Investment Protection and Dispute Settlement in Preferential Trade Agreements: A Challenge to BITs?

*August Reinisch**

I. THE PROLIFERATION OF PREFERENTIAL TRADE AGREEMENTS

PREFERENTIAL TRADE AGREEMENTS (PTAS), in particular in the form of bilateral or regional trade agreements, have multiplied since the 1990s, among them not only accords involving the U.S. or EU, but also numerous South-South and other free trade agreements (FTAs). The lack of progress of the Doha Round negotiations in the early 2000s[1] has reinforced this trend which has been captured

* August Reinisch is Professor of International and European Law at the University of Vienna, Austria, and Professorial Lecturer at the Bologna Center of SAIS/Johns Hopkins University in Bologna, Italy. He has served as legal expert and arbitrator in investment tribunals and is listed in the ICSID Panels of Conciliators and of Arbitrators. He may be contacted at August.Reinisch@univie.ac.at.

[1] Ch. Herrmann, "Bilaterale und Regionale Handelsabkommen als Herausforderung des Multilateralen Handelssystems (WTO)," *in* D. Ehlers, H.-M. Wolffgang and U.J. Schröder (eds.), Rechtsfragen Internationaler Investitionen 217 (2009); R. Fiorentino, L. Verdeja and Ch. Toqueboeuf, "The Changing Landscape of Regional Trade Agreements: 2006 Update," WTO Discussion Paper No. 12, *available at* http://www.wto.org/english/res_e/booksp_e/discussion_papers12a_e.pdf; P. Sutherland, "The Doha Development Agenda: Political Challenges to the World Trading System—a Cosmopolitan Perspective," 8 J. Int'l Econ. L. 363 (2005); D. Johnson et al., "What Future for the DOHA Development Agenda and the Multilateral Negotiating Regime?," *in* 101 Proceedings of the Annual Meeting of the American Society of International Law 243 (2007); M. Moore (ed.), World Trade Organization: Doha and Beyond: the Future of the Multilateral Trading System (2004).

by the notion of the "rise of bilateralism."[2] Many of the more recent PTAs contain investment chapters. In this context, the North American Free Trade Agreement (NAFTA)[3] clearly provided a blueprint of a broad trade agreement with an elaborate investment chapter (Chapter 11) that basically contained all the important features of a stand-alone investment treaty. The recent trend to negotiate PTAs, including such investment chapters, may have been stimulated by the fact that the multilateral forum intended to deal with investment, the WTO, *de facto* abandoned the so-called Singapore Issues,[4] of which one was "trade and investment," at the Cancun Ministerial Meeting in 2003.[5]

II. THE PREVALENCE OF STATE-TO-STATE DISPUTE SETTLEMENT IN PREFERENTIAL TRADE AGREEMENTS

Trade agreements focus on settling trade disputes, usually in a form following the State-to-State dispute settlement mechanisms contained in the WTO Dispute Settlement Understanding (DSU)[6] or in NAFTA dispute

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[2] K. Heydon and St. Woolcock, The Rise of Bilateralism: Comparing American, European and Asian Approaches to Preferential Trade Agreements (2009); S. Lester and B. Mercurio (eds.), Bilateral and Regional Trade Agreements (2009).

[3] North American Free Trade Agreement between the Government of Canada, the Government of the United Mexican States, and the Government of the United States of America (NAFTA) (Dec. 17, 1992), 32 I.L.M. 289 (1993).

[4] WTO, Ministerial Declaration, adopted at the 1st Session of the Ministerial Conference, Singapore, Dec. 13, 1996, WTO Doc. WT/MIN(96)/DEC (Dec. 18, 2009) (hereinafter "WTO Singapore Ministerial Declaration"), *available at* http://www.wto.org/english/thewto_e/minist_e/min96_e/wtodec_e.htm (decision to establish working groups to examine trade and investment, trade and competition policy, as well as transparency in government procurement practices); *see also* WTO, Ministerial Declaration, para. 22, adopted at the 4th Session of the Ministerial Conference, Doha, Nov. 14, 2001, WTO Doc. WT/MIN(01)/DEC/1 (Nov. 20, 2001), *available at* http://www.wto.org/english/thewto_e/minist_e/min01_e/mindecl_e.htm. Paragraph 22 reads as follows:

> [T]he Working Group on the Relationship Between Trade and Investment will focus on the clarification of: scope and definition; transparency; non-discrimination; modalities for pre-establishment commitments based on a General Agreement on Trade in Services (GATS)-type, positive list approach; development provisions; exceptions and balance-of-payments safeguards; consultation and the settlement of disputes between members. Any framework should reflect in a balanced manner the interests of home and host countries, and take due account of the development policies and objectives of host governments as well as their right to regulate in the public interest. The special development, trade and financial needs of developing and least-developed countries should be taken into account as an integral part of any framework, which should enable members to undertake obligations and commitments commensurate with their individual needs and circumstances. Due regard should be paid to other relevant WTO provisions. Account should be taken, as appropriate, of existing bilateral and regional arrangements on investment.

[5] Heydon and Woolcock, The Rise of Bilateralism, *supra* note 2, at 107.

[6] WTO, Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401, 33

settlement.[7] They may be seen as elaborate and institutionalized forms of diplomatic protection, based on the notion of an espousal of the grievances of the Contracting Parties' nationals in a hybrid form of dispute settlement containing elements of negotiation/conciliation and arbitration. Such a diplomatic protection paradigm makes eminent sense in the typical external trade situation where a sometimes large number of often small economic actors are affected by trade measures of WTO or NAFTA Parties, and where, understandably, the costs for pursuing individual claims would become prohibitive.[8] Further, since the interests of affected private parties are usually directed towards being able to assume or resume the trading possibilities they are supposed to enjoy under the relevant trade regime, trade dispute settlement is usually forward-looking in the sense of trying to achieve a solution that induces the Contracting Parties' to behave in accordance with their trade law obligations. Thus, the GATT/WTO as well as the NAFTA dispute settlement systems emphasize recommendations to act in accordance with WTO/NAFTA law instead of awarding damages for breaches of such law.

This is, of course, quite different in the context of investment disputes, which are normally disputes concerning one particular investor who has made a major investment in a host State and where the interests of such an investor are best pursued by the investor itself. Since investment disputes usually imply an investor's choice for an "exit strategy," there is usually no concern about rectifying host State behavior for the future. Instead, investment dispute settlement focuses on compensation and damages, usually in monetary terms. Unless investors seek to be re-established in their previous positions in order to continue their economic activities, where conciliation or mediation may provide a useful method for seeking a mutually acceptable way out for future cooperation,[9] arbitration (or judicial dispute settlement if available) will be

I.L.M. 1226 (1994); *see also* E.-U. Petersmann, International Trade Law and the GATT/WTO Dispute Settlement System (1997); J. Jackson, The World Trading System: Law and Policy of International Economic Relations (2nd ed. 1997); D. Palmeter and P. Mavroidis, Dispute Settlement in the World Trade Organization (2nd ed. 2004).

