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I. GLOBALIZING INVESTMENT DISPUTE SETTLEMENT

Emerging approaches in a global context.

Whoever drafted the text of the first bilateral investment treaty could not have imagined how popular his or her work would become. It has been copied by the thousands and found its way into not less than 2000 treaties today in force, in addition to it being reflected in various multilateral treaties dealing also wholly or in part with investments. It has been interpreted and reinterpreted by numerous international tribunals and some domestic courts.

Along this process, which is not long in time, a number of issues have been clarified, either in terms of the development of new approaches or understandings or of the placing of limits to some inevitable exaggerations that happen occasionally. The aggregate of developments have meant that the settlement of disputes relating to foreign investments has become truly global in the past decade, both in the meaning of substantive law and in respect of important jurisdictional questions. It is also opening the way for new developments concerning other important international activities, such as trade. It might well happen that in the long term these unfolding arrangements will also apply to a variety of aspects that today appear exclusively related to domestic law and jurisdictions.

This lecture purports to examine the main issues characterizing this evolution, with particular reference to those decisions of ICSID tribunals that have to a significant extent influenced a change in perspective, not only in respect of the extent of bilateral investments treaties and related instruments but also of the very meaning of international law in some aspects. In spite of critical perceptions, that are not entirely wrong in some matters, the end result of such a process has helped

thus far to reach a balance between the right of host States to undertake regulatory functions in the public interest and the right of foreign investors to carry on their business without arbitrary or unlawful interference.

The expression of consent and the avoidance of abuse.

On a number of occasions the State Party to the ICSID Convention that is brought to court by an investor raises the question that it has not expressly consented to the submission of that particular dispute to arbitration. In that point of view, commitment to arbitration under a bilateral investment treaty requires a specific "compromis" in which both parties will agree to that submission and its modalities. True enough, this was the traditional modality of inter-State arbitration in the early part of the twentieth century. States agreed to the arbitration of disputes under a treaty, but this was regarded only as a "pactum de contraherendo", the implementation of which required an additional and specific "compromis".

This is, however, the question that has fundamentally changed in the context of the settlement of investment disputes. Interestingly enough this is not the result of the ICSID Convention that only requires the parties to consent in writing to the submission of the dispute to the Centre. It is rather the result of the network of bilateral investment treaties that have provided for the overall expression of consent by States parties in respect of disputes that might arise with foreign investors. This same result can be obtained by a general offer of submission to ICSID arbitration in domestic law.

As these investors are not a party to the treaty but are the beneficiaries of rights bestowed directly upon them under international law, or under domestic law, their own expression of consent might come later in time or under separate instruments. This happens typically when consent by the investor is given in a direct agreement with the State concerned or simply by resorting to such a choice in writing, or even by instituting proceedings in the Centre.

ICSID tribunals have had no difficulty in finding that the offer by the State to submit to arbitration, followed by acceptance, is a definite binding legal obligation without further steps needed to establish jurisdiction. This incidentally is not just the result of the operation of the bilateral investment treaty in respect of ICSID but also in so far other choices are available to the investor, particularly arbitration under UNCITRAL rules.

But also ICSID tribunals have controlled exaggeration in this matter not

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2 This lecture is based in part on a study made by the author for the AFSIC forum on international investments, 2003.
5 ICSID Convention, Article 25.
accepting modalities that are far remote from a proper consent. In Cable TV v. St. Kitts and Nevis, for example, the tribunal ruled that references to an ICSID clause in domestic proceedings did not amount to consent to arbitration. On the other hand, however, tribunals have also been strict in not allowing a State that has expressed its consent to elude its obligations in respect of the foreign investor. So happened in CSOB v. Slovakia, where the Tribunal found that an ICSID clause included in a BIT not yet in force had been embodied by the parties in a direct agreement and upheld jurisdiction on this basis.

In this same case, although the pertinent treaty provided that upon the agreement of both parties the dispute would be submitted to the Centre, it was held that this did not mean, as alleged, that submission had to be made jointly as this would imply the need for an additional agreement to put into practice the consent expressed by the State in the treaty. The "pactum de contrahendo" approach was thus expressly ruled out.

"Arbitration without privity" is here to stay, as evidenced not only by a variety of bilateral investment treaties but also by multilateral arrangements. The NAFTA, in the context of the operation of the ICSID Additional Facility, like the Energy Charter Treaty, contain forms of unconditional consent to ICSID or UNCITRAL arbitration.

A rather disillusioning view has been recently held by a Respondent State in the context of a dispute submitted to ICSID under a bilateral investment treaty. Because there had been diplomatic demarches by the State of the investor's nationality in support of the investor's right to take the dispute to arbitration, the Respondent State made the argument that there was a State to State dispute that had to be settled first through the operation of the ad-hoc arbitration that investment treaties normally provide for disputes between States parties. It should be noted that diplomatic exchanges directed to facilitate the settlement of the dispute are not considered a form of diplomatic protection under Article 27(2) of the Convention.

That argument would have meant that recourse to ICSID arbitration by a private investor and the Centre's jurisdiction would be paralysed until a different arbitration finalizes. As diplomatic exchanges not amounting to diplomatic protection regularly take place when there is an investment dispute, it would be easy for any Respondent State to elude its obligations toward the investor by claiming the existence of an inter-State dispute. This situation would entangle ICSID's jurisdiction for long periods of time to the disadvantage of the investor. Moreover, it is quite evident that the kind of disputes between States parties to


which the inter-State procedures could apply are very different from those affecting the investor's rights under a bilateral treaty, a situation somewhat paralleled by Article 64 of the Convention and its negotiation history. The tribunal was wise to reject the request for staying of the proceedings before ICSID.

Developing practice on global bases

One most noticeable aspect of the globalization of foreign investment dispute settlement is that it is not exclusively related to a relationship between developed and developing countries as was to an extent originally conceived. It is much broader than that. In fact, developing countries have followed among themselves the same approach of bilateral investment treaties and signed such instruments by the hundreds, with no or little modification. And the same is true of multilateral investment treaties made among developing countries, such as the MERCOSUR Protocols or Free Trade Agreements.

There are two other aspects important to note in this process of globalization. The first is that under the ICSID Convention not only an investor can bring a State to court but also a host State can initiate proceedings against an investor provided a written consent has been given, as happens often under direct investment agreements. States has seldom used this alternative and it seems that awareness about its existence is not widespread. There is also of course the possibility of counterclaims in a proceeding initiated by an investor.

The second aspect is still more significant. For many years developed countries appeared to believe that bilateral investment treaties were a one way street allowing for claims against developing host States. Much to the surprise of a few OECD countries, investors from developing countries have recently initiated proceedings against them, thus evidencing that bilateral treaties mean a two-way street. At least one of these claims has been successful. This particular aspect will be discussed in another lecture.

The role of the most-favored nation clause

The expansion of the system, however, does not end there. Ever since the very outset of the protection of foreign traders by means of treaties of commerce and navigation, the most-favored-nation clause had a crucial role to play in terms of the material conditions in which trade was developed. This very trend continued

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11 See, for example, the 1994 Free Trade Agreement between Columbia, Mexico and Venezuela.
unabated under the modern system of protecting the rights of foreign investors. This development, however, will be the subject of a separate lecture too.

**Time matters.**

Time of course plays a most important role in affirming or dismissing jurisdiction in a given case. In Tradex v. Albania, for example, the Tribunal rejected jurisdiction on the basis of an investment treaty that had not yet entered into force. In Holiday Inn v. Morocco, however, the Tribunal faced a more complex situation. At the time of the investment agreement containing the consent to arbitration the pertinent States had not yet ratified the ICSID Convention, but these requirements were satisfied before proceedings were actually instituted. The Tribunal concluded that it was the date when conditions were satisfied that should be deemed to constitute the date of consent and, accordingly, affirmed jurisdiction as the request for arbitration was made after this date.

Also time is of the essence of most bilateral investment treaties in that disputes that can be submitted to arbitration are normally only those that arise after the treaty has entered into force. The investment in most cases might have been made earlier. Given the fact that discussions and disagreements between investors and host States might extend for a long period of time, tribunals occasionally have to decide on the time the dispute arose and whether it is under its jurisdiction. The test was explained in Maffezi, where it was held that disagreements and difference of views might extend for a period of time, even before the entry into force of the treaty, but what matters is the moment in which there is a claim with a legal meaning in respect of rights and obligations of the parties concerning the investment.

This jurisprudential line was, however, interrupted in Lucchetti where an ICSID tribunal, contrary to Maffezi, declined to admit jurisdiction in respect of a dispute concerning measures amounting to expropriation that originated after the treaty was in force, because it believed that an earlier dispute was one and the same in spite that it dealt with a construction permit. This decision of course opens the door for a State to claim that any dispute with an investor before the coming into force of the treaty, even if different, means that there is a continuing dispute excluding jurisdiction.

Available and unused safeguards.

There are a number of safeguards available to the parties of bilateral investment treaties that are not always resorted to and the very existence of which many times appear not to be particularly noted, until it is too late. States, for example, can exclude from investment treaties given classes of disputes. Most treaties, however, include broad expressions of consent. On occasions more limited expressions of consent are made in national legislation or in investment agreements, but then these may not be quite relevant if the dispute arises under the terms of a broadly defined treaty.

A second safeguard concerns the exhaustion of local remedies, a rather basic feature of traditional international claims that found its way into Article 26 of the ICSID Convention. As noted in the Annulment Decision in Amco v. Indonesia, this safeguard must be resorted to in an express manner and certainly before consent is perfected. Also, as noted in Maffezi, other procedural provisions, such as a submission to local courts for a certain period of time, are not equivalent to a requirement to exhaust local remedies.

One additional aspect concerning the expression of consent and safeguards needs to be examined in the light of this evolution. All bilateral investment treaties provide for a period in which amicable settlement must be attempted, most often a six-month period. It also happens that occasionally the investor will not follow this requirement or do so rather casually, and it happens more frequently that the government will ignore all the communications from the investor to this effect. The view has recently arisen that such is just a procedural step and not a jurisdictional requirement, and that what matters is to afford the government an opportunity to engage in such settlement which if not taken might open the way to arbitration even before the period in question has lapsed.

Two aspects appear relevant to find an answer to this question. The first is that, as noted in Tradex v. Albania, when the investor repeatedly requests the government to enter into discussions and this is ignored over a period of time, then on completion of the six-month period the request for arbitration may be introduced and such efforts will be considered enough to satisfy the amicable settlement requirement.

The second aspect is whether ICSID’s Secretary-General could register a request that has not complied with the six-month amicable settlement requirement. The answer to this is that probably it cannot. Then the conclusion is that the issue is not merely procedural but concerns a crucial question of jurisdiction. Just as the investor cannot pretend registration and ultimately jurisdiction if amicable settlement has not been attempted, so too the State cannot object to registration.

