

# **ILA Study Group on the Role of Soft-Law Instruments in International Investment Law**

## **Report**

**by**

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The Study Group was established by the ILA Executive Council in November 2008 for a three-year period. Its express mandate is “to study the development of soft law instruments in international investment law and the feasibility of a ‘codification’ of the present state of this field of international economic law”.

The Executive Council appointed Sir Franklin Berman (UK) as Chairman, as well as Andrea K. Bjorklund (US) and August Reinisch (Austrian) as Co-Rapporteurs of the Study Group. Other members of the Group are Yas Banifatemi (French), Giuditta Cordero-Moss (Norwegian), Melaku Desta (UK), Moshe Hirsch (Israeli), Daniel Magraw (US), Kate Miles (Australian), Audley Sheppard (UK), Christian Tietje (German), Matthew Weiniger (UK), Catherine Yannaca-Small (Greek), Andreas Ziegler (Swiss).

An interim report was submitted to The Hague Conference 2010 providing background on the establishment of the Study Group and its main purpose. At that conference, the Group decided to devote its main attention to the preparation of a book investigating whether investment law was ripe to be “codified” and, if so, whether a specific form of soft-law instrument might be particularly suited for this task, keeping in mind that the ILA has a long-standing tradition of formulating ‘Rules’, ‘Recommended Practices’, ‘Draft Articles’, etc. in an attempt to contribute to the codification and development of various fields of international law.

It is a “feasibility study” which has been produced by members of the Study Group and which will be presented at the Sofia Conference. The collected contributions have been edited by the Co-Rapporteurs of the Group and published under the title “International Investment Law and

Soft Law” by Edward Elgar.<sup>1</sup> As a “feasibility study” the book aims to present and assess the pros and cons of an attempted codification effort and to induce a more informed debate about the topic.

In recent years there is a growing interest in areas ‘where the action is’, such as trade and investment law. Both fields have been booming mostly as a result of the sharp increase in dispute settlement. In the case of trade law, this was institutionally anticipated through the ‘legalization’ of trade disputes, or the turn from trade diplomacy to trade law as a result of the Uruguay Round negotiations and the ensuing Dispute Settlement Understanding of the World Trade Organisation (WTO DSU), which brought not only a quasi-right to have a WTO panel hear a complaint, but also a much more contentious procedure resulting in a binding report. In parallel, investment disputes came of age as a result of the growing number of BITs and other IIAs which provided for investor/State dispute settlement and the crucial jurisprudential development of regarding these treaty provisions as offers from host states that could be accepted at any time by the protected investors of the other contracting parties. Thus, treaty arbitration has grown exponentially.

The treatification of international trade and investment law, combined with the availability of dispute settlement resulting in usually publicized awards, offers a rich and complex variety of sources that could influence a codification effort. Such an effort would not be a classic identification and codification of customary international law. Rather, we are faced with a multitude of interpretations given to multilateral (NAFTA/GATT/ECT) and bilateral (BITs) treaties providing a conventional core of rights and obligations sometimes supplemented by general international law. In addition, and particularly in investment law, there is often underlying customary international law that has to be addressed. For instance, the typical expropriation clause in an investment treaty frequently resembles very closely the so-called *Hull* formula,<sup>2</sup> which arguably represents (or has represented) customary international law at least at some stage.<sup>3</sup> Similarly, there is a view held by many and reinforced by the actual

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<sup>1</sup> Andrea K. Bjorklund & August Reinisch (eds.), *International Investment Law and Soft Law* (Edward Elgar 2012).

<sup>2</sup> Green Hackworth, 3 *Digest of International Law* (1942) 658-659 ([...] no government is entitled to expropriate private property, for whatever purpose, without provision for prompt, adequate and effective payment therefore.); Muthucumaraswamy Sornarajah, *The International Law on Foreign Investment* (CUP 2010) 210.

