ARBITRATION AND INVESTMENTS – INITIAL FOCUS

V. Inbavijayan[*] *& Kirthi Jayakumar*[**]

In a world which is evolving with globalization and Internet, has led in opening up unchartered avenues leading to much consternation in the growth of law. With the push of a button, money can be transferred from one place to another, shares can be bought and sold with ease, and property can be transferred without difficulty. Typically, the extrusion of a country's law occurs through its application by courts, nominally restrained by private international law, a context that is both transparent and subject to contest by the courts of other countries.[1]

Ten years ago, one could barely detect a separate breed of law for the investment industry, either in the courts or in the literature. In the classical system, national courts had very little role to play in the construction of international investment law and issues pertaining to the investment industry. Litigation involved national rights related to consumer based and contractual based claims made by individual people against investment contracting companies. Courts were reluctant even to adjudicate claims involving foreign investment issues and the rights of other countries' investment industries, prompting serial national litigation of multinational disputes. National courts are, however, beginning to tackle multinational cases and are thus contributing to the effective creation of international norms. This has occurred most perceptibly in the copyright context in the United States, India and theUnited Kingdom, where courts hear claims under foreign laws, provide multinational relief, and effectively regulate globally by localizing any Internet conduct in the United States.[2]

At the very outset, then the incremental character of common law comes to fore. It can achieve little that is akin to the dramatic rationalizations facilitated by major codification exercises or ratification of major international conventions.[3]

---

* *V. Inbavijayan, B.L.,MCIArb, International Arbitrator.*

** *Ms. Kirthi Jayakumar, Advocate, Madras High Court.*

1 Graeme B. Dinwoodie, *The International Intellectual Property Law System: New Actors, New Institutions, New Sources*, 10(2) MARQ. INTELL. PROP. L. REV. (2006).

2 Jane C Ginsburg, '*The Private International Law of Copyright in an Era of Technological Change', 1998* RECUEIL DES COURS DE L'ACADEMIE INTERNATIONALLE DE LA HAYE (1999); Paul E Geller, '*The Universal Electronic Archive: Issues in International Copyright*' 25 IIC 54 (1994).

3 Considering the development of the *Lex Fori Rule* as an example- Phillips v. Eyre L.R. 6 Q.B. 1,28-29 (1870); Boys v. Chaplin AC 356 (1971); Red Sea Insurance Co v. Bouygues *SA*, AC 190 (1995); See further, DICEY & MORRIS, THE CONFLICT OF LAWS 1512-13 (13th ed., 2000); Pearce v. Ove Arup Partnership Ltd 1 All ER 769

The decisions of a court are binding only in a particular jurisdiction, and even within a given jurisdiction, some courts have more power than others. For example, in most countries, decisions of appellate courts are binding on lower courts and have precedential value, but decisions of non-appellate courts only have persuasive value. Interactions between common law, constitutional law, statutory law and regulatory law also give rise to considerable complexity. However *stare decisis* (the principle that similar cases should be decided according to consistent principled rules so that they will reach similar results) lies at the heart of all common law systems.

I. What are Investment Treaties?

Investment treaties, as the name suggests, are treaties that are entered into with a view to make an investment by one, in the business ventures of the other. Investments can be of many kinds. Foreign direct investment ("FDI") to and from India has increased significantly over the recent years. Transnational investment flows are beneficial to both investors and the states that receive the capital i.e., the Host States. Investors, whether foreign or Indian, are both easily able to expand into new markets. In the process, the Host States gain access to improvements in infrastructure, technology, know-how and public services. Even despite the increase in the quantum of FDI and the burgeoning overall improvements that are taking place in global governance standards, one of the biggest concerns of foreign investors operating in India is the prevalence of political risk. In simple terms, the term political risk means the risk of government interventions that can adversely affect the financial viability of an investment,[4] such as changes in regulation, breach of contract, expropriation and impose restrictions on currency transfer. Indian companies investing abroad, particularly in other emerging markets, may also face similar risks.

When an investor decides on where to invest internationally, and then goes onto studying where to set up the structure for the foreign investment, his attention is usually focused on a comparison of the tax rules of the various countries under consideration. Often little or no attention is paid to the issue of investment protection under international law. Because of this, if a local government improperly interferes with the investment resulting in loss, then whether an investment treaty is applicable and provides for recovery is largely a matter of chance. However, it would be prudent for an investor and his adviser while considering where to place the investment and set up the structure for the foreign investment? It is also imperative to consider whether

---

(1999); Tolofson v. Jensen, 3 SCR 1022 (1994); John Pfeiffer Pty Limited v. Rogerson, HCA 36 (2000).

[4] Multilateral Investment Guarantee Agency World Bank Group, World Investment and Political Risk (2010), *available at:* http://www.miga.org/documents/WIPR10ebook.pdf.

the investment would be protected by an international investment treaty and what the requirements for this would be?

A foreign investment differs in nature from ordinary trading. Trading typically consists of the one-off exchange of goods and money. However, investing in a foreign country is based on a long-term relationship between the investor and the country where the investment is made (i.e., the "host state"). A key feature in planning foreign investment is identifying and assessing in advance the risks inherent in the long-term relationship involved, both from a commercial perspective and a legal one. Investing in other countries carries certain risks that are often quite different from those in one's own country (i.e., the "home state"). These risks are not necessarily those inherent in the investment, but rather the risks an investor runs in other countries as a result of interference by local governments, import and export restrictions, political unrest—and even war.