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14 Tradex v. Albania, ICSID Decision on Jurisdiction of December 24, 1996.
16 Supra note 12.
18 Amco v. Indonesia, ICSID Annulment Committee, ICSID Reports, Vol. 1, at 536.
and ultimately to jurisdiction if it has not reacted to the pertinent invitations to this effect during the established period of time.

Who is who.

Some of the most difficult issues that ICSID tribunals have had to deal with in examining jurisdiction of the Centre and their own competence concern the question of who may be a party to proceedings before the Centre. This is in part connected with the interpretation of Article 25 of the Convention, but it is also connected with the extent of investment agreements and investment treaties.

A first issue that has given place to growing confusion relates to the status of a constituent division or agency of a State as parties to an ICSID proceeding. Under the Convention, the participation of such division or agency requires the approval of the State or else that the State notifies that no such approval is necessary. Seldom has this been done. But when proceedings are instituted against the State because of acts or omissions of such divisions or agencies then often the argument is made that no approval has been given to the effect of their participation.

However, one thing is the participation of a division or agency in its own right and quite another is the responsibility of the State for the conduct of its organs, whether they are a part of the central government or entirely decentralized, including provinces, municipalities and other entities that exercise public functions. The designation envisaged in the Convention relates to the first aspect only, that is when an investment agreement has been entered into with a given subdivision or agency and then such entity is authorized by the State to participate in an ICSID proceeding in order to make effective the consent of the entity and the investor to submit their disputes to arbitration. It was thus held in Cable Television v. St. Kitts and Nevis that an investment agreement made with a constituent subdivision of that State that included an ICSID clause could not determine the jurisdiction of the Centre as that entity had not been designated by the State in accordance with Article 25.20

But if the dispute arises under a bilateral or multilateral investment treaty to which the State is a party and concerns an investment agreed to with a given subdivision or agency, even if such entity has not been designated to participate in ICSID proceedings, the State is still accountable for responsibility under international law. Article 4 of the Draft Articles on State Responsibility adopted by the International Law Commission, which on this point unequivocally reflects customary international law, is very precise in establishing the responsibility of the State for acts or omissions of its organs.21

This question was discussed and decided in the case of Compagnie Générale des Eaux (or Vivendi) v. Argentina, where the existence of a concession contract with an Argentine province and the fact that that province had not been designated to participate in ICSID proceedings, did not prevent the Centre's jurisdiction under a bilateral investment treaty between Argentina and France whose provisions governed the rights and obligations of the Republic of Argentina and foreign investors in its territory.22

The participation of natural persons as claimants in ICSID cases has not given place to particular difficulties as on this point the applicable rules of international law are generally well established, including the test of effectiveness in case of disputed facts as decided by the International Court of Justice in the Noltebohm case.23

The changing corporate structure.

Very different, however, is the situation concerning juridical persons. The very complexity of corporate structures and investment consortia offers fertile ground for divergent views about who can or cannot claim before ICSID or other arbitration mechanisms.

The private or public nature of the functions of a corporate entity has recently given place to important clarifications. The Convention envisaged allowing for claims by private entities against a State, but not by public entities against another State, although this alternative was not entirely ruled out in the negotiations. In CSONB v. Slovakia the claimant was a State agency of the Czech Republic that initiated proceedings against Slovakia what prompted an objection to jurisdiction on this basis. Interestingly enough, the Tribunal found that jurisdiction could be upheld as that particular entity, although owned by the State, was engaged in banking activities that had been privatized and were essentially commercial by nature.24

The test thus became not government control but the essence of the activities performed. The same test was later applied in Maffezini to establish whether some activities of an agency of the Spanish State were of a public or private nature and hence engaged or not the responsibility of the State.

Agreement of the parties on the question of corporate nationality will of course be most influential on a finding of jurisdiction by a tribunal. So happened, for example, in MiNE v. Guinea where an agreement of the parties establishing that a corporation had Swiss nationality prevailed over the fact that technically the nationality was different.25 Issues relating to the real interest behind the investment

20 Supra note 5.
23 Noltebohm Case (Second Phase), ICSI Reports, 1985.
24 Supra note 6.
and control of a corporation are relevant to this effect.

The ICSID Convention facilitates this more flexible approach. In particular, Article 25(2)(b) refers to the situation of a corporate entity that has the nationality of the Defendant State, but because of foreign control the parties have agreed it should be treated as a national of the other relevant State party, and thus can claim against the Defendant State. It is not unusual that bilateral investment treaties and investment agreements will contain clauses to this effect.

ICSID tribunals have occasionally found that certain arbitration clauses and other provisions might result in an implied agreement to treat a locally incorporated company as a foreign investor, as evidenced in Amco v. Indonesia and Klocek v. Cameroon. It should be noted that this same result can be achieved by means of the definition of investment, which if broad enough, as is usually the case, might not need an agreement on nationality or control.

Questions about who actually controls a corporation have also been discussed by ICSID tribunals. In SOABI v. Senegal, an ICSID tribunal went quite far in searching for the controlling entity of a locally incorporated company. The immediate controller was a Panamanian company, but Panama was not a party to the Convention; beyond that company, Belgian nationals were in control and Belgium was a State party. The tribunal ultimately accepted this last control. In Amco v. Indonesia, however, the tribunal refused to go beyond the control exercised by the immediate parent company of a locally incorporated company.

Whether joint control of a company by foreign investors of different nationality and protected under different bilateral investment treaties qualifies to the effect of admitting jurisdiction, was also raised in the recent parallel ICSID cases of Sempa-Camuzzi. The tribunal held that such control, arising out of a shareholders agreement that was public and approved by the host State, did qualify for protection under the treaty as the investment had been conceived as an integrated operation before the claim arose.

A second related issue that arises in this context is whether a foreign investor is allowed to claim for damages affecting a corporate entity only when such investor has a controlling interest or can do so even if it is a minority shareholder. This difficult question will, however, be examined in a separate lecture.

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49 Amco v. Indonesia, ICSID Decision on Jurisdiction of September 25, 1983.
50 Klocek v. Cameroon, ICSID Award of October 21, 1983.
51 SOABI v. Senegal, ICSID Decision on Jurisdiction, August 1, 1984.
52 supra note 25.

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Treaties and Contracts.

Because of the various forms that an investment venture can today adopt, there has also been a growing distinction between contracts made with the host State and the rights of the investors under the applicable bilateral investment treaty. Many times these are parallel arrangements that occasionally entail different dispute settlement mechanisms. This situation has become characteristic of concession contracts or license agreements made by a foreign investor with the host government while at the same time the investment qualifies for protection under a bilateral investment treaty. Again this issue will be discussed in a separate lecture.

Defining investment.

Many aspects discussed above are closely related to the definition of investment. It is well known that the Convention did not define “investment” as there was no agreement on this point. Many examples of investment were given along the negotiation of the Convention. The precise definition of investment was therefore left to the consent of the parties on jurisdiction, normally embodied in the bilateral investment treaties. This is not to say that these treaties are entirely free to define jurisdiction as the parties may please. The definition has to be compatible with the meaning of the Convention and not go beyond what can be reasonably regarded as investment.

In most cases the dispute will relate to an investment on which there can be no doubt. In a few instances doubt has arisen and the Secretary-General has refused registration because the case is manifestly outside the jurisdiction of the Centre. So too an ICSID tribunal can refuse to accept jurisdiction on this ground. As ICSID jurisprudence develops, a number of cases have clarified whether a particular activity is or not an investment under the relevant treaty. Taxation inconsistent with mining contracts, the development of a timber concession, construction contracts and other activities have been identified as a pertinent investment under the relevant treaties. On the other hand, for example, in Mihaly v. Sri Lanka negotiations on a construction project that had not materialized in a contract were held not to constitute an investment.

A dispute about whether a bank guarantee constitutes investment was decided in Joy Mining v. Egypt, leaving the tribunal decided that this was an ordinary commercial contingent liability and, therefore, it had no jurisdiction.
Two new situations have recently emerged. In Pope & Talbot, Inc. v. Canada, Canada argued that the dispute did not concern investment but trade and hence the tribunal lacked jurisdiction; the tribunal, however, found that the two questions were not "wholly divorced from each other." The tribunal in S. D. Myres, Inc. v. Canada faced similar arguments and decided that the questioned measures concerning goods "can relate to those who are involved in the trade of those goods and who have made investments concerning them." The connection between trade and investment is thus becoming a strong one.

Financial markets not ignored.

The second new development relates to financial instruments. Although not typically an investment of the traditional kind, financial instruments have become a crucial source for government financing and heavy investments are made in them worldwide. In Fedax v. Venezuela the tribunal had to deal with promissory notes issued by the government that had circulated internationally and Fedax, a foreign financial institution, had invested in them. The tribunal decided that the promissory notes were a means by which loans and credit benefitting the State had been made available and their purchase qualified as an investment under the investment treaty. Also in CSOB v. Slovakia, the tribunal held that loans in the circumstance of a large banking operation qualified as an investment. In both cases it was held that the resources made available to the State did not need to be physically transferred across borders to qualify as an investment.

Financial developments cannot of course extend indefinitely as a covered dispute and the circumstances will provide clear limits to this end. In a recent case, a Belgian investor who had bought a participation in an international asset fund claimed against Malaysia on the ground that general economic measures adopted by this country had diminished the value of his portfolio. Although this claim was dismissed on jurisdictional grounds, there was little hope for it to succeed on the merits.

Arising directly.

The Convention also requires the dispute to be a legal dispute and to arise directly from the investment. In Amco v. Indonesia, a dispute concerning general tax obligations under domestic law invoked in a counter-claim was held not to qualify as an investment as it did not arise directly from the investment made. Occasionally, however, there is some confusion between a dispute arising directly from an investment and the question of the investment being a direct and not an indirect one. The point was also discussed in Fedax v. Venezuela, where the tribunal held:

However, the text of Article 25 (1) establishes that the "jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment." It is apparent that the term "directly" relates in this Article to the "dispute" and not the "investment." It follows that jurisdiction can exist even in respect of investments that are not direct, so long as the dispute arises directly from such transaction. This interpretation is also consistent with the broad reach that the term "investment" must be given in light of the negotiating history of the Convention.

As noted above, the definition of investment agreed to in treaties is usually very broad and encompasses movable and immovable property, shares and other forms of participation in a company, claims to money and other contracts of financial value, intellectual property, business concessions and other matters. This broad definition is at the very heart of the interpretation of treaties made by ICSID and other tribunals. Although under Article 24(4) of the Convention a Contracting State can notify the Centre of classes of disputes it would or would not consider submitting to the jurisdiction, this is seldom done and in any event such a notification does not constitute consent under the Convention nor does it change any consent given in other instruments.

It might be important for governments and investors to be as precise as possible on the investments they intend to protect as this may avoid many disputes and misunderstandings and might also avoid ancillary claims and counterclaims that further complicate disputes submitted to arbitration.

A uniform approach to substantive treatment.

