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Third-Party Funding and the Objectives of Investment Treaties: Friends or foes?
Brooke Güven and Lise Johnson



A Bit of Anti-Bribery: How a corruption prohibition in FIPAs can bring a minimum standard of conduct for Canadian investors abroad
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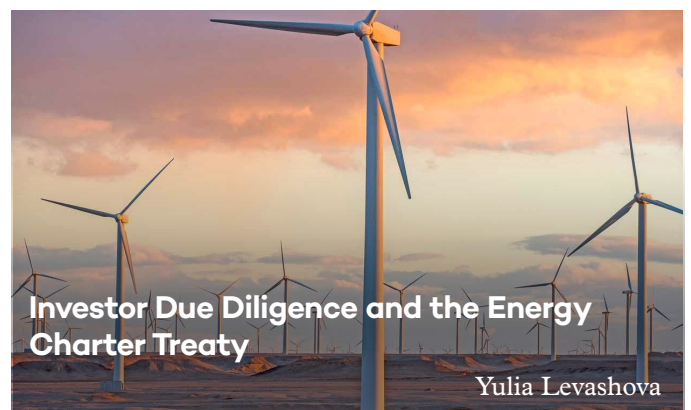
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International Institute for the Sustainable Development
International Environment House 2
9, Chemin de Balexert, 6th Floor
1219, Chatelaine, Geneva, Switzerland

Tel +41 22 917-8748
Fax +41 22 917-8054
Email itn@iisd.org
Twitter [iisd_news](https://twitter.com/iisd_news)

IISD Group Director – Economic Law & Policy
Nathalie Bernasconi

Editor-in-Chief
Martin Dietrich Brauch

French Editor
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Communications Officer
Sofía Baliño

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LIST OF ACRONYMS

ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Treaty
CETA	Comprehensive Economic and Trade Agreement
CJEU	Court of Justice of the European Union
COMESA	Common Market for Eastern and Southern Africa
CPTPP	Comprehensive and Progressive Trans-Pacific Partnership
CSR	Corporate Social Responsibility
EAC	East African Community
EC	European Commission
ECJ	European Court of Justice
ECOWAS	Economic Community of West African States
ECT	Energy Charter Treaty
EU	European Union
FDI	Foreign Direct Investment
FET	Fair and Equitable Treatment
FTA	Free Trade Agreement
GATT	General Agreement on Tariffs and Trade
ICC	International Chamber of Commerce
ICS	Investment Court System
ICSID	International Centre for Settlement of Investment Disputes
ICSID Convention	Convention on the Settlement of Investment Disputes between States and Nationals of Other States
IIA	International Investment Agreements
IISD	International Institute for Sustainable Development
ILO	International Labour Organization
ISDS	Investor–State Dispute Settlement
ITN	Investment Treaty News
MFN	Most-Favoured Nation
MIC	Multilateral Investment Court
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Co-operation and Development
PCA	Permanent Court of Arbitration
PPP	Public–Private Partnership
RCEP	Regional Comprehensive Economic Partnership
SADC	Southern African Development Community
SCC	Stockholm Chamber of Commerce
SDG	Sustainable Development Goal
TFEU	Treaty on the Functioning of the European Union
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
USMCA	United States–Mexico–Canada Agreement
VCLT	Vienna Convention on the Law of Treaties
WTO	World Trade Organization



INSIGHT 1

Third-Party Funding and the Objectives of Investment Treaties: Friends or foes?

Brooke Güven and Lise Johnson



Increasingly, investors suing governments in treaty-based ISDS are turning to third-party funding (TPF): third parties finance their litigation in exchange for a return or other financial interest in the outcome of a dispute, often accompanied by a contractual right for the funder to remain involved in, and potentially even control, the management of the claim.¹

TPF of ISDS claims is largely unregulated at the treaty level as well as under applicable arbitration rules. As its use rapidly expands, it is increasingly drawing the attention of governments, arbitral tribunals, civil society, academics, counsel, investors and funders.

Multilateral regulation is currently being considered in the context of ICSID's rule revision process as well as UNCITRAL's Working Group III on ISDS reform. Key initiatives such as the ICSID rule revision process, however, are focusing only on certain narrow issues such as implications of TPF for confidentiality, conflicts of interest and the state's ability to recover costs.

But as we recently argued in a [working paper](#),² it is crucial

to explore the more fundamental questions of whether and to what extent TPF aligns (or not) with the objectives of modern investment treaty law and how different regulatory approaches may affect that alignment.

Is TPF in ISDS appropriate in light of relevant policy objectives?

ISDS is integrated in investment treaties purportedly as a mechanism to advance their overarching objectives of promoting investment and shaping governments' treatment of it in order to foster sustainable development. These treaties are instrumentalist agreements: investor protections and ISDS claims are not the end goal but are justified as a means of achieving broader development objectives.

When evaluating TPF of ISDS cases it is therefore crucial to understand whether and how this particular financial structure and the incentives created by it affect the operation of ISDS and its role in advancing the object and purpose of investment treaties. In this context, it is useful to consider the impacts of TPF on three broad categories: (1) the conduct of investors; (2) the development of the law; and (3) the conduct of host states.

1. Impacts on investors' decisions

TPF may increase the number of ISDS cases because it reduces the risk and cost of pursuing a claim. TPF allows claimants to monetize illiquid interests in the outcome of their claims and to transfer some or all litigation risk to the funder. This may tilt decision making in favour of arbitration and can result in investors pursuing claims that, absent such funding, they would have been unwilling or unable to pursue. Research suggests that litigation finance does in fact drive up the number of cases brought.³

¹ See generally International Council for Commercial Arbitration (ICCA). (2018, April). *Report of the ICCA–Queen Mary task force on third-party funding in international arbitration*. Retrieved from https://www.arbitration-icca.org/media/10/40280243154551/icca_reports_4_tpf_final_for_print_5_april.pdf

² Güven, B., & Johnson, L. (2019, May). *The policy implications of third-party funding in investor–state dispute settlement* (CCSI Working Paper). Retrieved from <http://ccsi.columbia.edu/files/2017/11/The-Policy-Implications-of-Third-Party-Funding-in-Investor-State-Dispute-Settlement-FINAL.pdf>

³ Chen, D. L. (2015). Can markets stimulate rights? On the alienability of legal claims. *The RAND Journal of Economics*, 46(1), 23–65, pp. 25, 33; see also Abrams, D. S., & Chen, D. L. (2012). A market for justice: A first empirical look at third party litigation funding. *University of Pennsylvania Journal on Business Law*, 15, 1075, p. 1078.



TPF may impact investors' decisions to remain engaged in or exit the host state. Investment treaties are often justified as being tools to attract and retain FDI. However, evidence that investment treaties influence decisions to invest in a particular host country is unclear and disputed.⁴ Even less is known about whether the availability of ISDS and associated remedies influence investment decisions to remain invested in the host country and project, or exit and seek to cash out when circumstances or relations begin to deteriorate.

ISDS may have a negative impact on investor retention and long-term investor–state relationships. Powerful dispute settlement mechanisms and remedies, such as those offered through ISDS, risk crowding out cooperation by making exit and early payout more attractive, to the detriment of the long-term resilience of a project.⁵ While these effects can arise with ISDS alone, TPF may increase their likelihood because funders become an additional behind-the-scenes stakeholder attracted by the prospect of expectation damages, are less interested in non-monetary settlements that may enable the project to proceed, and reduce the cost and risk to the claimant of bringing a case, making ISDS even more attractive than it would be without TPF.

2. Impacts on the law and outcomes

TPF in ISDS may shift the development of investment law in a more funder- (and claimant-) friendly direction. Debates over the impact of TPF in ISDS often focus on whether TPF will result in more frivolous claims. However, given the infamously nebulous meaning of investment treaty standards, and structural disincentives to declare claims frivolous, it is useful to move beyond that label. Rather, the inquiry should be on whether TPF encourages *marginal* claims—those advancing arguments about investment law that seek to stretch its reach in unintended and potentially undesirable directions, such as to primarily challenge

government conduct taken in good faith to advance legitimate public interest objectives.⁶

It is also important to question whether funders are as averse to risky claims as is often professed. Analysis of TPF in the Australian domestic context, for instance, concluded that TPF led to the filing of more cases generally, and more novel and uncertain cases in particular. The novel or risky claims being pursued by funders can, if successful, push development of the law (in funder- or claimant-friendly directions). The research in Australia also notably found that third-party funded cases were particularly influential in developing the law, being reversed less and cited more than non-funded cases.⁷

Similar outcomes may arise in the ISDS context. A claimant's access to resources and sophisticated insider knowledge seems to be an important determinant of success in particular disputes. Funders can provide both types of advantages through direct contributions of insight and expertise, and via the retention of top law firms.⁸ Additionally, funders can strategically support disputes in order to push the law in directions that favour funders' interests. Portfolio funding further facilitates this practice by enabling funders to bundle novel long-shot cases with favourable potential for rule change (even those with an anticipated value of less than would be financially viable as an individually-funded claim) together with less risky claims.⁹ It therefore seems reasonable to conclude that the presence of TPF will have an impact on the outcomes in particular decisions and contours of the law in a way that expands the potential for claims and host state liability beyond what is desired by states and other stakeholders.

As Burford, one ISDS funder stated, “Our capital can change outcomes in litigation matters, and in particular our capital can create outcomes that may be legally correct but challenging when viewed through a broader lens.”¹⁰

⁴ Pohl, J. (2018). *Societal benefits and costs of international investment agreements: A critical review of aspects and available empirical evidence* (OECD Working Papers on International Investment, 2018/01). Paris: OECD Publishing. Retrieved from <https://doi.org/10.1787/e5f85c3d-en>; Bonnitcha, J. (2017). *Assessing the impacts of investment treaties: Overview of the evidence*. Winnipeg: IISD. Retrieved from <https://www.iisd.org/library/assessing-impacts-investment-treaties-overview-evidence>

⁵ See, e.g., Gilson, R., Sabel C.F., & Scott, R. E. (2010). Braiding: The interaction of formal and informal contracting in theory, practice, and doctrine. *Columbia Law Review*, 10, 1377, pp. 1387-1402

⁶ Pelc, K. J. (2017). What explains the low success rate of investor-state disputes? *International Organization*, 71(3), 559-583.

⁷ Chen (2015), *supra* note 3, p. 49; Abrams & Chen (2012), *supra* note 3, pp. 1105-1106.

⁸ Remmer, K. (2018). The outcomes of investment treaty arbitration: A reassessment. In L. Johnson & L. Sachs (Eds.). *Yearbook on international investment law & policy 2015-16*. Oxford University Press.

⁹ Burford Capital describes portfolio financing as “inherently flexible and ideally suited for...matters that would otherwise be less attractive for funding.” Burford Capital. (2016). *Beyond “litigation finance.”* Retrieved from https://www.burfordcapital.com/wp-content/uploads/2016/09/Burford-Beyond_Litigation_Finance-US_Web.pdf

¹⁰ Burford Capital. (2019). *Environmental, social and governance factors*. Retrieved from <https://www.burfordcapital.com/investors/investor-information/environmental-social-governance>



It is therefore crucial to better understand and address the role of TPF in driving “challenging” outcomes in investment law and ISDS cases.

TPF can impact decisions to settle, or not settle, claims. While not all funders take an active interest or role in management of a claim, some may consider this role to be of critical importance. Funders have various reasons to settle, or not, including the desire to book revenue of a certain amount or in a particular period, or to influence the development of the law. Additionally, funders’ primary ethical and regulatory obligations are to their shareholders, not to the funded party, so they may push settlement decisions or outcome demands that are different from those preferred by the local enterprise whose investment underlies the ISDS case.

A related issue is that the presence of a funder can shift bargaining power in favour of the claimant, with consequent impacts on the state’s willingness to settle and on settlement outcomes. Respondent states face risks related to ISDS claims that investors do not, including their unique risks of exposure to damage awards based on vague and unpredictable legal standards, and of perceived reputational harms. While investors may also assume risks in bringing claims, namely the risk of not recovering losses suffered, ISDS is not necessarily an investor’s only means of recourse, which could also include political risk coverage or domestic law or contract claims, or even diplomatic pressure. While this asymmetrical exposure to risk can alone tilt playing fields in the investor’s favour in settlement discussions, TPF can shift evolving power dynamics and settlement outcomes even further in favour of an investor and away from the state. This, in turn, can cause settlement terms to reflect those imbalanced power relationships more than the merits of the case.

3. Impacts on governments

TPF can impact governments’ willingness and ability to regulate investment in order to advance sustainable development aims. Governments need policy space in order to achieve public interest objectives and to react to changing circumstances, evidence, needs and priorities. Policy space is not, and should not be, unlimited, but it is also important not to overly deter by unduly discouraging (or requiring compensation for) good faith actions taken by governments in the public interest to achieve economic, social and environmental aims. It is therefore important to understand whether and how TPF may exacerbate risks of overdeterrence, whether by increasing the overall likelihood of an ISDS case, targeting certain types of governments, pursuing

certain types of claims, or increasing the likelihood of funder-favourable outcomes.

For instance, claims in extractive industries and infrastructure, with heightened damage awards, may be particularly attractive to third-party funders due to their large potential payouts.¹¹ Countries reliant on private investment in these industries as a development strategy may figure prominently on funders’ radars, especially if the regulatory frameworks governing either are relatively nascent, changing or a bubbling source of controversy. In such cases, as noted above, investors may hold a relatively strong upper hand in settlement negotiations when the threat of an ISDS case looms. The presence of a third-party funder backing the suit may further tilt bargaining power in the claimant’s favour and induce a settlement that, even if not causing the government to abandon the measure, increases its cost of maintaining it, which may deter the government from taking similar action in the future. The prospect of chill may be particularly problematic in these contexts given that robust government regulation of investments in the extractive industry and infrastructure is essential to capturing the benefits and avoiding the environmental, social and economic harms such projects may generate.

Of course, some governments may be more sensitive to regulatory chill than others. Governments with limited resources to fund a robust defense and any potential liabilities, those that are more sensitive to perceived reputational costs,¹² or those that are dependent on other countries for development assistance, economic regulations or diplomatic support may be less willing to contest claims. But, overall, it is crucial to understand whether TPF drives cases and outcomes that increase the likelihood and worsen the effects of overdeterrence.

Ban TPF in ISDS

More robust testing of the pros and cons of TPF is desirable, including the concerns highlighted above. Such testing, however, is difficult in light of the opacity surrounding funders’ involvement in ISDS cases. Given that it is funders, the potentially regulated actors, who hold the information that would be crucial for dispelling concerns about, and demonstrating the value of, their practices, the unavailability of information should not be used to justify a laissez-faire approach. Rather, given

¹¹ Hart, T. (2014). Study of damages in international center for the settlement of investment disputes cases. *Transnational Dispute Management*, 11(3), pp. 8–10.

¹² Kerner, A. & Pelc, K. (2019, forthcoming). *Do investor–state disputes harm FDI?* (Working paper). Montreal: McGill University.



the risks that TPF poses to the aims of the IIA system, a precautionary approach to regulation should apply, and a total ban on the practice should be of foremost consideration by policy-makers.¹³

Notably, various states have called for a ban on TPF in ISDS, particularly in the context of discussion in UNCITRAL's Working Group III discussions on ISDS reform.¹⁴ Argentina and the United Arab Emirates have gone one step further and actually included a ban in their 2018 BIT.¹⁵ The United States restricts TPF of domestic claims against the federal government.¹⁶

"Given the risks that TPF poses to the aims of the IIA system, a precautionary approach to regulation should apply, and a total ban on the practice should be of foremost consideration by policy-makers. The unavailability of information should not be used to justify a laissez-faire approach."

To the extent policy-makers determine that permitting TPF in certain kinds of cases advances the policy objectives of their investment treaty programs, partial bans could also be explored. For example, if governments have concerns about truly impecunious claimants accessing ISDS or decide that certain kinds of claims (for example, claims for direct expropriation) warrant TPF, mechanisms to permit TPF in those cases could be developed. Such mechanisms could, for example, place the burden on the claimant to

demonstrate that it meets clear criteria, which may include demonstrated impecuniosity, exhaustion of local remedies, and clean hands, among others.

A ban with specific exceptions could also be accompanied by other rules and mechanisms, such as requirements for funders to submit to the jurisdiction of the tribunal with respect to liability for cost awards, ethical obligations and transparency requirements, among other matters.

Overall, TPF in ISDS risks exacerbating problems with underlying investment standards and ISDS by introducing into the already asymmetric ISDS system a new actor with its own incentives for challenging even good faith government regulation needed to advance sustainable development objectives. The value of TPF to actors other than the arbitration bar, arbitrators, funders and some claimants has not yet been made clear, while the risks to treaty objectives are apparent. Reform initiatives and negotiations that fail to address TPF threaten to lock in a system and perpetuate an industry the intent and effects of which do not support—and may even undermine—the aims of modern international investment law.

Authors

Brooke Güven is legal researcher at the Columbia Center on Sustainable Investment (CCSI) and **Lise Johnson** is head of Investment Law and Policy at CCSI.

¹³ Garcia, F. J. (2018). Third-party funding as exploitation of the investment treaty system. *Boston College Law Review*, 59, 2911, p. 2930; Garcia, F. J. (2018, July 30). The case against third-party funding in investment arbitration. *Investment Treaty News*, 9(2), 7–9. Retrieved from <https://www.iisd.org/itn/2018/07/30/the-case-against-third-party-funding-in-investment-arbitration-frank-garcia>

¹⁴ Working Group III 35th Session, Audio recordings (April 25, 2018). Retrieved from <https://icms.unov.org/CarbonWeb/public/uncitral/speakerslog/a2ad492b-22e9-497c-93c8-4be3130e9978>; Working Group III 37th Session, Audio recordings (April 1, 2019). Retrieved from <https://icms.unov.org/CarbonWeb/public/uncitral/speakerslog/9e4160d4-6cef-4de6-83c0-d9c4645bf253>

¹⁵ Agreement for the Reciprocal Promotion and Protection of Investments between the Argentine Republic and the United Arab Emirates, signed April 16, 2018, not yet in force, Art 24. Retrieved from <https://investmentpolicy.unctad.org/international-investment-agreements/treaties/bilateral-investment-treaties/3819/argentina---united-arab-emirates-bit-2018->

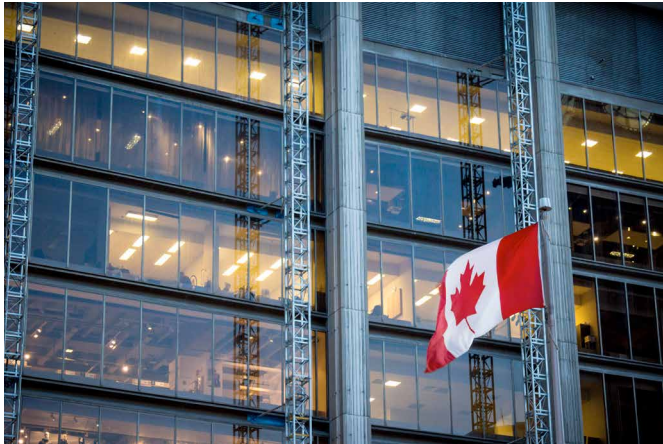
¹⁶ 31 USC § 3727 (United States Anti-Assignment of Claims Act).



INSIGHT 2

A Bit of Anti-Bribery: How a corruption prohibition in FIPAs can bring a minimum standard of conduct for Canadian investors abroad

Matthew A. J. Levine



In September 2015, the United Nations launched the SDGs. SDG 16, “Peace, Justice and Strong Institutions,” includes commitments to fight corruption, increase transparency and tackle illicit financial flows. What’s more, there is broad recognition that without meaningful action to reduce corruption, progress toward the SDGs is likely to be limited.

In that context, my recently published policy brief examines four Canadian legal initiatives against corruption of foreign officials: (1) a spike in enforcement of Canada’s foreign bribery prohibition; (2) the development of firm-level anti-bribery compliance norms; (3) the implementation of mandatory payment transparency for extractive industry investors; and (4) the progressive trade (and investment) agenda. The policy brief argues that simply prohibiting cross-border corruption at domestic criminal law is insufficient and that this diversified approach is promising, if incomplete.¹

This article focuses on the fourth component of a diversified approach: the necessity of ensuring that Canada’s investment treaties contribute to combating corruption. I first survey Canada’s Foreign Investment Promotion and Protection Agreement (FIPA) program. I then introduce the “Asymmetry Critique”

of IIAs and the unsettled legal landscape that has resulted from the lack of guidance in treaties about how tribunals should deal with corruption. In the third section I review recent developments toward a binding anti-corruption norm both in Canada’s treaty practice and in that of other states.

1. Canada’s FIPA program

Canada’s investment treaties include FIPAs as well as FTAs with investment chapters. Canada began negotiating FIPAs in the late 1980s, which resulted in a first generation of six FIPAs that were geographically focused on Eastern Europe. A more systematic approach to FIPAs emerged out of the NAFTA. On the basis of NAFTA Chapter 11, Ottawa developed a first Model FIPA, which was used in negotiations for the remainder of that decade. More than two dozen IIAs were concluded during this second generation. A third generation began in 2004 with the publication of a second Model FIPA.

As of May 2019, the Canadian government lists 38 FIPAs in force.² Canada’s Model FIPA has not been formally updated since 2004, but it is understood that changes to the model have been made on an ad hoc, rolling basis. In particular, FIPAs and FTAs signed at the end of the third generation—between 2013 and 2016—include anti-corruption language within a hortatory provision on CSR.³

² See <https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/index.aspx?lang=eng>

³ Brower, C. N., & Ahmad, J. (2019). The state’s corruption defence, prosecutorial efforts, and anti-corruption norms in investment treaty arbitration. In K. Yannaca-Small (Ed.). (2019). *Arbitration under international investment agreements: A guide to the key issues*. Oxford: Oxford University Press. Canada–Burkina Faso FIPA, Article 16; Canada–Guinea FIPA, Article 16; Benin–Canada FIPA, Article 16; Canada–Honduras FTA, Article 10.16; Canada–Republic of Korea FTA, Article 8.16; Canada–Cote d’Ivoire FIPA, Article 15(2); Canada–Serbia FIPA, Article 16; Canada–Nigeria FIPA, Article 16; Canada–Mali FIPA, Article 15(3); Canada–Mongolia FIPA, Article 14; Canada–Senegal FIPA, Article 16; Canada–Kosovo FIPA, Article 16. All agreements are available at <https://www.international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/index.aspx?lang=eng>

¹ Levine, M. A. J. (2019, June). *Canadian initiatives against bribery by foreign investors*. IISD: Winnipeg. Retrieved from <https://iisd.org/library/canadian-initiatives-against-bribery-foreign-investors>



More than 50 investor–state arbitrations are known to have been filed by Canadian investors abroad as of May 2019.⁴ Particular sustainable development concerns arise as many of these claims pertain to resource management or environmental protection measures applied to mineral, and oil and gas extraction projects.

