pecuniary obligations arising from it as if it were a final judgment of a court in that State.⁹ Of course, State immunity from execution

6 A. Broches, 'Bilateral Investment Protection Treaties and Arbitration of Investment Disputes' in *The Art of Arbitration: Essays on International Arbitration, Liber Amicorum Pieter Sanders* (Deventer: Kluwer Law & Taxation, 1982) 63 at 64.

7 The capacity of States and State-owned entities to conclude arbitration agreements was recognized in the 1961 Geneva Convention on International Commercial Arbitration (Article 11) but is excluded or made subject to special authorization in certain countries such as Saudi Arabia and Iran.

8 Article 42(1) provides as follows: '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.'

9 ICSID Convention, Article 54(1).

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poses a threat to the foreign investor's ability to recover the amount of the award from its sovereign partner, but the shift from absolute to relative State immunity from execution has reduced the size of this threat. Although the ICSID Convention does not provide a direct answer to this problem,¹⁰ the climate of cooperation it has helped to establish, combined with the World Bank's role in extending financial assistance to States willing to respect their international commitments,¹¹ encourages the spontaneous performance of Convention awards. It may be added that a State's failure to comply with an ICSID award will make it liable towards the investor's State for breach of treaty.

A second important instrument for foreign investment protection created under the auspices of the World Bank is the Convention Establishing the Multilateral Investment Guarantee Agency (the MIGA Convention), adopted in October 1985.¹² This Convention allows eligible investors to insure their investments not only against traditional risks relating to currency transfers, expropriation and like measures, war and civil disturbances, but also against the risk of a change in the law or a breach of contract by the host State. This may include a refusal to renegotiate in good faith the terms of the contract in accordance with the agreed method of consultation. Practical experience has shown that the risk of a change in the State's attitude during performance of the contract may be significantly mitigated by allowing the terms of the contract to be renegotiated if circumstances (such as a change in the law affecting the private investor's economic position) warrant this.¹³

During the last two decades, the number of international instruments dealing with investment—both bilateral and multilateral—has rocketed. The most striking development has been the emergence of bilateral investment treaties (BITs). Since the first BIT was concluded in the late 1950s,¹⁴ the spread of this instrument for protecting foreign investments has been growing incessantly, as evidenced by the figure of over 2,200 BITs concluded at the end of 2004 between States throughout the world.¹⁵ It is recognized that BITs have substantially contributed to giving certainty to the legal framework of many newly independent States in the field of foreign investment.

10 Article 54(3) of the Convention states: 'Execution of the award shall be governed by the laws concerning execution of judgments in force in the State in whose territories such execution is sought.'

11 As in the case of an award made under the ICSID Convention against the host State.

12 On 31 December 2003, the number of Contracting States to the MIGA Convention stood at 164.

13 P. Bernardini, 'The Renegotiation of the Investment Contract' (1998) 13 ICSID Rev. 411.

14 Between the Federal Republic of Germany and Pakistan on 25 November 1959; see R. Dolzer & M. Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff, 1995) at 1.

15 Source: World Bank's World Development Report for 2005, *A Better Investment Climate for Everyone* (2004) at 175.

It is beyond the scope of this paper to investigate the reasons for this extraordinary development. Through the widespread network of multilateral and bilateral treaties so established, customary rules of public international law have been confirmed or new rules have taken shape, improving the legal framework of investment protection.¹⁶ Accepted by developing countries, these new rules have helped to put aside the strong criticism expressed by such countries in the 1960s and 1970s over, amongst other things, the criteria for assessing compensation in the event of nationalization or expropriation (which, in their view, should be based on State law) and the competent forum for deciding disputes relating thereto (which, in their view, should be a national court). The critical position taken by developing countries towards the traditional principles of public international law—considered to be an expression of the ‘old international economic order’—has been affirmed in a number of United Nations General Assembly resolutions.¹⁷ Foreign investment flows have been fostered by this new legal framework, as well as by providing for international arbitration as the means of settling investment disputes in all BITS and a number of multilateral conventions. Most BITS allow investors to choose between ICSID arbitration (including the ICSID Additional Facility), the ICC Rules of Arbitration and *ad hoc* arbitration under UNCITRAL Arbitration Rules. This paper, dedicated to an eminent personality of the world of international arbitration, will focus on the most important respects in which BITS play a complementary role with respect to the ICSID Convention.

II. Interaction between the ICSID Convention and BITS

The extraordinary development of BITS has gradually brought new problems to the surface, which have not failed to attract the interest of practitioners of international arbitration in the field of investments and State contracts. As a result of this development, BITS have been increasingly prominent in the application of the ICSID Convention.¹⁸

16 S. Hindelang, ‘Bilateral Investment Treaties, Custom and a Healthy Investment Climate—The Question of Whether BITS Influence Customary International Law Revisited’ (2004) 5 *The Journal of World Investment and Trade* 789. Also, the formulation of the World Bank Group Guidelines on the Treatment of Foreign Direct Investment, published in September 1992 (ICSID Rev. 295), has been influenced by the development of BITS; see R. Dolzer & M. Stevens, *supra* note 14 at xii.

17 e.g. those concerning permanent sovereignty over natural resources (14 December 1962 and 25 November 1966), a new economic order (1 May 1974), or the economic rights and duties of States (12 December 1974).

18 On 1 December 2004, 106 out of a total of 171 ICSID cases were instituted on the basis of BITS. Other ICSID cases have been instituted on the basis of multilateral investment conventions.

