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INVESTMENT TREATY ARBITRATION AND DEVELOPING COUNTRIES: WHAT NOW & WHAT NEXT

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INVESTMENT TREATY ARBITRATION AND DEVELOPING COUNTRIES: WHAT NOW AND WHAT NEXT? IMPACT OF WHITE INDUSTRIES V. COAL INDIA AWARD

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For the first time in its long history of having signed more than 80 Bilateral Investment Treaties ("BITs"),[1] the Government of India has paid due to an arbitration award, brought by a private party, White Industries, of Australia, under the India-Australia BIT.

The ground for the award was that India did not comply with its obligation under the BIT to provide "effective means of asserting claims and enforcing rights" due to judicial delay of about eight years in respect of an arbitration award obtained by White Industries. The award was under challenge and an issue arising there from was under consideration of the Supreme Court of India.[2]

It is reported that the Government of India has agreed to "honour the award" and pay. It is, however, not known if the Government of India has appreciated the significance of the award nor if it is reviewing the existing BITs to ensure that there will not be repetition. In absence of transparency, everyone can only speculate.

However, careful analysis is required not only for its implications on other BITs but also for its effect on separation of powers provided for in our Constitutional polity. How far delays in courts could make the executive branch of the government responsible for its failure to provide "effective means to assert claims and enforce rights".

Although White Industries was the first case that gave a jolt to the Government of India, more jolts are on the way. After the Supreme Court cancelled 122 2G licences issued by the government,[3] private parties like *Telenor of Norway* and *Sistema of Russia*, relying upon the BITs that India has with their countries, have commenced or threatened to commence BIT arbitrations.[4]

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[1] *Available at:* http://finmin.nic.in/bipa/bipa_index.asp.

[2] The case was disposed of, as a part of a group of cases, by the Supreme Court in September 2012, along with the Bharat Aluminium case reported in (2012) 9 SCC 552.

[3] Centre for Public Interest Litigation v. UOI, (2012) 3 SCC 1, ¶ 60.

[4] *Available at:* http://rusembassy.in/index.php?option=com_content&view=article&id=5279%3Arussia-threatens-arbitration-on-2g-license-cancellation-for-

The effect is not just large economic loss. The effect is also political, and affects our political relations with not one but a circle of countries.

For example, in the *Sistema 2G* case, the Russian Embassy issued a statement on October 30, 2012 that stated that Russia is "very upset" about the Supreme Court decision on Sistema and that if the issue is not resolved, then it would have 'great repercussions' on Indo-Russian bilateral cooperation. Strong words, indeed.

This is ominous, as unlike some other cases, Sistema declined to apply for a fresh licence process. Sistema has sent a formal notice to Indian authorities, claiming that cancellation of the licence is contrary to India's obligation under the Indo-Russia BIT.

What are the lessons for India? There is little doubt that India needs Foreign Direct Investments ("FDI"). However, it should take decisions on FDI only after knowing its costs. Before we discuss the costs, it is useful to understand the background of how these BITs came about.

I. HISTORICAL BACKGROUND

The history of international investment law is a story of two competing objectives: one, protecting private property rights, and two, advancing social objectives. When, for example, a nation begins its economic development, it needs liberalisation in the sense that it follows the policies of welcoming FDI. A stage may be reached, when the State may conclude that the continuation of FDI is contrary to its social, economic or environmental objectives. The State may also conclude that it is essential in social interest, to exercise greater control over the investment than was being done so far. The State thereupon exercises its power in some way that affects the investment of the foreign investor for which the foreign investor does not get adequate compensation, which the foreign investor describes as expropriation.[5]

The classical way in which the international investment law dealt with this was that the countries providing FDI would require the countries to follow a

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sistema&catid=16%3Apress-on-bilateral-relations&lang=en.

[5] For a recent example, see the dispute between Chevron, a US company and Ecuador. There, Ecuador claims that Chevron's FDI led to serious environmental concerns and therefore it nationalised partly its subsidiary. Chevron claims compensation for nationalisation and Ecuador claim compensation for damages to environment; *Available at:* http://www.ft.com/cms/s/0/364e2f30-751d-11e2-8bc7-00144feabdc0.html#axzz2Pzm8zUC.

minimum standard of treatment.[6]

However, no "*minimum standard of treatment*" was universally accepted. Hence, the remedies ranged from either giving up the matter altogether (as for example, what happened to Coca Cola in India in 1977)[7] or topple the government by force (as happened in the case of Iran in 1952, when the Anglo-Persian Oil Co was nationalized).[8]

In 1980s, when many countries in the world accepted globalisation, the "*minimum standard of treatment*" began to be spelled out in the form of BITs and Free Trade Agreements ("FTAs").

In principle, the BITs and FTAs originally provide for investor rights, including, in particular, (a) a right to fair and equitable treatment and (b) a right to compensation upon expropriation and, (c) investor-State arbitration mechanism. The modern BITs often provide for greater protections, as will be discussed later in this article.

The objective of providing these rights is, generally speaking, two-fold: (a) to enable the developed countries to secure rights for their investors in markets offered by developing countries; and (b) to ensure that developing countries secure such rights of investors so as to attract necessary investment.

For developing countries, however, the dilemma is: they want foreign investments but wish to keep power to take decisions on how far in public interest the investments should be allowed to go; For developed countries, the dilemma is that they want markets for products and services, but do not want to be stopped in the middle because of perceived public interest.

In absence of a clear definition or acceptance of the concept of 'public interest', situations of conflict are bound to arise. For example, a country A may want to develop transport sector and for that purpose enters into a BIT with a country B. B's investors may make substantial investment and due to its modern management techniques may lead to near monopoly situation. The government of A may want to or need to regulate the expansion by claiming it to be in public interest. The foreign investor may disagree.

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[6] This concept is found in several investment agreements. It means that the host country will accord treatment to investments of foreign investors in accordance with the international norms.

[7] *Available at:*
http://www.nytimes.com/2006/08/07/business/worldbusiness/07cnd -soda.html?_r=0.

[8] *Available at:*
http://www.iranchamber.com/history/oil_nationalization/oil_nationalization.php.

The BITs are drawn up on the basis of these compromises. The situation stated in the previous paragraph can be imagined in advance and planned for by those writing the BIT.

However, there are innumerable situations in which this does not happen. For example, in February 2012, Indonesia passed a law requiring foreign mining companies to divest 51% of their holdings to an Indonesian partner after ten years. The government wants more money from mining of the rich deposits to build better infrastructure. Not everybody agreed. "The government regulation ... is impossible for foreign mining investors. It's impossible if in only 10 years after production they have to divest 51 percent of their stake in the mines," said the mining association's Abubakar. India's Adani Enterprises had also invested in mines in Indonesia. That soon after the news, the share value of Adani Enterprises fell by 9% shows the effect of such announcements.[9]

Another example: In May 2012, Argentina expropriated half of Spanish oil giant Repsols investment in YPF, leading to what is known as Shale wars. Argentina claimed that Repsols failed to keep its investment promises and instead funnelled profits out of the country through dividend payments. Repsols, which had 57% stake in the Argentianian subsidiary, found its 51% taken away by what it claimed was expropriation. Repsols demanded €8 bn (equal to around INR 4,800 crores) as compensation, while Argentina not only rejected the figure, but also claimed compensation for environmental damage.[10]

These conflicting versions would have to be resolved peacefully, for which the BITs or Regional Treaties (such as NAFTA) or Multilateral Treaties (such as ICSID or the proposed Trans-Pacific Partnership or TPP) provide for International investment arbitration. The question is whether this is a fair and just solution.

II. WHITE INDUSTRIES V. COAL INDIA BIT AWARD

In the *White Industries* case,[11] the brief facts were these: In 1989, White Industries Australia Ltd. entered into a contract with Coal India for supply of equipment to and development of a coal mine in India, which contained an ICC arbitration clause.

Disputes arose between the parties leading to, in 1999, arbitration in London.

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[9] *Available at:* http://www.mineweb.com/mineweb/content/en/mineweb-political-economy?oid=146885&sn=Detail.

[10] *Available at:,* http://www.forbes.com/sites/afontevecchia/2012/04/17/shale-gas-wars-on-argentinas- nationalization-of- repsol-ypf/.

[11] *Available at:* http://ilcurry.files.wordpress.com/2012/02/white-industries- award-ilcurry.pdf.

The arbitration led to an award in May 2002. The award was granted by a majority (the arbitrator appointed by Coal India, Mr. Justice B P Jeeven Reddy, dissented). On September 6, 2002, Coal India applied to Calcutta High Court for setting aside the award, in accordance with Section 34 of the Arbitration and Conciliation Act, 1996 ("the Act"), as it was entitled to do at the time in view of the law laid down by the Supreme Court of India in the *Bhatia International* case.[12]

On September 11, 2002, White Industries, not knowing about the petition before the Calcutta High Court, applied to the Delhi High Court for execution of the award as a decree in accordance with section 49 of the Act. White Industries then petitioned to the Supreme Court for transfer of the Calcutta case and also questioned the jurisdiction of the Calcutta High Court to examine the matter. As the matter made no progress until 2010, White Industries initiated BIT arbitration.

The BIT tribunal gave an award on November 30, 2011 in favour of White Industries, directing India to pay AU$4.08 mn to White Industries plus interest and costs.[13] Briefly, the findings of the Arbitral Tribunal were as follows:

- What White Industries had done under its contract with Coal India was 'investment' as defined in the India- Australia BIT.
- India had not failed to fulfil the legitimate expectations of White Industries of Indian judiciary in not entertaining the application of setting aside the international award made in favour of White Industries, as those expectations were not legitimate, because the Indian courts were regularly entertaining the issues arising out of its enactment pertaining to the New York Convention.[14]
- The Arbitral Tribunal also found that White Industries knew or ought to have known that the Indian courts are overburdened and therefore there was no 'denial of justice' or absence of 'fair play'.
- The India-Australia BIT contained the Most Favoured Nation clause ("MFN"). This meant that White Industries was entitled to the same treatment as other investors under other BITs.
- India was guilty of violating the India-Australia BIT because India did not provide "effective means of asserting claims and

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[12] Bhatia International v. Bulk Traders, S A (2002) 4 SCC 105.

[13] *Available at:* http://ilcurry.files.wordpress.com/2012/02/white-industries- award-ilcurry.pdf.

[14] That was an error as, if the New York Convention applied, Part II, and not Part I of the 1996 Act would apply. The issue was whether Part I, in which s. 34 is situate, would apply because of Bhatia's case. Ultimately, White Industries won a pyrrhic victory, as court overruled Bhatia but applied it prospectively. Effectively, therefore, White Industries lost.

enforcing rights", which the slowness of Indian judicial system made it impossible to comply.

- To the argument of India that India made no such commitment in India-Australia BIT, the Arbitral Tribunal's answer was to find that standard of "effective means of asserting claims and enforcing rights" was found in India-Kuwait BIT in its MFN clause.[15] Since in one means MFN in all, it applied to the case in hand.
- For determining the meaning of "effective means" standard, the Arbitral Tribunal relied upon the controversial arbitral award of 27 August, 1993 of *Chevron-Texaco v. Ecuador*. There the standard laid down was that the State that agrees to provide such a standard "*requires that the host State establish proper system of laws and institutions and that those systems work effectively in any given case*."

This finding is extraordinarily damaging to India. The judiciary in India is completely independent and separate in India from the executive branch. The Constitution of India does not confer power on either the executive or legislative branches to direct the judiciary to "work effectively in any given case". It is difficult to believe that these facts were not known to the arbitral tribunal that consisted of three well-known arbitrators, all from common law jurisdictions and obviously familiar with India's Constitutional structure.

White Industries could not have complained that other similar cases were being given preference over its case. Each Contracting State shall provide effective means of asserting claims and enforcing rights with respect to investments and ensure to investors of the other Contracting State the right of access to its courts of justice, administrative tribunals and agencies and all other bodies exercising adjudicatory authority, accompanied with the right to employ persons of their choice, for the purpose of the assertion of claims and the enforcement of rights with respect to their investments.

In fact, the case of White Industries was awaiting trial as it was referred to a larger bench of the Supreme Court, was heard along with a similar case where the petitioner was Bharat Aluminium, and was decided on September 6, 2012 along with the case of Bharat Aluminium.[16]

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[15] Article 4(5) of the India-Kuwait BIT provides: "Each party shall … provide effective means of asserting claims and enforcing rights with regard to investments …". Each Contracting State shall maintain a favourable environment for investments in its territory by investors of the other Contracting State. Each Contracting State shall in accordance with its applicable laws and regulations provide effective means of MFN.

[16] *See,* Bharat Aluminium Co. v. Kaiser Aluminium Technical Services Inc., (2012) 9 SCC 552. It was pleaded by both Bharat Aluminium and White Industries that Bhatia International had to be overruled. The court accepted the contention but applied it

As the Tribunal's ruling stands, the only solution appears to be that India should review the MFN provisions in its BITs and provide for exception in relation to the time taken by the courts.

There is another important point to be made. The Arbitral Tribunal held that all contractual rights, tangible or intangible are capable of being expropriated.[17] More importantly, in its view, the tribunal held that the foreign arbitral award itself is capable of being expropriated. There are cases that both support and oppose this statement of principle.[18]

It is true that the Tribunal refused White's plea that India had violated any of contractual rights and also that the award was expropriated as the case was pending in the court, nevertheless, these are warning signs for the government to take appropriate action to review other BITs.

It is regrettable that instead of challenging the award and publicly examining the potential effects of the findings of the Tribunal, the government of India is reported to have accepted the award and agreed to pay according to its terms. The effect on other investors is that they are emboldened to make similar claims of far larger amounts. Public Citizen, a US blog, in a somewhat but not materially different context said that the dispute resolution system in such BITs "exposes signatory countries to vast liabilities, as foreign firms use foreign tribunals to raid public treasuries"[19]

An open letter signed by former judges, law professors and prominent lawyers warns: "The foreign investor protections included in some … BITs, and their enforcement through Investor-State arbitration… threaten to undermine the justice systems in our various countries and fundamentally shift the balance of power between investors, states and other affected parties in a manner that undermines fair resolution of legal disputes".[20]

The final words of these former judges, law professors and prominent lawyers were:

"WE THEREFORE CALL UPON all governments engaged in the TPP

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prospectively to agreements entered into on or after September 6, 2012, thereby effectively rejecting the White Industries case that the foreign award could not be set aside under Part I.

[17] The Award, ¶¶ 12.3.1 - 12.3.2.

[18] For one view, see Saipem S p A v. Bangladesh, ICSID Case no. ARB/05/07, (March 21, 2007) and for an opposite view see GEA Group Aktiengesellschaft v. Ukraine, ICSID Case no. ARB/08/16, (March 31, 2011).

[19] *Available at:* http://www.citizen.org/documents/Leaked-TPP-Investment-Analysis.pdf.

[20] *Available at:* http://tpplegal.wordpress.com/open-letter/.

> negotiations to follow Australia's example by rejecting the investor-state dispute mechanism and reasserting the integrity of our domestic legal processes."

It is ironical that India's first experience of BIT, in which an Australian company won, was Australia's last.

DEFINING "INVESTMENT" – A DEVELOPMENTAL PERSPECTIVE

Aniruddha Rajput[*]

I. Introduction

There is hardly any area of international law, as divided and disputed as investment treaty arbitration[1]. The deep divide is an outcome of serious implications that it has on the exercise of sovereign power by the States. Investment treaties severely curtail regulatory freedom of States.[2] There is obviously a serious concern for the States, since their exercise of sovereignty is amenable to review before a private international tribunal, operating on commercial arbitration principles which would be otherwise performed by domestic courts under the umbrella of public law.[3] On the other hand, investor oriented approaches insist that since a foreign investor is risking an investment – the transaction should be treated as a mere private and contractual dispute.[4] This leaves nearly every aspect of investment treaty arbitration prone to vulnerability of severe disagreement. One such contested area is the definition of "investment".