[7] NAFTA, *supra* note 3, chs. 19–20; *see also* Kr. Oelstrom, "Treaty for the Future: the Dispute Settlement Mechanisms of the NAFTA," 25 L. & Pol'y Int'l Bus. 783 (1994); R. Folsom, M. Gordon and J. Spanogle, Handbook of NAFTA Dispute Settlement (1998); L. Trakman, Dispute Settlement under the NAFTA (1997).

[8] One should of course also mention that there may be one or the other case where a trade dispute *de facto* concerns only a small group of large companies or even one specific exporter/importer. *Cf.* the so-called *Kodak/Fuji* case where a U.S.–Japan trade dispute was in fact a dispute between the two major photographic film producers. WTO, Japan—Measures Affecting Consumer Photographic Film and Paper, Report of the Panel, WTO Doc. WT/DS/44/R (Mar. 31, 1998).

[9] Th. Wälde, "Efficient Management of Transnational Disputes: Mutual Gain by Mediation or Joint Loss in Litigation," 22 Arb. Int'l 205 (2006).

the most appropriate method of solving investment disputes. Permitting such dispute settlement to take place directly between the affected investor and the host State will help to "juridify" and, thus, to eliminate the political overtones of diplomatic protection.[10]

Where PTAs contain investment chapters the question thus arises as to whether State-to-State dispute settlement is sufficient or whether investor-State arbitration is also required. There seems to be an underlying assumption that PTAs in general contain State-to-State dispute settlement mechanisms only. However, it is often unclear whether this assumption stands the test of an empirical assessment of the existing structure of PTAs, or whether it is meant to represent a prescriptive statement about the need to include direct investor-State dispute settlement. Thus, these two aspects will be briefly addressed in the following sections.

III. EMPIRICAL ASSESSMENT: ARE INVESTMENT CHAPTERS OF PREFERENTIAL TRADE AGREEMENTS DEVOID OF INVESTOR-STATE ARBITRATION?

A brief overview of PTAs containing investment chapters demonstrates that investor-State arbitration may very well be included and is in fact often included in PTAs. A prime example is the U.S. FTA program. These PTAs often contain market access and classic investment-protection standards. Their investment chapters are typically based upon the NAFTA Chapter 11 model,[11] and, more recently, upon the blueprint provided by the 2004 U.S. Model BIT.[12] They all contain investor-State arbitration with the exception of the Australia–U.S. FTA.[13] The direct link to NAFTA as a model can be clearly seen, for instance, in the Dominican Republic–Central American FTA (DR–CAFTA), which provides for ICSID,[14] ICSID Additional Facility[15] or UNCITRAL[16]

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[10] *See* I. Shihata, "Towards a Greater Depoliticization of Investment Disputes: The Roles of ICSID and MIGA," 1 ICSID Rev.—FILJ 1 (1986).

[11] NAFTA, *supra* note 3, ch. 11. *See also* M. Kinnear, A. Bjorklund and J. Hannaford, Investment Disputes Under NAFTA: An Annotated Guide to NAFTA Chapter 11 (2006); Ch. Thomas, Investor-State Arbitration under NAFTA Chapter 11, 37 Can. Y.B. Int'l L. 99 (1999).

[12] 2004 U.S. Model BIT, *reprinted in* R. Dolzer and Ch. Schreuer, Principles of International Investment Law 385 (2008).

[13] *See* Australia–U.S. FTA (2004).

[14] Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention) (Mar. 18, 1965) 575 U.N.T.S. 159, 4 I.L.M. 532 (1965).

[15] Additional Facility for the Administration of Conciliation, Arbitration and Fact-Finding Proceedings, ICSID Doc. 11 (1979), *available at* http://icsid.worldbank.org.

[16] United Nations Commission on International Trade Law (UNCITRAL) Arbitration Rules, U.N. GAOR, 31st Sess., suppl. no. 17, ch. V, sec. C, U.N. Doc. A/31/17 (Dec. 15, 1976), 15 I.L.M. 701 (1976), *available at* http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1976Arbitration_rules.html.

arbitration.[17] In addition, DR–CAFTA contains detailed provisions concerning *amicus curiae* submissions[18] as well as transparency[19] and consolidation.[20] Similar provisions can be found in many other U.S. PTAs.

The most conspicuous absence of investor-State arbitration is found in the 2004 Australia–U.S. FTA. It has been remarked that the absence of this dispute settlement form may have been inspired by the parties' belief that the legal protection offered by their respective national courts would be sufficient for investment disputes.[21] It may be added that the U.S. in particular, having been named a respondent in numerous NAFTA cases,[22] may have had some interest in reducing the likeliness of being sued in investment arbitration by Australian investors. Needless to say that the Australian side also may not have been too enthusiastic about the prospect of being named a respondent in investment cases. It should be mentioned, however, that even the Australia–U.S. FTA is not totally silent on the matter of investor-State arbitration. Instead, while not explicitly providing for such dispute settlement, it acknowledges the potential need for it in some situations and provides for State-to-State consultations "with a view towards allowing such a claim and establishing such procedures."[23]

The U.S. is not alone in including investor-State arbitration in the investment chapters of its PTAs. For instance, among the more recent Japanese PTAs, the

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[17] DR–CAFTA, art. 10.16(3) (Aug. 5, 2004), *available at* http://www.ustr.gov/trade-agreements/free-trade-agreements/cafta-dr-dominican-republic-central-america-fta/final-text.

[18] *Id.* art. 10.20.

[19] *Id.* art. 10.21.

[20] *Id.* art. 10.25.

[21] *Cf.* UNCTAD, Investment Provisions in Economic Integration Agreements, U.N. Doc. UNCTAD/ITE/IIT/2005/10, at 116 (2006), *available at* http://www.unctad.org/en/docs/iteiit200510_en.pdf ("It appears from the language that both parties believed that an investor-State dispute resolution mechanism was unnecessary, presumably in the light of the nature of the legal system in the two countries, and thus both parties preferred that disputes be submitted to domestic courts.").

[22] *See* U.S. Department of State, NAFTA Investor-State Arbitrations webpage, http://www.state.gov/s/l/c3439.htm.

[23] Australia–U.S. FTA, *supra* note 13, art. 11.16 ("Consultations on Investor-State Dispute Settlement") states the following:

> 1. If a Party considers that there has been a change in circumstances affecting the settlement of disputes on matters within the scope of this Chapter and that, in light of such change, the Parties should consider allowing an investor of a Party to submit to arbitration with the other Party a claim regarding a matter within the scope of this Chapter, the Party may request consultations with the other Party on the subject, including the development of procedures that may be appropriate. On such a request, the Parties shall promptly enter into consultations with a view towards allowing such a claim and establishing such procedures.
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> 2. For greater certainty, nothing in this Article prevents a Party from raising any matter arising under this Chapter pursuant to the procedures set out in Chapter 21 (Institutional Arrangements and Dispute Settlement). Nor does anything in this Article prevent an investor of a Party from submitting to arbitration a claim against the other Party to the extent permitted under that Party's law.

agreements with Mexico,[24] Malaysia,[25] and Chile[26] all contain investor-State arbitration, while the one with the Philippines[27] provides for further negotiations on the issue of investor-State dispute settlement.

