

LCIA News

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Newsletter

Tylney Hall September 2001

This is the second year in which the LCIA has run two 'Tylney Halls'. The autumn Tylney Hall symposium was the first presided over by Gerold Herrmann, as President of the LCIA Court.

As in 2000, the second symposium of the year proved as great a success as the spring event. Around 80 delegates attended, having submitted the usual wide-ranging and highly topical questions for discussion.

We were particularly pleased to welcome many first-time attendees, as well as a good number of 'old hands', a combination which produced lively discussion and debate throughout the working sessions. Among the delegates was Robert Briner, Gerold's counterpart at the ICC; his attendance confirming, if any confirmation were needed, the continuing spirit of friendship and co-operation between the two institutions.

Our special thanks go to the Chairs of the working sessions, upon whom we rely so heavily to stimulate debate from the floor. These were Gerold Herrmann, Chris Newmark (Baker & McKenzie, London), Dushyant Dave (New Delhi), Yves Derains (Derains & Associés, Paris), David St John Sutton (20 Essex Street, London), Jean Timsit (Conflict Resolution Centre, Paris), Paul Hannon (London), Carla Potok (Potok International Law, London), Caroline Bell (Denton

Wilde Sapte, London), Matthieu de Boissésou (Darrois Villey Maillot Brochier, Paris), David Lindsey (Clifford Chance Rogers & Wells, New York) and Simon Morgan (Simmons & Simmons, London).

We were especially pleased to have with us so many overseas delegates, and particularly a number from the US, who elected to participate, despite the security concerns affecting us all since the horror of the terrorist attack in New York on 11 September. A special mention in this regard for Lucy Reed of Freshfields Bruckhaus Deringer, who travelled from New York, not only to participate in the conference, but also to make a most witty and incisive address at the working lunch on the Saturday, on the subject of 'communications'.

Alan Redfern gave the speech after dinner on Saturday, amusing and enlightening us on the theme 'The qualities of an arbitrator'.

In its inimitable style, the symposium combined the best of topical debate and good-humoured socialising among friends. Pictures taken at the symposium follow.

We shall run two Tylney Halls again next year. The first will be on 10 to 12 May, immediately preceding ICCA's flagship conference in London, at which the LCIA will co-sponsor the welcoming reception. The second will be over the weekend of 27 to 29 September ■ *Adrian Winstanley*

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ARBITRATING COMPENSATION FOR EXPROPRIATION

Investment Promotion and Protection Agreements as the New Frontier

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Louise Barrington

What do a disgruntled US waste management company, a nearly bankrupted Toronto funeral services enterprise and an expropriated Singaporean brewer all have in common?

Each is the claimant in a new breed of civil action created by international treaty and providing for private arbitration of disputes between foreign investors and the host sovereign nations who have allegedly 'done them wrong'.

First it was the BITs¹. Then ASEAN,² NAFTA³, the Energy Charter Treaty⁴, the Colonia Protocol in MERCOSUR⁵, and Lome⁶, to name but a few. Each of these treaties provides for the resolution of commercial claims by private Davids against government Goliaths in the private and neutral forum of international commercial arbitration – usually ICSID or UNCITRAL – but coming soon to an Asian forum near you.

The first Bilateral Investment Treaties (BITs) were signed in Europe in 1959;⁷ in the following two decades many South American countries signed BITs with Germany, France and Switzerland. The BITs exist to promote foreign investment. Signatory governments usually guarantee to investors non-discriminatory treatment, due process and freely convertible repatriation of capital, while abolishing obstacles such as performance guarantees and technology transfer obligations.

