

INTERNATIONAL INVESTMENT ARBITRATION: A PRIMER

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ESSENTIAL ELEMENTS

- **International Law**
- **Arbitration**
- **Investment**

ESSENTIAL ELEMENTS – INTERNATIONAL LAW

- Vienna Convention on Law of Treaties (**VCLT**)
- Articles on Responsibility of States for International Wrongful Acts (**ARSIWA**)
- Convention on the Settlement of Investment Disputes between States and Nationals of other States (**ICSID Convention**)
- **ICJ** Jurisprudence
- **Investment Treaty** Cases

ESSENTIAL ELEMENTS – ARBITRATION

- Arbitration is the process used by **agreement** of the parties to **resolve disputes**.
- In arbitration, disputes are resolved with **binding effect**, by a person or persons acting in a **judicial manner** in **private**, rather than by a national court of law that would have jurisdiction but for the agreement of the parties to exclude it.
- The decision of an arbitral tribunal is usually called an **award**

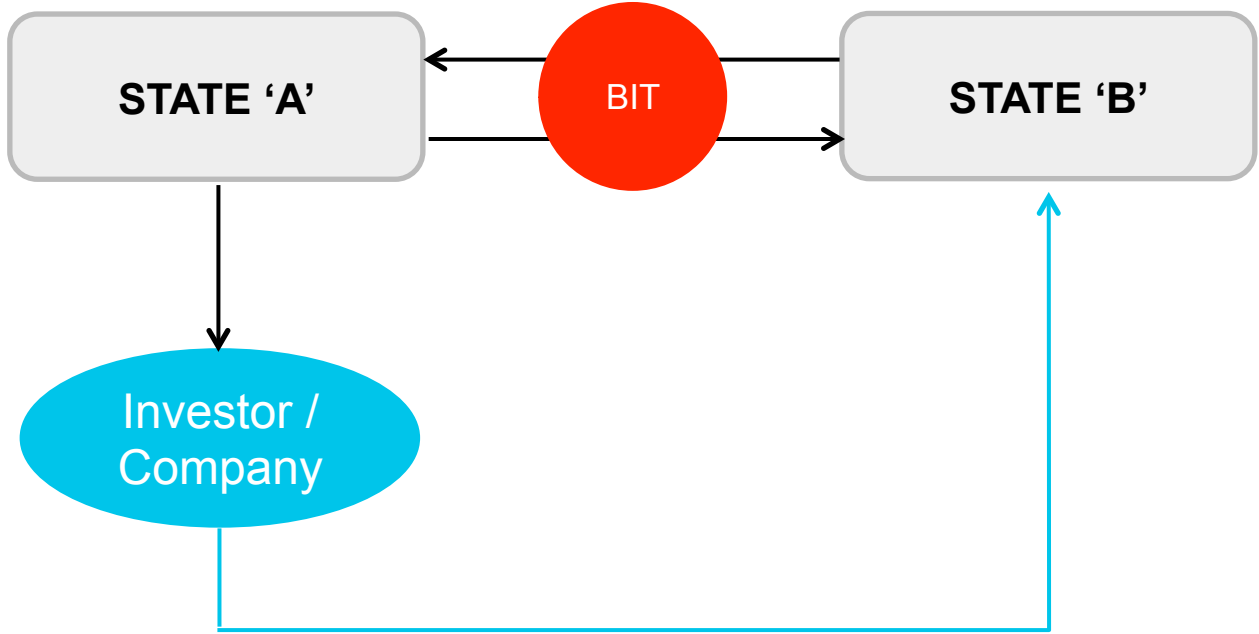
Source: Halsbury's Laws of England, 5th Edition, Book 2, "Arbitration"

INVESTOR-STATE DISPUTE SETTLEMENT (ISDS) BASICS

– HISTORICAL ORIGINS

- Nationality based Claims and Diplomatic Protection
 - Friendship, Commerce and Navigation (**FCN**) Treaties of the United States
 - **1948 Havana Charter** – International Trade Organisation
 - **1959 Abs-Shawcross Draft Convention** on Investments Abroad
 - **1967 OECD Draft Convention** on the Protection of Foreign Property
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ISDS BASICS – EXAMPLE OF INV. TREATY