Following elections in 2015, Canada’s approach to investment issues is supposed to be guided by a “Progressive Trade Agenda including investment issues.”⁵ Between mid August and late October 2018, the Canadian government held online consultations on how to make its FIPAs more progressive and inclusive,⁶ with the participation of over 350 Canadians.⁷ However, to date there has been no indication from the government about how Canadian FIPAs and FTAs will be “progressive” in anything more than name, as details of the government’s post-consultation intentions remain unavailable.

2. The “Asymmetry Critique” of international investment law

The historical approach to investment agreements is characterized by asymmetry: foreign investors are granted rights unaccompanied by obligations, while host states accept obligations unaccompanied by rights. Yackee provided an illuminating overview of this Asymmetry Critique with a particular focus on corruption.⁸ More recently Viñuales provided a response to the Asymmetry Critique arguing for a modified version thereof and reliance on a tribunal-driven, doctrinal “change of mindset.”⁹

⁴ Mertins-Kirkwood, H, & Smith, B. (2019). *Digging for dividends: The use and abuse of investor–state dispute settlement by Canadian investors abroad*. Ottawa: Canadian Centre for Policy Alternatives. Retrieved from <https://www.policyalternatives.ca/digging-for-dividends>. The work indicates that at least 43 cases have been brought by Canadian investors under treaties other than NAFTA. Meanwhile, according to UNCTAD, 15 arbitrations have been initiated by Canadian investors against the United States alone under NAFTA Chapter 11. See <https://investmentpolicy.unctad.org>

⁵ This terminology has been advanced by diplomats and politicians during the renegotiations of NAFTA (leading to the USMCA or CUSMA), negotiation of CPTPP and, to a certain extent, the inclusion of an MIC in the final text of the CETA.

⁶ See <https://www.international.gc.ca/trade-commerce/consultations/fipa-apie/index.aspx?lang=eng>

⁷ See <https://www.placespeak.com/en/topic/5788-public-consultation-canadas-international-investment-agreements-fipas/#/overview>. IISD played a leadership role in gathering stakeholders to identify ways in which a new Model FIPA could contribute to investment for sustainable development. See IISD. (2018, July). *Developing a progressive agenda for reform of international investment law: Canadian perspectives*. Retrieved from <https://www.iisd.org/library/developing-progressive-agenda-reform-international-investment-law-canadian-perspectives>; IISD. (2018, November). *Commentary: Reply to public consultation on Canada’s international investment agreements (FIPAs)*. Retrieved from <https://iisd.org/library/reply-public-consultation-canadas-international-investment-agreements-fipas>

⁸ Yackee, J. W. (2011). Investment treaties and investor corruption: An emerging defense for host states. *Virginia Journal International Law*, 52, 723.

⁹ Viñuales, J. E. (2017). Investor diligence in investment arbitration: Sources and arguments. *ICSID Review-Foreign Investment Law Journal*, 32(2), 346–370, p. 368.

Speaking to this need for a mindset shift, Llamzon cogently describes a “moral impetus” stemming from the “the need to hold investors seeking redress accountable for their own wrongdoing.”¹⁰ However, he also acknowledges that existing treaties give “comparatively little guidance to arbitrators about how corruption issues should be treated vis-à-vis the protections provided to investors under these treaties.”¹¹

In this context, tribunals draw on a dynamic basket of “implicit obligations”¹² to take account of investor misconduct. *World Duty Free v. Kenya* provides an example.¹³ There the host state alleged at the preliminary stages that the investor had used bribery to secure its investment. The tribunal found that it could not affirm jurisdiction under the relevant investment contract’s arbitration agreements.¹⁴ However, the basic limitation of the International Public Policy (IPP) Approach is that it relies on both the investor and the state being unusually candid about the payment of bribes.

The result of reliance on implicit obligations is described by one practitioner as “[a] lack of clarity with respect to the emerging implicit obligation for investments to accord with the law [that] may leave investors, states, and tribunals with an uncertain understanding as to when the substantive protections of an investment treaty should be denied to an investor.”¹⁵

The tribunal in *Metal-Tech v. Uzbekistan* also had to confront the issue of investor bribery. It relied on an “in accordance with the law” clause in the underlying investment treaty finding that circumstantial evidence—such as “red flags”—was sufficient to establish that bribes had been used to secure the investment.¹⁶ (In both *World*

¹⁰ Llamzon, A. (2015). Yukos Universal Limited (Isle of Man) v The Russian Federation: The state of the ‘unclean hands’ doctrine in international investment law: Yukos as both omega and alpha. *ICSID Review-Foreign Investment Law Journal*, 30(2), 315–325, p. 316.

¹¹ Llamzon, A. P. (2014). *Corruption in International Investment Arbitration* (pp. 238–281). Oxford University Press, para. 4.66.

¹² Llamzon (2015), *supra* note 10. Llamzon refers to implicit obligations for limitations that are thought to exist outside the four corners of the treaty text.

¹³ See Johnson, L. (2011). *World Duty Free v. Kenya*. In N. Bernasconi-Osterwalder & L. Johnson (Eds.). *International investment law and sustainable development: Key cases from 2000–2010*. Geneva: IISD. Retrieved from <https://www.iisd.org/itn/2018/10/18/world-duty-free-v-kenya>

¹⁴ This IPP Approach has a long history in international commercial arbitration: Yackee (2011), *supra* note 8, traces the origin of this doctrine against the use of arbitration to enforce a contract secured corruptly, to Judge Gunnar Lagergren’s 1963 Award in ICC Case No. 1110.

¹⁵ Moloo, R., & Khachaturian, A. (2010). The compliance with the law requirement in international investment law. *Fordham International Law Journal*, 34, 1473, p. 1475.

¹⁶ See Schacherer, S. (2018, October). *Metal-Tech v. Uzbekistan*. In Bernasconi-Osterwalder, N. & Brauch, M. D. (Eds.). *International investment law and sustainable development: Key cases from the 2010s*. Geneva: IISD. Retrieved from <https://www.iisd.org/itn/2018/10/18/metal-tech-v-uzbekistan>



Duty Free and *Metal-Tech* the international tribunals concluded on the facts that there was corrupt behaviour and therefore did not rely on a prior penal outcome in either the host state or the home state.)

It should be noted, however, that many investment treaties do not contain an “in accordance with the law” clause. And, in any case, even if the treaty does contain such a provision, its effectiveness in excluding investments made through corruption is contingent on the law of the host state. The more fundamental point is that, considering that Canadian law prohibits bribery of foreign officials,¹⁷ Canadian FIPAs should also exclude corrupted investments from their ambit of protection regardless of the legal particularities of the host state.

3. Improved treaty language: necessary if incremental progress

Canada has made limited progress in clarifying the unsettled legal landscape discussed above. This section introduces that development alongside other treaty negotiation initiatives.

In the CETA investments made through corruption have been explicitly excluded from dispute settlement. CETA Art. 8.18(3) states:¹⁸

For greater certainty, an investor may not submit a claim under this Section if the investment has been made through fraudulent misrepresentation, concealment, corruption, or conduct amounting to an abuse of process.

This should be cautiously viewed as a step in the right direction. (The language in CETA is yet to be interpreted by an arbitral tribunal.)

However, the Canada–Moldova FIPA and Canada–Kosovo FIPA, signed after CETA was concluded on October 30, 2016, do not include the CETA Art. 8.18(3) language.¹⁹ Although this may at first be surprising, it likely reflects the fact that Canadian negotiators have continued to operate under the prior negotiating template and will

continue to do so until the Model FIPA is updated.²⁰

In the two FIPAs concluded after CETA, the most significant development is outside the treaty text, in the form of a joint declaration,²¹ substantially identical in both cases and silent on the issue of corruption. In the document, the governments “commit to work together to help make international trade and investment policies more progressive and inclusive, to empower all members of society – particularly women, to have a positive impact on economic growth, and help reduce inequality and poverty.” They also reaffirm the right to regulate to achieve legitimate policy objectives and recognize the need to address certain ISDS-related issues.

It is unclear whether and when a new Model FIPA will be published and begin to inform Canada’s negotiations. Also unclear is whether the CETA Art. 8.18(3) language will be brought into a new Model FIPA, or whether the Canadian government—now operating under the banner of a Progressive Trade Agenda—might go even further in using FIPAs to combat corruption.

The Canadian government must ensure that FIPAs begin to establish a minimum standard of investor conduct applicable to Canadian corporations abroad. In this regard the 2012 South African Development Community (SADC) model investment agreement, the 2016 Morocco–Nigeria BIT and the 2018 model BIT of the Netherlands are all noteworthy.

The SADC model formulates a shared obligation regarding corruption that applies to investors, host states and home states. The main obligation thereunder is derived from the United Nations Convention against Corruption (UNCAC) and the OECD Convention’s prohibition approach on bribery. Enforcement of the prohibition is intended to be carried out by domestic authorities, and a breach of the prohibition is intended to have the effect of vitiating any investment tribunal’s

¹⁷ Levine (2019), *supra* note 1, Section 5.0.

¹⁸ CETA, Chapter 8 (Investment), October 30, 2016. Art. 8.18(3). Retrieved from <http://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/ceta-aecg/text-texte/toc-tdm.aspx?lang=eng>

¹⁹ Canada–Moldova FIPA, June 12, 2018 (not in force). Retrieved from <https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/moldova/fipa-apie/text-texte.aspx?lang=eng>; Canada–Kosovo FIPA, March 6, 2018, in force as of December 19, 2018. Retrieved from <https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/kosovo/fipa-apie/text-texte.aspx?lang=eng>

²⁰ On May 25, 2018, Canada and the United Arab Emirates concluded negotiations toward a FIPA. The FIPA text is not currently available. See https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/ united_arab_emirates-emirats_arabes_unis/fipa-apie/background-contexte.aspx?lang=eng

²¹ Joint declaration by the Government of Canada and the Government of the Republic of Moldova regarding progressive and inclusive trade and investment, June 12, 2018. Retrieved from <https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/moldova/fipa-apie/declaration.aspx?lang=eng>; Joint declaration by the Government of Canada and the Government of the Republic of Kosovo, March 6, 2018. Retrieved from <https://international.gc.ca/trade-commerce/trade-agreements-accords-commerciaux/agr-acc/kosovo/fipa-apie/declaration.aspx?lang=eng>



jurisdiction.²² The SADC model's linkage between home state enforcement (that is, retention of sovereign prosecutorial authority over criminal law matters) and exclusion of investment tribunal jurisdiction certainly merits consideration.

The Morocco–Nigeria BIT introduced a series of obligations on investors, including compliance with a rigorous environmental assessment screening and a social impact assessment.²³ What's more, Article 17 (Anti-Corruption) sets out comprehensive rules for prohibiting corrupt payments to an official or an intermediary of an official in the host state.²⁴

Finally, the recently finalized model BIT of the Netherlands²⁵ contains a series of changes aimed at controlling the scope of investment protection and introducing greater guidance as regards investor conduct. In particular, the model follows CETA Art. 8.18(3) and states: "The Tribunal shall decline jurisdiction if the investment has been made through fraudulent misrepresentation, concealment, corruption, or similar bad faith conduct amounting to an abuse of process."²⁶

Conclusion

In the context of the SDGs, Canada's gradual adoption of a diversified approach to combatting cross-border corruption is encouraging. To date, however, there has been only minimal recognition that investments made through corruption or otherwise tainted by corruption must be excluded from the ambit of protection afforded by FIPAs.

This is slowly starting to change, however. In concert with the Asymmetry Critique, there is broader recognition that FIPAs can no longer be devoted only to protection of foreign investors. Following the 2018

consultation on FIPAs, the Canadian government must at a bare minimum publish a new Model FIPA, with binding treaty language excluding protection to investments tainted by foreign bribery and addressing other issues raised by Canadians, and use it to guide the negotiation of "fourth generation" FIPAs. Canada should also seek to renegotiate outdated older-generation FIPAs.

When it comes to bribery of foreign officials, anything less than a continuation of the practice in CETA would be a move in the wrong direction. It would be a betrayal of not only the government's Progressive Trade Agenda rhetoric but also the simple legal fact that Canadian corporations are prohibited by law from paying bribes to officials of foreign countries. In this way, Canada can take a small but concrete step toward balancing the minimum standard of treatment of investors it demands of host states against a minimum standard of investor conduct on the part of Canadian corporations abroad.

Author

Matthew A. J. Levine is a Canadian lawyer (Barrister & Solicitor, Law Society of Ontario). In addition to domestic business law matters, his practice includes design and implementation of anti-corruption anti-bribery (ABAC) compliance programs under the United States Foreign Corrupt Practices Act (FCPA) and Canadian Corruption of Foreign Public Officials Act (CFPOA).

²² SADC. (2012, July). *SADC model bilateral investment treaty template with commentary*. Gaborone: SADC, Arts. 10.1–10.3 and commentary on p. 32. Retrieved from <http://www.iisd.org/itm/wp-content/uploads/2012/10/SADC-Model-BIT-Template-Final.pdf>

²³ Morocco–Nigeria BIT, December 3, 2016, Arts. 14(1) and 14(2). Retrieved from <https://investmentpolicy.unctad.org>

²⁴ *Id.*, Art. 17.

²⁵ For a comprehensive review of the draft text, see Verbeek, B.-J. & Knottnerus, R. (2018, July). The 2018 Draft Dutch Model BIT: A critical assessment. *Investment Treaty News*, 9(2), 3–6. Retrieved from <https://www.iisd.org/itm/en/2018/07/30/the-2018-draft-dutch-model-bit-a-critical-assessment-bart-jaap-verbeek-and-roeline-knottnerus>. The Dutch government adopted the model BIT on October 19, 2018.

²⁶ Netherlands Model Investment Agreement, October 19, 2018, Art. 16(2). Retrieved from <https://www.rijksoverheid.nl/binaries/rijksoverheid/documenten/publicaties/2018/10/26/modeltekst-voor-bilaterale-investeringsakkoorden/modeltekst-voor-bilaterale-investeringsakkoorden.pdf>



INSIGHT 3

Spain's Renewable Energy Saga: Lessons for international investment law and sustainable development

Isabella Reynoso



IAs and the accompanying ISDS regime are often praised as key to promoting FDI in countries and therefore aiding sustainable development. IAs provide foreign investors with broad and vague protections, which are then interpreted and applied by arbitrators through the ISDS regime. Investment arbitrators are therefore vital in defining the relationship between international investment law and sustainable development. Given that the regime provides little to no guidance and accountability for arbitrators, it creates opportunities for treaty protections to be applied inconsistently and arbitrarily. The result is a system tainted with uncertainty that is constraining the policy space of countries and consequently hindering sustainable development. The renewable energy cases against Spain are a prime example of problems that the ISDS regime can present for sustainable development in the energy sector specifically.

Renewable energy arbitrations against Spain: Background and published awards

In 2007 Spain implemented a number of regulatory measures with the purpose of incentivizing investment in renewable energy. However, because of the program's great success, a tariff deficit and the consequences of the financial crisis, Spain implemented a number of measures from 2010 onward, which retracted some features of the original regulations. As a result, approximately 40 arbitrations have been initiated against Spain.¹ The key

issue in the first four final awards publicly issued in these arbitrations involved the application of the FET standard and legitimate expectations.²

*Charanne v. Spain*³, the first award that was published (2016), concerned investors who owned photovoltaic installations in Spain.⁴ They argued that the evolution of the special regulatory framework created instability and lack of clarity which violated their legitimate expectations, contrary to ECT Article 10(1). The tribunal dismissed both claims, ruling in favour of Spain.⁵

In 2017, the tribunal in *Eiser v. Spain* ruled in favour of the investors of three concentrated solar plants.⁶ Unlike in *Charanne*, they argued that a set of later regulations from 2012 to 2014 had breached their rights under the ECT, significantly devaluing their investments and forcing their Spanish subsidiaries into debt restructuring negotiations. The tribunal found in favour of the investors.

*Isolux v. Spain*⁷—decided first, but only published after *Charanne* and *Eiser* became public—was in many respects a sort of companion case to *Charanne*, as it was brought by related investors, involved the same counsel,

² Hendel, C. (2017, July 27). Squaring the circle: Reconciling the conflicting awards in the *Eiser* and *Isolux* Spanish renewable cases (Part I). *Kluwer Arbitration Blog*. Retrieved from <http://arbitrationblog.kluwerarbitration.com/2017/07/27/squaring-circle-reconciling-conflicting-awards-eiser-isolux-spanish-renewable-cases-part/>

³ *Charanne and Construction Investments v. Spain*, SCC Case No. V 062/2012, Award, January 21, 2016. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw7047.pdf>

⁴ *Ibid.*, para 5.

⁵ *Ibid.*, paras. 280, 283–284.

⁶ *Eiser Infrastructure Ltd. and Energia Solar Luxembourg v. Spain*, ICSID Case No. ARB/13/36, Award, May 4, 2017. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw9050.pdf>. See also Schacherer, S. (2018, October 18). *Eiser v. Spain*. In N. Bernasconi-Osterwalder & M. D. Brauch. (Eds.) *International investment law and sustainable development: Key cases from the 2010s*. Retrieved from <https://www.iisd.org/itm/2018/10/18/eiser-v-spain>; Issac, G. (2017, September 26). Investors triumph over Spain in a claim concerning Spain's regulatory overhaul for clean energy. *Investment Treaty News*, 8(3), 17–18. Retrieved from <https://www.iisd.org/itm/2017/09/26/investors-triumph-over-spain-claim-concerning-spains-regulatory-overhaul-for-clean-energy-gladwin-issac>

⁷ *Isolux Netherlands, BV v. Kingdom of Spain*, SCC Case V2013/153, Final Award, July 17, 2016. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw9219.pdf>. See also Arietti Lopez, C. M. (2017, September 26). All claims by Isolux Infrastructure Netherlands against Spain are dismissed. *Investment Treaty News*, 8(3), 13–14. Retrieved from <https://www.iisd.org/itm/2017/09/26/all-claims-by-isolux-infrastructure-netherlands-against-spain-are-dismissed-isolux-infrastructure-netherlands-v-spain-scc-case-v2013-153-claudia-maria-arietti-lopez>

¹ Cosby, A. (2017, April). *Can investor-state dispute settlement be good for the environment?* Retrieved from <http://www.iisd.org/library/can-investor-state-dispute-settlement-be-good-environment>



and each party named the same co-arbitrators. Like in *Eiser*, *Isolux* disputed the 2012–2014 regulations. The investor claimed that Spain attracted its investment with the promise of maintaining a long-term feed-in tariff for the production of photovoltaic energy under a special regime, and that by later abolishing it, it breached ECT Article 10. The tribunal found in favour of Spain.

In February 2018, the tribunal in *Novenergia v. Spain* ordered Spain to pay EUR 53 million to a Luxembourg fund that had invested in photovoltaic plants in Spain.⁸ The claim in *Novenergia* related to the same 2012–2014 reforms as in *Eiser* and *Isolux*.

Although the same reforms sparked the abovementioned disputes, a closer look at the tribunals' interpretation and application of the FET standard in each award reveals the inconsistencies to which the ISDS regime can give rise. The awards shine light on four specific issues, explored in the rest of this essay.

1. Lack of clarity regarding whether an investor has legitimate expectations and, if so, of what

There is no consistent interpretation as to what gives rise to an investor's legitimate expectations that a regulatory framework will remain unchanged. It is true that none of the four awards can be understood to deny the state's right (and duty) to regulate (and re-regulate). Nor do they suggest that a state's right to regulate is limitless. Further, all awards recognize that Spain did have some form of obligation to respect the investor's legitimate expectations. At this point, however, the tribunals differed in their way of proceeding.

In *Charanne*, the investors alleged that the regulatory framework established by Spain prior to the 2008 crisis induced them to invest in Spain and generated the expectation that the terms would not be altered. However, the tribunal found that this framework could not provide legitimate expectations, as the documents were not specific enough. From the *Charanne* award, it can be understood that anything short of a stabilization clause or specific commitment to the

investors specifying that the regulatory framework will remain unchanged will fall short of creating such a legitimate expectation.⁹

In *Novenergia*, contrary to *Charanne*, the tribunal held that such expectations "arise naturally from undertakings and assurances" given by the state (para 650). These do not need to be specific undertakings such as contractual stabilization clauses—state conduct that objectively creates such expectations is sufficient.¹⁰ *Novenergia* was entitled to form legitimate expectations as to the 2007 regime based on statements by officials of Spain's Congress of Deputies, as well as Spain's marketing documents which, the tribunal held, constituted "bait."¹¹

"The discrepancy in the way in which both tribunals approached the analysis of an investor's legitimate expectations makes it difficult for a state to anticipate the boundaries of how statements and advertisements will be scrutinized in the event of a dispute."

Unlike in *Charanne*, however, the *Novenergia* tribunal was referring to the legitimate expectation that the regulations that incentivized the investors would not be *radically* altered. However, it did not distinguish between this test and that articulated in *Charanne*. The *Charanne* decision implies that the legitimate expectation that a state will not act unreasonably or disproportionately when regulating is embedded in the FET standard despite any statements made by a state. The *Novenergia* award seems to apply the analysis in *Charanne* to determine if investors had the right to expect the legislation would not be *radically* altered.