Then the question arises as to 'What are an investor's remedies if new legislation in the host state renders an investment worthless? Or if a host state government expropriates the investor's business? Or if property is damaged or even destroyed because of political riots, such as what has taken place in Egypt, Libya and Syria? Or if a host state arbitrarily revokes a license, thus preventing the investor from doing business any further? Ordinarily, there is no contractual relationship between an investor and the local government. This makes it difficult, if not impossible for an individual or company to pursue a contractual claim in the local courts. Insurance is one option for a careful company facing such risks. In some cases, it was and is possible to obtain insurance coverage for such risks. The costs are high, however, and the maximum coverage available is limited. This is especially true for investments in countries where the risks described above are a real possibility, the "capital importing countries". International law might apply, but is difficult to enforce. Historically, an individual or company seeking compensation from a host state because of a breach of international law could not do so directly.[5] Instead, the individual or company had to rely on its government to take up the claim on its behalf, sometimes by gunboat diplomacy. For instance, when Venezuela defaulted on its foreign debt in 1902, the government of Germany, Great Britain and Italy sent warships to the Venezuelan coast, demanding compensation for the losses incurred by their nationals.[6]

---

[5] Houthoff Buruma, Investment Arbitration, *The role of Bilateral investment treaties*, INTERNATIONAL ARBITRATION 2 (2012) *available at:* http://www.houthoff.com/uploads/tx_hhpublications/Brochure_Arbitration_2012.pdf [hereinafter 'Houthoff Buruma']

[6] Lars Glowinski, International Arbitration - protection of foreign direct investments and foreign investment dispute settlement under ICSID and the bilateral investment treaties,

One of the significant ways in which countries are keen to attract FDI is to address political risk by seeking to adopt bilateral and multilateral treaties towards the protection and promotion of FDI. Today, there have come to be as many as thousands of investment treaties all of which are signed by States across and all over the world. India, for its part, has gone on to conclude over about 80 investment treaties, each with various countries.[7] India is also in the process of talking and negotiating with several countries and organizations towards making many more such treaties. These treaties provide qualifying foreign investors with extensive protection against State interference with their investment. Most significantly, the majority of investment treaties, including all Indian investment treaties, allow investors to bring claims against the Host State for treaty violations directly to international arbitration, without first litigating in the local courts or involving their own government, i.e., the government of the home state on their behalf. The issue of a lack of awareness and the prevalence of misconceptions on investment treaties can mean that investors are consequently unaware of all the protections that are afforded by investment treaties. More particularly, the investors should be aware that under Indian investment treaties the following points are important:

- The conceptual framework of an "investment" protected by the treaty usually extends well beyond to what might be considered traditional notions of FDI. It usually covers a multitude of activities and contributions that might broadly be said to lead to the acquisition of any right or asset by the investor;

- The protection afforded by investment treaties is usually in addition to the normal contractual rights that the investor will have against its counterparty;

- As mentioned above, the protection afforded by investment treaties is directly enforceable by the investor against the Host State – often through international arbitration and without the need to litigate in the Host State's courts; and.

- Indian investment treaties do not just benefit foreign investors investing into India; claims can also be brought by Indian investors against foreign governments

---

available at: http://uctscholar.uct.ac.za/R/?func=dbin-jump- full&object_id=1348& local_base=GEN01.

[7] Dr. Marcus Desax and Dr. Marc, Investment Treaty arbitration in tax matters, *available at:* https://www.walderwyss.com/publications/1277.pdf.

II. The use of Bilateral Treaties

One other option that can be relied on is the entry into a bilateral investment treaty ("BIT"). Since 1959, when the first BIT was concluded between Germany and Pakistan,[8] and since the conclusion of the 1965 ICSID Convention (described further below), an individual or company may have a right of action directly against a host state under a BIT. A BIT serves to protect investments in both countries. This kind of treaty is not meant to provide insurance coverage, but to make it possible to resolve any disputes in an efficient way on the basis of international law. This is especially an attractive option if there is no contractual relationship, e.g. expropriation or the destruction of property in a political riot. Until November 2011, the Netherlands has concluded close to 100 BITs.[9] There are only a few other countries, such as Germany, that have entered into as many such treaties. BITs have acquired great significance for Dutch investors abroad, especially since the financial interests at stake are often considerable. The Dutch BIT system is so significant that even foreign investors are making use of this treaty network by structuring their foreign investments through Dutch holding companies.[10]

This treaty network has other components (which will not be dealt further in this overview). For instance, the Netherlands is a party to the Energy Charter Treaty, a multilateral treaty signed by over 50 countries to provide for substantive investment protection.[11] The protection offered under this treaty is comparable to that provided by BITs. Other well known treaties that offer protection comparable to BITs are the North American Free Trade Association ("NAFTA") and the Association of South East Asian Nations ("ASEAN").

The substratum of the purpose of a BIT, which is a treaty between two countries, is to promote foreign investments between the two countries and to offer protection to investors from one country investing in the other. For that purpose, a BIT contains binding rules on the treatment of investments originating from one country and made in the other. The treaties are always reciprocal. A BIT is normally limited in length, in most cases encompassing not more than 15 articles. Most countries have developed a model BIT on the basis of which they negotiate the final text. Because a BIT is concluded on the basis of negotiations conducted by the two countries, the texts of the various

---

[8] UNCTAD, *The Entry into Force of Bilateral Investment Treaties*, IIA MONITOR NO. 3 (2006) UNCTAD/WEB/ITE/IIA/2006/9 *available at:* http://bit.escwa.org.lb/CMSPages/GetFile.aspx?nodeguid=6f33da83- a49d-48fb-8c0d-a6eec1a0b62e.

[9] Loyens and Loeff, *The Netherlands: Sound and Proven Gateway to the World*, (2007), *available at:* http://www.loyensloeff.com/en-US/AboutUs/CountryDesks/Documents/gatewaytotheworld.pdf.

[10] Houthoff Buruma, *supra* note 5.

[11] *Id.*

BITs can differ considerably. In general, however, most BITs share a certain number of standards, recurring provisions.

Typically, the purpose of a BIT is stated in the preamble or introductory wording, which refers to both, the desire to intensify economic cooperation between the contracting states and, to recognition of the fact that encouraging and protecting investments will stimulate this economic protection. In general, a BIT affords eligible investors certain minimum protection of their investments in a host state. If a host state breaches the substantive protection-related provision in the BIT, in a manner adversely affecting the investor, the latter may (subject to certain conditions, as discussed further) commence proceedings directly against the state. As a result, it is often true that many BITs provide for arbitration by the ICSID when dispute arises between the investor and the host state. ICSID offers a method of resolving investor-state disputes through conciliation or arbitration.

