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Issue Editorial

INTERNATIONAL INVESTMENT LAW – QUESTIONS RIDDLING AN ANSWER

MANU SANAN*

Investment in markets beyond territorial confines has steadily grown to become an outstanding feature of economic integration. Notwithstanding the putative objectives, which are governed by political and economic factors, its documented effects remain diverse and far reaching. Apart from optimizing the economic curves associated with global consumer oriented commerce, cross border investment is increasingly perceived as a direct correlative of development. With over $1.5 trillion in investment flows which cross borders under the regulatory umbrella of an estimated 2000 bilateral agreements and an approximate 300 regional agreements, the logistics of the field are a telling statistic.[1]

However, the sunny economics of global investment being settled in principle, it is its complex legal framework which often finds shadow. Despite massive academic attention, which in part may serve to complicate, large tracts of global investment law remain indeterminate yet. Troublesome knots in the field may also be ascribed to the singular characteristics of investment law, which presents a vastly engaging but taut interface between private corporations and states. Also, with deeper roots than trade and a greater degree of permanence, the gravity of contextual issues are usually amplified under investment law *vis-à-vis* other legal interactions necessitated by globalization. Consistent conflict surrounding environmental issues, labour standards and the liability of multinational corporations is exemplar of the deep running influence of investment in a host State. Also, investment obligations usually entail a receding

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[1] M. Sornarajah, *The Fair and Equitable Standard of Treatment: Whose Fairness? Whose Equity? in* FEDERICO ORTINO *et al.*, INVESTMENT TREATY LAW (2007)

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sphere of sovereign exercise, a cost which developing countries often realize in painful retrospect. With such polar extremity in economic and legal analysis, cross border investments epitomize development and consumer benefit at their best while serving as euphemism for degenerative neo-colonialism at the nadir.

Additionally, the rich growth of academic contour in International Investment Law draws upon an arrayed jurisprudence of arbitral tribunals, compensation commissions, claims tribunals, World Trade Organization (WTO) as well as increasingly that of the International Court of Justice. It is little surprise then that the vast breadth of International Investment Law and its dynamics remain speckled with legal conflict, vacuum and challenge. Apart from these, disconcertingly, the procedural legitimacy of investor-State arbitration under Public International Law also merits questioning scrutiny. Its fundamentals mired in question, a few of which are discussed below, the answers, both economic and legal, provided by international investment are far from absolute.

As an incisive Gus Van Harten articulates in the present issue, amongst the prevalent interpretations of international investment, its construction as an assault on sovereignty is extremely challenging in international law. With multinational corporations possessing economic resources exceeding those of sovereigns at times, the steady erosion of state independence under economic compulsion engenders the most vexing aspect of international investment. In particular, as elucidated by Prof. Van Harten, this malady affects developing nations, which wield lesser bargaining power when attempting to attract investment. The response of the Argentinean government in the wake of the peso crisis and the massive liability under investment obligations as a consequence is a typical example of potential intrusion into state sovereignty.[2]

Further charting specific points of invasive ingress would require considering typically manifest vectors like the fluctuating content of the standard of treatment to be accorded as well as expansive constructions of indirect or regulatory expropriations.

An exceedingly common manifest of the standard of treatment under bilateral investment treaties (BITs) is the Fair and Equitable Clause. Depending upon its interpretation, the fair and equitable standard of treatment (FET) has the potential to reach further into the traditional *domaine reserve* of the host state than any one of the other rules of the bilateral arrangements as its applicability is sweepingly effects based. Further, its breadth is extremely potent as the content

[2] *See* CMS Gas Transmission Co. v. Argentine Republic (ICSID Case No. ARB/01/8) (July 17, 2003)

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of the customary standard yet remains formative.[3] Compounding its deleterious potential is the fact that a limited deference to state actions as espoused by the European Court of Justice (ECJ) and the European Court of Human Rights (ECHR) based on the "margin of appreciation" stands rejected as a rule of international law. Unchecked, the gamut of FET has steadily grown to include, inter alia, candour, consistency in state action, maintaining legitimate expectations, substantive and procedural access to justice and proportionality in action with the grip of FET clauses encompassing all facets of state action under international law. Potent intrusions stemming from these are those which extend into the judicial acts of a state which have been traditionally accorded a degree of deference as an essential sovereign function.[4]