The jurisdiction of an arbitral tribunal constituted under an investment treaty - bilateral investment treaty ("BIT") or an investment chapter in a free trade agreement ("FTA"), is limited in its scope by *rationae materiae*. In other words, the tribunal should have jurisdiction over the subject matter of a dispute. A dispute must arise out of an investment. The investor has to first establish that the activity claimed falls within the definition of 'investment' in the investment treaty under which the proceedings are initiated. It is possible that the host State might have breached its substantive obligations under the

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[1] M SORNARAJAH, THE INTERNATIONAL LAW AND FOREIGN INVESTMENT 1 (3rd ed. 2012); Some even dispute whether international investment law belongs to international law and argue for a different approach by treating it as an autonomous regime. However, the purpose of this article is not to venture into that debate. See International Thunderbird Gaming Corporation v. The United Mexican States (Jan. 26, 2006)(dissenting opinion of Thomas Waldetb), STEPHEN W. SCHILL, INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW (2010).

[2] Prabhas Ranjan, *Definition of Investment in Bilateral Investment Treaties of South Asian Countries and Regulatory Discretion,* 26(2) J. INTN'L ARB. 217, 225-226 (2009).

[3] GUS VAN HARTEN, INVESTMENT TREATY ARBITRATION AND PUBLIC LAW (2007); Gus Van Harten & Martin Loughlin, *Investment Treaty Arbitration as Species of Global Administrative Law,* 17(1) EUR. J. INTN'L L. 121, 145-148 (2006).

[4] RUDOLPH DOLZER & CHRISTOPHER SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW, 19-20 (2nd ed. 2012).

treaty, but if the investor fails to establish that an investment was made, within the definition of the treaty, the tribunal cannot proceed. The question of determination of existence of an investment is therefore a jurisdictional question.[5] The crux is - whether an investor has made an "investment" as all consequential rights depend on it.

The definition of investment has serious implications for developing countries. If an investment is interpreted widely, it will grant a broad jurisdiction to the arbitral tribunal and allow it to review the actions of the host State. But if the tribunal adopts a strict approach, the investor cannot lay open the allegations of breach of substantive standards of treatment. There is a lot more to the definition of investment itself, *albeit* the ingredients of the definition of an investment specified in the investment treaty. For the first time, the ICSID[6] tribunal in *Salini*[7] held that investment has its own meaning and laid down four objective tests that are to be satisfied to determine the existence of an investment – namely, contribution of investor, duration, existence of operational risk and contribution to the host State's development.[8]

Ever since the objective elements are identified, controversy has sparked as to the appropriateness of an objective test, especially the rationale of the four-test approach. This article emphatically argues for an objective approach to define investment generally and particularly the last criteria of the *Salini* test that is "contribution to the economic development of the host State". Contribution to economic development is a topic dear to the heart of developing countries. After the ravage of colonial exploitation and under-explored potential of their economies, developing countries looked towards foreign capital as a route for growth and prosperity. It is not certain and is unproved yet, that the BITs result into greater inflows of capital. The claims that merely entering into investment treaties will bring investment are unsubstantiated and subject to doubt.[9] But one thing is clear, that if incoming

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[5] In practice, tribunals decide it at the jurisdictional stage itself or decide at the stage of rendering a final award; See Yv es GL Wolters, *The Meaning of "Investment" in Treaty Disputes: Substantive or Jurisdictional?: Lessons from Nagel v. Czech Republic and SD Myres v. Canada,* 8 JOURNAL OF WORLD INVESTMENT AND TRADE 175 (2007).

[6] Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Mar. 18, 1965, 575 U.N.T.S. 159 [hereinafter ICSID Convention].

[7] Salini Costruttori S.P.A. and ltalstrade S.P.A. v. Kingdom of Morocco, ICSID Case no.ARB/OO/4, Decision on Jurisdiction, (July 23, 2001)[hereinafter '*Salini v. Morocco*].

[8] CHRISROPH SCHREUER, LORETTA MALINTOPPI, AUGUST REINISCH & ANTONY SINCLAIR, THE ICSID CONVENTION: A COMMENTARY, 140 (2nd ed. 2009).

[9] Jeswald W Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries,* 24 INT'L LAW. 655, 673-675 (1990); MARY HALLWARD-DRIEMEIER, WORLD BANK, DO BILATERAL INVESTMENT

investments do not contribute to development then their utility for the developing world is in question. Thus, this article argues for a developmental approach for defining investment.

The structure of this article is as follows. Part II and III give a foundation, since they focus on the need to define these standards. An exposition of their contents would underscore the point that developing countries shall not be exposed to uncertainties and adoption of unnecessarily broad interpretations to severely restrict their regulatory discretion. Part II discusses the notion of investment. It argues for an objective determination of the meaning of an investment, in contrast to the adoption of a category-based approach. It presents arguments based on treaty interpretation and course adopted by tribunals in that direction and their justifications for defining the notion of investment. Part III starts by discussing the problems that would arise for developing countries, if the notion of investment is not taken into account. An argument based on hazards of portfolio investment is advanced to make a case for exclusion of transactions, which do not have a lasting relationship with the host State and therefore cannot claim to be an investment due to their nature. It then looks at the situation prior to the evolution of the *Salini* test. Part IV puts the position of *Salini* test in the ICSID context and discusses the ambivalence in its application. It then looks at awards that have applied the *Salini* test in a non-ICSID arbitration. Part V discusses the last strand of the *Salini* test – contribution to development of the host State. This aspect is highly relevant for developing countries and certain doubts are cast on its scope and application. This part will speak for retention of the test and reasons for doing so. This is followed by Part VI which contains policy arguments for taking a developmental perspective. The argument is based on the historic development of BITs and how they are different from the Friendship Commerce and Navigation ("FCN") treaties, latter aimed at liberalization. This article finally concludes by arguing for the need to accommodate developmental concerns in arbitral jurisprudence as well as treaty-making.

II. Notion of Investment

The methodology employed in defining investment differs from treaty to treaty. Treaties normally follow a broad asset-based open-ended definition, making the task of defining investments a controversial topic.[10] The definition starts normally with the words, "investment means and includes every kind of asset" but "not exclusively" or "not limited to."[11] This is followed by an illustrative list

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TREATIES ATTRACT FDI? ONLY A BIT… AND THEY COULD BITE, (2003).

[10] M. Sornarajah, *Portfolio Investments and Definition of Investment*, 24 ICSID REV. FOREIGN INVESTMENT L.J. 516 (2009).

[11] UNCTAD, BILATERAL INVESTMENT TREATIES 1995-2006: TRENDS IN INVESTMENT RULE MAKING, 7-13 (2007); India Model BIT, Agreement Between the Government of

stipulating the categories of assets. Although specific description of the categories may differ, they typically contain the following:

- "Movable and immovable property and any other property rights such as mortgages, liens and pledges.
- Shares, stocks and debentures of companies or interests in the property of such companies.
- Claims to money or to any performance under contract having a financial value.
- Intellectual property rights and goodwill, and
- Business concessions conferred by law or under contract, including concessions to search for, cultivate, extract or exploit natural resources."[12]

The first contention is whether the categories of assets mentioned in the definition can be considered investment by themselves or is there a separate and additional requirement to constitute an investment. Whether "investment" has any meaning of its own – is referred to as the 'notion of investment'.

The notion of investment has become the most controversial issue in determining jurisdiction in investment arbitrations.[13]The investment claims adjudicated under ICSID shed illuminating light on the notion of investment. The ICSID is established with an objective of settlement of investment disputes.[14] The jurisdiction of an ICSID tribunal is limited to 'legal dispute arising directly out of an investment'.[15] The ICSID Convention through Article 25(1) does limit the operation of the Convention over an investment dispute but does not define an investment. During the drafting of the ICSID Convention there were irreconcilable differences of opinions in identifying the parameters of the definition.[16] Realizing this practical difficulty, the task of

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Republic of India and The Government of the United Kingdom or Great Britain and Northern Ireland for the Promotion and Protection of Investments, Article 1 (b), March 14, 1994; *Supra* note 2, at 226-230.

[12] UNCTAD, SCOPE AND DEFINITION: UNCTAD SERIES ON ISSUES IN INTERNATIONAL INVESTMENT AGREEMENTS, II 24 (2011).

[13] *Infra* note 21, p.193, citing E. Gaillard, *Identify or Define? Reflections on the Evolution of the Concept of Investment in ICSID Practice, in International Investment Law for the 21st Century: Essays in Honour of Chrisoph Schreuer* 403-416 (Binder et al. eds., 2009); Y. Andreeva, *Salvaging or Sinking the Investment? MHS v. Malaysia Revisited*, 7(2) THE LAW AND PRACTICE OF INTERNATIONAL COURTS AND TRIBUNALS 161 (2009); *Infra* note 34; *Infra* note 41, at 283.

[14] ICSID Convention, *supra* note 6, Art. 1(2).

[15] *Id.* Art.25(1).

[16] CHRISTOPHER SCHREURER, LORETTA MALINTOPPI, AUGUST REINISCH & ANTONY SINCLAIR, THE ICSID CONVENTION: A COMMENTARY, 82 (2nd ed. 2009).

defining was deliberately left for the parties.[17] If the transaction is not an investment according to Article 25(1), then an ICSID tribunal will not have jurisdiction to adjudicate such a dispute. Therefore, the existence of an investment becomes an indispensible inquiry. To address this problem, the tribunal in *Salini* declared that there is duality in ICSID arbitrations. Investment has two definitions – as under the BIT and the other under Article 25 (1) of the Convention.[18] The latter is an objective satisfaction necessary for an ICSID tribunal to possess the mandate to decide a dispute under the Convention. The tribunal looked at the definition in the BIT and declared that the existence of one of the categories of an investment is sufficient for the purpose of the BIT,[19] But for the purpose of the ICSID Convention, the notion of investment must satisfy something more, which would be a four pronged objective test – "contributions, a certain duration of performance of the contract, participation in the risks of the transaction and most importantly, on "reading the Convention's preamble, contribution to the economic development of the host State of the investment as an additional condition."[20] The consequence of *Salini's* analysis is – definition of an investment applies only to ICSID Convention and not to BITs. The need of defining an investment is underscored but was then limited only to ICSID. The criticism for adopting a limited approach is addressed in detail in Part IV. The argument here is limited to the necessity of defining the notion of investment.

The possibility of investment having a meaning of its own was stressed in *Romak* v. *Tanzania*.[21] The tribunal found it necessary to define the attributes of the notion of investment. In the view of the tribunal, with which this article expresses complete agreement, the ordinary meaning of an investment has to be seen.[22] The need of an independent meaning for it was summarized as follows:

> "*Accordingly, there must be some benchmark against which to assess those non-listed assets or categories of assets in order to determine whether they constitute "investment" within the meaning of Article 1(2). The term "investment" has a meaning in itself that*

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[17] REPORT OF THE EXECUTIVE DIRECTORS ON THE CONVENTION ON THE SETTLEMENT ON INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES p.27 (International Bank for Reconstruction and Development,1965), *available at:* https://icsid.worldbank.org/ICSID/StaticFiles/basicdoc/partB.htm; *Supra* note 8, at 115.

[18] *Supra* note 7, at 44.

[19] *Supra* note 7, at 45-49.

[20] *Id.* at p. 53.

[21] Romak SA v. Republic of Uzbekistan, PCA Case No. AA280, Award, (Nov. 29, 2009).

[22] *Id* at pp.176-177.

cannot be ignored when considering the list contained in Article 1(2) of the BIT."[23]

The tribunal further stressed that if the categories listed in the definition of investment are mechanically applied, it would produce a manifestly absurd or unreasonable result.[24] To avoid this consequence, which is disallowed by the Vienna Convention on the Law of Treaties[25], the tribunal must give an ordinary meaning to the term.[26]

Investment, like most of the terminologies in international trade law owes its origin to economic terminologies, like dumping, subsidies, capital transfers etc.[27] Therefore, just like dumping, subsidies, capital transfer etc. cannot be interpreted devoid of their inherent meaning; investment cannot be looked upon bereft of its natural meaning. Difference of specific wording of the category of an investment in different treaties can hardly be a justification to deprive investment of its natural meaning. The core notion of the terminology cannot be fluid; although its superimpositions may differ. While speaking of the notion of investment, the focus is not the superimpositions but the kernel being the meaning of investment. The enumerative list provided in the treaties is hardly a pointer. Defining the term would remove confusion.[28] It would be safe to state that the contents in the definition clause stipulate the kinds of assets that are entitled for protection under a BIT, but are not conclusive pointers for the definition of investment. Tribunals have from time to time suggested certain criteria, which would be helpful as well as appropriate to interpret the definition of 'investment'.[29] The starting point for the definition exercise shall be the term investment itself. The kind of investment enumerated in the definition clause of the treaty shall first satisfy that it is an investment *per se*, as any claim to money or performance under contract having a contractual value cannot by itself be protected. Such an interpretation would include any and every kind of claim irrespective of whether it is an investment.

Even during the negotiations for the Multilateral Agreement on Investment

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[23] *Supra* note 21, at 180.
[24] *Supra* note 21, at 184.
[25] Vienna Convention on the Law of Treaties, Art. 31, May 23, 1969, 1155 U.N.T.S. 331, 8 I.L.M. 679 (1969) [hereinafter VCLT].
[26] *Supra* note 21, at 181.The exact contents of this definition are discussed.
[27] Rudolph Dolzer, *The Notion of Investments in Recent Practice, in* LAW IN THE SERVICE OF HUMAN DIGNITY: ESSAYS IN HONOUR OF FLORENTINO FELECIANO-263 (Steve Charnovitz et al. eds., 2005).
[28] Sebastien Manciaux, *The Notion of Investment: New Controversies*, 9 J. WORLD INVESTMENT & TRADE 443, 448-449 (2008).
[29] *Id* at 449-450.

("MAI"),[30] need to provide definition of an investment was foreseen.[31] This shows the underlying presumption of negotiators that investment cannot be a term without a meaning. It cannot be motley of categories of assets without any meaning in the context.

The well-settled rule of *effective treaty interpretation* obliges the tribunal to give meaning to every term in the treaty. This principle is a part of the 'doctrine of good faith', in treaty interpretation.[32] The words in the treaty are presumed to have certain effect and they cannot be meaningless. This is reflected in the maxim *ut res magisvaleat quam pereat.*[33] One cannot simply ignore the existence of the word investment, in the treaties. It cannot be declared meaningless. The persuasion for the tribunal in *Romak* was its ordinary meaning; however it did not address the effective treaty interpretation principle to identify the meaning of investment. Nevertheless, the tribunal did arrive at a reasoned and a reasonable outcome by following a different route.

Efforts of defining investment are criticized on the ground that it is a conspiracy of academics and arbitrators[34]. The problem with adopting a *category based*[35] definition, rather than a *notion based* definition has blurred the distinction between ordinary commercial transactions and investments.[36] It is necessary that the distinction is retained[37], if not one is forced to remember the elementary point that these are investment treaties and not ordinary commercial transactions.[38]

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[30] MAI was intended to be a multilateral treaty dealing comprehensively with investment under the World Trade Organization (WTO), alongside other trade agreements. Developing countries through a spirited response succeeded in stalling the MAI and thus it failed.

[31] *Supra* note 27, at 265.

[32] IAN BROWNLIE, BROWNLIE'S PRINCIPLES OF PUBLIC INTERNATIONAL LAW 635 (James Crawford ed., 2012).

[33] LASA OPPENHEIM, OPPENHEIM'S INTERNATIONAL LAW 1280 (Robert Jennings and Arthur Watts eds., 1992).

