EXAMINING THE MECHANISMS FOR DISMISSAL OF FRIVOLOUS AND ABUSE OF PROCESS CLAIMS IN THE INTERNATIONAL INVESTMENT REGIME: A CASE OF FAILED LEGAL TRANSPLANT?

by

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Abstract

Investor-state arbitration is in a phase of reform. One aspect of this reform process is that the recently-negotiated treaties and updated arbitration rules include mechanisms for the early dismissal of frivolous claims (including those manifestly without legal merit and those unfounded as a matter of law). Some ISA tribunals have also, without an express provision empowering them and only in narrow circumstances, dismissed investors' claims as an abuse of process.

The mechanisms for early dismissal of frivolous and abuse of process claims in ISA vary across investment treaties and arbitration rules, but they all share a fundamental characteristic borrowed from domestic legal systems: that the same tribunal empowered to rule on the merits is also charged with identifying such claims and curtailing them early in the arbitral process. The system of investment arbitration, however, radically departs from the structural organization of the domestic legal systems, with their integrated judicial hierarchies, application of precedent, judicial review of administrative actions, and traditions of job tenure and other career safeguards that protect judicial independence. The comparative law literature teaches that legal transplants often fail when attention is not paid to the structural and doctrinal context of the recipient legal order.

This thesis situates the dismissal of frivolous and abuse of process claims within the broader context of the structures of the international investment regime and the incentives those structures create for decision-makers. It shows that the outcome of these factors is that arbitrators utilize and will continue to utilize the mechanisms for early dismissal only in overly narrow circumstances. This thesis then examines alternative mechanisms that may be used to identify and deter frivolous and abuse of process claims, and proposes a mandatory evaluative

conciliation procedure prior to arbitration as the effective option to facilitate early dismissal of frivolous and abuse of process claims. This pre-screening mechanism would provide opportunities for assessment of claims in a flexible and non-adversarial context, and would take the gatekeeping function out of the hands of arbitral tribunals, which are not well placed to perform it.

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List of Abbreviations

BIT	Bilateral Investment Treaty
CAFTA	Central American Free Trade Agreement
CETA	Comprehensive Economic and Trade Agreement
ChAFTA	China-Australia Free Trade Agreement
CSR	Corporate Social Responsibility
CPTPP	Comprehensive and Progressive Agreement for Trans-Pacific Partnership
ECT	Energy Charter Treaty
EC	European Commission
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
FET	Fair and Equitable Treatment
FPS	Full Protection and Security
FCN	Friendship Commerce and Navigation Agreements
GA	General Assembly
MAI	Multilateral Agreement on Investment
MFN	Most Favoured Nation
MST	Minimum Standard of Treatment
NGO	Non-Governmental Organization
NAFTA	North American Free Trade Agreement
IIAs	International Investment Agreements
ICJ	International Court of Justice

ICC	International Chamber of Commerce
ICSID	International Centre for Settlement of Investment Disputes
ICTY	International Criminal Tribunal for the former Yugoslavia
IISD	International Institute for Sustainable Development
IMF	International Monetary Fund
ISA	investor-state arbitration
ISDS	investor-state dispute settlement
LCIA	London Court of Arbitration
OECD	Organisation for Economic Co-operation and Development
PCIJ	Permanent Court of International Justice
SC	Security Council
SCC	Stockholm Chamber of Commerce
SIAC	Singapore International Arbitration Centre
TPP	Trans-Pacific Partnership
TTIP	Transatlantic Trade and Investment Partnership
VCLT	Vienna Convention on the Law of Treaties
WTO	World Trade Organization
UN	United Nations
UN ECOSOC	United Nations Economic and Social Council
UNCITRAL	United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development

Chapter 1

Introduction

Foreign investors can sue sovereign states for the purported breaches of international investment agreements (IIAs) under the mechanism of investor-state arbitration (ISA).[1] The investors' claims are easy to file but may be difficult and costly to defend.[2] The *Sydney Morning Herald* reports that Australia's costs for defending the claim of Phillip Morris on plain-packaging amounts to as much as USD 37 million.[3] If this information is accurate, such fees are significant, particularly given that the governments' funds come from the pockets of taxpayers.[4] A study conducted by multinational law firm Allen & Overy, however, shows that average costs of investment arbitration in 2014 were "US$4,437,000 for claimants and US$4,559,000 for respondents based on a review of 176 ISDS awards".[5] These numbers, as Diane Desierto points out, "invite scrutiny into States' uses of public funds in investor-State disputes, especially when one recalls States' continuing obligations to fulfil economic, social, and cultural

[1] Rudolf Dolzer & Christoph Schreuer, *Principles of International Investment Law* (Oxford: Oxford University Press, 2012).
[2] In addition to direct monetary costs, the ISA claims carry on social costs, and may generate regulatory chill. These issues are discussed in section 1.1.2.
[3] Adam Gartrell, Philip Morris Ordered to Pay Australia Millions in Costs for Plain Packaging Case, online:< https://www.smh.com.au/politics/federal/philip-morris-ordered-to-pay-australia-millions-in-costs-for-plain-packaging-case-20170709-gx7mv5.html>.
[4] Giuseppe Bianco, "Publication of Information at the Commencement of Arbitral Proceedings" in Dimitrij Euler et al, eds, *International Investment Arbitration: A Guide to the UNCITRAL Rules on Transparency in Treaty-Based Investor-State Arbitration* (Cambridge: Cambridge University Press, 2015) at 87.
[5] Jeffery Commission, "How Much Does an ICSID Arbitration Cost? A Snapshot of the Last Five Years" (29 February 2016), Kluwer Arbitration (blog), online:< http://arbitrationblog.kluwerarbitration.com/2016/02/29/how-much-does-an-icsid-arbitration-cost-a-snapshot-of-the-last-five-years/>.

rights owed to their populations".[6] Accordingly, the claims of foreign investors may be costly for governments, and one may say that justice is in principle costly, although worth the costs if it means investors' rights are vindicated and rogue governments are held accountable.

Foreign investors, however, do not always file their claims against states to vindicate their rights;[7] instead, they may seek to "game" the ISA system by filing claims that lack merit or constitute an abuse of process.[8] For instance, after almost seven years of proceedings, the Phillip Morris claim against Australia was dismissed as an "abuse of process" because (as the ISA tribunal eventually decided) the company undertook a corporate restructuring illegitimately for the sole purpose of gaining access to the protections of an IIA that otherwise would not have applied to it.[9]

This thesis examines the problem of frivolous and abuse of process claims in international investment arbitration: what threats they impose, how current rules and practices regulate the dismissal of such claims, and how those rules and processes might be improved. Accordingly, this thesis examines the mechanisms for the early dismissal of frivolous and abuse of process claims within the broader political, legal, and sociological context of the international investment regime. Such a contextual approach is valuable

[6] Diane Desierto, "Rising Legal Costs Claimed by States in Investor-State Arbitrations: The Test of 'Reasonableness' in Philip Morris v. Australia" (2017), EJIL, online:< https://www.ejiltalk.org/rising-legal-costs-claimed-by-states-in-investor-state-arbitrations-the-case-of-philip-morris-v-australia/>.

