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Are Bilateral Investment Treaties And Free Trade Agreements Drafted With Sufficient Clarity To Give Guidance To Tribunals?

Benard Hanotiau
Universities of Louvain and Namur, bernard.hanotiau@hvdb.com

SPEECHES

ARE BILATERAL INVESTMENT TREATIES AND FREE TRADE AGREEMENTS DRAFTED WITH SUFFICIENT CLARITY TO GIVE GUIDANCE TO TRIBUNALS?

BERNARD HANOTIAU*

INTRODUCTION

The issue that I have chosen to address is whether Bilateral Investment Treaties ("BITs") and Free Trade Agreements ("FTAs") are drafted with sufficient clarity to give guidance to arbitral tribunals. I will say at the very outset that, in my view, the answer to this question is a resounding no.

This problem has become more and more apparent with the large increase in the number of disputes submitted to the International Centre for Settlement of Investment Disputes ("ICSID") and the United Nations Commission on International Trade Law ("UNCITRAL") tribunals based

* Professor Emeritus, Universities of Louvain and Namur (Belgium); Member of the Brussels and Paris Bars; Partner, Hanotiau & van den Berg, Brussels and Singapore.

on BITs in particular.[1] This increase in the number of disputes submitted and the corresponding publication of resulting awards have demonstrated that arbitral panels often interpret BITs inconsistently with the consequence that there is a lack of clarity and transparency as to the nature and extent of the commitments made by the States vis–à–vis foreign investors.

Why is there such inconsistency between arbitral tribunals? The main reason is that many of the BITs, particularly the older ones, are not drafted with sufficient clarity. The provisions are generally vague.[2] They are comparable to general clauses in civil codes such as "good faith" or "bonos mores" that allow the decision maker to ascertain the normative content and the precise standards applicable to certain situations. In this respect, Article 31 of the Vienna Convention on the law of treaties provides that "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."[3] But what if the actual terms of the treaty are unclear or are ambiguous? In these circumstances, the arbitrator will have difficulty determining the meaning to be given to the terms or to the intent of the negotiators. Furthermore, BITs are written in multiple languages and this tends to accentuate the interpretive problems even further. Specifically, the lack of precise linguistic equivalence and differences in legal systems throughout the globe make it "virtually certain that multiple language versions will include terminological differences that lead to conflicting interpretations of the text."[4]

Lack of clarity leads to inconsistent decisions and inconsistency creates uncertainty and damages the legitimate expectations of investors and States.[5] Investors that have structured their investments in a manner

1. *See The ICSID Caseload – Statistics*, ICSID at 7 (2015), https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%202015-1%20(English)%20(2) Redacted.pdf (indicating that between 2000 and 2014, ICSID registered over 430 new investment disputes, as compared to just 66 in total between 1965 and 2000).

2. *See Investor–State Disputes Arising From Investment Treaties: A Review*, UNCTAD Series on Int'l Investment Policies for Dev. at 3 (2005), http://unctad.org/en/Docs/iteiit20054_en.pdf (noting that "the rather vague language of some treaty provisions (e.g. the fair and equitable treatment standard) and the increasing complexity of [International Investment Agreements] can make the outcome of arbitration less predictable") (internal quotations omitted).

3. Vienna Convention on the Law of Treaties art. 31 (1), May 23, 1969, 1155 U.N.T.S. 331.

4. Dinah Shelton, *Reconcilable Differences? The Interpretation of Multilingual Treaties*, 20 HASTINGS INT'L & COMP. L. REV. 611, 611–12 (1997) (explaining further that "language as a means of communication is fraught with ambiguities, mistakes, and deception.").

5. Susan D. Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions*, 73 FORDHAM L. REV. 1521, 1558 (2005)[hereinafter *The Legitimacy Crisis*]; *see also* Susan D. Franck,

designed to take advantage of the protection afforded by investment treaties suddenly discover that they will not receive those benefits.[6] Likewise, States find themselves in an untenable position of having to try to explain to tax payers why they are subject to damages of hundreds of millions of U.S. dollars in one case but not in another.[7]

There have been numerous examples of inconsistent decisions over what essentially amounted to the same dispute.[8] For example, in the *Lauder* arbitration, a Stockholm tribunal held that the Czech Republic breached a variety of its obligations to the Dutch corporate arm of a U.S. investor under the Netherlands–Czech Republic BIT.[9] Only ten days previously, on exactly the same set of facts, a London tribunal held that the Czech Republic only discriminated against a United States investor in violation of the United States–Czech Republic BIT.[10] The relevant provisions in the two treaties were identical. This inconsistency has presented challenges. After the *Lauder* awards, there was speculation that the Czech Republic might consider pulling out of its BITs.[11]

Another example of inconsistent cases is the *SGS* cases.[12] Both the Switzerland–Pakistan BIT and the Switzerland–Philippines BIT contained an umbrella clause.[13] The issue confronting the arbitrators in both cases was whether an umbrella clause in a treaty transforms a breach of contract

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The Nature and Enforcement of Investor Rights Under Investment Treaties: Do Investment Treaties Have a Bright Future, 12 U.C. DAVIS J. INT'L L. & POL'Y 47, 63 (2005) [hereinafter *The Nature and Enforcement of Investor Rights*] ("Inconsistency tends to signal errors, lends itself to suggestions of unfairness, creates inefficiencies, and generates difficulties related to coherence, most notably a lack predictability, reliability, and clarity.").

6. *The Legitimacy Crisis*, *supra* note 5.

7. *Id.*

8. *Id.* at 1545 (noting that there are three typical scenarios under which inconsistent decisions generally arise: (1) "different tribunals can come to different conclusions about the same standard in the same treaty;" (2) "different tribunals organized under different treaties can come to different conclusions about disputes involving the same facts, related parties, and similar investment rights;" and (3) "different tribunals organized under different investment treaties will consider disputes involving a similar commercial situation and similar investment rights, but will come to opposite conclusions.").