The definition of investment is not merely a jurisdictional question. It also touches heavily upon the merits of a claim as the action or omission of State organs and agencies will be measured against the type of investment concerned. The substantive treatment embodied in bilateral and other investment treaties is virtually the same. Fair and equitable treatment, national treatment, non-discrimination, most-favored-nation treatment, funds transfers and requirements.
and guarantees concerning expropriation are almost identical throughout the spectrum. It is interesting to note that the discussion on the merits in most cases relates to the balancing of the rights of the State with those of the investor. The protection of property and acquired rights is no longer a fundamental issue in international law. For a long time the right to protection could not be easily reconciled with the supremacy of national sovereignty. Only after difficult confrontations an understanding was reached about the limits of the respective contentions, and conditions were set to diplomatic protection and the right to expropriate, including the right to compensation. International adjudication was instrumental in reaching such understandings.

The success of this approach, together with inescapable economic realities, has been so evident that outright direct expropriation is today rather exceptional and has a number of well set requirements to be accepted as valid under international law. If one examines the list of ICSID and other relevant cases of the past few years will realize that this type of expropriation is quite exceptional.40 Some degree of accommodation has also been taking place in respect of indirect or regulatory expropriation, but this is thus far insufficient, scant and on occasions contradictory. The State holds its right to adopt measures in pursuance of public policies. Investors hold their right to be compensated if such measures amount to a taking. Neither of these views can be questioned in and of themselves. The problem lies in how and where the respective limits and conditions should be established, that is in identifying the point of common interest and reconciliation.

Yet, when we might have thought that the legal framework was rightly evolving in the direction of attaining such a balance, principally under the case law of ICSID, all of a sudden the confrontation flares up again. Is there a NAFTA/BIT treatment or just a minimum customary law standard? Are such standards those of the twenty-first century or still those of the nineteenth century?41

International legal thinking has had great difficulty in focusing on the right approach to the issue of regulatory authority, particularly if it entails indirect expropriations, as opposed to formal expropriation. This again is evidenced by examining the list of ICSID and NAFTA cases where the vast majority concerns such questions as the right of the State to adopt certain types of regulations.

40 Direct Expropriation was involved for example in the case Companhia de Desenvolvimento de Santa Brem S. A. v. Republic of Costa Rica, ICSID Award of February 17, 2000. In other prominent cases only regulatory measures alleged to have amounted to expropriation were involved, as was the case for example in Meridial v. Mexico, 49 International Legal Materials 55 (2001) and Waiz Management Inc. v. Mexico, 49 International Legal Materials 56 (2001).

the distribution of powers within the State and its various provincial or local governments, the effects of those measures and their connection with the treatment embodied in treaties.

Two issues on which this discussion is based must be disposed of at the outset. There can be no doubt about the first such issue, namely the right of the State to adopt regulatory measures in implementation of legislation and other expressions of sovereignty. The second issue is that regulatory authority cannot be validly exercised if it violates the framework of legal rights and obligations in which it operates. This will be subject to scrutiny by constitutional bodies, judicial entities or international mechanisms.

Limits of regulatory powers

The problem lies in establishing the limit of such powers or functions under international law. First, it appears that it is a well-established principle that States may not act in a manner contrary to treaties and contracts, at least those contracts that are under some form of protection of international law itself.42 Second, as noted, it is quite evident that under the principle of attribution States are responsible under international law for acts not only of central government authorities but also of any other public agency exercising regulatory functions of some sort.

In the light of recent ICSID and NAFTA case law, as well as under many other international precedents,43 it has also become evident that most of the problems with regulatory authority entailing some form of expropriation occur not with central government authorities that are conscious of international obligations but with lesser governmental units, local states, municipalities and the like. This has gone so far that in a recent treaty it was necessary to expressly provide for the obligation to adopt measures to ensure the compliance with the treaty provisions by national, provincial and regional authorities and a mechanism of supervision was established to this effect.44

Domestic and international judicial control over administrative decisions of States and its various agencies has helped to pave the way for finding the right balance in this respect. More recently, again in the light of both domestic and international experiences, the doctrine of legitimate expectation appears to be gaining momentum as a standard that has to be respected in terms of citizens' rights, or for that matter investors' rights.

41 Sadigh, ibid., 606-607.
42 Protocol to the Argentina-Chile Treaty on Mitrin Integration and Cooperation, 20 August 1999, Article 5.
In search of legitimate expectation

In Preston, a leading English case, the House of Lords ruled that unfairness amounting to an abuse of power could arise from conduct equivalent to breach of contract or representation.44 Still more directly in the recent case R. v. North and East Devon Health Authority, ex p. Coughlan45 the Court of Appeal in England sought to redress the inequality of power between the citizen and the State.46 In this case it was held that:

Where the Court considers that a lawful promise or practice has induced a legitimate expectation of a benefit which is substantive, not simply procedural, authority now establishes that here too the court will in a proper case decide whether to frustrate the expectation is so unfair that to take a new and different course will amount to an abuse of power. Here, once the legitimacy of the expectation is established, the court will have the task of weighing the requirements of fairness against any overriding interest relied upon for the change of policy.51

The Court, having examined prior cases, then added:

The court’s task in all these cases is not to impede executive activity but to reconcile its continuing need to initiate or respond to change with the legitimate interests or expectations of citizens or strangers who have relied, and have been justified in relying, on a current policy or extant promise.52

The situation is not altogether different under international law. Governments and international organizations may undertake changes of policy in their continuing need to search for the best choices in the discharge of their functions. However, to the extent that policies earlier in force might have created legitimate expectations both of a procedural and substantive nature for citizens, investors, traders or other persons, these may not be abandoned if the result would be so unfair as to amount to an abuse of power. This also assumes the international protection of the rights concerned. Herein lies the limit of discretion and the role of judicial review as a means of redress.

Because this approach is rooted in fairness it would not be unthinkable that from citizens’ rights and foreign investors’ rights it might gradually expand into other areas of concern for the international community, most notably trade, the international civil service and other matters. Global society is approaching, quite rightly, global protection.

II. NEW APPROACHES TO THE MOST-FAVORED-NATION CLAUSE53

Old problems, new look

A rather old legal question has been recently discussed anew in the framework of a jurisdictional decision of an ICSID tribunal. The question is whether the most-favored-nation clause included in most bilateral investment treaties (BITs) can be applied, in addition to the usual substantive business of custom duties, capital transfers and like subjects, to the procedural arrangements embodied in that particular treaty for the settlement of disputes that may arise under it.

In the jurisdictional phase of Maffezi54, an ICSID tribunal was confronted precisely with this question. Under an Argentina–Spain BIT, the investor is required to apply to the local courts for a period of time before resorting to arbitration. Senor Maffezi, an Argentine investor in Spain, did not do this and resorted directly to arbitration under the ICSID Convention.

Counsel for the claimant presented to the tribunal the rather novel argument that the investor was not required to apply to the local courts because in the light of a provision of a Chile–Spain BIT, resort to arbitration could be done directly. As the pertinent treaty had included the usual most-favored-nation clause, it was further argued that this also applied to the provisions on the settlement of disputes. Chilean investors in Spain being treated for more favorably for this purpose, that same treatment ought to extend to Senor Maffezi.

Spain of course opposed these contentions on three principal arguments. First, the treaties made by Spain with third countries were in respect of Argentina res inter alios acta and, consequently, could not be invoked by the claimant. Second, under the principle ejusdem generis the most favored nation clause could only operate in respect of the same matter and could not be extended to matters different from those envisaged in the basic treaty. Hence the reference to “matters” in the most favored nation clause of the Argentina–Spain BIT could only be understood to refer to substantive matters or material aspects of the treatment granted to investors.

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45 R v North and East Devon Health Authority ex p. Coughlan (2003) 3 All ER 450.
47 R v North and East Devon, et al., per 57.
48 R v North and East Devon, et al., per 65.
49 This lecture is based on the presentation made by the author to the Swiss Arbitration Association in Zurich, 2003, on " Bilateral Investment Treaties and the Most Favored Nation Clause: Implications for Arbitrators in the Light of a Recent ICSID Case", in Gabrielle Kaufmann-Kohler and Rainer Stauder (eds.), Investment Treaties and Arbitration, 2002, 139-144.
and not to procedural or jurisdictional questions. And third, since the purpose of the most favored nation clause was to avoid discrimination, such discrimination could only take place in connection with material economic treatment and not with regard to procedural matters.

These same issues were posed directly or indirectly in earlier cases submitted to international tribunals. However, those issues had been addressed partially or not conclusively as some of those cases had been finally decided on different grounds. In particular such questions have been addressed in the Anglo-Iranian Oil Company case (jurisdiction)\(^{36}\), in the case concerning the US Nationals in Morocco\(^{38}\) and in the Ambatiello case (obligation to arbitrate)\(^{37}\), as well as in the proceedings of the Ambatiello case before a Commission of Arbitration\(^{39}\).

**Identifying the basic treaty.**

A first question that needs to be discussed is that of the basic treaty governing the rights of the beneficiary of the clause as it is this treaty that will determine whether the clause can be rightly invoked. This question was discussed in the Anglo-Iranian Oil Company case, where the International Court of Justice determined that the basic treaty upon which the claimant could rely was that "containing the most-favored-nation clause"\(^{37}\). The Court then held that:

It is this treaty which establishes the juridical link between the United Kingdom and a third-party treaty and confers upon that State the rights enjoyed by the third party. A third-party treaty, independent of and isolated from the basic treaty, cannot produce any legal effect as between the United Kingdom and Iran: it is res inter alios acta.\(^{38}\)

It was on this basis that the International Court of Justice ruled against the extension of principles of international law envisaged in treaties between Iran and third parties to the United Kingdom, as these principles were unrelated to the basic treaty containing the clause\(^{39}\).

This discussion had practical consequences for the application of the most favored nation clause in Maffezini. The tribunal was of the opinion that if the subject matter to which the clause applies is indeed established by the basic treaty, it follows that if these matters are more favorably treated in a third-party treaty then, by operation of the clause, that treatment is extended to the beneficiary under the basic treaty. If the third-party treaty refers to a matter not dealt with in the basic treaty, that matter is res inter alios acta in respect of the beneficiary of the clause.

**Dispute settlement and fair and equitable treatment.**

A second major issue concerns the question whether the provisions on dispute settlement contained in a third-party treaty can be considered to be reasonably related to the fair and equitable treatment to which the most favored nation clause applies under basic treaties on friendship, commerce and navigation or on investments. The question that follows is whether those provisions can be regarded as a subject matter covered by the clause. This is the issue directly related to the ejusdem generis rule.

This question was indirectly but not conclusively touched upon in the case concerning the US nationals in Morocco. Here, the International Court of Justice was confronted with the question of whether the clause contained in a treaty of commerce could be understood to cover consular jurisdiction as expressed in a third-party treaty. However, the Court did not need to answer the question posed because its main finding was that the treaties from which the USA purported to derive such jurisdictional rights had ceased to operate between Morocco and the third states involved\(^{40}\).