For an individual or company seeking protection, the preliminary matter to be determined is whether a BIT has been concluded with the host state. Whether a BIT is in place can be verified by consulting various sources, including the websites of the Ministry of Foreign Affairs and the World Bank. Most BITs state expressly when the treaty enters into force and when it expires. This is important, because in many cases investments made before a BIT entered into force will not be protected. In more recent BITs, and in most BITs to which the Netherlands is a contracting state have clauses to provide for the protection of investments made in the period before the treaty entered into force,[12] in which case the BIT has retroactive effect.

Once it has been established that a BIT has been concluded with the host state, the next question is whether an investor is entitled to protection under that BIT. To be protected, an investor must be an "investor" within the meaning of the BIT. Generally, a BIT differentiates between individuals and companies. Individuals must have the nationality of one of the contracting states. Whether an individual is a national of a contracting state or not is determined according to the national law of that state. In *Soufraki v. UAE*,[13] which was under the BIT between Italy and the United Arab Emirates, the claimant produced several Italian certificates of nationality. Nevertheless, the tribunal found that the claimant had lost its nationality as a consequence of becoming a Canadian national, for which the claimant was unable to rely on the BIT between Italy and the UAE. Moreover, Canada was not a party to ICSID.

A determination of the nationality of a company is based on three criteria, i.e.

---

[12] *Id.*
[13] Soufraki v. UAE, ICSID Case No. ARB/02/7, Decision on Jurisdiction, (July 7, 2004).

the nation of incorporation of the company, the nation where the company is controlled, and the nation where the company is managed. In general, unincorporated entities and groupings are not entitled to legal protection, but this may depend on the wording in the BIT. For instance, in the Argentina-Germany BIT, the definition of "national" is "any legal person and any commercial or other company or association with or without legal personality".[14]

Generally speaking, to be eligible for protection, a company must have been incorporated in one of the contracting states in accordance with the laws of that state. In *Tokios Tokelès v. Ukraine*,[15] which was under the Lithuania-Ukraine BIT, the claimant was a business enterprise established under the laws of Lithuania but the nationals of the Ukraine owned 99% of its shares. The tribunal nevertheless accepted the claimant as a national of Lithuania. In most of the BITs to which the Netherland is a party, companies controlled by a company or national of a contracting state also qualify as "*investor*". Other countries use different criteria. Germany, for example, considers the country from which a company is managed as determinative of whether a company enjoys the protection of a BIT to which Germany is a party. The United States, on the other hand, considers only the place of establishment to be important. The place where the company conducts its activities or where the management is seated is not relevant in determining whether a company is entitled to protection under a U.S.-BIT. Investors planning international investments, and setting up investment structures are often only led by the tax-related possibilities in the various countries. Such investors should, however, also consider the possible protection of applicable investment treaties. To create such protection, the criteria of the different BITs to which the envisaged host state is a party, should be reviewed and assessed. On that basis, the investor may consider making an investment in a host country through a specially created investment vehicle that is established in a state which is party to a favourable BIT with the host state.

III. Investment Treaty Arbitration

There has been an unprecedented increase in the number of investment treaty arbitrations in the last few years, as knowledgeable and well advised investors have begun to take advantage of the range of protections afforded by investment treaties as per the statistics from ICSID. Although ICSID was established in 1965, in the 35 years till July 2000 it had registered only 66 arbitration cases.

[14] Houthoff Buruma, *supra* note 5.
[15] Tokios Tokelés v. Ukraine, ICSID Case No. ARB/02/18, Decision on Jurisdiction, (Apr. 29, 2004).

Since 2000, the number of cases has grown to nearly 400.[16] India, however, is one of few countries that have not signed the ICSID Convention. As a result, India cannot be a party to ICSID proceedings.

Besides ICSID, other arbitral institutions – such as International Chamber of Commerce ("ICC") and Stockholm Chamber of Commerce ("SCC") – often administer investment treaty arbitrations. Parties may arbitrate under the United Nations Commission on International Trade Law ("UNCITRAL") Arbitration Rules. Indian investment treaties often provide that in the event when either of the parties is not a member to ICSID, then the foreign investors may initiate ad hoc arbitration proceedings in accordance with the UNCITRAL Arbitration Rules.

Other than this, the Permanent Court of Arbitration ("PCA") is an international organization based in Hague, Netherlands. It was established in 1899 through one of the acts of the first Hague Peace Conference, making it the oldest institution for international dispute resolution. The creation of the PCA is set out under Articles 20 to 29 of the 1899 Hague Convention for the specific settlement of international disputes, which was a result of the first Hague Peace Conference. At the second Hague Peace Conference, the earlier Convention was revised by the 1907 Convention for the Pacific Settlement of International Disputes. As of August 2009, 109 countries were party to one or both of these founding Conventions of the PCA. The PCA is not a court in the conventional understanding of that term, but an administrative organization with the object of having permanent and readily available means to serve as the registry for the purposes of international arbitration and other related procedures, including commissions of enquiry and conciliation. It is a permanent framework available to assist temporary arbitral tribunals or commissions. The PCA is housed in the Peace Palace in The Hague, which was built specially for the Court in 1913 with an endowment from Andrew Carnegie. In 1922, the building also housed the distinctly separate Permanent Court of International Justice, which was later replaced by the International Court of Justice ("ICJ") in 1946. Unlike the ICJ, the PCA is not just open to states but also to other parties. The PCA provides services for the resolution of disputes involving various combinations of states, state entities, intergovernmental organizations, and private parties. In the early 1980s, the PCA helped in setting up the administrative services of the Iran-United States Claims Tribunal. The public at large is usually more familiar with the ICJ than with the PCA, partly because of the closed nature of cases handled by the PCA and to the low number of cases dealt with between 1946 and 1990. The PCA's caseload has, however, increased since then. The PCA

---

[16] See Michael Waibel & Yanhui Wu, Are Arbitrators Political?, *available at:* http://www.wipol.uni-bonn.de/lehrveranstaltungen-1/lawecon-workshop/archive/dateien/waibelwinter11-12.

administers cases arising out of international treaties (including bilateral and multilateral investment treaties), and other agreements to arbitrate. The cases conducted by the PCA span a wide range of legal issues, including disputes over territorial and maritime boundaries, sovereignty, human rights, international investment (investor-state arbitrations), and matters concerning international and regional trade. Hearings are rarely open to the public and sometimes even the decision itself is kept confidential at the request of the parties. Many decisions and related documents are available on the PCA website.