The discrepancy in the way in which both tribunals approached the analysis of an investor's legitimate expectations makes it difficult for a state to anticipate the boundaries of how statements and advertisements

⁸ *Novenergia II - Energy & Environment (SCA) (Grand Duchy of Luxembourg), SICAR v. The Kingdom of Spain*, SCC Case No. 2015/063, Final Arbitral Award, February 15, 2018. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw9715.pdf>. See also Issac, G. (2018, July 30). Luxembourg fund awarded EUR 53.3 million for FET breach arising out of Spain's curtailment of renewable energy incentive schemes. *Investment Treaty News*, 9(2), 28–29. Retrieved from <https://www.iisd.org/itn/2018/07/30/luxembourg-fund-awarded-eur-53-3-million-for-fet-breach-arising-out-of-spains-curtailment-of-renewable-energy-incentive-schemes>

⁹ *Charanne*, *supra* note 3, para. 504.

¹⁰ *Novenergia*, *supra* note 8, para. 650; Power, R. (2018, March 20). *Novenergia v. Kingdom of Spain, the ECT and the ECJ: Where to now for intra-EU ECT claims?* *Kluwer Arbitration Blog*. Retrieved from <http://arbitrationblog.kluwerarbitration.com/2018/03/20/novenergia-v-kingdom-of-spain>

¹¹ *Novenergia*, *supra* note 8, para. 674.



will be scrutinized in the event of a dispute.

2. Different approaches and lack of reasoning on whether Spain's regulatory changes were reasonable

The *Eiser* tribunal generally failed to provide analysis on what the investor's legitimate expectations were or could have been based on the particularities of the case. Instead, the tribunal went straight to considering how Spain could have violated the FET standard regardless of any specific commitments, by virtue of it acting unreasonably when regulating, an issue that the tribunals in *Charanne*, *Isolux* and *Novenergia* also went on to consider.¹² This approach highlights the second issue prevalent in all awards: the lack of consistency when deciding whether Spain's regulatory changes were reasonable.

Each tribunal differed in explaining what they meant by "reasonableness." The *Isolux* tribunal simply stated that the reasonableness standard requires a state's conduct to bear a reasonable relationship to some rational policy.¹³ On the other hand, the *Charanne* tribunal considered the issue in more depth and provided a detailed and quite high threshold. It first stated that it would consider whether Spain's measures were unreasonable, disproportionate or contrary to the public interest.¹⁴ As for proportionality, the tribunal considered that this criterion would be satisfied as long as the changes were not capricious or unnecessary and did not suddenly and unpredictably eliminate the essential characteristics of the existing regulatory framework.¹⁵ In *Novenergia*, however, the tribunal applied a seemingly narrower test, stating that the FET standard protects investors from a "radical or fundamental" change to legislation rather than simply an "unreasonable or disproportionate" change, as was stated in *Charanne*.¹⁶ The tribunal in *Novenergia* failed to define the boundaries of the test it proposed, illustrating yet another source of uncertainty for states. Furthermore, although the tribunal in *Eiser* held that Spain had acted unreasonably and breached the FET, it failed to provide any information on how it was judging the reasonableness of Spain's measures. This explains why Spain has recently applied for annulment of the decision, based on a failure to state reasons and a manifest excess of power.¹⁷

¹² *Eiser*, *supra* note 6, paras. 513–516.

¹³ *Isolux*, *supra* note 7, para. 822.

¹⁴ *Charanne*, *supra* note 3, para. 515.

¹⁵ *Ibid.*, para. 517.

¹⁶ *Novenergia*, *supra* note 8, para. 681.

¹⁷ Power (2018), *supra* note 10.

The tribunals also differed in their analysis of the disputed provisions. The *Eiser* tribunal paid disproportionate attention to the economic impact the regulations had on the investment. It began by distinguishing *Charanne* on the basis that the measures had less dramatic effects for the claimants in *Charanne* (losses of approximately 10 per cent) than in *Eiser* (losses of more than 60 per cent).¹⁸ The *Eiser* tribunal described the negative impact the disputed measures had on the investment for several pages, highlighting that Spain's new measures deprived the claimants of essentially all of the value of their investment.¹⁹

"The second issue prevalent in all awards is the lack of consistency when deciding whether Spain's regulatory changes were reasonable. Each tribunal differed in explaining what they meant by "reasonableness." The tribunals also differed in their analysis of the disputed provisions."

The economic impact of a measure should not be entirely ignored. However, it is an element that is usually considered in expropriation claims and rarely found as an element in the test to establish a breach of the FET standard. The *Eiser* tribunal's decision to ignore the expropriation claim and focus on FET may have led to its overemphasis on the negative impact of the measures and lack of analysis of whether the new measures were reasonable.

3. Inconsistent conclusions of different tribunals considering the very same regulations

The third issue is that *Eiser* and *Isolux* differ in their conclusion as to whether the same provisions were reasonable, and both tribunals fail to provide satisfying reasoning for their conclusions.

In *Isolux*, the tribunal first held that "Spain's conduct was a rational policy which, whether anybody liked it or not, had the aim of protecting the consumer,"²⁰ without providing any further explanation of why that

¹⁸ *Eiser*, *supra* note 6, para. 368.

¹⁹ *Ibid.*, para. 418.

²⁰ *Isolux*, *supra* note 7, para. 823 (translated by the author).



was the case.

In turn, the tribunal in *Eiser* stated that the new system was based on quite different assumptions and used a new and untested regulatory approach, all intended to significantly reduce subsidies to existing plants,²¹ but failed to explain how it was judging the “reasonableness” of the regulatory changes, why it held the new regime as unreasonable and on what its reasoning was based. Its further discussion on whether Spain gave an indication for changing the rate of reasonable return and whether the standard used (which depended on an “efficient” plant) was common or not, fails to provide guidance or clarity.

"Eiser and Isolux differ in their conclusion as to whether the same provisions were reasonable, and both tribunals fail to provide satisfying reasoning for their conclusions."

From this analysis it did not seem that Spain's measures were discriminatory or had been applied in an arbitrary and unreasonable way. At one point, the *Eiser* tribunal recognizes Spain's economic difficulties and accepts it had to implement measures to address its tariff deficit.²² However, it seems to suggest that a more reasonable policy would have been to allow inefficient plants to receive the same rate of return as efficient ones, despite the clear moral hazard this would create.

Whether one agrees with the outcome in either *Eiser* or *Isolux*, the lack of in-depth reasoning in both decisions is unsatisfying, and the resulting discrepancy is worrying.

4. Lack of an appellate mechanism to correct inconsistencies

Although *Charanne* and *Isolux* do provide some guidance on the legitimate expectations question, the dissenting opinion of arbitrator Tawil in both the *Isolux* and *Charanne* awards highlights the significant potential for inconsistency in the current ISDS regime. In *Charanne*, Tawil concurred with the majority on the issue of the tribunal's jurisdiction and shared the view that Spain had not indirectly expropriated

the Claimants' investment. However, he opined that legitimate expectations could be created in other situations where there was no specific commitment.²³ He was of the view that the original scheme was designed to incentivize investors and was directed to a specific group of investors, and that this was sufficient to show legitimate expectations on the part of the claimants.²⁴ On that basis, he thought it did not seem legally acceptable to recognize the host state's prerogative to modify or eliminate the benefit without providing compensation.²⁵ He dissented on the same grounds in *Isolux*.

"Whether one agrees with the outcome in either Eiser or Isolux, the lack of in-depth reasoning in both decisions is unsatisfying, and the resulting discrepancy is worrying."

Indeed, dissenting opinions in judicial decisions are very common and in most cases relate to some of the most complex and ambiguous aspects of the law. However, the worrying aspect of Tawil's dissent is that, unlike most judicial disputes, awards in the ISDS regime are not confined by precedent or the accountability imposed by the ability to appeal a decision. Tawil's opinion shows that, were the tribunal constituted by another arbitrator of similar views, the decisions in *Charanne* and *Isolux* would have swung in the opposite direction. There is no way a state can anticipate such possibility at the time of instituting regulatory changes.

Is ISDS compatible with sustainable development?

Although no conclusive lessons can be derived from these awards, they do highlight some of the main issues present in the current ISDS regime. Its ad hoc nature makes it extremely difficult for states to anticipate when trying to regulate and re-regulate

²¹ *Eiser*, *supra* note 6, para. 391.

²² *Ibid.*, para. 371.

²³ *Charanne and Construction Investments v. Spain*, SCC Case No. V 062/2012, Dissenting Opinion of Prof. Guido Santiago Tawil, January 21, 2016, p. 4-5.

Retrieved from https://www.italaw.com/sites/default/files/case-documents/italaw7048_0.pdf

²⁴ *Ibid.*, p. 9.

²⁵ *Ibid.*, p. 11.



on vital policy issues. As a result of the uncertainty and arbitrariness surrounding the interpretation of vital standards in the ISDS regime, there is a risk of so-called regulatory chill: states may shy away from regulatory changes when considering the risk of costly and embarrassing arbitration.²⁶ This is deadly for states pursuing sustainable development goals, which requires states to be able to regulate freely.

"International processes such as UNCITRAL Working Group III on ISDS reform should be seized as opportunities to foster the cooperation of all stakeholders in developing solutions for the issues identified in the ISDS regime and ensuring that it does not hinder states' right to regulate to achieve sustainable development objectives."

Several stakeholders have argued that the best way to counteract those issues is by instituting a single investment court or tribunal that could determine particular legal standards applicable to similar cases.²⁷ This would allow states to easily establish a benchmark for their regulatory changes, and investors would be able to anticipate in what cases their losses could be compensated. In its recent FTAs, the EU has moved away from ad hoc investment arbitration toward an ICS mechanism, composed of a first instance tribunal and an appeal tribunal.²⁸ The EU also has directives to negotiate a convention establishing a MIC,²⁹ which it has been advocating in

the context of the UNCITRAL Working Group III on ISDS reform.³⁰

Establishing a MIC may be an attractive solution to the flaws of the current ISDS regime, by resolving a number of procedural issues such as transparency and accountability as well as ensuring the development of clear legal standards that can be applied consistently in similar cases. However, any MIC proposal would have to address controversial issues such as how costs will be allocated, how judges will be appointed and how the interests of all relevant investment stakeholders will be represented. Developing countries are already dissatisfied with the ISDS regime due to its exorbitant costs, impartiality and legitimacy concerns. Therefore, a MIC that balances the flexibility needed to satisfy all stakeholders while still offering the predictability that the current ISDS regime is lacking will not come into being without significant difficulty.

International processes such as UNCITRAL Working Group III on ISDS reform should be seized as opportunities to foster the cooperation of all stakeholders—including governments, communities and individuals, and investors³¹—in developing solutions for the issues identified in the ISDS regime and ensuring that it does not hinder states' right to regulate to achieve sustainable development objectives.

Author

Isabella Reynoso holds an LL.M. in International Legal Studies from NYU and an LLB from King's College London. She will begin her Training Contract at White & Case London in September 2019.

²⁶ IISD. (2012). *Investment treaties and why they matter to sustainable development: Questions and answers*. Winnipeg: IISD. Retrieved from <https://www.iisd.org/library/investment-treaties-and-why-they-matter-sustainable-development-questions-and-answers>

²⁷ See, for example, Van Harten, G. (2008, September 1). Commentary: A case for an international investment court. *Investment Treaty News*. Retrieved from <https://www.iisd.org/itn/2008/08/07/commentary-a-case-for-an-international-investment-court>

²⁸ ITN. (2015, November 26). Investment Court System proposed by European Commission. *Investment Treaty News*, 6(4), 12. Retrieved from <https://www.iisd.org/itn/2015/11/26/investment-court-system-proposed-by-european-commission>

²⁹ ITN. (2018, April 24). Council of the European Union adopts negotiating directives: EU Commission to negotiate a convention establishing a multilateral investment court. *Investment Treaty News*, 9(1), 13. Retrieved from <https://www.iisd.org/itn/2018/04/24/council-of-the-european-union-adopts-negotiating-directives-eu-commission-to-negotiate-a-convention-establishing-a-multilateral-investment-court>

³⁰ Brauch, M. D. (2018, December 21). Multilateral ISDS reform is desirable: What happened at the UNCITRAL meeting in Vienna and how to prepare for April 2019 in New York. *Investment Treaty News*, 9(4), 4–7. Retrieved from <https://iisd.org/itn/en/2018/12/21/multilateral-isds-reform-is-desirable-what-happened-at-the-uncitral-meeting-in-vienna-and-how-to-prepare-for-april-2019-in-new-york-martin-dietrich-brauch>

³¹ IISD. (2017, March). *Reply to the European Commission's public consultation on a multilateral reform of investment dispute resolution*. Winnipeg: IISD. Retrieved from <https://www.iisd.org/library/reply-european-commission-s-public-consultation-multilateral-reform-investment-dispute>



INSIGHT 4

Investment Facilitation at the WTO: An attempt to bring a controversial issue into an organization in crisis

Sofía Baliño and Nathalie Bernasconi-Osterwalder



Out of the WTO's 164 members, 70 have formally signed on to so-called “structured discussions” aimed at identifying what issues and elements could form a basis for a multilateral framework for investment facilitation that they could present at the 12th Ministerial Conference in Kazakhstan in June 2020. The members involved in this effort plan to wrap up the latest phase of their work by the end of July 2019, which has been devoted to reviewing concrete examples of different investment facilitation issues that members raised throughout last year. These structured discussions have brought investment back into the limelight, a subject that has a long and complex history, but has only recently re-emerged within the WTO context.

We describe how the investment facilitation debate has evolved in the WTO, from the early days of investment as a so-called “Singapore issue” to the 11th Ministerial Conference in Buenos Aires in December 2017 and the structured discussions that have unfolded since.

1. From Singapore to Cancún: The failed attempts to develop multilateral rules on investment at the WTO

When the WTO replaced the GATT system in January 1995, it already had in its rules some limited provisions relating to investment, including those incorporated in the General Agreement on Trade in Services (GATS) and featured throughout the Agreement on Trade-Related Investment Measures (TRIMs). At the WTO's first-ever ministerial conference in Singapore

in 1996, members set up working groups devoted to the relationship between trade and investment, trade and competition policy, transparency in government procurement, and trade facilitation.¹

These Singapore issues were later brought into the 2001 Doha Ministerial Declaration, which launched the Doha Round, where members were due to negotiate reforms on agriculture, non-agricultural market access, services, and various other items while placing developing country members’ “needs and interests at the heart” of this work.² Along with adopting this Doha work program, ministers agreed that negotiations on these Singapore issues would begin after their Fifth Session. The paragraphs in the Doha Declaration on investment refer to “the case for a multilateral framework to secure transparent, stable and predictable conditions for long-term cross-border investment, particularly foreign direct investment, that will contribute to the expansion of trade, and the need for enhanced technical assistance and capacity-building in this area.”^{1,2}

Ultimately, that “Fifth Session” turned into the 2003 Cancún Ministerial, one of the most high-profile collapses in the WTO's history, which fell apart partly due to severe disagreement over whether to launch negotiations on the Singapore issues, and if so which ones. After days of round-the-clock negotiations, ministers were unable to agree on a declaration or other consensus statement when the meeting closed.³ The July 2004 meeting of the WTO General Council dropped all the Singapore issues except for trade facilitation, which was incorporated into the Doha Round.⁴

This was not the only effort underway to negotiate a multilateral agreement on investment. Negotiations

¹ WTO. (1996). *Singapore Ministerial Declaration*. Retrieved from https://www.wto.org/english/thewto_e/minist_e/min96_e/wtodec_e.htm

² WTO. (2001). *Doha Ministerial Declaration*. Retrieved from https://www.wto.org/english/thewto_e/minist_e/min01_e/mindecl_e.htm#tradeinvestment

³ Bridges Daily Update. (2003, September 15). *Cancun collapse: When there's no will there's no way*. Retrieved from <https://www.ictsd.org/bridges-news/bridges/news/bridges-daily-update-6-cancun-collapse-where-theres-no-will-theres-no-way>

⁴ WTO. (2004). *The July 2004 package*. Retrieved from https://www.wto.org/english/tratop_e/dda_e/dda_package_july04_e.htm



on such an accord had previously taken place at the OECD, which would have also involved the participation of non-OECD countries, but ultimately were abandoned in 1998.⁵

While investment was dropped as a WTO negotiating issue in 2004, the international landscape on investment protection and liberalization continued to evolve through BITs and other treaties with investment provisions. These treaties and associated ISDS regimes now face intense criticism and calls for reform.

More recently, the subject of investment facilitation has gained attention as another aspect of investment law and policy. Investment facilitation is at the centre of Brazil's innovative investment treaty model developed in 2015, which has since served as the basis for various agreements that the South American country has negotiated with other partners.⁶ Investment facilitation is also integrated in the work of several international organizations, such as UNCTAD, the OECD, and the World Bank.⁷ In 2016, UNCTAD released its Global Action Menu on Investment Facilitation.⁸

2. New attempts to include investment in the WTO via investment facilitation

Investment started re-emerging as an area of interest for some WTO members, initially within two coalitions: MIKTA (Mexico, Indonesia, South Korea, Turkey, and Australia) and the Friends of Investment Facilitation for Development (FIFD), which involved various developing country members. These two groups convened informal meetings and workshops throughout 2017 on whether and how the WTO could be a place for considering “measures that Members could take to facilitate investment.”⁹

⁵ See Drabek, Z. (1998). *A multilateral agreement on investment: Convincing the sceptics*. Retrieved from https://www.wto.org/english/res_e/reser_e/pera9805.doc; OECD. *Multilateral agreement on investment*. Retrieved from <https://www.oecd.org/investment/internationalinvestmentagreements/multilateralagreementoninvestment.htm>

⁶ See Martins, J. H. V. (2017). Brazil's cooperation and facilitation investment agreements (CFIA) and recent developments. *Investment Treaty News*, 8(2), 10–12. Retrieved from <http://www.iisd.org/itn/2017/06/12/brazils-cooperation-facilitation-investment-agreements-cfia-recent-developments-jose-henrique-vieira-martins>; Bernasconi-Osterwalder, N., & Brauch, M. D. (2015). *Brazil's innovative approach to international investment law*. Geneva: IISD. Retrieved from <https://www.iisd.org/blog/brazils-innovative-approach-international-investment-law>

⁷ See Zhang, J. (2018, July). *Investment facilitation: Making sense of concepts, discussions and processes*. Geneva: IISD. Retrieved from <https://www.iisd.org/library/investment-facilitation-making-sense-concepts-discussions-and-processes>

⁸ UNCTAD. (2017, May). *Global action menu for investment facilitation*. Geneva: UNCTAD. Retrieved from <https://investmentpolicy.unctad.org/publications/148/unctad-global-action-menu-for-investment-facilitation>

⁹ WTO. (2017, April 21). *Proposal for a WTO informal dialogue on investment facilitation for development*. Retrieved from https://docs.wto.org/dol2fe/Pages/FE_Search/FE_S_S009-DP.

That effort led to the adoption of a Joint Ministerial Statement on Investment Facilitation for Development at the 11th Ministerial Conference in Buenos Aires at the end of 2017, with 70 members announcing the launch of “structured discussions with the aim of developing a multilateral framework on investment facilitation.” To address some members’ concerns about an attempt to develop multilateral rules on investment liberalization and protection, the group clarified that this work would exclude market access, investment protection and ISDS.¹⁰

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While the exclusion of ISDS seems straightforward, the delineation between investment facilitation on the one hand and market access and protection on the other is blurry at best, so that the distinction would be hard to implement. Indeed, some issues that are already being considered in this context, and which could lead to potential disciplines, such as mandatory time limits for government decisions on the admission of proposed investments, go directly to market access questions and the ability of governments to evaluate proposed investments effectively before making decisions.

These structured discussions are not formal negotiations, given that launching negotiations on new issues within the WTO requires consensus from the entire membership, as stated in the 2015 Nairobi

¹⁰ WTO. (2017, December 13). *Joint ministerial statement on investment facilitation for development*. Retrieved from https://docs.wto.org/dol2fe/Pages/FE_Search/FE_S_S009-DP.

The sponsors listed on the joint statement included Argentina, Australia, Benin, Brazil, Cambodia, Canada, Chile, China, Colombia, Costa Rica, El Salvador, the European Union, Guatemala, Guinea, Honduras, Hong Kong, Japan, Kazakhstan, South Korea, Kuwait, Kyrgyz Republic, Lao People's Democratic Republic, Liberia, Macao, Malaysia, Mexico, Moldova, Montenegro, Myanmar, New Zealand, Nicaragua, Nigeria, Pakistan, Panama, Paraguay, Qatar, Russian Federation, Singapore, Switzerland, Tajikistan, Togo and Uruguay.



Ministerial Declaration.¹¹ Still, even the exclusion of the most contentious issues from the structured discussions was insufficient to convince the remaining 94 WTO members to join at that stage.

The structured discussions aim primarily to identify a set of issues and elements within the areas listed in the joint statement, namely on how to ensure “transparency and predictability of investment measures; streamline and speed up administrative procedures and requirements; and enhance international cooperation, information sharing, the exchange of best practices, and relations with relevant stakeholders, including dispute prevention.”⁷

Throughout 2018, participants in the joint initiative met regularly to discuss issues that could be considered within the broader areas described in the Buenos Aires statement.¹² This led to the preparation of an 81-item checklist of issues for further examination and potential inclusion in a multilateral framework. Despite claims that the discussions are fully transparent, the full list has been kept out of public scrutiny to date.^{13, 14} Participants have since been looking at and compiling concrete examples of investment facilitation measures that are featured in the checklist, looking to finalize this stage by the end of July.¹⁶

The ongoing work of the joint initiative on investment facilitation should not obscure how openly controversial the initiative is among the wider WTO membership, with several—such as Eswatini, the Gambia, India, South Africa, Uganda, and Zimbabwe¹⁵—arguing that this issue falls outside the WTO’s mandate and that any negotiation on new issues will, as stated in Nairobi, require consensus from the full membership and could have major systemic implications. Several members, particularly some developing country members, have warned that the energy devoted to new issues could

distract from advancing negotiations on priority issues from the original Doha agenda.¹⁶

The proponents of investment facilitation in the WTO appear to look towards the success in negotiating the Trade Facilitation Agreement (TFA) as proof that the global trade body’s members can and should use it as inspiration when negotiating on certain “new issues”—even when the TFA’s context may not apply. The TFA is the only full-fledged multilateral agreement adopted since the WTO’s creation, though it too required about a decade of negotiation.¹⁷

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Upon closer consideration, the parallels between trade and investment facilitation—besides the obvious similarities in name, and the shared background in terms of the Singapore issues—are limited in theory and practice. Trade facilitation involves what happens to goods as they cross national borders, with TFA measures focused on issues such as the release and clearance of goods. Investment facilitation, by comparison, goes well beyond border issues and relates to the establishment and subsequent operation of an enterprise, potentially involving a wide range of regulatory issues as diverse as environment, labour, consumer protection, competition, transportation, anti-corruption, taxation, health, and safety, among others.¹⁸ The TFA experience therefore is an inappropriate anchor for promoting the investment facilitation discussions.