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According to Article 25(1) of the ICSID Convention, ICSID jurisdiction extends to 'any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of the Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre'. As has been authoritatively stated, '[t]his Article defines the outer limits within which parties can put its [i.e. the Convention's] mechanisms into operation'.¹⁹

BITs may be said to have a complementary role in relation to certain key provisions in the ICSID Convention. Four issues are concerned:

1. the existence of 'consent';
2. the presence of 'an investment' out of which the dispute arises;
3. the presence, as party to a dispute with a Contracting State, of 'a national of another Contracting State';
4. the applicable law.

1. 'Consent'

Parties traditionally express their consent to international arbitration by including in their contract an arbitration clause providing for the settlement of disputes arising under or in connection with the contract. However, the relations established by the investment of a private party in the host State's territory do not always originate in a contract with the State. More and more investments are made on the basis of contractual arrangements with State-owned entities (rather than States) or even without a specific contract at all. This is the case, for example, of investments made on the basis of a local law promoting and regulating foreign investments, pursuant to which the foreign party's investment is approved by the competent authority and its object and amount are officially recorded.

The parties' consent under the ICSID Convention has been described as the 'cornerstone' of ICSID jurisdiction.²⁰ Consent must exist when ICSID is seized, but the Convention does not indicate at what moment the consent should be given. Likewise, the Convention does not specify whether the parties' consent should be expressed in a single instrument (such as an investment contract) or may be expressed in separate instruments at different times. The only explicit requirement is that consent must be 'in writing'.

¹⁹ A. Broches, *supra* note 6 at 67.

²⁰ Report of the Executive Directors on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (IBRD, 18 March 1965) (hereinafter 'Directors' Report') at para. 23.

a) *The State's offer*

In keeping with this flexibility, the Directors' Report indicates that a host State might offer to submit disputes arising out of certain kinds of investment to ICSID jurisdiction in its investment promotion legislation, and that the investor might give its consent by accepting this offer in writing.²¹ In this case, consent by the investor may be expressed either at the outset, when filing an application in accordance with the State's investment promotion legislation,²² or after a dispute has arisen, by initiating arbitration on the basis of the legislative provision offering this method of dispute settlement.

The State's consent may be likewise expressed in an offer of arbitration contained in an international treaty concluded with the investor's national State. BITs come into play here and provide a legal basis for consent to arbitration in the absence of a contractual relationship between the private investor and the host State and an arbitration clause binding the two parties.²³

While early BITs generally provide for *ad hoc* arbitration, those made after the entry into force of the ICSID Convention in 1966 have increasingly included a reference to ICSID arbitration, either exclusively or alongside other alternative forms of arbitration (usually under the UNCITRAL Arbitration Rules or the ICC Rules of Arbitration or, less frequently, the Rules of the Arbitration Institute of the Stockholm Chamber of Commerce).²⁴ Once again, such references allow foreign investors to resort to investment arbitration 'without aid or intervention of his national State'.²⁵

21 *Ibid.* at para. 24. The first ICSID case to be based on domestic investment promotion legislation was *SPP v. Arab Republic of Egypt*: the decision of 14 April 1988, confirming ICSID jurisdiction, was based on Egyptian law no. 43 of 1974, (1991) XVI Y.B. Comm. Arb. 28.

22 Early acceptance by the investor of the State's offer will avoid the risk of the legislation containing the offer being repealed or amended.

23 J. Paulsson, 'Arbitration Without Privity' (1995) ICSID Rev. 232. Multilateral treaties providing for a similar basis for consent under the ICSID Convention are the 1992 North American Free Trade Agreement (NAFTA), the 1994 Energy Charter Treaty, the 1994 Colonia and Buenos Aires investment protocols relating to the common market of South America (MERCOSUR) and the 1994 Cartagena Free Trade Agreement.

24 Given the rather limited spread of BITs at the time, the Directors' Report contemplated only the State's offer of arbitration in investment promotion legislation.

25 A. Broches, *supra* at 64. To produce this effect, a BIT must have come into force as an instrument of public international law. In *Ceskoslovenska Obchodni Banka, A.S. v. Slovak Republic*, the Tribunal held that the jurisdiction of ICSID and the Tribunal was based on the parties' incorporation by reference in their contract of the Czech/Slovak BIT even though the entry into force of the treaty was disputed (decision on jurisdiction, 24 May 1999, (1999) 14 ICSID Rev. 251).

In order to determine whether the consent requirement under the ICSID Convention is satisfied, the specific provisions of BITs in which reference is made to arbitration must be examined. This can only be done on an individual basis, as not all BITs contain an irrevocable offer by the State to have recourse to international arbitration—be it ICSID or another—for settling disputes with foreign investors.

Few BITs provide that disputes shall be submitted to international arbitration only if the parties so agree.²⁶ Some BITs provide that the State shall give its consent in the event of a request by the foreign investor to submit a dispute to ICSID arbitration.²⁷ In all these cases there is no irrevocable offer by the State that the investor could accept to satisfy the requirement for consent under the ICSID Convention.²⁸

A State's consent to ICSID jurisdiction may be found to exist, even in the absence of any provision to that effect in the BIT between that State and the investor's State, if the BIT contains a most-favoured nation clause extending to provisions on the settlement of disputes. If the host State has consented to ICSID jurisdiction in another BIT, the investor under the first-mentioned BIT is entitled to rely on the more favourable treatment so accorded by the same State to investors under another BIT.²⁹

Most recent BITs set out explicitly the State's consent to resort to ICSID arbitration, as is the case in the UK BITs, the relevant provision of which leaves no room to doubt the existence of the State's consent:

Each Contracting Party hereby consents to submit to the International Centre for the Settlement of Investment Disputes . . . for settlement by . . . arbitration . . . any legal dispute arising between the Contracting Party and a national or company of the other Contracting Party concerning an investment of the latter in the territory of the former.³⁰

²⁶ One treaty that does is the 1991 Canada-Hungary BIT (Article IX(2)); see A.R. Parra, 'Provisions on the Settlement of Investment Disputes in Modern Investment Laws, Bilateral Investment Treaties and Multilateral Investment Instruments' (1997) 12 ICSID Rev. 287 at 322.