ISDS BASICS – CONSENT

- State parties upon signing a BIT, **consent** to settlement of Investment disputes by Arbitration
- Such an agreement is a **standing offer** to arbitrate
- The agreement to arbitrate is complete upon an **investor submitting a claim** to the appropriate forum

ISDS BASICS – INVESTMENT TREATIES

- More than **3000+ *Investment Treaties*** in force; India is party to 72 such agreements
- Bilateral Investment Treaties (**BITs**)
- Free Trade Agreements (**FTAs**)
- Energy Charter Treaty (**ECT**)

Source: UNCTAD; Ministry of Finance, India

ISDS BASICS – OBJECT & PURPOSE

- To provide foreign investors with ***substantive protection*** against any ***adverse governmental action***
- To afford a foreign investor a ***direct route to enforce treaty rights*** against a Sovereign State
- To provide a ***neutral forum*** to resolve disputes by way of arbitration

ISDS BASICS – STAGES

Investment Treaty Arbitration proceedings are broadly divided into two stages:

- **Jurisdiction & Admissibility**
 - *Ratione Materiae*
 - *Ratione Personae*
 - *Ratione Voluntatis*
 - *Ratione Temporis*

- **Merits & Liabilities**
 - *Breach of Substantive Protection Standards*
 - *Damages*



JURISDICTIONAL STAGE

ISDS BASICS – JURISDICTIONAL CLAUSES

- **‘Fork in the Road’**
 - *Investors usually have a choice between seeking a local remedy or an international arbitration*
 - *Once a choice is made, the other options become redundant*

- **‘Sunset’**
 - *Applicability of a treaty beyond its termination*

ISDS BASICS – JURISDICTIONAL CLAUSES

‘Fork in the Road’

If any dispute between an investor of one Contracting Party and the other Contracting Party cannot be thus settled within a period of six months from the written notification of a claim, the investor shall be entitled to submit the case, at his choice, for settlement to:

- (a) a court of competent jurisdiction or an administrative tribunal of the Contracting Party which is the party to the dispute, or
 - (b) the International Centre for Settlement of Investment Disputes (ICSID) having regard to the applicable provisions of the Convention on the Settlement of Investment Disputes between States and Nationals of other States opened for signature at Washington D.C. on 18 March 1965, or
 - (c) the London Court of International Arbitration for arbitration under its Rules.
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ISDS BASICS – JURISDICTIONAL CLAUSES

‘Sunset’

“In respect of investments made prior to the termination of this Agreement, the provisions of this Agreement shall continue to be effective for a period of ten years from the date of its termination”

ISDS BASICS – CONSENT & DURATION

Entry into Force, Duration and Termination

1. This Agreement shall enter into force on the date of the last written notification through diplomatic channels of the fulfillment by the Contracting Parties of all the necessary internal procedures for bringing this Agreement into force.
 2. This Agreement shall remain in force for a period of ten years. Thereafter, it shall remain in force until the expiration of a twelve month period from the date either Contracting Party notifies the other in writing of its intention to terminate the Agreement.
 3. In respect of investments made prior to the termination of this Agreement, the provisions of this Agreement shall continue to be effective for a period of ten years from the date of its termination.
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ESSENTIAL ELEMENTS – INVESTMENT

For a dispute to be settled by **Investment Treaty Arbitration**, there needs to be a valid:

- **Investment**
- **Investor**

ISDS BASICS – INVESTMENT

- ***Bilateral Investment Treaties*** typically provide for a definition of the terms ‘Investment’ and ‘Investor’
- ***ICSID Convention*** does not define the term ‘Investment’
- ***Energy Charter Treaty*** defines the term ‘Investment’ in two stages [***Art. 1(5) & (6)***]

INVESTMENT – ICSID CONVENTION

‘Salini Test’ and other developments

- ***Certain duration***
- ***Element of risk***
- ***Significant contribution*** to the development of Host State
 - *Beneficial to public interest*
 - *Transfer of Know-how*
- In Accordance with ***Host-State laws***
- ***Bonafide***