¹¹ WTO. (2015, December 19). *Nairobi Ministerial Declaration*. Retrieved from https://www.wto.org/english/thewto_e/minist_e/mc10_e/minddecision_e.htm

¹² WTO (2018, 2-4 October). *WTO public forum: Trade 2030: Working session 29, Investment facilitation for development*. Session notes taken on site, supporting audio available online at <https://www.wto.org/audio/pf18session29.mp3>.

¹³ Graduate Institute, German Development Institute (2019, May 23). *A multilateral framework on investment facilitation*. Retrieved from <https://www.die-gdi.de/en/events/details/a-multilateral-framework-on-investment-facilitation>.

¹⁴ WTO. (2019). *Informal dialogue on investment facilitation for development*. Retrieved from https://www.wto.org/english/thewto_e/acc_e/ifd_feb2019_v1.pdf

¹⁵ See statements available at https://www.wto.org/english/thewto_e/minist_e/mc11_e/mc11_plenary_e.htm

¹⁶ WTO. (2017, July 21). *Minutes of the meeting held in the Centre William Rappard on 10 and 18 May 2017*. Retrieved from https://docs.wto.org/dol2fe/Pages/FE_Search/DDFDocuments/237843/q/WT/GC/M167.pdf

¹⁷ WTO. (2014). *Bali package and November 2014 decisions*. Retrieved from https://www.wto.org/english/thewto_e/minist_e/mc9_e/balipackage_e.htm#trade_facilitation

¹⁸ Brauch, M. D., Mann, H., and Bernasconi-Osterwalder, N. (2019, January). *SADC-IISD investment facilitation workshop: Report of the meeting held August 21–23, 2018 in Johannesburg, South Africa*, pp. 4–5. Geneva: IISD. Retrieved from <https://iisd.org/library/sadc-iisd-investment-facilitation-workshop>



3. Investment facilitation and international investment governance

The history above indicates that launching investment negotiations in the WTO would face tremendous challenges and risk using up resources that could be better spent in other, more urgent areas. Launching negotiations on investment would also risk splitting the WTO membership further at a time when trade multilateralism is already in crisis. But it is not only for these reasons that we believe that governments should refrain from embarking on investment facilitation negotiations. The WTO is about developing binding *disciplines* to regulate trade. But the issue of investment facilitation at the international level should focus instead on better understanding needs, developing cooperative structures and building capacity. There are few, if any, empirical studies on what has been successful and what is needed to facilitate investment, and even less so on facilitating investment for sustainable development, which inherently requires government decision-making powers to be exercised.¹⁹ Rather than imposing requirements to set up one-stop shops or consultation processes for instance, states should benefit from technical support from specialized international agencies, such as UNCTAD²⁰ and the OECD, to facilitate investment for sustainable development purposes through informed, innovative and efficient decision-making processes.

Furthermore, the international community should ask whether introducing binding multilateral rules on the narrow issue of investment facilitation at the WTO could lead to duplication and further fragmentation of international investment governance. No other area of international economic law has developed in a fashion as piecemeal as investment. There are investment protection rules in BITs and FTAs; investment liberalization in regional agreements, BITs and FTAs; investment dispute settlement in UNCITRAL, ICSID, BITs, FTAs and other treaties with investment provisions; international investment policy oversight, dialogue, and capacity building at UNCTAD; investment promotion and facilitation support at

UNCTAD, OECD and the World Bank; and business and human rights and responsible business conduct at the Office of the United Nations High Commissioner for Human Rights (OHCHR) and OECD. In addition, investment for sustainable development is intrinsically linked to the SDGs under Agenda 2030.

"Reflections on investment facilitation should form one aspect of broader discussions on international investment governance. These should take place through an inclusive, open, and publicly accessible process and result in creative solutions on how specialized institutions can best coordinate and collaborate to achieve the overarching objective of investment for sustainable development."

Instead of rushing into disciplines in an organization that lacks the necessary substantive expertise on investment and has struggled to fulfil the sustainable development part of its mandate through its rule-making efforts, states should consider how to best structure international investment governance to advance sustainable development. Reflections on investment facilitation would form one aspect of such broader discussions on international investment governance. These should take place through an inclusive, open, and publicly accessible process, likely in the United Nations but in partnership with other relevant organizations outside the UN, such as the WTO and the OECD, and result in creative solutions on how specialized institutions can best coordinate and collaborate to achieve the overarching objective of investment for sustainable development.

Authors

Sofía Baliño is a media and communications officer with a background in trade journalism working in the Economic Law and Policy Program at IISD. **Nathalie Bernasconi-Osterwalder** leads the Economic Law and Policy Program at IISD and is Executive Director of IISD Europe in Geneva.

¹⁹ UNCTAD. (2015). *Investment policy framework for sustainable development*. Retrieved from <https://investmentpolicy.unctad.org/publications/149/unctad-investment-policy-framework-for-sustainable-development> Note that the UNCTAD action items on investment facilitation are not suggested as potential legal obligations but are meant rather for promoting effective decision-making.

²⁰ Brauch, M. D. (2017, December). *A risky tango? Investment facilitation and the WTO Ministerial Conference in Buenos Aires*. Geneva: IISD. Retrieved from <https://www.iisd.org/library/risky-tango-investment-facilitation-and-wto-ministerial-conference-buenos-aires>



INSIGHT 5

The Kenyan Parliament and Investment Treaty Making

Bosire Nyamori



Background

For decades, the Kenyan government concluded BITs without parliamentary oversight. This is now changing. The Constitution of Kenya 2010 introduces greater democratization of the treaty-making process and practice by requiring parliamentary scrutiny and public participation in the approval process.

However, parliament has used its oversight powers more in the breach than in the observance. For instance, although the country has ratified seven BITs since the constitution came into force,¹ there is little, if any, evidence of parliamentary involvement in the process.

The recent High Court of Kenya's decision in *Tax Justice Network—Africa v. Cabinet Secretary for National Treasury & 2 others*² (*TJN-A Case*) held that parliament's scrutiny and approval is not necessary for Kenya to conclude double taxation treaties (DTTs). This further serves to diminish public awareness and accountability in the process.

The decision is a setback for greater democratization of the treaty-making process and practice envisaged in the Kenyan constitution. In this article, I discuss the

adverse ramifications the decision has for the treaty-making process in a broad spectrum of policy areas, including BITs.

Pre-2010 Parliament and treaty policy and practice

Before the 2010 constitution, the country was governed by the 1969 constitution, which contained no express provision for treaty making and implementation. Its Section 23 vested executive authority in the president, and there was implicit understanding that treaty-making powers fell under this purview.

As a former British colony, the country followed the British system under which treaty making is a function of the executive, and a treaty is not part of Kenyan law unless and until it has been incorporated into the law by legislation.³ The Court of Appeal in *Okunda v. Republic*⁴ endorsed this approach, saying that “the provisions of a treaty entered into by the Government of Kenya do not become part of the municipal law of Kenya save in so far as they are made such by the law of Kenya.”

When the country embarked on the process of rewriting the constitution, there were suggestions from the public that “Parliamentary approval should be sought before the Executive gives consent to any treaty.”⁵ This was intended to enhance public accountability and transparency in entering into treaties, as opaqueness and secrecy have serious ramifications for the country's social, economic and political architecture.

On the investment front, poorly designed and implemented BITs with ISDS mechanisms can produce expensive bills and constrain policy and regulatory processes. They increase risks of litigation and give developed countries more rights and powers, among other challenges and problems they pose. Indeed, three different companies have so far sued the government,

¹ National Treasury. (2019). *Investment promotion and protection agreements*. Retrieved from <http://treasury.go.ke/investment-promotion-and-protection-agreements.html>

² High Court of Kenya. Petition No. 494 of 2014. Judgment, March 15, 2019. [2019] eKLR. Retrieved from <http://kenyalaw.org/caselaw/cases/view/169664>

³ Constitution of Kenya Review Commission. (2005). *The Final Report*. p. 149. Retrieved from <http://kenyalaw.org/kl/fileadmin/CommissionReports/The-Final-Report-of-the-Constitution-of-Kenya-Review-Commission-2005.pdf>

⁴ *Okunda v. Republic* [1970] E.A. 453, p. 460.

⁵ Constitution of Kenya Review Commission, *supra* note 3, p. 155



challenging a range of policy decisions and regulatory measures. Public awareness and scrutiny could help mitigate the adverse consequences.

Post-2010 Parliament and treaty policy and practice

The 2010 constitution came into force on August 27, 2010. It has wide-ranging implications for a broad swathe of the country's economic, social and political governance. Treaty making and treaty policy are no exception.

Article 2(6) of the constitution specifies: "Any Treaty or convention ratified by Kenya shall form part of the law of Kenya under this Constitution." The Treaty making and Ratification Act⁶ implements Article 2(6) of the constitution, setting out procedures for making and ratification of treaties.

The national executive is responsible for initiating, negotiating, signing and ratifying treaties.⁷ When initiating a treaty-making process, the national executive is required to consider several variables, including the costs of formulating and adopting the treaty. If the government decides to proceed with the treaty process, the Cabinet Secretary, in consultation with the Attorney-General, must submit the text of the treaty for cabinet approval. After cabinet approves a treaty, the Cabinet Secretary must then table this in parliament.⁸ As part of its approval process, parliament must facilitate public consultation.⁹

The reformed treaty-making process has now been in place for over five years. During this time, Kenya extended its network of IIAs. The new BITs include agreements with Japan, South Korea, Mauritius, Turkey and the United Arab Emirates. The BITs with Japan and South Korea are in force.

Also, Kenya has had to contend with two investment disputes. In *Cortec Mining v. Kenya*,¹⁰ the tribunal held that environmental impact assessment is mandatory for anyone considering investment and thereby dismissed the

claimant's case that the cancellation of a special mining licence breached the Kenya–United Kingdom BIT.¹¹ The award in favour of Kenya was rendered on October 22, 2018, but on March 19, 2019 ICSID registered the claimants' application to annul the award; the annulment proceedings are pending at the time of writing.¹²

In an ongoing contract-based arbitration case, *WalAm Energy Inc v. Republic of Kenya*,¹³ the claimant has sued the government at ICSID for USD 600 million as compensation for the cancellation of the geothermal prospecting licence. The government contends that the claimant lacked the wherewithal to explore geothermal resources. While this claim was brought under a contract, similar cases have also been brought to ICSID under treaties in the past, demonstrating the types of risks inherent to international investment arbitration more generally.

Yet it is striking that the parliament has not taken note of these developments or sought to interrogate the law and policy that is giving rise to these huge claims. Its role is little more than perfunctory, mechanically passing investment treaties with virtually no scrutiny even as these instruments have gradually expanded in scope—and arguably shifted in purpose.

Parliament's role in the process is not meant to be perfunctory and mechanical. Rather, it is meant to enhance public awareness and improve democratic accountability. After all, parliament represents the sovereignty of the people. After the passing the 2010 constitution, the executive's treaty-making power was constrained by the need for legislative approval and thus an intentionally greater democratization of the treaty-making power, one expressly driven by notions of popular sovereignty.

The TJN-A Case and implications for investment treaty making

The Kenya–Mauritius DTT was published by the Cabinet Secretary for Treasury on May 23, 2014 through Legal Notice 59 of 2014. In the *TJN-A Case*, the High

⁶ Act No. 45 of 2012 (Treaty Making and Ratification Act, 2012). Retrieved from <http://kenyalaw.org/lex/actview.xql?actid=No.%2045%20of%202012>

⁷ Ibid, Section 4(1).

⁸ Ibid, Section 8.

⁹ Ibid, Section 8(3).

¹⁰ Lin, X. (2018). Kenya prevails in BIT arbitration: British investors' claims dismissed due to the absence of environmental impact assessment. *Investment Treaty News*, 9(4), 19–20. Retrieved from <https://www.iisd.org/itn/en/2018/12/21/kenya-prevails-in-bit-arbitration-british-investors-claims-dismissed-due-to-the-absence-of-environmental-impact-assessment-xiaoxia-lin>

¹¹ *Cortec Mining Kenya Limited, Cortec (Pty) Limited and Stirling Capital Limited v. Republic of Kenya*, ICSID Case No. ARB/15/29, Award, October 22, 2018, Retrieved from <https://www.italaw.com/cases/3974>

¹² *Cortec Mining Kenya Limited, Cortec (Pty) Limited and Stirling Capital Limited v. Republic of Kenya (ICSID Case No. ARB/15/29)*. Retrieved from <https://icsid.worldbank.org/en/Pages/cases/casedetail.aspx?CaseNo=ARB/15/29>

¹³ *WalAm Energy Inc. v. Republic of Kenya*, ICSID Case No. ARB/15/7. Retrieved from <https://icsid.worldbank.org/en/Pages/cases/casedetail.aspx?CaseNo=ARB/15/7>



Court of Kenya invalidated the DTT on the basis that the legal notice, which gives effect to the tax treaty, was not tabled before parliament as required by the Statutory Instruments Act.¹⁴

It is possible that if a BIT had been the subject of litigation in the *TYN-A Case* instead of a DTT, the court would have arrived at the same conclusion, given that tax treaties and BITs have one stated purpose in common—seeking, in their own ways, to increase and attract foreign investments. However, both DTTs and BITs have important monetary impacts for states. In fact, the impact of BITs on the national budget tends to be even greater, because they subject the state to binding international arbitration, which often involves significant monetary risks. Accordingly, the risks involved in both types of treaties—and in BITs in particular—justify and recommend parliamentary scrutiny.

Even though the decision ultimately invalidated the DTT on procedural grounds, several conclusions of the court significantly limit parliament’s role in taxation (and possibly investment) treaty making and policy. First, the court held that parliamentary approval was not required for approval of tax treaties and that public participation was ostensibly unnecessary. The court stated that “[t]he Constitution is clear that there must be public participation when enacting law, but the question that lingers on is what public participation is and what the process is,” and agreed with the respondent that “there is need for creation of legislation to guide the process of public participation” (para. 35 of the judgment).

In arriving at this position, the court disregarded constitutional and legislative measures without giving any plausible explanation. Section 8 of the Ratification and Treaty Making Act enjoins parliament to facilitate public participation, while Section 6 says the executive is bound by the values and principles of the constitution when negotiating treaties. Under Article 10 of the constitution, the values and principles that government organs must observe in policy and legislative processes include public participation.

Second, the court ruled that tax treaties are not subject to the Ratification and Treaty Making Act because they deal with government business as well as technical, administrative or executive matters. Section 3(4) allows the government to negotiate bilateral agreements

“necessary for matters relating to government business” or “relating to technical, administrative or Executive matters,” without following the framework set out in the act, but gives no guidance as to the meaning of these terms.

This lack of clarity is problematic because it may give government officers room to argue that BITs are entered into for “government business” and, as a result, are not subject to scrutiny. As argued above, however, parliamentary scrutiny of investment treaties is constitutionally required given the significant monetary risks they pose.

Looking to the future

It is now axiomatic that the conducting of international relations must be in conformity with Kenya’s 2010 constitution, which intends that the treaty-making power be democratized through legislative approval and public participation. Yet to date the Kenyan Parliament has played little more than a perfunctory role in the adoption of investment treaties.

The Kenyan government has announced that it is reviewing investment treaties with a view to safeguarding national interests, as well as developing an investment treaty model and a policy on international investment negotiations.¹⁵ As the government continues to review Kenya’s investment treaty-making policy and approach to ensure it advances sustainable development, parliament, too should seize the opportunity to ensure that investment treaties ratified by Kenya are well understood by the public and promote the country’s interests and development goals. This will only make Kenya’s negotiating position stronger.

Author

Bosire Nyamori is teaches tax law and international investment law at the University of Nairobi and practices tax law and commercial law with Ogetto, Otachi & Co. Advocates.

¹⁴ Act No. 23 of 2013 (Statutory Instruments Act, 2013). Retrieved from <https://www.ecolex.org/details/legislation/statutory-instruments-act-2013-no-23-of-2013-lex-faoc122294>

¹⁵ See, for example, KenInvest. (2018). *Kenya hosts 11th Annual Forum of Developing Countries Investment Negotiators*. Retrieved from http://invest.go.ke/wp-content/uploads/2018/02/KenInvest-Press-Release-Annual_Forum-7-2-18.pdf; Kariuki, J. (2018). Global mining firms sue Kenya for Sh334bn compensation. *Business Daily*. Retrieved from <https://www.businessdailyafrica.com/corporate/companies/Global-mining-firms-sue-Kenya-for-Sh334bn-compensation/4003102-4295742-d8c86gz/index.html>; Ngila, D. (2018). Global mining firms sue Kenya for \$3.2 billion compensation. *The East African*. Retrieved from <https://www.theeastafrican.co.ke/business/mining-firms-sue-Kenya-compensation/2560-4296070-hi7wmr/index.html>



INSIGHT 6

Investor Due Diligence and the Energy Charter Treaty

Yulia Levashova



At the end of 2018, the Subgroup on Modernization of the Energy Charter Conference agreed on a list of topics to be considered in the process of ECT modernization.¹ Next, the subgroup will identify the policy options for each topic; negotiations based on these will start sometime in 2019. Among the topics identified for modernization are the definition of FET and the right to regulate.

This article discusses the implications of the current ECT formulation of FET for the interpretations of this standard adopted by recent tribunals in renewable energy cases. It focuses on the assessment of the stability requirement provided for in ECT Article 10(1), on the one hand, and the state's regulatory flexibility on the other. In particular, it looks into whether a requirement of investor due diligence, as one of the options in reforming the FET standard under the ECT, could help rebalance investors' right to "stability" and states' right to change their laws.

1. The requirement of stability under the ECT: Cases against Spain

The FET standard under the ECT is one of the most commonly invoked provisions, and the ECT itself is the

most frequently invoked IIA in investment arbitration.² Currently, ECT Article 10(1) is formulated in an unqualified and open manner, committing host states to provide FET "at all times to Investments and Investors." This formulation is typical of older-generation IIAs. ECT Article 10(1) also includes the obligation of stability, providing that states shall "encourage and create stable, equitable, favourable and transparent conditions for Investors."

The wave of investment arbitrations in the renewable energy sector exemplifies foreign investors' reliance on the FET and stability provisions under the ECT.³ Spain is the most frequent respondent state in renewable energy disputes and is currently facing 36 arbitrations.⁴ In the cases against Spain, investors have argued that drastic alterations of the Spanish regulatory framework for renewable energy frustrated their legitimate expectations derived from the ECT obligation of stability.

The changes to the regulatory regime were motivated by an increasing electricity tariff deficit. The deficit resulted from the difference between the subsidies (feed-in tariffs) granted by Spain to renewable energy producers and the tariffs paid by consumers. The situation worsened because of the global economic crisis between 2008 and 2014.⁵ In response to the tariff deficit and the crisis, Spain implemented several regulatory measures between 2010 and 2014, transforming the regime of subsidies for renewable energy producers. Several affected investors initiated ECT claims.⁶

² International Energy Charter. (2019, January 11). *The Energy Charter Treaty (ECT) remains the most frequently invoked IIA*. Retrieved from <https://energycharter.org/media/news/article/the-energy-charter-treaty-ect-remains-the-most-frequently-invoked-ia>

³ Spain, Italy, Czech Republic that reformed their renewable energy policies are currently facing the multiple claims under the ECT and in some cases under BITs. Draguiev, D. (2018). Investment treaty arbitration in the renewable energy sector: Overview of arbitral case law on legitimate expectations in the light of policy. *Oil, Gas & Energy Law Journal (OGEL)*, 16(5).

⁴ At the time of writing, 36 arbitrations refer to pending renewable energy cases against Spain. See <https://investmentpolicy.unctad.org>

⁵ Bank of Spain. (2017). *Report on the financial and banking crisis in Spain, 2008-2014*. Madrid: Bank of Spain. Retrieved from https://www.bde.es/f/webbde/Secciones/Publicaciones/OtrasPublicaciones/Fich/InformeCrisis_Completo_web_en.pdf

⁶ In de Braekt, M., & Geldhof, W. (2017, July 19). Mixed results in recent arbitral awards concerning Spain's renewable energy policy. *Stibbe Blog, Lexology*. Retrieved from <https://www.lexology.com/library/detail.aspx?g=d384a0ee-31cf-4411-8898-adc714c414b6>; Power, R., & Baker, P. (2018, April 10). The European arbitration review 2018 – Energy arbitrations. *Clyde&Co*. Retrieved from <https://www.clydeco.com/insight/article/the-european-arbitration-review-2018-energy-arbitrations>

¹ International Energy Charter. (2018). *Approved topics for the modernisation of the Energy Charter Treaty*. Retrieved from <https://energycharter.org/media/news/article/approved-topics-for-the-modernisation-of-the-energy-charter-treaty>; see also the Bucharest Energy Charter Declaration, signed on November 28, 2018. Retrieved from <https://energycharter.org/media/news/article/energy-charter-conference-adopts-the-bucharest-declaration>



2. State's right to change its laws versus the obligation to provide stability

The central issue in concluded cases against Spain—*Charanne v. Spain*, *Eiser v. Spain*⁷, *Isolux v. Spain*⁸ and *Antin v. Spain*⁹—was the extent to which the host state can exercise its right to regulate by changing its laws without violating FET.¹⁰ The tribunals assessed this issue by balancing the stability obligation under ECT Article 10(1) against the state's right to change its laws.