<sup>3</sup> Patrick Norton, ‘A Law of the Future or a Law of the Past? Modern Tribunals and the International Law of Expropriation’ (1991) 85 *AJIL* 488, 495; Davis R Robinson, ‘Expropriation in the Restatement’ (1984) 78 *AJIL* 176, 177; K Scott Gudgeon, ‘Valuation of Nationalized Property under United States and other Bilateral

formulation found in some IIAs that the fair and equitable treatment standard reflects, or at least encompasses, the (customary) international minimum standard of treatment of aliens.<sup>4</sup>

While technically the treaty provisions which reflect the refinement of trade and investment law must have primacy, general international law remains highly relevant as contextual background. In both areas, the issue of systemic integration as a specific interpretation tool under Article 31(3)(c) of the VCLT plays an increasingly important role.<sup>5</sup> The increased interest in the two fields of trade and investment is also evidenced by the ILC's current work on MFN.<sup>6</sup>

### **Hard codification in trade and investment law**

In the fields of trade and investment law, 'hard' codification has been only partly successful. With regard to trade law, it is difficult to speak of a 'codification' of customary rules in general since most trade rules embodied in bilateral as well as multilateral trade agreements like the GATT contain specifically extended trade benefits or privileges, such as better access to domestic markets for goods originating in other contracting states, that are typically specifically negotiated between parties and do not arise under customary international law.<sup>7</sup>

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Investment Treaties' in Richard B Lillich (ed), *IV The Valuation of Nationalized Property in International Law* (1987) 113-114.

<sup>4</sup> Stephen M Schwebel, *The Influence of Bilateral Investment Treaties on Customary International Law* (2007), Proceedings of the 98<sup>th</sup> Annual Meeting of the American Society of International Law (31 March – 3 April 2004) 29-30; Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties, Standard of Treatment* (Kluwer Law International 2009) 270; Ian Brownlie, *Principles of Public International Law* (OUP 2003) 520; Bernard Kishoiyian, 'The Utility of Bilateral Investment Treaties in the Formulation of Customary International Law' (1994) 14 NJILB 327; Steffen Hindelang, 'Bilateral Investment Treaties, Custom and a Healthy Investment Climate? The Question of Whether BITs influence Customary International Law Revisited' (2004) 5 JWIT 767; Ioana Tudor, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* (OUP 2008) 53-84.

<sup>5</sup> Brigitte Stern, 'Interpretation in International Trade Law' in Malgosia Fitzmaurice, Olufemi Elias and Panos Merkouris (eds), *Treaty Interpretation and the Vienna Convention on the Law of Treaties: 30 Years On* (Koninklijke Brill NV 2010) 48, 111; Campbell McLachlan, 'The Principle of Systemic Integration and Article 31(3)(c) of the Vienna Convention' (2005) 54 ICLQ 279; *United States – Import Prohibition of Certain Shrimp and Shrimp Products*, WTO Dispute Settlement Body WT/DS58/AB/R (Report of the Appellate Body of 12 October 1998) at 158; *Pope & Talbot Inc v Canada*, NAFTA, Award on the merits of 10 April 2001, Award in respect of damages of 31 May 2002; *EC measures concerning meat and meat products (hormones)*, WTO Dispute Settlement Body WT/DS-26/AB/R – (Report of the Appellate Body of 16 January 1998); Campbell McLachlan, Laurence Shore and Matthew Weininger, *International Investment Arbitration, Substantive Principles* (OUP 2007) 66.

<sup>6</sup> Report of the International Law Commission, Sixty-third Session (2011) General Assembly Official Records Supplement No 10 (A/66/10) Chp XII, para 345.

<sup>7</sup> Stephen Zamora, 'Is there Customary International Economic Law?' (1990) 32 GYIL 9-42; Ignaz Seidl-Hohenveldern, *International Economic Law* (Kluwer Law International 1999) 29 et seq.

Nevertheless, the Uruguay Round, like the Tokyo Round before it, led to some extent to the codification of earlier institutional practices, e.g. of dispute settlement under Article XXIII GATT, coupled with a number of rather innovative elements of progressive development, such as reverse consensus<sup>8</sup> and cross-retaliation.<sup>9</sup> Also in other fields of trade law, past practice was codified, such as in the Antidumping<sup>10</sup> and Subsidies<sup>11</sup> Agreements, the Agreement on Technical Barriers to Trade<sup>12</sup>, and the Agreement on the Application of Sanitary and Phytosanitary Measures.<sup>13</sup> WTO law also provides examples for a potential hardening of soft codification, such as the importation of non-binding standards set by various institutions, like the International Organization for Standardization (ISO), into the hard-law TBT and SPS Agreements.<sup>14</sup>