Similarly, Singapore's PTAs also contain investor-State arbitration. A good example is provided by Article 48 of the EFTA–Singapore FTA, which contains the usual dispute settlement clause providing for ICSID, ICSID Additional Facility or UNCITRAL arbitration after consultations and a waiting period of six months, with the only practical drawback being that both parties to the dispute must consent to the arbitration.[28]

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[24] Agreement Between Japan and the United Mexican States for the Strengthening of the Economic Partnership, art. 76 (Sept. 17, 2004) (hereinafter "Japan–Mexico FTA"), *available at* http://www.sice.oas.org/Trade/MEX_JPN_e/JPN_MEX_e.asp#Section2*.

[25] Agreement Between the Government of Japan and the Government of Malaysia for an Economic Partnership, art. 85 ("Settlement of Investment Disputes between a Country and an Investor of the Other Country") (Dec. 13, 2005), *available at* http://www.mofa.go.jp/region/asia-paci/malaysia/epa/content.pdf.

[26] Agreement Between Japan and the Republic of Chile for a Strategic Economic Partnership, art. 89 (Mar. 27, 2007), *available* at http://www.sice.oas.org/Trade/CHL_JPN/CHL_JPN_text_e.asp#s82.

[27] Agreement between Japan and the Republic of the Philippines for an Economic Partnership, art. 107 ("Further Negotiation") (Sept. 9, 2006), *available at* http://www.mofa.go.jp/region/asia-paci/philippine/epa0609/main.pdf. The text of the Article reads as follows:

> 1. The Parties shall enter into negotiations after the date of entry into force of this Agreement to establish a mechanism for the settlement of an investment dispute between a Party and an investor of the other Party.
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> 2. In the absence of the mechanism for the settlement of an investment dispute between a Party and an investor of the other Party, the resort to international conciliation or arbitration tribunal is subject to mutual consent of the parties to the dispute. This means that the disputing Party may, at its option or discretion, grant or deny its consent in respect of each particular investment dispute and that, in the absence of the express written consent of the disputing Party, an international conciliation or arbitration tribunal shall have no jurisdiction over the investment dispute involved.

[28] EFTA–Singapore FTA, art. 48 ("Disputes Between an Investor and a Party") (June 26, 2002). The Article provides as follows:

> 1. If an investor of a Party considers that a measure applied by another Party is inconsistent with an obligation of this Chapter, thus causing loss or damage to him or his investment, he may request consultations with a view to solving the matter amicably.
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> 2. Any such matter which has not been settled within a period of six months from the date of request for consultations may be referred to the courts or administrative tribunals of the Party concerned or, if both parties to the dispute agree, be submitted to one of the following:
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> a) arbitration under the Convention on the Settlement of Investment Disputes between States and Nationals of other States (the "ICSID Convention"), if this Convention is available;
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> b) conciliation or arbitration under the Additional Facility Rules of the International Centre for the Settlement of Investment Disputes;
>
> c) arbitration under the Arbitration Rules of the United Nations Commission on International Trade Law.
>
> 3. A Party may conclude contractual agreements with investors of another Party giving its unconditional and irrevocable consent to the submission of all or certain types of disputes to international conciliation or arbitration in accordance with paragraph 2 above. Such agreements may be notified to the Depositary of this Agreement.

The most important set of PTAs which do not contain investor-State arbitration are the FTAs of the European Community (EC) which are traditionally limited to trade issues. Though such EC PTAs have gradually added the topic of trade in services, through rules on establishment and provision of services, etc., to the core trade in goods coverage, they usually fall short of genuine investment coverage. The main reason why these European PTAs do not contain any post-establishment rules is found in the division of powers between the Community and its member States. At least before the entry-into-force of the Lisbon Treaty,[29] the power to enter into agreements regulating the post-establishment treatment of investments was largely considered to be within the competence of the member States.[30] Since EC PTAs focused on the liberalization and not on the protection of investment, European PTAs with investment-relevant rules did not contain investor-State dispute settlement rules.

The lack of a full investment competence of the EC did not imply, however, that investment rules could not be agreed upon in treaties based on both EC and member States' powers. This is the typical feature of so-called mixed agreements.[31] In fact, the conclusion of the Energy Charter Treaty (ECT)[32] in 1994, as such a mixed agreement by the EC and its member States, on the

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[29] Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community (Dec. 13, 2007), 2007 O.J. (C 306) 1.

[30] On the issue of the new post-Lisbon EU powers on investment *see* M. Bungenberg, "Centralizing European BIT Making under the Lisbon Treaty," Draft Paper prepared for the 2008 Biennial Interest Group Conference in Washington, D.C., November 13–15, 2008, *available at* http://www.asil.org/files/ielconferencepapers/bungenberg.pdf; J. Ceyssens, "Towards a Common Foreign Investment Policy?—Foreign Investment in the European Constitution," 32 L. Issues Econ. Integration 259 (2005); J. Griebel, "Überlegungen zur Wahrnehmung der neuen EU-Kompetenz für ausländische Direktinvestitionen nach Inkrafttreten des Vertrags von Lissabon," Recht der Internationalen Wirtschaft 469 (2009); J. Karl, "The Competence for Foreign Direct Investment: New Powers for the European Union?", 5 J. World Investment & Trade 413 (2004); N. Maydell, "The European Community's Minimum Platform on Investment or the Trojan Horse of Investment Competence," *in* A. Reinisch and Ch. Knahr (eds.), International Investment Law in Context 73 (2008); L. Mola, "Which Role for the EU in the Development of International Investment Law," Soc'y Int'l Econ. Law (SIEL) Inaugural Conference 2008, Online Proceedings Working Paper no. 26/08 (July 2, 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1154583; W. Shan, "Towards a Common European Community Policy on Investment Issues," 2 J. World Investment & Trade 603 (2001); Ch. Tietje, "Die Außenwirtschaftsverfassung der EU nach dem Vertrag von Lissabon," Beiträge zum Transnationalen Wirtschaftsrecht no. 83 (2009); St. Woolcock, "The Potential Impact of the Lisbon Treaty on EU External Trade Policy," Swed. Inst. Eur. Pol'y Studies (SIEPS), European Policy Analysis no. 8 (June 2008); A. Reinisch, "The Division of Powers between the EU and its Member States 'after Lisbon,'" *in* M. Bungenberg, J. Griebel and St. Hindelang (eds.), Eur. Y.B. Int'l Econ. L. (Special Issue: International Investment Law and EU Law) (forthcoming 2011).

[31] *See* D. O'Keeffe and H. Schermers (eds.), Mixed Agreements (1983); R. Wessel, "The EU as a Party to International Agreements: Shared Competences, Mixed Responsibilities," *in* A. Dashwood and M. Maresceau (eds.), Law and Practice of EU External Relations: Salient Features of a Changing Landscape 152 (2008).