In all four cases, the tribunals affirmed the legitimate right of the state to regulate to remedy the tariff deficit problem, emphasizing that Spain had the right to change its laws to overcome financial difficulties.¹¹ One of the central criteria in the tribunals' assessments of regulatory stability was whether the change was disproportionate in view of its impact on the investments. The tribunals indicated that the changes must be consistent with the "public interest, economic reasonableness and the principle of proportionality."¹² They specified that a state's regulatory measure is considered disproportionate when it amounts to a "sudden and unpredictable elimination of the essential characteristics of the existing framework."¹³ However, the tribunals had different views on what constitutes such an elimination.

⁷ Schacherer, S. (2018, October 18). *Eiser v. Spain*. In N. Bernasconi-Osterwalder & M. D. Brauch. (Eds.) *International investment law and sustainable development: Key cases from the 2010s*. Retrieved from <https://www.iisd.org/itm/2018/10/18/eiser-v-spain>; Issac, G. (2017, September 26). Investors triumph over Spain in a claim concerning Spain's regulatory overhaul for clean energy. *Investment Treaty News*, 8(3), 17–18. Retrieved from <https://www.iisd.org/itm/2017/09/26/investors-triumph-over-spain-claim-concerning-spains-regulatory-overhaul-for-clean-energy-gladwin-issac>

⁸ Arietti López, C. M. (2017, September 26). All claims by Isolux Infrastructure Netherlands against Spain are dismissed. *Investment Treaty News*, 8(3), 13–14. Retrieved from <https://www.iisd.org/itm/2017/09/26/all-claims-by-isolux-infrastructure-netherlands-against-spain-are-dismissed-isolux-infrastructure-netherlands-v-spain-scc-case-v2013-153-claudia-maria-arietti-lopez>

⁹ Menon, T. (2018, October 17). Spain found to have breached the Energy Charter Treaty in award by ICSID tribunal. *Investment Treaty News*, 9(3), 23–24. Retrieved from <https://www.iisd.org/itm/2018/10/17/spain-found-to-have-breached-the-energy-charter-treaty-in-award-by-icsid-tribunal-trishna-memon>

¹⁰ Matteoti, S. & Payosova, T. (2017). The role of fair and equitable treatment standard: Regulatory coherence for trade and investment in renewable energy. In T. Cottier & I. Espa (Eds.). *International trade in sustainable electricity*. Cambridge: Cambridge University Press.

¹¹ *Antin Infrastructure Services Luxembourg S.à.r.l. and Antin Energia Termosolar B.V. v. Kingdom of Spain*, ICSID Case No. ARB/13/31, Award, June 15, 2018, para. 555. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw9875.pdf>; *Eiser Infrastructure Ltd. and Energia Solar Luxembourg v. Spain*, ICSID Case No. ARB/13/36, Award, May 4, 2017, para. 371. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw9050.pdf>; *Isolux Netherlands, BV v. Kingdom of Spain*, SCC Case V2013/153, Final Award, July 17, 2016. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw9219.pdf>; *Charanne Construction v. Spain*, SCC Case No. 062/2012, Award, January 21, 2016, paras. 500 and 536. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw7047.pdf>

¹² *Charanne Construction v. Spain*, *supra* note 11, para. 514; *Eiser v. Spain*, *supra* note 11, para. 370.

¹³ *Charanne Construction v. Spain*, *supra* note 11, para. 517.

In *Eiser* and *Antin*, the tribunals adopted a broad interpretation of the stability requirement, stressing that the "obligation to accord [FET] necessarily embraces the obligation to provide fundamental stability in the essential characteristics of the legal regime relied upon by investors in making long-term investments."¹⁴ Through this prism, these tribunals primarily focused on the impact of the regulatory change on the investors.¹⁵

"In *Charanne v. Spain*, *Eiser v. Spain*, *Isolux v. Spain* and *Antin v. Spain*, the tribunals affirmed the legitimate right of the state to regulate to remedy the tariff deficit problem, emphasizing that Spain had the right to change its laws to overcome financial difficulties."

For the *Charanne* and *Isolux* tribunals, however, the issues addressed were whether the presence of the specific representations had led to legitimate expectations on the part of investors regarding regulatory stability.¹⁶ In a more restrictive interpretation of the state's duty to ensure the stability of the regulatory framework, the tribunals emphasized that investors must comply with their due diligence obligations in order to be able to claim the protection of their (legitimate) expectations.

3. Implications of the divergent interpretations of the stability requirement under FET

The discrepancy among the cases against Spain concerning the interpretation of the FET standard and specifically the notion of stability is problematic on different counts.

First, there is a lack of predictability and consistency as to how the state's right to regulate is weighed against the notion of stability. There is no clear understanding of how tribunals value the relevant considerations in

¹⁴ *Eiser v. Spain*, *supra* note 11, para. 382. *Antin v. Spain*, *supra* note 11, para. 532.

¹⁵ *Eiser v. Spain*, *supra* note 11, paras. 362 and 365; *Antin v. Spain*, *supra* note 11, para. 532.

¹⁶ *Charanne Construction v. Spain*, *supra* note 11, paras. 499 and 504; *Isolux Netherlands, BV v. Kingdom of Spain*, *supra* note 11, paras. 764 and 775.



assessing the FET standard. For example, as illustrated by the cases discussed above, in weighing the economic circumstances concerning the tariff deficit challenge against investors' rights under the FET standard, tribunals have adopted different views on the role of these circumstances in assessing the question of whether they could justify the disputed state measures.

The *Charanne* tribunal, in evaluating whether the 2010 reforms were in the public interest, concluded that the measures of the Spanish authorities constituted legitimate public policies and had been adopted to “limit the deficit and price increases.”¹⁷ The special circumstances in the host state were one of the main considerations to support the decision of the tribunal that the host state had not breached the FET standard.

The *Eiser* tribunal also acknowledged the tariff deficit as a legitimate public policy problem. However, the tribunal placed less significance on this factor, by expressing the view that Spain, in dealing with the tariff deficit challenge, should still be able to comply with FET under the ECT.¹⁸ To balance the state's right to change its laws with its duty to provide certain degree of stability, a tribunal should compare the impact of a regulatory change on an investor with other factors, such as the economic and socio-political circumstances of the change and the investor's due diligence.

Second, the notion of stability in ECT Article 10(1) does not reflect the current evolution of the investment policy landscape. Many states have undertaken efforts to reform the FET standard in their IIAs. The approaches towards FET adopted in recent IIAs vary significantly. The different approaches include: (1) an omission of the FET standard from the treaty altogether;¹⁹ (2) clarification of the content of the FET standard, with a list of the state's obligations and an exclusion of the obligation of stability from the scope of the treaty;²⁰ and (3) an elimination of

protection of legitimate expectations.²¹

Accordingly, different avenues could be considered to rebalance stability and regulatory flexibility of the FET standard in a modernized ECT. This piece focuses on the approaches recently adopted by the EU, given that the EU and all of its member states (with the exception of Italy) form the majority of the state parties to the ECT. Therefore, ECT modernization is more likely to follow the approach taken in EU treaties.

"There is a lack of predictability and consistency as to how the state's right to regulate is weighed against the notion of stability. There is no clear understanding of how tribunals value the relevant considerations in assessing the FET standard."

Recent EU IIAs continue to include the FET standard, but attempt to narrow it down by excluding the requirement of stability from the scope of the treaty. The CETA, the EU–Singapore FTA and the EU–Vietnam FTA, for example, provide for the state's right to regulate and specify that the “mere fact” of a change to the regulatory framework in a “manner which negatively affects an investment or interferes with an investor's expectations” does not amount to a breach of investment obligations under the agreement.²² However, this formulation does not exclude the possibility that, in combination with other facts—for example, manifest arbitrariness, one of the possible grounds for the violation of FET under CETA Art. 8.10(2)(c)—a change to a regulatory framework could play a role in a tribunal's assessment

¹⁷ *Charanne Construction v. Spain*, *supra* note 11, para. 514; *Eiser v. Spain*, *supra* note 11, para. 536.

¹⁸ *Eiser v. Spain*, *supra* note 11, para. 371.

¹⁹ Government of India. (2015). *Model text for the Indian bilateral investment treaty*. Retrieved from http://indianbusiness.nic.in/newdesign/upload/Model_BIT.pdf; see Treaty Between the Republic of Belarus and the Republic of India on Investments, September 24, 2018. Retrieved from <https://investmentpolicy.unctad.org>; see also Brazil's Cooperation Facilitation Investment Agreements (CFIAs) concluded since 2015. Retrieved from <https://investmentpolicy.unctad.org>

²⁰ Recent EU IIAs have adopted such approach to FET. See: Comprehensive Economic and Trade Agreement, Canada–European Union, October 30, 2016. Retrieved from [https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:22017A0114\(01\)](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:22017A0114(01)) [hereafter “CETA”]; Free Trade Agreement between the European Union and the Republic of Singapore, October 15, 2018. Retrieved from <https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=COM%3A2018%3A0196%3AFIN> [hereafter “EU–Singapore FTA”]; Draft Free Trade Agreement between the European Union and the Socialist Republic of Viet Nam. Retrieved from <https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1551257348905&uri=CELEX:52018PC0691> [hereafter “EU–Viet Nam FTA”].

²¹ In some recent treaties, states clarified that the “mere” violation of the legitimate expectations will not violate the said treaty. See: Agreement between the United States of America, the United Mexican States, and Canada, November 30, 2018, Article 14.6. Retrieved from <https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/agreement-between>; and the Free Trade Agreement between the United States and the Republic of Korea, June 30, 2007, revised as of January 1, 2019, Article 11.5(4). Retrieved from https://ustr.gov/sites/default/files/uploads/agreements/fta/korus/Chapter_Eleven_Investment.pdf

²² CETA, *supra* note 20, Article 8.9 (2); EU–Singapore FTA, *supra* note 20, Article 2.2(2); see also, with slightly different formulation, EU–Viet Nam FTA, *supra* note 20, Article 13 bis (2).



of whether the legitimate expectations of an investor were frustrated.

Therefore, treaty language in recent EU IIAs reduces to some extent the host state's risk of incurring liability under the FET standard, when it changes its regulatory framework. However, it does not provide clear criteria for determining the extent of regulatory change that may lead to liability. One such criterion could be the inclusion of a due diligence obligation in the treaty.

4. Investor's due diligence as a yardstick in assessing the stability requirement

Should the FET and stability language be maintained in a modernized ECT, adding an obligation of due diligence of the investor as a condition for the protection of its legitimate expectations could help balance the rights and obligations of states and investors under the FET standard. Numerous tribunals have underlined that an investor bears the responsibility of appraising the reality and the context of the state where the investment is being made by performing due diligence and risk assessments.²³ The investor must be aware of and take into account the relevant policies and regulations concerning its investment in order to anticipate possible risks.²⁴

"The inclusion of an FET standard that leaves open the door to legitimate expectations remains inherently unpredictable due to the subjectivity of the concept. Only a diligent investor, performing a proper assessment of the laws and regulations in a host state and potential changes, should be able to rely on the specific representations under the FET standard."

This is especially relevant for cases in which the legitimate expectations claim is based on the changes to a general regulatory framework. The extent of an investor's due diligence investigation can operate as a yardstick in judging whether the contested changes could have been predicted by an investor. Only if the changes were not foreseeable by a prudent investor,²⁵ despite visible efforts to collect the information about the future of the regulatory framework, would the legitimate expectations of the investor be protected under the treaty.

While the inclusion of an FET standard that leaves open the door to legitimate expectations remains inherently unpredictable due to the subjectivity of the concept, the inclusion of a requirement for investors to undertake due diligence in order to benefit from FET would at least provide some additional clarification: only a diligent investor, performing a proper assessment of the laws and regulations in a host state and potential changes, would be able to rely on the specific representations under the FET standard. From the perspective of balancing the rights of the investor and the state's right to regulate, such a reference could also strengthen the importance of investors' responsibilities in international investment law.

Author

Dr. Yulia Levashova is an Assistant Professor at Nyenrode Business University and an Associate Research Fellow at Utrecht University. She is an investment law consultant to UNCTAD in Geneva. The opinions expressed in this article are solely those of the author and do not reflect views of affiliated organizations.

²³ *Mamidoil Jetoil Greek Petroleum Products Société S.A. v. Republic of Albania*, ICSID Case No. ARB/11/24 Award, March 30, 2015. Retrieved from <https://www.italaw.com/sites/default/files/case-documents/italaw4228.pdf>; *Charanne Construction v. Spain*, *supra* note 11.

²⁴ *Charanne Construction v. Spain*, *supra* note 11, para. 505.

²⁵ *Isolux Netherlands, BV v. Kingdom of Spain*, *supra* note 11, para. 781.



NEWS IN BRIEF

UNCITRAL Working Group III: July 15 deadline for submissions on proposed reform solutions

Delegates involved in the [UNCITRAL Working Group III](#) process on multilateral ISDS reform have until July 15, 2019 to submit to the UNCITRAL Secretariat their reform proposals and the timing for when such items may be considered in an overarching project schedule. That schedule would help guide the working group under Phase 3 of its mandate, which is devoted to crafting solutions to ISDS-related concerns.

The July 15 deadline was one of the agreed outcomes of the [April 2019 meetings](#) of the working group, held in New York. The working group [agreed](#) that it would “discuss, elaborate and develop multiple potential reform options simultaneously,” using the project schedule as a core component of coordinating work across these parallel tracks. One track would focus on structural reforms, while the other would involve other types of solutions.

The project schedule will be developed during the working group’s Vienna session, currently slated for October 14–18, 2019. That meeting would also serve as an opportunity to examine the reforms proposed in the July submissions, along with developing these ideas further.

The April 2019 meetings also addressed the topic of [third-party funding](#), with the working group agreeing that reforms were needed “to address concerns related to the definition, and to the use or regulation” of this type of financial support in the context of ISDS arbitration.

The working group also examined a set of “[other concerns](#)” to see whether any should be added to those previously identified at other sessions.

Among the possible “other concerns” raised in April were alternative options for resolving disputes or preventing them; requirements for investors to exhaust local remedies before resorting to arbitration; the participation of third parties, such as the general public or local communities; the possibility of states or third parties to lodge counterclaims; the potential for regulatory chill from ISDS; and issues with arbitral tribunals’ calculation of damages.

In all instances, the working group decided not to add

these to the existing list of concerns that have been identified in Phase 2 of its discussions. The reason for this decision, the working group said, is that these issues involve tools for addressing concerns, rather than serving as concerns themselves, and that some of these issues could fall within the scope of previously identified concerns.

EU Commission proposes negotiating directives for ECT modernization

The EC released on May 14 a set of [draft negotiating directives](#) setting out its proposed approach in “modernizing” the [Energy Charter Treaty \(ECT\)](#).

The ECT is an agreement among over 50 contracting parties that has been in force since 1998 that aims to foster improved international cooperation on [energy](#) in areas such as investment protection and international trade. In October 2017, the Energy Charter Strategy Group created a Subgroup on Modernization to discuss the potential update of the ECT, seizing the opportunity of the 2019 review provided for in Article 34.7 of the treaty.

In November 2018, the ECT’s governing and decision-making body adopted the “[Bucharest Declaration](#).” The Energy Charter Conference, as this body is known, said that modernizing the ECT is “essential to properly address developments in the energy sector, especially in light of the rapid changes that have occurred in recent years,” along with reflecting updated standards related to investment protection and revised rules on transit.

The Energy Charter Conference also approved at that time the [list of topics](#) that they would address in the modernization effort, including several investment provisions, following [consultations](#) with ECT observer states and the energy industry. Formal negotiations are expected to begin in 2019.

The EC’s proposed directives for these negotiations still require the endorsement of the Council, meaning that these could change. The EC argues that the ECT’s investment protections “do not correspond to modern standards as reflected in the EU’s reformed approach on investment protection,” and stresses that this discrepancy



should be the focus of upcoming negotiations.

The EC adds that these negotiations should not cover any provisions on pre-investment, but if they do come up in the talks, then the ECT's dispute settlement terms should not apply.

Brussels is calling for the ECT to incorporate a "right to regulate" provision, along with revising its existing terms on expropriation, which among other changes would be "appropriately defined to clarify the nature of indirect expropriation." Other areas where the EC is calling for clearer standards for investor and investment protections include MFN and national treatment provisions, FET and denial of benefits.

On the subject of sustainable development and corporate social responsibility, the EC argues that the ECT should "include provisions on sustainable development, including on climate change and clean energy transition," and that its contracting parties should also undertake commitments on transparency and responsible business conduct that would help ensure that human rights and internationally recognized labour standards are respected.

Also notable in the EC's proposal is the recommendation that any ECT modernization efforts on ISDS hold off until after the process to revise the ICSID arbitration rules and discussions on the EU's proposed MIC have "deliver[ed] tangible results."

AfCFTA enters into force; Phase II on investment, competition, IPRs to last through 2020–2021

The African Continental Free Trade Area (AfCFTA) entered into force on May 30, 2019, with the first phase of the deal taking effect for 24 countries. An extraordinary summit on the trade agreement is planned for July 7, 2019 in Niamey, Niger, while Phase II negotiations on intellectual property rights (IPRs), investment and competition policy are expected to take at least another year.

According to the [African Union \(AU\) Commission](#), as of early June there have been 24 instruments of ratification deposited for the AfCFTA. The minimum for entry into force was 22. Of the AU's 55 countries, 52 have signed the agreement, with the [exceptions](#) being Benin, Eritrea and Nigeria.

The AfCFTA aims to establish "a single market for

goods, services, facilitated by movement of persons in order to deepen the economic integration of the African continent," according to its [final text](#). The agreement also states as an objective the "sustainable and inclusive socio-economic development, gender equality and structural transformation of the State Parties."

Other objectives include eventually developing a customs union spanning the continent's countries; slashing tariffs and removing non-tariff barriers; and improving intra-country cooperation in investment, IPR, customs and trade facilitation, competition policy and other trade-related areas.

The text now in force does not yet include tariff schedules for goods, nor does it have completed schedules for services, which are both still under negotiation.

As part of the Phase II negotiations, the countries involved are now looking to negotiate protocols on investment, competition and intellectual property rights. Further details on what may feature in those documents may become clearer after the terms of reference for the related working groups are issued. [Expert meetings](#) on the investment protocol were held in November 2018 and February 2019.

Niger President Mahamadou Issoufou [recommended](#) to the AU earlier this year that they extend to June 2020 a previous January 2020 deadline for concluding negotiations on the investment, competition and IPR protocols. The AU Assembly [subsequently said](#) that the draft legal text for those protocols should be submitted by January 2021 for the assembly's adoption.

CJEU finds ICS in Canada–EU CETA to be in line with EU law

The CJEU has deemed that the ICS included in the Canada–EU CETA is consistent with EU law, issuing its final opinion on April 30, 2019.

The CJEU opinion is binding and was issued nearly two years after [Belgium asked](#) for the bloc's highest court to examine whether the ICS would affect the "autonomy of the EU legal order." In other words, it asked whether ICS tribunals would be able to weigh in on matters relating to EU law beyond what is included in CETA. Belgium also asked the CJEU to consider whether the ICS upholds the EU's general principle of equality and "practical effect" and whether it ensures that Canadian investors, including small and medium-sized enterprises (SMEs), are able to access an independent tribunal.



On all three questions, the court found that the ICS mechanism's design and safeguards were such that they would not infringe on EU law in any of the areas raised by Belgium.

"CETA does not confer on the envisaged tribunals any jurisdiction to interpret or apply EU law other than that relating to the provisions of that agreement," the court said. According to the court, any ICS tribunal would be unable to "call into question the choices democratically made within a Party" on core public policy objectives, such as health, safety and environmental protections. On the access issue, the court referred to the pledges made by two of the EU institutions—the Council and Commission—to support SMEs' ability to access these tribunals.

A prior, [non-binding opinion](#) by Yves Bot, an Advocate General of the CJEU, had also said that the ICS was compatible with EU law.

The CJEU opinion was welcomed by European Commission officials, who noted that this would make it easier for EU member states to ratify CETA. That is an ongoing process that is necessary for the ICS to take effect, as well as the provisions on investment protection and market access involving portfolio investments. Aside from those areas, CETA is being provisionally applied in Canada and the European Union.

"One of the key pledges in the political guidelines I presented for this Commission in 2014 was to not accept that the jurisdiction of courts in the EU member states is limited by special regimes for investor disputes. We delivered on that with the Investment Court System," said European Commission President Jean-Claude Juncker in response to the CJEU opinion.

Juncker added that the opinion validated the EU's approach to incorporate the new ICS in its recent investment negotiations, as well as its plan to push for these in subsequent agreements in lieu of the "notorious ISDS."

Mexican Senate Ratifies USMCA

The Mexican Senate [approved](#) the implementing legislation for the USMCA on June 19, 2019, by an overwhelming majority of 114 votes in favour, with less than a dozen against or abstaining.

The vote came just over a week after Mexican President Andrés Manuel López Obrador announced the extraordinary Senate session for the vote on [replacing NAFTA](#) with the USMCA.

The USMCA negotiations [wrapped up](#) in September 2018, just over one year after the three countries began formal talks to [update NAFTA](#). The leaders of the three countries involved signed the deal in late November 2018. Among the notable changes to the 1994 NAFTA text was [the revised ISDS language](#). The changes would [limit the application of ISDS](#) only to disputes involving Mexico and the United States and outline which types of claims investors can make under that provision.

The USMCA needs to be ratified by all three signatories, after which three months will need to pass before the agreement's [entry into force](#). The Mexican process is currently the most advanced.

The office of the Canadian Prime Minister submitted [Bill C-100](#) to the Canadian House of Commons on May 29, 2019, which would be the implementing legislation for the USMCA in Canada. A first reading was held that day, followed by a second reading on [June 11, 2019](#). The implementing legislation still needs to undergo several further steps, including being approved in both the Canadian House of Commons and Senate, before ratification is complete in that country.

U.S. Vice President Mike Pence [said in May](#) that the White House is hoping for Congress to ratify USMCA promptly, ideally completing that process before the end of the summer. The Office of the U.S. Trade Representative (USTR) has already sent a draft statement of administrative action on the USMCA, which Speaker of the House Nancy Pelosi said in late May [was premature](#).