9. *Id.* at 1559.

10. *Id.*

11. *The Nature and Enforcement of Investor Rights*, *supra* note 5, at 61.

12. *See generally* SGS Société Générale de Surveillance S.A. v. Republic of the Philippines, ICSID Case No. ARB/02/6 (Jan. 29, 2004); SGS Société Générale de Surveillance S.A. v. Pakistan, ICSID Case No. ARB/01/13, Decision of August 6, 2003, 18 ICSID Rev. 307 (2003); 42 I.L.M 1290 (2003).

13. *See The Legitimacy Crisis, supra* note 5, at 1568–69 ("Umbrella clauses are designed to protect investors' contractual rights against interference from a breach of contract or an administrative or legislative act.").

into a breach of treaty.[14] The Pakistan tribunal definitely said no, and the Philippines tribunal said yes. This was quite astonishing[15] since both awards dealt with an umbrella clause that was presumably borrowed from one sole model, the Swiss model.

Such cases are not isolated incidents. Argentina has been subject to multiple treaty claims related to its currency crisis.[16] These different claims have resulted in divergent applications of the same or similar treaty provisions and different conclusions regarding liability for the same government conduct.

There have also been inconsistent decisions in cases under the North American Free Trade Agreement ("NAFTA").[17] For example the three cases *S.D. Myers Inc. v. Canada*, *Metalclad v. Mexico*, and *Pope & Talbot v. Canada* used different approaches to determine how the standard of fair and equitable treatment should be interpreted and applied.[18]

This lack of consistency is a big problem. Without the clarity and consistency of the rule of law and its application, some scholars note that "there is a detrimental impact upon those governed by the rules and their willingness and ability to adhere to such rules, which can lead to a lack of legitimacy."[19] If there is no predictability, possibility of reliability, or legal certainty, companies and governments cannot anticipate how to comply with the law and plan their conduct accordingly, thereby undermining legitimacy.[20]

How can this problem be addressed? One possible solution recently adopted by the three NAFTA countries was to issue an Interpretative Note regarding the obligation under Article 1105(1) to treat NAFTA investors "in accordance with international law, including fair and equitable treatment . . . ."[21] The Free Trade Commission ("FTC"), a body composed of representatives of the three State parties, can adopt binding interpretations of the treaty.[22] The FTC declared in the Interpretative Note that Article 1105 of the Treaty only encompassed *the minimum* standard of

14. *Id.* at 1569.

15. *Id.* at 1574 (noting that, "[e]ven though the Philippines tribunal had the opportunity to consider the Pakistan award and discussed the case in its own decision, reconciling the two awards is challenging").

16. *See The Nature and Enforcement of Investor Rights*, *supra* note 5, at 62.

17. *See generally The Legitimacy Crisis*, *supra* note 5, at 1575–82.

18. *See generally id.*

19. *See id.* at 1584.

20. *See id.*

21. North American Free Trade Agreement, Can.–Mex.–U.S., art. 1105(1), Dec. 17, 1992, 32 I.L.M. 605, 639 [hereinafter NAFTA].

22. *Id.* art. 2001(1).

treatment in customary international law.[23] Since this note was issued, NAFTA tribunals have applied Article 1105 in a more uniform fashion.[24]

Similar provisions requiring tribunals to decide the issues in dispute in accordance with applicable rules of international law are found in many BITs and FTAs. For example, Article 30(3) of the United States Model BIT (both 2004 and 2012) provide for a mechanism that is similar to the one in the NAFTA.[25]

Other examples include Article 27(2) of the investment chapter of the ASEAN–Australia–New Zealand Free Trade Agreement ("AANZFTA"), which authorizes a tribunal to request a joint interpretation by the parties of any provision of the agreement.[26] Furthermore, Article 27(3) establishes the binding nature of that joint interpretation.[27]

This method is efficient, but it has one notable detractor: states may strive to issue official interpretations in an attempt to influence proceedings to which they are parties.[28] As the example of the July 2001 interpretation of the FTA under NAFTA demonstrates, the home states of disputing investors are more interested in protecting state respondents than protecting their own nationals when it comes to treaty interpretation.[29] This is why commentators and jurists have expressed concern about the legitimacy of these interpretative mechanisms.

Putting these interpretative mechanisms to one side, what are the other

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23. *See* NAFTA Free Trade Commission, Notes of Interpretation of Certain Chapter11 Provisions (July 31, 2001), http://www.sice.oas.org/tpd/nafta/Commission/CH11understanding_e.asp ("Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party."); *see generally id.* art. 1105(1), (2)(c); The Legitimacy Crisis, *supra* note 5, at 1581–82.

24. *The Legitimacy Crisis*, *supra* note 5, at 1582.

25. *See, e.g.*, 2012 U.S. Model Bilateral Investment Treaty art. 30(3) (2012), http://www.state.gov/documents/organization/188371.pdf ("A joint decision of the Parties, each acting through its representative designated for purposes of this Article, declaring their interpretation of a provision of this Treaty shall be binding on a tribunal, and any decision or award issued by a tribunal must be consistent with that joint decision."); *see also* 2004 U.S. Model Bilateral Investment Treaty art. 30(3) (2004), http://www.state.gov/documents/organization/117601.pdf.

26. Free Trade Agreement, ASEAN–Australia–New Zealand, art. 27(2) (Feb. 27, 2009), http://www.asean.org/storage/images/archive/22260.pdf ("The tribunal shall . . . request a joint interpretation of any provision of this Agreement that is in issue in a dispute.").

