# Arbitration under International Investment Agreements

Tokyo, 27 September 2007

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## International Investment Agreements (IIAs)

- 2,500 Bilateral Investment Treaties (BITs)
- 232 Other Agreements
  - Multilateral Investment Agreements
    - E.g., Association of South-East Asian Nations (ASEAN), North American Free Trade Agreement (NAFTA), Energy Charter Treaty (ECT)
  - Free Trade Agreements/Economic Partnership Agreements (FTAs/EPAs)

## BITs offer powerful protections for foreign investors

In recent years, investors have successfully obtained recourse under BITs in respect of state conduct that has adversely affected their investments, such as

- Changes in local regulatory regimes
- Changes in tax regimes
- Denial, or withdrawal, of permits relevant to the investment activity
- The absence of transparency in a local administrative process
- The outright or effective taking of an investment
- Denial of justice in local courts



## Substantive rights under investment treaties

- Fair and equitable treatment
  - "Minimum standard" debate
  - Calvo Clause/national standard
- No expropriation (direct or indirect) without prompt, adequate and effective compensation
  - Measure of damages – "fair market value"
- Full protection and security
- No differential treatment
  - National treatment and MFN
- Umbrella clauses
- Others

## Practical aspects of investment-treaty arbitration

1. What considerations do investors take into account in structuring their investments?
2. What is the role of political risk insurance?
3. What are the benefits of having the protection of an IIA?
4. Forum selection: is ICSID the best route?
5. Practical considerations when starting an arbitration under an investment treaty
6. Do IIAs encourage FDI?
7. Do Japan's own IIAs help Japanese investors?



## 1. Structuring investments to take advantage of an IIA

- Can be very effective
  - *Saluka Investments BV v The Czech Republic* involved a Dutch-incorporated special investment vehicle of Nomura
  - The claim was brought under the Netherlands-Czech Republic BIT
  - Nomura won on liability (damages to be determined)
- Issues include:
  - Definition of "investor"
    - ability of "brass plate" companies to bring claims
    - source of capital
    - "forum shopping" concerns

## 1. Structuring investments to take advantage of an IIA (cont'd)

- Nearly all IIAs provide expressly (and all by implication) that investments must be made in compliance with the laws of the host state
- Considered in *Saluka Investments v Czech Republic* (2006)
- Most recently considered in *Fraport v Philippines* (2007)
- Interesting question of abuse or selective application of local laws (e.g., Sakhalin II)



## 1. Structuring investments to take advantage of an IIA (cont'd)

- Do investors actually do this?
- Different attitudes by different investors
  - Size of company
    - Do large companies bring fewer claims?
  - Size/nature of investment
    - Hydrocarbons (Sakhalin II)
    - Power plants (Turkey)
    - Financial services (Nomura)

## 2. Political Risk Insurance

- Different definitions of, e.g., expropriation
- Difficulties of enforcement of arbitral awards
- Can make pursuing arbitration more worthwhile
  - *Himpurna* case
  - Cases against Argentina
- Not very common



## 3. What are the benefits of having the protection of an IIA?

- Arbitration can cause damage to long-term relationships with the Government of the Host State
  - Long-term agreements such as PSAs in the oil and gas sector
  - Exclusion from tenders for further licences/concessions
- BUT
  - Increased bargaining power in renegotiations
  - Increased ability to deflect hostile government action
- 'Insurance policy' if all else fails
- Different if no long-term relationship (actual or envisaged)

## 4. Forum selection: is ICSID the best route?

- National courts or arbitration
  - Investment treaties usually provide a choice
- Institutional or ad hoc arbitration
  - Pros and cons of different rules (ICSID, SCC, UNCITRAL)
  - World Bank connection for ICSID
- Parallel proceedings (arbitrations and court proceedings) and fork-in-the-road clauses



## 5. Practical considerations in starting an arbitration under an IIA

- Requirements of the IIA (notification of claim, cooling-off period, etc)
- Requirements of the ICSID Convention (registration of the Request after scrutiny by the Secretariat)
- Constitution of the Tribunal under the different sets of Rules
- Overall time between notification of claim and final award
- ICSID internal annulment procedure vs setting-aside proceedings in national courts
- Enforcement