²⁷ e.g. the 1992 Japan-Turkey BIT (Article 11(1)); *ibid.* at 322-23.

²⁸ For a detailed analysis of such provisions in BITs see A. Broches, *supra* note 6 at 64-67; by R. Dolzer & M. Stevens, *supra* note 14 at 132-134; C.H. Schreuer, *The ICSID Convention: A Commentary* (Cambridge University Press, 2001) at 210-21.

²⁹ As in some BITs concluded by the United Kingdom; see the Tribunal's analysis in *Emilio Agustín Maffezini v. Kingdom of Spain*, (2001) ICSID Rev. at paras 52-56.

³⁰ Initial wording of Article 8(1) of the 1980 UK/Sri Lanka BIT, on the basis of which the first ICSID arbitration founded on a BIT was initiated. Similar language may be found in the US/Uruguay of 25 October 2004, <www.ustr.gov>.

The host State's consent to ICSID jurisdiction under BITs is regarded as the same type of offer to refer investment disputes to ICSID arbitration as is found, according to the Directors' Report, in similar provisions in a State's investment promotion legislation. The host State's offer to submit to arbitration is firm and irrevocable so long as the relevant BIT remains in force between the two contracting States. In principle, the offer of ICSID arbitration extends to all disputes arising from an investment as defined by the BIT, and with an investor that is a national of the other Contracting State as defined by the BIT, subject to any limitations upon arbitrability set forth in the BIT and compliance with the objectives of the ICSID Convention. In some BITs the State's offer is qualified by a reference to any applicable previous agreements regarding the settlement of disputes as may be contained in investment contracts.³¹

Article 26 of the ICSID Convention provides that consent to ICSID jurisdiction excludes any other remedy but that a Contracting State may require local remedies to be exhausted 'as a condition of its consent to arbitration under this Convention'. Whilst this would be another example of BITs complementing the ICSID Convention, the number of BITs providing for the prior exhaustion of local remedies as a condition for the State's consent is relatively few. Some of them provide that ICSID arbitration is available to the investor if the remedy has not been exhausted after a specified period of time following the instigation of local proceedings.³²

b) *The investor's acceptance*

It has been made clear that '[t]he requirement of the consent of the parties does not disappear with the existence of the Treaty. The Convention envisages an exchange of consents between the Parties . . . It appears therefore that the two States cannot, by virtue of Art. 25 of the Convention compel any of their nationals

³¹ Under many US BITs, recourse to arbitration is an alternative to settling disputes 'in accordance with any applicable previously agreed dispute-settlement procedures', see e.g. 1994 Trinidad and Tobago-US BIT, 1993 Ecuador-US BIT.

³² e.g. the 1991 BIT between Belgium-Luxembourg and Uruguay providing that consent to ICSID jurisdiction applies only if the competent judicial or administrative authority has failed to decide within eighteen months or has not ruled in accordance with the BIT or international law; see A. Parra, *supra* note 26 at 333. A similar provision is found in the 1991 Argentina/Spain BIT (Article X). The decision on jurisdiction of 25 January 2000 in *Emilio Agustín Maffezini v. The Kingdom of Spain*, (2001) ICSID Rev. at para. 64, held that the Argentine investor was entitled to rely on Spain's consent contained in the BIT between Spain and Argentina, without needing to resort to Spanish courts prior to arbitration, as required in Article X(2) of that BIT. This was by virtue of the most-favoured nation clause in the BIT, which allowed the investor to rely on the Chile/Spain BIT, in which there was no such condition for ICSID jurisdiction.

to appear before the Centre; this is a power that the Convention has not granted to the States.³³ In order for the required consent to be established, the State's offer has to be accepted by the investor. Such acceptance may occur at any point in time and cover all possible future disputes or relate to a given dispute once it has arisen. Practice shows that the first situation is purely hypothetical. ICSID has in fact never recorded an investor's acceptance of the State's offer prior to the outbreak of a dispute. Typically, it is when the dispute emerges that the foreign investor accepts the State's offer, especially as it is usually only then that the investor discovers the existence of a BIT enabling it to resort to ICSID jurisdiction. The investor's consent may be manifested in a written declaration signed by the investor when filing a request for arbitration with ICSID.³⁴ The latter will forward this declaration to the State concerned, with the result that when it is reached by the offering State the mutual written consent required by the ICSID Convention may be said to exist. Alternatively, the request for arbitration itself may serve the purpose of expressing the investor's acceptance of the State's offer of ICSID jurisdiction. Notice of such acceptance will reach the State when the request is transmitted to it by ICSID in accordance with Article 36(3) of the ICSID Convention.³⁵

The way in which the State's offer is formulated will determine whether only the investor or also the State may take the initiative of instituting an ICSID arbitration for the settlement of an investment dispute. If the State's offer of arbitration leaves it up to the investor whether or not to accept it, there will be no way for the State to initiate an ICSID arbitration (or any other arbitration provided by the BIT) against the investor. An example is the standard draft of 29 November 1991 for Danish BITs, Article 9(2) of which states:

If any dispute between an investor of one Contracting Party and the other Contracting Party continues to exist after a period of three months, investor shall be entitled to submit the case either to: (a) [ICSID] . . .³⁶

³³ *American Manufacturing & Trading, Inc. v. Republic of Zaire*, award of 21 February 1997, (1997) XXII Y.B. Comm. Arb. 60 at 66-67.