[32] Energy Charter Treaty, Annex 1 to the Final Act of the Conference on the European Energy Charter (Dec. 17, 1994), 34 I.L.M. 381 (1995).

one hand, and many other European States, on the other hand, demonstrates that a full-fledged investment agreement may be concluded by the EC.[33] What is most significant for present purposes is the fact that this investment treaty also contains investor-State arbitration. The ECT's dispute settlement article provides for arbitration under ICSID, ICSID Additional Facility, UNCITRAL or Stockholm Chamber of Commerce arbitration rules in case of "disputes between a Contracting Party and an Investor of another Contracting Party."[34] Since the European Community is an ECT contracting party, it may be a party to investment arbitration under the ECT. This possibility has been acknowledged by the EC's statement that it will internally clarify with its member States who should be the proper respondent in a case brought by an investor.[35]

Numerous ECT cases[36] demonstrate that the option of investor-State

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[33] *See* E. Paasivirta, "The European Union and the Energy Sector: The Case of the Energy Charter Treaty," *in* M. Koskenniemi (ed.), International Law Aspects of the European Union 198 (1998); Th. Wälde (ed.), The Energy Charter Treaty: An East-West Gateway for Investment & Trade (1996).

[34] ECT, *supra* note 32, art. 26.

[35] Statement submitted by the European Communities to the Secretariat of the Energy Charter Treaty pursuant to Article 26(3)(b)(ii) of the Energy Charter Treaty, Final Act of the European Energy Charter Conference (Dec. 17, 1994), 1998 O.J. (L 69) 115 ("The Communities and the Member States will, if necessary, determine among them who is the respondent party to arbitration proceedings initiated by an Investor of another Contracting Party. In such case, upon the request of the Investor, the Communities and the Member States concerned will make such determination within a period of 30 days.")

[36] *AES Summit Generation Ltd. v. Hungary*, ICSID Case No. ARB/01/4, Order of the Tribunal for Discontinuance of the Proceeding (Jan. 3, 2002) (settlement agreed by the parties and proceeding discontinued at their request); *AES Summit Generation Ltd. and AES-Tisza Erőmű Kft. v. Republic of Hungary*, ICSID Case No. ARB/07/22 (pending); *Alapli Elektrik B.V. v. Republic of Turkey*, ICSID Case No. ARB/08/13 (pending); *Alstom Power Italia SpA, Alstom SpA v. Mongolia*, ICSID Case No. ARB/04/10, Order of the Tribunal Taking Note of the Discontinuance of the Proceeding (Mar. 13, 2006) (settlement agreed by the parties and proceeding discontinued at their request); *Azpetrol Int'l Holdings B.V., Azpetrol Group B.V. and Azpetrol Oil Services Group B.V.* v. *Azerbaijan*, ICSID Case No. ARB/06/15, Award (Sept. 8, 2009); *Barmek Holding A.S. v. Azerbaijan*, ICSID Case No. ARB/06/16, Award (Sept. 28, 2009) (settlement agreed by the parties and settlement recorded at their request in the form of an award); *Cementownia "Nowa Huta" S.A. v. Republic of Turkey*, ICSID Case No. ARB(AF)/06/2, Award (Sept. 17, 2009); *EDF International S.A. v. Republic of Hungary* (UNCITRAL) (pending); *Electrabel S.A. v. Republic of Hungary*, ICSID Case No. ARB/07/19 (pending); *Europe Cement Investment and Trade S.A. v. Republic of Turkey*, ICSID Case No. ARB(AF)/07/2, Award (Aug. 13, 2009); *EVN AG* v. *The Former Yugoslav Republic of Macedonia*, ICSID Case No. ARB/09/10 (pending); *Hrvatska Elektropriveda d.d. (HEP) v. Republic of Slovenia*, ICSID Case No. ARB/05/24, Decision on the Treaty Interpretation Issue and Individual Opinion (June 12, 2009); *Hulley Enterprises Ltd. v. Russian Federation*, PCA Case No. AA 226 (UNCITRAL), Interim Award on Jurisdiction and Admissibility (Nov. 30, 2009); *Ioannis Kardassopoulos v. Georgia*, ICSID Case No. ARB/05/18, Decision on Jurisdiction (July 6, 2007); *Libananco Holdings Co. Ltd. v. Republic of Turkey*, ICSID Case No. ARB/06/8, Decision on Preliminary Issues (June 23, 2008); *Liman Caspian Oil B.V. and NCL Dutch Investment B.V. v. Republic of Kazakhstan*, ICSID Case No. ARB/07/14 (pending); *Limited Liability Company Amto v. Ukraine*, SCC Case No. 080/2005, Final Award (Mar. 26, 2008); *Mercuria Energy Group Ltd. v. Republic of Poland*, Arbitration Institute of the SCC (pending); *Nykomb Synergetics Technology Holding AB v. Latvia*, SCC Case No. 118/2001, Award (Dec. 16, 2003); *Plama Consortium Ltd. v. Bulgaria*, ICSID Case No. ARB/03/24, Award (Aug. 27, 2008); *Petrobart Ltd. v. Kyrgyzstan*, SCC Case No. 126/2003, Award (Mar. 29, 2005); *Vattenfall AB, Vattenfall*

arbitration under this international investment agreement is a real and effective one. Although to date no cases have been brought against the EC, it is already a legal possibility. It also demonstrates that there is a possibility for the EU to include such investor-State dispute settlement options should it choose to exercise its new foreign direct investment powers under Articles 206 and 207 of the post-Lisbon Treaty on the Functioning of the European Union (TFEU).[37] It would appear that the crucial question is less about the legal options available to the EU. Rather, it seems that it will mainly depend on the political will of the EU whether to include investor-State arbitration in future European PTAs. This question, of course, should be seen in a broader prescriptive context which considers the advantages and disadvantages of including investor-State arbitration in PTAs in general.

IV. PRESCRIPTIVE APPRAISAL: DO INVESTMENT CHAPTERS OF PREFERENTIAL TRADE AGREEMENTS REQUIRE INVESTOR-STATE ARBITRATION?

The following thoughts about the pros and cons of investor-State arbitration are by no means exhaustive. However, it appears appropriate to consider them when reflecting on its inclusion or omission in such agreements.

A. Policy Reasons against Investor-State Arbitration

The growth of investment arbitration over the last two decades—with an exponential increase over the last ten years—has brought to the fore a number of deficiencies and problematic aspects. While some commentators question the legitimacy of the entire system[38] and others debate a potential "backlash"

Europe AG, Vattenfall Europe Generation AG v. Federal Republic of Germany, ICSID Case No. ARB/09/6 (pending); *Veteran Petroleum Ltd. v. Russian Federation*, PCA Case No. AA 228 (UNCITRAL), Interim Award on Jurisdiction and Admissibility (Nov. 30, 2009); *Yukos Universal Ltd. v. Russian Federation*, PCA Case No. AA 227 (UNCITRAL), Interim Award on Jurisdiction and Admissibility (Nov. 30, 2009).