In investment law, hard codification has been rather unsuccessful. Attempts to agree on a multilateral investment agreement – such as the OECD projects of the 1960s, ending with a Draft Convention on the Protection of Foreign Property,<sup>15</sup> and the 1990s, leading to the aborted MAI negotiations,<sup>16</sup> – led nowhere; though there are currently some signs on the horizon of a renewed interest in this matter. This, too, is likely a result of a lack of consensus on the nature of the customary international law that might be codified; the failure of the codification attempts of the 1960s can be traced to the post-colonial dissatisfaction with international law that culminated in the New International Economic Order of the 1970s; the failure of codification attempts of the 1990s had perhaps more to do with generalized distrust

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<sup>8</sup> Article 16 of the Dispute Settlement Understanding (DSU).

<sup>9</sup> Article 22 of the DSU.

<sup>10</sup> Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-dumping Agreement), 15 April 1994, entered into force 1 January 1995, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1868 UNTS 201.

<sup>11</sup> Agreement on Subsidies and Countervailing Measures, 15 April 1994, entered into force 1 January 1995, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 UNTS 14.

<sup>12</sup> Agreement on Technical Barriers to Trade, April 15, 1994, entered into force 1 January 1995, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1868 UNTS 120.

<sup>13</sup> Agreement on the Application of Sanitary and Phytosanitary Measures, April 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 UNTS 493.

<sup>14</sup> The Agreement on Technical Barriers to Trade encourages State Parties to comply with a Code of Good Practice; local government, non-governmental and other standardizing bodies, including the ISO, can also accept the Code of Good Practice. This cooperative approach contributes to a uniformity of technical regulations that facilitates, rather than impedes, trade. The Agreement on the Application of Sanitary and Phytosanitary Measures encourages members to use international standards, guidelines, and recommendations, such as those set out by the ISO.

<sup>15</sup> The OECD Council published a Draft Convention on the Protection of Foreign Property in 1967, but the draft was never formally adopted. Resolution of the OECD Council, 12 October 1967, 7 ILM 117.

<sup>16</sup> From 1995 to 1998 the OECD hosted a series of negotiations designed to produce a multilateral agreement on investment (MAI). The negotiating group produced a draft text, but the negotiations stalled. For a draft text, see *The Multilateral Agreement on Investment: Draft Consolidated Text*, DAF/MAI(98)7/REV1 (22 April 1998).

of ‘globalization’ rather than with specific objections to many of the core international investment law norms which by then were included in most BITs.

Indeed, in the 1960s states started to conclude investment protection treaties on a bilateral basis leading to a dense web of almost 3,000 BITs. To some extent this decentralized BIT codification may be regarded as a substitute for the failed multilateral approach. This is not to say that all BITs are identical; some contain different formulations of similar ideas (viz. different formulations of umbrella clauses and MFN clauses), while others do not contain those obligations at all. One of the most contentious issues in investment law is the extent to which these differences in treaty language should lead to divergent outcomes, or whether treaties should be harmonized by use of various interpretive techniques. Although technically speaking, each BIT is an ‘island to itself’ it is obvious that the striking similarity between BITs suggests that they are regulating common problems in a common fashion. This justifies reliance on BIT arbitral decisions – not as binding precedent – but as part of a *de facto* case-law or *jurisprudence constante*.<sup>17</sup>

This search for consistency may be viewed as the collective professional deformation of lawyers, but it is probably more than that. With the growth of an investment ‘case law’, the question becomes more and more acute whether a common law of investment can be ascertained and, if so, whether and to what extent it may be identified and described.

Traditionally, this would call for a hard-law codification, but in the field of investment law, it seems that currently such a solution would be hard to achieve; thus a soft-codification attempt is likely to prove more effective.