³⁴ This declaration of consent is compulsory under Article 1121 of NAFTA Chapter 11, Section B.

³⁵ For the consent to be valid, the acceptance must correspond to the offer by the State, i.e. it must relate to an 'investment' (see part II.2 below) and originate from an 'investor' (see II 3) below) and may not cover investment disputes that are not arbitrable under the BIT; see A. Parra, *supra* note 26 at 337-339).

³⁶ R. Dolzer & M. Stevens, *supra* note 14 at 176. A similar approach is adopted in Article 11 (2) of the German model treaty of February 1991 (*ibid.* at 187) and in Article 9 of the draft Dutch BIT of May 1993 (*ibid.* at 209). Under the Energy Charter Treaty only investors may instigate arbitration against the State.

Other BITs contain more detailed provisions aimed at ensuring that both parties are entitled to initiate arbitration. Thus, the model form of the US BIT of February 1992 provides (in Article VI) for a two-step procedure.³⁷ The investor must first 'choose to consent in writing to the submission of the dispute for settlement by binding arbitration' either to ICSID jurisdiction or under the ICSID Additional Facility, the UNCITRAL Arbitration Rules or any other arbitration rules mutually agreed between the parties to the dispute. Once the investor has so consented, either party may initiate arbitration in accordance with the choice so made by the investor. Even under this procedure the State's entitlement to initiate ICSID arbitration is subject to two limitations: firstly, it will depend on the investor's having accepted ICSID jurisdiction;³⁸ secondly, it may only relate to the particular dispute for which arbitration has been accepted by the investor.

A third category of BITs takes an approach the legal effectiveness of which is highly questionable. For example, the Austrian draft BIT of February 1994 provides that '[i]n the case of arbitration, each Contracting Party, by this Agreement irrevocably consents in advance, even in the absence of an individual arbitral agreement between the Contracting Party and the investor, to submit any such dispute to this Centre [i.e. ICSID] and to accept the award as binding' (Article 8(2)).³⁹ It is hardly conceivable that ICSID would accept jurisdiction in a situation in which the investor has failed to give its consent to arbitration.

Even when BITs provide that either party is entitled to initiate arbitration, the State would have difficulty availing itself of this possibility whenever the investor's consent is manifested only in the request for arbitration,⁴⁰ i.e. when arbitration has already been initiated. In this case, however, nothing will prevent the defendant State from presenting a counterclaim in the same arbitration.

37 *Ibid.* at 240. The same approach is adopted in Article 2(2) of the Swiss standard draft BIT of 1 June 1986 (*ibid.* at 218) but not by the recent US-Uruguay BIT of 25 October 2004 (*supra* note 30), in which there is no provision for arbitration to be initiated by the host State.

38 The investor will take this initiative if it wants to avoid being sued by the State in a national court—which might be the local court of the State in question. It may discover that this has happened during the cooling-off period that BITs normally allow for the parties to attempt to resolve their dispute amicably.

39 R. Dolzer & M. Stevens, *supra* note 14 at 167.

40 Unless such expression of consent by the investor is deemed not to be in compliance with the arbitration provisions of the particular BIT.

2. 'Investment'

The parties' ability to set the ICSID mechanism in motion presupposes that the other conditions laid down in Article 25(1) of the Convention have been met. One of these conditions is that the dispute must arise 'out of an investment'. One would have expected investment to be defined, given its relevance to the application of the ICSID Convention. However, no such definition, nor even a general description of what is meant by this concept, is to be found anywhere in the Convention. This was a deliberate decision by the drafters, in view of the difficulty of finding an acceptable definition of investment. The Directors' Report explains that the term was left undefined as the parties' consent would in any case be required to establish ICSID jurisdiction and that each Contracting State is left free to exclude classes of disputes from the application of the ICSID Convention (Article 25(4)).⁴¹

The lack of a definition of investment makes it possible to exercise greater flexibility when deciding whether or not an operation qualifies as an investment for purposes of the ICSID Convention. Certain minimum requirements nonetheless have to be met for this to be the case. According to the OECD definition, adopted also by the European Community, 'foreign direct investments' are those made by non-residents for the purpose of establishing lasting economic ties with an enterprise over which management rights are exercised.⁴² Under this definition, a sales transaction where the price is paid upon delivery of the product may not be considered as an investment.⁴³ A dispute over a State's refusal to allow an investment would also fall outside the scope of the ICSID Convention since it could not be said to arise directly out of an investment, even if the BIT in question considers that it could be referred to ICSID jurisdiction.⁴⁴ Subject to these minimum requirements, which must be met in order for ICSID to have jurisdiction, the parties are likely to take advantage of the flexibility offered by the Convention to bring disputes within ICSID jurisdiction when expressing their consent to that effect. If their consent is

⁴¹ Director's Report at para. 27.

⁴² G. Sacerdoti, 'Bilateral Treaties and Multilateral Instruments on Investment Protection' (1997) 269 *Collected Courses of the Hague Academy of International Law* 306.

⁴³ In one reported case ICSID refused to register a request for arbitration since the cause of action was a sale of goods. The award in *Mihaly Int. corp. v. Republic of Sri Lanka*, (2002) ICSID Rev. 142, found that ICSID and the Tribunal's jurisdiction was lacking as the activity carried out by the claimant could not be characterized as an investment under the US-Sri Lanka BIT on the basis of which ICSID arbitration had been initiated.