The same issue came up in the Ambatiello case. Greece contended before the International Court of Justice that her subject - Ambatiello - had not been treated by the English courts according to the standards applied to British subjects and foreigners who enjoyed a most favored nation treatment under treaties in force. The Court did not deal with the matter of the most favored nation clause, except that some interesting views were expressed in a dissenting opinion\(^ {41}\), but this was done by the Commission of Arbitration to which the dispute was ultimately submitted.

The Commission of Arbitration confirmed the relevance of the ejusdem generis rule. It affirmed that "[t]he most-favored-nation clause can only attract matters belonging to the same category of subject as that to which the clause itself relates."\(^ {42}\) However, the scope of the rule was defined in broad terms:

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\(^{36}\) International Court of Justice, Reports, 1952, p. 93.

\(^{37}\) International Court of Justice, Reports, 1952, p. 176.

\(^{38}\) International Court of Justice, Reports, 1953, p. 10. See also generally, International Law Reports, 1953, p. 547.

\(^{39}\) Award of the Commission of Arbitration established for the Ambatiello claim between Greece and the United Kingdom, dated March 5, 1956, United Nations, in Reports of International Arbitral Awards, Vol. XII, 1963, p. 91.

\(^{40}\) International Court of Justice, Reports, 1952, p. 129.

\(^{41}\) Ibid., p. 109.


\(^{43}\) International Court of Justice, Reports, 1973, p. 19.

\(^{44}\) Dissenting opinion by Judges McFarlane, Klabunde, Klass and Beal, judgement cit., supra note 4, at p. 28.
It is true that the 'administration of justice', when viewed in isolation, is a subject-matter other than 'commerce and navigation', but this is not necessarily so when it is viewed in connection with the protection of the rights of traders. Protection of the rights of traders naturally finds a place among the matters dealt with by treaties of commerce and navigation. Therefore it cannot be said that the administration of justice, in so far as it is concerned with the protection of these rights, must necessarily be excluded from the field of application of the most-favored-nation clause, when the latter includes 'all matters relating to commerce and navigation'. The question can only be determined in accordance with the intention of the Contracting Parties as deduced from a reasonable interpretation of the Treaty.\(^{16}\)

The Commission accepted the extension of the clause to questions concerning the administration of justice and found it to be compatible with the ejusdem generis rule. It concluded that the protection of the rights of persons engaged in commerce and navigation by means of dispute settlement provisions embraces the overall treatment of traders covered by the clause. On the merits of the question, the Commission determined, however, that the third-party treaties relied upon by Greece did not provide for any "privileges, favours or immunities" more extensive than those resulting from the basic treaty and that "accordingly the most-favored-nation clause contained in Article X has no bearing on the present dispute (...).\(^{16}\)

**Distinctions in national courts.**

A few significant decisions of national courts have also dealt with the principle, some with reference to jurisdictional and procedural matters. One decision refused to apply the clause because the basic treaty concerned "rights under international law" between France and Germany in commercial matters, while the treaty invoked as the source of rights related to "rights under civil law" for commercial relations between subjects of France and Switzerland\(^ {17}\). Another decision also refused to apply the provisions of a Franco-Swiss treaty dispensing with the requirements to provide for security of costs, because the basic treaty dealt with matters of "general character" in commercial relations between Britain and France\(^ {18}\).

**Bilateral investment treaties emphasis on dispute settlement.**

Can it be said that the arbitration clauses of bilateral investment treaties are so inextricably related to the protection of the rights of traders, or for that matter

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\(^{16}\) Ibid.

\(^{16}\) Ibid., at 109, 110.

investors, so as to be included under the operation of the clause like any other treatment relating to the substance of the protection? Under most BITs, and some multilateral treaties as well, the key of the protection of the investor lies not so much in the substantive provisions of the treatment accorded, which are rather scant and basic, but in the arrangements allowing for the submission of the disputes to arbitration. The conclusion reached by the Commission in the Ambatielos as to the non-exclusion of administration of justice from the operation of the clause is perhaps even more appropriate in the context of BITs.

Some BITs have provided expressly that the most favored nation treatment extends to the provisions on settlement of disputes. This is particularly the case of investment treaties concluded by the United Kingdom. Thus, for example, Art. 3 (3) of the Agreement between the United Kingdom and Albania stipulates: "For the avoidance of doubt it is confirmed that the treatment provided for in paragraphs (1) and (2) above shall apply to the provisions of Articles 1 to 11 of this Agreement."\(^{19}\) Among the enumerated provisions are the clauses on dispute settlement and the consent to submit to conciliation or arbitration under ICSID.

Here it is beyond doubt that the parties intended the most-favored-nation-clause to include dispute settlement in its scope. Furthermore, the parties included this model clause in the Agreement with the express purpose of "the avoidance of doubt".

In most treaties, however, the question is not addressed explicitly. Some refer to the most-favored-nation-clause as applying to "all rights contained in the present Agreement"\(^ {20}\) or, as the basic Argentina-Spain BIT does, to "all matters subject to this Agreement". It follows that it must be established, like the Commission did in the Ambatielos, whether the parties intended to apply the clause to dispute settlement arrangements or if this can be reasonably inferred from the practice followed by the parties in their treatment of foreign investors and their own investors.

If the purpose of the BIT is to provide protection to the investor through recourse to international arbitration, it is not difficult to conclude that such recourse is a "right" covered by the clause. The same holds true of such being a "matter" subject to the agreement.

Prior to ICSID, only one decision appears to have dealt with the most favored nation treatment. In the case Asian Agricultural Products Limited v. Republic of Sri
arbitration was really more favorable to the investor than the recourse to local courts. The drafting history of the ICSID Convention, however, provides ample evidence of the conflicting views of those favoring arbitration and those supporting policies akin to different versions of the Calvo Clause.

On the basis of those considerations the tribunal concluded that:

If a third-party treaty contains provisions for the settlement of disputes that are more favorable to the protection of the investor’s rights and interests than those in the basic treaty, such provisions may be extended to the beneficiary of the most favored nation clause as they are fully compatible with the ejusdem generis principle. Of course, the third-party treaty has to relate to the same subject matter as the basic treaty, be it the protection of foreign investments or the promotion of trade, since the dispute settlement provisions will operate in the context of these matters; otherwise there would be a contravention of that principle.

Developing an integrated network

It is necessary to examine next which are the possible implications of this finding. There are at present over 2000 BITs known to be in force, perhaps some more not known, and a number of multilateral treaties which also regulate investment. All such treaties can be considered as the basic treaty containing the most-favored-nation-clause. It is not difficult to realize then that the operation of the clause will have the effect, among other, of connecting dispute settlement arrangements in a broad international network.

The principle that applies is that any basic treaty containing the clause could attract the provisions of another treaty signed by one of the parties containing elements that are more favorable to the beneficiary, including the provisions on dispute settlement. This effect is hardly surprising in a world characterized by globalization, at any rate for those states that have signed a considerable number of

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54 Ibid., at p. 272.
55 See, for example, Magnuson Moving & Storage Co. v. United States Supreme Court, Decision of November 13, 1991, in U.S. Reports, Vol. 264, p. 33, where it was held that...
operate both ways. The treatment accorded to the foreign investor in the host country also applies to the treatment that its investors are entitled to receive from the other party. However, in spite of this being an elementary rule, capital-exporting countries often believe that the treaties are only to be applied by the other party to the benefit of the investors of the former and are highly surprised when the same provisions are invoked the other way round.

If this perspective is kept in sight, then a government should not require from others a treatment to foreign investors that it is not prepared to give itself. This exercise would certainly avoid situations of discrimination in the treatment of foreign investors and would make less likely the operation of the clause.

**Limits of public policy**

A fourth aspect that qualifies the finding in Maffezini is that relating to the questions of public policy that must also be taken into consideration. The tribunal stated in this respect that “the beneficiary of the clause should not be able to override public policy considerations that the contracting parties might have envisaged as fundamental conditions for their acceptance of the agreement in question, particularly if the beneficiary is a private investor, as will often be the case.” The clause then cannot apply to just any matter or in just any circumstance.

The tribunal gave four examples where a conflict with public policy might arise:

- a) when one party has conditioned the consent to arbitration to the prior exhaustion of local remedies, this requirement should not be bypassed by invoking the clause in respect of an agreement that does not contain this element. The exhaustion of local remedies was considered a fundamental rule of international law allowed for under the ICSID Convention. It can also be an important principle of the state’s own public policy. In the Argentina-Spain BIT, the resort to local courts was not strictly an exhaustion of local remedies, an aspect the tribunal expressly clarified;
- b) if the parties have agreed to a “fork in the road” clause, making the choice between submission to domestic courts or to international arbitration final and irreversible, this cannot be reverted by invoking the clause;
- c) the choice of a particular forum for the arbitration, say ICSID, cannot be changed by invoking the clause in order to refer the dispute to a forum chosen in a different treaty;

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d) when the parties have defined a highly institutionalized and very precise procedural mechanism to conduct arbitration, as it happens under NAFTA and other specialized arrangements, neither this can be altered by invoking the clause in respect of different arrangements in other treaties. Otherwise, the intent of the parties in providing for a particularly organized arrangement would be defeated.

Right and wrong: the limits to observe

Lastly, the tribunal also made an important distinction between what is right and what is wrong in this context, stating:

"[i]t is clear, in any event, that a distinction has to be made between the legitimate extension of rights and benefits by means of the operation of the clause, on the one hand, and disruptive treaty-shopping that would play havoc with the policy objectives of underlying specific treaty provisions, on the other hand." 39

From the above considerations it can be concluded that the clause has a useful role to play in the development of a more uniform and broader system for the settlement of disputes under bilateral investment treaties. But it must also be concluded that this does not mean that it can be used to distort the intent of the parties or the public policies underlying those treaties. Within these limits lie both the benefits and the difficulties that arise from the operation of the clause in this new context.

Maffezini becomes popular, perhaps more than deserved.

Some requests for arbitration brought to ICSID since Maffezini have invoked that decision to justify the invocation of the most-favored-nation clause in the disputes concerned. Some of these are probably most reasonable and comparable to Maffezini, some perhaps not.

In Salini v. Jordan, 40 the operation of the clause was dismissed by the Tribunal on the ground that the Claimant had failed to demonstrate that the parties to the treaty between Italy and Jordan had had the intention to apply the clause to dispute settlement procedures.

Two recent cases, however, have introduced variations in this discussion. In Siemens v. Argentina, the tribunal offered what appears to be a broader interpretation of the pertinent BIT most-favored-nation clause as it held that this was applicable in spite that the treaty did not refer to all matters subject to the Agreement, as in Maffezini, but only to activity in connection with investment.41

In Plama v. Bulgaria, however, the tribunal held a narrower interpretation and dismissed the application of the clause on the view that it did not specifically cover dispute settlement arrangements and the clause could not substitute for the mechanisms chosen by the parties.42 Other recent cases have also dealt with the clause, with particular reference to Técnicas Medioambientales Tecnom. v. Mexico.