### **Soft Codification in Investment Law**

It appears that a soft-law codification instrument could provide a contemporary view of the state of the emerging and in several areas already settled jurisprudence of international investment law. Indeed, a significant contribution would be to identify those areas in which one can identify a *jurisprudence constante*. Such a “codified” text could serve tribunals,

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<sup>17</sup> See Andrea K Bjorklund, ‘Investment Treaty Arbitral Decisions as Jurisprudence Constante’ in Colin Picker, Isabella Bunn and Douglas Arner (eds), *International Economic Law: The State and Future of the Discipline* (2008) 265; Gabrielle Kaufmann-Kohler, ‘Arbitral Precedent: Dream, Necessity, or Excuse’ (2007) 23 *Arbitration International* 357; August Reinisch, ‘The Role of Precedent in ICSID Arbitration’, in *Austrian Arbitration Yearbook* (2008) 495; Ian A Laird, ‘The Emerging Jurisprudence of International Investment Law: Introduction to Conference’ in Andrea K Bjorklund, Ian A Laird and Sergey Ripinsky (eds), *Investment Treaty Law, Current Issues III*, (British Institute of International and Comparative Law 2009); Paolo Vargiu, ‘Beyond Hallmarks and Formal Requirements: A “Jurisprudence Constante” on the Notion of Investment in the ICSID Convention’ (2009) 10 *J World Inv. & Trade* 753.

parties, and counsel in helping to identify the current state of investment arbitral jurisprudence and scholarship (in the sense of Article 38 of the ICJ Statute). By objectively describing the current state of international investment law, it could facilitate the identification of customary international law. Such an instrument could also assist governments in the negotiation and renegotiation of existing bilateral investment treaties where the trend is to incorporate (or react to) investment arbitral jurisprudence by adding much more detail to the hitherto quite open-ended treaty obligations. Finally, it could even provide an early model and drafting text for another attempt at a legally binding multilateral investment convention.

The Study Group's book, however, also analyses the potential disadvantages of soft-law instruments. It is evident that in situations where there is no established case law, a soft-law instrument would leave a gap or would have to state a principle by endorsing an approach that had not earned consistent or near-universal support. In the case of conflicting approaches, choices made at the drafting stage might result in wording that would not necessarily be representative of any leading approach. Finally, a soft-law instrument might have to be formulated so generally to be representative of all various approaches that it could not induce harmonization when specific questions have to be decided.

Furthermore, the variety of potential end users described above could prove to be a challenge should the Study Group conclude that drafting a soft-law instrument is feasible. A precise descriptive statement of existing law might be of most use to counsel and arbitrators, whereas a more prescriptive approach suggesting innovative practices might be more appropriately addressed to legislative bodies. In either case, a clear and objective assessment of purpose is essential to establish the credibility of the drafters and the reliability of the product.

Given the preceding considerations, the book encompassing the feasibility study is organized as follows. After an introductory chapter by the Co-Rapporteurs of the Study Group, the first section of the book, comprising three chapters, discusses different facets of 'soft law'. Chapter two by Moshe Hirsch introduces the primary sources of international law and describes their relationship with soft law. In chapter three Melaku Desta addresses soft law generally, while chapter four by Andrea K. Bjorklund examines the factors that lead soft-law instruments to be successful and critically appraises the advantages and disadvantages of various instruments with an eye towards their efficacy in the field of international investment law.

The second section contains three studies of the ways that soft law has been used in various fields. In chapter five Kate Miles examines the important influence soft-law instruments have had in the field of international environmental law. Chapter six by Giuditta Cordero-Moss assesses the effectiveness of various soft-law manifestations in international commercial law. Chapter seven by Melaku Desta turns to the innovative ways the WTO Agreements have encouraged the mingling of hard and soft law.

The third section looks more specifically at international investment law's ripeness for codification. Chapter eight by Christian Tietje and Emily Sipiorski explores the development of international investment treaties and examines the common strands that unify the current generation of investment treaties. In chapter nine Andreas Ziegler assesses whether the most-favoured-nation obligation is ripe for codification or multi-lateralization. Chapter ten by August Reinisch examines particularly the 'legality' requirement in the standard of expropriation and attempts a sample codification. Finally, a concluding chapter by the Co-Rapporteurs addresses the ripeness of international investment law for concretization in a soft-law instrument.