[34] Devashish Krishnan, *A Notion of ICSID Investment, in* INVESTMENT TREATY ARBITRATION AND INTERNATIONAL LAW 64-66 (TJ Grierson Weiler ed., 2008).

[35] By *category based* definition, this article means treating the categories of investment in the definition to as investments on their own.

[36] Joy Mining Machinery Ltd. v. Arab Republic of Egypt, ICSID Case No. ARB/03/11, Award on Jurisdiction, p.58 (Aug. 6, 2004) [hereinafter *Joy Mining Case*]; *Infra* note 57, at 42; *Cited with approval in Supra* note 21, at 185.

[37] *Supra* note 21, at 185; *Ibid* (*Joy Mining Case*), at 58; *Infra* note 57, at 42.

[38] Secretary General of ICSID declined to register a case, since it arouse out of an ordinary sale of goods transaction. *See* I.F.I. Shihata & A. Parra, *The Experience of the International Centre for Settlement of Investment Disputes*, 14 ICSID K. FOREIGN INVESTMENT L.J 299, 308 (1999).

From the standpoint of developing countries, emphasis on definition of the notion of investment is important. If this exercise is disregarded by an investment tribunal, then any commercial transaction would become an investment. The description of these transactions as categories of investment in BITs is already broad. Contractual claims, decided otherwise by domestic courts or international commercial arbitral tribunals will be brought before investment tribunals. Investor can thus evade domestic courts completely and decide all its disputes before a tribunal of its own choice.[39] Though this does not fit anywhere in the scheme of investment treaty framework, unless investment is seen objectively, developmental concerns cannot be addressed.

III. Definition of Investment: an objective test

The definition of investment as per the International Monetary Fund ("IMF") reflects the objective of obtaining a lasting interest by the resident entity in one economy as compared to a resident in another economy in an enterprise[40]; where "lasting" implies a long term relationship. The economic debate on the definition of a direct investment involves - transfer of funds, long-term project, objective of regular income, participation of person transferring funds, although to a limited extent in management of project and business risk. They distinguish an investment from portfolio investment or ordinary transaction of sale or purchase, for a short term.[41]

There are strong arguments to exclude short term investments from the definition of investment, especially from the developing countries perspective.[42] During the Asian crises, the Asian economies have burnt their hands with fluid capital in share markets.[43] Portfolio investments do not contribute in any manner in the development of the host State's economy because the investor does not have any lasting interest in the host State's economy. The investor is not serious and does not intend to stay in the market for a long duration, rather the investment is temporary – until share value appreciates. Also the entry of an

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[39] Investors are already taking a "second bite at the cherry". If commercial arbitration awards are not enforced within the expected time and to the complete satisfaction of investors, investment treaty claims will be brought to get the awards enforced indirectly, especially against developing countries. *See* Patricia Nacimiento & Sven Lange, *Case Comment: White Industries Australia Limited v The Republic of India,* 27(2) ICSID REV. 274, 279-280 (2012).

[40] Joachim Karl, *The Competence for Foreign Direct Investment: New Powers for the European Union?,*5 J. WORLD INVESTMENT & TRADE 413, 420 (2004); OECD, OECD BENCHMARK DEFINITION OF FOREIGN DIRECT INVESTMENT 22 (2nd ed., 2008).

[41] *See* N Rubins, *The Notion of "Investment", in* ARBITRATING FOREIGN INVESTMENT DISPUTES (Norbert Horn & Stephan Kroll ed., 2004).

[42] SORNARAJAH, *supra* note 10, at 518.

[43] JOSEPH STIGLITZ, GLOBALISATION AND ITS DISCONTENTS DISCONTENTS (2003).

investment is not through authorization of the government and cannot claim any protection. All treaties make mention to shares. If a *category based* approach is adopted, investments for the shortest possible time and losses arising thereof will give rise to investor-state arbitration claims. It will create havoc, unfathomable for developing countries. To maintain the health of an economy, it is necessary that short term transactions are not treated as investments.

Portfolio investment is of a purely financial character, passive and does not involve control. It is sold on appreciation with no intention to hold on to it. It does not result in technology transfer, training of local employees and other benefits associated with investment.[44]Adoption of a definition for an investment and inclusion of objective criteria would exclude portfolio investment and reduce uncertainties for developing countries.

By identifying objective tests and specially contribution to economic development; the *Salini* test excluded temporal engagements, which do not have any relevance for development and thus cannot be categorized as investment. The instances of assets covered under the definition of investment have gradually increased over time. There are perennial efforts by tribunals and authors to broaden the definition of investment. This covers various kinds of assets which otherwise would not have been covered.[45] The tribunals prior to *Salini*, in *Alcoa Minerals of Jamaica Inc*. v. *Jamaica*[46], *Kaiser Bauxite* v. *Jamaica*[47], and *Letco* v. *Liberia*[48] never enunciated an objective test, but relied on investment to implicitly contain certain conditions without paying closer attention to the actual meaning of the term.[49] Those cases are mostly related to contracts for exploration of resources, wherein existence of investment was apparent. There was no dispute about whether the commitment and contribution was an investment. Therefore, absence of examples of adoption of objective criteria, prior to *Salini* can hardly discredit the relevance of the *Salini test*.

The *Salini* test has resonated strongly in the ICSID context and dithered in the BIT discourse. Its journey within ICSID has been turbulent, but imposing and convincing. Various tribunals have adopted this definition. A pragmatic approach would be to apply an objective test to investment because whether a

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[44] UNCTAD, *supra* note 12, at 29.
[45] SORNARAJAH, supra note 1, at pp.11-18.
[46] Alcoa Minerals of Jamaica Inc. v. Jamaica, ICSID Case No. ARB/74/2, Decision on Jurisdiction and Competence, (July 6, 1975).
[47] Kaiser Bauxite Company v. Government of Jamaica, ICSID Case No. ARB/74/3, Decision on Jurisdiction and Competence, (July 6, 1975).
[48] Liberian Eastern Timber Corporation v. Government of the Republic of Liberia, ICSID Case No. ARB/83/2, (Mar. 31, 1986).
[49] RUDOLPH DOLZER, *supra* note 27, at 267.

transaction would be an investment or not, will depend on the objectives of the treaty set out in the first sentence of the Preamble.[50]There is variation in the application of the objective criteria. Few tribunals have expressly or impliedly criticized the *Salini* test.[51] However, certain tribunals adopted the "conceptual" approach but refused to endorse all the constitutive elements in it.[52]In *Mahaley* v. *Sri Lanka,* the expenditure incurred by an investor in negotiations for investment at a per-investment stage was held not to be covered by the definition.[53] The tribunals in *Phonex Action*[54], *Patrick Mitchell*[55], *CSOB*[56], *Fedax*[57] have relied on this definition. Their degree and approach would certainly differ.

IV. Salini Test and Beyond

The restrictive definition adopted in the ICSID arbitrations can ensure sustained

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[50] Ceskoslovenska Obchodni Bank, A.S. v The Slovak Republic, ICSID Case No. ARB/97/4, Decision on Jurisdiction, p.64-90 (May 24, 1999) [hereinafter *Ceskoslovenska Obchodni Case*].

[51] See MCI Power Group, LC and New Turbine, Inc v. Ecuador, ICSID Case No. ARB/03/6, Award, p.165 (July 31, 2007); CMS Gas Transmission Company v. Argentine, ICSID Case No. ARB/01/8, Decision of the ad hoc Committee on the Application for Annulment, p.71 (Sept. 25, 2007); Biwater Gauff (Tanzania) Ltd v. United Republic of Tanzania, ICSID Case No. ARB/05/22, Award, p.312-317 (July 24, 2008); Malaysian Historical Salvors SDN v. The Government of Malaysia, ICSID Case No. ARB/05/10, Decision of the ad hoc Committee on the Application for Annulment, p. 78-79 (Apr. 16, 2009) (citing *Biwater* v. *Tanzania*).

[52] See Consortium Groupement LESI-Dipenta v. People's Democratic Republic of Algeria, ICSID Case No. ARB/03/8, Award, p.13 (iv) (Jan. 10, 2005); LESI, SpA and Astaldi, SpA v. People's Democratic Republic of Algeria, ICSID Case No. ARB/05/3, Award on Jurisdiction, p.72 (iv) (July 12, 2006); Bayindir Insaat Turizm Ticaret VeSanayi AS v. Islamic Republic of Pakistan, ICSID Case No. ARB/03/29, Award on Jurisdiction, p.130 (Nov. 14, 2005); Jan de Nul NV and Dredging International NV v. Arab Republic of Egypt, ICSID Case No.ARB/04/13, Award on Jurisdiction, p.91 (June 16, 2006); Saipem SpA v. People's Republic of Bangladesh, ICSID Case No. ARB/05/07, Award on Jurisdiction and Recommendation on Provisional Measures, p.99; Ioannis Kardass opoulos v. Georgia, ICSID Case No. ARB/05/18, Award on Jurisdiction, p.116 (July 6, 2007).

[53] Mihaley International Corporation v. Sri Lanka, ICSID Case NO. ARB/00/2, Award, (Mar. 15, 2002).

[54] Phoenix Action, Ltd. v. The Czech Republic, ICSID Case No. ARB/06/5, Award, (Apr. 15, 2009).

[55] Patrick H. Mitchell v. Democratic Republic of Congo, ICSID Case No. ARB/99/7, Award, (Feb. 9, 2004).

[56] *Ceskoslovenska Obchodini Case , supra* note 50.

[57] Fedax N.V. v. The Republic of Venezuela, ICSID Case No.ARB/96/3, Award, (Mar. 9, 1998).

contributions by an investor to the economic development of the host State.[58] This definition was applied outside the ICSID context, by the tribunal in *Romak*.[59] The factual controversy related to non-payment of dues towards importation of food grains into Uzbekistan by a public corporation. The claimant initiated arbitration proceedings under its contractual relationship[60] and succeeded in getting an award in its favour.[61] The claimant tried to enforce the award in Uzbek and French courts, but initially the efforts failed[62] but later on it succeeded partially by attaching the accounts of the government.[63] The arbitral proceedings under an investment treaty are aimed at recovering the amounts unpaid under the arbitral award.

The tribunal decided that, investments shall be given an ordinary meaning and be tested against some benchmark; otherwise every commercial transaction will become an investment.[64] A mechanical approach to treat the categories of investment as investment would create, *de facto,* a new instance of review of State court decisions concerning the enforcement of arbitral awards."[65] Finally, such an approach would mean every award or judgment in favour of a national of one party to the BIT will be treated as an investment. This would imply that States have renounced the applicable domestic law – chosen as the governing law by the parties; and consequentially surrender the jurisdiction of domestic courts.[66] Investment must be given its proper meaning.[67] The tribunal adhered to ICSID jurisprudence since the Convention "incidentally, does not contain a definition of the term "investment".[68] Since it is an admitted fact that ICSID does not contain a separate definition of investment and drafters deliberately did not offer the definition, it is improper to suggest that the term has a different definition in ICSID context than in BITs.[69] Although there is ambivalence in application of the *Salini* test as the tribunal found no reason to reject it and apply to the facts in question[70] to conclude that a one off sale transaction cannot be an investment.[71] The path

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[58] Anna Turinov, *"Investment" and "Investor" in Energy Charter Treaty Arbitration: Uncertain Jurisdiction*, 26(1) J. INT'L ARB. 1-20 (2009).
[59] Romak SA v. Republic of Uzbekistan, *supra* note 21.
[60] Romak SA v. Republic of Uzbekistan, *supra* note 21, p.41-52.
[61] *Id.* at 58.
[62] *Id.* at 64-66.
[63] *Id.* at 68-69.
[64] *Id.* at 177, 180-181, 184-185.
[65] *Id.* at 186.
[66] *Id.* at 187.
[67] *Id.* at 160.
[68] *Id.* at 192.
[69] *Id.* at 194.
[70] *Id.* at 207-208.
[71] *Id.* at 242.

chartered in *Romak* is followed in *Alps Finance and Trade* v. *Slovak Republic*[72] and *Compagine International de Maintenance (CIM)* v. *Ethiopia*[73].

The only instance outside the ICSID Convention where requirement of objective criteria is rejected is *White and Industries* v. *India*[74]. The claimant was seeking to enforce an arbitral award against the Government of India. India resisted, *inter alia*, on the ground that the *Salini* test was not satisfied. The tribunal rejected the argument on the ground that the *Salini* test was limited to ICSID arbitrations.[75] However, it did not dwell much on the reasoning for arriving at such a finding It was introduced in Part II that investment was never defined in the ICSID Convention and the effort in that direction was specifically abandoned. Initially, the drafting committee of the World Bank proposed a definition of investment for the purposes of Article 25 because it was a definite objective that non-investment disputes shall not be raised before ICSID. During negotiations, no consensus could emerge on an acceptable definition of investment. Realizing this problem, the Secretary General Broches suggested that the task of defining investment be left to the states.[76] The tests developed by *Salini* were specifically rejected during the negotiations.[77] It was left for the States to define investment with a broad autonomy.[78] The parties to ICSID never intended to define investment in a manner limited to ICSID cases. The definition was integrated with that of the BIT. Thereby, effort of any ICSID tribunal at defining investment would automatically get added to the notion of investment generally, and not limited to ICSID. The word cannot be a surplusage in non-ICSID cases and the word of reference in ICSID cases it would be improper to limit the application of definition of an investment only to ICSID cases. *Salini* therefore made a mistake by stating that its jurisprudence is limited to the meaning of investment under Article 25(1) and did not apply to the notion of investment. The tribunal in *Salini* did limit itself to the meaning of investment under Article 25(1) of ICSID[79] but the tribunal was addressing the term on its autonomous meaning.

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[72] Alps Finance and Trade v. Slovak Republic, Award (Preliminary Redacted Version), p. 241. (Mar. 5, 2011).

[73] Compagine International de Maintenance (CIM) v. Ethiopia, Award, is unpublished but for discussion. *See* Jarrod Hepburn & Luke Eric Peterson, *Ethiopia Prevailed in Face of Foreign Investor's Attempt to Use Investment Treaty to Sue Over ICC Arbitration Award*, INVESTMENT ARB. REP. (2012).

[74] White Industries Australia Ltd. v. The Republic of India, (UNCITRAL), Final Award, (Nov. 30, 2011).

[75] *Id.* at 7.4.8, 7.4.9.

[76] DOLZER, *supra* note 27, at 266.

[77] Julian Davis Mortenson, *The Meaning of "Investment": ICSID's Travaux and the Domain of International Investment Law,* 51(1) HARV. INT'L L.J. 257, 280-281 (2010).

[78] *Id.* at 301.