In recent diplomatic practice the Maffezini interpretation has been expressly ruled out in the understanding that it cannot refer to dispute settlement arrangements. This has been the case of the United States-Central America Free Trade Agreement, the Free Trade Agreement between the United States and Singapore and the draft Free Trade Agreement of the Americas.43

The fact of the matter, however, is that the operation of the most-favored-nation clause responds to the needs of globalization and the harmonization of the treatment applicable to investors and traders. If it becomes clear that dispute settlement arrangements are a part of the protection accorded to investors, then the clause will be applicable as the issue becomes one of substantive treatment.

III. DEVELOPMENTS IN INTERNATIONAL CORPORATE LAW AND SHAREHOLDER’S RIGHTS.44

An historical obstacle to the operation of State Responsibility.

The most formidable obstacle raised by States to the operation of State Responsibility has not been connected to substantive rules of international law, such as those governing the justification of certain unlawful acts or their excuse, but concerns a question of admissibility of claims, usually dealt with as a procedural matter. This question is the protection of shareholders under international law, first by excluding claims on the basis of lacking a company the nationality of the claiming State and next by preventing the jurisdic of shareholders in their own right.

For years it was taken for granted that the law on the matter had been firmly laid down by the International Court of Justice in the Barcelona Traction Case, 45 where the Court held...

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39 Maffezini, par. 65.
43 On these developments are generally both Teißen's "What's Afraid of Maffezini? Recent Developments in the Interpretation of Most Favored Nation Clauses," Paper prepared for the American Society of International Law, February 2005.
44 This lecture is based in part on an article published by the author in Maurizio Ragazzi International State Responsibility Today, 2005.
It is a basic characteristic of the corporate structure that the company alone, through its directors or management acting in its name, can take action, in respect of matters that are of a corporate character. Notwithstanding the separate corporate personality, a wrong done to the company frequently causes prejudice to its shareholders. But the mere fact that damage is sustained by both company and shareholder does not imply that both are entitled to claim compensation. The situation is different if the act complained of is aimed at the direct rights of the shareholder as such. But a distinction must be drawn between a direct infringement of the shareholder's rights and difficulties or financial losses to which he may be exposed as the result of the situation of the company. Thus, the legal issue is reducible to the question of whether it is legitimate to identify attack on company rights, resulting in damage to shareholders, with the violation of their direct rights.

The Court appears to have oversimplified the question in two respects. First, the Court believed that because international law was generally silent on the matter this had to be interpreted against the rights of the shareholder. A number of historical cases have been cited either in favour of the rights of a shareholder or against such rights, thus evidencing that in the best of cases the matter was not clearly settled. This is why the Court ultimately invoked rules of corporate personality under domestic law to reach its decision.

The second oversimplification is that the real issue was not whether company rights can be identified with the direct rights of shareholders, but was and still is whether a shareholder entitled to some form of international protection can claim in its own right for wrongful acts of the State affecting its economic interest in the company. This means that the issue is that of identifying where the real economic interest lies.

Broadening shareholders' right to claim.

The decision of the International Court of Justice has been occasionally criticized by distinguished writers on the account of having been based on the wrong assumptions. However, the fundamental problem with this decision was that it came at a time when the over powerful State's rights of the past were beginning to change in favour of an open recognition of the rights of individuals under international law.

The legal consequence of this phenomenon was that the scope of State Responsibility was progressively broadened to include the rights of shareholders to the extent that international law is called to govern the matter. The formidable obstacle of the past began to give place to the recognition of new economic realities. In fact, it has been rightly noted that it was the very Barcelona Traction decision that brought about major changes as States and investors reacted against its adverse implications.

This progression is evidenced by a variety of concurring legal directions. The first is found in the realm of domestic corporate law, which gradually is permeating international law. Issues such as the piercing of the corporate veil and, above all, the admission of derivative suits by shareholders and investors' class actions against a variety of defendants who affect the company's rights and the interest of those shareholders, is evidencing that again the issue is that of recognizing the real interest involved and not merely observing a corporate formality. The economic choice of maximizing the shareholders' wealth is the underlying rationale for these developments.

Other developments are found specifically in the realm of international law. The protection of foreign investments under bilateral or multilateral investment treaties is perhaps the most outstanding example of this progression. Other expressions include State practice as evidenced by lump-sum agreements and negotiated settlements, the jurisprudence of international claims tribunals and commissions, notably the Iran-United States Claims Tribunal and the United Nations Compensation Commission, and the very meaning of diplomatic protection in terms of it being conceived at the service of the affected individual and not any longer exclusively at the service of the protecting State. These developments will be examined next.

The fact that international law has taken direct interest in the matter also has another important consequence. It does not any longer appear to be a valid proposition to decide this kind of issues by recourse to the domestic law of a given country or even by reference to principles common to various legal systems, as was done in Barcelona Traction and is often argued by the Defendant State whose

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responsibility is called into operation. It is a matter to be decided principally under international law itself, which now has all the necessary legal tools to do so.

The International Court of Justice was not unaware of the early developments that were beginning to take shape at the time of its decision. In fact, the Court stated:

...In the present state of the law, the protection of shareholders requires that recourse be had to treaty stipulations or special agreements directly concluded between the private investor and the State in which the investment is placed. States even more frequently provide for such protection, in both bilateral and multilateral relations, either by means of special instruments or within the framework of wider economic arrangements. Sometimes companies are themselves vested with a direct right to defend their interests against States through prescribed procedures. 91

Ultimately, it was the absence of any such investment protection treaty between the parties that led the Court to decide the question under general international law. Had a treaty to this effect existed, probably the conclusion would have been different, as in fact happened two decades later in the Eletronica Sicula case involving the provisions of a Treaty of Friendship, Commerce and Navigation between Italy and the United States. 92 In this case the International Court of Justice accepted the protection granted by the State of nationality to shareholders in a foreign company in a claim brought against the State of incorporation.

A massive State practice.

State practice massively points in the direction of extending protection to shareholders in affected companies. British claims against Mexico, as United States claims against Peru and Hungary, relied on a fifty percent interest of their nationals in the total corporate capital. 93 The same percentage is required by the Algiers Declaration on the Settlement of Iran–United States claims for the determination of nationality of companies, while the right to claim is generally related to an interest of nationals enough to control the corporation, not excluding minority shareholders. The United States practice on diplomatic protection has relied on a fifty percent ownership of a corporation by its citizens, like Switzerland has required that a company be mainly owned by its citizens. It should be noted, however, that there is nothing magic in those percentages. The practice shows too that only a twenty percent ownership was required for United States claims against the former Yugoslavia. 94 The Iran–United States Claims Tribunal has adjudicated claims by shareholders with a 25% interest 95 and on one occasion with an interest ranging from 4% to 51%. 96 Evidence of controlling interest has also been evaluated with flexibility. 97 Recent studies on the meaning and extent of lump-sum agreements also evidence a broad variety of approaches and requirements, most of which tend to accommodate the affected interest with increasing flexibility. 98

The practice of the United Nations Compensation Commission is also most relevant to the understanding of current trends. Under its Rules, 99 corporate claims not espoused by the State of incorporation may anyhow be submitted directly by the affected company with an explanation. If agreed, one government may claim on behalf of entities or nationals of another. Shareholders barred because of nationality may in any event claim directly for their losses in an affected corporation. Partnerships are also allowed to claim proportionately to the protected interest if otherwise ineligible to claim on their own. Trusteeship representation is also allowed for. Most importantly, under Resolution 123 (2001) an elaborate system is made available for claims when the real owner cannot appear as a shareholder because of domestic legal restrictions. 100

The work on diplomatic protection of both the International Law Commission 101 and the International Law Association 102 has shown conclusively that the fundamental change underlying these developments is that the right being asserted through international claims is no longer that of the State of nationality but that of the affected individual. This is in essence what explains that the individual has been recognized many times a direct right of action, and even where State intervention is still necessary the claim is being increasingly de-linked from State discretionary espousal, the intervention of political interests and, above all, the right of the State to dispose of the compensation or to introduce damages different from those of the affected individual. Diplomatic protection is thus becoming a residuary mechanism.

All these evolving trends have come together in the law governing the protection

91 Recurso Tratado, para. 95.
94 Orgeon Viscose, at 357.
of foreign investments under a variety of treaty and other arrangements. It is in this context that diplomatic protection has been altogether excluded to the benefit of international arbitration, except in very specific circumstances. To this extent, whatever meaning the Barcelona Traction decision might have had it was only relevant in connection with diplomatic protection as the prevailing mechanism for international claims at the time. Two ICSID tribunals have recently found to this effect, holding that decision not to be controlling.86 Once the international legal system has moved beyond diplomatic protection other relevant principles govern the process of claims.

Shareholders can claim in their own right.

A consistent line of decisions of ICSID, UNCITRAL and NAFTA tribunals has made plain evident that the right of shareholders to claim for their affected interest independently from the corporate entity is now upheld as a matter of law. To this extent, there is no longer an obstacle for making effective State Responsibility by means of a direct right of action by those affected by the wrongful act. The principle is thus no longer that of protecting the State by invoking formal legal structures but of protecting the individual who is the real holder of an economic interest under international law.

The right of action of shareholders to claim separately from the affected corporate entity has been upheld in AALP v. Sri Lanka,87 AMT v. Zaire,88 Antoine Goetz and consorts v. Republic du Burundi,89 Maffrenzi v. Spain,90 Benacor v. Argentina,91 Genin v. Estonia,92 the Aguas de Vivendi Award93 and Annuity94 CME v. Czech Republic,95 CMS v. Argentina,96 Azurix v. Argentina97 and Enron v. Argentina,98 among other cases. This new perspective was well explained by the Tribunal in Goetz v. Burundi:

...the Tribunal observes that the jurisprudence ante quem of the CIRDI does not limit the quality of rights to those persons morally directed vis-à-vis les mesures litigieuses mais l'étend aux actionnaires de ces personnes, qui sont les veritable investisseurs.99

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90 CMS (2003), para. 19.
91 CMS (2003), para. 19.
92 CMS (2003), para. 19.
93 CMS (2003), para. 19.
94 CMS (2003), para. 19.
95 CMS (2003), para. 19.
96 CMS (2003), para. 19.
97 CMS (2003), para. 19.
98 CMS (2003), para. 19.

Minority and non-controlling shareholders

This discussion has been recently taken a step beyond. As on not few occasions States have required foreign investors to set up locally incorporated companies to channel the investment, and not infrequently these companies participate in joint ventures or consortia with other entities, the question has arisen whether the direct right of action extends to minority shareholders of the affected company. A positive answer to this question is not unprecedented in the light of the State practice noted above. However, as with most issues concerning investments, the answer is case specific, as it will depend on the actual wording of the agreement or treaty protecting the rights of the investor.

