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In defense of bilateral investment treaties

by

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The creation of the International Centre for Settlement of Investment Disputes (ICSID) is the boldest step in the modern history of international cooperation on the protection of foreign investment. It has furthered the flourishing of arbitration between investors and states, itself one of the most progressive developments in international law of the past sixty years. Since Germany concluded the first bilateral investment treaty (BIT) with Pakistan in 1959, some 3,000 BITs have been concluded. Yet, there are reports that the European Union (EU), led by Germany, may exclude investor-state arbitration from the Transatlantic Trade and Investment Partnership (TTIP) with the United States (US), impairing the ubiquity of investor-state arbitration.

Opponents of investor-state arbitration claim that it faces a “legitimacy crisis.” There are three essential contentions advanced by such critics: (1) tribunals are biased toward multinational enterprises; (2) arbitration is asymmetrical because of investors’ freedom to bring claims against states, while states cannot bring claims against investors; and (3) arbitral awards are often conflicting. These criticisms are more colorful than they are cogent.

With regard to bias, Susan Franck’s research concluded that, of 144 publicly available awards as of January 2012, states won 87 cases when arbitrators resolved a dispute arising under a treaty, while investors won 57.[1] Her research further showed that, even when investors were awarded damages, they won significantly less than the amount claimed, and that about a quarter of investment claims were dismissed at the jurisdictional stage. These findings hardly suggest bias against states.

Second, though the international investment process is indeed asymmetrical, states can, and have, brought counterclaims against investors. Arbitral rules, such as those of ICSID and UNCITRAL, expressly authorize counterclaims. In any event, any suggested imbalance is exaggerated since states not only have police powers, but the police; their means of exerting pressure upon foreign investors are multiple. The ability of the investor to initiate arbitration only mitigates that imbalance.

Moreover, to the extent that BITs constrain states’ ability to regulate investment, critics of investor-state arbitration fail to consider that the very purpose of treaties is

to constrain the freedom of states. Notwithstanding this inherent constraint, states that enter into BITs are free to confirm and specify their rights to regulate within their borders, as demonstrated by some recent model BITs. Legitimate questions may arise about how far BIT provisions bear upon those rights. If those questions have not been settled by the terms of the BIT, they can be dealt with through recourse to the treaty's mechanism for dispute settlement. To cast aside investor-state arbitration because of an unrealized apprehension of adverse effects upon states would be a profound misjudgment of the procedures for the peaceful settlement of international disputes.

Finally, the inconsistency of some arbitral awards hardly justifies denouncing investor-state arbitration. Admittedly, cases sometimes assert conflicting interpretations of BIT provisions, and conflicts in interpretation are, of course, undesirable. But in view of the decentralized, horizontal nature of the international system, they are not unusual. In fact, even in the relatively centralized, hierarchical judicial systems of a state, conflicts among courts are common, aptly demonstrated by the inconsistencies that exist between state and federal jurisprudence in the US. Moreover, conflicting interpretations of similar provisions in BITs often arise because tribunals are responding to differences in the facts of each case.

To address some of these criticisms, opponents of investor-state arbitration have proposed the establishment of a tenured appellate court, such as the Appellate Body of the World Trade Organization. In principle, this proposal is appealing; but it would present many difficulties, as ICSID found when it examined the possibility. Furthermore, states have shown little disposition toward taking this path.

Another course proposed by opponents is for national courts to settle investor-state disputes. However, national courts may find themselves constrained by state immunities, or subject to political influence, corruption or simply be nationalistic in their perception of the facts and the law. Accordingly, it is perfectly reasonable for foreign investors to prefer international arbitration, just as many thousands of parties engaging in international commerce have for many years.

Acceptance of investor-state arbitration should not suggest that there are no areas for improvement. For example, arbitrators encounter many tactical challenges, and tribunals or institutions should be empowered to impose sanctions on parties or their counsel who abuse the making of challenges.

Another reform that merits consideration is institutionalizing security for costs. Special purpose vehicles may bring thin claims against states, thereby imposing a financial burden on states. Even if the state wins the arbitration and is awarded costs, it may find that the special purpose vehicle used by the claimant lacks the funds to pay costs. It is toward shortcomings such as these that reform efforts should be directed.

International investment law is a profoundly progressive development of international law: it should be nurtured rather than restricted and denounced. The substitution of national adjudication for international investment arbitration would be a regressive development that is to be resisted rather than furthered.

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[1] Susan D. Franck, "Using investor-state mediation rules to promote conflict management: An introductory guide", *ICSID Review*, vol. 29 (Winter 2014), pp. 66-89.

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