⁴⁴ A. Parra, *supra* note 26 at 325.

given in an arbitration clause, it may be inferred that the parties have also agreed to consider the transaction covered by the agreement as an investment for the purposes of the ICSID Convention.⁴⁵

The flexibility allowed by the ICSID Convention with regard to the concept of investment has opened the way for BITs to play a complementary role. Indeed, unlike the Convention, BITs carefully define investments in order to clearly establish the limits, *ratione materiae*, of the protection that one Contracting State undertakes to accord to nationals of the other Contracting State when entering into the treaty. They follow a common pattern, which consists in first giving a rather broad definition and then a non-exhaustive list of what may constitute an investment.⁴⁶ By consenting to ICSID jurisdiction within the framework of a given BIT, investor and host State are thus deemed to have accepted that, *ratione materiae*, the condition set out in Article 25(1) of the ICSID Convention is met. An ICSID tribunal will have to examine carefully whether the transaction to which the dispute relates meets the investment criterion under both the Convention and the BIT.⁴⁷

45 The 1993 ICSID model clauses suggest incorporating the following wording in the agreement: 'It is hereby stipulated that the transaction to which this agreement relates is an investment.'

46 A broad definition is given by the US model BIT of February 1992, Article I of which provides:

'1. For the purposes of this Treaty,

(a) "investment" means every kind of investment in the territory of one Party owned or controlled directly or indirectly by nationals or companies of the other Party, such as equity, debt, and service and investment contracts; and includes:

(i) tangible and intangible property, including rights, such as mortgages, liens and pledges;

(ii) a company or shares of stock or other interests in a company or interests in the assets thereof;

(iii) a claim to money or a claim to performance having economic value, and associated with an investment;

(iv) intellectual property which includes, inter alia, rights relating to literary and artistic works, including sound recordings, inventions in all fields of human endeavor, industrial designs, semiconductor mask works, trade secrets, know-how, and confidential business information, and trademarks, service marks, and trade names; and

(v) any right conferred by law or contract, and any licenses and permits pursuant to law;

(b) "company" of a Party means any kind of corporation, company, association, partnership, or other organization, legally constituted under the laws and regulations of a Party or a political subdivision, thereof whether or not organized for pecuniary gain, or privately or governmentally owned or controlled;

(c) "national" of a Party means a natural person who is a national of a Party under its applicable law;

(d) "return" means an amount derived from or associated with an investment, including profit; dividend; interest; capital gain; royalty payment; management, technical assistance or other fee; or returns in kind;

(e) "associated activities" include the organization, control, operation, maintenance and disposition of companies, branches, agencies, offices, factories or other facilities for the conduct of business; the making, performance and enforcement of contracts; the acquisition, use, protection and disposition of property of all kinds including intellectual property rights; the borrowing of funds; the purchase, issuance, and sale of equity shares and other securities; and the purchase of foreign exchange for imports.'

47 C.H. Schreuer, *supra* note 28 at 129.

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In *AMT v. Zaire* the Tribunal rejected the respondent's argument that the dispute was not really with the claimant but with a Zairian company in which the claimant held a majority interest, since under the US-Zaire BIT the term investment included 'shares of stock or other interests in a company'.⁴⁸ In *Fedax v. Venezuela* the Tribunal held that promissory notes were covered by the definition of investment in the Netherlands-Venezuela BIT which includes 'every kind of asset' and, more specifically, 'titles to money'.⁴⁹ Likewise, in *CSOB v. The Slovak Republic* the Tribunal held that a loan was to be considered as included in the definition of investment contained in the Czech Republic-Slovak Republic BIT.⁵⁰ In *Salini Costruttori v. Morocco* the Tribunal held that the construction contract out of which the dispute had arisen fell within the definition of investment provided by the BIT between Italy and Morocco.⁵¹ The Tribunal in this case considered that an investment implies 'contributions, a certain duration of performance of the contract and a participation in the risks of the transaction . . . [and] the contribution to the economic development of the host State of the investment'.⁵² In *CMS Gas Transmission v. Argentina* the Tribunal had to deal with an objection by Argentina that since the claimant was only a minority shareholder in the company (TGN) affected by certain measures it had adopted, the claimant did not hold the rights upon which it based its claim. The Tribunal examined this issue both under the ICSID Convention and under the definition of investment contained in the US-Argentina BIT of 14 November 1991 on which ICSID jurisdiction was founded. That definition referred in particular to 'a company or shares of stock or other interests in a company or interest in the assets thereof'. It concluded that the claimant was an investor in respect of its own shareholding in TGN and accordingly had a direct right of action.⁵³ In *Azurix v. Argentina* the Tribunal found that the fact that the claimant had made an investment by paying a 'canon' to obtain the concession for providing the Province of Buenos Aires with water and wastewater

48 *American Manufacturing & Trading Inc. v. Republic of Zaire*, *supra* note 33 at 66.

49 *Fedax N.V. v. The Republic of Venezuela*, decision on jurisdiction, 11 July 1997, (1998) 37 I.L.M. 1378 at 1381.

50 *Ceskoslovenska Obchodni Banka, A.S. v. The Slovak Republic*, *supra* note 25 at 277, 282, where the BIT, whose entry into force was disputed, was taken into consideration by the Tribunal due to being incorporated by reference into the parties' agreement under the applicable choice of law clause.

51 *Salini Costruttori SpA and Italstrade SpA v. Kingdom of Morocco*, decision on jurisdiction, 23 July 2001, (2002) 129 J.D.I. 196 (in the French original, annot. E. Gaillard); (2003) 42 I.L.M. 609. Dr Robert Briner, to whom this paper is dedicated, was the chairman of the ICSID Tribunal.

52 *Ibid.* at para. 52.