[7] Some commentators go as far to suggest that foreign investors (with assistance of lawyers) are "modern pirates" that intentionally pursue claims against states in "weakened conditions" to extract compensations or revert governmental regulation. Pia Eberhardt & Cecilia Olivet, "Modern Pirates: How Arbitration Lawyers Help Corporations Seize National Assets and Limit State Autonomy" (2018) 77:2 American Journal of Economics and Sociology 279 at 291-296.

[8] UNCTAD, *Issues Related to International Arrangements, Investor-State Disputes and Policy Implications*, TD/B/COM.2/62 (New York: United Nations, 2005) at para. 7. (The Report states that "there have been fears about frivolous or vexatious claims that could inhibit legitimate regulatory action by Government"). [UNCTAD (2005)].

[9] Andrea Bjorklund, "The Legitimacy of ICSID" in Harlan Grant Cohen et al, eds, *Legitimacy and International Courts* (Cambridge: Cambridge University Press, 2018) at 250 (discussing abuse of process and forum shopping).

because it can inform the drafting of future international investment treaties by teaching that the development of new procedural mechanisms must take into the account broader context of the system in which such mechanisms are to function.

By contextual approach, I mean an approach which takes into account the fact that procedural mechanisms do not stand alone, but rather operate within a system's structures and the incentives for participants that those structures create.[10] This approach is inspired by the literature on "legal transplants", a field of comparative legal scholarship that explores the features of legal systems and how they enable the inter-systemic transfer of legal principles, mechanisms, institutions, and norms. Strictly speaking, the project is not a comparative one, in other words, it does not compare two or more jurisdictions, systems, or legal traditions. Instead, this thesis focuses on vertical bottom-up legal transplantation, whereby norms, principles, institutions, and mechanisms are borrowed from domestic legal systems and imported into international law by uncoordinated, organic processes through the dynamic interactions between the states, foreign investors, arbitration participants and arbitration institutions.

Adoption of the "legal transplant" framework helps to achieve two goals. First, it makes possible an appreciation of the systemic context when legal borrowing occurs, since the existing procedures for regulation of frivolous and abuse of process claims in international investment arbitration have been adapted from domestic legal models.

[10] Of course, we talk here about the "perceived incentives" that the system's structures can potentially generate. OECD, Directorate for Financial and Enterprise Affairs Organisation for Economic Co-operation and Development, *Appointing Authorities and the Selection of Arbitrators in Investor-State Dispute Settlement: An Overview*, Consultation Paper (2018), online:<https://www.oecd.org/investment/investment-policy/ISDs-Appointing-Authorities-Arbitration-March-2018.pdf> at para.33. (A similar approach has been taken by the OECD ("[t]he focus is on perceived incentives; no view is expressed about whether any particular incentives have any actual impact on appointing authority action. As elsewhere, however, perceptions about incentives can be important facts to be considered by policy makers in adjudication systems").

Second, it enriches thinking about procedural mechanisms in international law through the lens of comparative legal scholarship. These key points will be developed in greater detail in Chapters Four and Five of this thesis.

To ensure that the procedural mechanisms operate adequately to achieve their declared purpose (that is, are effective),[11] it is essential to examine such mechanisms within the broader context of the system within which they operate, particularly that system's structural features and the incentives those structures create. This thesis undertakes exactly such an endeavour and, in doing so, seeks to answer a series of related research questions.

Some questions are prescriptive whereas others are descriptive. The descriptive questions seek to identify what constitutes a frivolous or abuse of process claim in the investment regime and to determine how the currently existing mechanisms for the dismissal of such claims function. Specifically, the descriptive questions are the following: "Why are frivolous and abusive claims problematic? What costs/harms do they impose? Why do foreign investors bring them? What procedures currently exist for dealing with frivolous and abuse of process claims? What criteria are used for early dismissal? Where in the arbitral process are frivolous and abusive claims addressed? Who is in charge of considering whether to dismiss them? How are arbitrators likely to decide on applications to dismiss frivolous and abusive claims?"

The prescriptive research questions are intended to identify a strategy for effectively responding to challenge posed to the investment regime by frivolous and abuse of process claims. They are: "what procedures for early dismissal are likely to be

[11] Yuval Shany, "Assessing the Effectiveness of International Courts: A Goal Based Approach" (2012) 106:2 AJIL 225 at 230 ("the rational-system approach, which offers a straightforward formulation: an action is effective if it accomplishes its specific objective aim").

more effective? Can measures other than dismissal by investment arbitration tribunals work (e.g. cost-shifting)? Would switching to a more judicial-type body of adjudicators work? When and by whom should frivolous and abusive claims be screened out?" This dissertation addresses these questions but not necessarily in this order.

To study the mechanisms for the dismissal of frivolous and abuse of process claims, this thesis employs conventional doctrinal legal methodology, which requires analysis of international treaties, relevant legislation, case-law, and doctrine. The doctrinal study includes writings of international arbitrators, commentaries of international institutions such as UNCTAD and ECOSOC, and commentaries of scholars. Where relevant, this study examines various publicly available materials, such as interviews with arbitrators, judges and World Bank officials and the diplomatic cables publicized by WikiLeaks in 2010.

This chapter consists of six main subsections, the purpose of which is to introduce the readers to the project by defining the terms employed in this thesis, providing a detailed overview of the project, situating the project within a broader context of the literature on the investment arbitration. It also provides an overview of the theoretical framework that this project employs.

1.1 Overview of the Key Terms and Reasons Why Frivolous and Abuse of Process Claims Are Problematic

This section provides an overview of the key terms employed in this thesis and explains why frivolous and abuse of process claims are problematic in the context of the investment regime.

1.1.1 Defining Terms

Before delving into the discussion on frivolous and abuse of process claims, it is necessary to explain what the notion of international investment regime means.[12] The regime is composed of IIAs and the dispute settlement mechanism known ISA.[13] The term "regime" in this dissertation is broadly understood in the sense proposed by Krasner: ". . .principles, norms, rules, and decision making procedures around which actors' expectations converge in a given area of international relations".[14] The investment regime functions through "stand alone"[15] IIAs and independently-operating ISA tribunals. Such a decentralized character encourages some authors to contest the application of the notion "regime" to what can also be regarded as a disorganized bundle of the investment treaties and independent *ad hoc* tribunals.[16] The term "regime", however, helps to systemically organize thinking about the actions and reactions of the regime's key participants (states, foreign investors, tribunals and arbitration centres)[17] that contribute to the rule development on investment protection.[18]

[12] For greater clarity, the terms the "investment regime" and "international investment regime" are used interchangeably throughout this thesis.
[13] Dolzer & Schreuer (2012), at 28.
[14] Stephen Krasner, *Power, the State, and Sovereignty: Essays on International Relations* (London: Routledge, 2009) at 113.
[15] Jeswald Salacuse, "The Emerging Global Regime for Investment" 51:2 (2010) Harv Intl L J 427.
[16] Martins Paparinskis, "Good Faith and Fair and Equitable Treatment in International Investment Law" in Andrew Mitchell, Muthucumaraswamy Sornarajah & Tania Voon, eds, *Good Faith and International Economic Law* (Oxford: Oxford University Press, 2015) at 144 ("[w]hether international investment law is a hybrid regime in search of its identity, an accidental combination of different unrelated developments, a run-of-the-mill regime of international law, or something entirely different, is a question about which reasonable people may disagree"). James Crawford & Penelope Nevill, "Relations between International Courts and Tribunals: The "Regime" Problem" in Margaret Young, ed, *Regime Interaction in International Law: Facing Fragmentation* (Cambridge: Cambridge University Press, 2012) at 235, 258–259.
[17] From the outset, it is necessary to underscore that participants of the investment regime are different from the stakeholders of the regime. In this dissertation, the notion "stakeholders" is broader and includes the actors that are affected by the investment regime but do not necessarily participate in the investment regime by virtue of rule-making or litigation. In contrast, the key participants directly participate in the regime and as such contribute to its evolvement.
[18] Cédric Dupont & Thomas Schultz, "Towards a New Heuristic Model: Investment Arbitration as a Political System" (2016) 7:1 Int Disp Settlement 3.