[79] *Id.*

It would equally result into unreasonable consequences by arguing that the meaning of investment would depend on the forum before which the claims are raised.[80] Institutions cannot award jurisdictions. This will run counter to the rule of construction developed by the International Court of Justice ("ICJ"), that if the same term is employed in the same or similar context by a State party to two or more treaties; the terms shall be given same or a compatible meaning.[81] It is in the interest of developing countries, whether they are a Contracting Party to the ICSID Convention or not, in order to support the *Salini* test and its extension beyond ICSID. Apart from the arguments on merits, for extending these principles, there is a special relevance of the last ingredient of the facets of investment that is "*the contribution to development.*"

V. Contribution to Development

The four criteria test of investment has been applied with variations by tribunals. It is not entirely clear if the tribunals have applied these criteria as "essential requirement for the existence of investment" or "typical character or indicator", but their repeated application strengthens the perception that these are not merely features indicative of investment, but mandatory standards.[82] The criteria are not that rigid but nevertheless their existence is necessary.[83]

While defining investment in *Salini*, the tribunal made a specific and special reference to the need of contribution to development. Other ingredients of definition such as substantial contribution have not been a problem,[84] but contribution to development is most controversial.[85] Contribution to economic development of the host economy was introduced with reference to the Preamble of the ICSID Convention.[86] The intention behind creation of the ICSID Convention was to protect the interest of investors as well as those of host States[87] by stimulating large flow of capital[88]. ICSID is not merely a dispute resolution mechanism but also "an instrument of international policy for the promotion of economic development".[89]

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[80] Romak SA v. Republic of Uzbekistan, *supra* note 21, at 195.
[81] Agean Sea Continental Shelf (Greece v Turkey), 1978 I.C.J. 3 (Dec. 19),
[82] SCHREUER, MALINTOPPI, REINISCH & SINCLAIR, *supra* note 8, at 129-130.
[83] *Id.* at 133
[84] *Joy Mining Case, supra* note 36, p.57; Jan de Nul v. Egypt, ICSID Case No. ARB/04/13, Jurisdiction, p.92 (June 16, 2006); Helnan International Hotels A/S v. Arab Republic of Egypt, ICSID Case No. ARB/05/19, Jurisdiction, p.77 (Oct. 17, 2007).
[85] SCHREUER, MALINTOPPI, REINISCH & SINCLAIR, *supra* note 8, at 137.
[86] Salini v. Morocco*, supra* note 7, at 44.
[87] INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT, *s*upra note 17, at 13.
[88] *Id.* at 12.
[89] SCHREUER, MALINTOPPI, REINISCH & SINCLAIR, *supra* note 8, at 4-5; UNCTAD, *supra*

A general study of various BITs shows that they frequently make reference to "economic development" in one form or the other. In some cases, there is a reference to technical co- operation,[90] technology transfer[91] or simply through mutual development. The reference is normally made in the Preamble. The fact of reference to a specific objective of development makes contribution to development an indispensible "context" for treaty interpretation under Article 31 of the VCLT. The tribunal in *Patrick Mitchell* looked at the Preamble of the US Model BIT, to confirm that contribution to development is necessary.[92] The phraseology may differ but the underlying object remains– development. The tribunal in *LESI*[93] declined to apply the criteria of contribution to the development of host State independently, because the criteria in its view is difficult to establish and is *implicitly* covered by the first three.[94] There is however, no outright rejection of the criteria.

However the principle was elucidated in *Patrick Mitchell* v. *Democratic Republic of Congo*[95]. The military court of Congo, the Respondent State, had passed an order directing the premises of law firm of Mr. Mitchell to be seized, and the employees were forced to leave the premises.[96] A jurisdictional objection was raised on behalf of the Respondent, whether providing legal services can be termed as an investment. The tribunal had declined to find the existence of contribution to development, because it was presumed that the objective elements are frequently present in investment projects, and there is no formal requirement for finding if they are actually present.[97] The ad hoc Annulment Committee viewed the four criteria test to be interdependent and stated the need to treat them comprehensively.[98] Contribution to economic development of the host State has always been taken into account, either expressly or impliedly by the ICSID tribunals.[99] Therefore, even in cases where it has not been specifically mentioned, the tribunal has always been conscious that contribution to the development of host State exists.[100] The legal consulting services provided

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note 12, at 52.

[90] Agreement on the Promotion and Protection of Investments, Austl-Egypt, 2001, IC-BT 1451 (2001); Free Trade Agreement, Colom-Venez-Mex, June 13, 1994 (entered into force Jan. 1, 1995).

[91] Agreement Concerning the Encouragement and Reciprocal Protection of Investments, S. Kor.-Brunei, Nov. 14, 2000 (entered into force Oct. 30, 2003).

[92] Patrick H. Mitchell v. Democratic Republic of Congo, *supra* note 55, at 32.

[93] *Supra* text accompanying note 52.

[94] *Id.*

[95] Patrick H. Mitchell v. Democratic Republic of Congo, *supra* note 55.

[96] *Id.* at 1.

[97] Patrick H. Mitchell v. Democratic Republic of Congo*, supra* note 55, at 56-57.

[98] *Id.* at 27.

[99] *Id.* at 29.

[100] *Ibid* at 30; citing Alcoa Minerals of Jamaica Inc. v. Jamaica, ICSID Case No.

would fall within the category of investment under a BIT but that does not satisfy the definition of investment.[101] The claimant had failed to establish that the legal consulting services contributed to the economic development of the host State for which no protection could be claimed under the investment treaty.[102]

It is argued that development of the host State criterion is not relevant because it does not distinguish between transactions that are investments and those that are not. All foreign investments do not participate in the development of a host State, and all transactions that participate in the development of the host State are not necessarily investments.[103] This argument fails to understand the reason for inclusion of contribution to the host State economy as a criterion. These criteria are applied to "investments". The argument works the other way round, merely because some transaction contributes to development, it does not become an investment. Moreover, even if there is an investment - in the literal sense of the term, but it does not contribute to the economic growth it will not fall within the definition of investment. The Ad hoc Committee in *Patrick Mitchell* has stated that 'contribution to economic development of the host State is not sufficient by itself to constitute an investment'. It is one of the criteria to identify the existence of an investment and set out the extent of contribution to economic development that shall be made in the following words:

> "*The ad hoc Committee wishes nevertheless to specify that, in its view, the existence of contribution to the economic development of the host State as an essential – although not sufficient – characteristic or unquestionable criterion of the investment, does not mean that this contribution must always be sizable or successful; and, of course, ICSID tribunals do not have to evaluate the real contribution of the operation in question. It suffices for the operation to contribute in one way or another to the economic development of the host State, and this concept of economic development is, in any event, extremely broad but also variable depending on the case.*"[104]

ARB/74/2, Decision on Jurisdiction and Competence, (July 6, 1975); Tradex Hellas S.A. v. Republic of Albania, ICSID Case No. ARB/94/2, Award, (Apr. 29, 1999); *SGS* Societe Generale de Surveillance S.A. v. Islamic Republic of Pakistan, ICSID Case No.ARB/01/13, Decision on Objections to Jurisdiction, (Aug. 6, 2003); SGS Societe Generale de Surveillance S.A. v. Republic of the Philippines, ICSID Case No. ARB/02/6, Jurisdiction, (Jan. 29, 2004).

[101] Patrick H. Mitchell v. Democratic Republic of Congo, *supra* note 55, at 7-38.

[102] *Id.* at 39.

[103] SEBASTIEN MANCIAUX, *supra* note 28, at 459.

[104] Patrick H. Mitchell v. Democratic Republic of Congo, *supra* note 55, at 33.

The quality of 'contribution' to the state would include any significant financial resource or transfer of knowhow, equipment and personnel.[105] An approach to "significant contribution to the economy" is that investment may also result into certain social and political benefits; therefore there is no need of separate contribution. A social and political contribution cannot be sufficient. The development contemplated by FDI is not a social or cultural development but economic development.[106]The entire exercise of BITs is aimed at economic development. The fact that there is some other form of development achieved is only tertiary and peripheral. Additionally, uncertainty of the notion cannot be a reason to disregard its application. By that standard, every treaty standard is uncertain and non- specific. Even customary international law falls in the same category.

The contribution cannot always be sizable and successful- this is understandable. One cannot insist on certain amount of success of investment, unless so stipulated in the treaty. A tribunal may not evaluate the "real contribution" of operation in question. It is sufficient that the contribution is made one way or the other to the economic development of the host State and the investor has discharged the burden. The concept of contribution to development is extremely broad and variable, depending on the case.[107]The debate at the moment is still stuck on the presence of contribution to economic development of host State. It shall now mature and shift to the extent of economic cooperation and parameters for measurement.

VI. Developmental Perspective

There are certain sound policy reasons for adoption of a development oriented approach. Most of the BITs in the first generation were concluded between a capital exporting developed country and a capital importing developing country. This happened at the time when the newly independent third world gave birth to the New International Economic Order ("NIEO"). Developing countries with their numerical majority in the General Assembly of the United Nations declared sovereignty over natural resources[108] and States were declared to possess the authority to remove aliens from their territory at their wish by payment of "appropriate compensation".[109] The idea behind BITs was to make the developing world give up its harsh stand and allow foreign investment to enter

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[105] Bayinder Insaat Turizm Ticaret VeSanayi AS v. Islamic Republic of Pakistan, ICSID Case No. ARB/03/29, Jurisdiction, p.131 (Nov. 14, 2005); Saipem S A v. Peoples Republic of Bangladesh, ICSID Case No. ARB/05/7, Jurisdiction, p.100 (Mar. 21, 2007).
[106] *Supra* note 28.
[107] *Supra* note 21, at 33.
[108] G.A. Res. 1803, U.N. GAOR, 17th Sess., Supp. No.17, U.N. Doc.A/5217 (1962).
[109] G.A. Res. 3281 (XXIX), UN Doc.A/RES/29/3281 Article 2.2(c) (emphasis added).

their jurisdiction for promoting development. It was only once the BIT program arrived, developing countries joined the BIT bandwagon by abandoning the NIEO.[110] Developing countries would not have joined the BIT program without expecting infusion of foreign capital and technology transfer. The developing world entered the sphere by subjecting its sovereign authority to control, expecting development in return. Although the BIT says that the treaty is between two equals, one is inevitably the recipient of capital and the other is an exporter.[111]Although normally a BIT is an agreement between equals, in practice it is different. It is not a quid pro quo bargain but a fiction where one is an exporter of capital and the other is importer.[112]

Most of the BITs contain a Preamble aimed at satisfying developmental needs of recipient states. It is difficult to imagine, why a developing country would otherwise allow an investor. The investment treaties are not entered into with liberalization objectives. If it was so, multilateral efforts at an investment treaty would have never failed. To this extent, as well as BITs are different from Friendship Commerce and Navigation ("FCN") treaties. FCN treaties were treaties aimed at liberalization and entered into between developed countries. They provided greater access to markets.[113]A cleavage of liberalization and development would shed light. Most of the BITs are entered with the objective of attracting capital for development, rarely for market access. The ASEAN Framework agreement is a mixture of both these objectives. The preamble says so in following words:

> "*Reaffirming the importance of sustenance of economic growth and development in all Member States through joint efforts in liberalizing trade and promoting inter-ASEAN trade and investment flows…"*[114]

There is an increasing move towards entering BITs for liberalization and market access[115]; especially amongst European states there is a move from the developmental objective to the market access objective.[116] It is understood from these cases, that the investment treaties are entered for obtainingaccess to markets rather than achieving the developmental goal. Investment treaties aimed

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[110] STEPHEN SCHILL, MULTILATERALISATION OF INTERNATIONAL INVESTMENT LAW 91 (2009).
[111] Adeoye Akinsanya, *International Protection of Direct Foreign Investments in the Third World,* 36 INT'L & COMP. L.Q. 58 (1987).
[112] *Supra* note 1, at 177.
[113] RUDOLPH DOLZER & MARGARETE STEVENS BILATERAL INVESTMENT TREATIES (1995), pp. 10-13.
[114] ASEAN Framework Agreement on the Facilitation of Goods in Transit, Preamble, Signed 16th December 1998.
[115] *Supra* note 12, at 1.
[116] *Supra* note 40.

at liberalization are not yet prevalent amongst developing countries.[117] But, until the treaty specifically provides that its aim is market access, its primary aim would be development.

An important necessity is that the investments are made in accordance with the laws of the host State.[118] Investment is exposed to domestic regulation mostly at the entry point.[119] A treaty would normally declare that domestic regulations will apply. In any case, an investment cannot operate contrary to the domestic legal framework. The requirement is implied,[120]also referred to as, the doctrine of legality.[121] If the investment is not made in accordance with the domestic law of the host State, the tribunal will decline to exercise jurisdiction, consequentially rejecting the claim of protection under a treaty.[122] By retaining the power to screen investments at entry state, host States, especially developing courtiers can exercise greater control over the entry of investments. The need of compliance with entry requirements, getting licenses, certificates and registration is not merely procedural but a necessary pre-requisite for a qualified investment.[123]The developing countries can exercise this power to grant permission for those investments, which its domestic economy needs for development. It can choose labor intensive as well as high technology oriented investments, which can eventually lead to employment generation as well as enrichment of domestic technical knowhow. The most famous entry route has been joint venture corporations, since they ensure greater engagement.[124] Chinese policy towards foreign investment was driven by the condition that the investments shall aim at establishing export oriented and technologically advanced enterprises.[125] China has adopted a liberal approach for entry; however, it exercised heavy control in the initial phases. The entry was limited to contractual or equity joint ventures

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[117] *Supra* note 12, 33 & 36.

[118] Most of the treaties entered into by India contain this clause.

[119] M. Sornarajah, *India China and Foreign Investment, in* CHINA, INDIA & THE INTERNATIONAL ECONOMIC ORDER 145 (M Sornarajah et al. eds., 2011).

[120] *Supra* note 12.

[121] Gabriel Bottini, '*Legality of Investments under ICSID Jurisprudence*', *in* THE BACKLASH AGAINST INVESTMENT ARBITRATION 298 (Michael Waibel et al. eds., 2010); Investments that are not made in accordance with the domestic legal framework will be illegal investments. See InceysaVallisoletana S.L v. El Slavador, ICSID Case No. ARB/03/06, Award, (Aug. 2, 2006); Fraport AG Frankfurt Airport Services Worldwide v. Philippines, ICSID Case No. ARB/03/25, Award, (Aug. 16, 2007).

[122] Yuang Chi OoPtd Ltd. v. Myanmar, ASEAN ID Case No. ARB/01/1, Award, (Mar. 31, 2003).

[123] *Id.* at 34.

[124] M SORNARAJAH, SETTLEMENT OF FOREIGN INVESTMENT DISPUTES, INTERNATIONAL LAW ON FOREIGN INVESTMENT, (2000).

[125] *Supra* note 119, at 143.

but it has now moved on to allow wholly owned enterprises.[126] Developing countries in the capacity of a host Sate can have a greater say and participation in the working of the industry set-up as a part of the investment.

Exercising control at entry point is seen as a strong tool for achieving developmental goals for developing countries. Comparatively, India follows a conservative approach allowing only sector specific entry which is subjected to caps.[127]The Indian approach allows sector-wise assessment and development. This can avoid swamp in a swathe of investments, either warranted or unwarranted.[128]

VII. Conclusion

If notion of investment is appropriately defined it will bring certainty to the investors as well as States. The investor would know if his claim would ever be covered under the BIT, and the States would know which investments would operate as a limitation on its authority. There is a tendency to treat every kind of asset as an investment because it carries economic value. The number of assets has drastically increased over time – from equity stocks in companies to intellectual property rights.[129] There is a need to set clear benchmarks as to what is an investment, so that other commercial transactions can be excluded.[130] It is important for developing countries to keep purely commercial transactions out of the definition. At the same time, those investments, which do not possess any value for the economy and are purely a short-term enterprise, shall be excluded. China has established the benefits that can be reaped by channelizing investments for development.

An exercise of imposing performance conditions on an investor is non-prevalent. It may or may not turn out to be a vigorous proposition but need to contribute to host economy can always be specifically added into the treaty. The Singapore-US FTA has achieved in adding elements to the definition of investment, through a footnote, which reads as under:

> *"Where an asset lacks the characteristics of an investment, that asset is not an investment regardless of the form it may take. The characteristics of an investment include the commitment of capital, the expectation of gain or profit, or the assumption of risk."*

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[126] *Supra* note 119, at 142-143.
[127] Government of India, FDI Policy, 2012, *available at:* http://dipp.nic.in/English/Policies/FDI_Circular_01_2012.pdf.
[128] *Supra* note 19, at 143.
[129] *Supra* note 12, at 8.
[130] *Supra* note 12, at 9.