The question was discussed in the ICSID case CMS v. Argentina, where the claimant owned a 29% of the company affected by the measures complained of.101 The Respondent government was of the view that a shareholder could not claim separately from the affected company and that, in any event, the ICSID precedents mentioned above either dealt with cases concerning majority or controlling shareholders or the dispute was about the expropriation of the shares owned. The Tribunal dismissed the jurisdictional objection raised, partly in the light of the ICSID Convention and the specific rights established in the governing bilateral investment treaty, and partly in the light of international law. In this last respect the Tribunal, after having examined the Barcelona Traction decision and current State practice, held:

The Tribunal therefore finds no bar in current international law to the concept of allowing claims by shareholders independently from those of...
the corporation concerned, not even if those shareholders are minority or non-controlling shareholders.\textsuperscript{118}

The limits of indirect minority participation

Yet a more complex issue arose in Enron v. Argentina, where the claimants had a controlling interest in several locally incorporated companies, which in turn had a 35% minority shareholding in the affected company.\textsuperscript{119} The Respondent government rightly raised the issue that if minority shareholders can claim independently from the affected corporation this could trigger an endless chain of claims, as any shareholder making an investment in a company that in turn invests in another company could invoke a direct right of action for measures indirectly affecting an entity at the very end of the chain.

The Tribunal shared the need to establish a cut-off point beyond which claims should not be permissible as having only a remote connection to the affected company, holding that this cut-off point was determined by the extent of the consent to arbitration of the host State. If such consent covered a given investment it could be concluded that the claim was admissible under the treaty. Otherwise the claim would fall beyond the consent and admissibility as being too remote. In the instant case, the Tribunal found that it had jurisdiction as that specific investor had actually been invited to participate in the investment and required to set up local companies.\textsuperscript{120}

The issue was also discussed, although not actually decided, in the case Gruslin v. Malaysia, concerning a portfolio investment.\textsuperscript{121} Here again, the Respondent government objected to jurisdiction on the ground that no investment had been made in that country and the claim had no connection with the investment treaty. The Tribunal, however, held that it lacked jurisdiction on another ground and needed to decide the question of remote connection. Whether the claimant was the owner of the investment was also argued in the case, as there was a financial company involved in the management of the portfolio; it was pointed out by Counsel that the rights of the claimant in such company were no more than rights of a contractual nature.

The Barcelona Traction view was again argued in the Mondev case,\textsuperscript{122} where the United States was of the position that shareholders cannot claim for injury to a corporation and can do so only for direct injuries suffered in their capacity of shareholders. The Tribunal, however, dismissed those arguments and accepted the claimant's standing. It must also be noted that the United States Supreme Court has held, in the context of the Foreign Sovereign Immunities Act, that if direct ownership of shares is envisaged in legislation this should be understood as referring to the ownership of a majority of shares, but when legislation refers to indirect ownership this signals that minority shareholders might be entitled to certain rights as well.\textsuperscript{123}

As most bilateral investment treaties protect investment in shares and define investments broadly to include direct or indirect ownership or control, it is quite difficult for a tribunal deciding a case under those rules to ignore claims by shareholders in their own right or to exclude claims by minority shareholders. Moreover, as happened in the Mondev case, what the State of nationality of the investor might argue in a given case to which it is a party is not opposable to an investor of that nationality in a separate case to which that investor is a party. As explained by the Tribunal in Enron,

This is precisely the merit of the ICSID Convention in that it overcame the deficiencies of diplomatic protection where the investor was subject to whatever political or legal determination the State of nationality would make in respect of its claim.\textsuperscript{124}

General international law has also changed

In the context of these developments, even if connected to specific treaty provisions, it is hardly conceivable that general international law might still be identified with the Barcelona Traction findings. General international law might not be as detailed as those treaties suggest, but certainly is not indifferent to such trends. As decided by the Tribunal in CMS,\textsuperscript{125}

...the fact is that lex specialis in this respect is so prevalent that it can now be considered the general rule, certainly in respect of foreign investments and international claims and increasingly in respect of other matters. To the extent that customary international law or generally the traditional law of international claims might have followed a different approach - a proposition that is open to debate- then that approach can be considered the exception.\textsuperscript{126}

However dramatic these developments might seem, certainly as compared to the time of over powering State privileges, they are in fact not alien to the meaning

\textsuperscript{118} CMS (2003), para. 48.

\textsuperscript{119} Enron (2004), para. 11.

\textsuperscript{120} Enron (2004), paras. 50-52.

\textsuperscript{121} Philippe Gruslin v. Malaisia, Award, 2001. 3 ICSID Reports, at 483, para. 10.3.15.1.

\textsuperscript{122} Mondev International Limited v. United States of America, Award, 2002, International Centre for Settlement of Investment Disputes, 41 ILM (2003), at 85.

\textsuperscript{123} U.S. Supreme Court, Dole Food Co. v. Patrickson, 123 S.Ct. 1655 (2003).

\textsuperscript{124} Enron (2004), para. 48.
of international law. Since its inception international law has been at the service of the individual. The law of international claims was devised to allow wronged individuals to bring forth their complaints, at first through the intervention of its own State of nationality and later by means of direct right of action. State responsibility was also devised to make States accountable for wrongful acts. The fact that today they have to face direct action by individuals so as to put that responsibility into operation is just one other consequence of the evolution of international law.

It can thus be concluded that to the extent that State responsibility becomes available to the truly affected, as these developments indicate, it will come to perform a true measure of justice in the international community. Procedural safeguards are necessary and justified when they contribute to due process but not when they distort justice. A major historical distortion based on the exclusion of corporate claims or their modalities stands now to be corrected.

IV. CONTRACTS AND TREATIES: ARE THEY STILL DISTINGUISHABLE?

The paradoxes of global change in the law

Not long ago teachers of international law used to explain that treaties are like contracts, only between States. Today it is necessary to explain that contracts are like treaties, only between individuals and the State. Paradoxical as it may seem, these different explanations respond to the changing reality underlying the process of globalization of the law. What used to be a useful comparison between international law and a separate domestic legal framework - treaties and contracts - has now become a part of a single legal structure which encompasses both contracts and treaties as well as a host of other instruments.

This phenomenon is of course noticeable in respect of activities that have become to a greater extent globalized, such as trade and investments, but it also relates both actually and potentially to a number of other matters that are following the same path. Examples of it can be found in Government commitments to the individual creating a legitimate expectation, a question that used to be confined to the realm of domestic law, but that today has gained increasing international recognition and effects. Environmental covenants and other instruments that have substituted private commitment for governmental regulation are also a matter whose effects are felt far beyond the confines of national borders.

This article seeks to explain the process leading to this profound transformation of the law, with particular reference to the internationalization of contracts and the manner how they have begun to interact with treaties. Both private and public international law developments are intertwined in this process to a degree that they become difficult to distinguish. In addition, the influence of lex mercatoria provides for a further enlargement of the governing legal framework. All of it leads in turn to a most meaningful role of international arbitration in consolidating the legal trends emerging from this state of flux.

The internationalization of private contracts.

Internationalization of contracts is not a new phenomenon. In fact, ever since trade crossed over national borders the process of internationalization was present to a greater or lesser extent. It has been appropriately written that "a contract is an international contract when it brings into play the interests of international trade." True enough, international trade and the international sale of goods was the salient feature of this process at a first stage, which was soon followed by the more complex operation of international investments, whether associated to trade or not, and resulting in the global reach of economics and finance that we know today. The overarching effect of international public regulation of international trade in the framework of the GATT, the World Trade Organization and Free Trade Agreements, and the similar effect of the 1965 Convention establishing the International Centre for the Settlement of Investment Disputes and the related network of bilateral and multilateral investment treaties that will be discussed below, are not alien to this process of transformation.

The law, however, has been slower to react to the new needs of a globalized economy. There is still an ongoing legal debate about the definition of an international contract as opposed to a domestic contract and the role of the sources of law in establishing a line of separation. But, as Lagarde has commented, this is a false debate in that the international legal order is the one increasingly governing internal situations by means of a variety of conventions.

The nature of international markets determines that every passing day fewer and fewer transactions can be exclusively considered of a purely internal or domestic nature. The very role of the principle of subsidiarity has changed in this context. At the time when transactions were largely domestic international rules were applied as subsidiary, while today, where transactions are mostly international, it is the national rules that are applied as subsidiary. This is not a small effect in the scope and nature of the law.

18 CMS (2003), para. 98.
19 This lecture is based in part on the article by the author, "Of Contracts and Treaties in the Global Market", 18th
Conventions laying down rules of substantive law soon began to interact with the traditional approaches to private international law, mostly concerned with the identification of jurisdictions and applicable law among competing sovereignties. Conventions on substantive law had of course the advantage of looking at the broader spectrum of international markets and their legal transactions. This is the basis on which these conventions gradually began to prevail over domestic approaches.131 The larger the degree of internationalization of contractual transactions, the greater the choice the parties had to opt for both the competent jurisdiction and the applicable law, particularly when such developments were coupled with the resort to international arbitration.

Although conventions on substantive or material law appeared somewhat late, soon they gained momentum and from one to the other there were noticeable changes, each leading to a larger degree of internationalization. The Hague Conventions of 1964,132 for example, not only required that buyer and seller be established in different countries but also that there should be some additional element of international significance, such as transportation or delivery of the goods beyond the State where offer and acceptance had materialized in a contract. The 1980 Vienna Convention133 did not retain such additional elements and required only that buyer and seller be established in two different countries.134 A number of other conventions followed this simpler approach, thereby evidencing that internationalization was rapidly gaining ground.135

Other developments leading in the same direction have been noted in connection with the UNIDROIT Principles on international commercial contracts,136 the Principles on a European law of contracts137 and the studies on a European Civil Code.138

The most significant contribution to the internationalization of contracts has been that of international arbitral tribunals, which as rightly noted need to settle specific disputes between operators of international trade and are for the most independent from national jurisdictions and State sovereignty.139 Arbitration under the International Chamber of Commerce has built a powerful body of legal approaches to contemporary trade and financial transactions, most of which has in sight the needs of the effective operation of international markets rather that isolated requirements of national legislation.

Both from the point of view of jurisdiction and the substantive law governing

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135 Witz, 653-6.
140 Kahn, 853-4.
142 Witz, 653-8.
legal regime giving rise to transnational law, every possible legal alternative seems to have been explored. 168

Irrespective of the position taken by each author or tribunal, the fact that stands out is that this category of contracts is by definition one where internationalization is still more prominent than that resulting from purely private contracts. Not infrequently this feature is enhanced by the commitment of the State not to alter the contract and to abide by various kinds of stabilization clauses and other legal assurances. In addition, the general safeguards of international law in connection with private rights are always available, particularly in so far unlawful expropriation, denial of justice and other forms of interference by the State will positively engage its international responsibility and the duty to compensate, among other possible remedies.

The end result of this legal development is that even in the case where a contract cannot be considered as such to be governed or subject to international law, and hence it allows for a greater role of a domestic legal system and national sovereignty, some key aspects of such contract will in any event be subject to the operation of international law either because there are specific clauses to this effect or because the general safeguards of international law will be always at hand. The latter will of course operate independently from the contract to the extent that there is an international wrong.