For greater clarity and to ensure terminological consistency, it is necessary to define some key terms. Black's Law Dictionary defines a "frivolous claim" as one "that is not legally tenable and as such is worthless".[19] Accordingly, such claims clearly have no legal merit. In this thesis, the term "frivolous claims" encompasses two categories of claims, those that "manifestly lack legal merit" and those "in which an award in favour of a claimant cannot be made". In general, this thesis will use the term "frivolous" to describe both categories of claims. At times, however, it will be useful to distinguish between them. As will be discussed in Chapters Three and Four, IIAs, ISA tribunals and the applicable arbitration rules employ such formulations.

An abuse of process claim is a "legal action that is regarded by the courts as misuse or even abuse of the legal process".[20] This dictionary definition of abuse of process is not particularly helpful, except to reaffirm that a claimant or respondent should not misuse legal procedure.[21] It does not elucidate what kind of misuse is relevant and under what circumstances such misuse will result in the dismissal of a claim as an abuse of process. The definition thus requires assessment of an action in the context of a given system and, thus, confers a broad discretion on adjudicators.

Notably, there is overlap between the two concepts; they can be conflated and confused. As will become apparent in Chapter Three, even domestic legal systems suffer from terminological inconsistency when operating with these categories of claims. Abuse

[19] Black's Law Dictionary, 2nd ed, sub verbo "frivolous action", online, <http://thelawdictionary.org/frivolous-action/>.
[20] Black's Law Dictionary, 2nd ed, sub verbo "abuse of process", online:< http://thelawdictionary.org/abuse-of-process/>.
[21] IIAs rarely incorporate any reference to abuse of process, and to the author's knowledge no IIA defines this concept. For example, in *Iran-Slovakia BIT* (2016), at art.14(c), IIA provides that a claim may be dismissed as an abuse of process, but gives no explanation of what constitutes abusive conduct, not does it provide tribunals with any other guidance as to when the power to dismiss abuse of process claims should be exercised. See also the *Colombia-UK BIT* (2010), at art.9.12.

of process claims are often addressed as "the claims that misuse legal process" or "abuse of rights" claims. For greater clarity, this thesis considers the terms "abuse of process" and "abuse of rights" as two manifestations of a single concept that aims to prevent the manipulation or exploitation of legal rights in a way that contradicts the very purpose of those rights.[22]

In ISA, abuse of process claims arise in four sets of circumstances, examined in detail in Chapter Four of this thesis that employs Emmanuel Gaillard's categorization.[23] Gaillard identifies the following broad scenarios when the ISA tribunals can dismiss claims as abuse of process. First, an abuse of process may arise from the manner in which a corporate investor seeks to secure the jurisdiction of an arbitral tribunal, for example by corporate restructurings purely for the purpose of securing jurisdiction or accessing the protections of a particular IIA.[24] Second, an abuse of process may occur when a foreign investor "initiates more than one proceeding to resolve the same or related dispute in order to maximize its chances of success".[25] Third, an abuse of process may materialize when a foreign investor brings a claim to acquire a benefit "inconsistent with the purpose of investment arbitration".[26] A fourth scenario that Gaillard does not mention explicitly

[22] The tribunal in Phillip Morris uses the terms abuse of process and abuse of rights interchangeably without drawing distinction. *Philip Morris Asia Limited v The Commonwealth of Australia* (2015), Award on Jurisdiction and Admissibility, PCA Case No. 2012-12 (Permanent Court of Arbitration) (Arbitrators: Gabrielle Kaufmann-Kohler, Don McRae, Karl-Heinz Böckstiegel) [Philip Morris v Australia] at para.585. Other positions also exist: Zimmerman explains the difference as follows "abuse of process is a special application of the prohibition of abuse of rights […] it consists of the use of procedural instruments or rights by one or more parties for the purposes which are alien to those for which the procedural rights were established". Andreas Zimmermann *et al*, eds, *The Statute of the International Court of Justice: a Commentary* (Oxford: Oxford University Press, 2006) at 831. Eric De Brabandere ''Good Faith'', ''Abuse of Process'' and the Initiation of Investment Treaty Claims' (2012) 3:3 J Intl Disp Settlement 609. (argues that abuse of process is a special manifestation of abuse of rights).
[23] Section 4.2.2.of this thesis.
[24] Emmanuel Gaillard, "Abuse of Process in International Arbitration" (2017) ICSID Rev 1 at 3.
[25] *Ibid* at 6.
[26] *Ibid* at 10. (As two examples of such conduct, Gaillard points to the action of a German state-owned company, which brought an arbitration claim before the ICC to gain publicity, and to the investment

but which he seems to imply throughout his paper encompasses conduct by parties that violates the integrity of the tribunals' processes.[27]

A disclaimer must be made that in discussing abuse of process claims in the investment regime, this thesis will not consider claims in which foreign investors violated the domestic law of the host state or claims in which an investor was engaged in the bribery of foreign officials or human rights violations.[28] While such claims also imply investors' misconduct, tribunals have not characterized them as abuses of process; in ISA, the doctrine of abuse of process has a much narrower application. In some cases of investor misconduct, for example when the investor was engaged in bribery, the tribunals have dismissed claims on the basis that the investor did not comply with the domestic law

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dispute *Rompetrol Group NV v Romania*, where the claimant launched the arbitration for the sole purpose of "terminat[ing] or to hinder[ing] legitimate criminal proceedings and investigations in Romania"). *RomPetrol v Romania* (2008), Decision on Respondent's Preliminary Objections on Jurisdiction and Admissibility ICSID Case No ARB/06/03 (International Centre for Settlement of Investment Disputes) (Arbitrators: Franklin Berman, Donald Francis Donovan, Marc Lalonde) at para.59. [*RomPetrol v Romania*]

[27] Lucy Reed, "Ab(use) of Due Process: Sword vs Shield" (2017) 33 Arbitration International 361 at 375. (It is yet not clear what particular actions result in such categorization. As will be discussed in Chapter Four, the tribunal in *Waste Management* highlights this possibility but does not give an example of what actions will constitute such a violation. Lucy Reed suggests that integrity of the tribunals'processess can be violated if, "a party—in the name of due process, its counsel's hand on heart—may insist on: 1) Extension after extension—'just because we need it, or else . . .'; or on 2) Postponing a hearing because a witness or client 'somehow' accepted a conflicting engagement; or on 3) Jettisoning the timetable to instruct 'necessary' new or additional counsel; or on 4) Stubbornly pursuing a virtual death march of document disclosure disputes—each document more 'critical' to presenting its case than the last; or on locking closure of the proceedings by introducing new evidence after posthearing submissions. Most often, abuse of due process is all of the above. It also feeds on itself. For example, one side might apply to put in late evidence, again 'absolutely critical to allow it to present its case'. If the tribunal says no, the applicant's due process flag goes up. If says yes, the other party will hoist its due process flag, claiming prejudice unless it is allowed to respond to the new evidence, which may postpone the hearing or lead to one or both parties claiming prejudice. And so on, perhaps not ad infinitum but quite likely ad nauseam").