IV. Investment Treaties and the provisions offering protection

Some of the more specific contents and matter contained in the form of protections that are provided by investment treaties do tend to vary. Consequently, it is always necessary and important to make sure to check the wording of any particular treaty. There are often important differences – but, a point to note here is that there are certain protections that are common to many investment treaties, including the presence of investment treaties to which India is a party. Some of these relevant protections are set out as below:

A. Protection from expropriation or nationalisation without compensation

Almost all investment treaties, Indian or otherwise, promise market-value compensation in the event of expropriation or nationalisation of their investment to the investors. Generally, expropriation is not prohibited, provided that it is undertaken for a public purpose, being non- discriminatory and keeping in accordance with due process; and is also subjected to prompt, adequate and effective compensation expropriation without appropriate compensation. The process of an abusive process involving the imposition of any kind of a regulatory or a taxation oriented measure may also amount to an indirect form known as "*creeping*" expropriation - if it seems to be eating into the economic value of an investment to the point that it is effectively worthless, notwithstanding that the State may not actually deprive an investor of its property rights. Again, in such situations, the Host State is obliged to compensate the investor. In *CME Czech Republic B.V.* v. *Czech Republic*,[17] which was based on the BIT between the Netherlands and the Czech Republic, an investor in a joint venture in the Czech Republic argued that the joint venture had collapsed after the official Czech broadcasting authority had forced the joint venture to give up its exclusive licensing rights and changed other key terms of the joint venture agreement. The tribunal held that the acts of the Czech authority had interfered with the economic and legal basis of the investment, ruining the commercial value of the investment and, thus, amounting to improper expropriation. The seven decisions in 2008 in which a

[17] CME Czech Republic B.V. v. Czech Republic, UNCITRAL, Partial Award, (Sept. 2001).

claim based on improper expropriation was addressed by an international arbitration tribunal, only in two instances did the tribunal find in favour of the claimant and only in one case did the tribunal actually award damages.[18] However, if a tribunal finds that an investor's property was improperly expropriated and that the host state must compensate the investor, the compensation may be substantial because the compensation is to be based on loss of market value and interest calculated up to the date of the arbitration decision.

B. Fair and equitable treatment

The concerned Host States must not involve themselves or take any arbitrary, grossly unfair or discriminatory measures against foreign investments. They are instead, supposed to provide a transparent and predictable regulatory framework for the investment and respect the legitimate expectations upon which the investors relied when they made their investment. In *Azinian v. Mexico*,[19] a claim brought under NAFTA, the tribunal accepted that in principle the host state could be liable for the decisions of its courts, especially (i) if the courts refused to entertain the suit, (ii) subjected the suit to undue delay, (iii) administered justice in an inadequate way, or (iv) if there was a clear and malicious misapplication of the law. The second, more important category deals with the review of administrative decisions. The majority of such cases have been concerned with the granting or withholding of investment licences or a fundamental change in the law affecting the investment climate. In *Biwater v. Tanzania*,[20] an arbitration proceeding brought under the BIT between the United Kingdom and Tanzania, the tribunal found that a series of public announcements denigrating the investor's poor performance and announced that a new public entity would be taking over the service were in violation of the fair and equitable treatment standard. The tribunal noted that, despite its poor record, the investor "still had a right to the proper and unhindered performance of the contractual termination process [and] the Republic's public statements at this time constituted an unwarranted interference in this".

In *Duke Energy et al. v. Ecuador*,[21] an arbitration based on the BIT between the United States and Ecuador, the Tribunal considered that, for an investor to be protected, the investor's expectations must be legitimate and reasonable at the time the investor makes the investment. It was held that, Ecuador had failed

---

[18] Houthoff Buruma, *supra* note 5.

[19] Azinian, Davitian, & Baca v. Mexico, ICSID Case No. ARB (AF)/97/2 (NAFTA), Award, (Nov. 1, 1999).

[20] Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania, ICSID Case No. ARB/05/22, Award, (July 24, 2008).

[21] Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador, ICSID Case No. ARB/04/19 (US/Ecuador BIT), Award, (Aug. 18, 2008).

to accord fair and equitable treatment to the investor by not implementing the specific payment guarantee expressly promised in one of the investment contracts.

C. Full protection and security

The government of the concerned Host States are under an obligation to ensure that they exercise due diligence by physically protecting the foreign investment, including the investment's officials, employees and facilities. Furthermore, there are a number of investment treaty awards that have gone on to record and suggest that protection and security obligations under a treaty also include a guarantee of regulatory and legal security for investments. In *AAPL v. Sri Lanka*,[22](concerning the United Kingdom-Sri Lanka BIT), Sri Lankan security forces had destroyed the investor's shrimp farm and killed more than 20 of its employees in order to curb Tamil insurgents. On the basis of the full protection and indemnity clause in the BIT, the tribunal found that the Sri Lankan government had violated its obligation of full protection and indemnity by not taking all measures to prevent the killing and the destruction of the investor's property.

In more recent arbitration cases, such as the *Siemens v. Argentina*,[23] arbitration based on the Germany-Argentina BIT, the tribunal confirmed that the standard of fair and equitable treatment extends beyond physical protection to the protection against infringements of the investor's rights by operation of laws and regulations of the host state.