The question that remains is whether this means that State contracts are treaties, at least from the point of view of their legal effects. The question becomes still more pressing when the State has undertaken a commitment to other States, normally by treaty, making of the enforcement of the contract an international legal obligation. The so-called "umbrella clauses" or "traits de couverture", 169 because of the higher degree of submission of the contract to international law, have been on occasions considered to safeguard the sanctity of the contract and to transform any interference with its enforcement into a treaty violation. 170 The specific implications of this type of clauses in recent arbitral decisions concerning foreign investments will be discussed further below.

But one thing is to strengthen the observance of State contracts by building upon the role of international law, directly or indirectly, and quite another to assimilate contracts to treaties. 171 As concluded by Professor Weil in his forward looking course of the Hague Academy of International Law in 1969,

170 "Well, at 124, 130.
172 Well, at 186.
173 Well, at 106.
The globalization of foreign investment law

The third major line of development emerged in connection with the protection of foreign investments. Following the conflictive relationship between those who favoured submission of all disputes to domestic courts under some form or other of "Calvo Clause" and those who would insist in the role of diplomatic protection, and hence of State intervention to protect their investments and other rights, arbitration gradually emerged as the common ground where the interests of all could be satisfied. This was the key turning point of the 1965 Convention establishing the International Centre for the Settlement of Investment Disputes (ICSID).113 No further diplomatic protection, except in unusual situations, no further submission to domestic courts and recourse instead to international arbitration, largely institutionalized under ICSID or UNCTITRAL rules, are the core elements of the new balance stricken between State sovereignty and international developments.114

Although restricted to the field of investments, however largely this may be defined by treaty, national legislation or contract, this particular development covers the most important international transactions of the modern world, which take the form of investments. Developments in the World Trade Organization, albeit different, tend to address the other major source of contemporary economic activity which is that concerned with international trade and related matters.

Over 2000 bilateral investment treaties ensuring the protection of foreign investments are today in existence, together with a host of multilateral conventions and a number of free trade agreements.115 They all share the common feature that in spite of being inter-State agreements, individual private investors can avail themselves of the provisions of such instruments both in terms of the standards of treatment and the choice of forum for the settlement of disputes, including most prominently international arbitration.116

Most investments, however, are done by means of contracts with the State and it is here where the new connection between contracts and treaties has emerged. Not infrequently, contracts provide for the application of domestic law and for the submission of disputes to domestic courts. How can this be reconciled with the parallel existence of a treaty providing some times for a different governing law, ensuring a substantive treatment under international law which is usually different from that under domestic law, and allowing for the submission of disputes to international arbitration if the investor so chooses?

As in the past, two major approaches have emerged as an answer. For the host State, it is quite naturally the contract and the domestic legal framework that have to prevail. For the investor, it is quite naturally the treaty and the international law governance that have to prevail. And quite naturally too, it has been for the arbitral tribunal where the dispute is taken to settle the issue. Because this is normally a jurisdictional issue its discussion in arbitration tribunals has been informed by the determination of the appropriate forum, thereby increasing the link between the conceptual aspects of the matter and the role of international arbitration to a much greater extent than was the case in the past.

The first case that explicitly addressed the matter was Lanco International Inc v. The Argentine Republic.117 In this case the investor chose to take the dispute to ICSID under a bilateral investment treaty in spite that the concession contract executed with Argentina provided for the submission of disputes to local courts. The Tribunal held that consent to arbitration under the treaty prevailed over any other provision to the contrary and that such consent could not be diminished by the submission of a dispute to local courts under the concession contract.118 In this case, like in Salini, it has been held that since parties cannot opt for the jurisdiction of a domestic administrative court, because it entails a kind of mandatory jurisdiction, there can be no triggering of the "fork in the road" mechanism in respect of ICSID arbitration.119

A distinction between different types of claims in connection with the test of triple identity has also been made. To the extent that a dispute might involve the same parties, object and cause of action it might be considered as the same dispute and if it has been submitted by the investor to domestic courts the "fork in the road" mechanism, by which the investor's choice becomes final, would preclude its submission to international arbitration.120

A purely contractual claim would thus normally find difficulty in passing the jurisdictional test of treaty-based tribunals, which will of course require allegation of a specific violation of treaty rights as the foundation of their jurisdiction. As the ad hoc Committee held in Vivendi, "A treaty cause of action is not the same as a contractual cause of action; it requires a clear showing of conduct which is in the circumstances contrary to the relevant treaty standard."121


The question, however, is not easy to resolve in practice as has been evidenced by the discussions of various tribunals. The Vivendi ad hoc Committee explained that "In a case where the essential basis of a claim brought before an international tribunal is a breach of contract, the tribunal will give effect to any valid choice of forum clause in the contract." However, to the extent that the fundamental legal basis of a claim is a treaty, the existence of an exclusive jurisdiction clause in a contract between the claimant and the respondent state "cannot operate as a bar to the application of the treaty standard." A similar reasoning applies to the operation of the "fork in the road" mechanism, as the choice of one or other forum will depend on the nature of the dispute submitted and these are not necessarily or always incompatible.

This situation was explained by the Annullment Committee in Wena in respect of the interplay of leases and treaty claims, the first being contractual and the second arising under a treaty:

The leases deal with questions that are by definition of a commercial nature. The IFFA [treaty] deals with questions that are essentially of a governmental nature, namely the standards of treatment accorded by the State to foreign investors... It is therefore apparent that Wena and EHC [Egyptian Hotel Corporation] agreed to a particular contract, the applicable law and the dispute settlement arrangement in respect of one kind of subject, that relating to commercial problems under the leases. It is also apparent that Wena as a national of a Contracting State could invoke the IFFA for the purpose of a different kind of dispute, that concerning the treatment of foreign investors by Egypt. This other mechanism has a separate dispute settlement arrangement and might include a different choice of law provision or make no choice at all... The private and public functions of these various instruments are thus kept separate and distinct."182

The difference between contract-based claims and treaty-based claims has also been discussed by several other international arbitral tribunals, as evidenced by the decisions in Lauder,146 Genin,147 Aguas del Aconquija,148 CMS149 and Azurix.150

182 Lexen, par. 49.
146 Vivendi Annulment, par. 101.
147 Lexen art, par. 9.
152 Vivendi Annulment, par. 98.
153 CMS par. 80; Azurix, par. 89.

and of the ad hoc Committee in Vivendi explained above.156 The Tribunal held in CMS, referring to this line of decisions, that "as contractual claims are different from treaty claims, even if there had been or there currently was a recourse to the local courts for breach of contract, this would not have prevented submission of the treaty claim to arbitration."157

"Umbrella Clauses" as a mechanism of further integration between contracts and treaties

In the recent case of SGS v. Pakistan, the Tribunal came to the conclusion that it did not have jurisdiction over contract claims "which do not also constitute or amount to breaches of the substantive standards of the BIT."171 In SGS v. The Philippines, where contractual claims were more easily distinguishable from treaty claims, the Tribunal referred certain aspects of contractual claims to local jurisdiction while retaining treaty-based jurisdiction.172

A further difficulty found by the tribunals in these last two cases was that both treaties contained an "umbrella clause". As noted further above, "umbrella clauses" or "traités de couverture" might potentially transform a contractual obligation of the State into a treaty obligation, thus erasing the distinction between one and the other. To this extent is that contracts might be considered as treaties from the point of view of their legal effects.

However, it must also be noted that the tribunal in SGS v. Pakistan was not convinced that umbrella clauses could always have such a broad effect as there would be no further difference between contract-based claims and treaty-based claims; it therefore undertook the task of examining both the legal purport of the clause and the intention of the parties in building this clause into the treaty. The Tribunal recognized that States can agree if they so wish that "all breaches of each State’s contracts with investors of the other State are forthwith converted into and to be treated as breaches of the BIT", but that in that particular case there was "no clear and persuasive evidence that such was in fact the intention."173
In SGS v. The Philippines the Tribunal took the rather unusual step of criticizing the decision of the Tribunal in SGS v. Pakistan, concluding that in the treaty concerning the Philippines the umbrella clause "makes it a breach of the BIT for the host State to fail to observe binding commitments, including contractual commitments, which it has assumed with regard to specific investments. But it does not convert the issue of the extent or content of such obligations into an issue of international law". A claim concerning this last aspect was the one the Tribunal held should be submitted to local courts while retaining jurisdiction for the treaty-based aspect of the dispute. Although the reasoning of the Tribunal cannot be easily followed, the fact is that the umbrella clause was assigned a broad effect in the context of that particular treaty.

The increasing interaction of public law and private rights in the light of legitimate expectation.

As mentioned further above, in spite that contracts have been increasingly subject to international law and detached from domestic legal constraints this does not mean that they have been transformed into treaties. Similarly, many of the attributes of treaties can be extended to contracts, including pacta sunt servanda and observance in good faith, but this does not mean that treaties are contracts as they govern a different relationship in the international community.

What is most interesting to realize is that the closer the interactions between treaties and contracts the greater the nexus between one and the other will develop. This is noticeable, for example, when States undertake by means of a full-fledged and unequivocal "umbrella clause" to treat breaches of contract as a breach of a treaty protecting the rights of investors. This is also the case of the extraordinary development embodied in the ICSID Convention to the extent that States enter into treaties that provide for the consent of host States to international arbitration in respect of unnamed investors who at any point in time may exercise the option of resorting to such arbitral jurisdiction. Investment contracts are thus linked automatically by the treaty to international arbitration and the standards of treatment laid down by the treaty and international law.

While this interaction is today typical of investments and increasingly so in respect of trade and financial transactions in the international market, the question that remains is whether other fields of activity will follow the same path. International contracts, even if purely private, are already pointing in this direction. Will many other contracts be subject to global standards concerning both jurisdiction and substantive rules of applicable law?

It must first be noted that indeed the interactions are increasing. One element has been the interplay of the most favored nation clause in connection with bilateral investment treaties, both in procedural and substantive terms. Another element has been the recognition of the nature of global financial markets and its effect on the law.

The answer in the end is connected to the examination of a broader issue, namely the need to establish limits to the overarching powers and functions of States in respect of the individual. A number of these limits have been established by means of legal safeguards, including the question of controlling the abuse of rights and discretionary powers of the administration, and by the role of domestic courts in ensuring their implementation. However, at least in connection with international legal transactions, this is a task that has also to be undertaken by international law.

It is a well-established principle that States may not act in a manner contrary to treaties and contracts, at least those contracts that are under some form of protection of international law itself. Although the identification of the standard of observance of and compliance with contracts by States has not been easy in a historical perspective, increasingly there is a noticeable influence in domestic and international courts of the standard of legitimate expectation. Whether this has been a development undertaken in express terms or many times implied, the fact is that what finally counts is the protection of the rights of the individual, not exclusively those of the State as in the past.