Additionally, the above reading of the FET may be broadened in a variety of ways, the first is by a prescription of a standard beyond the customary FET standard, which is a complex affair as both the content of the customary standard as well as its status of a custom is in itself a matter of contest. The second, with a comprehensive analysis to be further found by Stephan Schill in the present issue, is by the operation of the most-favoured-nation (MFN) clause which often forms a conduit for expanded application of rights conforming to obligations undertaken by the state under treaties different from the BIT. Often, this reading is augmented by controversial *umbrella clauses* which assure stability in the host State – an excellent study of which is to be found in this issue by Mihir Naniwadekar.

That a bilateral arrangement is incapable of evidencing customary law is a settled principle in Public International law. However, the burgeoning number of BITs and their contribution to international custom is a moot point in the opinion of many. Significantly, the *Diallo* case, currently before the ICJ provides ample opportunity for acknowledging the customary minimum standard of treatment as equivalent to the customary FET standard, thus capable of settling many a loose end.[5]

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[3] Stephen Schewebel, *The United States 2004 Model Bilateral Investment Treaty: an Exercise in the Regressive Development of International Law in* REFLECTIONS ON INTERNATIONAL LAW, COMMERCE AND DISPUTE RESOLUTION, LIBER AMERICORUM IN HONOUR OF ROBERT BRINER, (G. Aksen *et al.,* eds., Paris, 2005) 815; International Law Commission, *Draft Articles on Diplomatic Protection with Commentaries,* U.N. GAOR, 61st sess., Supp No 10, U.N. Doc A/61/10 (2006)

[4] The Lowen Group Inc. and Raymond L. Loewen v. United States of America, ICSID Case No. ARB (AF)/98/3 (June 26, 2003)

[5] Ahmadou Sadio Diallo (Guinea v. Dem. Rep. Congo) (May 24, 2007) *available at* http://www.icj-cij.org/docket/files/103/13856.pdf (last visited Jan. 8, 2010) (hereinafter *Diallo*); Saluka Investments BV (The Netherlands) v. The Czech Republic, UNCITRAL,

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The second mode of ingress into State sovereignty is by affixing liability on the State for expropriation which is often limits the regulatory ambit of the host state. This is due to the fact that expropriation includes not only deliberate and acknowledged takings but also covert or incidental interference with the property which reduces the economic benefit expected from the enterprise. Illustrative cases under various forums have predominantly agreed in principle that an expropriation may assume varied forms and that its determination must be either effects based or purpose based. Thus where an irrevocable and theologically driven neutralization of property hinders a reasonably expected economic benefit, the measure may amount to an expropriation.

While some view the definition of expropriation as entangled in the divergence in cultural, economic and legal concepts of property furthered by the heterogeneity of state practice, others have consistently expounded *proportionality* as a conclusive test to determine expropriation. Thus, even in the absence of intent, a substantial deprivation of interests in the property have qualified as expropriation as endorsed by various judicial forums. Though proportionality does in effect represent economic reality, underlying political and traditional notions serve to complicate a determination of *when* and at *what point* does an act ascribable to the host state amount to an expropriation.

The current conflict largely centers around the character of the government action as a central affair in justifying an expropriation on the basis of the purpose test. A measure taken to serve a "public purpose" or a more amorphously defined "public welfare" in legitimate exercise of police powers thus excepts the host state liability for expropriation. Non-discriminatory due process requirements also find a mention in most treaties as constituents of the exception. The character of state regulation has thus assumed much importance under the operation of these exceptions.