Far-reaching economic reforms of the 1980s and 1990s brought trade liberalization into fashion and increased enthusiasm for investment cooperation. New investment regimes were geared to promote foreign investment through the granting of national treatment and the elimination of most restrictions on capital and profit remittances.⁸ The 1990s brought an explosive growth in the number of foreign direct investment treaties, contributing to the phenomenon we know today as globalisation. From the early 1990s, emerging economies – initially the former socialist countries and later the Asians and Africans – have realized the power of IPPAs to lure foreign capital. Hundreds, even thousands of BITs and multilateral treaties are in force today.⁹

The initial steps were often tentative and ambiguous,

with limited application and doubtful interpretation, but NAFTA and the Energy Charter Treaty are both explicit in terms and vast in scope.¹⁰ ASEAN's terms are no less generous to the foreign direct investor. Under both NAFTA and the ECT, as well as many of the modern IPPAs, the 'dramatic extension of arbitral jurisdiction in the international realm'¹¹ has provided private complainants with the right to direct recourse against host states, through international commercial arbitration.

The vast scope of the investment treaty network has some surprising legal and political implications, as sovereign states see immunity shrinking, and arbitration becomes the norm for dispute resolution, whether expressly chosen in the contract or not.

1. Scope

The thousands of BITs in existence today were drafted over the course of the last four decades of the twentieth century, by negotiators of varying political and economic stripe and unequal negotiating power. Any one state will have difficulty imposing its own preferred version on all its trading partners, so each state will doubtless have a variety of different agreements in its portfolio.¹² To the BITs have been added in the last fifteen years, a number of multilateral treaties, by which the signatory states undertake to accord to foreign investments equal treatment with domestic investments and the status of MFN ('most favoured nation').

2. Why NAFTA and the other 'modern' treaties are different

All BITs offer protection against confiscation, that is, expropriation of property without adequate compensation to the owner. One novelty however, is the expanded definition of property contained in the newer treaties. In NAFTA¹³ and other modern investment promotion treaties, an 'investment' encompasses not only land (for example, to build a roadway over private property), but also the commercial value of assets, and

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'interests arising from the commitment of capital or other resources, ' and perhaps even the expectation of future profits. Additionally, the expropriation need not now be a physical taking; it may include laws, policies or administrative measures having a 'similar effect' to expropriation. These features have produced a new, expanded definition of expropriation:

'Any national or sub-national government regulations (laws, treaties, administrative measures, policies) which reduce or limit the value of the private commercial property can be considered a form of regulatory expropriation.'¹⁴

The other novel feature of NAFTA and other modern multilateral accords and BITs, is their departure from the traditional mode of international dispute settlement between governments. Until recently, a private corporation had no status to bring an action under a treaty between sovereign states. An investor wishing to complain of treatment received in a foreign state first had to persuade its own government to bring proceedings, usually in the International Court of Justice at the Hague. Provided the government decided a case was important enough to intervene, most preferred to use diplomatic channels rather than the sledgehammer approach of international legal action against another sovereign nation. Thus the procedure was slow and often ineffective for providing redress. NAFTA, the new BITs, and ASEAN's Malaysia Agreement all contain a provision entitling private investors to commence arbitration proceedings *directly* against the host nation, without having to rely on inter-government action.

Those familiar with arbitration lore are well aware that the jurisdiction of the arbitral tribunal originates in the agreement of the parties to choose the private resolution of their disputes instead of litigation in a state court. Under NAFTA¹⁵, ASEAN and the others, the signatory nation consents in advance to arbitration with respect to its obligations under the treaty. The aggrieved investor can thus initiate arbitration proceedings complaining that a host state which is party to the accord has breached one of its treaty obligations, *without first obtaining a submission specific to the contract under which the claim is being made*.¹⁶

The combined effect of the broadened definitions of 'assets' and of 'expropriation', and the new status of the individual investor to force a sovereign state into neutral-venue arbitration, may be much greater than what was intended by the signatories.

3. The Investor-to-state claim

Thus it happened that in August of 2000, the global business community saw the first¹⁷ ruling in a new breed of cases: the investor-to-state claim in arbitration, founded not on a traditional arbitration clause, but on an inter-state treaty.¹⁸

Metalclad, an American company that had partially cleaned up a toxic waste site in San Luis Potosi, Mexico, was then refused permission to re-open the site

for toxic waste disposal, after a local government study suggested that the waste would contaminate the local water supply. The governor declared the state an ecological zone. Metalclad claimed that these actions constituted an expropriation under the expanded definition, and in the ensuing arbitration obtained an award for US\$16.7 million plus interest.