[37] Article 207(1) of the Consolidated Version of the Treaty on the Functioning of the European Union (TFEU), O.J. (C 115) 47 of May 9, 2008, states (with emphasis added):

> The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, *foreign direct investment*, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to be taken in the event of dumping or subsidies. The common commercial policy shall be conducted in the context of the principles and objectives of the Union's external action.

[38] G. Van Harten, Investment Treaty Arbitration and Public Law (2007).

against investment arbitration,[39] some ponder the need to improve aspects of the current way in which investment disputes are arbitrated and would regard the ascertained deficiencies as natural concomitants of any system of dispute settlement that is coming of age. Indeed, it may be premature to assess whether, and to what extent, investment arbitration has a future and how far it has to adapt to current challenges.[40] Nevertheless, when discussing the policy option of including investor-State arbitration in PTAs it appears sensible to face the major arguments currently raised against such dispute settlement.

It is often argued that the investment arbitration system based on a myriad of BITs potentially leads to multiple proceedings with a number of ensuing risks such as inconsistent or even contradictory awards, forum shopping by claimants relying on the most advantageous BIT, multiple recoveries by different investors, etc. Indeed, there have been a few prominent examples where investors managed to pursue investment arbitration before different tribunals established according to different BITs, applicable to their different corporate emanations. The *Lauder/CME* Awards[41] are still the most telling example because the two arbitral tribunals came to different conclusions, which taught host countries the simple, but painful lesson that it is not enough to win one case to escape unharmed. Rather, host States have to successfully defend all parallel cases brought against them, while investors need to win only one.

The potential inconsistencies of the outcomes of parallel cases, or even cases that are not directly related to each other but address similar legal issues, is certainly a serious problem because it may lead to a decrease of the trust in the arbitration system required for its acceptance by investors and States.[42] It is hard to see, however, why this danger should lead to a total abolition of investor-State arbitration. The threat of inconsistent outcomes is one that appertains to any dispute settlement system that produces a certain number of decisions, and it increases with each decision rendered. Legal systems have adopted different responses; on the domestic level these have been mostly appeals procedures.

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[39] M. Waibel et al. (eds.), The Backlash Against Investment Arbitration: Perceptions and Reality (2010).

[40] A. Reinisch, "The Future of Investment Arbitration," *in* Christina Binder et al. (eds.), International Investment Law for the 21st Century—Essays in Honour of Christoph Schreuer 894 (2009).

[41] *See Lauder v. The Czech Republic* (UNCITRAL), Final Award (Sept. 3, 2001), 9 ICSID Rep. 66 (2006), 14 World Trade & Arb. Materials 35 (2002); *CME Czech Republic B.V. v. The Czech Republic* (UNCITRAL), Partial Award (Sept. 13, 2001), 9 ICSID Rep. 121 (2006), 14 World Trade & Arb. Materials 109 (2002); *CME Czech Republic B.V. v. The Czech Republic* (UNCITRAL), Final Award (Mar. 14, 2003) (hereinafter *CME v. Czech Republic* Final Award), 9 ICSID Rep. 264 (2006); on this latter case *see also* C. Brower and J. Sharpe, "Multiple and Conflicting International Arbitral Awards," 4 J. World Invest. 211 (2003); A. Reinisch, "The Use and Limits of *Res Judicata* and *Lis Pendens* as Procedural Tools to Avoid Conflicting Dispute Settlement Outcomes," 3 L. & Practice Int'l Cts. & Tribs. 37 (2004).

[42] *See* A. Reinisch, The Future of Investment Arbitration, *supra* note 40, at 905.

But also in international law the introduction of a WTO Appellate Body by the Marrakesh Agreement's DSU with the task of hearing appeals from panel cases[43] served this purpose, expressed in the DSU as "providing security and predictability to the multilateral trading system."[44]

The debate within ICSID concerning the potential adoption of an appellate mechanism for investment arbitration[45] demonstrates that, though hardly feasible from a political standpoint,[46] such a technical solution is legally possible.[47] And the continued discussion of such a possibility pursuant to some investment treaties[48] shows that the idea is still alive. Another successful practical approach employed by some tribunals in order to prevent divergent outcomes lies in the consolidation of related proceedings.[49] This idea has been expressly incorporated in a number of more recent BITs[50] and investment chapters of PTAs.[51]

In the meantime, however, practice teaches that in spite of some divergences—as in the interpretation of umbrella clauses[52] or the assessment of emergency

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[43] WTO DSU, *supra* note 6, art. 17(1). *See also* G. Sacerdoti, "Appeal and Judicial Review in International Arbitration and Adjudication: The Case of WTO Appellate Review," *in* E.-U. Petersmann (ed.), International Trade Law and the GATT/WTO Dispute Settlement System 247 (1997).

[44] WTO DSU, *supra* note 6, art. 3(2).

[45] Possible Improvements of the Framework for ICSID Arbitration, ICSID Secretariat Discussion Paper (Oct. 26, 2004), *available at* http://icsid.worldbank.org.

[46] Ch. Schreuer et al., The ICSID Convention: A Commentary 1105 (2nd ed. 2009).

[47] *See also* the discussion in K. Sauvant and M. Chiswick-Patterson (eds.), Appeals Mechanism in International Investment Disputes (2008); A. Qureshi, "An Appellate System in International Investment Arbitration?", *in* P. Muchlinski, F. Ortino and Ch. Schreuer (eds.), The Oxford Handbook of International Investment Law 1154 (2008).

[48] *See, e.g.*, DR–CAFTA, *supra* note 17, annex 10-F (establishing a negotiation group for an appellate body).

[49] *See, e.g.*, *Canfor Corp v. U.S. and Tembec et al. v. U.S. and Terminal Forest Products Ltd. v. U.S. (NAFTA), Order of the* Consolidation Tribunal (Sept. 7, 2005), *available at* http://naftaclaims.com/Disputes/USA/Softwood/Softwood-ConOrder.pdf; *Canfor Corp. v. U.S.* and *Terminal Forest Products Ltd. v. U.S.* (NAFTA), Decision on Preliminary Question (June 6, 2006), *available at* http://naftaclaims.com/Disputes/USA/Softwood/NAFTA-Softwood_Consolidation-Preliminary_Decision-6_June_2006.pdf.

[50] *See, e.g.*, Article 33(1) of the 2004 U.S. Model BIT, *supra* note 12, which states:

> Where two or more claims have been submitted separately to arbitration under Article 24(1) and the claims have a question of law or fact in common and arise out of the same events or circumstances, any disputing party may seek a consolidation order in accordance with the agreement of all the disputing parties ….

[51] *See, e.g.*, Article 83(1) of the Japan–Mexico FTA, *supra* note 24 ("When a disputing party considers that two or more claims submitted to arbitration ... have a question of law or fact in common, the disputing party may seek a consolidation order in accordance with the terms of paragraphs 2 through 9 below.").