27. *Id.* art. 27(3) ("A joint decision of the Parties, declaring their interpretation of a provision of this Agreement shall be binding on a tribunal, and any decision or award issued by a tribunal must be consistent with that joint decision.").

28. Christoph Schreuer & Matthew Weiniger, *A Doctrine of Precedent?*, *in* THE OXFORD HANDBOOK OF INTERNATIONAL INVESTMENT LAW 1201 (Peter T Muchlinski, Federico Ortino & Christoph Schreuer eds., 2008).

29. *Id.*

possible solutions? Various suggestions have been made. Some commentators have, for example, suggested replacing investor–State arbitration with a mechanism that would require such claims to be brought before a permanent judicial body, perhaps something akin to the International Court of Justice ("ICJ").[30] While this would help to create a coherent body of investment treaty jurisprudence, there would be still no check on the court's discretion should the court simply get it wrong. In other words, shifting disputes to a permanent court will not completely solve the problem.

Another suggestion is to allow parties to have the option of submitting a question to a court in the manner of a preliminary ruling like the one provided by article 234 of the EU Treaty.[31] Another option would be to create a system of appeal or an appellate body that would focus on establishing a clear and coherent body of law and would correct legal errors in specific cases. It has even been suggested that the ICJ have appellate jurisdiction over investment treaty cases. But this would only prolong the procedure by several years and still increase the cost of these types of cases, which is already very high and heavily criticized.

In my view, it is better to tackle the problem from its root. We should look at the actual BITs themselves. The best solution to the problem resides in the drafting process. The goal is to create treaties that accurately capture the intent of the contracting states and then articulate those intentions in a form that can be appropriately interpreted in future relations. One of the ways to implement this method involves working backwards, identifying the flaws in arbitral interpretation, and hypothesizing ways to avoid them when constructing the document itself. It is only through awareness of how treaties are interpreted that the drafting process can be amended.

To put it differently, by providing enhanced textual clarity about the meaning of substantive rights, or more precisely, by providing detailed definitions of all the relevant legal terms, arbitrators will have better guidance thus leading to a more consistent interpretation of treaty provisions.[32] For instance, if investment treaties guarantee freedom from arbitrary and discriminatory treatment, states might include clear and precise definitions for the terms "arbitrary" and "discriminatory" in these

30. *See e.g.,* Charles H. Brower, *Structure, Legitimacy, and NAFTA's Investment Chapter*, 35 VAND. J. TRANSAT'L L. 37, 90 (2003).

31. Treaty on the European Union, art. 234, Feb. 26, 2001 ("Where such a question is raised before any court or tribunal of a Member State, that court or tribunal may, if it considers that a decision on the question is necessary to enable it to give judgment, request the Court of Justice to give a ruling thereon.").

32. *See The Nature and Enforcement of Investor Rights*, *supra* note 5, at 84.

treaties.[33]

Such an approach has two benefits. First, it permits states to choose what rights they wish to grant to investors.[34] Second, by elucidating the parameters of investors' substantive rights, this approach brings more textual clarity to an individual treaty, and this will in turn generate a more consistent interpretation of its provisions.[35] Of course, this approach is not without its problems.[36] There is a risk that over–definition of rights might generate more issues for litigation, which also in turn would lead to more inconsistency.[37] Not to mention the fact that renegotiating the terms of thousands of BITs presents political challenges and looks impractical.[38] But in my opinion, it still remains the better approach.

I will now test this proposal by examining older and more recent BITs in five areas: the notion of investment, fair and equitable treatment, full protection and security, the most favored nation ("MFN") clause, and expropriation.

II. AN EXAMPLE OF THE PROBLEM AND ITS SOLUTION: THE NOTION OF INVESTMENT

The definition of "investment" is important in ICSID arbitrations because unless an asset or an economic activity constitutes an investment under Article 25(1) of the ICSID Convention, it is not subject to ICSID jurisdiction.[39] Unfortunately, the drafters of the ICSID Convention chose not to define the meaning of investment within the Convention, generating significant debate. The five criteria retained in the *Salini* award[40] have

33. *See id.*

34. *Id.* at 85.

35. *Id.*

36. *Id.*; *see also* Brower, *supra* note 30, at 87–88 (explaining several problems that arise in drafting "perfectly clear rules," including the inability of negotiators to capture a complex balance of stakeholder interests in simple rules, the potential for such simple rules to produce absurd results at the margins, and the potential for creating "a sense of constructive indeterminacy and a paradoxical reduction of legitimacy.").

37. *The Nature and Enforcement of Investor Rights*, *supra* note 5, at 85.

38. *Id.*

39. Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, art. 25(1), Mar. 18, 1965, 17 U.S.T. 1270 ("The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State").

40. Salini Costruttori S.p.A. v. Morocco, ICSID Case No. ARB/00/4, Decision on Jurisdiction, ¶ 52 (July 23, 2001) (identifying five criteria indicative of the existence of an investment, including: (1) substantial commitment or contribution, (2) duration, (3) assumption of risk, (4) contribution to economic developing, and (5) regularity of profit and return).

been referred to in many cases but nowadays, at least two of these criteria are no longer considered relevant by many. I will not dwell on this since we are concentrating on BITs. I will instead concentrate on the definition of investment in those BITs. However, I wanted to make the point that since arbitral tribunals generally recognize that there is a double barrel test, the absence of a definition of *"investment"* in the ICSID Convention complicates matters and explains why in ICSID arbitrations, sometimes more than half of the submissions, which often means several hundred pages, are only devoted to jurisdiction and, in particular, to the issue of whether there is a protected investment.