53 *CMS Gas Transmission Company v. Republic of Argentina*, decision on jurisdiction, 17 July 2003, (2004) 22 ASA Bulletin 72.

services and had established a local company to carry out the investment brought the transaction within the wide definition of investment contained in the US-Argentina BIT.⁵⁴ In *Joy Mining Machinery Ltd. v. The Arab Republic of Egypt* the Tribunal rejected the claimant's argument that a bank guarantee was an investment rather than simply 'a contingent liability' and accordingly found that jurisdiction to hear the case was lacking.⁵⁵

Some BITs include contractual rights in the definition of investment.⁵⁶ However, this would be insufficient to establish ICSID jurisdiction if the relevant contract does not meet the minimum standards to be characterized as an investment under the ICSID Convention, as would be the case with a contract for the sale of goods.

Provided the investment is made by 'a national of another Contracting State', there is no requirement under Article 25(1) or otherwise under the ICSID Convention that the origin of the investment be foreign. The only reference to the non-domestic character of the investment foreseen by the ICSID Convention is contained in the Preamble, which speaks of 'private international investment'.⁵⁷ The international character of the investment is not contradicted by the circumstance that what is invested is property already in the territory of the host State or profits generated therein as a result of a previous foreign investment, provided the owner of such property or profits is a national of another State, which, rather than repatriating its wealth, chooses to invest it in the host State's territory.

The sources used by the investor to finance its investment were considered irrelevant in *Tradex Hellas v. Albania*.⁵⁸ Likewise, in *Tokios Tokelès v. Ukraine* the foreign origin of the investment was not regarded as relevant since the investment was owned by a national of another Contracting State according to the definition of nationality contained in the BIT between Lithuania and Ukraine on which ICSID jurisdiction was founded.⁵⁹

54 *Azurix Corp. v. Republic of Argentina*, decision on jurisdiction, 8 December 2003, (2004) 22 *ASA Bulletin* 95 at 105.

55 *Joy Mining Machinery Ltd. v. Arab Republic of Egypt*, award of 6 August 2004, <www.asil.org/ilil/JoyMining_Egypt.pdf>.

56 The Swiss standard draft BIT of 1 June 1986 includes in the term 'investments' also 'rights . . . given by Contract' (Article 1(c)(ee)); see R. Dolzer & M. Stevens, *supra* note 14 at 220.

57 ICSID Convention, Preamble: 'Considering the need for international cooperation for economic development and the role of private international investment therein . . .'

58 *Tradex Hellas S.A. v. Albania*, award of 29 April 1999, (1999) 14 *ICSID Rev.* 197 at 226-227.

59 *Tokios Tokelès v. Ukraine*, decision on jurisdiction, 29 April 2004, <www.worldbank.org/icsid/cases/awards.htm> at para. 80.

If, as is not uncommon, a BIT provides that an investment, as defined by the BIT, must be approved in accordance with the host State's legislation, such approval is a constituent element in the State's offer of ICSID jurisdiction. If it is lacking, consent may be deemed not to exist.⁶⁰

To come within ICSID jurisdiction a dispute must arise '*directly*' out of an investment. This adverb relates to the dispute rather than the investment.⁶¹ The parties' consent cannot modify this condition, since the dispute's direct connection with an investment is an objective requirement. This means that disputes and differences that BITs describe as 'concerning an investment',⁶² 'with respect to investments'⁶³ or an 'investment dispute'⁶⁴ may be submitted for settlement by binding arbitration under the ICSID Convention provided they arise '*directly*' out of the investment.

It is worth recalling that in all cases where ICSID has no jurisdiction because the dispute does not arise directly out of an investment, the parties may have recourse to the ICSID Additional Facility Rules if, as often happens, the relevant BIT provides for such alternative form of arbitration⁶⁵ and at least one of the parties is a Contracting State or a national of a Contracting State (Article 2).

3. 'Nationality' of a Contracting State

The ICSID Convention neither offers a definition of nationality nor indicates under what conditions nationality is to be ascertained in each given case. When describing what 'national of another Contracting State' means, Article 25(2) merely states that for both physical persons and legal entities nationality must exist on the date on which the parties consented to ICSID arbitration and, in

60 In *SPP v. Arab Republic of Egypt*, a case based on Egyptian investment promotion legislation of 1974, the respondent contended that the investment did not comply with Egyptian legislation as approval of the project had been withdrawn. The Tribunal, however, held that the investment had been validly approved at the outset; decision on jurisdiction, 27 November 1985, (1995) 3 *ICSID Reports* 112 at 123-24.

61 In *Fedax N.V. v. Republic of Venezuela*, *supra* note 49 at 1383, the Tribunal held that jurisdiction can exist even if the investment is not direct, provided that the dispute arises directly from the transaction.

62 German and Hong Kong model BITs; see R. Dolzer & M. Stevens, *supra* note 14 at respectively 194 and 205.

63 Swiss standard draft BIT; *ibid.* at 224.

64 US model BIT of February 1992; *ibid.* at 246-47.

65 The US model BIT of February 1992 provides (in Article VI) for alternative submission, for settlement by binding arbitration, 'to the Additional Facility of the Centre, if the Centre is not available' (*ibid.* at 247).

the case of a physical person, on the date the request for arbitration is registered. A legal entity that possesses the nationality of the Contracting State party to the dispute may satisfy this *ratione personae* requirement if the parties have agreed that, because of foreign control, it should be treated as a national of another Contracting State (Article 25(2)(b)).