With foreign investment obligations shackling regulatory independence, investment obligations share a manifest interface with national administrations which are being pressured by globalization. The interface however remains an amorphous sphere in the wake of BIT proliferation. Focal emphasis has gradually shifted to the procedural rights guaranteed under various domestic administrations evidenced, *inter alia*, by Article 230 of the EC Treaty which guarantees procedural sanctity.[6] Further analysis of various domestic

¶ 292-3 (Mar. 17, 2006) available at: http://www.pca-cpa.org/showpage.asp?pag_id=1149 (last visited May 8, 2010)

[6] Art. 230, Treaty establishing the European Community [1996] O.J. C 100/1; Appellate Body Report, *United States-Import Prohibition of Certain Shrimp and Shrimp Products*, WT/DS58/AB/R (Oct. 12, 1998).

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administrations reveals a growing trend towards transparency, requirements of reasoning and the problem of delayed justice. So far, states seem to have grudgingly accepted the standard rules, interpretation and application of investment treaties, in a way that is leading towards the creation of an emerging body of international rules of administrative law.

However, the common requirements of global administration, converging from various jurisdictions in various legal forms, are yet to gain sufficient traction to identify as a referent for the international minimum standard, which would provide a conclusive touchstone in international law to test domestic actions.

Correspondingly, an emerging body of "Global Administrative Law" seeks to regulate global institutional structures which are each confronted with demands for transparency, consultation, participation, reasoned decisions and review mechanisms to promote accountability. Significantly, the "legitimacy crisis" in investment arbitration remains fertile ground for the enunciation and development of Global Administrative Law. Investment arbitration possessing massive economic implications for States, a definitive Global Administrative Law may answer its disconcerting legitimacy deficit in the coming future.

Despite the numerous interfaces as above, determining the actual reach of international investment law and the strength of its influence may be attempted using two parameters. The first would be how fragile a connection between the investment and the host state can be potentially covered. This indicates the strength of economic bond an investment agreement is capable of protecting, a threshold beyond which it would find circumstantial application. The second would be the standard of the obligations invoked by the agreement to be provided to the investment and the investor covered therein.

Gauging these parameters is largely a BIT specific exercise, which depends on the language of various BITs and at their zenith an investment agreement may seek to protect pre-investment expenditures providing them a standard far beyond the customary minimum. A BIT may also specify that an investor is entitled to protection independent of an investment having arisen.

However, a generalization of these standards is dependent on an emergence of a uniform custom in international law which in the case of bilateral agreements is a disputed affair. Would the sheer volume of the number of these agreements indicate the emergence of a custom as argued by Prof. F.A Mann or is the difference in language and content across the BIT's, as put forth by Prof. Sornarajah, an insurmountable obstacle to the creation of a custom.

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The latter view is fortified by the interesting observation of Prof. Sornarajah that an estimated 800 BITs remain unratified of the much touted figure of 2500. This is also seminal evidence of a lack of *opinio juris* as some countries have chosen not to commit to such binding relations. Also, because most BITs exist between capital importing and capital exporting States, it may be said that capital importing States enter into obligations because of pressing economic needs rather than a sense of legal obligation. In both cases, the proposition of a discernible custom arising from the massive growth of BIT's, becomes untenable.

Thus a generalization of the reach of investment obligations across the world cannot possibly be gleaned from bilateral language specific investment arrangements. However, multilateral investment arrangements such as the Energy Charter Treaty, North American Free Trade Agreement and limited investment related obligations under the WTO framework would serve well to flesh out any emergent custom in the field of international investment by virtue of a greater and a more universally applicable subscription.

Investment measures under the WTO are provided for under the General Agreement on Trade in Services (GATS) and the Agreement on Trade Related Investment Measures (TRIMS). The TRIMS Agreement remains related to investment measures which affect trade in goods only and is therefore of limited application.[7] Even within this limited sphere, the TRIMS Agreement only requires conformity with national treatment and quantitative restriction requirements as expounded under the GATT. This limited sphere of operation of the TRIMS has led many to advocate GATS as a more effective instrument governing investments under the WTO, which in practical measure provides for investment as a mode of service. However, with commitments under the GATS being country specific, it reflects yet again the vicious grip of a bilateral arrangement deleterious to the formation of generalized principles governing international investment.