[28] Andrew Newcombe, "Investor Misconduct: Jurisdiction, Admissibility or Merits?" in Chester Brown & Kate Miles, eds, *Evolution in Investment Treaty Arbitration* (Cambridge: Cambridge University Press, 2011) at 187. *Plama Consortium Limited v Bulgaria* (2008), Award ICSID Case No. ARB/03/24, 44 ILM 721 (International Centre for Settlement of Investment Disputes) (Arbitrators: Carl Salans, Albert Jan van den Berg, Van Vechten Veeder) at para. 129,135 (misrepresentation of investor's identity to the local authorities and fraud) [*Plama Consortium*]. *Inceysa Vallisoletana S.L. v Republic of El Salvador* (2006), Award ICSID Case No. Arb/03/26, (International Centre for Settlement of Investment Disputes) (Arbitrators: Rodrigo Oreamuno Blanco, President Burton Landy, Claus von Wobeser). *Freeport AG Frankfurt Airport Services Worldwide v Philippines* (2007), Award ICSID Case No. ARB/03/25 (International Centre for Settlement of Investment Disputes) (Arbitrators: Yves Fortier, Bernardo Cremades,Michael Reisman) at para.396-402.

of the host state.[29] Accordingly, the tribunals seem to characterize such claims under the rubric of illegality or violation of "international public policy", rather than abuse of process.[30]

Although an investor's claim may be both frivolous and abusive, frivolous claims must be distinguished from abuse of process claims (at least in the context of the investment regime). Frivolous claims are claims that have no legal foundation or prospect of success as a matter of law. The party that brings such a claim may unrealistically overestimate the claim's chances of success.

In contrast, abuse of process claims may very well have legal merit. They aim to manipulate or somehow exploit the legal process, i.e. to take advantage of the process in a way that will contradict the very purpose for which such legal process exists. In *Saipem SpA v the People's Republic of Bangladesh*, the tribunal noted that "[i]t is generally acknowledged in international law that a State exercising a right for a *purpose* that is different from that for which that right was created commits an abuse of rights".[31] Admittedly, the definition is rather vague and, thus, confers broad discretion upon tribunals. Explaining the way tribunals do and should make use of that discretion is one of the goals of this thesis, pursued in Chapters Four.[32]

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[29] *World Duty Free Company Limited v Kenya* (2006), Award ICSID Case No. ARB/00/07, 46 ILM 337 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gilbert Guillaume, Andrew Rogers, V.V.Veeder) at para.188. Newcombe (2011), at 204.

[30] *Ibid* at para.157 ("in light of domestic laws and international conventions relating to corruption, and in light of the decisions taken in this matter by courts and arbitral tribunals, this tribunal is convinced that bribery is contrary to the international public policy of most, if not all, States or, to use another formula, to transnational public policy. Thus, claims based on contracts of corruption or on contracts obtained by corruption cannot be upheld by this arbitral tribunal").[Emphasis added].

[31] *Saipem SpA v The People's Republic of Bangladesh* (2009), Award ICSID Case No ARB/05/07, 48 ILM 996 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gabrielle Kaufmann-Kohler, Christoph Schreuer, Philip Otton) at para.160. [Emphasis added] [*Saipem*].

[32] Sections 4.2.2.1-4.2.2.4.

It is worth noting that investors can be aware that the claim is weak or likely to be a loser but still choose to sue for tactical reasons. In my view, such claims will fall into the category of abuse of process because the objective of the claimant is not to vindicate its rights but to obtain the leverage against the state possibly with the purpose to achieve profitable settlement. To author's knowledge, however, the ISA tribunals so far have not discussed or categorized such claims as abuse of process in their decisions.

1.1.2. Why Frivolous and Abuse of Process Claims Are Problematic in the Investment Regime?

This section briefly identifies why frivolous and abuse of process claims may be particularly problematic in the investment regime. There are two main reasons: such claims can impose unreasonable and disproportionate costs, and they undermine credibility of the investment regime. Before examining these reasons in greater detail, it is worth noting that costs and credibility arise as important concerns for all types of ISA claims, not only frivolous and abuse of process claims.

However, in the context of frivolous and abuse of process claims, these concerns (as Krzysztof Pelc rightly points out) are exacerbated by the systemic feature of the investment regime known as "private standing",[33] which refers to the unilateral ability of investors to launch investment arbitrations, and to do so at relatively low financial cost (by simply filing the notification about an intent to bring the claim) and correspondenly low reputational cost (as they generally cannot be countersued).[34]

Private standing creates an asymmetry that skews incentives, in part because investors can easily obtain leverage by merely threatening to bring a claim in ISA or by

[33] Krzysztof Pelc, "What Explains the Low Success Rate in Investor-State Disputes" (2017) 71:3 International Organization 559 at 565-566.
[34] *Ibid*.

filing a notice to arbitrate. Even an unmeritorious or manipulative claim requires the respondent state to spend resources to conduct at least a preliminary evaluation of the claim. Investors bear no such burden and may therefore be willing to launch claims to explore the boundaries of a legal argument or for other tactical reasons. In addition, private standing creates distinctive dynamics in the ISA process in comparison to state-to-state dispute resolution because it "eliminates an important source of restraint against raising legal challenges by doing away with reciprocity and the fear of retaliatory challenges".[35] These factors, separately and in combination, alter the dynamics of claim filings, particularly if foreign investors "filing these claims may derive a benefit from litigation no matter whether they win if they are able to sway policy".[36] In light of these factors, frivolous and abuse of process claims exacerbate costs and credibility concerns in ISA.

1.1.1.1 Monetary, Social and Political Costs

Frivolous and abuse of process claims are problematic for at least two reasons. First, such claims impose monetary costs on the states respondents. Second, such claims may result in broader social and political costs. According to United Nations Conference on Trade and Development,

> investors may abuse the system. Investors may be eager to claim as many violations of the applicable IIAs as possible in order to increase their chances of success. This may take a heavy toll in terms of time, effort, fees and other costs, not only for the parties to the dispute, but also for the arbitral tribunal.[37]

[35] *Ibid*.
[36] *Ibid* at 580.
[37] UN, *United Nations Conference on Trade and Development, Investor-State Dispute Settlement and Impact on Investment Rulemaking* (New York: United Nations Publications, 2007) at 82.

When foreign investors make an investment claim, state respondents have to spend resources to defend the claims. It is necessary to remember that "suits are easy to file and hard to defend". This way "litigation becomes a predatory instrument rather than a method of resolving honest disputes".[38] In the domestic settings, there are many examples of such conduct. For instance, claimants can choose to bring the lawsuits with a sole objective to drive participants from the market or extract favourable settlements.[39] In domestic litigation, 'patent trolls' have a business model of threatening claims against other market participants with a purpose to extract favourable settlement.[40] In the context of investment arbitration, claimants can drag respondents into expensive and long arbitration proceedings, with the purpose not to vindicate their legitimate grievances, but in hope to impose costs upon the defending governments.