"We all agree that we must replace NAFTA, but without real enforcement mechanisms we would be locking American workers into another bad deal," said Pelosi, adding that the Democratic Party, which holds a majority in the House, has "been on a path to yes." Under the [U.S. Constitution](#), any legislation that involves the raising of government revenue, including trade agreements, must begin in the U.S. House of Representatives before being voted on in the Senate.

China, EU leaders announce 2020 target for investment deal

Leaders from China and the EU have pledged to finalize negotiations for their Comprehensive Investment Agreement next year, announcing their target date and further details about the process during a summit in Brussels, Belgium, on April 9, 2019.



European Council President Donald Tusk, European Commission President Jean-Claude Juncker and Chinese Premier Li Keqiang issued a [joint statement](#) outlining various objectives for the negotiations, naming “liberalization commitments” as a priority area for 2019 discussions.

Beijing and Brussels launched formal negotiations on the proposed investment agreement in 2013 and confirmed [its scope](#) in 2016. They have held 20 rounds to date, with the latest [taking place](#) in February 2019. That round included talks on market access offers, ISDS, state-state dispute settlement and language involving sustainable development. The 21st negotiating round is slated for June, though technical talks were planned for early April and are also expected in May.

The China-EU investment negotiations are being conducted as a standalone process, which was a [notable first](#) for the European Commission at the time that talks were launched. The two sides are not currently negotiating an FTA, though European Commission officials have [previously said](#) that the results of the investment discussions could help determine whether to pursue a trade agreement with Beijing, among various other factors.

Leaders said in Brussels this April that they hope to see an “ambitious” investment agreement, including a “balanced investment protection framework” as well as better market access terms than are currently in place. They have announced a “stocktaking” for their next leaders’ level summit, though the dates for this meeting have not been publicly announced.

They also established a “political mechanism” to regularly track the negotiations and provide an assessment of the negotiating state of play before 2020.

Australia inks new BIT with Uruguay, trade and investment deals with Hong Kong

Australia has signed a new BIT with Uruguay and an investment deal with Hong Kong. The agreements feature some changes or clarifications to past deals’ provisions on ISDS and on government regulations designed to fulfill public policy objectives, such as health.

The new Uruguay agreement, on taking effect, would terminate the [2001 BIT](#), while overriding that agreement’s duration, termination and survival clauses. The new BIT, signed in April 2019, [includes](#)

[preambular language](#) on the states’ right to regulate and flexibility to “set legislative and regulatory priorities.” Its exceptions article notes that “nothing in this Agreement shall be construed so as to prevent a Party from adopting or enforcing measures” essential for certain public policy objectives.

Australia’s new [investment agreement](#) with Hong Kong, signed in March 2019, has a dedicated article on “investment and environmental, health and other regulatory objectives.” Parties will not be precluded from pursuing “any measure otherwise consistent with this agreement” that aims at ensuring that investments are “sensitive to” certain public policy objectives. It features exceptions articles similar to the Australia-Uruguay BIT.

Once the new Australia-Hong Kong investment agreement is in force, the prior Australia-Hong Kong BIT will immediately be terminated. The [original BIT](#) has a 15-year survival clause. Under the new agreement, existing investments would be covered under the original BIT’s terms for 10 years from the date of entry into force of the new BIT.

Both treaties have drawn the attention of investment watchers, particularly over whether they would adapt their wording around ISDS and the right to regulate following the investment disputes that emerged under the existing Australian and Uruguayan BITs on involving tobacco plain packaging and control measures. Australia and Uruguay also have a shared history in pursuing these and related public health measures.

In November 2011, Philip Morris launched a case under the Australia-Hong Kong BIT, [claiming](#) that Australia’s Plain Packaging Act amounted to an expropriation of its intellectual property and led to the company’s Australian investments to lose much of their “real value.” An arbitral tribunal [dismissed the case on jurisdictional grounds](#) in December 2015. Australia has also faced complaints [at the WTO](#) and [under its own constitution](#) over the plain packaging legislation.

Uruguay is also a long-time proponent of tobacco control, including through plain packaging. While these measures were challenged by Philip Morris in 2010, the case was [ultimately dismissed](#) and the tobacco giant was ordered to cover some of Uruguay’s legal fees, along with all costs of the arbitration itself.



AWARDS AND DECISIONS

Claims against Albania dismissed by ICSID tribunal as the Anglo-Adriatic Group did not have a protected investment

Anglo-Adriatic Group Limited v. Republic of Albania, ICSID Case No. ARB/17/6

Pietro Benedetti Teixeira Webber

An ICSID tribunal decided that it had no jurisdiction to rule on the claims brought against Albania by Anglo-Adriatic Group (AAG), a company incorporated in the British Virgin Islands. The arbitrators issued the award on February 7, 2019.

Background and claims

The company Anglo Adriatika Investment Fund (AAIF) was created in 1996 to participate in Albania's post-Soviet privatization process. Half of its shares were owned by four non-Albanian shareholders, while an Albanian citizen owned the remaining half.

In the same year, AAG was registered in the British Virgin Islands with the main business purpose to hold shares in the AAIF. AAG maintained that it made two investments: first, the foreign shareholders had declared in 1996 to hold their shares in trust for AAG, providing it with the beneficial ownership in AAIF (First Investment); second, AAG had given loans to AAIF (Second Investment).

AAG alleged that Albania prevented AAIF from participating in the privatization process, indirectly expropriating AAIF's value and treating it in a discriminatory manner compared to other foreign and domestic investors. In December 2016, AAG initiated the arbitration based on Albania's Law No. 7764 (Law on Foreign Investments), which provides for ICSID arbitration.

In the award, the arbitrators addressed two issues: (1) whether AAG owned the First Investment and (2) whether the Second Investment qualified as a protected investment under the Law on Foreign Investments.

AAG did not own shares in AAIF

AAG argued that it had made a protected investment by receiving beneficial ownership of the shares held by the foreign shareholders in 1996.

The tribunal applied a three-step test to assess whether it had jurisdiction to hear the case: (1) whether a protected investment existed; (2) whether a protected investor existed; and (3) whether the protected investor owned the protected investment. The burden of proof of the compliance with these requirements lay with AAG, following the reasoning of *Phoenix Action v. Czechia*.

According to the arbitrators, AAG proved the existence of AAIF and its foreign-owned shares, as well as the capital contribution, thus fulfilling the first requirement. In addition, it concluded that AAG established that it was a legal person constituted in accordance with the laws of a foreign country, qualifying as a protected investor. However, it found that AAG did not comply with the last requirement, as it did not prove that it was the owner or titleholder of the foreign-owned shares.

AAG alleged that the shares had been transferred through four trust deeds governed by English law. The tribunal defined a common law trust as "a legal relationship created by a 'settlor' by which assets [...] are placed in the ownership of a 'trustee' for the benefit of a 'beneficiary'" (para. 226). When analyzing these documents, the arbitrators verified that AAG appeared both as settlors and beneficiaries. Thus, the trust deeds did not support AAG's position that the foreign shareholders transferred beneficial ownership of their shares to AAG.

Furthermore, the tribunal considered that Albanian Law No. 7979 (Law on Investment Funds) required transfers of shares to be registered with the authorities within 10 days, and that the identity of the shareholders had to be reported every quarter. Even so, there was no evidence that either AAIF or AAG had informed the authorities of the alleged transfer of the foreign-owned shares.

Finally, the arbitrators found that there was no proof that AAG had paid the appropriate consideration to the foreign shareholders in exchange for the transfer. Relying on *KT Asia v. Kazakhstan*, they held that an investor who had not paid any consideration is not entitled to investment protection.

Therefore, the tribunal concluded that AAG failed to prove that the foreign shareholders transferred ownership of their shares or that AAG paid any consideration in exchange for the shares. Thus, it held that AAG did not own the First



Investment and that the tribunal had no jurisdiction.

AAG did not make a protected investment

AAG also alleged it had made a protected investment, since it had loaned AAIF USD 5,334,133 in order to cover its operating expenses. To prove the existence of the loans, AAG produced a document named “Ongoing Funding Agreement” and a spreadsheet regarding AAIF’s operating expenses.

The tribunal revisited the three-step inquiry and concluded that AAG failed to prove the first requirement—the existence of a protected investment. The arbitrators found that the Ongoing Funding Agreement merely stated the possibility of supplying loans in the future; it did not prove that AAG actually provided money to AAIF. Moreover, according to the tribunal, the spreadsheet of operating expenses also did not prove how or when AAG covered the costs. Furthermore, the tribunal considered that it would be easy for a company that provides a loan of more than USD 5 million to produce convincing evidence of the money transfer.

Regardless of the failure to prove the loans’ existence, the tribunal held that only investments made in accordance with Albanian law qualify as protected foreign investments under the Law on Foreign Investments. However, it noted that Albanian law in force when the investment had allegedly been made prohibited investment funds such as AAIF from receiving any type of loans or borrowing money. Hence, the loans AAG allegedly made to AAIF would have been made in breach of Albania’s Law on Investment Funds.

The arbitrators concluded that AAG did not make a protected investment, because it did not prove the loans allegedly provided to AAIF and because, even if proved, the investment would have been made in breach of Albanian law.

Decision and costs

The tribunal concluded that AAG did not own shares in AAIF and did not otherwise make a protected investment under the Albanian Law on Foreign Investments. Hence, ICSID had no jurisdiction and the tribunal had no competence to rule on the claims submitted by AAG.

The arbitrators relied on ICSID Convention Article 61(2) and ordered AAG to bear all arbitration costs. However, considering that AAG’s claims were not

unreasonable, it decided that each party should bear its own legal costs and expenses.

Notes: The arbitrators were Juan Fernández-Armesto (presiding arbitrator appointed by the co-arbitrators, Spanish national), Georg von Segesser (claimant’s appointee, Swiss national) and Brigitte Stern (respondent’s appointee, French national). The award of February 7, 2019 is available at <https://www.italaw.com/sites/default/files/case-documents/italaw10349.pdf>

Pietro Benedetti Teixeira Webber is a lawyer at Judith Martins-Costa Advogados (Porto Alegre, Brazil). He is also the President of the Brazilian Association of Arbitration Students (ABEARb).

ICSID tribunal finds Spain breached ECT obligations by failing to provide a reasonable rate of return

RREEF Infrastructure (G.P.) Limited and RREEF Pan-European Infrastructure Two Lux S.a r.l. v. Kingdom of Spain, ICSID Case No. ARB/13/30

Gregg Coughlin

On November 30, 2018, an ICSID tribunal determined that Spain breached the ECT by retroactively applying a new tax regime and failing to ensure RREEF Infrastructure (G.P.) Limited (RREEF) earned a reasonable rate of return on its solar investments.

Background and claims

In 2007, Spain implemented several laws governing its renewable energy (RE) power generation sector, including Royal Decree (RD) 661/2007. RD 661/2007 guaranteed above-market payments to operators in the RE industry by providing a feed-in-tariff (FiT). Throughout 2011, RREEF made several investments in Spain’s wind and Concentrated Solar Power (CSP) sectors. RREEF owned an interest in five wind farms and three CSP plants, each of which registered under RD 661/2007 to receive FiTs.

In 2012, Spain enacted Law 15/2012, which imposed a 7 per cent levy on all income obtained by generators, including those in the RE industry. Spain amended its RE regulations in 2013 and replaced FiTs with a guarantee of a reasonable rate of return, which turned out to be 7.398 per cent (pre-tax).



As a result of these changes in Spain's regulatory regime, RREEF filed for arbitration in October 2013, alleging that these regulatory changes violated Spain's obligations under ECT Article 10(1) to provide legal stability, FET, transparency, nondiscrimination, and proportionality and reasonableness. RREEF also alleged that Spain breached its legitimate expectations.

Applicable legal standards: FET and legitimate expectations apply, but the umbrella clause does not

The tribunal first determined that the FET standard under the ECT is the same FET standard required in international law, and that it includes commitments on transparency, protection and security, non-impairment, nondiscrimination, proportionality and reasonableness. Notably, the tribunal clarified that although the FET standard requires a state to respect the legitimate expectations of an investor, it is not reasonable for an investor to expect that the conditions surrounding its investment will not change at all.

A majority of the tribunal also rejected RREEF's contention that the umbrella clause of the ECT should apply, which would have brought breaches of contractual obligations within the scope of the ECT. The tribunal found the umbrella clause inapplicable because it requires a contractual obligation between the investor and state, and RREEF had no contractual relationship with Spain.

Commitment to stability in the ECT

RREEF contended that the ECT stability requirement operates as a free-standing obligation whereby states must maintain a stable legal framework for the duration of an investment. In contrast, Spain argued that the stability requirement fits within the broader FET standard of the ECT.

The tribunal noted stability is not absolute and does not equate with immutability absent a clear stabilization clause. The tribunal went on to say that "the obligation to create a stable environment certainly excludes any unpredictable radical transformation in the conditions of the investments" (para. 315). Although RD 661/2007 provided that "a reasonable rate of profitability shall always be guaranteed with reference to the cost of money in the capital markets" (para. 318), the tribunal did not interpret this clause as a firm pledge to not change the conditions of the investment. Instead, the tribunal interpreted it as envisioning future adjustments to the regulatory regime.

The tribunal was thus tasked with determining whether Spain's regulatory changes amounted to a substantial change and ultimately determined that one particular

aspect of case—the retroactive application of RD 661/2007—constituted a breach of this stability principle. To the extent the contested measures applied retroactively by clawing back shareholders' previously vested rights, the tribunal ordered Spain to pay RREEF appropriate compensation for the damage caused by the breach.

Legitimate expectations

RREEF argued that Spain's regulatory changes were unpredictable and not in line with RREEF's legitimate expectations. Spain responded by contending that absent a specific commitment to regulatory stability, investors cannot legitimately expect that a regulatory framework such as Spain's will not change. The parties agreed that the investors had the burden to prove their expectations were reasonable and objective at the time the investment was made.

In determining whether RD 661/2007 violated RREEF's legitimate expectations, the tribunal considered whether the regulatory change constituted a drastic and radical change "affecting unexpectedly the conditions of the investments" (para. 379). The tribunal determined that because Spain had guaranteed a reasonable rate of return or reasonable profitability in several laws governing its REI, the only legitimate expectation of RREEF "was to receive a reasonable return for its investment" (para. 386). Crucially, this meant that RREEF could not legitimately expect to receive a fixed rate of return for the duration of its investment, as originally provided through the FiT regime.

Transparency and discrimination

RREEF also alleged that Spain dismantled the RD 661/2007 regime non-transparently and applied the new regime in a discriminatory manner by implementing the 7 per cent levy on RE generators but not installations. Because RD 661/2007 contemplated that an adjustment was possible and Spain made its regulatory changes in public, the tribunal determined that there was no breach of transparency. It also noted that the discrimination claim revolved solely around the 7 per cent tax, and the tribunal had previously determined it did not have jurisdiction to decide tax matters. As a result, the tribunal could not decide the discrimination claim.

Proportionality and reasonableness

Finally, RREEF alleged that Spain did not satisfy the proportionality and reasonableness test, as the new regime imposed an improper burden on RREEF in relation to the benefit sought by Spain, particularly given the alternative measures available. The tribunal



determined that a government measure would meet the reasonable and proportional test so long as it was not “random, unnecessary or arbitrary” (para. 460). Because Spain only guaranteed a reasonable return, the majority held that a determination of whether Spain violated the proportionality and reasonableness principles was inseparable from an assessment of damages. As a result, the tribunal next turned to a damages assessment to determine whether RREEF earned a reasonable return after Spain modified its regime.

RREEF earned reasonable return on wind investments

In assessing damages, the tribunal determined Spain must compensate RREEF for 1) damages created by retroactively applying the modified tax and regime and 2) damages to the extent RREEF did not earn a reasonable rate of return following the regime modifications.

RREEF claimed losses of EUR 297 million using a discounted cash flow (DCF) analysis. Spain used an internal rate of return (IRR) approach and claimed RREEF’s losses did not exceed EUR 31 million. The tribunal agreed with Spain’s approach, noting that RREEF should only receive compensation “to the extent that the modifications would have exceeded the limits of what is reasonable” (para. 515).

The tribunal determined that the IRR applied is reasonable if i) it entitles the producers to a return after operating costs; ii) it provides a reasonable benefit, meaning one that is not disproportionate or irrational; and iii) the reasonableness determination is made “with reference to the cost of money in the capital market” (para. 524). Because the IRR of RREEF’s wind farms was 13 per cent and significantly over the cost of money in the capital market, the majority determined that Spain did not violate RREEF’s legitimate expectation of a reasonable return.

RREEF did not earn a reasonable return on solar investments

The tribunal determined that the guaranteed return of 7.398 per cent (pre-tax) on CSP investments under the new regime was equivalent to an IRR of 5.8 per cent (post-tax). Taking into account the Spanish 10-year bond as the risk-free rate of 4.398 per cent, a market risk premium of 5.5 per cent, a beta of 0.455 per cent, a debt/equity ratio of 60/40, and a cost of debt of 3.43 per cent, the majority calculated the weighted average cost of capital (WACC) to be 5.86 per cent. The majority added a risk premium of 1 percentage point to reflect that the “the Claimants had legitimate expectations that the return on their investment would be above the mere level of the WACC since the Respondent attracted investments

in the renewable energy sector by raising hope of above-average profits” (para. 587).

The majority concluded that Spain violated RREEF’s legitimate expectations to receive a reasonable return because the WACC of 6.86 per cent on its CSP investments was higher than the IRR of 5.8 per cent guaranteed by the new regime. Spain was thus deemed liable for the difference between the IRR of 5.8 per cent RREEF earned on its CSP investments and the WACC rate of 6.86.

Award

Ultimately, the tribunal found that the damages calculations provided by either party did not adequately represent the actual IRR per project or measure the retroactive damage to RREEF’s shareholders. As a result, it encouraged the parties to find agreement on the damages amount. Failing that, the tribunal stated it would appoint an expert of its own choosing to perform the damages valuation.

Notes: The tribunal was composed of Alain Pellet (president, appointed by the chair of the ICSID Administrative Council, French national), Robert Volterra (claimants’ appointee, Canadian national) and Pedro Nikken (respondent’s appointee, Venezuelan national). The award is available in English at https://www.italaw.com/sites/default/files/case-documents/italaw10455_0.pdf

Gregg Coughlin is a Geneva International Fellow from University of Michigan Law and an extern with IISD’s Investment for Sustainable Development Program.

ICSID tribunal upholds Panama’s plea of illegality in the making of an investment in a tourism project located in an Indigenous area

Álvarez y Marín Corporación S.A., Bartus van Noordenne, Cornelis Willem van Noordenne, Estudios Tributarios AP S.A. and Stichting Administratiekantoor Anbadi v. Republic of Panama, ICSID Case No. ARB/15/14

Juan Carlos Herrera-Quenguan

A group of Dutch and Costa Rican investors lost a legal battle against Panama before an ICSID arbitral tribunal. After more than three years of proceedings, the tribunal rendered its award declining jurisdiction on October 12, 2018. The case concerned a tourism project in an Indigenous-protected area. According to



the claimants, the project was frustrated due to locals' opposition and a governmental report, in breach of the Netherlands–Panama BIT and the Central America–Panama FTA.

Background and claims

In 2010 a group of investors acquired four rustic farms in order to develop the Cañaveral eco-tourism project along the Panamanian Caribbean, in the Indigenous protected reserve known as Comarca Ngöbe-Buglé, created by law on March 7, 1997. However, the Panamanian government questioned the legality of the acquisition from the very beginning. In that line, the state's national land management authority (*Autoridad Nacional de Administración de Tierras*) issued a report on July 9, 2013, concluding that two of the four farms were in fact outside the Comarca.

The Comarca is a special territorial regime in which the Indigenous communities have collective ownership of the lands in the reserve. Therefore, third-party ownership is limited and can only be granted under specific circumstances. Namely, (i) private ownership over the lands should have existed prior to the enactment of the law creating the Comarca, and (ii) the Comarca communities have the right of first option to purchase the lands; a third party may acquire the lands only when the Comarca communities do not want them.

The claimants said the July 2013 report frustrated the Cañaveral project because it relocated two of the four farms, thus reducing the area of the project from 685 to 250 hectares. Furthermore, they argued that the report was leaked and created an atmosphere of opposition and criticism from the Comarca, which led to the illegal occupation of the farms and ultimately made the project unfeasible.

Panama argued that the claimants illegally acquired the farms in the Comarca area through acquisitive prescription (so-called "squatter's rights") proceedings that had produced judgements granting ownership to third parties. It alleged that such proceedings were tainted by fraud and irregularities.

On March 15, 2015, the claimants initiated ICSID arbitration. The Dutch claimants relied on the 2000 Netherlands–Panama BIT, and the Costa Rican claimants relied on the 2002 Central America–Panama FTA. They argued that Panama (i) expropriated their investment without compensation, without cause of public utility and without respect for due process; (ii) did not treat them fairly and equitably; and (iii) did not give their investment full protection and security.

The existence of the legality requirement in the treaties

Panama raised four preliminary objections, namely: (i) the investment was illegal; (ii) some of the claimants were not investors protected by the treaties; (iii) some of the investors did not prove that their investment meets the *Salini* test; and (iv) the claimants did not demonstrate prima facie a breach of the treaties. The tribunal only considered it relevant to address the first preliminary objection.

Panama argued that BIT Art. 2, FTA Art. 10.12 and public international law enshrine the requirement of legality in the investment. Hence investments made in breach of the good faith, clean hands, abuse of process and illicit enrichment doctrines are not protected, according to Panama. Conversely, the claimants argued that the BIT does not impose obligations on the investor as such, but only on the state, and that the FTA does not impose any formality or requirement on the investment.

The tribunal agreed with the claimants that neither treaty includes a provision on the legality requirement. However, it understood that "the legality requirement, although not explicitly expressed in the Treaties, forms an implicit part of the concept of protected investment" (para. 118).

It also concluded that not all types of illegality entail that a given investment is not protected by the treaties, considering that such a consequence would be severe. In that sense, it held that protection should only be denied when it constitutes a proportionate response to an investor that severely infringed the law of the host state. The severity of the breach should be assessed in light of the relevance of the infringed regulation and the intention of the investor.