D. Implementation of the principle of National treatment

All foreign investors must be treated equally with local competitors by the host states. Host States cannot offer more favourable conditions to their own nationals or companies, or place more onerous conditions on foreign investors.

E. Implementation of the principle of Most-favoured-nation treatment

The government of the host states often tends to promise not to treat investors of any third State any better than investors of the Home State. The practical effect of this is that investors may be able to rely upon more favourable commitments in other treaties entered into by the Host State. Indian investment treaties, however, often contain exceptions to the MFN principle for the purposes of taxation and obligations imposed by free trade agreements or

---

[22] Asian Agricultural Products Ltd. v. Sri Lanka, ICSID Case No. ARB/87/3, Final Award, (June 27, 1990).

[23] Siemens v. Argentina, ICSID Case No. ARB/02/8, Decision on Jurisdiction, (Aug. 3, 2004).

custom areas. Investors are also sometimes able to benefit from more favourable dispute-settlement procedures in other treaties.

F. Protection against breach of a legal obligation

It is also significant that the host states must and should observe any legal obligation they have entered into with foreign investors or in relation to their investments. While they remain controversial, a number of tribunals have confirmed that the effect of these so-called overarching or as the term denotes - "umbrella" clauses is that the occurrence of a breach of the provisions contained in it by the State of a contract or licence entered into with a foreign investor may also amount to a breach of treaty, attracting international law remedies and procedures.

G. Right to repatriate investment and returns

Most instances of investment treaties typically contain a commitment towards refraining from going out to restrict investors' freedom to transfer both the capital and returns from an investment out of the Host State and into another currency. A small number of Indian investment treaties, however, permit restrictions on this right in order to achieve certain regulatory objectives, such as avoiding balance-of-payment difficulties.

V. Examples

Some examples of investor-state disputes include:

- On the basis of bilateral investment treaties, tobacco giant Philip Morris is suing both Uruguay and Australia over their anti-smoking laws. The company argues that compulsory large warning labels on cigarette packs prevent it from effectively displaying its trademarks, causing a substantial loss of market share. In the case of the dispute against Australia, according to posts on the International Economic Law and Policy Blog,[24] the Philip Morris subsidiary in Hong Kong appears to have bought shares in Philip Morris Australia some months after Australia made public its plans to introduce further regulatory measures for plain packaging to discourage smoking. The share purchase was aimed at enabling the Hong Kong subsidiary to use the Hong Kong- Australia BIT to sue Australia.
- In 2009, Swedish energy multinational Vattenfall sued the German government, seeking 1.4 billion Euros ($1.9 billion) plus interest in compensation for environmental restrictions imposed on one of its

[24] Third World Resurgence, Investment arbitration a 'self-serving' industry, says study,: *available at:* http://www.twnside.org.sg/title2/resurgence/2012/268/econ1.htm.

coal-fired power plants. The case was settled out of court after Germany agreed to water down the environmental standards, exacerbating the effects that Vattenfall's power plant will have on the Elbe River and its wildlife.[25]

- In 2012, Vattenfall launched a second lawsuit seeking 3.7 billion Euros ($4.6 billion) for lost profits related to two of its nuclear power plants. The case followed the German government's decision to phase out nuclear energy after the Fukushima nuclear disaster. Both actions were taken under the Energy Charter Treaty, which includes BIT-like investment protection provisions.[26]
- In 2007, Italian investors sued South Africa over its Black Economic Empowerment Act which aims to redress some of the injustices of the apartheid regime. It requires, for example, mining companies to transfer a portion of their shares into the hands of black investors. The dispute (under South Africa's BITs with Italy and Luxembourg) was closed in 2010 after the investors received new licenses requiring a much lower divestment of shares.[27]
- When Argentina froze utility rates (energy, water, etc.) and devalued its currency in response to its 2001-02 financial crises, it was hit by over 40 lawsuits from investors. Big companies like CMS Energy (US), Suez and Vivendi (France), Anglian Water (UK) and Aguas de Barcelona (Spain) demanded multimillion compensation packages for revenue losses.[28]

VI. India and Bilateral Investment Treaties

India signed its first Bilateral Investment Treaty (BIT) in 1994 with the United Kingdom. Since1994 up till now, India has signed BITs with more than 80 countries, most of which are already in force. The majority of these BITs were actually signed and entered into in the 1990s; nevertheless, India continues to sign more BITs, albeit at a slower pace. For example, India is currently negotiating a BIT with the U.S. and Canada. In addition to this, India has also recently entered into Comprehensive Economic Cooperation Agreements (CECAs) with several countries, including some very important trading partners like Japan and Singapore. CECAs are very comprehensive economic agreements that cover a wide range of issues, including investment, trade, competition policy and intellectual property rights. India is currently negotiating

---

[25] Vattenfall v. Germany I & II, ICSID Case No. ARB/12/12, (May 31, 2012).

[26] *Id.*

[27] Foresti and others v. South Africa, ICSID Case No. ARB(AF)/07/1, Award, (Aug. 10, 2010).

[28] CMS and 40 other companies v. Argentina ICSID Case No ARB/01/8, Award, (May 12, 2005).