The problems posed by nationality are less acute problems when it comes to physical persons.⁶⁶ Those who reside permanently in a Contracting State but are not nationals of that State or who hold the nationality of a non-Contracting State may not have access to ICSID jurisdiction, even if the BIT defines them as nationals of a Contracting State.⁶⁷

Determining the nationality of a legal entity, on the other hand, is a more complex matter, due to the variety of criteria that may be applicable. BITs are obviously concerned to clearly identify the investors to which the State's protection is meant to extend, and this is therefore another area where they complement the nationality requirement under the ICSID Convention. The most widely used criteria for determining nationality are the place of incorporation, the registered office, the place of actual management or the effective seat.⁶⁸ The parties are free to agree on one or other of these criteria, or more than one. The most simple solution is that found in the US Model BIT of February 1992, which refers to 'nationals or companies of the other Party' and defines 'company of a Party' as any kind of corporation, company, association, partnership or other organization legally constituted under the laws and regulations of a Party' (Article 1(b)).⁶⁹

Commentators have not reached a consensus regarding the acceptability of the control test, i.e. determination of the nationality of the investor on the basis of a reference by the parties or the BIT to the nationality of the party holding a controlling interest.⁷⁰ This test might be considered incompatible with the ICSID

66 The award of 7 July 2004 in *Soufraki v. U.A.E.*, <<http://ita.law.uvic.ca/documents/Soufraki.pdf>>, is indicative of the difficulties that the Tribunal had to overcome in establishing the nationality of a natural person. The Tribunal found that the claimant's claim that he was an Italian national failed for lack of evidence and that, accordingly, the dispute fell outside ICSID jurisdiction.

67 A. Parra, *supra* note 26 at 299, 324.

68 C.H. Schreuer, *supra* note 28 at 277.

69 See *supra* note 46.

70 The control criterium is referred to in the Dutch draft BIT of May 1993, which defines 'nationals' of a Contracting Party as: '(i) natural persons having the nationality of that Contracting Party; (ii) legal persons constituted under the law of that Contracting Party; (iii) legal persons not constituted under the law of that Contracting Party but controlled, directly or indirectly, by natural persons as defined in (i) or by legal persons as defined in (ii) above.' (R. Dolzer & M. Stevens, *supra* note 14 at 210, emphasis added).

Convention if it allows a national of a non-Contracting State or an agency or a public entity controlled by a Contracting State to be regarded as investors.⁷¹ Article 25(2)(b) of the ICSID Convention supports this view since it refers to 'control' in only one specific and exceptional situation,⁷² and would thus appear to exclude its use in other situations.⁷³ The guiding principle should be that a nationality test chosen by the parties or specified in a BIT is to be accepted except when, in a given case, the result would be clearly contrary to the objectives of the ICSID Convention. If ICSID jurisdiction is excluded for this reason, the parties may resort to the other forms of arbitration provided by the BIT.

4. Applicable law

Whatever the basis of the arbitration instituted by the investor against the host State—be it an arbitration clause in an investment agreement or a BIT—the investor may assert a claim for breach of any provisions of the BIT between its own State and the host State. The great majority of BITs provide for common standards in the treatment of foreign investors and foreign investment, relating to fair and equitable treatment, full protection and security, non-discrimination, national treatment and most-favoured-nation treatment.⁷⁴

In the case of arbitrations conducted in accordance with the ICSID Convention on the basis of a BIT, it could be argued that, in the absence of a choice of law by the parties, the domestic law of the host State and rules of international law should apply pursuant to the second part of Article 42(1) of the ICSID Convention. Reference to the provisions of the BIT on which ICSID jurisdiction is based will not prevent the investor from also relying on any other rules of international law that may be applicable, as permitted by Article 42(1) of the ICSID Convention. Such rules will not only serve to fill gaps in the domestic

71 The decision on jurisdiction of 24 May 1999 in *CSOB v. The Slovak Republic*, *supra* note 50 at para. 21, found CSOB to be a 'national of another Contracting State' within the meaning of Article 25(1) of the ICSID Convention, according to the functional test, i.e. although more than 65 per cent of CSOB's shares were owned by the Czech Republic, CSOB was not acting as an agent for the government or discharging an essentially governmental function.

72 According to Article 25(2)(b), a national of the Contracting State party to the dispute may, that notwithstanding, be a party to the same dispute 'because of foreign control'.

73 It is worth recalling that the history of the drafting of the ICSID Convention shows that attempts to introduce the control test were defeated by a large majority of the delegates; see C.H. Schreuer, *supra* note 28 at 278.

74 For a description of these various standards see R. Dolzer & M. Stevens, *supra* note 14 at 58–66.

law of the host State and to correct it in the event of a conflict with international law,⁷⁵ but will also allow the parties and the ICSID arbitrator to apply international law as an autonomous body of substantive rules independently of the law of the host State.⁷⁶

A different approach seems preferable, on the other hand, in all cases in which ICSID jurisdiction is founded on a BIT as an instrument of public international law. Here, it is assumed that, by referring to the BIT as the basis of their arbitration agreement, the parties have implicitly chosen the BIT's provisions as rules of law governing their dispute, pursuant to the first part of Article 42(1) of the ICSID Convention, and have thereby excluded any provisions of the law of the host State. As stated in the *Antoine Goetz et al v. Republic of Burundi* award:⁷⁷ 'The Bilateral Treaty on investment protection is not only the basis for the jurisdiction of the Centre and of the Tribunal; it also determines the applicable law.'⁷⁸ If the BIT provision on applicable law refers to the law of the host State in addition to the BIT itself and the rules and principles of international law,⁷⁹ State law too will have to be applied. The arbitrator will

75 This dual role was first affirmed by the *ad hoc* Committee's decision on annulment in *Klückner Industrie-Anlagen GmbH and others v. United Republic of Cameroon and Société Camerounaise des Engrais*, 3 May 1985, (1986) 1 ICSID Rev. 90.