Indeed, most BITs traditionally aimed at protecting investments.[41] Therefore "investment" was defined in a way that was both broad and open–ended, covering "not only the capital that has crossed the borders, but also practically all other kinds of assets invested by an investor in the territory of the host country."[42] A significant number of BITs have included a standard definition of "investment," covering "every kind of asset" owned or controlled by an investor of another party.[43] This broad definition of "investment" is typically complemented by an illustrative list of assets that are included within the definition.[44] Such list commonly includes five categories of assets: movable and immovable property, interests in companies (including both portfolio and direct investment), contractual rights, intellectual property, and business concessions.[45]

This kind of approach can still be found in recent draft BITs, like the 2006 French Model BIT.[46] In such an approach, not only is the list of assets in the definition non–exhaustive, but the use of broad generic terms, such as "every kind of assets," "movable and immovable property,"

41. U.N. Conference on Trade and Development, *Investor–State Dispute Settlement and Impact on Investment Rulemaking* 22 (2007).

42. *Id.*

43. *Id.*

44. *Id.*

45. *Id.*

46. *See* 2006 French Model Bilateral Investment Treaty art. 1(a)–(e) (2006) (defining the term "investment" to mean "every kind of assets, such as goods, rights and interests of whatever nature, and in particular though not exclusively: (a) movable and immovable property as well as any other right in rem such as mortgages, liens, usufructs, pledges and similar rights; (b) shares, premium on share and other kinds of interest including minority or indirect forms, in companies constituted in the territory of one Contracting Party; (c) title to money or debentures, or title to any legitimate performance having an economic value; (d) intellectual, commercial and industrial property rights such as copyrights, patents, licenses, trademarks, industrial models and mockups, technical processes, know–how, trade names and goodwill; (e) business concessions conferred by law or under contract, including concessions to search for, cultivate, extract or exploit natural resources, including those which are located in the maritime area of the Contracting Parties.").

"claims to money," can complicate the issue of whether the transaction falls within one of the categories of investment protected by the BIT.

In recent years, the way the notion of investment has been interpreted by some arbitral tribunals has created great concern in some countries. Some of these interpretations have been considered too broad and go beyond what the contracting parties considered an *"investment"* when negotiating the BIT. For instance, in *Pope & Talbot v. Canada*, the tribunal found that a market share through trade could be regarded as part of the assets of an investment.[47] And in *S.D. Myers v. Canada,* the tribunal held that the establishment of a sales office and the carrying out of marketing constituted a sufficient investment.[48] Experience has shown the risk of having an extremely broad and unqualified definition of investment.

Another problem is that, at times, the definition itself lacks clarity. As chairman of an arbitral tribunal, I recently encountered this problem in an ICSID case. The Germany–Sri Lanka BIT provides in its Article 1: "1. The term "investment" comprises every kind of asset, in particular: . . . (c) claims to money which has been used to create an economic value or claims to any performance having an economic value and associated with an investment."[49] We were confronted with the issue of whether the phrase "claims to money which has been used to create an economic value" could stand on its own or whether it was required to be associated with a separate investment in order to qualify for protection. The majority of the Tribunal decided that the categories enumerated (which included "claims to money which has been used to create an economic value") were an illustrative list of assets every kind of which was considered to be an investment and that defining an investment by reference to investment would be a circular reasoning. We could not reach unanimity on this solution. It is clear that if the terms of the provision had been expressed with more clarity, this debate would not have taken place.[50]

So what is the solution to this issue? One form of approach is for the BIT signatories to adopt negative definitions of an investment. For example, the 2012 United States Model BIT provides the following:

> Some forms of debt, such as bonds, debentures, and long–term notes, are more likely to have the characteristics of an investment, while other forms of debt, such as claims to payment that are immediately due and

47. *See* Pope & Talbot, Inc. v. Canada, Interim Award, ¶ 96 (June 26, 2000).

48. *See Investor–State Disputes Arising From Investment Treaties supra* note 2, at 16.

49. Treaty Between the Federal Republic of Germany and the Democratic Socialist Republic of Sri Lanka Concerning the Promotion and Reciprocal Protection of Investments, Germany–Sri Lanka, Feb. 25, 2002, art. 1.

50. *See supra* note 6 and accompanying text.

> result from the sale of goods or services, are less likely to have such characteristics.[51]
>
> Whether a particular type of license, authorization, permit, or similar instrument (including a concession, to the extent that it has the nature of such an instrument) has the characteristics of an investment depends on such factors as the nature and extent of the rights that the holder has under the law of the Party. Among the licenses, authorizations, permits, and similar instruments that do not have the characteristics of an investment are those that do not create any rights protected under domestic law. For greater certainty, the foregoing is without prejudice to whether any asset associated with the license, authorization, permit, or similar instrument has the characteristics of an investment.[52]
>
> The term "investment" does not include an order or judgment entered in a judicial or administrative action.[53]

Similarly, the Chile–Korea FTA also provides that neither "claims to money that arise solely from (i) commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Party to an enterprise in the territory of the other Party; or (ii) the extension of credit in connection with a commercial transaction, such as trade financing;"[54] nor "an order entered in a judicial or administrative action"[55] are included in the definition of "investment."

Another way of avoiding an overly broad definition of investment is to use a "closed–list" definition, consisting of a varied but finite list of tangible and intangible assets. Originally envisaged in the context of the United States–Canada Free Trade Agreement, this approach evolved towards the definition used in Article 1139 of the NAFTA.[56] Subsequently, the "closed–list" approach has been frequently used by several countries in the definition of "investment" in their BITs. For example, Article 96 of the Free Trade Agreement between Japan and Mexico illustrates this approach in its definition of "investment."[57] The definition includes such categories

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51. *See* 2012 U.S. Model Bilateral Investment Treaty, *supra* note 25, art.1 n. 1.

52. *Id.* art. 1 n. 2.

53. *Id.* art. 1 n. 3.

54. Free Trade Agreement, Chile–S. Kor., Feb. 15, 2003, art 10.1(i).

55. *Id.* art 10.1(j).