At first this standard was concerned mainly with procedural questions or with the need to take into account a previous policy. In Preston, however, the House of Lords ruled that unfairness amounting to an abuse of power could arise from conduct equivalent to breach of contract or representation. In the recent case R. v. North and East Devon Health Authority, ex p. Coughlan the Court of Appeal in England sought to redress the inequality of power between the citizen and the State. In this case it was held that:

Where the Court considers that a lawful promise or practice has induced a legitimate expectation of a benefit which is substantive, not simply procedural, authority now establishes that here too the court will in a proper case decide whether to frustrate the expectation is son unfair that

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168 SGS v. Philippines, ICSID Case No. ARB/02/26, Decision on Objection to Jurisdiction, 29 January 2004, p. 163.
169 SGS v. Pakistan, p. 171.
170 SGS v. Philippines, p. 128.
171 Macrlell v. Spire, ICSID Award of November 13, 2000. This case came to rest the discussion initiated by both the International Court of Justice and the Commission of Arbitration in the Amalgieka Case, United Nations, Reports of International Arbitral Awards, 1963, p. 160.
to take a new and different course will amount to an abuse of power. Here, once the legitimacy of the expectation is established, the court will have the task of weighing the requirements of fairness against any overriding interest relied upon for the change of policy. 183

The Court, having examined prior cases, then added:
The court's task in all these cases is not to impede executive activity but to reconcile its continuing need to initiate or respond to change with the legitimate interests or expectations of citizens or strangers who have relied, and have been justified in relying, on a current policy or extant promise. 183

The reasoning of the court is not only relevant in terms of domestic legal constraints but extends equally to those policies and contracts that have been internationalized. Governments may undertake changes of policy in their continuing need to search for the best choices in the discharge of their functions. However, to the extent that policies earlier in force might have created legitimate expectations both of a procedural and substantive nature for citizens, investors, traders or other persons, these may not be abandoned if the result would be so unfair as to amount to an abuse of power. Discretionary powers of the State, unchecked in the past, are today subject to a legal scrutiny so as to prevent frustration of individual rights.

This approach is also permeating the work of international tribunals. The World Bank Administrative Tribunal, for example, has applied the standard of legitimate expectation in several recent decisions so as to examine the administrative powers of the institution in the light of the rights of the affected individual. 184

Global protection under international law

The implications of this view for international law have not passed unnoticed. Professor Ian Brownlie 185 and Lady Fox 186 have recently raised the question whether matters giving rise to legitimate expectation on the part of an individual should be included among the exceptions to the law of State immunity, just as the commercial activity of States has been recognized as a fundamental exception to immunity, so too there might be a need to accommodate the increased supervision of government functions. The underlying rationale for such exception is that


184 Associated Provincial Pictures House Ltd v Wednesbury Corporation (1947) 2 All ER 490, (1948) 1 ER 223.


186 V. v North and East Devon Health Authority, ex parte Coughlan (2000) 1 All ER 870.


188 V. v North and East Devon Health Authority, per 57.

189 V. v North and East Devon Health Authority, per 65.

V. COMMON PRINCIPLES AND GLOBAL NATIONALITY

The Future of International Economic Law

The search for common principles.

Little doubt can there be about the fact that International Economic Law has become global. A global society where goods and capitals flow every passing day with fewer restrictions could not do otherwise. The process of internationalization begins with the old treaties on Friendship, Commerce and Navigation, it follows with modern investment contracts governed by specific stabilization clauses and ends up, for the time being, with the ever expanding network of bilateral investment treaties and multilateral conventions, including recent Free Trade Agreements.

The legal framework underlying this process has become so interconnected and mutually-reinforced that it would not be an exaggeration to believe that
the governing rules respond to common fundamental principles, in spite of the many variations in their application to specific cases. Domestic foreign investment legislation has for the most also become permeated by the main principles of this internationalized system. International arbitration and judicial decisions have also significantly contributed to this process of gradual integration and legal harmonization.

It would be wrong to believe that this process is not surrounded by difficulties, but one must be also aware that they are typical of a transitional period in which rules and institutions are adjusted to new realities. What counts is the long-term outcome.

State functions in transition

Sovereign prerogatives are today confronted with a new globalized regime concerning foreign investments, just as they are subject to continued pressures from the international trade system, human rights claims and other matters. This does not mean, however, that the sovereign state is fading away as it is still the major actor of the international legal and political system and ultimately, in many cases, the guarantor of democratic rights and values of its citizens, on occasions threatened by ideological and miscarried interpretations of international law. State functions are not being abandoned, they are simply transiting from the absolute to the relative, from occasional arbitrariness to accountability, from serving over-powerful states to ensuring citizens' rights.

The distinction between the jure imperii and the jure gestionis is thus becoming sharper as there is no reason for treating commercial activities differently if carried out by the state. Under the same token, however, the issue of why should foreign investors be treated better than national economic agents has been rightly posed. The privileged position of protected investors has been criticized in domestic debates and argued repeatedly in international arbitration.

Yet, the answer to this question does not lie in treating all operators, foreign or domestic, under the same national standard and have their disputes adjudicated by national courts. That would make Mr. Calvo and his doctrine most happy but would result in the uncertainty that arises from many different national standards which on occasions are not conducive to attract the needed capital investments. The real option appears to be different: to treat all economic agents, again foreign or domestic, under a same standard ensuring both certainty and predictability. This is precisely what is beginning to happen.

Transitions are quite naturally difficult to handle. While some states might be moving forward with this understanding, mainly out of necessity, some other appear to be moving backward, mainly as a result of their passing from capital exporter to capital importer status. A number of debates in the United States in connection with NAFTA and other international bodies are clearly reminiscent of discussions in Latin America in the past.

This of course begs the question of how a common standard can be achieved in the light of current tensions. Here is where the role of foreign investment law and international arbitration comes into play.

Harmonizing international and domestic standards

A first avenue for attaining this goal is the gargantuan expansion of bilateral investment treaties and multilateral instruments, also extending, as mentioned, to the new orientations of national legislation governing foreign investment. In terms of which developments are to be attributed to treaty law and which to customary law the situation is in a state of flux. This is so, first, because rules of customary law are indeed reflected in a significant number of treaties and, next, because treaty rules are in a number of cases transiting into customary law. Whichever direction the process takes, the end result is that the standard envisaged becomes the law common to the international community.

In some matters the identification and meaning of the relevant standard of treatment appears to have completed its process of harmonization. This is mainly the case of the standard governing expropriation and nationalization, which today may be considered common both to major domestic legal systems and international law, both customary and conventional, and has largely passed into the domain of basic human rights.

A greater debate surrounds, however, another major standard, that applicable to regulatory or indirect expropriation or other measures that seriously interfere with the rights to which an investor is entitled by contract, law or treaty. The question here is whether “fair and equitable treatment” and related aspects of the protection extended to the investor are different in domestic law, customary law and treaty law, and if so which should prevail.

The NAFTA Free Trade Commission appears to have taken the view that customary law sets a standard less demanding than that which could be understood by panels and tribunals to be the case under that treaty and other recent free trade agreements. That may be true historically if you consider as customary the standard envisaged, say in the Neer case.

Probably no one could today identify with any precision which is the customary law standard as it has been significantly evolving along time and embodies a number of concerns which are not alien, again, to major domestic legal systems and to human rights. In fact, panels have not been unimpressed by domestic standards, just as the European Court of Human Rights has significantly contributed to a more
precise interconnection between property and human rights.

It is probably right to believe that in the light of a number of recent decisions "fair and equitable treatment" is not really different from legitimate expectation as developed, for example, by the English courts and also recently by the World Bank Administrative Tribunal. International law is not unaware of major domestic legal developments, particularly when the rights of citizens are entangled in promises made by their governments and have in good faith relied upon them. Whether this standard may be developed beyond foreign investments or international administrative law, is just a question of time. The common standard thus continues to evolve.

Overcoming discrimination.

A second major avenue for the harmonization of relevant standards is the combination of national treatment and the most favored nation clause, all pointing to the need of eliminating discrimination. Under national treatment, citizens and foreigners are to be treated alike, in the understanding that the former might be in a situation more privileged than the latter. If the reverse turns out to be the case, then again the answer lies in upgrading the treatment of nationals to the international standard available and not the opposite.

More importantly, under most favored nation treatment no discrimination among foreign beneficiaries of certain defined rights should take place. The end result is again that the process of harmonization of international and domestic standards becomes yet more intense. This has become perhaps the greatest tool available for the avoidance of discrimination, particularly in the light of the most favored nation clause inserted in all treaties of commerce and navigation, bilateral and multilateral investment treaties and a number of trade arrangements, most notably the WTO.

There is indeed a continuing search for the harmonization of applicable standards and mechanisms and however much Maizezini is narrowed or enlarged this concern will not fade away, just as the need to avoid discrimination will persevere.

The benefits of decentralization

A different issue concerns the institutional needs of foreign investment law. Tempting as the idea of channeling this evolving process by means of a single or central mechanism is, I am not quite persuaded by its merits. All large institutions, like states themselves, sooner or later tend to make policies directed to serve the institution and lose sight of the needs of their assumed beneficiaries.

I see more merit in a continuing decentralized function where various mechanisms will compete for efficiency, timeliness and professionalism. To the extent that users of the system, whether investors or host states, have a choice, this will result in the increased search for improvement. The availability of ICSID and UNCITRAL tribunals as major mechanisms for the settlement of investment disputes has been appropriate. The International Chamber of Commerce might consider developing an alternative facility to this effect, which is already in demand under some treaties and contracts.

The risk of contradictory decisions and forum shopping cannot be ignored, as recent cases have evidenced, but this is a rather minor inconvenience of the existing decentralized system when compared to its benefits. A strong community of arbitrators, scholars and practitioners is a guarantee sufficient to overcome difficulties of the sort as the process evolves.

The proposal to establish an appeals mechanism in the context of foreign investment arbitration decisions is today the hottest item in the menu. The very fact of an increasing number of requests for annulment, either under the ICSID convention or domestic courts under UNCITRAL rules, is also the expression of the search for a review mechanism. If the intention of these initiatives is to contribute to the improvement of the system of international arbitration, they may well succeed as has been the experience of the Appellate Body of WTO. However, if the intention is to reverse and to re-nationalize the evolving process, it might not meet an equally successful fate as the world moves in the opposite direction.

A number of alternative suggestions have been made and they certainly deserve a careful consideration. Why not extend the ICSID annulment mechanism to decisions under the special facility, if the concern has been to challenge NAFTA decisions in this context? Why not to establish a Court of International Arbitral Decisions, where international investment and commercial litigation might have the opportunity to challenge adverse decisions? This suggestion would certainly contribute to the full internationalization of arbitration departing from the present day challenges before domestic courts. The International Chamber of Commerce could make available a special facility to this effect under the Court of International Arbitration. Again in this matter the system could offer the benefits of decentralization.

Global investments, like global trade and human rights, require truly international dispute settlement arrangements. The present day shortcomings can be well understood in a transitional period between the traditional system and the new endeavors of global society. Yet, they cannot last for long as they would hamper the very activities that are the engine of the ongoing changes.
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