CECAs including investment chapters with Indonesia, Mauritius and New Zealand. India is also negotiating a rather ambitious FTA with the European Union. This FTA also includes a separate chapter on the process of investment between India and its own countries. What is amply significant among all this is that, the investment chapters in CECAs and FTAs often contain market-access provisions, which tend to make them stronger instruments of liberalisation rather than BITs, which effectively only tend to deal with post-establishment protections. Owing to this considerably expansive network, India has an investment treaty with as many as 9 of its top 10 sources of FDI, and with as many as 5 of the top 10 destinations for Indian FDI. As a result, therefore, as much as up to 90.2% of all FDI coming into India, and 74.9% of all FDI going out of India, may potentially be protected by investment treaties.[29]

VII. Investment Treaty Arbitrations against India

In the past two years a number of reported investment treaty arbitrations (and potential claims) against India, under various BITs has been witnessed. Before 2011, the only publicly known investment treaty dispute against India concerned the Dabhol Power Project in Maharashtra, where Bechtel and General Electric, each of which held a 10% stake in the USD 3 billion Dabhol power plant, had brought in claims under the India-Mauritius BIT, alleging that their interests in the power plant had been expropriated by the Indian Government. Those claims, however, were settled after India agreed to compensate the investors for their losses. In November 2011, the first publicly known investment treaty award was issued under an Indian investment treaty, after nine years of unsuccessfully trying to enforce an ICC award against Coal India Ltd (a State-owned mining utility) in the Indian courts. White Industries, an Australian mining company which commenced arbitration proceedings under the UNCITRAL against India under the Australia-India BIT. The claim advanced by White Industries primarily rested on alleged breaches of a wide range of substantive protections contained in the Australia-India BIT by both Coal India Ltd. and the Indian Government, including protection against expropriation without compensation and the fair and equitable treatment standard. White Industries also invoked the Australia-India BIT's most-favoured-nation clause and relied on India's obligation to provide effective means of asserting claims and enforcing rights contained in the India-Kuwait BIT.

---

[29] Business-Maps of India, FDI Inflows to Boilers and Steam Generating Plants, *available at:* http://business.mapsofindia.com/fdi-india/sectors/boilers-steam-generating-plants .html.

The Tribunal, which was seated in London for the hearing, ruled that the failure of the Indian courts to resolve White Industries jurisdictional claim over a period of nine years and, in particular, the Indian Supreme Court's delay in hearing the appeal amounted to a breach of India's obligation to provide them with an effective means of asserting claims and enforcing rights. The Tribunal acknowledged that court's congestion and backlogs were relevant factors to consider but did not accept that they constituted a complete defence. Accordingly, the Tribunal ordered India to pay White Industries the original amount as payable under the ICC award with interest. The White Industries award highlights the possibility of using investment treaty arbitration as an alternative route for enforcing commercial awards in circumstances where the foreign investor's efforts are frustrated by delays in Indian courts. The key advantage of procuring a treaty award is that White Industries can enforce the award against Indian assets outside India as opposed to merely against the assets of its former contractual counterparty, Coal India Ltd. India's decision to voluntarily comply with payment of the award is also an encouraging sign that the Indian Government intends to comply with its treaty obligations.[30]

Later, the Indian Supreme Court decision on 2G licenses was also significant. In February 2012, the Indian Supreme Court cancelled 122 2G telecom licenses awarded to various Indian and foreign companies after finding irregularities in the original award process. This ruling meant that several foreign companies that owned investments in the Indian telecom sector will lose the majority, or all, of their licenses. In response, many of them lodged or threatened claims against India under various investment treaties. These claims, for which information is only available through press statements made by the investors or Indian Government officials, were listed as being that a Russian firm, Sistema JSFC, served a notice of dispute in February 2012 under the Russia-India BIT; that a Norwegian firm, Telenor, served a notice of dispute on 27 March 2012 under the India-Singapore CECA, which includes investment protection provisions. Telenor was able to claim these protections as it had entered the Indian market through its Singapore subsidiary; that a Mauritius based investors Capital Global and Kaif Investment, owners of Loop Telecom, served a notice of dispute in May 2012 under the India-Mauritius BIT and that it has recently been reported that the Malaysian firm Axiata Group, which holds approximately a 20% stake in Idea Cellular, has launched a claim under the India-Mauritius BIT. Axiata had routed its investment through Mauritius.

Aside from investment treaty claims arising out of the Indian Supreme Court's

---

[30] India: Investment treaties stifle public policy objectives, *available at:* http://donttradeourlivesaway.wordpress.com/2012/04/28/india-investment-treaties-stifle-public-policy- objectives.

decision to cancel 2G telecom licences, there are several other treaty claims pending against India. These are plenty including within its fold the fact that Vodafone, a UK-based telecom major, served a notice of dispute on 17 April 2012 under the India-Netherlands BIT. Vodafone's claim relates to the recent amendment to the Indian Income Tax Act which allows tax authorities retrospectively to tax overseas transactions in which an Indian asset is transferred. The amendment effectively overturns the Indian Supreme Court's decision in *Vodafone International Holdings v. Union of India*[31] in 2012, where the Court dismissed a USD 2.6 billion tax demand made by the Indian authorities in relation to Vodafone's acquisition of the Indian mobile assets of Hutchison Essar in 2007. A UK-based hedge fund, The Children's Investment Fund ("TCI"), served a notice of dispute on 16 May 2012 under the Cyprus-India BIT, alleging mismanagement by the Indian Government of the 90% State-owned Coal India Ltd., in which TCI owns a minority stake. A Russian firm, Bycell, served a notice of dispute on 18 June 2012, alleging violations of both the Russia-India and Cyprus-India BITs. Bycell's claims relate to a decision taken by India's Foreign Investment Promotion Board in 2009 to withdraw certain security clearances that had earlier been granted to the investor.

The Investment treaty claims brought by Indian investors were significant. While it is in principle a difficult task to count the exact number of arbitrations (pending or concluded) brought by Indian investors, the only publicly known instance where an Indian national has brought a claim under a BIT concerns a dispute between the Indian national and a local UK authority over payment of rent. A Court of Appeal decision in 2008, *City of London v. Ashok Sancheti*,[32] revealed that the UK Government was defending an investment treaty arbitration commenced by Sancheti, a lawyer of Indian nationality, under the ambit of the India-UK BIT. The arbitration concerned outstanding rent owed by Sancheti to his landlord, the City of London Corporation (the Corporation), in relation to office premises rented by Sancheti in London between the period 2001 and 2004. In the BIT arbitration, Sancheti alleged that he had been the subject of targeted harassment and racial discrimination by the Corporation and various organs of the UK, as a result of which he had been forced to stop his law practice at the premises. The Corporation had commenced separate proceedings against Sancheti in a County Court, claiming the rent allegedly due. In response, Sancheti made an application for a stay of proceedings under the Arbitration and Conciliation Act 1996 ("Act") on the ground that he had already invoked the arbitration provisions in the BIT. In the leading judgment, Lawrence Collins LJ held that the Corporation was not a party to the India-UK BIT and therefore any award made in Sancheti's favour in the BIT arbitration would