This explanation of investment would leave out commercial transactions as it cannot serve as a template for all the developing countries. Additional features may be added depending on the need of respective countries. Adding contribution to development will be one such feature. A contemporary threat that still remains is adoption of open-ended definitions of investment. New treaties are adopting techniques to narrow down the open ended asset-based definition of investment. This trend is in response to the expansive interpretations of open-ended terminologies adopted by tribunals.[131] There is a tightly defined closed-list approach emerging but the league is lead by developed countries.[132] Developing countries are still to make strides on this front. An enterprise based definition of investment – insisting establishment of an enterprise in the host State is a tested mechanism in treaty practice.[133] This ensures that employment is generated in the host State along with contribution to economic growth. Such a definition gives greater control at entry level.[134] Likewise, the EU's economic agreements have the need of "commercial presence".[135] To retain health of developing economies, short term and commercial transactions – portfolio investments, commercial contracts, certain loans, duration, debt securities etc shall be excluded.[136] For example, the Peru-US FTA, 2006, Article 10.28 excludes bonds, debentures, other debt instruments and loans that do not have a character of investment.

Investments also bring lot of costs along with them. Developing countries have to achieve an increased flow of investment and maximize benefits while minimizing costs.[137]One investor-state arbitration claim can replenish the benefits that the entire regime may bring for a developing state. The investment tribunals have been awarding heavy damages. Some states, especially Argentina have become a regular target of investors.[138] The costs shall not outweigh the benefits. It is in the interest of developing states to narrow down the width of

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[131] *Supra* note 12, Executive Summary, (xi).

[132] Canada 2004 Model BIT, Agreement between Canada and …for the Promotion and Protection of Investments, *available at:* http://italaw.com/documents/Canadian2004-FIPA-model-en.pdf.

[133] Canada-US FTA of 1992 adopted this model. Later NAFTA continued it along with other traditional open-ended definitions.

[134] *Supra* note 12, at 22.

[135] *Supra* note 12, at 23.

[136] *Supra* note 12, at 29.

[137] J W Salacuse, *Foreign Direct Investment and the Law in Developing Countries,* 15 ICSID REV. 382 (2000).

[138] *See* José E. Alvarez & Gustavo Topalian, *The Paradoxical Argentina Cases*, Wilmer Cutler Pickering Hale and Dorr Scholar-in- Residence Seminar, Dec. 17, 2012, *available at:* http://www.law.qmul.ac.uk/events/items/87203.html.

definition of investments. There are various advisories which emphasize this approach[139] – especially of sustainable development.[140]

The developing countries do not seem to yet tone their treaties down. There is a paradox in their approach, when compared with trade law. In trade law, it is development all over the place. An important reason for deadlock in the Doha Negotiations is the "developmental issues", which are "related to addressing the trade-related development challenges faced by the least-developed countries ("LDC"), and the so-called 'small, weak and vulnerable developing countries'[141]same is yet to be reflected in investment-treaty making. One reason could be that the negotiations at the Doha Round are multilateral and developing countries can consolidate themselves and resist any proposal that does not satisfy their developmental needs. On the other hand, they are alone fighter in an investment- treaty negotiation. If they intend to stay afloat in the swamp of investor clams, there is a need of serious rethinking on the drafting of treaties and for arbitrators to take note of the reasons why developing states enter into investment treaties.

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[139] J ANTHONY VANDUZER, PENELOPE SIMONS & GRAHAM MAYEDA, INTEGRATING SUSTAINABLE DEVELOPMENT INTO INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE FOR DEVELOPING COUNTRIES, (2012).

[140] MARIE-CLAIRE CORDONIERSEGGAR, MARKUS W GEHRING AND ANDREW NEWCOMBE, SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW, (2011).

[141] See Faizel Ismail, *One year Since the Hong Kong Ministerial Conference: Developing countries reclaim the development content of the WTO Doha Round*, *in* ECONOMIC DEVELOPMENT THROUGH WORLD TRADE: A DEVELOPING WORLD PERSPECTIVE 122 (Yong-Shik Lee ed., 2008).

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]

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[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

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(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]

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[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

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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

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[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.

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[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.

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[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

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[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

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[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

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[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

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[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.

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[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

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[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

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[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,

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[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.

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[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

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[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.

INTERNATIONAL INVESTMENT LAW AND DEVELOPING ECONOMIES: THE GOOD, BAD AND COMME CI, COMME ÇA

Aravamudhan Ulaganathan Ravindran[*]

I. Introduction

Investor-State dispute resolution relates to the process of decision-making that transnational corporations undergo when analyzing whether to invest their capital in a particular country. The international community has created a variety of devices, such as the Washington Convention for Settlement of Investment Disputes ("Washington Convention or the ICSID Convention") and the International Centre for the Settlement of Investment Disputes ("ICSID"), that enable the developing countries to signal the rest that they are willing to adopt a system that provides for protection of foreign direct investment ("FDI")[1] These signals transform into 'credible commitments' to treat foreign investors fairly[2] and presumably increase the appeal of these countries to foreign investors.

The developing economies and their attitude towards the ICSID Convention and the ICSID have been complex. During the first decades of ICSID's existence, most of the Association of Southeast Asian Nations ("ASEAN") countries adopted it, but virtually all Latin American countries avoided it, preferring to adopt a system of "internationalisation" of foreign investment contracts, which was inherently weak. In the 1990's, developing countries started to open up their economies and steps were taken in order to attract foreign capital. Developing countries' contempt for FDI largely disappeared and a vast majority of the Latin American countries became member States of the ICSID. Other developing countries like Russia and China joined in the 1990's. India never joined the ICSID. Though all the BRIC (Brazil, Russia, India and China) countries have entered into a lot of BITs for the promotion of trade, there seems to be a variety in the attitude of these countries when it comes to dispute resolution.

Conversely, the attitude of the developing countries towards ICSID in the recent past has been bordering the negative. This seems to be the case especially with Latin America. The most hostile of the developing countries are Bolivia, Ecuador, and Venezuela. In 2007, Bolivia became the first country ever to

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[1] Ignacio A. Vincentelli, *The Uncertain Future of ICSID in Latin America*, 16(3) LAW & BUS. REV. AM. 409 (2010).

[2] Zachary Elkins, Andrew T. Guzman and Beth A. Simmons, *Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000,* 60(4) INTERNATIONAL ORGANIZATION 822 (2006).

denounce the ICSID Convention, thus formally withdrawing from ICSID.[3] Ecuador and Venezuela followed suit.

This article looks at the reasons developing economies entered into Bilateral Investment Treaties ("BITs"), the settlement of disputes though investment arbitration, the frustration of developing economies with investment arbitration and possible outcomes in the future for the settlement of investment disputes.

II. Foreign Direct Investments and Developing Economies

One of the key factors for growth and development of a country's economy is capital. Foreign direct investments are one source of capital that developing economies are keen to tap into. Many developing countries enter into BITs with developed countries and with each other for transfer of capital.[4] Allowing FDI though looks like a sound economic choice, States will have to realize that international investments attract international rules and hence international forums for settlement of dispute. These international disputes and the awards from international disputes become enforceable through various treaties and conventions such as the ICSID, the country is part of.

FDI through BITs lays down various structural stresses on the host state. This starts right at the beginning when the host state provides tax incentives or tax breaks, special export or import tariff, waiver of various customs and excises, carbon credits, infrastructural benefits and such other exemptions to lure investment. Though the investment brings about short terms gains, in the longer run, how much the host state gains is a questionable factor. Host nations hence should account for the various factors before entering into a BIT. Host nations should also negotiate better to address its concerns before setting off to sign investment treaty agreements. They should also have a strong administrative system coupled with an active legislature and a robust judiciary. Though most BITs have clauses that reduce the functions of the host states involvement, it is up to the host state to convince the investor to repose faith in the domestic system. Investors are in general, uncomfortable with host state's administration and they further distance themselves from the host state's judiciary for reasons of bias. One of the reasons the investors prefer investment arbitrations is the factor of neutrality. Investors are apprehensive about the host state's administration, especially with developing countries, more so, with underdeveloped countries. These countries are in a developmental phase in

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[3] VINCENTELLI, *supra* note 1.

[4] Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Arab Republic of Egypt for the Promotion and Protection of Investments, *signed* June 11, 1975, *entered into force*, February 24, 1976 and India and Mauritius, BIT, September 4, 1998, w.e.f June 20, 2000.

regard to their administrative structure. BITs[5] provide for offsetting the lacunae in the domestic structure by providing for international investment arbitration. Investment arbitrations provide the structure needed to address investor- state disputes. Though the host state might not accept it willingly, it becomes one of the precursors for the FDI to go through, as the investment provides the much needed capital that gives the host country a competitive edge amongst other developing countries in a globalised economy.

The scope of Bilateral Investment Treaties is generally applied to all or most of the economic activities of foreign investors as a result of the broad connotation provided to the term 'investment' under the treaty. Hence, the scope of the investor to bring about an investment dispute against the host country, before an arbitral tribunal, is also expanded.

III. Investor Rights

Though Bilateral Investment Treaties are assumed to promote the interests of the foreign investor, the underlying principles of such treaties emanate from sound principles entrenched traditionally under international law. The right of equality and fair play are the basis from which investment treaties developed,[6] in allowing not just the state parties to the treaties, but the investors themselves to directly bring a claim before an international tribunal. Also, a number of treaties are drafted to ensure that contracts concluded by the host state and a foreign investor under the laws of the host state are also subject to the international guarantees provided by the treaty, including the dispute settlement mechanism under Articles 25 and 26 of the ICSID Convention, which pose that states have to refrain from requesting that local remedies be pursued. In turn, the investor's home state agrees not to grant diplomatic protection. Because the guarantees contained in the treaty are placed outside of the realm of diplomatic negotiations on the state-to-state level, the laws of the host state are subject to international review at the will of a foreign investor. At the same time, the classical stance of international law as inter-state law is modified in the field of foreign investment by lifting individuals onto the international plane vis-`a-vis the host state.[7]

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[5] Giorgio Sacerdoti, *The Proliferation of BITs: Conflicts of Treaties, Proceedings and Awards* (Bocconi Legal Studies Research Paper No. 07/02, 2007).

[6] Review written by Dr. Stephan W. Schill for IOANA TUDOR. *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment.* Oxford: Oxford University Press, Pp. xxxii (2008),

[7] Aishwarya Padmanabhan, *Relationship Between FDI Inflows and Bilateral Investment Treaties/International Investment Treaties in Developing Economies: An Empirical Analysis* 22, (2011) (unpublished manuscript) *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1764342.

In investment treaty arbitration jurisprudence, there are various ways for an individual entity or person to be qualified the right to bring an international claim against the state. The problem lies in the fact that under investment treaties, the particular form of individualization that is adopted is far- reaching. This is strengthened by two essential aspects. First, many investment treaties limit or remove the duty of the investor the need to exhaust local remedies and allowing them to bring a claim before the host state's courts have had the opportunity to resolve the dispute.[8] This was also laid down in the case of Maffezini (Emilio Agustin) v. Kingdom of Spain (2000)[9], CME Czech Republic BV v. Czech Republic (2003)[10] as well as Societe Generale de Surveillance v. Pakistan (2003)[11]. Second, these treaties encourage forum-shopping by allowing claims by foreign corporations without imposing restrictions in shareholder nationality or minimum thresholds of foreign ownership and control.[12] Thus, this gives a multitude of individual investors to bring claims more easily to the detriment of the host state, leading invariably to large number of litigations.

Further, under investment treaties, the host state's general consent and ratification of the bilateral treaty entails a broad waiver of its immunity from suit, not only before an international tribunal but also before a domestic court called upon to enforce an award. In addition, investment treaties authorize the enforcement of awards by investors under the ICSID Convention or the New York Convention. As a result, investors can seek enforcement of an award against assets of the respondent state in any state that is a party to these treaties.[13]

Thus, if a state refuses to abide by an award, it may be subject to diplomatic and economic pressure from the home state, from other capital-exporting states, from international financial institutions, and from the international capital market. Further, investment treaties often obligate states in express terms to recognize and enforce an award issued under the treaty, which allows an investor to seek enforcement in the courts of any state party to the treaty itself. Most importantly, where an investment treaty provides for enforcement under the ICSID Convention, the Panama Convention or the New York Convention, an investor can seek enforcement in the domestic courts of any state party to these arbitration treaties. This method of enforcement, according to Van Harten, is

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[8] GUS VAN HARTEN, INVESTMENT TREATY ARBITRATION AND PUBLIC LAW (Voughan Lowe ed., Oxford Univ. Press 2007).

[9] Agustín Emilio Case Maffezini v. The Kingdom of *Spain*, ICSID No. ARB/97/7.

[10] CME Czech Republic BV v. Czech Republic, Partial award and separate opinion, Ad hoc—UNCITRAL Arbitration Rules, IIC 61 (2001).

[11] SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan, ICSID Case No. ARB/01/13. Decision on objection to jurisdiction, (Aug. 6, 2003)

[12] *See Id.*

[13] *Id.*

exceptionally powerful as most states have ratified at least one of these three treaties: for example, approximately 165 states are party to either the New York Convention or the ICSID Convention

Based on this structure, investment treaty awards are more widely enforceable than the rulings of any court or tribunal, international or domestic that has the authority to resolve individual claims in regulatory disputes. For instance, the few human rights treaties that allow an international court or tribunal to hear individual claims do not authorize enforcement by domestic courts, whereas judgments of the International Court of Justice are enforceable only by the UN Security Council. In contrast, awards issued by investment treaty tribunals are enforceable in the courts of as many as 165 countries, which gives them coercive power and force that is unrivalled in public law adjudication.[14] Thus, as a system, the treaties greatly expand state liability in public law by extending it to legislative and judicial acts, and by allowing damages to be awarded in the absence of fault.

By opening the door to parallel claims and forum-shopping under so many treaties, states, specially developing economies, have moved too far to their detriment in international business. It seems they have executed a transformation of international obligations and adjudication without adequate consideration of the consequences.

IV. Reversal of fortunes for International Investment Arbitration

International Investment Arbitration has drawn the ire of the developing countries as it is seen as one sided and favouring the investors. Interpretation of contracts by arbitral tribunals vary, but the assumption of developing countries is that tribunals look only into the business aspect of contracts and seldom look into overall picture for which the BIT was signed. This pushes countries to prefer local jurisdiction over international investment arbitration.

Countries that plunge into economic crises get affected the most. A few examples are Argentina, Indonesia and Venezuela.

A. Case Study

i. Argentina

More than 30 cases of the cases presently pending before ICSID have been brought against the Republic of Argentina and assert that the Argentine Government's response to the catastrophic financial crisis that hit the country in late 2001 and 2002 impaired investor rights secured under several of Argentina's

[14] *Id.*

BITs/IIAs.[15] These cases are of extraordinary importance, not just because of the immense financial liability to which they expose Argentina, but also because, in response, Argentina has invoked a broad set of legal arguments about the rights of states to craft policy responses to extraordinary situations such as a massive financial collapse.

It all started in the last weeks of 2001 when Argentina experienced a financial collapse of magnum proportions.[16] In one day alone, the peso lost 40% of its value. In response to the crisis, which some likened to the Great Depression of the 1930s in the United States, Argentina adopted several measures to stabilize the economy and restore political confidence. Among these efforts was a significant devaluation of the peso through terminating the currency board, which pegged the peso to the US dollar, the pacification of all financial obligations, and the effective freezing of all bank accounts through a series of measures known collectively as the Corralito.[17]

Though these measures offered a long-term prospect of restored economic confidence and stability, they also imposed immediate and painful costs on all participants in the Argentine economy, including foreign investors. While the Argentine citizens had little recourse legally, many foreign investors, who were harmed by Argentina's response to the crisis, sought legal protection under the regime of BITs which Argentina had entered in to the 1980s and 1990s; (UNCTAD, 2000) apart from offering investors guarantees including the internationalisation of contractual breached ("umbrella clauses"), national treatment and most favoured nation protections, these treaties often provided investors the possibility of direct investor-state arbitration.[18]

For investors harmed by Argentina's response to the economic crisis, the possibility of direct arbitration against the Argentine government for breaches of BITs offered a potentially promising means to recoup losses suffered during the crisis. Claims framed as a violation of a BIT could be brought directly against

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[15] William W. Burke-White, *The Argentine Financial Crisis: State Liability under BITs and the Legitimacy of the ICSID System, in* THE BACKLASK AGAINST INVESTMENT ARBITRATION: PERCEPTIONS AND REALITY 407, 408 (Michael Waibel et al. eds., 2010) [hereinafter Burke-White, 2010].