56. NAFTA, *supra* note 23, art. 1139 (defining investment by limited terms and providing certain exceptions so long as the kinds of interests set out in the finite list are not involved).

57. The Agreement between Japan and the United Mexican States for the Strengthening of the Economic Partnership, Jap.–Mex., art. 96, Sept. 17, 2004, (defining "investment" to a closed list of eight limited categories, including (1) an enterprise; (2) an equity security of an enterprise; (3) a debt security of an enterprise; (4) a loan to an enterprise; (5) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise; (6) an interest in an enterprise that entitles the owner to share in the assets of that enterprise on dissolution; (7) a real estate or

as "a debt security of an enterprise (a) where the enterprise is an affiliate of the investor, or (b) where the original maturity of the debt security is at least three years, but does not include a debt security, regardless of original maturity of a Party or a state enterprise"[58] and "a loan to an enterprise (a) where the enterprise is an affiliate of the investor, or (b) where the original maturity of the loan is at least three years, but does not include a loan, regardless of original maturity, to a Party or a state enterprise."[59] The text concludes with the limiting language presented above in the Chile–Korea FTA.[60]

In the face of such a specific definition of investment that already indicates the duration (three years) of certain types of investment, an ICSID tribunal will not be able to contradict the BIT when assessing whether the duration characteristic under Article 25 has been fulfilled for a loan or debt security to an enterprise.[61] The closed–list of investments also indicates to some extent what sort of risk or commitment is acceptable as an investment and the tribunal should also take that into account in considering whether the Article 25 definition has been fulfilled.[62]

During the last decade, the "closed–list" definition of "investment" has also begun to be used in the context of BIT negotiations.[63] In 2004, Canada abandoned the asset–based definition of "investment" in its foreign investment protection and promotion agreements and opted to incorporate into its new Canadian Model BIT a relatively detailed "closed–list" definition of "investment."[64] In addition to being finite, the list contains a series of specific clarifications to prevent the application of the agreement to certain kinds of assets that would otherwise fall under the definition of investment.[65] The Canadian Model BIT that defines investment by utilizing nine categories,[66] the same type of approach used in the Japan–

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other property, tangible or intangible, and any related property rights; and (8) interests arising from the commitment of capital or other reasons in the Area of a Party to economic activity in such Area).

58. *Id.* art. 96(CC).

59. *Id.* art. 96(DD).

60. *Supra* notes 55–56 and accompanying text.

61. Michael Hwang & Jennifer Fong Lee Cheng, *Definition of "Investment" – A Voice from the Eye of the Storm*, 1 ASIAN J. OF INT'L L. 99, 126 (2011).

62. *Id.*

63. *Investor–State Dispute Settlement and Impact on Investment Rulemaking,* UNCTAD at 73 (2007), http://unctad.org/en/Docs/iteiia20073_en.pdf.

64. *Id. See generally* 2004 Canadian Model Bilateral Investment Treaty art. 1(I)–(IX) (2004).

65. *Investor–State Dispute Settlement and Impact on Investment Rulemaking, supra* note 63, at 73.

66. 2004 Canadian Model Bilateral Investment Treaty, *supra* note 64.

Mexico FTA,[67] and it continues

> For greater certainty:
>
> (i) a loan to, or debt security issued by, a Party or a state enterprise thereof is not an investment; and
>
> (ii) a loan granted by or debt security owned by a cross–border financial service provider, other than a loan to or debt security issued by a financial institution, is an investment if such loan or debt security meets the criteria for investments set out elsewhere in this Article.[68]

The definition includes the same exclusions concerning certain claims to money and also any other claims to money that do not involve those kinds of interests expressly enumerated within the FTA.[69]

Another approach used to clarify the definition of "investment" has been to qualify an otherwise very broad definition.[70] Accordingly, numerous recently negotiated BITs incorporate a definition of "investment" in economic terms—that is, they cover, in principle, every asset that an investor owns and controls but add the qualification that such assets must have the characteristics of an investment.[71] For this purpose, they refer to criteria developed in ICSID practice, such as "the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk."[72] This approach is complemented by explicit exclusions of several kinds of assets, which are not to fall within the category of covered investments under the agreement.[73]

Article 10.1 of the Chile–Korea FTA illustrates that approach and defines the term "investment" in the following manner: "investment means every kind of asset that an investor owns or controls, directly or indirectly, and that has the characteristics of an investment, such as the commitment of capital or other resources, the expectation of gains or profits and the

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67. *See supra* note 57 and accompanying text.

68. *See* 2004 Canadian Model Bilateral Investment Treaty, *supra* note 64, art. 1(v)(iii)–(iv).

69. *Id.* art. 1(X)–(XI) ("[B]ut investment does not mean, (X) claims to money that arise solely from (i) commercial contracts for the sale of goods or services by a national or enterprise in the territory of a Party to an enterprise in the territory of the other Party, or (ii) the extension of credit in connection with a commercial transaction, such as trade financing, other than a loan covered by subparagraphs (IV) or (V); and (XI) any other claims to money, that do not involve the kinds of interests set out in subparagraphs (1) through (IX).").

70. *Investor–State Dispute Settlement and Impact on Investment Rulemaking*, *supra* note 63, at 73.

71. *Id.*

72. *Id.*; *see also* United States–Colombia Trade Promotion Agreement, Colom.–U.S., art. 10.28, Nov. 22, 2006.

73. *Investor–State Dispute Settlement and Impact on Investment Rulemaking*, *supra* note 63, at 73.

assumption of risk."[74] The section continues by enumerating eight forms that an investment may take, akin to those discussed above,[75] and clarifying through an exclusionary clause that certain kinds of money and of orders entered in a judicial or administrative action do not qualify as an investment.