The farthest reach of the agreement is probably in its market access commitments, which if undertaken, lead to binding obligations unless explicitly desisted from. Importantly, these commitments encompass to a fair degree the pre investment conditions such as a deregulation of economic measures to create propitious conditions for foreign investments which is a measure beyond national treatment requirements. In contrast, the Energy Charter Treaty only mandates national treatment as regards the making of investments, its pre investment obligations being soft, non-binding and not open to unilateral challenge.[8]

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[7] Art. 2(2), Annex., General Agreement on Trade in Services, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, annex 1B, 1869 U.N.T.S. 183

[8] Art.10(2),10(4),(27) Energy Charter Treaty, Dec. 1994, 34 I.L.M. 360 (1995)

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The inability of multilateral agreements as well as BITs to provide a source of custom in international law leaves only the declarations of the ICJ as a definite source of determining the universal content of investment law. The ICJ has had six occasions, including two pending decisions, to expound International Investment Law. While the first two occasions, in 1952 and 1957, were dismissed for a lack of jurisdiction, the *Barcelona Traction* case[9] in 1970 has become a lodestar in International Investment Law. Dealing exhaustively with the constituents of corporate nationality while demarcating the ambit of diplomatic protection, the principal ratio of the case upholding incorporation as the primary test of nationality, holds yet against much academic opinion and differing state practice. The *ELSI* case[10] in 1989, though an investment dispute under a friendship, commerce and navigation (FCN) treaty is known for allowing flexibility in the rigidity set in by the *Barcelona Traction* judgment by acknowledging *lex specialis* relations under the FCN.

Also, as further explored by Dolores Bentolila in the present issue, the *Diallo* case, presently before the ICJ holds much promise as an opportunity to put forth a concrete and contemporary exposition of the current status of International Investment Law as well as the International Law Commission's Draft Articles on Diplomatic Protection.[11] In specific, the right of shareholders to diplomatic protection under international law, a right much circumscribed by *Barcelona Traction* has been upheld by the *Diallo* preliminary judgment[12]. What is awaited is the content of the rights of a shareholder in customary international law, a violation of which would entitle the shareholder to diplomatic protection. Though the ICJ has fulfilled a commendable role, its declarations are not coeval with the economic reality governing investments globally and the progress of custom in international investment is yet to be addressed. Current legal development thus fails to conclude decisively upon almost all facets of international investment law.

Notwithstanding the above, to fully comprehend the chaotic and leviathan proportion investor state dispute resolution has assumed, it is necessary to consider the trends governing the recent spurt in investor state dispute resolution. The first trend meriting notice is the expansive standing recognized for minority shareholders and indirect investors far removed from the actual investment by several rungs of corporate ownership. Fostering this is an ever-expanding

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[9] Case concerning the Barcelona Traction, Light and Power Company (Belgium v Spain) [1970] I.C.J. REP. 44.

[10] *Elettronica Sicula S.P.A. (ELSI)*, Judgment, [1989] I.C.J. REP. 15.

[11] International Law Commission, Draft Articles on Diplomatic Protection with Commentaries, U.N. GAOR, 61st sess, Supp No 10, U.N. Doc A/61/10 (2006)

[12] *Diallo, supra* note 5.

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definition of investment under competing BIT's which often cover intellectual property, FDI as well as portfolio investments under the definition. An attempt to rein these expansive trends, at least under the ICSID, could be the application of stringent limitations under jurisdictional requirements as argued by Omar E. García-Bolívar in his note. The second phenomenon is a broadening universe of protection by the operation of the MFN clauses which enable investors to choose from a wide array of clauses across all BITs applicable to the State.[13]

Compounding the problems posed by these skewed legal developments are the telling logistics of investor state arbitration which hit the developing countries hardest. Consider theis: the largest known pending investment claim is for a staggering amount of $28.3 billion; 93% of ICSID claims are against middle and low income developing countries; 29% of all ICSID claims are against natural resources; in over seven instances the investor's revenue exceeded the GDP of the country being sued.[14] Argentina, a nation faced with more than 30 suits as a consequence of the emergency currency stabilizing measures taken in 2002 is classic example of the havoc investment obligations may wreck on the sovereignty of a state.[15]