[52] Contrast *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/01/13, Decision on Jurisdiction (Aug. 6, 2003), 18 ICSID Rev.—FILJ 301 (2003); 42 I.L.M. 1290 (2003), with *SGS Société Générale de Surveillance S.A. v. Republic of the Philippines*, ICSID Case No. ARB/02/6, Decision on Jurisdiction (Jan. 29, 2004), 8 ICSID Rep. 515 (2005). While the *SGS v. Pakistan* Tribunal held that via an umbrella clause "breaches of a contract [are not] automatically 'elevated' to the level of breaches of international law," the *SGS v. Philippines* Tribunal found that that an umbrella clause "makes it a breach of the BIT for the host State to fail to observe binding commitments." A number

situations[53]—tribunals are not "running wild."[54] Instead, they generally attempt to avoid inconsistencies rather carefully by "relying" on, or rather taking into consideration, previous decisions on similar points. Thus, a *jurisprudence constante* or *de facto* case law[55] develops which is, in fact, surprisingly consistent, given the fact that each tribunal is only empowered to decide one single case. The fact that many investment cases involving large sums of money are brought by a highly sophisticated and specialized bar that often proffers vast exhibits of legal authorities is certainly a helpful element in this process.

Another point of criticism often raised against investment arbitration relates to the lack of transparency of its proceedings. Sometimes the allegations that investment arbitration would constitute a system of secret justice display a certain conspiracy theory quality.[56] Still, the truth of the matter is that depending on

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of tribunals followed the *SGS v Pakistan* approach. *Cf. El Paso Energy Int'l Co. v. The Argentine Republic*, ICSID Case No. ARB/03/15, Decision on Jurisdiction, para. 82 (Apr. 27, 2006); *BP America Production Co. et al. v. The Argentine Republic*, ICSID Case No. ARB/04/8, Decision on Preliminary Objections, para. 113 (July 27, 2006). Others endorsed the *SGS v Philippines* approach. *Cf. Eureko B.V. v. Republic of Poland*, Partial Award, para. 257 (Aug. 19, 2005).

[53] Contrast *CMS Gas Transmission Co. v. The Argentine Republic*, ICSID Case No. ARB/01/8, Award, paras. 320–321 (May 12, 2005), 44 I.L.M. 1205 (2005); *Enron Creditors Recovery Corp. (formerly Enron Corp.) and Ponderosa Assets, L.P. v. Argentine Republic,* ICSID Case No. ARB/01/3, Award, para. 31 (May 22, 2007); *Sempra Energy Int'l v. The Argentine Republic*, ICSID Case No. ARB/02/16, Award, para. 355 (Sept. 28, 2007); *BG Group Plc v. Argentina* (UNCITRAL), Award (Dec. 24, 2007), with *LG&E Energy Corp., LG&E Capital Corp. and LG&E Int'l Inc. v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability, para. 257 (Oct. 3, 2006), 46 I.L.M. 40 (2007); *Continental Casualty Co. v. Argentine Republic*, ICSID Case No. ARB/03/9, Award (Sept. 5, 2008). *See also* A. Bjorklund, "Emergency Exceptions: State of Necessity and Force Majeure," *in* Muchlinski, Ortino and Schreuer, Oxford Handbook, *supra* note 47, at 459; W. Burke-White and A. von Staden, "Investment Protection in Extraordinary Times: Interpreting Non-Precluded Measures Provisions," 48 VA J. Int'l L. 307 (2007); T. Gazzini, "Necessity in International Investment Law: Some Critical Remarks on CMS v Argentina," 26 J. Energy & Nat. Res. L. 450 (2008); Ch. Leben, "L'Etat de nécessité dans le droit international de l'investissement," 349 Gazette de Palais 19 (2005); A. Reinisch, "Necessity in International Investment Arbitration—An Unnecessary Split of Opinions in Recent ICSID Cases? Comments on *CMS* and *LG&E*," 8 J. World Investment & Trade 191 (2007); St. Schill, "International Investment Law and the Host State's Power to Handle Economic Crises," 24 J. Int'l Arb. 265 (2007); M. Waibel, "Two Worlds of Necessity in ICSID Arbitration: *CMS* and *LG&E*," 20 Leiden J. Int'l L. 637 (2007).

[54] *See* the famous treatise of Rasmussen on the ECJ's gouvernement des juges, H. Rasmussen, On Law and Policy in the European Court of Justice: A Comparative Study in Judicial Policymaking 81 (1986). *See, however*, M. Cappelletti, "*Is the European Court of Justice Running Wild?"*, 12 Eur. L. Rev. 3 (1982).

[55] *See* A. Bjorklund, "Investment Treaty Arbitral Decisions as Jurisprudence Constante," *in* C. Picker, I. Bunn and D. Arner (eds.), International Economic Law: The State and Future of the Discipline 265 (2008); G. Kaufmann-Kohler, "Arbitral Precedent: Dream, Necessity, or Excuse," 23 Arb. Int'l 357 (2007), A. Reinisch, "The Role of Precedent in ICSID Arbitration," *in* Austrian Arb. Y.B. 495 (2008).

[56] *See* the famous New York Times article on NAFTA Chapter 11 arbitration, "NAFTA's Powerful Little Secret; Obscure Tribunals Settle Disputes, but Go Too Far, Critics Say," N.Y. Times (Mar. 11, 2001), which describes NAFTA tribunals in the following way:

> Their meetings are secret. Their members are generally unknown. The decisions they reach need not be fully disclosed. Yet the way a small group of international tribunals handles disputes between investors and foreign governments has led to national laws being

the chosen arbitration rules there are different degrees of transparency currently applicable in investment arbitration. While the institution of all ICSID cases is made public on the Centre's homepage and while most awards are now equally published, this is not necessarily so with many investment cases arbitrated under the UNCITRAL Rules[57] where the parties are free and actually often opt for confidentiality not only of the final award, but also of the proceedings themselves.

Advocates of a purely inter-State dispute settlement system also for investment cases may point to the virtues of WTO and regional trade dispute settlement such as NAFTA where all procedures and their outcomes, in the cases of NAFTA sometimes even substantial parts of the pleadings,[58] are readily available to the public.[59] One should not overlook, however, that also in the field of trade dispute settlement this is the result of a gradual development. The original GATT dispute settlement in the form of trade diplomacy was a highly informal and confidential process. Until the early 1990s it was often very difficult to obtain GATT Panel rulings from the trade departments of foreign ministries and other sources within a reasonable time. It is clear that the technological development of the internet and other means of communication have played a primary role in increasing transparency here. Similar to the gradual, panel-driven development in trade dispute settlement,[60] investment tribunals have started accepting submissions by non-parties to ICSID or non-ICSID proceedings.[61]

In addition, however, one should not overlook the simple fact that confidentiality vs. transparency is a policy matter that may be taken into account in any dispute settlement system. As there is no inherent transparency

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revoked, justice systems questioned and environmental regulations challenged. And it is all in the name of protecting the rights of foreign investors under the North American Free Trade Agreement.

[57] UNCITRAL Arbitration Rules, *supra* note 16.