The wording of this definition indicates that for an asset to be considered a covered investment, a minimum of three conditions must be satisfied.[76] First, it must be owned or controlled by an investor as defined by the agreement; second, it must have the characteristics of an investment; and third, it must not fall within any of the excluded categories.[77]

The definition does not list all the characteristics that an asset must have in order to be considered an investment.[78] However, the definition does include some minimum parameters, namely the commitment of capital, the expectation of gain or profit, or the assumption of risk.[79] The inclusion of these criteria within the definition of investment has the effect of excluding *ab initio* certain assets: this would normally be the case for real estate or other property, tangible or intangible, not acquired in the expectation, or used for the purpose, of economic benefit or other business purposes.[80]

III. FAIR AND EQUITABLE TREATMENT

Despite its popularity, the precise legal meaning of the fair and equitable standard has also been the subject of much debate. And in recent BITs and FTAs, the negotiators have not only clarified the meaning of investment but also of several key obligations like fair and equitable treatment or expropriation.

The main problem concerning fair and equitable treatment is whether the standard incorporates the international minimum standard required by customary international law or whether it imposes other, possibly more stringent, obligations on the host country.[81]

Several old generation BITs are unclear in this respect. Either they grant covered investments fair and equitable treatment without making reference to international law or to any criteria to determine the content of the standard; or they just provide that the fair and equitable standard shall not

74. *Supra* note 53 and accompanying text.

75. *See e.g., supra* note 46 and accompanying text.

76. *Investor–State Dispute Settlement and Impact on Investment Rulemaking*, *supra* note 63, at 74.

77. *Id.*

78. *Id.*

79. *Id.*

80. *Id.*

81. *See The Legitimacy Crisis*, *supra* note 5, at 1575.

be less favorable than national treatment or most favored nation treatment granted to the investment or the investor concerned; or they just refer to the duty to abstain from impairing the investment through unreasonable or discriminatory measures. Some BITs also make the fair and equitable standard contingent on the domestic legislation of the host country.

More recent BITs and FTAs have clarified the issue. One example of this is contained in the 2005 BIT between the United States and Uruguay which provides in Article 5.1 that "[e]ach party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment . . . ."[82] Article 5.2 goes on to state that:

> For greater certainty, paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights.[83]

Another example is Article 11.5 of the Free Trade Agreement negotiated between Australia and the United States, which begins much like the FTA between the United States and Uruguay discussed above but goes on to say:

> The obligation in paragraph 1 to provide: (a) "fair and equitable treatment" includes the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world . . . .[84] A determination that there has been a breach of another provision of this Agreement, or of a separate international agreement, does not establish that there has been a breach of this Article.[85]

This provision is complemented by an annex that clarifies the understanding of the parties regarding the concept of customary international law as follows:

> The Parties confirm their shared understanding that "customary international law" generally and as specifically referenced in Article 11.5 and Annex 11.B results from a general and consistent practice of States that they follow from a sense of legal obligation. With regard to Article 11.5. the customary international law minimum standard of treatment of

82. Treaty Between the United States and the Oriental Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investment, U.S.–Uru., art. 5.1, Oct. 24, 2004, 44 I.L.M. 272, https://ustr.gov/sites/default/files/uploads/agreements/bit/asset_upload_file748_9005.pdf.

83. *Id.* art 5.2.

84. *Id.* art. 5.2(a).

85. *Id.* art 5.3. *Compare* Free Trade Agreement, Austl.–U.S., art. 11.5.3, May 18, 2004, KAV 6422 *with id.* art. 5.3.

aliens refers to all customary international law principles that protect the economic rights and interests of aliens.

IV. FULL PROTECTION AND SECURITY

In many BITs, the standard of full protection and security is defined in very broad terms. The most common expression is in the form of "full protection and security." However, there are different variants such as "constant protection and security," "protection and security," or "physical protection and security," and this raises various issues.[86] Does the word "full" make a difference? Is it limited to physical violence? Or does it impose a general duty upon States to prevent harm to the investment from the acts of government and non–government actors? Generally speaking, the more fundamental issue is whether the standard is a strict liability standard or is limited to the customary international law standard to the treatment of aliens.

Here again, a better drafting of the BITs would certainly help. A good example is Article 5 of the United States Model BIT that provides:

> 1. Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.[87]
>
> 2. For greater certainty, paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. The concept of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights. The obligation in paragraph 1 to provide:
>
> [. . . .]
>
> b) "full protection and security" requires each Party to provide the level of police protection required under customary international law.[88]

The United States Model BIT is therefore explicit in two ways. First, it links the full protection and security standard to the minimum standard of customary international law for the treatment of aliens.[89] Second, it refers only to the level of police protection. It helps clarify the debate in recent cases on the application of this standard beyond police protection.[90]

Another approach is the ASEAN Investment Agreement of 2009 that

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86. *See generally* Mahnaz Malik, *The Full Protection and Security Standard Comes of Age: Yet another challenge for states in investment treaty arbitration?*, IISD BEST PRACTICES SERIES at 2 (2011), http://www.iisd.org/pdf/2011/full_protection.pdf.

87. *See* 2012 U.S. Model Bilateral Investment Treaty, *supra* note 25, art. 5.1.

88. *Id.* art. 5.2(b).