Trenchant criticism of the ICSID is usually founded upon the fact that it has given corporations both an international identity equal to States as well as a forum to challenge State authority thus unleashing an economic onslaught upon the countries, which often find their natural resources and consequently their sovereignty at stake. Also, the institutional legitimacy of the World Bank and the International Monetary Fund, which virtually control global economics and finance, has often been the subject of informed assault based on their internal governance. Thus, unbecomingly, at the root of the global investment superstructure private commercial interests potentially trump public welfare. This is manifest by egregious examples of legitimate state autonomy being suppressed by investment obligations.[16]

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[13] Gas Natural SDG, S.A. v. The Argentine Republic, (ICSID, Decision on Jurisdiction) (Case No. ARB/03/10) (June 17, 2005); Maffezini v. Spain ICSID Case No. ARB/97/7 Decision on Jurisdiction (2000)

[14] Sarah Anderson & Sara Grusky, Corporate Investor Rule (April, 2007)

[15] Siemens AG v. Argentina, ICSID Case No. ARB/02/8 (Feb. 2007)

[16] Piero Foresti, Laura de Carli and others v. Republic of South Africa (ICSID Case No. ARB(AF)/07/1); Occidental Exploration and Production Co. v. Republic of Ecuador London Ct. of Int'l Arb. Case No. UN 3467 (July 1, 2004); RSM Production Corporation v. Grenada *ICSID Case* No. ARB/05/14 (March 13, 2009); Azurix Corp. v. Argentine Republic ICSID Case No. ARB/01/12 (Dec. 8, 2003)

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As seen above, with multinational corporations having been exalted to the level of states for the purpose of addressing commercial concerns, what remains unsettling is an absence of a mechanism to affix liability upon multinational corporations. Arguably, corporations functioning under the host State are to be governed by the laws of the host State. However, this loses relevance if the host States' regulatory structure is itself subject to review. Uncomfortably, sets of guidelines for multinationals and transnational corporations provide extremely feeble, if any, legal ground to affix liability on coercive investor conduct.[17]

An impossibly possible avenue, which could be considered, is that of holding home States responsible for the coercive acts of corporations abroad as a corollary of diplomatic protection extended to wronged transnational corporations in foreign territory. This would then level the balance of positive rights upon both capital importing as well as capital exporting States as both would be mindful of the balance sought under an investment promotion arrangement.

Building further, economic duress and coercion by multinational corporations against foreign states could then be ascribed to the state of nationality of the corporation. This could be a possible solution to an evident imbalance in investor-state relations in international law, barring *lex specialis* arrangements to the contrary between the parties. This line of thought, however, finds little endorsement if any, possibly because of politically unreal overtones.

As evident, International Investment Law must mature rapidly to incorporate essential contemporary requirements of economic reality and legitimacy if it is to stand scrutiny of general international law. Its popularity is not a measure of its acceptance and its global influence – social, political and economic is a force to be reckoned with. Its empirical nature pillared in an indispensible need for growth and development, it is disheartening to find massive jurisprudence upon the topic failing to provide conclusions which are universally acceptable. In its current state, therefore, International Investment Law remains riddled with more questions than it can answer.

This being, in personal perception, a broad sketch of contemporary landscape of International Investment Law, I leave topical analysis to run its own course under the present Special Issue. As an Editor, it gives me immense pleasure to present a rich array of incisive and thought provoking literature. Additionally, the present issue also marks the maiden anniversary of *Trade, Law and Development*, which is a proud moment for the dedicated editorial team whose sustained efforts

[17] UNGA, Code of conduct on transnational corporations, U.N. Doc. A/RES/45/186 (21 Dec. 1990).

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have been consistent and laudable. I also thank the Contributors, Advisors and Subscribers to *Trade, Law and Development* for having been a source of steady encouragement and inspiration. The following pages beckoning with a stellar legal analysis of International Investment Law, I must leave the reader, without further ado, to contemplate the enriching content independently.

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