[58] In addition to rulings of NAFTA tribunals, even pleadings in investment claims brought against the U.S. are publicly available at the U.S. State Department's website: Cases Filed Against the U.S., http://www.state.gov/s/l/c3741.htm.

[59] *See* NAFTA Free Trade Comm'n, Notes of Interpretation of Certain Chapter 11 Provisions, para. A(1) (July 31, 2001), *available at* http://www.state.gov/s/l/c3439.htm ("Nothing in the NAFTA imposes a general duty of confidentiality on the disputing parties to a Chapter Eleven arbitration, and, … precludes the Parties from providing public access to documents submitted to, or issued by, a Chapter Eleven tribunal.").

[60] *See* A. Reinisch and Ch. Irgel, "The Participation of Non-governmental Organizations (NGOs) in the WTO Dispute Settlement System," 1 Non-State Actors & Int'l L. 127 (2001).

[61] *See, e.g.*, *Suez, Sociedad General de Aguas de Barcelona, S.A. and Vivendi Universal, S.A. v. Argentine Republic*, ICSID Case No. ARB/03/19, Order in Response to a Petition for Transparency and Participation as Amicus Curiae (May 19, 2005), *available at* http://ita.law.uvic.ca/documents/suezMay19EN.pdf; *Suez, Sociedad General de Aguas de Barcelona S.A. and Interagua Servicios Integrales de Agua S.A.* v. *Argentine Republic*, ICSID Case No. ARB/03/17, Order in Response to a Petition for Participation as Amicus Curiae (Mar. 17, 2006), *available at* http://ita.law.uvic.ca/documents/Aguas-Amici-17March2006.pdf.

in trade dispute settlement, there is no inherent confidentiality in investment arbitration.[62] The 2006 amendments to the ICSID Arbitration Rules have demonstrated that investment arbitration may incorporate a high level of transparency not only as regards the public availability of its awards, but also with regard to public or semi-public hearings, the permission of *amicus curiae* briefs, etc.[63]

If PTA negotiators consider transparency an important issue, they are free to include the required provisions. As a matter of fact, many of the more recent agreements seem to reflect the growing awareness that investment arbitration is not merely a matter between two parties but instead may have broader implications, in particular for the public in the host State, that require a minimum level of transparency.[64]

A further argument frequently raised against investor-State arbitration by NGOs and willingly echoed by States relates to the potential financial risks of investment arbitration. The sheer amount of compensation or damages resulting from investment awards may have devastating effects on the often already-weak budgetary situation in a host country. Extremely large awards as in the case of *CME v Czech Republic*[65] or *CSOB v Slovak Republic*[66] in the hundreds of millions U.S. dollars or Euros certainly speak for themselves. It is of course true that in the absence of investor-State arbitration these awards would not have been rendered. However, it is not that clear whether the respondent States would always have gotten away financially unaffected. The traditional system of diplomatic protection may lead to similar financial effects where home States insist on making good the harm suffered by their investors. It may even lead to unforeseen collateral damage where they resort to economic sanctions. The total financial consequences of such measures often exceed the original amount in dispute. Also where investors do not receive the support of their home States, host States will not always go unpunished. Other investors may chose to avoid

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[62] On this issue, *see generally* G. Born and E. Shenkman, "Confidentiality and Transparency in Commercial and Investors State International Arbitration," *in* C. Rogers and R. Alford (eds.), The Future of Investment Arbitration 5 (2009).

[63] Amendments to the ICSID Rules and Regulations and the Additional Facility Rules (effective Apr. 10, 2006), *available at* http://icsid.worldbank.org. *See also* Ch. Knahr, "Transparency, Third Party Participation and Access to Documents in International Investment Arbitration," 23 Arb. Int'l 327 (2007); A. Antonietti, "The 2006 Amendments of the ICSID Rules and Regulations and the Additional Facility Rules," 21 ICSID Rev.—FILJ 427 (2006).

[64] *See, e.g.*, Article 39 (Submissions by a Non-Disputing Party) of the 2004 Canadian Model BIT, *available at* http://ita.law.uvic.ca/documents/Canadian2004-FIPA-model-en.pdf (providing for *amicus curiae* briefs).

[65] *CME v. Czech Republic* Final Award, *supra* note 41.

[66] *Československa obchodní Banka, a.s. v. The Slovak Republic*, ICSID Case No. ARB/97/4, Final Award (Dec. 29, 2004).

the actual or perceived grave political risk of investing in host States which are unavailable for investment arbitration and invest elsewhere. While the relation between BIT protection and actual investment remains a contested issue,[67] it is not implausible to imagine a deteriorated investment climate having a deterring effect on potential investors.[68]

Finally, opponents of investor-State arbitration often lament the loss of control of States over this form of dispute settlement, as opposed to the traditional inter-State dispute settlement system where they fully remain in the driver's seat. Since investor-State arbitration is usually triggered by private parties against States, the latter find themselves regularly acting as respondents at the receiving end. Though most forms of mixed arbitration provide for the possibility of proceedings instituted by States against private investors, this rarely happens.[69] In the current debate on investment protection as an integral part of larger PTAs, many States may perceive another chance to regain full control over economic disputes by emphasizing the inter-State character of trade disputes. In this context, the debate within the WTO concerning the Singapore issue of investment[70] appears quite illustrative. Though carefully worded in diplomatic phrases, the Secretariat's summary of the discussions demonstrates the rather reserved attitude of many States when it comes to investor-State arbitration.[71]

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[67] *See* M. Hallward-Driemeier, "Do Bilateral Investment Treaties Attract FDI? Only a Bit … and They Could Bite," World Bank Policy Research Working Paper no. WPS 3121 (World Bank 2003); J. Salacuse and N. Sullivan, "Do BITs Really Work? An Evaluation of Bilateral Investment Treaties and Their Grand Bargain," 46 Harv. Int'l L. J. 67 (2005); E. Neumayer and L. Spess, "Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?", 33 World Dev. 1567 (2005).

[68] The preamble of the ICSID Convention, *supra* note 14, specifically considers "the need for international cooperation for economic development, and the role of private international investment therein." According to the Report of the Executive Directors on the Convention, "adherence to the Convention by a country would provide additional inducement and stimulate a larger flow of private international investment into its territories, which is the primary purpose of the Convention." 1 ICSID Rep. 25 (1993). *See also* Schreuer et al., The ICSID Convention: A Commentary, *supra* note 46, at 4, preamble, para. 11; A. Broches, "The Convention on the Settlement of Investment Disputes between States and Nationals of Other States," 136 Recueil des Cours 331, 342 (1972-II); I. Shihata, "Promotion of Foreign Direct Investment—A General Account, with Particular Reference to the Role of the World Bank Group," 6 ICSID Rev.—FILJ 484 (1991).