---

[31] Civil Appeal No.733 OF 2012 (arising out of S.L.P. (C) No. 26529 of 2010).
[32] EWCA Civ 1283 [2008].

not bind the Corporation.[33] On that basis, the Court of Appeal dismissed Mr Sancheti's application for a stay of proceedings. It is not known whether Sancheti continued to prosecute his BIT claim despite the Court of Appeal's decision and, if so, what was the result of the BIT arbitration. Practical considerations Investment treaty protection is not merely fortuitous; it can be maximised. Foreign investors in India, and Indian investors investing abroad, should consider certain factors early in the drafting stage of any transaction or project to seek to ensure they can benefit from treaty protection.

Potential investors should consider whether there is additional legal protection available from any applicable investment treaty. If a proposed investment does not benefit from the potential protection of an investment treaty, it may be possible to consider restructuring the manner and entities through which the investment is proposed to be made as such that the investor can avail itself of treaty protection. If the transaction does come under the protective umbrella of an investment treaty, then it is still worth considering, at the contract formation stage, whether there are any steps that can be taken to enhance the investor's position. Issues to consider include: the nationality and standing of the investor, especially in light of its position in any chain of holding companies; whether the transaction qualifies as an "investment" under the treaty; if the counterparty is a State entity, the appropriate dispute settlement provisions. For example, it is possible to draft a clause that allows recourse to local courts for interim measures, waives sovereign immunity for executing the award, sets out in advance how costs are to be divided and specifies where the arbitration will be located; and whether dispute resolution procedures in any project or contract documents are consistent with applicable investment treaty procedures.

VIII. Enforcement of a Bilateral Treaty through Investment Arbitration

Most BITs provide for a cooling-off period that must lapse before proceedings can be initiated. The cooling-off period serves to allow the parties the opportunity to explore a settlement. Generally, this cooling-off period starts on the investor sending a "trigger letter" to the highest authorities of the host state, such as the head of state or the ministry dealing with the investment. The letter briefly sets out the facts and the nature of the dispute and requests the host state to enter into negotiations. If the negotiations do not succeed—often because of a lack of response by the host state—an action can be commenced against the host state.

Resort may be had to ICSID arbitration. The BIT, furthermore, directs by which

---

[33] The Mayor And Commonalty & Citizens Of The City Of London v. Ashok Sancheti EWCA Civ.1283 [2008].

action can be taken. The most common dispute resolution option is the submission of the dispute to arbitration according to the ICSID Convention, Regulation and Rules. For example, the Dutch model BIT provides that a dispute between an investor and a host state must be submitted to arbitration according to the ICSID Convention, Regulation and Rules:

> "*Each Contracting Party hereby consents to submit any legal dispute arising between that Contracting Party and a national of the other Contracting Party concerning an investment of that national in the territory of the former Contracting Party to the International Centre for Settlement of Investment Disputes for settlement by conciliation or arbitration under the Convention on the Settlement of Investment Disputes between States and Nationals of other States, opened for signature at Washington on 18 March 1965.*"[34]

Other arbitration options also exist. Other common options are ad hoc arbitration under the arbitration rules of the UNCITRAL ICC or the SCC. It is beyond the scope of this booklet to look at the arbitration rules of all these arbitration tribunals. Because of ICSID's special nature, its specific rules and regulations, and the fact that most investor-state disputes are settled under its rules, we will focus below on arbitration conducted according to the ICSID Convention, Regulation and Rules. Arbitration can be relied on as a last resort. Finally, certain BITs require that a dispute must first be submitted to the national courts of the host state.

Originally, investor-state arbitration was envisioned for instances of straightforward expropriation, such as when the government took over a factory. But the system has spun out of control with multinationals using it to chase down lost profits. The last two decades have seen a number of multimillion-dollar claims against the alleged effects of public legislation. 'Developed and developing countries on every continent have been challenged for tax measures, fiscal policies, bans on harmful chemicals, bans on mining, requirements for environmental impact assessments, regulations relating to hazardous waste etc. Sometimes, the threat of a dispute has been enough to freeze government action, making policymakers realise they would have to pay to regulate.'

According to the report, these legal challenges have raised a global storm of critical objection to investment treaties and arbitration. Some countries have realised the injustices and inconsistencies of international investment arbitration and are .trying to abandon the system. In spring 2011, the Australian government announced that it would no longer include investor-state dispute settlement provisions in its trade agreements. Bolivia, Ecuador and Venezuela have terminated several BITs and have withdrawn from ICSID,

[34] Houthoff Buruma, *supra* note 5.

sending a clear political message that they refuse to cooperate in the future. Argentina, which has been swamped with investor claims related to emergency legislation in the context of its 2001-02 economic crises, refuses to pay arbitration awards. South Africa has announced that it will not renew old investment treaties due to expire. And India is reported to have decided not to include investor-state dispute provisions in future free trade agreements (after the government was sued for carrying out the orders of the country's Supreme Court to cancel some 2G band telecommunication licenses over scam and corruption charges).

In another case, just reported in the Economic and Political Weekly, a Singapore-based arbitral tribunal has criticised the Supreme Court of India and the Indian judiciary for its delays in hearing and disposing of cases, and asked the Indian government (which under the Indian Constitution has no control over the judiciary) to compensate an Australian party, having a contract dispute with an Indian firm, for these delays.[35] According to the TNI-CEO report, the UN has recognised that international investment agreements can severely curb states' abilities to fight financial and economic crises. Argentina has been sued more than 40 times as a result of the economic reform programmes implemented after its economic crisis in 2001. By the end of 2008, awards against the country had reached a total of $1.15 billion. That's the equivalent of the average annual salary for 150,000 Argentinean teachers or 95,800 public hospital doctors.