89. Malik, *supra* note 86, at 3.

90. *Id.*

does not expressly refer to the standard of customary international law, but it does note that full protection and security requires member States to take such measures as may be reasonably necessary to ensure the protection and security of covered investments.[91] Thus, it clarifies that the standard does not impose strict liability but a duty to take reasonable measures.[92]

V. MOST FAVORED NATION TREATMENT ("MFN")

Many BITs contain an MFN clause. In early BITs, as national treatment was not granted automatically, the inclusion of an MFN treatment clause was generalized in order to insure that the host states, while not granting national treatment, would accord a covered foreign investor a treatment that is no less favorable than it accords to a third foreign investor and would benefit from national treatment as soon as the country granted it.[93] Nowadays, the overwhelming majority of BITs have an MFN provision that is granted alongside national treatment, mostly in a single provision.[94]

In practice, violations or breaches of the MFN treatment *per se* have not been controversial.[95] However, an unexpected application of MFN treatment in investment treaties has given rise to a debate that has not yet been concluded and has generated different and sometimes inconsistent decisions by arbitral tribunals.[96] The issue is the application of the MFN treatment provision to import investor–State dispute settlement ("ISDS") provisions from third treaties considered more favorable to solve issues relating to admissibility and jurisdiction over a claim, such as the elimination of a preliminary requirement to arbitration or the extension of the scope of jurisdiction.[97]

The disputed issue goes back to *Maffezini v. Spain* where the tribunal held that the MFN clause in the 1991 Argentina–Spain BIT could be used by the claimant to circumvent an eighteen–month waiting period before recourse to international arbitration was available.[98] The claimant argued that the third treaty concluded between Spain and Chile did not contain

91. *Id.*

92. *Id.*

93. Most–Favoured–Nation–Treatment, UNCTAD(2010), http://unctad.org/en/Docs/diaeia20101_en.pdf.

94. *Id.*

95. *Id.*

96. *Id.*

97. *Id.*

98. *See* Maffezini v. Spain, ICSID Case No. ARB/97/7, Decision of the Tribunal on Objections to Jurisdiction, ¶ 56 (Jan. 25, 2000) ("[I]f a third–party treaty contains provisions for the settlement of disputes that are more favorable . . . than those in the basic treaty, such provisions may be extended to the beneficiary of the [MFN] clause . . . .").

such a requirement and that the investor State dispute settlement clause in this third treaty was therefore less restrictive.[99] It could then be imported under the MFN clause contained in the basic treaty.[100] The tribunal found that even though the MFN clause did not expressly refer to dispute settlement, there were good reasons to conclude that dispute settlement arrangements were inextricably related to the protection of foreign investors.[101]

This decision created an intense debate which is still on–going as to whether MFN treatment includes access to international arbitration as contained in the ISDS provisions of respective agreements.[102] The *Maffezini v. Spain* approach was followed in a number of cases: *Siemens v. Argentina*, *Gas Natural v. Argentina*, *National Grid v. Argentina*, *AWG v. Argentina*; however, it was rejected by arbitral tribunals in other cases, such as *Wintershall v. Argentina, Salini v. Morocco, Plama v. Bulgaria, Telenor v. Hungary,* and *Berschader v. Russian Federation.*[103] For example, in *Wintershall v. Argentina*, the tribunal gave particular weight to "consent" as the founding principle upon which jurisdiction is found.[104] The tribunal considered that the timing rule (the eighteen–month waiting period) constituted "part and parcel of Argentina's integrated 'offer' for ICSID jurisdiction," which should be "accepted by the investor on the same terms."[105] The tribunal also based its decision on an analysis of the MFN clause's wording and found that the treatment to which it extended did not include dispute settlement. It considered that the application of the MFN clause could not dislodge the dispute resolution provision in the basic treaty unless the MFN clause in the basic treaty clearly and unambiguously indicates that it should be so interpreted.

In *Salini* and *Plama*, the tribunals have based their decision on the consideration that the contracting parties could not reasonably have intended that jurisdiction would be formed through an incorporation by reference, unless such intent had been explicitly reflected in the relevant

99. *Id.* ¶ 60.

100. *Id.* ¶ 54.

101. *Id.*

102. *Most–Favoured–Nation–Treatment, supra* note 93, at 69.

103. *Id.* at 73.

104. Wintershall Aktiengesellschaft v. Argentina, ICSID Case No. ARB/04/14, Award, ¶ 160(3) (Dec. 8, 2008) ("Besides, it is a general principle of international law that international courts and tribunals can exercise jurisdiction over a State only with its consent. The principle is often described as a corollary to the sovereignty and independence of the State. A presumed consent is not regarded as sufficient, because any restriction upon the independence of a State (not agreed to) cannot be presumed by courts".).

105. *Id.* ¶ 162.

provisions of the basic BIT.

Once again, the controversy concerning the application of the MFN clause to dispute settlement provisions included in other treaties results from the fact that, in many BITs, the clause is broadly framed. For example: "[n]either contracting party shall in its territory subject investments or returns of investors of the other Contracting Party to treatment less favorable than that which it accords, in like circumstances, to investments or returns of its own investors or to investments or returns of its investors of any third states."[106]

Another solution to the problem could be a better formulation of the MFN clause, clarifying that it does not apply to any procedural provisions. In other words, a second section could be added to the MFN clause clarifying that "[f]or greater certainty, the obligation referred to in paragraph 1 above shall not apply to [such and such articles or sections] of this agreement." If you take for example the Chile–Colombia FTA of 2006, it provides in its Annex 9.3 that:

> [T]he parties agree that the scope of application of Article 9.3 [the MFN clause] only covers the matters related to the establishment, acquisition, expansion, administration, conduct, operation, sale or other disposition of investments, and hence, does not apply to procedural issues, including dispute settlement mechanisms such as that contained in section B of this chapter.[107]

This is probably the right approach to follow.

VI. EXPROPRIATION

In recent years, drafters of BITs have also ensured that greater clarity is given to the definition of expropriation. The classic example of an expropriation is an act that transfers ownership or possession of the investment to the State.[108] An act that completely destroys the value of an investment is also typically regarded as an expropriation.[109] But more and more often expropriation occurs through a series of actions rather than a single act,[110] and consequently, many BITs have defined expropriation to include measures that, taken together, are equivalent to, or have the same effect as, an expropriation. Indeed, BITs include clauses that use the following terms: "expropriation, nationalization and any other measure that

106. *See e.g.,* 2008 U.K. Model Bilateral Investment Treaty art. 3(1) (2008).