The issue of costs becomes particularly acute in the context of persisting inequality of states. Of course, international law mandates that all states are equal sovereigns. The social and economic reality is however different; states are not equal in their capacity to resists a potential pressure of costly investor's claims and proceedings. Developing and least developed nations can be particularly vulnerable and sensitive to

[38] Mark Kravitz, "Unpleasant Duties: Imposing Sanctions for Frivolous Appeals" (2002) 4 J App Practice & Process 335.
[39] Bita Amani, *State Agency and The Patenting of Life in International Law: Merchants and Missionaries in A Global Society* (Burlington: Ashgate, 2009).
[40] *Ibid* at 68.

how the tax dollars are spent. [41] Investment disputes can generate significant "social costs" that may be a serious burden for poorer states or states with smaller economies.[42]

For the governments of developed states, investment arbitration can also be a costly enterprise. Admittedly, developed states with large economies most likely can afford to uphold defences against arbitration claims. While some developed states can afford to pay the legal costs, they may be unable to afford the "political" costs of defending such claims. When the government has to participate in arbitration proceedings, it may be difficult for the government to rationalize for domestic stakeholders why money is spent to defend against an apparently frivolous or abuse of process claim. For instance, in Germany, the UK and Australia, there were serious parliamentary debates regarding whether these states should participate at all in ISA. [43]

1.1.1.2 Credibility Concerns

Foreign investors can submit claims to achieve other strategic purposes beyond vindicating their rights under investment treaties.[44] Taylor St John documents such

[41] Some states have to use third-party funding and expertise to carry on the defense. For example, Uruguay was able to survive a legal battle against tobacco companies only with the financial and expert support of Michael Bloomberg and other anti-tobacco advocates. Heather Wipfli, *The Global War on Tobacco: Mapping the World's First Public Health Treaty* (Baltimore: JHU Press, 2015) at 132. UNCTAD at para. 17-19. Similar work has been done in the context of World Trade Organization (WTO), Joan Apecu Laker, *African Participation at the World Trade Organization: Legal and Institutional Aspects 1995-2010* (The Hague: Martinus Nijhoff Publishers, 2013) at 20.

[42] Profiting from Injustice at 15.

[43] Luke Nottage, *Investor-State Arbitration Policy and Practice in Australia* (2016) CIGI Research Paper No 6. Leon Trakman, "Investor-State Arbitration: Evaluating Australia's Evolving Position" (2014) 15:1 JWIT 152. Marc Burgenberg, *A History of Investment Arbitration and Investor-State Dispute Settlement in Germany*, ISA Paper No.12, online:<https://www.cigionline.org/publications/history-investment-arbitration-and-investor-state-dispute-settlement-germany>. In Canada, some prominent academics signed the petition that condemns the investment regime for its pro-investor orientation. Gus Van Harten *et al*, *Public Statement on the International Investment Regimes - 31 August 2010*, available online:<http://www.osgoode.yorku.ca/public-statement-international-investment-regime-31-august-2010/>. [Public Statement on ISA].

[44] Strategic use of litigation is a popular tactic that claimants pursue in the domestic settings. Frederick Lipman, *Whistleblowers: Incentives, Disincentives, and Protection Strategies* (New York: John Wiley & Sons, 2011). In the US Congress, one of the witnesses called sham litigation "an anticompetitive practice", "a deadly weapon" that "results in extorting the tax payers money by using the threat of legal action".

conduct the early ISA cases when corporation Alcoa brought a claim against Jamaica for introducing a tax on mining operations, reportedly, to fund an "educational reform".[45] The measure was quite popular in Jamaica at the time with the media reporting that "every Jamaican stands two inches taller today and the Prime Minister four inches".[46]

According to St John, Alcoa filed a claim in ICSID against Jamaica – to the great frustration of the US Justice Deparment that was overly concerned that the claim will jeopardize friendly relations between the two counrties – only to "negotiate from the strongest position they can possibly develop" and to show to their "stockholders" that the company used all possible legal remedies available.[47] Henry Kissinger, the United States Secretary of State and National Security Advisor, also observes that "Alcoa Executives [...] believe [that] existence of their suit against GOJ is key lever in negotiations, and they intend to keep this pressure on GOJ until agreement is reached".[48] The Alcoa executives intended to keep the ICSID claim ongoing but "without coming to a judgment during negotiations".[49] An investor delayed proceedings and leveraged the claim in ICSID to extract more favourable conditions in negotiations with Jamaica.

If foreign investors submit claims without merit, launch multiple proceedings or intentionally delay the process of arbitration, it may influence the positions of states with

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Corporations can display similar behavioural patterns, particularly when they have something to gain. Michael Meurer, "Controlling Opportunistic and Anti-Competitive Intellectual Property Litigation" (2002-2003) 44 B.CL Rev 509 at 511.

[45] Taylor St John, *The Rise of Investor-State Arbitration* (Oxford: Oxford University Press, 2018) at 214-217.

[46] WikiLeaks cable 1974KINGST01762_b (Microfilm, Bureau of Inter-American Affairs).

[47] St John (2018), at 197. Julian Lew, *Contemporary Problems in International Arbitration* (The Hague: Brill Archive, 1987) at 25-26 (generally discussion on the jurisdictional aspects of Jamaican cases in ICSID).

[48] WikiLeaks cable 1976STATE012599_b at para.2 (Microfilm, Alcoa Negotiations: Bureau of Inter-American Affairs).

[49] *Ibid* at para.1. Wikileaks cable 1975KINGST05000_b at para.1 (Microfilm, Alcoa Negotiations: Bureau of Inter-American Affairs) ("as evidence of good faith Alcoa will undertake to to do whatever is necessary to delay ICSID proceedings").

regards to the participation in the investment regime. In other words, such claims can undermine the regime's credibility and exacerbate its legitimacy deficits. Tania Voon, Andrew Mitchell, and James Munro have found that even a single investment claim can trigger a state reaction against the investment regime.[50]

1.2 Overview of the Project

In the international investment regime, foreign investors can sue sovereign states for purported breaches of IIAs[51] before tribunals usually composed of three arbitrators.[52] Of course, in many instances foreign investors bring ISA claims to vindicate their rights in cases of genuine mistreatment by a state. For example, an investor may bring a claim if a state expropriates the investor's assets, undertakes some discriminatory actions or violates due process against the investor.[53] But ISA is also susceptible to various abusive tactics similar to those confronted by national courts.[54] Foreign investors have changed their nationality in order to gain illegitimate access to the protections available under