IX. Conclusion

The ADR mechanism can be effectively used to settle investment disputes by modifying it as per the need. It is time effective and cost efficient. It can also overcome the geographical hurdles. However, there are certain issues revolving around ADR mechanism like the need for personnel with knowledge of investment, sufficient understanding of ADR and law; technical concerns; legal sanctity of proceedings; industry support and such other matters. But these hurdles are just a passing phase. The use of ADR mechanisms for resolving online disputes is increasing day by day. A number of web-sites provide for some type of investment dispute resolution method like arbitration, negotiation, mediation etc. and also certain conflict management services. These services fall into the general categories of complaint handling, negotiation, mediation and arbitration. These services will be in great demand in the future. As the Act, 1996 has given paramount importance to "party autonomy" by accepting the intention of parties as a platform for dispute resolution. Thus, what law will be applicable will depend on the intention of parties.

---

[35] Investment arbitration a "self-serving" industry, says study, *available at:* http://www.ftamalayasia.org/article.php?aid=305.

If the parties have adopted the mechanism of investment dispute resolution, then it will definitely apply with necessary minor modifications. The language used in various sections of the Act give options to the parties to opt for the procedure as per their agreement during the arbitral proceedings before the arbitrator. So if there is an agreement between the parties with regard to the procedure to be followed by the arbitrator, the arbitrator is required to follow the said procedure. However, this would not mean that in appeal parties can contend that the appellate procedure should be as per their agreement. The appellate procedure would be governed as per the statutory provisions and parties have no right to change the same. It must be noted that party autonomy presupposes the existence of an arbitration agreement. There may be a situation where the parties had not entered into an arbitration agreement. If the parties agree to arbitration, then the provisions of the Act will apply and that will go outside the stream of the court.

The idea of investment arbitration as a fair and independent space to resolve disputes between multinationals and governments is one of the key justifications for a system which has cost taxpayers dearly and undermines the capacity of sovereign governments to act in the interests of their people. According to the report, 'the alleged fairness and independence of investment arbitration is an illusion. The law and the consequential disputes are largely shaped by law firms, arbitrators and, more recently, a phalanx of speculators who make a lot of money from the disputes.' Driven by their own profit interests, this 'arbitration industry' actively encourages an ever-growing number of corporate claims, while creating the necessary legal loopholes and funding mechanisms for its continued functioning. This industry is also responsible for growing its own business with pro-investor interpretations of the treaties.

The world of Alternative Dispute Resolution ("ADR") represents an unconventional medium for most disputes. ADR offers a system with practical flexibility, a broad range of corrective options, and a focus on individualized justice. ADR performs convenient and useful works that cannot be done, or cannot easily be done, through formal adjudication.[36] And in every case in which one of the various modes of ADR offers a process or reaches a result that differs materially from those of the formal courts, there is in fact a rival system.[37] In complete contrast to conventional litigation, ADR offers an alternative system for relief from the hardship created by the substantive and procedural law of formal adjudication. The freedom and simplicity of ADR bear a striking similarity to traditional Equity, offering relaxed system of evidence and procedure, and a simpler and less legalistic structure, improved

---

[36] Scott H. Blackmand and Rebecca M. McNeill, *Alternative Dispute Resolution in Commercial Intellectual Property Disputes*, 47 AM. U. L. REV. 1709, 1734 (1998).
[37] Thomas O. Main, *ADR: The New Equity*, 74 U. CIN. L. REV. 329 (2005).

access to justice, and a casual relationship with the substantive law. Such measures are welcome, but litigation has always been perceived as too slow and expensive.

There are several reasons why ADR is relevant in disputes relating to investment issues and conflicts. Investment related litigation is frequently more complicated and difficult to comprehend than other types of litigation. In addition, the monetary costs of litigation can be sky-high, often due to the costly discovery process necessary in such disputes. Because of the lengthy discovery process typical of investment disputes, they often drag on for excessive periods of time. One of the best reasons to apply ADR to investment disputes, however, is its ability to provide a flexible resolution which benefits all people involved. ADR offers a cheaper, faster, more creative, and mutually beneficial solution. Investment Laws require an ability to understand scientific or technical concepts. This obligation might prevent key figures from clearly understanding the issues before them. In ADR, parties can select neutrals that are familiar with the particular type of technology or process at issue. This will likely result in a fairer resolution to both parties, as the neutral can concentrate on the details and specifics of the case, as opposed to trying to learn or better understand the technical process. Investment law is not entirely scientific or technical but there is a considerable necessity to understand the technicalities that go into allowing the industry function comfortably. Although it may sound like a simple task for a typical jury or judge, the process of understanding and comprehending newer forms of technology can be difficult and confusing.

In the last decade, international investment law and arbitration have grown exponentially, as a result of the growth in foreign direct investment in the world and investors' increasing reliance on investment treaties to bring arbitration proceedings against host States. It is a fast evolving field of law and dispute resolution which presents numerous difficult issues and can only be handled effectively with adequate specialized knowledge. Most investment arbitrations nowadays are brought on the basis of bilateral or multilateral treaties (BITs, NAFTA, the Energy Charter Treaty, etc.) and are conducted under the ICSID Convention, UNCITRAL Arbitration Rules, or less frequently also under the Arbitration Institute of the Stockholm Chamber of Commerce, ICC and LCIA arbitration rules.

Once again, the presence of an informed neutral that is familiar with investment law can make the process more efficient and tolerable for both parties. At the other end of the investment law spectrum, is the birth of environmental issues which falls under the ambit of investment law, and protects larger and greater global concern. The advantages of ADR are reduced time and cost and a neutral forum, which take on increased significance in the field of investment disputes because investment litigation tends to be lengthy, costly, and implicates the laws and residents of several jurisdictions simultaneously. These advantages more than compensate for any shortcomings due to the use of streamlined procedures. The creation of Arbitration Centres has resulted in a valuable asset for all those in the investment industry.