[16] William W. Burke-White, *The Argentine Financial Crisis: State Liability under BITs and the Legitimacy of the ICSID System* 3 (U of Penn, Inst for Law & Econ Research Paper No. 08-01, 2008) [hereinafter Burke-White].

[17] CARINA LOPEZ, STANDARD & POOR'S, THE ARGENTINE CRISES: A CHRONOLOGY OF EVENTS AFTER THE SOVEREIGN DEFAULT (2002) *available at* http://www.standardandpoors.com/europe/francais/Fr_news/Argentine- Chronology-of-Events_12-04-02.html.

[18] M. SORNARAJAH, THE SETTLEMENT OF FOREIGN INVESTMENT DISPUTES 95 (2000).

Argentina through ICSID. Only limited means are available to challenge ICSID awards and such awards are generally enforceable in national courts.[19]

Not surprisingly, Argentina has become subject to no fewer than 43 ICSID arbitrations brought by investors asserting that Argentina's response to the crisis harmed investments protected by various BITs/IIAs (ICSID, 2007). Argentina's potential liability from these cases alone could be greater than US $ 8 billion, more than the entire financial reserves of the Argentine government in 2002. Some have speculated that the total value of potential claims against Argentina could reach US $ 80 billion.[20]

Argentina asserted two separate arguments that go to the heart of the sovereign prerogative of states to develop policies to address exceptional circumstances. This first is based on treaty law and the second, on customary international law. Argentina's treaty law argument invokes the non- precluded measures ("NPM") provisions of Argentine BITs that exempt certain actions taken by states in response to extraordinary circumstances from the substantive protections of the treaties. According to Argentina's customary international law argument, the doctrine of necessity precludes the wrongfulness of Argentina's actions in response to the crisis. These arbitrations, thus, test both the limits of state freedom of action and investor protections under the BIT regime in exceptional circumstances. The resulting jurisprudence of the ICSID tribunals in the four cases against Argentina decided as of early 2008 is deeply problematic, due to poor legal reasoning and questionable treaty interpretations. In fact, these litigations have cost Argentina very dearly as it has been made responsible for harms to investors notwithstanding the severe financial crisis it faced.

From the case studies stated above, a reasonable amount of apprehension and caution must be applied as conflicting decisions have arisen from the tribunals in these cases and establish no precedent and hence there is no stability or certainty that could comfort developing and emerging economies that could face a catastrophic crisis.

Companies have certain options that countries are not endowed with, which in turn permit companies to excuse themselves for dishonouring contracts. An option for a company that goes through bankruptcy can end up with rescheduled or even discharged debt, renegotiated union contracts and relief from contractual pension obligations. Surely, it is not surprising that a backlash occurs when a host country fails to receive similar relief from obligations to direct investors when it faces severe economic problems.

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[19] BURKE-WHITE, *supra* note 16, at 5.
[20] BURKE-WHITE, 2010, *supra* note 15, at 411.

In fact, the regimes that handle sovereign obligations of developing countries generate oddly perverse outcomes. With arbitrators' rigid interpretation on contract, foreign direct investors are likely to come out better in crisis-stricken countries than are holders of sovereign debt. Governments sometimes reduce the value of debt unilaterally – by 70% or so in the Argentine case- or negotiations in the London Club or the Paris Club result in rescheduling or partial discharge – while foreign direct investors stand to be made whole by arbitrators. This creates a topsy-turvy world where foreign direct investors stand ahead of debt holders in the queue for claims in crises. Direct investors hold equity in their projects and contend that they should earn higher returns than lenders, as compensation for the risks associated with equity.[21] Yet, when it comes to dispute settlement for countries in crises, the priorities are the opposite of what a bankruptcy court would establish inside an industrialized country.

Further, States have increasingly relied on customary public international law as a defence to excuse investment treaty breached. Argentina, in particular, has recently invoked the doctrine of necessity to excuse any breaches of its investment treaty obligations in the numerous disputes that arose from the economic crisis of 1999-2002. Such public international law defences, collectively called state defences, excuse a state's actions if specific preconditions are met. These include force majeure, necessity, bribery or international public policy, legitimate exercise of sovereignty, including other several defences based on customary public international law. Though these defences can be invoked even in the absence of a specific provision in an investment treaty, they are subject to strict limitations. Only a limited number of investment arbitration tribunals have accepted state defences.[22]

Moreover, it needs to be pointed out that even when these defences are successful; their effect is often merely to suspend the state's obligation for a short period of time. In practice, that means that the state defence will only reduce the amount of compensation payable and the state will not be fully excused for its behaviour. Thus, state defences are not an easy way for a state to escape its international responsibility. Even the defense of "legitimate use of sovereign power" has not yet been established in the realm of investment arbitration – only three tribunals have relied on this defence to date. However, it has been noted by Martinez that the trend is beginning to look as if the tribunals are now more willing to consider the specific circumstances faced by states and less perceptive to the plight of investors. This is arguably a symptom of the backlash against investment arbitration.[23]

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[21] WAIBLE, MICHAEL, ET. AL, THE BACKLASH AGAINST INVESTMENT ARBITRATION: PERCEPTIONS AND REALITY (2010).
[22] PADMANABHAN, *supra* note 7, at 29.
[23] *See id.*

Further, under almost all BITs/IIAs, the state has no authority to go to arbitration to collect damages from an investor that does not carry out its obligations under an investment agreement.[24] Most of the time, it is the investor who is able to initiate the renegotiation of the contract when they face problems. A World Bank study of renegotiation of infrastructure investment agreements in Latin America found that more than half of renegotiations have been initiated by investors, not by the host nation.[25]

One good instance of this was in the Aguas Argentinas case (Aguas Argentina S.A. Suez, Sociedad General de Aguas de Barcelona S.A. and Vivendi Universal S.A. v. The Argentina Republic, IICSID Case ARB/03/17) involving water for Buenos Aires, which was heard at the ICSID. In the past, Suez and other investors in this project had initiated renegotiations to change the terms to be more favourable to them. The government had no international rights to enforce the terms of its original contract when faced with investor demands. On the other hand, when the Argentine financial crisis struck and the government was under pressure to renegotiate, the lead investor filed for arbitration to enforce the most recent version of its agreement.

ii. Indonesia

Following the Asian currency crisis, two US investors in Indonesia were given awards by arbitrators that showed little sympathy for the need for relief (*Karaha Bodas Company* v. *Perusahaan Pertambangan Minyak Dan Gas Bumi Negara*, 2000).[26] With the collapse of the Indonesian currency, the government– and the state-owned Power Company – had tried to renegotiate contracts for unfinished power plants that would have produced electricity thought not to be needed in the subsequent deep recession and which required its purchase at prices that were up to six times in local currency what had been originally negotiated. It would have been political suicide for the government to authorize such price increases.[27]

Many investors renegotiated their arrangements. Some, however, refused and turned to arbitration. Arbitrators, with little attention to the collapsing economy in Indonesia, awarded investors not only what they had invested in the projects

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[24] *Id.*
[25] SORNARAJAH, *supra* note 18.
[26] *Karaha Bodas Company LLC* v. *Perusahaan Pertambangan Minyak Dan Gas Bumi Negara and PT. PLN (Persero)*, ad hoc arbitration under UNCITRAL rules, Final award of (18 Dec., 2000).
[27] PADMANABHAN, *supra* note 7, at 26.

to date – a sensible base award- but also a substantial portion of the net present value of 30 years of future earnings.[28]

iv. Venezuela

President Carlos Andrés Pérez, opened up Venezuela to FDI in the early 1990's. Pérez's presidency came to halt on grounds of corruption accusations, which began after his presidency undertook a major reform in the country that has been called 'neo-liberal.' Among the most relevant aspects of such reform were: (i) privatisation of the country's public companies, including a national airline, the national phone company, and different electricity companies; (ii) liberalisation of the interest rates, which, until then, were fixed by the Ministry of Finance and (iii) an increase in the price of gas.[29]

These reforms proved to be very unpopular. After Pérez's removal, the head of the Venezuelan Congress, Ramón J. Velásquez, served for the remainder of the presidential term. In the 1993 elections, former President Rafael Caldera was elected for a second term in office. During Caldera's second presidency, Venezuela experienced a rapid downward economic spiral. The government's response included the continuation of several of the unpopular economic measures adopted by Pérez. Among the measures implemented in the framework of a program called Agenda Venezuela, were: liberalisation of interest rates, raising the price of fuel, devaluation of the currency, imposition of a foreign currency exchange control regime, and further opening of the oil sector to FDI, through continuation of a program called the Apertura Petrolera (Oil Opening).[30]

However, the social-economic and legal scenario radically changed in Venezuela after the December 1998 elections, when Chávez gained power. The arrival of a former insurrectionist in power, four years after being condoned by the incumbent President Caldera, drastically halted the free-market measures implemented by the past governments. When President Chávez took office in February 1998, he promised a major reform of the National Constitution, and the installation of a new economic system. In 1999, a new Constitution was passed by a national constituent assembly. The Chávez administration gradually implemented major legal reforms, including enactment of a new Hydrocarbons Law in 2001. Such reforms gave momentum to major strikes and public manifestations of discontent, which resulted in the ousting of Chávez in April, 2002 for two days. Shortly after his return to power, Chávez became more drastic in the implementation of his programs. Finally in February 2005,

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[28] Louis T.Wells, *Double Dipping in Arbitration Awards? An Economist Questions Damages Awarded to Karaha Bodas Company in Indonesia,* 19(4) ARB INT'L L 472 (2003).
[29] VINCENTELLI, *supra* note 1.
[30] VINCENTELLI, *supra* note 1, at 52.

President Chávez said for the first time that his programs and policies were all directed towards the "socialism of the 21st Century."[31]

The Chávez Administration announced the strict application of the Hydrocarbons Law of 2001 through the implementation of the programs Plena Soberanía Petrolera (Full Petroleum Sovereignty), and Siembra Petrolera (Planting Petroleum). These programs involved renegotiation of the oil contracts with private investors, and a consequent dramatic increase of the country's share in the profits. The Apertura Petrolera had died. Some investors resisted the mandated change (a.k.a., process of migration) from a private to a mixed corporate form, with a majority stake in the hands of the State. ExxonMobil and ConocoPhillips preferred to file a claim against Venezuela before ICSID during the last trimester of 2007, rather than accept the new terms.[32]

While announcing the arrival in Socialism to Venezuela, Chávez commenced a series of expropriations and nationalizations changing the panorama for foreign investors and FDI. The first expropriations were targeted at agricultural farms. Two of the highest-profile cases were Hato La Marqueseña and Hato El Charcote. The latter belonged to the Vestey Group, from the United Kingdom, who decided to take Venezuela before ICSID in 2006. Recently, other strategic industries have been targeted by the government, including: telecommunications, by the announcement of the de-privatization of the national phone company – CANTV-; electricity, by the announcement of the de- privatization of the Caracas' power company – Electricidad de Caracas-; and cement, by the announcement of the acquisition of the four largest cement companies (Andino, Caribe-Holcim, LaVega-Lafarge, and Vencemos-Cemex). These rationalizations have also resulted in two ICSID claims against Venezuela.[33]

Venezuela has settled four of the six cases already concluded before ICSID. The only two cases that have reached an arbitral award did not involve large amounts. Recently, Venezuela has taken some measures that are unfriendly towards ICSID arbitration, directly targeted to potential claims that may arise out of the recent expropriations and nationalizations. Aside from the hostile political discourse against ICSID, the two most important "anti-arbitration" steps taken by the government are the denunciation of the Venezuela-Netherlands BIT, and the Supreme Tribunal's Decision number 1541 of October 17, 2008. Yet, it remains to be seen what will be the effects of these "anti- arbitration" measures in the other four cases against Venezuela currently outstanding before ICSID, and in any other potential claim that may be filed in the near future.[34]

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[31] *See id.*
[32] VINCENTELLI, *supra* note 1, at 53.
[33] *Id.* at 54.
[34] *Id.* at 55.

One of the crucial aspects is the process through which deals are struck by foreign investors in developing countries. Reflections on these deals suggest corruption or incompetence, or both, on the part of government officials. This is mostly due to the relative political instability in developing nations apart from a few. New governments tend to overrule agreements and treaties signed by previous government leading to disputes. This puts host state under more pressure as failure to meet treaty obligations will eventually result in the tribunal favouring the investor. Though arbitration panels have concluded that an agreement was unfair to the host country because there were kickbacks paid, such awards are seldom made. The standards of proof to prove corruption has also been set so high that very few governments have been able to produce convincing evidence. A good example of this was the Indonesian electric power cases where in all the three power projects that went to arbitration, members of government officials' families or military organizations (in a country with a military-backed government at the time) had received shares in the projects for no obvious contributions – money, skills or market access.[35]The arbitrators did not look in to these factors at all. As a result, contracts that are unfair to the host government are enforced. Thus, developing countries would be forced to pay up even on what they reasonably view to be "odious agreements" which had been signed by previous corrupt or inefficient governments. This onerous legacy and liability would continue to persist on the countries' governments.

Moreover, investor-state arbitration has been infamous for attracting calumny regarding arbitrators' integrity. Arbitrators tend to favour the claimant- investor in order to increase prospects of reappointment.[36] ICSID arbitrations receive most of the slander in this regard. This perceived apprehension on behalf of the host state, on the bias of the arbitrators, also makes investment arbitration an unfavourable option. These contentions and perceived bias apprehensions have been also offset by the number of decisions of tribunals that have been in favour of the host states.

V. Future Possibilities for dispute resolution

The apprehensions (not exhaustive) of the host state for trusting investment arbitration have been put forward. A few possible options for settling investment disputes are discussed hereunder.

A. Multilateral Investment Treaty

The current fragmented international investment regime shows the degree of complexity and confusion of the system, with many contracting parties, some

[35] PADMANABHAN, *supra* note 7, at 30.
[36] VAN HARTEN, *supra* note 8, at 4.

bilateral, others regional or even multilateral, as we have seen in the case of WTO Agreements. This fragmented regime may encourage regulatory competition among the various models of international investment agreements. This fragmentation of the international investment regime may also create an incentive for treaty shopping by those foreign investors who seek protection even in situations where their country has not concluded or ratified investment agreements that offer the same level of protection as those achieved in other countries.[37]

The proliferation of investor-state arbitrations is evidence of the fact that, for the time being, bilateral and regional governance of investment via BITs and investment chapters of FTAs will be the prevailing means of governing FDI. That said, so much investor-state arbitration is causing issues of conflicting arbitral awards and forum shopping. All of this would be solved with the creation of a stable, non-discriminatory multilateral investment treaty. Hence, it is desirable to create a multilateral investment treaty.[38]

Furthermore, as analysed above, environmental and labour standards – which until now have only been treated marginally in international investment agreements – are increasingly seen as inseparable from foreign investment and therefore, from a substantive point of view, it is key to ensure that they are incorporated in a future multilateral framework for investment. This will be even more justified as globalisation continues to be a reality that affects the social and environmental responsibility of foreign investors.[39]

One of the suggestions for the way forward has been a Multilateral Investment Treaty ("MIT"). This was brought about in the year 2001 during the Doha negotiating round of the WTO. This treaty was strongly opposed by many of the developing countries including BRIC for the fear of losing control to adjudicate matters in their domestic courts.