[50] Tanya Voon, Andrew Mitchell & James Munro, "Parting Ways: The Impact of Investor Rights on Mutual Termination of Investment Treaties" (2014) 29:2 ICSID Rev 451 at 452. (Tanya Voon, Andrew Mitchell & James Munro recognize impact of particular disputes on states and on the regime. They argue that "Specific disputes may also provide an independent motivation for parties to terminate an IIA").
[51] Stephan Schill, "Authority, Legitimacy, and Fragmentation in the (Envisaged) Dispute Settlement Disciplines in Mega-Regionals" in Stefan Griller, Walter Obwexer & Erich Vranes, eds, *Mega-regional Trade Agreements: CETA, TTIP, and TiSA: New Orientations for EU External Economic Relations* (Oxford: Oxford University Press, 2017) at 146.
[52] Fernando Tupa, "Arbitrator Challenges in Investment Arbitration: Is an Overhaul Needed?" in Ian Laird et al, eds, *Investment Treaty Arbitration and International Law* (New York: Juris Publishing) at 29-30, 37-45.
[53] Christopher Dugan et al, *Investor-State Arbitration* (New York: Oxford University Press, 2011) at 41-42.
[54]August Reinisch, "The Issues Raised by Parallel Proceedings and Possible Solutions" in Michael Waibel, *The Backlash against Investment Arbitration: Perceptions and Reality* (The Hague: Wolters Kluwer, 2010) at 114. (phenomena familiar to any national legal system but rather foreign to international law appeared on the international scene: litigants engaging in strategic considerations about where and how to bring their claims (forum shopping), litigants trying to pursue their claims before different fora, be it simultaneously or subsequently (duplication or multiplication of proceedings), different courts and tribunals reaching different or sometimes even contradictory results with regard to similar or even identical issues (divergent outcomes/ inconsistent decisions). The threat of unpredictability and instability easily fed into international lawyers' fears of fragmentation of international law). Gaillard (2017), at 3-4.

IIAs,[55] have initiated multiple parallel proceedings to increase the likelihood of a favourable outcome,[56] have submitted fraudulent evidence in arbitral proceedings,[57] and have intentionally delayed the proceedings to impose costs and force a settlement.[58] In some cases, foreign investors knowingly bring claims that lack any legal merit.[59]

Arbitration rules and IIAs incorporate provisions that empower ISA tribunals to dismiss frivolous claims early in the proceedings, usually as a matter of preliminary objection. For example, the *International Centre for Settlement of Investment Disputes* (ICSID) Arbitration Rule 41(5) (added in 2006) permits dismissal of claims that "manifestly lack legal merit".[60] The *Singapore International Arbitration Centre* (SIAC) Arbitration Rule 29 (added in 2016) authorizes ISA tribunals to dismiss manifestly unmeritorious claims early in the proceedings.[61] Some IIAs also incorporate legal mechanisms for the dismissal of meritless claims. For example, the *Dominican Republic-Central America Free Trade Agreement* (DR-CAFTA), article 10.20 (4) allows tribunals to dismiss claims in which "an award in favour of a claimant cannot be made".[62] The

[55] Jorun Baumgartner, *Treaty Shopping in International Investment Law* (Oxford: Oxford University Press, 2016) at 221. Duncan Watson & Tom Brebner, "Nationality Planning and Abuse of Process: A Coherent Framework" (2017) ICSID Rev 1. Tania Voon, Andrew Mitchell & James Munro, "Legal Responses to Corporate Maneuvering in International Investment Arbitration" (2014) 5 J Intl Disp Settlement 41 at 61.
[56] Chin Leng Lim, Jean Ho & Martins Paparinskis, *International Investment Law and Arbitration* (Cambridge: Cambridge University Press, 2018) at 253. (discussing *Lauder v Czech Republic* and *CME v Czech Republic* arbitrations).
[57] Newcombe (2013), at 204 (discussing the *Cementownia S.A. v Turkey* case, in which the investor engaged in the sham transactions and presented the tribunal with false documents).
[58] Reed (2017), at 375.
[59] Rodrigo Polanco Lazo, "The Changing Role of the State in Investor-State Disputes" in Shaheeza Lalani & Rodrigo Polanco, *The Role of the State in Investor-State Arbitration Lazo* (The Hague: Martinus Nijhoff Publishers, 2014) at 244 (discussing emerging concerns over frivolous claims). Michele Potestà & Marija Sobat, "Frivolous Claims in International Adjudication: A Study of ICSID Rule 41(5) and of Procedures of Other Courts and Tribunals to Dismiss Claims Summarily" (2012) 3:1 J Intl Disp Settlement 137.
[60] *International Centre for Settlement of Investment Disputes: Regulations and Rules* (2017), 7 ILM 2 at 376, Rule 41(5). [ICSID Rules]
[61] Singapore International Arbitration Center (SIAC) Arbitration Rules, online:< http://www.siac.org.sg/our-rules/rules/siac-rules-2016 > at Rule 29 (1). [SIAC Arbitration Rules]
[62] *The Central America- Dominican Republic-United-States Free Trade Agreement* (2004), 43 ILM 514 at art.10.20, [DR-CAFTA].

Comprehensive Economic and Trade Agreement between the European Union and the Government of Canada (CETA) includes two provisions, which allow the early dismissal of claims that are (1) manifestly without legal merit or (2) in which an award in favour of a claimant cannot be made.[63] The record of deliberations in the Parliament of the United Kingdom on the *Transatlantic Trade And Investment Partnership* (TTIP) showed its intention to incorporate provisions on the early dismissal of frivolous claims in the treaty.[64] The publicly available text of the treaty demonstrates that the states followed up on this intention, as the final text incorporates a mechanism for the early dismissal of frivolous claims.[65] On frivolous claims, the *Comprehensive and Progressive Agreement for Trans-Pacific Partnership* (CPTPP) follows the CETA model and incorporates two provisions to dismiss claims that are manifestly without legal merit and claims in which an award in favour of a claimant cannot be made.[66] Claims without legal merit can be dismissed at the very early stages of the arbitration process as a matter of preliminary objection.[67] Chapter Four examines these mechanisms in a greater detail.

By contrast, most IIAs and arbitration rules do not include any provisions for the early dismissal of abuse of process claims.[68] ISA tribunals, however, have dismissed claims as abuses of process in their decisions. Accordingly, a tribunal can examine abuse

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[63] *Comprehensive Economic and Trade Agreement between the European Union and the Government of Canada* (2016), at article 8.32-8.33. [*CETA*]

[64] UK, *House of Commons: Business, Innovation and Skills Committee, HC 804 - Transatlantic Trade And Investment Partnership Great Britain* (London: The Stationery Office, 2015) at 15.

[65] TTIP at art.17; TPP at art.9.23(4).

[66] *Comprehensive and Progressive Agreement for Trans-Pacific Partnership* (2018), at article 9.23(4) and 9.29.

[67] *Brandes Investment Partners LP v Venezuela* (2009), Decision on the Respondent's Objection under Rule 41 (5) of the ICSID Arbitration Rules ICSID Case No. ARB/08/3, (International Centre for Settlement of Investment Dispute) (Arbitrators: Rodrigo Oreamuno, Karl-Heinz, Böckstiegel, Brigitte Stern) at para.12. [*Brandes*]

[68] It is worth noting that the new generation of treaties may require the tribunal to dismiss the claim if an investor's conduct amounts to an abuse of process. For example, *Iran-Slovakia BIT* (2016) at art.14 requires the tribunal to dismiss the claim outright if "the investor or investment" submitted a claim where its conduct amounted to an abuse of process.

of process allegations (usually made by a state) and can address them at any stage during the proceedings.[69] The authority of the tribunals to screen out claims as being an abuse of process is not explicitly stated in the relevant international treaties and arbitration rules, which led Chester Brown to the conclusion that international courts and tribunals have an inherent power to dismiss claims as abuses of process.[70] In justifying his position, Brown draws on the presumption that international adjudicatory bodies fulfil a public function: to contribute to the development of international law, to preserve the integrity of the adjudicatory process, and to prevent the administration of justice from falling into disrepute.[71] While in principle Brown's position is sound, it requires some further critical scrutiny in the context of the investment regime.