76 The *ad hoc* Committee's decision on annulment in *Wena Hotels v. Arab Republic of Egypt*, 5 February 2002, (2002) I.L.M. 933, considering the second part of Article 42(1) to be applicable to the question of Egypt's compliance with the BIT provisions, underlined the relevance of the reference to rules of international law contained in that Article. For a commentary see E. Gaillard & 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 Rev. 375.

77 Award of 10 February 1999 (French original in (2000) 15 ICSID Rev. 488; English translation in (2001) XXVI Y.B. Comm. Arb. 31).

78 This approach is endorsed by the annulment decision of the *ad hoc* Committee in *Compañía de Aguas del Aconquija S.A. and Vivendi Universal v. Argentine Republic*, 3 July 2002, (2002) 41 I.L.M. paras 45-46): 'whether there has been a breach of the BIT and whether there has been a breach of the contract are different questions. Each of these claims will be determined by reference to its own proper or applicable law – in the case of the BIT by international law; in the case of the Concession Contract, by the proper law of the Contract' (emphasis added). The same approach was advocated by Carolyn Lamm in her paper 'The applicable rules of law to disputes between State entities and private companies – the interaction between contract arbitration and treaty arbitration', ICC/AAA/ICSID Joint Colloquium on International Arbitration, 19 November 2004.

79 As does the Spain/Cuba BIT.

In the *CME/Lauder v. Czech Republic* arbitration, the award of 31 September 2001 rendered under the UNCITRAL Arbitration Rules was challenged before the competent Court of Appeal in Stockholm on grounds of 'excess of mandate' for having failed to apply Czech law in accordance with Article 8(b) of the 1991 Netherlands/Czech Republic BIT and having relied instead on public international law. The Court of Appeal rejected the challenge in a judgment made on 15 May 2003, (2003) 42 I.L.M. 919. Both the award and the judgment are available at <www.cetv-net.com>.

in that case be confronted with the problem (as in the second part of Article 42(1)) of prioritizing these different sources. In addition, the essential characteristics of an arbitration system resulting from two international legal instruments—the ICSID Convention and a BIT—would in any case require that mandatory rules of public international law (*jus cogens*) be respected. The suspension of diplomatic protection until the award is rendered (ICSID Convention, Article 27(1)) and the recognition of an ICSID award as having the same value as a final court judgment in each Contracting State (Article 54(1)) have been given as reasons why international law must be respected in awards made within the framework of multilateral and bilateral conventions.⁸⁰

III. Concluding remarks

Under BITs arbitration has emerged as the preferred method for resolving investment disputes and the ICSID Convention as the most widely accepted form of arbitration. The fact that most BITs refer to the ICSID Convention marks a significant development for a form of arbitration that, from its inception, has proved capable of handling in a balanced way the delicate issues arising from investment disputes. ICC arbitration has also—albeit to a lesser extent—established its presence in this field.⁸¹

Whereas parties that consent to arbitration on the basis of an arbitration clause in their contract stand on an equal footing, in the context of BITs it is only the investor that can complete the necessary bilateral consent by initiating arbitration against the State. As a rule, therefore, the State can only act as defendant in the proceedings instituted by the investor.⁸² This is not necessarily prejudicial to its interests, however, for the State is at liberty to raise a counterclaim in the same arbitration proceedings and there is nothing stopping it from bringing a claim against the investor in a competent national court, including its own courts, before the investor accepts its offer to settle disputes by arbitration.

⁸⁰ A. Giardina, 'Clauses de stabilisation et clauses d'arbitrage : vers l'assouplissement de leur effet obligatoire ?' *Rev. arb.* 2003.645 at 658–61.

⁸¹ The role of ICC arbitration in investment disputes was dealt with by E. Silva Romero in his paper 'Arbitrage institutionnel et investissements internationaux', delivered at the conference *Arbitrage et investissement international*, Sciences Po, Paris, 13 May 2004.

⁸² The position of the investor in arbitrating under a BIT is described as '*privilegiée*' by A. Giardina, *supra* note 80 at 664.

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The unexpected expansion of the ICSID system brought about by BITs creates new challenges calling for solutions that respect the private parties' legitimate expectations and the States' prerogatives. With regard to those aspects outlined in this paper, where BITs play a complementary role by making use of the flexibility permitted by the ICSID Convention, care should be taken to avoid solutions that go beyond the 'outer limits within which parties can put [ICSID] mechanisms into operation'.⁸³ This will reduce the temptation for States to renege on the terms of the BITs they have concluded in order to prevent them from being interpreted and applied in a manner that would be contrary to their expectations.⁸⁴ Reconciling the legitimate expectations of both the private investor and the host State is the objective ICSID awards should strive to achieve. This will help to ensure that the new phase of investment dispute resolution, marked by the emergence of BITs incorporating consent to ICSID arbitration, will be a fruitful development for tackling the delicate problems posed by foreign investment.

⁸³ A. Broches, *supra* note 6 at 67.

⁸⁴ A. Giardina, *supra* note 80 at 665. It is known that as a result of the award in *SPP v. Arab Republic of Egypt*, *supra* note 21, Egypt enacted law no. 8 of 1997 amending its law no. 34 of 1974 on investment promotion, so as to prevent it from being interpreted to mean that the State had made an offer of arbitration allowing the investor to initiate arbitration proceedings against it. The decision on jurisdiction of 15 November 2004 in *Salini Costruttori SpA and Italstrade SpA v. Hashemite Kingdom of Jordan*, <www.worldbank.org/icsid/cases/awards.htm>, represents in this respect a well-balanced answer to the issues raised by the co-existence of contractual claims and claims of breach of a BIT.