A comprehensive multilateral framework for investment would serve as a template for a new generation of bilateral and regional investment treaties. It would help to reduce transaction costs and enhance the economic benefits of FDI. Regarding the design of such a multilateral framework for investment, the WTO has the opportunity to encapsulate years of development of an international framework for investment in the first truly multilateral agreement for investment. Such an agreement in the WTO context would not replace current bilateral and regional investment regulatory regimes, but could clarify

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[37] Rafael Leal-Arcas, *The Multilateralization of International Investment Law,* 35(1) N.C.J. INT'L L. & COM. REG. 105, 919 (2009).
[38] *Id.*
[39] *Id.*

the relationship among the GATS, the TRIMs Agreement, and BITs. Although the success of this project remains unknown, much work has already been inherited via the BITs, the GATS, the NAFTA, the Energy Charter Treaty, the TRIMs Agreement, and the failed MAI. The WTO has the chance to build upon these experiences.[40]

Though MIT was opposed the first time, there is lot of open space that can be explored. Issues brought by the developing countries can be researched and a better adjudication process can be brought about. The *ratione materiae* for adjudication can be clearly defined. The MIT could also propose an investment court for settlement of disputes of a defined nature. Hence, the scope for a Multilateral Investment Treaty still exists.

B. International Investment Court

There is also a case for an international investment court. One of the chief proponents of this argument is Gus van Harten. This argument is presented relative to existing arrangements that use a treaty-based arbitration mechanism to resolve investment disputes between states and investors.[41]

This argument presents a narrow central distinction between judges and arbitrators: the secure tenure of the former and the insecure tenure (case-by-case appointment) of the latter. This orientation of the argument leads by implication to the assertion that there is something wanting in terms of the independence and impartiality of arbitrators in the existing arrangements based on investment treaty arbitration. Given this, the present case is meant to respond to a critical flaw in an existing arrangement for international adjudication by elaborating upon an alternative.[42]

It should be made clear from the outset that apparent bias in investment treaty arbitration is just that: it is a reasonable suspicion of bias (not actual bias) arising from structural failings of arbitration when used to determine matters of public law. The critique of investment treaty arbitration should thus not be taken as a condemnation of anyone involved in investment arbitration; there are many jurists, lawyers, academics, and business people of skill and integrity who sit as arbitrators and whose reputation is not sullied by an objective critique of the structure of the system and, in particular, its lack of objective guarantees of independence and impartiality. The difficulty is that the current structure of investment treaty arbitration casts a pall over all awards, and all legal interpretations, that emerge from the system in spite of the

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[40] *Id.*
[41] VAN HARTEN, *supra* note 8, at 4.
[42] *Id.*

experience, qualifications, integrity, etc. of the arbitrators, for reasons quite unique to this system and not to others where arbitration is used.[43]

There is a possibility of other alternatives that could be better at providing impartial and independent awards. This system could also take into account various stakeholders including countries, governments, investors, and even other systems that rely properly on arbitration to resolve disputes, especially commercial arbitration. The clearest alternative to the present arrangement is to establish an international investment court.

One of the prime bases of this argument is that International Investment Law is a subject matter of Public International Law and hence investment treaty arbitration is a form of public law adjudication in which the meaning of public law is resolved finally by adjudication. Second, for this reason, it should be evaluated according to standards that apply historically in public law. Third, the current system's failure to satisfy these standards, especially security of tenure, calls for an institutional arrangement that does satisfy them. Lastly, various counter-arguments that have been offered or that might be offered in opposition to an international investment court, founded on the principle of security of tenure in public law adjudication, do not warrant maintaining investment treaty arbitration as an alternative to such a court. For this reason, States should be encouraged to establish an international investment court in accordance with well-known principles of judicial decision- making in public law.[44]

The argument remains grounded in the theoretical distinction between the use of arbitration to resolve regulatory disputes and its use to resolve commercial or other private disputes. There are powerful criticisms of public-private distinctions from various perspectives and elucidate specific differences in casting the major types of adjudication, while acknowledging the possibility that the distinction may leave gray areas or be simply inappropriate in some circumstances. The public- private distinction rests in turn on a concept of the state as sovereign.

The concept of state as sovereign has received some stick in the recent past. For purposes of a public adjudication system, the reference to sovereignty is as an instrument for identifying and analysing certain activities of states as activities that states alone are able to engage in; for example, the passage of general rules accepted as binding in society and ultimately enforceable by the state's coercive power. Recognising this uniqueness of the state as sovereign, arising from its role as the representative of a political group

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[43] *Id.*
[44] *Id.* at 3.

associated with a particular territory, is useful in that it helps to reveal the distinctiveness of the relationship between the state and those who are subjected to or affected by regulatory activity of the state. As a concept, sovereignty is a means of social ordering that is important (though of course not beyond challenge or doubt) and that has sufficient probative value here, it is suggested, to enable an elaboration of the sorts of disputes that arise between investors and states and how those disputes differ from disputes arising between parties that are equally capable of possessing legal rights and obligations.[45]

An important aspect of disputes arising between a sovereign state and a foreign investor is that they are one-sided in that the powers and obligations of the entity on one side, the state, has a different set of powers and obligations in law than the entity on the other side, the investor. In some respects, the state will possess rights that private parties cannot hold such that the state will have powers that are specifically sovereign. In other respects, the state may be bound by sovereign obligations that a private party cannot possess or that a private party is in a unique position legally to avoid or abbreviate (by for example declaring bankruptcy). Where a dispute between a state and a private party occurs in relation to the state's exercise of these uniquely sovereign powers or its assumption of uniquely sovereign obligations, the dispute is described here as a 'regulatory dispute' and the adjudication of that dispute as a form of 'public law adjudication'.[46]

Thus, for present purposes, the public-private distinction entails recognition of the state as an entity with unique characteristics and of this concept of the state as the basis for public law as a category of study, enabling (even if roughly or with doubt) a distinction between instances in which adjudication is used to resolve regulatory disputes and instance in which it is used to resolve disputes originating in a reciprocal relationship between juridical equals.

The skeletal argument presented by Gus Van Harten is that there is (1) that investment treaty arbitration is a form of public law adjudication, (2) that it fails to satisfy standards of independence and impartiality in public law, and (3) that various reasons that might be offered to justify this are unsatisfactory in light of the importance of these standards. The next step would be to explore the various possibilities and prospects. An international investment court could be multilateral, regional, or bilateral. It could be a full court or an appellate body court that would hear appeals from decisions made in the first instance by arbitrators. It could be an autonomous entity or housed within

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[45] *Id.* at 4.
[46] *Id.* at 5.

existing institutions. It could be staffed by dedicated judges or via a roster of jurists who sit on domestic courts. Ultimately, it is not so important to arrive at a specific design for an international investment court that suits all states or all commentators. Much more important is to recognise that the present system is flawed and call upon states to address this flaw. Ideally, states will act jointly to do so but to the extent that cooperation proves elusive, like-minded states should not hesitate to pursue alternatives to investment treaty arbitration with respect to their own treaty networks.

The critical point is that alternatives should be measured against the criteria of judging in public law, especially the related concepts of openness and independence. Without these standards being met, one does not have a system that depoliticizes disputes and subjects them to the rule of law, or that deserves the respect of all interested parties, above all developing states. At present, when Argentina or Ecuador or the Czech Republic is unsuccessful in investment treaty arbitration, its government and people have justifiable reason to reject the result as unfair, the process as structured unfairly against the host state, and the award as inferior in legitimacy to that of a court decision.

There is clearly an important role for arbitration in contexts outside of public law, where the concerns elaborated here are much less pertinent. There is also a need for international adjudication to address concerns arising from domestic regulation of foreign investment in a global economy and the threat of arbitrary or discriminatory treatment by host governments. In this respect, it would be beneficial for investors in general, as well as states, to establish a system that is widely regarded to be free of perceived bias. And regardless of one's views about whether there is a sufficient basis for doubts about the integrity of decisions emanating from the current system, why risk the possibility of many believing this to be the case? There is a clear alternative that is achievable, with awareness and political will, and states should be encouraged to pursue it.[47]

VI. Conclusions: Twilight

In a globalised world, flow of capital cannot be stopped. But the flow of capital also has to be protected, measured and controlled. Investment arbitration seemed to be the answer to protect capital and also to provide the much need control that host countries needed over the capital. Investment arbitration appeared to fill the gap in the *Barcelona Traction* case. In that case, the ICJ held that a State could make a claim when investments by its nationals abroad were prejudicially affected in violation of the right of the State itself to have nationals enjoy certain standards of treatment previously agreed in a treaty or

[47] *Id.* at 30.

special agreement ("diplomatic protection"). Yet, the common situation when no such treaty or special agreement existed, thereby covering the particular conflict, was that investors would be left unprotected.[48] Though conventions like ICSID try fill the lacunae left by the *Barcelona Traction* case,[49] they are incomplete Investment arbitrations appear to work well when the economy is growing, domestic institutions at host countries are transparent and corruption free and there is political will to honour international commitments. But when there is deficit in any of the conditions prescribed above, investment arbitration fails.

The alternatives to investment arbitration like Multilateral Investment Treaties and International Investment Court seem farfetched at this point, but not entirely impossible. Though there are various grievances within the present system of investment arbitration, this system is there to stay in the light of lack of alternatives. If the current system is tweaked a little, with a wholesome approach, taking all stakeholders into account, the system is there to say for some time.

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[48] VINCENTELLI, *supra* note 1, at 1.
[49] *Id.*

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LEGAL AND CONSTITUTIONAL JUSTIFICATION OF WHITE INDUSTRIES

Pranshu Paul[*]

I. INTRODUCTION

It is often said that *"justice delayed is justice denied"*. The Arbitral tribunal in *White Industries Australia Limited ("White")* v. *Republic of India ("India")*[1] fell short of this conclusion when it held that justice delayed is not quite justice denied but certainly amounted to failing to provide "effective means" of asserting claims. This is of course in the context of White failing to have its jurisdiction claims *asserted* in the Apex Court of India, although it is a fundamental principle of international law that domestic legislation cannot override obligations of a sovereign State under international law.[2] This was upheld by various cases such as the *Lockerbie*[3] and *La Grand*[4] matters in the ICJ. At the same time, domestic law and constitutional arrangements such as the requirement of ratification are not utterly irrelevant[5] since Governments cannot bind States through treaties in excess of their powers or in violation of the procedure under domestic law.[6] It is also clear that once White approached the Supreme Court of India, the Government of India could have done nothing to expedite or resolve the dispute under the Constitution of India. But it is equally true that if a country wants to be economically competitive in a globalised world, it must keep an efficient mechanism to resolve the disputes arising out of the same.

Domestic standards cannot be the sole criteria for defending State efforts in honouring an international obligation. From the judgment, it is important to note that India has been penalized not because the government failed to act in a certain manner. It has been penalized because the State as a whole, the executive and the judiciary have failed to put an institutional structure which is expeditious in nature, to support the BIT entered into with Australia. Thus, at the heart of this lies the age-old debate of international law versus municipal law, on which much juristic ink has been spilled. Some view the award as attacking

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[1] White Industries v. India, *available at:* http://italaw.com/documents/WhiteIndustriesv.IndiaAward.pdf.

[2] *ICJ Rep*. 1988, at 12,34 *reprinted in* 82 ILR 225.

[3] *ICJ Rep*. 1992, at 3,32.

[4] *ICJ Rep*. 2001, at 90-1.

[5] *See*, KRYSTYNA MAREK, DROIT INTERNATIONAL ET DROITINTERNE (1961).

[6] MALCOM N. SHAW, INTERNATIONAL LAW, 124-26 (5th ed. Cambridge University Press, 2003); *See also*, C.W. JENKS, THE PROSPECTS OF INTERNATIONAL ADJUDICATION (1964); H. LAUTERPACHT, THE DEVELOPMENT OF INTERNATIONAL LAW BY THE INTERNATIONAL COURT 43 (1958).

judicial sovereignty, because an external authority evaluated Indian court orders, indicting the Indian judicial system as "slow" and "seriously overstretched",[7] while it should be considered as a rude awakening by developing countries entering into BIT's with other nations to lure capital and flow of resources from it, as we can see that India has started the process of renegotiation of such treaties.[8]

II. FACTS

The origin of this decision can be traced back to 28th September 1989, wherein Coal India entered into a contract with White Industries to develop an open cast mine in Piparwar. It was signed by the subsidiary of Coal India, Central Coal fields limited, under the Indian-Australian Bilateral Assistance Programme. It had been negotiated between the two companies, who had agreed on exclusion of the Indian Arbitration Act 1940, and provided for an arbitration tribunal to be set up following the rules of UNICTRAL having a seat in Paris.[9] The government had almost no part in this decision_ making process, where White Industries was to provide Coal India with a soft loan for the same.

Disputes arose between Coal India and White Industries with respect to the terms of the contract which provided that Coal India will receive a bonus when the mining was on schedule with the target being met and pay a penalty when the target fell short. Further disputes arose about the quality of coal being produced, which according to Coal India did not meet the specifications as stated in the contract. Thus, disputes arose about the amount of bonus and nature of bonus to be paid to White Industries as per the contractual obligations between the two companies. Under such circumstances, Coal India encashed the bank guarantee as given by White Industries to the tune of 2.77 Million AUD$, aggrieved by which White Industries filed a request to initiate arbitration proceedings.

The ICC tribunal, formed on 28th June 1999, gave a decision on 27th May 2002, wholly in favour of White Industries.[10] White Industries initiated proceedings in the Delhi High Court to enforce the Award of the tribunal in 2002, but Coal Industries filed an anti-suit injunction in the Calcutta High Court

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[7] P.K. Suresh Kumar, *Globalisation and the Judicial Sovereignty of India*, 47(49) EPW 47,(2012).

[8] Vivek Vashi & Kanika Sharma, *Increasing litigation under Bilateral Investment Treaties – should the Government be worried?,* INDIAN L. J. (date of article in format: Oct. 28, 2012 within brackets) *available at:* http://indialawjournal.com/volume5/issue_2/article_1.html.

[9] White Industries v. India, *supra* note 1, at 1, at para. 3.2.18.

[10] *Id.*, at ¶.3.2.33.

to prevent the enforcement of the same. The Calcutta High Court assumed jurisdiction even though a clear arbitration clause had been spelt out, taking into consideration the newly formed Arbitration and Conciliation Act of 1996. White Industries appealed against this decision, which was rejected and finally had to approach the Supreme Court in July 2004. The matter remained stayed and lingered in the Supreme Court till 2009, and the Delhi High Court awaited the decision of the Supreme Court.

Agitated and aggrieved, White Industries wrote to the government in 2009, asking them to intervene and solve the matter as per Article 13(2) of the BIT[11] by coming to an amicable solution. But, the Indian government did not respond within the specified period of six months as per the BIT clause, following which White initiated an Investment Arbitration against the Union of India, which was decided in its favour. The tribunal applied the benchmark of "effective means" to hold India in want of the provisions of the BIT and provide White Industries with the compensation of the arbitral award plus interest and other expenses.

III. LEGAL JUSTIFICATION

A. International Law

"There is little use in going to law with the devil while the court is held in hell." stated by Humphrey O' Sullivan, refers to the argument preferred by all parties going to investment arbitration under a BIT as they state that domestic courts are not objective.[12] They go against State actions and believe that domestic courts would be biased. State actions and practice forms an important part of international law as has been mentioned in the famous *Scotia Case*,[13] and we cannot attribute State action on predictability in case of no State enforcement. In *White industries* too, the government did not break Article 3(1) of the BIT which stipulates creation of favourable conditions and Fair and Equitable Treatment[14] by not creating favourable conditions for redressal, but these conditions were out of its control due to the doctrine of separation of powers as stated in the Indian constitution. Even the tribunal acknowledged that *White Industries* knew of the Indian judiciary being "slow" and "seriously overstretched" and thus no legitimate expectation can be attributed as stated in *TECMED S.A* v. *United Mexican States*.[15] Thus, there was definitely no breach, under the denial of justice standard, as per the

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[11] *Available at:* http://unctad.org/sections/dite/iia/docs/bits/australia_india.pdf.