Although the arbitration proceedings physically took place in Washington, DC, the legal site of the arbitration was in British Columbia, Canada, a neutral venue. The Mexican government asked the British Columbia Supreme Court to review the case on the basis that the arbitration tribunal lacked jurisdiction to decide the issues involved. The British Columbia Supreme Court, in a controversial decision in May 2001, upheld most of the award.¹⁹

An earlier case, between US chemical producer Ethyl Corp and the Canadian government, was settled when Canada withdrew pending environmental legislation banning MMT, Ethyl's product, and agreed to pay Ethyl US\$13 million. Other arbitrations, involving all three of the government parties to NAFTA, are currently in progress. In one case, a Canadian company is seeking US\$970 million from the US government in compensation for damages it alleges were caused by Californian environmental legislation. Loewen Corp, the Toronto-based funeral service mentioned above, is demanding compensation from the US government as a result of a US\$500 million Mississippi jury verdict in a contract dispute valued at US\$980,000.

As ICSID Deputy Secretary General Antonio Parra notes, 'The creation of this vast network of treaties ... has had a dramatic impact on the caseload of ICSID ... Three-quarters of the new cases have been brought ... by investors relying for the consent of the host State on the dispute-settlement provisions of one of its investment treaties.' Of 36 cases, 28 had a BIT as its underlying treaty, while the other eight were founded on NAFTA.²⁰

4. The Asian Angle ...

Hong Kong currently has thirteen Investment Promotion and Protection Agreements in force,²¹ and almost every other Asian country has at least a few. The first reported arbitration awards have concerned cases under NAFTA, but there are hundreds of other investment treaties with similar provisions. ASEAN countries signed an investment promotion and protection accord at Manila on 15 December 1987. Article I defines 'investment' as

'every kind of asset and in particular shall include, though, not exclusively:

- (a) movable and immovable property and any other proper rights such as mortgages, liens, and pledges;
- (b) shares, stocks and debentures of companies or interests in the property of such companies;
- (c) claims to money or to any performance under

contract having a financial value;
(d) intellectual property rights and goodwill;
(e) business concessions conferred by law or under contract, including concessions to search for, cultivate, extract or exploit natural resources.⁷²²

Under the Manila Agreement, investments of nationals of other ASEAN states

'... shall not be subject to expropriation, nationalization or any measure equivalent thereto ... except for public use, or public purpose, or in the public interest, and under due process of law and on a non-discriminatory basis and upon payment of adequate compensation ...'

The apparently broad exceptions do not detract from this open-ended definition, which puts the onus on the host state to justify its actions, once the claimant can prove its investment has been taken.²³

An aggrieved investor from another ASEAN state has status to bring arbitration proceedings under Article X of the Manila Agreement, and in fact can choose between ICSID, UNCITRAL rules, the Kuala Lumpur Regional Centre, or 'any other regional centre for arbitration in ASEAN.'²⁴

The Singaporean investor, allegedly was forced at gunpoint from its property in Myanmar²⁵, has reputedly instituted a claim under the Manila Agreement for breach of the host government's obligation to prevent an unlawful taking and to avoid discriminatory treatment of foreign investors.

When arbitration awards do come out, we are certain to see court challenges in a number of states, and judicial attitudes may well affect the final outcomes of individual cases. However, even in these early days, it is safe to say that the IPPAs – both bilateral and multilateral – are going to give disgruntled investors a great deal of scope for seeking compensation. Host governments may also feel political repercussions, if they are obliged to consider the cost of the 'taking' before they decide whether to implement it. According to one commentator, 'NAFTA has caused serious structural damage to the traditional state-based system of international legal standing and legal personality for non-state actors.'²⁶

One thing is certain even now: the scope for this new breed of claim is enormous. What we are seeing now are the initial sparks from what may turn out to be a volcano ■