ISA tribunals exercise their powers based on the consent of the parties; the question is thus whether the parties empowered ISA tribunals of an *ad hoc* nature to exercise such a public function and what the limits on that function might be.[72] Thirlway warned against "attributing to an international tribunal […] inherent powers traced on the basis of municipal analogies. It needs to be recalled once more that the essence of

[69] *Ibid*. *Chevron and Texaco Petroleum Company v The Republic of Ecuador* (2008), Interim Award PCA Case No 34877, (United Nations Commission on International Trade Law) (Arbitrators: Karl-Heinz Böckstiegel, Charles Brower, Albert Jan van den Berg) at para 137.

[70] Chester Brown, *A Common Law of International Adjudication* (Oxford: Oxford University Press, 2007) at 245.

[71] Chester Brown, "The Inherent Powers of International Courts and Tribunals" (2006) 76:1 BY Intl L 195 at 231-232.

[72] The tribunals expressed divergent views, for example in Saipem and Romak as observed by Joshua Karton. Joshua Karton, "Choice of Law and Interpretive Authority in Investor-State Arbitration" (2017) 3:1 CJCCL 217 at 239. ("Rather, the point is that the Saipem tribunal was asking the wrong question – how should tribunals conceive of their role? – while the Romak tribunal was asking the right one – what role have the parties assigned to the tribunal?"). *Romak SA v The Republic of Uzbekistan* (2009), Award PCA Case No AA280, (United Nations Commission on International Trade Law) (Arbitrators: Fernando Mantilla-Serrano, Noah Rubins, Nicolas Molfessis) at para 171. ("the Arbitral Tribunal has not been entrusted, by the Parties or otherwise, with a mission to ensure the coherence or development of "arbitral jurisprudence." The Arbitral Tribunal's mission is more mundane, but no less important: to resolve the present dispute between the Parties in a reasoned and persuasive manner"). [*Romak*] *Saipem* at para 90 ("it has a duty to seek to contribute to the harmonious development of investment law and thereby to meet the legitimate expectations of the community of States and investors towards certainty of the rule of law").

jurisdiction is consent".[73] If the parties did not explicitly consent to confer such powers, it is "self-contradictory" to assume that they "implicitly consented to a wider power".[74] ISA tribunals, however, have dismissed claims as abuses of process in a number of cases (as discussed in Chapter Four) but they have done so with extreme caution. In part such caution may be result of the combination of factors such as lack of explicit instructions from the parties whether the arbitrators possess such powers or where the limits to such powers; the possibility of annulment or a potential risk of non-enforceability of an arbitral award. Accordingly, as currently designed, the procedural mechanisms for the dismissal of frivolous and abuse of process claims make the arbitrators the "gatekeepers" in charge of "policing" investors' claims in the investment regime.[75]

As mentioned, the investment regime is not insulated from frivolous and abuse of process submissions.[76] Two examples are worth considering to illustrate such claims. With regards to abuse of process claims in ISA, two factors are important to keep in mind. First, tribunals make such determinations on a case-by-case basis.[77] Second, tribunals are under no formal requirement to consider the dismissal of abuse of process

[73] Huh Thirlway, "The Law and Procedure of the ICJ 1960-1989: Part Nine" (1998) BY Intl L 1 at 21.
[74] *Ibid*.
[75] To my best knowledge, Diane Desierto was the first to employ the terms "gatekeeping" and "policing" in relation to abuse of process claims in ISA. I find Desierto's choice of words the most suitable for the question of whether arbitrators can effectively act as "policemen", given consensual nature of arbitral authority. Accordingly, I employ Desierto's terminology in this thesis. Diane Desierto, "Arbitral Controls and Policing the Gates to Investment Treaty Claims against States in Transglobal Green Energy v Panama" ICSID Case No. ARB/13/28,, and Philip Morris v Australia, EJIL, online:<https://www.ejiltalk.org/arbitral-controls-and-policing-the-gates-to-investment-treaty-claims-against-states-in-transglobal-green-energy-v-panama-and-philip-morris-v-australia/.
[76] Céline Lévesque, "Preliminary Legal Assessments of Investor Claims as a Tool to "Fitting the Forum to the Fuss" in Susan Frank and Anna Joubin-Bret, eds, *Investor-State Disputes: Prevention and Alternatives to Arbitration II*, Proceedings of the Washington and Lee University and UNCTAD Joint Symposium on International Investment and Alternative Dispute Resolution, (United Nations, 2011) at 77-79.
[77] *Tidewater v Bolivarian Republic of Venezuela* (2013), Decision on Jurisdiction ICSID Case No ARB/10/5, (International Centre for Settlement of Investment Disputes) (Arbitrators: Campbell McLachlan, Andrés Rigo Sureda,Brigitte Stern) at para.147 ("[u]nder general international law as well as under ICSID case law, abuse of right is to be determined in each case, taking into account all the circumstances of the case"). [*Tidewater v Venezuela*].

claims according to a particular timeline.[78] In *Phillip Morris v Australia*, Australia argued that Phillip Morris committed an abuse of process when it conducted a corporate restructuring for the sole purpose of gaining protections guaranteed under a particular IIA.[79] After five years of arbitral proceedings, the tribunal held that the change of nationality by Phillip Morris constituted an abuse of process and dismissed the claim as inadmissible at the jurisdictional stage of the proceedings.[80] The claim produced a significant backlash against investment arbitration, giving the impression that ISA as a system permits manipulations of state public policy regulations by powerful multinational corporations.

In *Methanex v United States*, a NAFTA arbitration, the USA argued that the Methanex's argument had no legal foundation and thus was inadmissible.[81] The tribunal, constituted under the *United Nations Commission on International Trade Law* (UNCITRAL) Arbitration Rules, refused to dismiss the claim as frivolous.[82] According to the tribunal, neither the UNCITRAL Arbitration Rules nor the NAFTA explicitly gave the tribunal the authority to declare a claim inadmissible on these grounds.[83] Without such express authorization, the tribunal found, it had no power to dismiss frivolous

[78] Gaillard (2017), at 17.
[79] *Philip Morris Asia Limited (Hong Kong) v The Commonwealth of Australia (2015)*, PCA Case No 2012-12, Award on Jurisdiction and Admissibility (United Nations Commission on International Trade Law) (Arbitrators: Karl-Heinz Böckstiegel, Donald McRae, Gabrielle Kaufmann-Kohler).
[80] *Ibid* at para. 585- 586.
[81] *Methanex Corporation v United States of America* (2002), Preliminary Award on Jurisdiction and Admissibility, 44 ILM 1345 (United Nations Commission on International Trade Law) (Arbitrators: William Rowley, Michael Reisman,Van Vechten Veeder) at para.109 ("the USA's challenges to admissibility are based upon the legal submission that, even assuming all the facts alleged by Methanex to be true, there could still never be a breach of the individual provisions pleaded by Methanex; and hence Methanex' claims are bound to fail, regardless of any factual evidence to be adduced by Methanex").
[82] *Ibid* at para.110, 126 ("The Tribunal faces an obvious practical problem in addressing the USA's various challenges. The parties' respective cases raise a large number of disputed issues of fact and law").
[83] *Ibid* at para.123-124. ("Article 21(1) of the UNCITRAL Arbitration Rules does not accord to the Tribunal any power to rule on objections relating to admissibility. There is no express power; and it is not possible to infer any implied power" […] "Nor is such a power to be found elsewhere in Chapter 11 NAFTA").