First preliminary objection: The illegality of the investment

Having concluded that the legality requirement is relevant to the dispute, the tribunal went on to analyze whether the claimants indeed breached the requirement.

For Panama, the acquisition of the investment was illegal considering that the acquisitive prescription proceedings were tainted by fraudulent witness statements and other irregularities. Even in the event that the claimants did not participate in the fraudulent process, Panama maintained that they could not argue that they were good-faith holders of the farms, given that several times they were presented with inconsistencies in the



judicial proceedings and in the purchase of the farms. Furthermore, Panama pointed out that the claimants never conducted any georeferenced procedure on the area in order to confirm the exact location of the farms.

The tribunal concluded that the investment was procured in breach of the applicable legal regime in a severe way and therefore neither the claimants nor their investment could enjoy protection from the treaties and international law. It assessed the intention of the claimants in light of the red flags and irregularities in the acquisition, and concluded that the situation required a higher standard of due diligence from the investors. The tribunal found that this was especially the case as the acquisition of the farms interacted with a highly relevant special regime, which created the Comarca and provided for specific and essential requirements that were not met: the Indigenous Peoples' right of first option to purchase the lands had not been respected. According to the tribunal, the violation of this regime is of such severity that the whole transaction must be deemed null.

Decision and costs

In light of the insurmountable illegality of the investment, resulting in the loss of protection under the applicable treaties and international law, the tribunal concluded that it lacked jurisdiction to decide on the merits. It ordered each party to bear its own costs, but ordered Panama to bear the onsite inspection costs.

Notes: The tribunal was composed of Juan Fernández-Armesto (president appointed by the parties, Spanish national), Horacio A. Grigera Naón (claimants' appointee, Argentinian national) and Henri C. Álvarez (respondent's appointee, Canadian national). The award is available in Spanish only at <https://www.italaw.com/sites/default/files/case-documents/italaw10491.pdf>

Juan Carlos Herrera-Quenguan is a senior associate at Flor & Hurtado in Quito, Ecuador. He specializes in public international law and international dispute settlement.

India found in breach of BIT with Germany by UNCITRAL tribunal in respect of agreement for lease of electromagnetic spectrum

Deutsche Telekom AG v. the Republic of India, PCA Case No. 2014-10

Trishna Menon

An UNCITRAL tribunal dismissed India's preliminary objections and found it in breach of the FET standard in the India–Germany BIT in a PCA-administered arbitration initiated by Deutsche Telekom AG (DT). The interim award on liability was rendered on December 13, 2017.

Background and claims

An agreement for the lease of S-band electromagnetic spectrum on two satellites (Agreement) was concluded on January 28, 2005 between Devas Multimedia Private Limited (Devas) and the Indian state-owned company Antrix Corporation Limited (Antrix). Between 2008 and 2009, DT's wholly owned Singaporean subsidiary Deutsche Telekom Asia Pte Ltd (DT Asia) acquired roughly USD 97 million worth of shares in Devas, reaching a shareholding of 19.62 per cent.

Around April 2004, discussions had commenced within various Indian government agencies—including the Ministry of Defence, the Indian Space Research Organisation (ISRO) and Department of Space (DOS)—on reserving S-band electromagnetic spectrum for military and strategic use. At a press conference in February 2011, the DOS and the ISRO announced the decision to terminate the Agreement. On February 16, 2011, the DOS secretary issued a note recommending the termination of the Agreement to the Cabinet Committee on Security (CCS), the highest decision-making authority. One day later, based on this note, the CCS decided that “in light of the policy of not providing orbit slot in S Band to Antrix for commercial activities, the Agreement . . . shall be annulled forthwith” (CCS Decision).

In the arbitration, initiated on September 2, 2013, DT argued that India illegally repudiated the Agreement for commercial reasons and political considerations arising out of certain other corruption allegations against Indian space authorities. According to DT, India's conduct breached the BIT standards on expropriation and FET.

India, in turn, argued that it instructed Antrix to terminate the Agreement for reasons linked to the country's essential security interests, and that certain



threshold issues precluded DT from asserting its claims in the arbitration: (1) the BIT does not cover indirect investments and indirect investors; (2) it does not protect pre-investments; and (3) it contains an “essential security interests” clause.

Indirect investment

The tribunal considered this issue through two questions: (1) whether the BIT required the home state national to hold the relevant assets directly, and (2) whether the home state national who did not directly own the assets affected by the contested measures could claim for BIT breaches.

The tribunal found no requirement of direct ownership in the definition of “investment” in the BIT. The provision requires that the relevant asset be “invested” but did not specify that it must be invested directly. In the absence of any qualifying language in the BIT as to the indirect or direct nature of investments, the tribunal interpreted the terms “investment” and “invested” according to VCLT Article 31(1), taking into account the ordinary meaning, context, and object and purpose of the treaty. It also relied on *Guaracachi v. Bolivia* and *Siemens v. Argentina*, which held that an unqualified definition of “investment” would include indirect investments through the acquisition of shares.

The tribunal also looked into the definition of “investor.” For a home state national or company to be considered an investor, first, it must have “effected” or be “effecting” an investment and, second, such investment must be in the territory of the host state. The tribunal relied on *CEMEX v. Venezuela* to state that investment tribunals have consistently refused to read into the reference to the territory of the host state a requirement for direct ownership of the assets constituting the investment.

India’s submission that the definition of “investment” grants direct shareholders the standing to bring an expropriation claim, with the result that indirect shareholders would lack such standing, was also not supported by the language of the BIT, according to the tribunal. The arbitrators pointed out that DT did not present itself as the beneficiary of protections owed to its subsidiaries; it was instead claiming for the reflective loss that it itself suffered due to India’s alleged breaches of the BIT. Therefore, the tribunal concluded that the BIT could not be read to restrict the shareholder’s right to claim on its own behalf.

Pre-investment actions

India submitted that DT’s activities in India remained at a pre-investment stage, since DT had not obtained the

necessary governmental approvals, including the crucial Wireless Planning and Coordination (WPC) licence, and that the shares in Devas are not a relevant investment, since India neither expropriated them nor otherwise prevented the shareholders from managing the company.

While the tribunal agreed that the shares in Devas should not necessarily be viewed as an investment in isolation of the company’s activities, it considered that DT had contributed substantial financial resources to obtain its indirect shareholding in Devas and that those equity contributions were protected investments under BIT Article 1(b)(ii). The tribunal found that while Devas had not obtained the WPC licence, the BIT’s definition of “investment” could not be restricted to going concerns holding all the relevant authorizations to carry out their business.

Essential security interests

The tribunal first held that BIT Article 12, which contains the clause on essential security interests, must be interpreted on its own terms, without incorporating requirements from the customary international law state of necessity defence that were not present in the treaty text. It did not consider that Article 12 is limited to situations of “emergency,” or that the state must prove that a measure is the “only one” available, or that it must not have contributed to the situation of necessity.

Article 12 provides for the following conditions: (1) a Contracting Party must apply a prohibition or restriction, (2) for the protection of a state’s “essential security interests,” and (3) “to the extent necessary for” such protection.

The CCS Decision held that India would not be able to provide S-band electromagnetic spectrum to Antrix for commercial use and consequently determined that the Agreement needed to be annulled. Accordingly, on the first condition, the tribunal was of the view that the disputed measure was a prohibition and restriction.

The tribunal noted that while taking back the S-band from Antrix–Devas, there was no indication that the CCS allocated it to the military or otherwise earmarked that spectrum for security interests. It also noted that the mention of “strategic” and “societal” needs is recurrent in the majority of documents leading to the CCS Decision, and these needs are almost invariably presented together. While the so-called “strategic needs” expressed by the armed forces, as well as the national security interests expressed by internal security agencies, would meet the test for essential security interests, the tribunal concluded that no



reasonable reading of BIT Article 12 could include the other “societal needs” such as train tracking, disaster management, tele-education, tele-health and rural communication, without distorting the natural meaning of the term “essential security interests.”

For a successful invocation of Article 12, the existence of a much more restricted range of interests must be shown, which India failed to do, according to the tribunal.

Violation of the FET standard; other claims dismissed

The tribunal found that the decision to annul the Agreement was arbitrary and unjustified, as it was manifestly not based on facts, but on conclusory allegations, and was the product of a flawed process. It concluded that the rush to seek an annulment of the Agreement following press reports of corruption, which triggered all the subsequent actions, was taken without any documentary evidence, sound justification or record. In addition, the tribunal concluded that the post-annulment facts corroborate the conclusion that there were no military needs that were irreconcilable with the Agreement.

Even if there were proof of any military and societal needs irreconcilable with the Agreement, the tribunal reasoned, it was incumbent on India to raise the issues it had identified in the Agreement with Devas or DT. The tribunal found that at no time after the conclusion that the Agreement needed to be annulled was arrived at did Devas or DT get the opportunity to explain, address or meet the concerns asserted. Consequently, it held that India’s conduct breached the FET standard in multiple respects.

With relation to the expropriation and full protection and security claims, the tribunal chose to dispense with addressing these claims, in the interest of judicial economy, as their resolution would not change the outcome of the dispute in terms of quantification of damages.

Decision and costs

The tribunal held that it had jurisdiction over the dispute and that India breached the FET standard under BIT Article 3(2). The tribunal will take the necessary steps for the continuation of the proceedings toward the quantum phase.

India challenged this interim award before the Swiss Federal Tribunal, the court of supervision of the arbitration, arguing that the tribunal did not have jurisdiction to hear the dispute, on the basis of the same three threshold objections raised before the

tribunal. In a judgment dated December 11, 2018, the Federal Tribunal dismissed these arguments and rejected India’s application for the annulment of the award by a 3:2 majority.

Notes: The tribunal was composed of Gabrielle Kaufmann-Kohler (president, Swiss national), Daniel M. Price (claimant’s appointee, U.S. national) and Brigitte Stern (respondent’s appointee, French national). The award is available at <https://www.italaw.com/cases/2275>

Trishna Menon is an Associate at Clarus Law Associates, New Delhi, India.

SCC tribunal finds Poland liable for expropriation over divestment order to Luxembourg bank

PL Holdings S.à.r.l. v. Republic of Poland (SCC Case No. V2014/163)

Gladwin Issac

In a final award dated September 28, 2017, an SCC tribunal ordered Poland to pay EUR 176 million to a Luxembourg-based private equity firm after finding that the forced divestment of the company’s stake in a bank amounted to an expropriation under the Luxembourg–Poland BIT. In particular, the tribunal ruled that although the claimant was not deprived of its investment, the restrictions imposed by Poland’s banking regulator severely restricted certain rights forming part of the investment, thereby depriving the “Claimant of the full benefit of its rights of ownership to such an extent as to constitute an expropriation” (para. 320, Partial Award).

Background and claims

Capital PL Holdings S.à.r.l., a Luxembourg-based entity and a wholly owned subsidiary of Abris CEE Mid-Market Fund L.P. (Abris), invested in two Polish banks that were then merged to become FM Bank PBP (the bank), eventually becoming a 99.5 per cent shareholder.

Following the merger, KNF, the Polish banking regulator, initiated a series of measures stating certain management irregularities. In April 2014, KNF issued an order suspending the claimant’s exercise of voting rights and requiring it to sell all of its shares in the bank by December 31. Although KNF retracted its order in July 2014, the restriction on voting rights remained in force. Further, KNF instituted proceedings against the



claimant to re-mandate the forced sale of its shares. In November 2014, KNF issued a third order requiring the claimant to sell all of its shares by April 30, 2015.

Despite assuring the claimant of reconsidering its third order, KNF repeatedly postponed the deadline for reconsideration, leaving the claimant with a limited period to execute a sale in order to avoid administrative sanctions. On November 26, 2014, the claimant filed arbitration, alleging that KNF's measures amount to an expropriation of its investment without compensation, in violation of the BIT.

Tribunal dismisses Poland's jurisdictional objections, including the intra-EU objection

Poland presented two belated objections to the tribunal's jurisdiction. First, it argued that although the claimant is based in Luxemburg, the actual investor is Abris, registered in Jersey. Therefore, according to Poland, "the claimant was merely a 'tool' through which Abris made and controlled its own investment in Poland" (paras. 273–275, 296, Partial Award).

Second, relying on VCLT Articles 30 and 59, Poland asserted that the dispute resolution provisions of the BIT are incompatible with EU law, and that once Poland has acceded to the EU, its treatment of an investor from an EU member state (Luxembourg, in this case) is governed exclusively by EU law and may be challenged exclusively in the courts of the EU or its member states (para. 302, Partial Award). In addition, according to Poland, TFEU Article 344 vests exclusive authority to adjudicate the present dispute in the European judiciary.

The tribunal chose to address the objections despite the delay, but dismissed both of them, noting that Poland adduced no evidence to contradict the claimant's representations on the claimant's status as an investor under the BIT.

As regards the intra-EU objection, the tribunal, relying on *RREF v. Spain*, affirmed that "the treaty from which the tribunal emanates is for all practical purposes the tribunal's 'constitution,' and it is on that instrument and that instrument alone that the tribunal's authority depends" (para. 309, Partial Award). It held that neither VCLT Article 30 nor Article 59 nullify the BIT and thereby negate the authority of the tribunal to resolve the dispute. It further held that TFEU Article 344 has no application in this case as it is between the investor of an EU member state and another member state and not between two EU member states as envisaged under the TFEU.

Poland's measures lead to deprivation of certain rights arising out of the investment, amounting to indirect expropriation

The claimant argued that KNF's measures deprived it of its voting rights for a period of nearly 18 months, from April 2015 until it was forced to sell its shares, and that it thus sustained a loss of reasonably anticipated profits. According to the claimant, neither the order depriving it of its voting rights nor the order to sell its shares satisfies the conditions for lawful expropriation under BIT Article 4(1). Poland countered that it was well within its rights to regulate in certain areas, without such regulation being considered as a breach of the BIT.

In its analysis, the tribunal observed that the claimant was not deprived of its investment in the technical sense, but rather of certain rights forming part of it, namely, the right to vote and the right to dispose of the investment as it saw fit. It agreed with the claimant's views that KNF's measures severely restricted these rights, thereby depriving the claimant of the full benefit of its rights ownership to such an extent as to constitute an expropriation within the meaning of the BIT.

Poland's measures found in breach of the proportionality principle

The claimant added that the measures taken by KNF could not be justified as legitimate good-faith regulations because they were arbitrary, inappropriate and out of proportion. Although the tribunal did not decide on the law applicable to the principle of proportionality, it applied a three-prong test to review whether the measures were (a) suitable for achieving KNF's legitimate public purpose; (b) necessary for achieving that purpose, so that no less burdensome measure would suffice, and (c) not excessive in that its advantages are outweighed by its disadvantages.

As regards the first element of the test, although the tribunal was convinced that KNF's measures were implemented to further a legitimate and substantial public interest, it found that the measures were not necessarily suitable. In its view, the management irregularities and the changes to the management board not being brought to KNF's attention did not sufficiently justify the measures, especially when the bank's financial and economic situation was stable and presented no threat to the security of customer deposits, and every irregularity flagged by KNF to the bank and its shareholders was swiftly fixed. It added that not only were these drastic measures imposed



by KNF unnecessary and unwarranted, they were counter-productive in nature, thereby finding that the third prong of the test was satisfied: the measures were excessive by any measure, as the situation facing KNF was not so dire as to justify them.

Poland's order to dispose of shares violated the claimant's procedural rights

In addition to an expropriation claim, the claimant also alleged that KNF violated its procedural rights with these measures, in particular, by repeatedly postponing the deadline for deadline for reconsideration of the third order until such time as the claimant's shares were required to be sold, thereby effectively depriving the claimant of its rights of appeal and the judicial protection afforded. Poland, in turn, argued that the third order merely ordered the claimant to "dispose of" (and not "sell") its shares and that the claimant ultimately sold the shares of its own volition, at a juncture when a reconsideration ruling was pending.

The tribunal, however, found Poland's position to be untenable as the most obvious way of disposing of the shares was by selling them. In addition, it noted the "most egregious procedural irregularity" (para. 408, Partial Award) at the hands of KNF when it postponed its decision on reconsidering its third and final order, thus barring the claimant's fundamental right of access to court for redress.

Decision and costs

The tribunal found that Poland was in breach of BIT Article 4(1) on account of its expropriation of the claimant's shareholding in the bank through restrictions taking the form of a suspension of its voting rights and the compulsory sale of shares.

In its partial award dated June 28, 2017, the tribunal made a determination as to the most accurate formula and valuation date for establishing asset value and damages, on the basis of which the experts adopted an agreed financial model.

In the final award, the tribunal adopted the experts' joint report, ordering Poland to pay the claimant damages of PLN 653,639,384 (EUR 176 million), plus pre- and post-award interest set by reference to the Polish law on debts. It also made a costs order of EUR 3.5 million in favour of the claimants, while splitting the costs of the arbitration evenly.

Notes: The tribunal was composed of George A. Bermann (chair appointed by the SCC, U.S. national),

Julian D. M. Lew (claimant's appointee, British national) and Michael E. Schneider (respondent's appointee, German national). The partial award is available at <https://www.italaw.com/sites/default/files/case-documents/italaw9378.pdf> and the final award is available at <https://www.italaw.com/sites/default/files/case-documents/italaw10467.pdf>

Gladwin Issac is a graduate of the Gujarat National Law University, India.

Investors' legitimate expectation claims against Italy dismissed due to the absence of specific commitments

Blusun S.A., Jean-Pierre Lecorcier and Michael Stein v. Italian Republic, ICSID Case No. ARB/14/3

Xiaoxia Lin

On December 27, 2016, an ICSID tribunal constituted under the ECT issued its award, dismissing all three investors' claims. Notably, this was the first investment arbitration award against Italy stemming from the Italian reform in the solar energy sector.

Background and claims

The claimants were Blusun S.A., a holding company incorporated in Belgium, and its shareholders, Jean-Pierre Lecorcier, a French national, and Michael Stein, a German national. Blusun was established in 2009 to pursue a 120 MW energy project in Puglia, Italy, through two Italian subsidiaries, Eskosol and SIB. One of the main legislative sources at the time the claimants invested in the project was Legislative Decree 387/2003 enacted in January 2004, which established a simplified authorization procedure for the construction of plants powered by renewable sources.

The investors disputed a series of measures taken by the Italian authorities between 2010 and 2012, including the Constitutional Court's decision of 2010, ruling the provisions of Legislative Decree 387/2003 unconstitutional; the Romani Decree of March 2011, limiting the application of the feed-in tariffs applicable for that time period; and the Fourth Energy Account adopted in April 2011, making further changes to the feed-in tariffs. The claimants asserted that Italy's regulatory measures and judicial decisions breached the FET standard under ECT Article 10(1) and had



an effect equivalent to nationalization or expropriation under ECT Article 13(1).

Tribunal dismisses jurisdictional objection

Italy objected to the tribunal's jurisdiction, denying that the claimants had a protected investment as the project did not amount to an investment but could only be characterized as a pre-investment activity.

Apart from noting that construction of the solar plants had commenced, the tribunal specified that it was not a mere paper project of a speculative character once there were "substantial measures of implementation, including assumption of financial risk" (para. 269).

Italy also argued that the claims were inadmissible since the claimants lacked "clean hands" in pursuing the project by failing to conduct an environmental impact assessment (EIA). The tribunal dismissed this objection since the ECT did not require investors to carry out an EIA for any proposed project. The tribunal also observed that while Italian law required large solar plants to complete a screening process as a result of which an EIA may be imposed, it did not require an EIA procedure for small solar power plants. In the tribunal's view, given the "aggregative" character of the project, there existed uncertainty as to the applicability of the screening procedure (para. 276). The tribunal noted that no screening seemed to have been required for individual plants and that the time for an EIA had passed by the time Eskosol acquired the 12 development companies.

The European Commission submitted an amicus curiae brief, objecting to the tribunal's jurisdiction over the intra-EU dispute. First, the tribunal stated that the text of the ECT did not carve out or excluded issues arising between EU member states and that EU member states did not lack competence to enter into obligations between themselves in the treaty. Drawing from a series of arbitral awards that unanimously rejected intra-EU jurisdictional objections, the tribunal concluded that there was no incompatibility between the TFEU and the ECT, because the obligations between EU member states under the ECT had not subsequently been modified or superseded by later EU law.

Tribunal frowns on the legal instability claim

The tribunal first interpreted the commitment set out in the first and second sentences of ECT Article 10(1). It suggested that the obligation to create stable conditions embedded in the first sentence is part of the FET standard which, as pointed out by various previous

tribunals, is the core commitment under Article 10(1) by virtue of the second sentence. The tribunal disagreed with the criteria suggested in *Charanne v. Spain*, namely, "public interest" and "unreasonableness," because they were largely indeterminate; however, the tribunal endorsed the "disproportionality" criterion, as it carried built-in limitations and was more determinate.

In analyzing the alleged measures that caused the instability, the tribunals examined each of the state acts complained of by the investors and concluded that none of them was a breach of Article 10(1). First, with respect to the Constitutional Court decision of 2010, the tribunal held that while this decision may have contributed to some initial market uncertainty, it had never created doubts about the applicable legal regime. According to the tribunal, by proceeding with their investments despite the pending constitutional challenge, the claimants took the risk on their own.

Second, the tribunal found that while the reduction in feed-in tariffs introduced in the Romani Decree and the Fourth Energy Account was substantial, it was a response to a genuine fiscal need and was not in itself crippling or disabling. Therefore, it concluded that the measures were not disproportionate.

Finally, with respect to the stop-work order that was "the final blow to the project" as alleged by the claimants (para. 351), the tribunal held that the stop-work episode did not create legal instability as it was temporary, legally motivated and in accordance with due process of law. Furthermore, the order was not arbitrary or discriminatory, but fell well "within the range or legal risk of an industrial enterprise, in particular one based on debatable regulatory grounds" (para. 360).

Legitimate expectations claim dismissed in the absence of specific commitments

The investors alleged that multiple representations made by Italy gave rise to legitimate expectations, that their investment relied on such representations, but that their expectations were frustrated due to Italy's later legislation (paras. 165–168). Italy's main argument was built on the lack of a causal link between the state's conduct and the failure of the project.