## 5. Practical considerations in starting an arbitration under an IIA (cont'd)

- Enforcement
- Almost universal compliance with arbitral awards pursuant to an investment treaty
  - In the interests of the State to honour the award
  - Washington (ICSID) Convention for ICSID awards
  - New York Convention on the Recognition and Enforcement of Arbitral Awards for UNCITRAL awards
  - Failure to comply with an arbitral award would itself be a breach of the treaty and ultimately subject to state-to-state proceedings



## 6. Do IIAs encourage FDI?

- Purpose of IIAs
  - Recognition of need for FDI in developing economies
  - Studies on role of IIAs in encouraging FDI
- Criticism of IIAs and investment-treaty arbitration
  - "Law of greed"
  - Public interest
  - Sustainable development
  - Do IIAs encourage good governance?

## 7. Do Japan's own IIAs help Japanese investors?

- *Saluka v Czech Republic* is the only case (indirectly) involving a Japanese investor to date
- Japan has entered into 12 BITs
  - Of these, some are Soviet-style (eg China, Russia) with limited right of recourse to arbitration
- Japan has entered into 8 EPAs (3 in force)
- Japan is a signatory to the Energy Charter Treaty
- Japanese companies may need either to (a) use an MFN argument (see below) or (b) structure their investments through a third country



## 7. Do Japan's own IIAs help Japanese investors? (cont'd)

### The Extent of MFN Protection

- No direct right to arbitration in the Japan-China and Japan-Russia BITs except for determining the amount of compensation payable for an expropriation
- China's and Russia's more recent BITs (e.g., China's BITs with the Netherlands, Germany, Finland and Iran) provide a broader right to arbitration
- Can the MFN provision in the Japan-China and Japan-Russia BITs be used to latch onto these more favourable BITs?

## The Extent of MFN Protection (cont'd)

| YES | NO |
|---|---|
| ***Maffezini v Spain*** (January 2000)<br>Dispute settlement arrangements are inextricably related to the protection of foreign investors | ***Plama v Bulgaria*** (February 2005)<br>The intention to incorporate dispute settlement provisions must be clearly and unambiguously expressed |
| ***Gas Natural SDG SA v Argentina*** (June 2005)<br>Unless clear that the parties agreed otherwise…most-favoured-nation provisions in BITs should be understood to be applicable to dispute settlement | ***Salini v Jordan*** (November 2004)<br>Concerns over "treaty shopping" and wording of clause |
| ***Suez et al v Argentina*** (May 2006)<br>Distinction made between wholesale adoption and more limited application | ***Berschader v Russia*** (April 2006)<br>MFN clause that related to "all matters" did not apply to matters of procedure! |
| | ***Telenor v Hungary*** (September 2006)<br>Depends on wording of the MFN clause in question and the intention of the parties to the treaty |



## The Extent of MFN Protection (cont'd)

- **Japan-China BIT MFN clause:**
  - The treatment accorded by either Contracting Party within its territory to nationals and companies of the other Contracting Party *with respect to investments, returns and business activities in connection with the investment* shall not be less favourable than that accorded to nationals and companies of any third country.
- **Japan-Russia MFN clause:**
  - The investors of each Contracting Party shall be accorded treatment … not less favourable than the one it offers to investors of any third country *in respect of capital investments, incomes and investment-related business activities*.
- **It is strongly arguable that Japanese investors could take advantage of more favourable dispute-resolution provisions in more modern treaties with third countries**
- **Works both ways: a Chinese investor is bringing a claim against Peru**

## Investment-Treaty Arbitration involving Asia-Pacific Parties

**Overview**

**ICSID cases**

- No cases involving Japan's investment treaties
- No case against China; one claim by a Chinese investor
- At least 6 ICSID arbitrations have been commenced by Asian investors
- At least 17 ICSID arbitrations involving 10 Asia-Pacific States

**Non-ICSID cases**

- Difficult to establish number due to lack of publicity
- At least 11 non-ICSID investment-treaty arbitrations involving Asian parties
- One case involving a Japanese investor (through a Dutch investment vehicle)



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