[12] *See*, HUMPHREY O'SULLIVAN, THE DIARY OF AN IRISH COUNTRYMAN 1831 (Dufour Editions, 1997).

[13] *The Scotia*, 81 U.S. 14 Wall. 170 (1871).

[14] *See supra* note 11

[15] Tecnicas Medioambientales Tecmed v. Mexico, 43 I.L.M. 133 (2004).

standards held in *Chevron* v. *Ecuador*.[16] Then how is India accused of not being able to provide the effective means not stated under the BIT, something beyond the power and control of the government?

The legitimacy of the same is derived from treaties signed by a nation under international law. *Pacta sunt servanda*[17] provides that all nations would be bound by the obligations as signed by them with another nation. No nation can in such a manner outrun such an obligation which is like a contract. The obligation created here arose when a sovereign government, India, contracted a treaty, i.e. BIT, creating obligations towards any investor from the contracting country with respect to protection of investment and fair and equitable treatment. But additional obligations arose because of 'treaty shopping' via the "most favoured nation" principle, leading to a binding obligation on the host State, wherein White industries borrowed the principle from other treaties to which India was a party.

Furthermore, when such a claim is to be treated as legitimate, the question which arises is about its breach. Following the dualist theory in international law,[18] one cannot take the defence of domestic laws to escape international obligations. International obligations have to be of paramount importance (*Arbitmte Case*),[19] which can be further supported by looking at article 27 of the Vienna convention on law of treaties,[20] to which India might not be a signatory, but has become a customary rule under international law.[21] Therefore, as seen in the *Alabama Claims Tribunal*,[22] one nation cannot take a defence of domestic impediments or law to absolve itself of international obligations. Like in *Lockerbie*,[23] the executive could not have gone beyond its powers once the

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[16] Chevron v. Ecuador, UNCITRAL, PCA Case No. 2009-23.

[17] VCLT Art.26 (1969).

[18] JANNE NIJMAN & ANDRE NOLLKAEMPER, NEW PERSPECTIVES ON THE DIVIDE BETWEEN NATIONAL AND INTERNATIONAL LAW 57 (1st ed., Oxford Univ. Press, 2007) (Dualism appears to be that the international law and municipal law are viewed as separate legal systems, which may be defined as self-contained, because within each system the only existing rules are those part of the system. Rules which are not created within the system may nevertheless be relevant for the system if they are referred to by a rule included in the system).

[19] *ICJ Rep*. 1988, at 12,34 *reprinted in* 82 ILR 225, 252.

[20] *Available at:* http://untreaty.un.org/ilc/texts/instruments/english/conventions/1_1_1969.pdf (Internal law and observance of treaties: A party may not invoke the provisions of its internal law as justification for its failure to perform a treaty. This rule is without prejudice to Article 46).

[21] *See*, Kearney & Dalton, *The Treaty on Treaties*, (1970) 64 AM. J. INT'L L. 517; *See also*, Sir Humphrey Waldock, OR 1968 COW158, para.73; *See also*, Sir Humphrey Waldock, OR 1968 COW 53, para.31.

[22] J. B. MOORE, INTERNATIONAL ARBITRATIONS 495 (1898)

[23] *ICJ Rep,* 1992, pp. 3, 32.

case was initiated in the judiciary due to the strict separation of powers and the structure of the Indian constitution providing absolutist rights to the judiciary in disposing of maters when approached. And imposing upon the same would have been seen as a violation of the same and would be invalid as per law.

Therefore, the State, without fault under international law, can be held to a legitimate claim, leading to reparation by the State. *Rainbow Warrior arbitration,*[24] clearly shows that international law does not distinguish between contractual breach and the breach by any other method. It recognises that there should have been existence of State Responsibility, which can be interpreted by both the treaties being read together. Secondly, applying the objective or strict responsibility test under international law as held in the *Sapiem Tribunal*,[25] an act or omission which took place with or without the fault of the government itself can lead to a legitimate claim, and thirdly, damage should have resulted which can be claimed to take place due to the delay in the enforcement under the *White industries case*. But it must be seen that India did not breach the "fair and equitable treatment" clause nor did it expropriate any property of White Industries yet a *lex specialis* was breached between the parties. The clause being breached was the effective means clause as imported into the Indo-Australian BIT via Treaty Shopping. This points to the fact that India as a State was responsible for working of all its organs and not just of the government of India.

B. Constitutional Challenges

With increased globalization of economic regimes, ideas of State sovereignty have undergone dramatic changes. In reality, with the phenomenal growth in communications and consciousness, and the constant reminder of global rivalries, not even the most powerful of States can be entirely sovereign. Reality circumscribes the concept of sovereignty in operation. In such a context, the award, in consonance with India's international obligations under the India-Australia BIT, can hardly be said to be an attack on State sovereignty. In the alternative, the BIT as a whole may be called unconstitutional for allowing the violation of the principle of separation of powers. But as long as the International Arbitration Tribunal, in granting its award, was simply acting in accordance with the BIT, the award itself cannot be challenged.

This leads to the inevitable question: in a situation of conflict, do international obligations prevail over domestic law, or vice-versa? States cannot invoke internal law provisions to justify their failure to perform international

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[24] New Zealand v. France, 82 ILR 17 499. (*Saipem* v. *Bangladesh*, ICSID Case No. ARB/05/7.)

[25] Saipem S A v. Peoples Republic of Bangladesh, ICSID Case No. ARB/05/7, Jurisdiction, p.100 (Mar. 21, 2007).

obligations.[26] But international law conflicts with domestic law, theorists usually turn to one of the three possible theories: monist, dualist and the Fitzmaurice doctrine. While the first views municipal and international law as one unified whole, the second sees them as separate entities. Monist countries adhere to international law when it is in conflict with domestic obligations, while in dualist countries, municipal law prevails in such situations. The Fitzmaurice doctrine on the other hand, denies them any common field of operation, so that neither system is superior or inferior to the other.

India is dualist; its Parliament must actively legislate to incorporate international obligations into municipal law.[27] But its written Constitution complicates matters. India has ratified UNCITRAL's 1958 "New York" Convention, and our Arbitration and Conciliation Act is based on UNCITRAL's 1976 Arbitration Rules and 1985 Model Law.[28] Thus, we have passed national legislation conforming to our international obligations in the arena of international commercial arbitration. The dualist requirements have so been fulfilled, but it cannot be said with certainty, that during situations of conflict, domestic law will always prevail in the Indian legal system, in strict adherence to the dualism theory.

Therefore, even though the Indian constitution provides for strict separation of powers, it also grants the executive the power to enter into international obligations. Although, they cannot be held to be superior to internal obligations, each organ of the State has to bear the responsibility as such international obligations tend to treat the State as a whole rather than as separate organs. The basic structure and principle of separation of powers has to be reconciled when such matters have international obligations. Thereby, even if the executive could not have been able to take any steps once the matter had reached the judiciary, the judiciary should have seen its responsibility and worked towards them, prioritizing such commitments which treat the State as a whole.

IV. ISSUES RAISED BEFORE THE TRIBUNAL

The Tribunal, in its quick award, discussed issues as to how such money can be considered an investment and how the Indian government been in breach of the treaty. For our specific area of interest, we will focus on how the Indian government has breached the BIT and not been able to reconcile obligations with respect to the Indian constitution. Therefore, there are two implications of the Tribunal ruling pertaining to how India can potentially violate its BIT obligations, with respect to the "effective means" standard. Inordinate

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[26] VCLT Art.27 (1969).

[27] The Constitution of India, art.51, 253 ; Verghese v. Bank of Cochin, AIR 1980 SC 470; Gramophone Company of India v. Pandey, AIR 1984 SC 667.

[28] Arbitration and Conciliation Act, Preamble (1996).

delays in the Indian courts can be one way of violating a BIT. The second way of a tribunal holding India in its breach of a BIT can be through "treaty shopping" i.e. using a broad MFN provision to import investor guarantees from others BITs.

India argued that Article 4(2) of the India-Australia BIT did not incorporate Article 4(5) of the India–Kuwait BIT[29], for two main reasons; first, to do so would *fundamentally subvert the carefully negotiated balance* of the BIT; second, it would be contrary to the emphasis that India and Australia placed on the application of national laws to investments. The tribunal disagreed with India's contentions and upheld White's contention, the ratio being that a MFN agreement was supposed to achieve precisely what White sought.

It was held that Article 4(5) of the India-Kuwait treaty could be imported since Article 4(5) was not contrary to the present BIT. Article 31 of Vienna convention on treaties necessitates a good faith interpretation of treaties.[30] The Tribunal, in the present case, that the claimant is relying on a "more favorable provision" present in another treaty which was held to be permissible in *CME* v. *Czech Republic*.[31] However, the pre-requisite to this is the existence of a provision to the same or lesser effect.

The *Maffezini*[32] decision and the case of *Siemens AG* v. *The Argentine Republic*[33] allowed for an import of a "third party" treaty since the other was broader. However, this distinguishing factor as was seen in the case of *Plama Consortium* v. *Bulgaria*[34] wherein, the tribunal held that "the intention to incorporate dispute settlement provision must be clearly and unambiguously expressed" (Para. 225). The self-adaptation of an MFN provision has the effect of the investor being able to pick and choose from various BITs entered into with various permutations of dispute settlement which would result in a chaotic

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[29] *Supra* note 1, at 1, at para. 11.2.2 – 11.2.4 (India Asserts that Article 4(5) of the India-Kuwait-BIT ought not to be incorporated into the BIT as to do so would (in the words of Mclachlan, Shore and Weiniger) 'have the effect of fundamentally subverting the carefully negotiated balance of the BIT in question').

[30] VCLT art.31 (1969) (A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.).

[31] CME Czech Republic v. Czech Republic (March 14, 2003) *available at:* http://italaw.com/documents/CME- 2001PartialAward.pdf.

[32] Maffezini v. Spain, ICSID Case No. ARB/97/7, Decision on Objections to Jurisdiction, (Jan. 25, 2000).

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

[34] Plama Consortium v. Bulgaria, ICSID Case No. ARB/03/24, , Decision on Jurisdiction, (Feb. 8 2005).

situation.

Therefore, it is permissible to import provisions of other treaties, though only when less favorable provisions to the same or lesser effect is present in the disputed treaty. The India- Australia BIT does not contain such a dispute settlement provision which is the pre-requisite for the import of a different and a more favorable dispute settlement provision, that is, the India- Kuwait treaty. None of these cases were considered by the tribunal, though granted they were before the ICSID, however, the principle in question was similar to the present case. Thus, in the absence of such a provision, the import of Article 4(5) of the India-Kuwait treaty is not justified completely and the obligation of India did not extend to providing dispute resolution under India-Australia BIT. But the Tribunal allowed White Industries to 'treaty shop' and White Industries imported Article 4(5) from the India- Kuwait treaty by the principle of MFN as provided to all WTO member States.

The 'effective standard' was subsequently developed from *Chevron-Texaco* v. *Ecuador*[35] The 'effective means standard' found in Article II(7) of the United States–Ecuador BIT[36] in *Chevron* was similar to that of the India–Australia BIT. The tribunal, after discussing the extensively the meaning and application of the 'effective means standard', found it apt to be considered in the current case. It then applied the test in two avenues- enforcement proceedings and setting-aside proceedings. Regarding the delay as a whole in the enforcement proceedings, though the tribunal agreed it was 'less than ideal', it held White had not successfully shown that India had failed to provide effective means for it to enforce its rights under the award. Regarding the setting-aside proceedings, the tribunal held that although it did not constitute denial of justice, it amounted to India breaching the BIT by failing to provide White with 'effective means' of asserting claims and enforcing rights.

Although one agrees with the Tribunal's final decision in the matter of "effective means", one disagrees with the components of the test as enumerated by the Tribunal. Clause (f) of the *Cheveron case* providing the "effective means" test states '*the issue of whether or not "effective means" have been provided by the host State is to be measured against an objective, international standard*'. Such a take on what constitutes "effective means" is deeply problematic and simply highlights why many scholars are skeptical about international commercial arbitration being a

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[35] Chevron Corporation and Texaco Petroleum Company v. Ecuador, UNCITRAL, PCA Case No. 2009-23 *available at:* http://www.italaw.com/sites/default/files/case-documents/ita0154.pdf.

[36] *Available at:* http://www.state.gov/documents/organization/43558.pdf (Each Party shall provide effective means of asserting claims and enforcing rights with respect to investment, investment agreements, and investment authorizations)

fair method of adjudication. Certain observations were recorded in an empirical study by the International Institute for Sustainable Development when it studied various judgements, and found as stated by Gus Van Harten:-

> *"Two significant tendencies were observed. First, there was a strong tendency towards expansive resolutions of contested issues of law that enhanced the compensatory promise of the system for claimants and, in turn, the risk of liability for respondent States. The second was an accentuated tendency toward expansive resolutions where the claimant was from a Western capital-exporting State."*[37]

Furthermore, a BIT usually involves a treaty between a capital intensive country and a developing country. In the latter, institutional mechanisms are at a nascent stage. If *"effective means"* includes "*an objective, international standard",* the conundrum lies in finding the international standard. How can an international standard be found objectively when most BITs effectively deal with two countries at the polar opposite position of economic development? It is implicit that adopting such a standard will most probably put one country (the developing one) at a disadvantageous position.

Thus, the *White Industries Tribunal* held that the delay by the judicial system of 9 years, amounted to breach of the *'effective means'* standard and for such reasons, the Indian government was liable.

In India's case, the Tribunal's decision has been seen by many as opening up floodgates of litigation alleging breach of multiplicity of BITs. But such a scenario seems far-fetched for various reasons. First, failure to provide "effective means of asserting claims" has to be proven by either of the two ways- MFN or the BIT itself. Secondly, an "investment" has to be shown to exist under the BIT and there is no formal doctrine even after the present case. Lastly, there can be no enforcement of such a standard on the grounds of legitimate expectations as the Indian courts are plagued with constant and continuous delays.

V. CONCLUSION

Therefore, the Republic of India can be held responsible for the acts of its organs including its Judiciary. However, there is a requirement of wrongful act for the applicability of this standard. Thus, there is a necessary requirement of existence of conduct of State which induced the delay to hold the Republic of India responsible and allow the claim for damages, but although it may have

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[37] Gus Van Harten, *Pro-investor or pro-State bias in investment-treaty arbitration? Forthcoming study gives cause for concern, available at:* http://www.iisd.org/itn/2012/04/13/pro-investor-or-pro-State-bias-in-investment-treaty-arbitration- forthcoming-study-gives-cause-for-concern/

been absent explicitly under the constitution and executive actions in the present case, the State as a whole has to be considered for act and obligations of an international treaty.

In conclusion, one holds that the arbitral award is not in contravention of any internal law or the treaties in play. But one is deeply unsettled as far as the components of the "effective means" are concerned, particularly the one discussed above. Given the geo-political and economic power matrix, "international" is often seen as synonymous with "western". This will put the poor countries in a BIT at a disadvantageous position in international commercial arbitrations.

Given that India has been held to breach a BIT, the clarion calls for faster adjudicatory mechanism to be finally acted upon. The call for a faster adjudication mechanism certainly came from an unusual source- an UNCITRAL tribunal. But, the irony here is that White industries has to battle the snail paced Indian judiciary to enforce the second award, the same ground on which it was awarded as it is under UNCITRAL rules, but this decision can lead to future claims, caused due to the overburdened judiciary as one being prepared by the Russian conglomerate Sistema JSFC.

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