107. Chile–Colombia Free Trade Agreement, Chile–Colombia, Annex 9.3, Nov. 28, 2006.

108. U.N. Conference on Trade and Development, *Investment Provisions in Economic Integration Agreements*, 107, U.N. Doc. A/CONF (Oct. 2005).

109. *Id.*

110. *Id.*

has an effect tantamount to expropriation or nationalization;" "measures that deprive the investor of their investment, either directly or indirectly;" "expropriation or nationalization or similar measures;" "direct or indirect expropriation or nationalization, or any other equivalent measure having an effect similar to dispossession;" or still "shall not, directly or indirectly, expropriate or nationalize or take any measure with equivalent character or effect."[111]

It is not clear from such language what degree of interference with ownership rights is required for an act (or series of acts) to constitute an expropriation. Furthermore, acts that only partially devalue an investment may be viewed by the host country as routine regulatory acts that are not the equivalent of an expropriation.

These problems are why recent BITs tend to contain provisions clarifying two specific aspects. First, a text has been included in order to make it explicit that the obligations regarding expropriation are intended to reflect the level of protection granted by customary international law. Second, such clarification has been complemented by guidelines and criteria in order to determine whether, in a particular situation, an indirect expropriation has taken place.

In this regard, modern BITs state that an adverse effect on the economic value of an investment, as such, does not establish that an indirect expropriation has occurred. It is further stated that, except in rare circumstances, non–discriminatory regulatory actions by a party aimed at protecting legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations.[112]

For example, Article 12 of the BIT between Mauritius and Comoros in 2001 states: "[n]othing in this agreement shall be construed to prevent a contracting party from adopting any measure necessary to protect its essential security interests or in the interest of public health or the prevention of diseases affecting animals and plants."[113]

Similarly, some investment treaty models used by European and American countries contain clauses relating to protection of the environment, health, and labor rights. This is true of the models used by United States, Canada, Belgium, Finland, and Austria.

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111. *See* Suzy H. Nikièma, *Best Practices Indirect Expropriation*, IISD BEST PRACTICES SERIES at 5 (2012), http://www.iisd.org/pdf/2012/best_practice_indirect_expropriation.pdf.

112. *See e.g.*, United States–Chile Free Trade Agreement, U.S.–Chile, Annex 10–D, June 6, 2003, https://ustr.gov/trade–agreements/free–trade–agreements/chile–fta/final–text.

113. OECD Investment Policy Reviews: Mauritius 2014, OECD 108 (2014) (quoting Article 12 of the Mauritius–Comoros Free Trade Agreement).

The scope of such provisions is limited. They merely affirm the States' sovereign rights to regulate in the public interest, which is already recognized in customary international law. Often, these clauses that reaffirm the States' rights to regulate do not stipulate whether the State is relieved of its obligation to compensate in the event that the exercise of its sovereign right harms the investor. But some of them are more carefully drafted, as we will see in the following two examples that seem to be the most comprehensive articles on expropriation.

The first one is Annex 10–D of the Free Trade Agreement between Chile and the United States:

> The Parties confirm their shared understanding that:
>
> (1) Article 10.9(1) is intended to reflect customary international law concerning the obligation of States with respect to expropriation.
>
> (2) An action or a series of actions by a Party cannot constitute an expropriation unless it interferes with a tangible or intangible property right or property interest in an investment.[114]

It then goes on to explain that the expropriation article addresses two situations. The first is direct expropriation[115] and the second situation is indirect expropriation.[116] It further details:

> (a) The determination of whether an action or series of actions by a Party, in a specific fact situation, constitutes an indirect expropriation, requires a case–by–case, fact based inquiry that considers, among other factors:
>
> (i) the economic impact of the government action, although the fact that an action or series of actions by a Party has an adverse effect on the economic value of an investment, standing alone, does not establish that an indirect expropriation has occurred;
>
> (ii) the extent to which the government action interferes with distinct, reasonable investment–backed expectations; and
>
> (iii) the character of the government action.
>
> (b) Except in rare circumstances, nondiscriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations.[117]

This is a very comprehensive definition of expropriation.[118]

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114. *See* United States–Chile Free Trade Agreement, *supra* note 112, Annex 10–D.

115. *Id.* Annex 10–D(3) (defining direct expropriation as "where an investment is nationalized or otherwise directly expropriated through formal transfer of title or outright seizure.").

116. *Id.* Annex 10–D(4) (defining indirect expropriation as "where an action or series of actions by a Party has an effect equivalent to direct expropriation without formal transfer of title or outright seizure.").

117. *Id.* Annex 10–D(4)(a)–(b).

118. *See also* Agreement Establishing the ASEAN–Australia–New Zeeland Free

CONCLUSION

It is obvious that many BITs and FTAs, particularly the older ones, are not drafted in a sufficiently precise manner. This lack of clarity means that arbitral tribunals do not have sufficient guidance when attempting to interpret them.[119] It is therefore essential that treaties be drafted in a more precise manner in order to simplify the debate when a dispute arises or even potentially eliminate a number of disputes. More precise drafting will moreover permit to avoid inconsistencies and guarantee a higher level of predictability and reliability for both investors and governments in their efforts to comply with the law.

Trade Area, Annex on Expropriation and Compensation ¶ 2(a)–(b), Feb. 27, 2009, http://www.asean.fta.govt.nz/assets/Agreement-Establishing-the-ASEAN-Australia-Ne

w-Zealand-Free-Trade-Area.pdf (providing an identical definition of expropriation).

119. *See supra* note 5 and accompanying text.