The tribunal endorsed the view in *Charanne v. Spain*, *El Paso v. Argentina* and *Philip Morris v. Uruguay*, in which the tribunals made a distinction between a law and a promise or contractual commitment and declined to "sanctify laws as promises" (paras. 367–371). The tribunal stressed that in the absence of specific commitment, the state had no obligation to



grant subsidies such as feed-in tariffs, or to maintain them unchanged once granted. The tribunal, however, added an exception to this rule by stressing that the modification should be done in a manner that “is not disproportionate to the aim of the legislative amendment, and should have due regard to the reasonable reliance interests of recipients who may have committed substantial resources on the basis of the earlier regime” (paras. 319, 372).

The tribunal took the view that the expectations in this case were less powerful. In the tribunal’s view, Italy did not make special commitments with respect to the extension and operation of feed-in tariffs, nor did it specifically ensure that relevant laws would remain unchanged.

Tribunal rejects expropriation claim

The claimants argued that the measures enacted by Italy had an effect equivalent to nationalization or expropriation, leading to a total loss of the investment value. They argued that the land could no longer be used for the purpose of the project and that the substations were disconnected and served no purpose.

The tribunal noted that the laws enacted by Italy had significantly changed the terms laid down in previous legislation in the green energy sector in a non-discriminatory way. The claimants’ project, as observed by the tribunal, was “radically incomplete” and therefore never “qualified for feed-in tariffs” (para. 401). Hence, the tribunal held that the original value of the land had been retained after the project’s failure and that the investor’s argument would have only been valid if there was a completed project already entitled to the benefit of feed-in tariffs.

Based on the above reasons, the tribunal dismissed all of the claimants’ claims on the merits. Italy was ordered to pay USD 29,410.69 to the claimants as its share of the costs of the proceedings.

Notes: The tribunal was composed of James Crawford (president appointed by the parties, Australian national), Stanimir Alexandrov (claimants’ appointee, Bulgarian national) and Pierre-Marie Dupuy (respondent’s appointee, French national). The award is available at <https://www.italaw.com/sites/default/files/case-documents/italaw8967.pdf>

Xiaoxia Lin is an alumna of New York University’s IFD Fellowship with IISD’s Investment for Sustainable Development Program.

ICSID tribunal constituted by virtue of an MFN clause holds Turkmenistan liable for FET breach for requiring investors to produce *smeta*, a cost estimate required by Turkmen law

Garanti Koza LLP v. Turkmenistan, ICSID Case No. ARB/11/20

Ksenia Koroteeva

On December 19, 2016, an ICSID tribunal ordered Turkmenistan to pay compensation for denial of FET to Garanti Koza, a British company ultimately controlled by Turkish nationals.

Factual background and claims

In 2007, Garanti Koza was awarded a contract to build 28 of the 119 bridges along the highway between the cities of Mary and Turkmenabad, for the lump sum price of USD 100 million. The award of the contract between Turkmenistan’s State Concern Turkmenavtoyollary (TAY) and Garanti Koza was approved by Presidential Decree No. 9429.

Both the contract and the decree required Garanti Koza to complete its work in October of 2008. Work at the bridge sites had been planned to commence on May 1, 2008, but actually began on July 25, 2008. Garanti Koza justified the delay by TAY’s refusal to pay invoices.

TAY argued that Garanti Koza’s payment application was rejected not because of delays in the completion of the project, but because there was no *smeta*—the document containing approximate estimate of expenses, commonly used in post-Soviet countries. Although the contract did not mention *smeta*, Turkmenistan argued that the contract was governed by Turkmen law, which required Garanti Koza to present *smeta* anyway.

In 2010, TAY terminated the contract and instructed the Prosecutor General of Turkmenistan to commence proceedings against Garanti Koza in the *Arbitrazh* (Commercial) Court of Turkmenistan, the forum designated by the contract. The next day, the court adopted an order attaching Garanti Koza’s assets as a provisional measure granting TAY security for amounts owed to it by Garanti Koza.

Garanti Koza initiated ICSID arbitration in 2011, contesting the compatibility of these measures with the 1995 United Kingdom–Turkmenistan BIT. It alleged that Turkmenistan’s measures breached, among others, the expropriation, FET and full protection and



security (FPS) standards under the BIT.

Jurisdiction: The tribunal imports consent to ICSID arbitration through the MFN clause

BIT Article 8(2) identifies three arbitration rules to which an investor and Turkmenistan together *may agree* to refer the dispute: ICSID, ICC or UNCITRAL. Article 8(2) also says that, if “there is no agreement to one of the above alternative procedures,” the dispute *shall* be submitted by investor to arbitration under the UNCITRAL Rules.

Turkmenistan argued that it never agreed to refer its dispute with Garanti Koza to ICSID arbitration and, therefore, that the ICSID tribunal lacked jurisdiction to hear the dispute; the dispute may be heard by an UNCITRAL tribunal only. Moreover, under the ICSID Convention, Turkmenistan’s consent to ICSID arbitration must be expressed in writing, which is manifestly absent in the dispute with Garanti Koza.

Garanti Koza argued that Turkmenistan’s consent to submit the dispute to ICSID arbitration may be created by operation of the MFN clause in the BIT. Given that other investors—for instance, Swiss investors under the Switzerland–Turkmenistan BIT—may choose to arbitrate their disputes at ICSID, Garanti Koza claimed that it should be given the same opportunity.

The majority of the tribunal affirmed its jurisdiction over the dispute, given that Turkmenistan:

1. Consented in the United Kingdom–Turkmenistan BIT to submit investment disputes to *international arbitration*.
2. Promised to accord to British investors and their investments treatment not less favourable than that accorded to investors of other states or their investments.
3. Expressly provided that the MFN treatment “shall apply” to the dispute resolution provision of the BIT.
4. Provided investors of third states, specifically Switzerland, with an unrestricted choice between ICSID Arbitration and UNCITRAL Arbitration.

Arbitrator Laurence Boisson de Chazournes appended a dissenting opinion, saying that consent cannot “be *imported* from one treaty to another treaty” (p. 22). She considered that for the purposes of ascertaining the tribunal’s jurisdiction, it shall first and foremost analyze

“whether consent to ICSID arbitration is or is not *established* under the UK–Turkmenistan BIT” (p. 22). She argues that in the dispute with Garanti Koza the consent to ICSID arbitration was absent.

Definition of investment: The *Salini* test does not apply to ICSID arbitration

Turkmenistan also objected to the existence of an investment. Relying on the *Salini* test, the state argued that Garanti Koza failed to satisfy the criteria of risk, duration and contribution.

Garanti Koza questioned the application of the *Salini* test in the ICSID context. Alternatively, it argued that the tribunal should follow ICSID cases that view the test as a set of flexible and liberal characteristics. Even so, Garanti Koza maintained that its investment fulfilled the *Salini* test.

The tribunal underlined that BIT Article 1(a) defines “investment” to mean “every kind of asset” and provides a non-exclusive, illustrative list of assets. It found that Garanti Koza negotiated a contract to build bridges in Turkmenistan, put resources into the country and actually built a number of bridges; therefore, its activities qualified as investments.

Importantly, the tribunal refused to apply the *Salini* test. According to the tribunal, the term “investment” as used in the ICSID Convention refers to the definition of investment in the applicable BIT. The tribunal concluded that by satisfying the definition of investment in the United Kingdom–Turkmenistan BIT, Garanti Koza’s investment satisfied the ICSID Convention’s definition of investment.

Existence of protected investor: Place of incorporation matters the most

Turkmenistan also advanced that Garanti Koza was not a British investor. It argued that Garanti Koza undertook no actions of its own accord; rather, the bid was submitted and the tender was won entirely on the basis of the reputation and track record of Garanti Koza İnşaat (GKI), its Turkish parent company. Garanti Koza’s managers presented themselves not as representatives of the unknown British company, but rather as representatives of GKI, an experienced and well-known Turkish construction company.

Garanti Koza argued that it—not GKI—had made the investment in Turkmenistan. It relied, among others, on the fact that the contract was entered into between Turkmenistan and Garanti Koza and approved by more than nine Turkmen government authorities.



The tribunal concluded that the BIT contains no specific definition of “investor,” but that its substantive provisions protect “investments of nationals or companies of the other Contracting Party.” According to the tribunal, Garanti Koza satisfied the sole requirement of the BIT to bring its investments within the protection of the treaty, namely, that it be incorporated in the United Kingdom.

Never-ending debate: Treaty and contract claims

Turkmenistan also contended that ICSID was not the proper forum for the resolution of a purely contractual dispute, but that it must be submitted to the *Arbitrazh* (Commercial) Court of Turkmenistan, selected by the parties in the contract.

However, the tribunal agreed with Garanti Koza that ICSID was the proper forum, as the causes of action arise out of provisions of the BIT, rather than the contract. The tribunal also endorsed the “elevating” effect of umbrella clauses, applying their ordinary meaning in accordance with VCLT Article 31.

Expropriation: Turkmenistan's measures fall within the legal procedure under domestic law

Garanti Koza claimed that Turkmenistan’s measures amounted to direct and indirect expropriation. It also proposed importing an additional requirement for lawful expropriation from Article 5 of the France–Turkmenistan BIT, namely, that an expropriation must not be contrary to a specific commitment of the host state.

However, the tribunal refused this proposal as well as Garanti Koza’s expropriation claims. It concluded that the termination of the contract and the seizure of Garanti Koza’s factory and equipment was a matter of normal legal process under Turkmen law, following Garanti Koza’s default under the contract.

FET and FPS: Imposing *smeta* on foreign investors is unfair and inequitable

The tribunal ruled that Turkmenistan’s insistence that Garanti Koza’s payment invoices conform to *smeta* was a breach of Turkmenistan’s FET obligation. It underlined that the insistence on *smeta* invoicing forced Garanti Koza to choose between submitting accurate invoices, and consequently accepting less compensation than it had bargained for, or manipulating its invoices to receive the full compensation that TAY had agreed to pay. The tribunal considered that using governmental power to put an investor in such a situation is fundamentally unfair and therefore amounts to an FET breach.

The tribunal refused to address the FPS claim, as it substantially overlapped with Garanti Koza’s FET submissions. It also rejected Garanti Koza’s claims for termination of the contract, loss of factory and equipment as well as tax penalties imposed by Turkmenistan.

Costs and damages

The tribunal awarded the investor damages of USD 2,529,900 for Turkmenistan’s requirement to use *smeta*. It noted that although Garanti Koza prevailed in the arbitration, it was awarded only about 5 per cent of the compensation it sought; accordingly, the tribunal denied Garanti Koza’s application for reimbursement of its legal fees and expenses. Each party was ordered to bear its own legal costs.

Notes: The tribunal was composed of John M. Townsend (U.S. national, president appointed by the Chair of the ICSID Administrative Council), George Lambrou (Greek national and British resident, claimant’s appointee) and Laurence Boisson de Chazournes (French and Swiss national, respondent’s appointee). The decision on the objection to jurisdiction for lack of consent, the award and the dissenting opinion of arbitrator Boisson de Chazournes are available at https://www.italaw.com/sites/default/files/case-documents/italaw8189_12.pdf

Ksenia Koroteeva is pursuing the MIDS LL.M. in International Dispute Settlement in Geneva. Previously, she worked as legal counsel and tribunal secretary at the Russian Arbitration Center (RAC).



RESOURCES AND EVENTS

RESOURCES

Canadian Initiatives Against Bribery by Foreign Investors

By Matthew A. J. Levine, published by IISD, June 2019

This report builds on the broad recognition that corruption—with bribery as a particularly significant manifestation—is a grave threat to sustainable development. It focuses on Canadian legal initiatives against bribery by Canadian businesses investing abroad. By digging into both domestic and international law, the policy brief identifies four key points of interest to sustainable development stakeholders: (1) a spike in enforcement of Canada’s Foreign Bribery Prohibition; (2) the recent expansion of firm-level anti-bribery compliance requirements; (3) the adoption of mandatory payment transparency rules for extractive industry firms; and (4) the Canadian government’s stated goal to move to a “progressive” trade (and investment) agenda. Available at <https://iisd.org/library/canadian-initiatives-against-bribery-foreign-investors>

Local Content Policies in the Mining Sector: Scaling up local procurement

By Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development (IGF), published by IISD, April 2019

This paper focuses on local procurement policies designed to boost the number of goods and services purchased by mining operations from local stakeholders. It unpacks various objectives that a local procurement policy can help respond to. It also details various types of policy instruments that can be used in the design of local procurement policies and underlines the strengths and weaknesses of each type of measure. In developing countries, the mining sector generally does not have a good track record when it comes to leveraging its potential for industrial development and economic transformation. Yet the potential is significant: if harnessed well, mining can unlock industrial activities through more value addition; create business opportunities for the domestic private sector from local procurement, in particular close to mine sites; generate indirect jobs along the supply chain; and provide wider

opportunities for the economy, notably through the use of infrastructure and mining-related capabilities for other economic sectors. Available at <https://www.iisd.org/library/local-content-policies-mining>

World Investment Report 2019: Special economic zones

By UNCTAD, published by UNCTAD, June 2019

The World Investment Report (WIR) supports policy-makers by monitoring global and regional FDI trends and documenting national and international investment policy developments. The 2019 edition provides an overview of the global landscape concerning Special Economic Zones. In 2018, global FDI flows fell by 13 per cent to USD 1.3 trillion, the lowest level since the global financial crisis. The chapter on international investment policy-making notes that, in 2018, countries signed 40 IIAs and that terminations entered into effect for at least 24 treaties. IIA reform is progressing, but much remains to be done: while countries are increasingly interpreting, amending, replacing or terminating outdated treaties, the stock of old-generation treaties is 10 times larger than the number of modern, reform-oriented treaties. Investors continue to resort to old-generation treaties; in 2018, they initiated at least 71 ISDS cases. Reform efforts are occurring in parallel and often in isolation. Effectively harnessing international investment relations for the pursuit of sustainable development requires holistic and synchronized reform through an inclusive and transparent process. Available at <https://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=2460>

Responsibility of the EU and the Member States under EU International Investment Protection Agreements: Between traditional rules, proceduralisation and federalisation

By Philipp Theodor Stegmann, published by Springer, 2019

This book provides a comprehensive portrait of how international responsibility of the EU and EU member states is structured under the EU’s international investment protection agreements. It analyzes both the old regime as represented by the ECT and the new regime as represented by the new EU investment treaties, such as CETA and the agreements with



Singapore and Vietnam. The book puts forth the thesis that the determination of the EU or an EU member state as respondent in a dispute under the new EU investment treaties has a substantive effect on the respondent's international responsibility. It compares the EU regulation that allocates financial burdens between the EU and EU member states arising out of international investment disputes with the only other genuinely existing allocation system in federal states to date, namely that of Germany. The book reveals shortcomings of the new EU responsibility regime in international investment law and provides suggestions on how they can best be remedied. Available at <https://www.springer.com/gp/book/9783030043650>

SustainableFDI.org

By UNCTAD, published by UNCTAD, June 2019

SustainableFDI.org is UNCTAD's dedicated site on promotion and facilitation of investment for sustainable development, in line with the 2030 Agenda and all the SDGs. It provides content related to investment in affordable and clean energy and climate action, as well as in each of the SDGs. It offers four main services: 1) News on Sustainable FDI, including events and publications by UNCTAD and partners working on mobilizing investment in the SDGs; 2) Global IPA Network, an interactive map with links to the websites of national investment promotion agencies; 3) Sustainable Development Goal Resource Center, a library of over 300 publications for investment promoters, classified by relevant SDGs; and 4) Sustainable FDI Opportunities, with links to investment promotion agency project databases. Available at <http://sustainablefdi.org>

Investment Policy Hub

By UNCTAD, published by UNCTAD, May 2019

UNCTAD gave its Investment Policy Hub a facelift to make it more user-friendly. The main policy tools in the Hub are: 1) Country Navigator: the entry point for all country-specific investment policy data; 2) Investment Policy Monitor: the latest developments in investment policies around the world; 3) Investment Laws Navigator: a comprehensive online database of national investment laws; 4) International Investment Agreements Navigator: a comprehensive free database of investment treaties and model agreements; 5) Investment Dispute Settlement Navigator: details on all publicly known treaty-based ISDS cases; 6) Investment Policy Review: evaluation of a country's legal, regulatory and institutional framework to attract direct investments; 7) Investment Policy Framework: reference for policy-makers in formulating investment

policies and negotiating investment agreements. Available at <http://investmentpolicy.unctad.org>

Good Faith in Investment Treaty Arbitration

By Emily Sipiorsky, published by Oxford University Press, April 2019

This book considers the application of good faith by arbitral tribunals and parties in international investment disputes, encompassing both procedural and substantive aspects of good faith. It follows the arbitral process from jurisdiction to the final tribunal decisions, identifying the various applications of the principle of good faith in investment disputes. The author offers detailed analyses of the application of good faith at the jurisdictional phase of an investment dispute, then delves into the ways the principle informs tribunals' decisions. Available at <https://global.oup.com/academic/product/good-faith-in-international-investment-arbitration-9780198826446>

Arbitration Costs: Myths and realities in investment treaty arbitration

By Susan D. Franck, published by Oxford University Press, April 2019

This book tests claims about investment arbitration and fiscal costs against data so that policy reforms can be informed by scientific evidence. It uses insights drawn from cognitive psychology and hard data to explore the reality of investment treaty arbitration, identify core demographics and basic information on outcomes, and drill down on the costs of parties' counsel and arbitral tribunals. It analyzes how and when cost-shifting occurs, parses tribunals' rationalization (or lack thereof) of cost assessments and models the variables most likely to predict costs, using data to point the way toward evidence-based normative reform. Available at <https://global.oup.com/academic/product/arbitration-costs-9780190054434>

Yearbook on International Investment Law & Policy 2017

By Lisa Sachs, Lise Johnson, and Jesse Coleman (Eds.), published by Oxford University Press, March 2019

The 2017 edition of the annual publication provides a comprehensive overview of developments in the international investment law and policy field, focusing on trends and issues in FDI, investment treaty practice and investor-state arbitration. Available at <https://global.oup.com/academic/product/yearbook-on-international-investment-law-and-policy-2017-9780198830382>



Extraction Casino: Mining companies gambling with Latin American lives and sovereignty through international arbitration

By Jen Moore and Manuel Perez Rocha, published by Mining Watch Canada, Institute for Policy Studies and Center for International Environmental Law, April 2019

This report exposes 38 cases of mining companies that have been filing dozens of multi-million dollar claims against Latin American countries before investment arbitration tribunals, demanding compensation for court decisions, public policies and other government measures that they claim reduce the value of their investments.

In most of these cases, communities have been actively organizing to resist mining activities and defend their land, health, environment, self-determination and ways of life.

Available at <https://ips-dc.org/report-extraction-casino>

Digging for Dividends: The use and abuse of investor-state dispute settlement by Canadian investors abroad

By Hadrian Mertins-Kirkwood and Ben Smith, published by Canadian Centre for Policy Alternatives, April 2019

This report concludes that ISDS cases launched by Canadian investors outside North America follow a pattern of disproportionately targeting environmental policy in developing nations and that environmental policy is the fastest growing trigger for such cases. It finds that, since 1999, Canadian investors have initiated at least 43 ISDS claims against countries outside North America, whereas only one case has ever been brought against Canada by investors from a country other than the United States or Mexico. Available at <https://www.policyalternatives.ca/digging-for-dividends>

China–European Union Investment Relationships: Towards a new leadership in global investment governance?

By Julien Chaisse (Ed.), published by Edward Elgar, 2018

Bringing together expert contributors, this book provides a critical analysis of the current law and policy between the EU and China. This book deals with the key issues of the EU–China investment partnership and its implications, both internally and internationally. Each chapter covers a core theme of the subject of international economic law, including competition law, financial regulation, economic integration and dispute resolution. Available at <https://www.e-elgar.com/shop/china-european-union-investment-relationships>

EVENTS 2019

September 3

ICC/ ITA/ ALArb CONFERENCE, International Chamber of Commerce, Institute for Transnational Arbitration, Asociación Latinoamericana de Arbitraje, in Medellín, Colombia, <https://iccwbo.org/event/icc-ita-alarb-conference>

September 25–26

3rd UNCITRAL WORKING GROUP III INTER-SESSIONAL REGIONAL MEETING ON ISDS REFORM, in Conakry, Guinea, <https://uncitral.un.org/en/events/25-26.9.2019>

September 26–27

COLLOQUIUM “ACTORS IN INTERNATIONAL INVESTMENT LAW: BEYOND CLAIMANTS, RESPONDENTS AND ARBITRATORS,” at University Paris II Panthéon-Assas, in Paris, France, <https://www.transnational-dispute-management.com/news/20190926.pdf>

October 3–4

14th ICC NEW YORK CONFERENCE ON INTERNATIONAL ARBITRATION, International Chamber of Commerce, in New York, United States, <https://iccwbo.org/event/icc-new-york-conference-international-arbitration>

October 7–11

15th IGF ANNUAL GENERAL MEETING: “MINING IN A CHANGING CLIMATE,” Intergovernmental Forum on Mining, Minerals, Metals and Sustainable Development, in Geneva, Switzerland, <https://www.igfmining.org/event/15th-annual-general-meeting>

October 8–11

WTO PUBLIC FORUM, at Centre William Rappard, in Geneva, Switzerland, https://www.wto.org/english/forums_e/public_forum_e/public_forum_e.htm



October 14–18 [to be confirmed]

38th SESSION OF UNCITRAL WORKING GROUP III, “INVESTOR–STATE DISPUTE SETTLEMENT REFORM,” United Nations Commission on International Trade Law, Vienna, Austria, https://uncitral.un.org/en/working_groups/3/investor-state

October 25–26

WORLD TRADE FORUM, “INTERNATIONAL ECONOMIC DISPUTE SETTLEMENT: DEMISE OR TRANSFORMATION?” at World Trade Institute (WTI) of the University of Bern, and the European University Institute (EUI), Bern, Switzerland, https://www.wti.org/media/filer_public/b1/2e/b12e1c5d-8def-40ad-92bf-6c77cd3ffcfc/call_for_papers_wtf_2019.pdf



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