Notes

- 1 Bilateral Investment Treaties.
- 2 Association of South East Asian Nations, established 8 August 1967 by the ASEAN Declaration: Brunei, Cambodia, Indonesia, Malaysia, Philippines, Singapore, Thailand and Vietnam. Laos and Myanmar joined in 1997.
- 3 North American Free Trade Association, 17 December 1992, in force since 1 January 1994
- 4 Signed on 17 December 1994 by the European Community (as it then was) and 49 other states
- 5 Signed 17 January 1994 among MERCOSUR countries: Brazil, Argentina, Uruguay, Paraguay and two associates, Chile and Bolivia.
- 6 A series of four successive conventions regulating trade between the European Union and the ACP (African Caribbean and Pacific) States.
- 7 Germany/Pakistan, signed 25 Nov. 1959, in force since 1962; Dominican Republic/Germany, signed Dec. 16, in force since 1960. See Stevens and de Alwis, *References on Bilateral Investment Treaties*, in ICSID Review v.7 #1, Spring 1992 at p. 229.
- 8 SICE, Investment Treaties in the Western Hemisphere: A Compendium, on the SICE website: www.sice.oas.org/cp_bits/english/bit_inte.asp
- 9 Approximately 1100 in 1997. See Parra, *Provisions on the Settlement of Investment Disputes...* ICSID Review, v.12, no. 1, Spring 1997 at p. 287.
- 10 See Paulsson, *Arbitration Without Privity*, in ICSID Review, v.10 no.1, Spring 1995, p 232 at p 233.
- 11 Ibid, p 233
- 12 That being said, the 13 BITs to which Hong Kong is currently party bear remarkable similarities in form and content. All were signed in a 6-year period between 1993 and 1999.
- 13 Article 1139, NAFTA
- 14 Greenfield, *The NAFTA ruling on Metalclad vs. Mexico*, September, 2000, at home.wtal.de/bl/ck/nafta01.htm

- 15 NAFTA Chapter 11B, Article 1122, which also provides that this consent is sufficient to satisfy the requirements of the New York, ICSID and Panama Conventions. See Alvarez, *Arbitration Under the North American Free Trade Agreement*, *Arbitration International*, v. 16, no.4, 2000 at p. 393
- 16 *ibid*, Articles 1116 and 1117. Under NAFTA, the private party initiating the arbitration must consent in writing and waive its right to administrative or judicial remedies.
- 17 Because of the confidential nature of most arbitrations, there may have been other unreported awards under BITs which have not come to the attention of the international legal community.
- 18 *Metalclad vs. Mexico*, an international tribunal chaired by S. Ely Lauterpacht, QC, awarded Metalclad US\$16.8 million on 25 August 2000.
- 19 See Todd Weiler interview, *Questions Remain...* in *Mexican Forecast*, v. X, no. 9, May 15, 2001
- 20 Parra, *Applicable Substantive Law in ICSID Arbitrations Initiated Under Investment Treaties*, ICSID Website: www.worldbank.org/icsid/news/n-17-2-5.htm
- 21 With Australia, Austria, Denmark, France, Germany, Italy, Japan, Korea, Netherlands, New Zealand, Sweden, Switzerland and the U.K. (Source: Hong Kong government website: www.justice.gov.hk/bil/.htm. Bangladesh has 12; China 71; India 11; Japan 4; Laos 10; Malaysia 42; Nepal 3; Pakistan 14; Papua New Guinea 5; Philippines 13; Singapore 13; Sri Lanka 19; Thailand 17; Vietnam 25. Not all may be currently in force. (Source: ICSID website: www.worldbank.org/icsid/treaties)
- 22 Source: ASEAN website: www.ascansec.org/economic/agrfin87.htm
- 23 *ibid*, Article VI
- 24 *ibid*, Article X
- 25 Myanmar joined ASEAN on 23 July 1997, acceding to the Manila Agreement (and others) by the Subang Jaya Protocol at article 9.
- 26 Lazar, *NAFTA Dispute Resolution: Secret Corporate Weapon?* In *Journal of Global Financial Markets*, vol. 1 no. 3, Winter 2000'

The views expressed in this article are those of Louise Barrington and are not expressed on behalf of the LCIA.