[69] To date only three ICSID cases have been instituted by States: *Gabon v. Société Serete S.A.*, ICSID Case No. ARB/76/1, Order Taking Note of the Discontinuance Issued by the Tribunal (Feb. 27, 1978) (settlement agreed by the parties and proceeding discontinued at their request); *Tanzania Electric Supply Co. Ltd. v Independent Power Tanzania Ltd.*, ICSID Case No ARB/98/8, Award (July 12, 2001), interpretation proceedings pending; *Government of the Province of East Kalimantan v. PT Kaltim Prima Coal and Others*, ICSID Case No. ARB/07/3, Award (Dec. 28, 2009). Though the exact number of non-ICSID cases is hard to ascertain, it is likely that the number of State-instituted cases is equally low under other procedural rules. *See also* G. Laborde, "The Case for Host State Claims in Investment Arbitration," 1 J. Int'l Disp. Settlement 97 (2010).

[70] *See* WTO Singapore Ministerial Declaration, *supra* note 4.

[71] WTO, Working Group on the Relationship between Trade and Investment, Consultation and the

The loss of control argument displays a certain parallel to the debate on the direct applicability of WTO law within the members' legal systems.[72] Those arguing against according direct effect to WTO rules also stress that States would otherwise lose their power to negotiate and determine policy issues independent from GATT and other WTO dictates. In fact, even in the many ECJ rulings on this matter the Court stressed the importance of a strong EU position based on a negotiation/diplomacy approach which should not be trumped by a further legalization in the form of direct effect of WTO law.[73]

B. Policy Reasons for Investor-State Arbitration

It seems that in spite of the aforementioned policy reasons sometimes voiced against investor-State arbitration there is indeed a strong case for this form of economic dispute settlement which can easily be integrated into PTAs or other trade agreements, as demonstrated by NAFTA and other treaties.[74]

The possibility of direct legal recourse of affected parties against host States not only eliminates the uncertainties of diplomatic protection for investors but also removes the additional nuisance value of inter-State disputes that may seriously affect the economic and political relations between States. Without the need for espousal of claims by the home States of investors—or in the case of ICSID even without such possibility[75]—host States and investors are much more likely to negotiate, mediate or arbitrate their disputes in a legal fashion without touching on too many unrelated political issues. This depoliticization

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Settlement of Disputes between Members, Note by the Secretariat, WTO Doc. WT/WGTI/W/134 (Aug. 7, 2002). Paragraph 7 of the Note reads:

> Regarding investor-State dispute resolution provisions, a number of delegations have indicated that possible WTO rules on investment should not provide for a right of individual investors to have recourse to international dispute settlement procedures. It was also pointed out that, given the intergovernmental nature of the WTO, the issue of investor-State dispute settlement in the WTO required careful examination. However, it was suggested that there could be rules requiring domestic judicial review.

[72] *See* J. Trachtman, "Bananas, Direct Effect and Compliance," 10 Eur. J. Int'l L. 655 (1999); St. Griller, "Judicial Enforceability of WTO Law in the European Union. Annotation to Case C-149/96, *Portugal* v. *Council*," 3 J. Int'l Econ. L. 417 (2000).

[73] Most explicitly, Case C-149/96, *Portugal v. Council*, *1999* E.C.R. *I-8395, paras. 34–47. See also the ECJ's earlier case law in* Joined Cases 21–24/72, *International Fruit Company*, 1972 E.C.R. 1219; Case 9/73, *Schlüter*, 1973 E.C.R. 1135; Case C-280/93, *Germany v. Council*, 1994 E.C.R. I-4973.

[74] *See supra* note 17 and accompanying text.

[75] *Cf.* Article 27 of the ICSID Convention, *supra* note 14, which states:

> No Contracting State shall give diplomatic protection, or bring an international claim, in respect of a dispute which one of its nationals and another Contracting State shall have consented to submit or shall have submitted to arbitration under this Convention, unless such other Contracting State shall have failed to abide by and comply with the award rendered in such dispute.

of investment disputes has already been praised at an early stage,[76] and practice has aptly demonstrated that this assumption was correct.

In addition to avoiding the political overtones of disputes elevated to the inter-State level, direct investor-State arbitration also contributes significantly to turning the substantive rights conferred upon investors in investment agreements into effective ones. According to the "no rights without remedies" paradigm, investment arbitration in the current form of investor-State dispute settlement has greatly contributed to the general perception of international law as a body of enforceable legal rules and not merely exhortatory guidance. The possibility to have substantive rights enforced through investment arbitration is often viewed as one of the main assets of modern investment protection.[77]

Even some of the perceived disadvantages of investor-State arbitration may prove to have some positive impact. To take the loss of control argument: granted, any consent to third-party adjudication leads to a loss of control in the sense that it constitutes a restraint on the freedom of action. In the context of investor-State arbitration such restraint appears in the form of awards sometimes involving very high monetary amounts "punishing" non-compliance with investment treatment standards. However, there is another side of this coin. If the potential financial liability effectively leads to compliance with investment standards, and if the standards are not only formally consented to because they are included in the applicable investment instrument but also substantially agreed upon and accepted as the "right," rule of law-inspired limits on the regulatory powers of host States, then an effective compliance system like investor-State arbitration should be welcome. In this sense, investment arbitration's function as an instrument for improving internal (good) governance should not be underestimated.[78]

V. CONCLUSION

This paper addressed the question whether PTAs pose a challenge to BITs. In order to attempt to answer this query it is worthwhile to differentiate the

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[76] *See* Shihata, "Towards a Greater Depoliticization of Investment Disputes," *supra* note 10.

[77] *See, e.g.*, *National Grid plc v. The Argentine Republic* (UNCITRAL), Decision on Jurisdiction, para. 49 (June 20, 2006) ("[A]ssurance of independent international arbitration is an important—perhaps the most important—element in investor protection."); *Eastern Sugar BV* v. *Czech Republic* (UNCITRAL), SCC Case No. 088/2004, Partial Award and Partial Dissenting Opinion, para. 165 (Mar. 27, 2007) ("From the point of view of the promotion and protection of investments, the arbitration clause is in practice the most essential provision of Bilateral Investment Treaties.").

[78] *See* R. Dolzer, "The Impact of International Investment Treaties on Domestic Administrative Law," 37 N.Y.U. J. Int'l L. & Pol. 953 (2006); St. Schill, "Fair and Equitable Treatment under Investment Treaties as an Embodiment of the Rule of Law," IILJ Working Paper 2006/6 (Global Admin. L. Ser.) (Inst. Int'l L. & Justice 2006), *available at* http://www.iilj.org/publications/documents/2006–6-GAL-Schill-web.pdf.

component issues by making them more specific. On the one hand, one may ask whether there is a challenge in the sense of "taking over" the regulatory space hitherto governed by BITs. The answer is probably yes, since many PTAs tend to include the traditional post-establishment protection standards and are not satisfied with merely regulating "trade-like" access issues by liberalizing the cross-border flow of investment. On the other hand, one may ask whether there is a challenge in the sense of ending the established investor-State dispute settlement mechanisms of BITs. The right answer appears to be that such a scenario is possible, but not inevitable. Investor-State arbitration as one of the core aspects of modern investment protection is perfectly suitable for being included in extended PTAs. It will depend upon the political will of those negotiating such agreements to ensure that this important element of traditional BITs will not fall into obsolescence.