Source: *Salini Construtorri S.p.A and Italtrade S.p.A vs. Kingdom of Morocco*, 2001;
Phoenix Action Ltd. vs. Czech Republic, 2009

ISDS BASICS – SCOPE OF ‘INVESTMENT’

- **Shares, stocks, debentures** and other forms of interest in a Company
- **Tangible property including property rights** such as mortgages, liens, pledges etc.
- **Intellectual Property Rights** (Trademarks, Copyrights, Patents, Industrial Design etc)
- **Contractual rights**
- **Rights conferred by law:** Licenses and Permits

ISDS BASICS – QUALIFIED ‘INVESTOR’

- ***Citizen / National*** of a Contracting State to a treaty
- ***Company / Legal Entity*** incorporated in a State that is a Contracting Party to a treaty
- ***Subsidiary companies/entities*** registered/structured in a State that is a Contracting Party to a treaty



SUBSTANTIVE PROTECTION STANDARDS

ISDS BASICS – SUBSTANTIVE STANDARDS

- Fair and Equitable Treatment (**FET**)
- Full Protection and Security (**FPS**)
- Protection against *Expropriation*
- Most Favoured Nation Treatment (**MFN**)
- Other Guarantees (*‘Umbrella Clause’*)

ISDS BASICS – FET STANDARD

Fair and Equitable Treatment protection standard encompasses:

- Doctrine of ***Legitimate Expectations***
- Non-arbitrariness
- Non-discriminatory
- Transparency
- Due Process

Exception

- Doctrine of ***Necessity***
 - Essential Security Interests
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ISDS BASICS – FPS STANDARD

Full protection and security protection standard deals with:

- State's commitment to protect 'investments' against harmful/unlawful acts
- Obligation of '***reasonable care***' and not '***strict liability***' (*AAPL vs. Srilanka*, 1990)
- May extend to ***beyond physical*** security (*Vivendi II Award*, 2007)
- Inter-linked with the FET standard

Duty of Investor

- *Due diligence* (*Lauder vs. Czech Republic*, 2001)
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ISDS BASICS – NON DISCRIMINATION

- Treatment no less than a national of a Contracting Party (National Treatment)
- Treatment no less than investors/nationals of a third State (***MFN Treatment***)
- ***Effect of discrimination*** is the key criteria while ***intention*** to discriminate is not relevant
- ***‘Effective means’*** provision effected through MFN Clause (*White Industries Australia vs. Republic of India, 2001*)

ISDS BASICS – EXPROPRIATION

- Expropriations may be *lawful* or *unlawful*
- *Lawful expropriation*
 - Public Purpose
 - Non-discriminatory
 - Due process of law
 - Fair Market Value Compensation
- Only *unlawful expropriations* are compensable in ISDS

ISDS BASICS – EXPROPRIATION

- ***Types of Expropriation***

- Direct
- Indirect
- Creeping

- ***Examples***

- Seizure of property
- Nationalisation
- Arbitrary termination/withdrawal of license, contract, concessions, permits etc.
- Regulatory taking

ISDS BASICS – UMBRELLA CLAUSE

- **Example**

“Each Contracting Party shall observe any other obligation it may have with regard to a specific investment of an investor of the other Contracting Party”

- States may not use their **Sovereign Authority** to **undo** their commitments or obligations
- **Contractual obligations** of a State may be **elevated** to a treaty claim



DAMAGES

ISDS BASICS – PRINCIPLES OF DAMAGES

- ***Causal link*** vs. ***Remoteness of Damages***
- Appropriate ***Discount Rate*** for risk assessment and computation of Compensatory Damages
- ***Book Value valuation*** for Companies that have limited operating history

Source: Thomas Walde and Borzu Sabahi, The Oxford Handbook of International Investment Law: Chapter 26, *Compensation, Damages and Valuation*

ISDS BASICS – PRINCIPLES OF DAMAGES

- ***International Investment Agreements*** are not insurance policies against business judgement. Investors are duty bound to:
 - Conduct full assessment of risks
 - Provide effective management
- ***Damages*** caused by investors' folly are ***not compensable***

Source: *Maffezini vs. Spain*, 2000

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