The ILA Study Group has thus focused on identifying the main issues surrounding a potential 'codification' of investment law and investigating whether and in which form investment law may be 'codified.' This 'feasibility study' has led to a nuanced outcome. While it has identified a number of areas which embody relatively robust and coherent practical application of investment rules, evidenced by a homogeneous case law, which may thus be regarded as 'codifiable', it has also demonstrated that there is a growing number of fields where investment tribunals have given diverging interpretations to identical or similar BIT provisions. Examples go beyond the well-known divergent approaches by individual tribunals to the most-favoured-nation clause, the 'umbrella' clause, the notion of investment, or the nature and prerequisites of the necessity defence. In addition, they now include the question of how to interpret so-called narrow dispute settlement clauses referring to the amount and modalities of compensation in the case of expropriation<sup>18</sup> or the nature of so-called waiting periods.<sup>19</sup>

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<sup>18</sup> Contrast the narrow interpretation of such clauses by the tribunals in *Vladimir and Moise Berschader v The Russian Federation*, SCC Case No 080/2004, Award of 21 April 2006; *RosInvestCo UK Ltd. v The Russian Federation*, Award on Jurisdiction 2007, SCC Case No ARB/V079/2005; *Austrian Airlines AG v The Slovak Republic*, UNCITRAL Final Award of 9 October 2009, with the wide interpretation given in *Saipem S.p.A. v The People's Republic of Bangladesh*, ICSID Case No ARB/05/07, Decision on Jurisdiction and Recommendation

This does not mean that a soft codification is impossible, but that any codification attempt must take into account the variations in treaty language that might result in different interpretations. It also must faithfully represent the strands of thought in areas in which agreement on the correct interpretation has yet to coalesce. These considerations will require careful handling if the goal of the soft-law instrument is to induce harmonisation rather than divergence.

Indeed, notwithstanding the above caveats, it appears that a ‘soft codification’ of international investment law is already taking place primarily through the coherent interpretation of investment law instruments by investment tribunals. This trend could be reinforced and harmonious interpretation strengthened by a soft-law instrument providing guidance to users of the systems, such as arbitrators, litigators, negotiators, scholars, and others.

But a soft law instrument may be of use not only in the actual application of investment law, but also in the phase of its creation. Such an instrument could assist governments in the negotiation and renegotiation of existing BITs where the trend is to incorporate (or react to) investment arbitral jurisprudence by adding much more detail to the hitherto quite open-ended treaty obligations. Finally it could, if a window of political opportunity would emerge, provide an early model and drafting text for another attempt at a legally binding multilateral investment convention.

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on Provisional Measures of 21 March 2007; *European Media Ventures SA v Czech Republic*, Judgement of the High Court of England and Wales of 5 December 2007, (2007) EWHC 2851 (Comm); *Tza Yap Shum v Republic of Peru*, ICSID Case No ARB/07/6 (China/Peru BIT), Decision on Jurisdiction and Competence of 19 June 2009. See also August Reinisch, ‘How Narrow are Narrow Dispute Settlement Clauses in Investment Treaties?’ (2011) 2 *Journal of International Dispute Settlement* 115-174.

<sup>19</sup> Most investment tribunals have treated consultation periods as directory and procedural rather than as mandatory and jurisdictional in nature.’ *SGS Société Générale de Surveillance S.A. v Islamic Republic of Pakistan*, ICSID Case No ARB/01/13, Decision on Jurisdiction of 6 August 2003), para 184; *Ronald S. Lauder v The Czech Republic*, UNCITRAL, Final Award of 3 September 2001), para 190; *Bayindir Insaat Turizm Ticaret Ve Sanayi AS v Pakistan*, ICSID Case No ARB/03/29, Decision on Jurisdiction of 14 November 2005) para 100. More recently, however, a number of tribunals have insisted on the jurisdictional character of such requirements. *Burlington Resources Inc. v Republic of Ecuador and Empresa Estatal Petróleos del Ecuador (PetroEcuador)*, ICSID Case No ARB/08/5, Decision on Jurisdiction of 2 June 2010); *Murphy Exploration and Prod. Co. Int’l v Republic of Ecuador*, ICSID Case No ARB/08/4, Award on Jurisdiction of 15 December 2010).



The Study Group proposes that it should now initiate a reflection phase assessing the reactions to the outcome of its collective efforts as published in *International Investment Law and Soft Law*. This reflection phase should not exceed two further years. Rather, it should lead to a recommendation to the ILA Executive Council whether to pursue “codification” plans or devote attention to other aspects of international investment law.

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