claims. In the wake of *Methanex*, the US incorporated provisions on the dismissal of frivolous claims into its 2004 Model BIT.[84]

The dismissal of frivolous and abuse of process claims in the investment regime seems to be modelled after domestic legal systems because it puts the arbitrators (as adjudicators) in charge of the dismissal.[85] In their awards, pleadings and memorials, the ISA tribunals, states and foreign investors themselves often refer to analogous legal instruments on frivolous and abuse of process claims that originate in domestic legal systems.[86]

This thesis does not attempt to show that all jurisdictions around the world have rules on the dismissal of frivolous and abuse of process claims or assert that such rules are consistent with each other. For example, in some common law jurisdictions abuse of process "generally operates to preclude proceedings 'if it is necessary for a court to prelude a misuse of its procedure' or 'to avoid the risk that the administration of justice might be brought into disrepute among right-thinking people".[87] As will become evident from Chapter Four, in civil law jurisdictions, the content and scope of abuse of process

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[84] Chester Brown, *Commentaries on Selected Model Investment Treaties* (Oxford: Oxford University Press, 2013) at 756. Edward Kehoe, "Motions to Dismiss in International Treaty Arbitrations" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers 2015* (The Hague: Brill, 2016) at 90.

[85] Brown (2007), at 242, 245-247. ("possibly inspired by the competence of certain domestic courts to strike out proceedings, in the past some international courts have recognized that they might possess power to dismiss proceedings before reaching the phase of litigation where they ordinarily decide on their jurisdiction"). Michael Byers, "Abuse of Process: An Old Principle, A New Age" (2002) McGill LJ 389 at 391-395 (discussing a principle of abuse of process in the domestic jurisdictions and how it got transferred into international law).

[86] *The Renco Group Inc v The Republic of Peru* (2010), Renco Submission Response to the Preliminary Objections UNCT/13/1, (United Nations Commission on International Trade Law) (Arbitrators: Michael Moser, Yves Fortier, Toby Landau) at para.7-8. [*Renco v Peru*]

[87] Brown (2007), at 231. Yuval Shany, *The Competing Jurisdictions of International Courts and Tribunals* (Oxford: Oxford University Press, 2004) at 258. ("even English law has long accepted the idea that abuse of rights should be proscribed in specific situations, including the exercise of rights in the framework of the legal process. Therefore, one can assert, for the purposes of the present thesis, that all main systems apply or, at least are willing to recognize, some kind of 'abuse of rights' rule in relation to the exercise of rights during adjudication").

varies significantly.[88] The dismissal of frivolous claims as a preliminary matter is largely a feature of common law rather than civil law jurisdictions.[89]

Nonetheless, as this thesis demonstrates in Chapter Four, domestic legal systems (both civil and common law) put *judges* in charge of identifying frivolous and abuse of process claims and dismissing such claims early in the proceedings. It appears that the design for dismissal in the investment regime follows the same pattern, i.e. the adjudicator empowered to rule on the merits identifies and dismisses such claims early. However, as Chapter Five demonstrates, arbitrators are not judges. Arbitrators are subject to different structural incentives and are involved in radically different social dynamics than judges in domestic courts. For example, arbitrators lack the procedural and administrative guarantees that ensure judicial independence. Those guarantees are designed for judges to preserve the integrity of the judicial system as a whole, of which a small part is the policing frivolous and abuse of process claims.

Investment arbitrators themselves are not particularly keen on exercising the power of early dismissal, and seem rather cautious.[90] For example, in *Rompetrol v Romania*, the tribunal rather carefully noted that "the Claimant's application for arbitration constitutes an abuse of process [...] is evidently a proposition of a very far reaching character".[91] The tribunal in *Rompetrol* was particularly concerned about dismissing the claim as an abuse of process after it established that it had jurisdiction to hear the dispute.[92] The tribunal observed that the dismissal of the claim as an abuse of process, "after having determined conclusively (or at least prima facie) that the parties to

[88] Jean-Francois Hebert, "Issues of Corporate Nationality in Investment Arbitration" in Armand De Mestral & Céline Lévesque, *Improving International Investment Agreements* (London: Routledge, 2013) at 236.
[89] Chapter 4, section 4.1.1.
[90] *Ibid*.
[91] *RomPetrol v Romania* at para.115.
[92] *Ibid*.

an investment dispute had conferred on it by agreement jurisdiction to hear their dispute" would be unduly "high reaching", and thus needed "to be backed by some positive authority in the Convention itself, in its negotiating history, or in the case-law under it".[93] The tribunal refused to dismiss the claim as an abuse of process early in the proceedings and, instead, concluded that it would review the matter at the merits stage if necessary.[94] *Rompetrol* demonstrates the cautious approach of tribunals to dismissal; ISA tribunals are likely to prefer to examine a claim in a full hearing rather than to uphold an abuse of process allegation by a state at the early stages of arbitration proceedings as will be discussed in Chapter Four.[95]

Before turning to the conceptualization of relevance of legal transplants to the procedural mechanisms for the early dismissal of frivolous and abuse of process claims, it is worth considering why such claims are in principle problematic. From the discussion above, it is apparent that states recognize that such claims are problematic in the investment regime.[96] By analogy with domestic legal systems, the rationale is that frivolous and abuse of process claims can put the administration of justice into disrepute, impose significant and unnecessary expenses on respondents, and waste both the time

[93] *Ibid*.
[94] *Ibid*.
[95] See subsections 4.6.1.2.1.1.and 4.6.2.3.
[96] UNCTAD (2005), at para. 7. (the Report states that "there have been fears about frivolous or vexatious claims that could inhibit legitimate regulatory action by Government"). UNCITRAL, Investor-state Dispute Settlement and Impact on Investment Rulemaking (New York: United Nations Conference on Trade and Development United Nations Publications, 2007) at 82. UNCTAD, *Investor-State Dispute Settlement: Review of Developments in 2016* at 8. Andreas Ziegler & Jorun Baumgartner, "Good Faith as a General Principle of (International) Law" in Andrew Mitchell, M. Sornarajah & Tania Voon, eds, *Good Faith and International Economic Law* (Oxford: Oxford University Press, 2015) at 13. Newcombe (2011), at 192. Andreas Kulick, "Reassertion of Control: An Introduction" in Andreas Kulick, ed, *Reassertion of Control over the Investment Treaty Regime* (Cambridge: Cambridge University Press, 2016) at 24. Eric De Brabandere, "The ICSID Rule on Early Dismissal of Unmeritorious Investment Treaty Claims: Preserving the Integrity of ICSID Arbitration" (2012) 9:1 Manchester J Intl Econ L 23.

and resources of the adjudicatory system.[97] That said, little justification has been offered that is specific to the context of the international investment regime as to why such claims may constitute a problem for individual states specifically and for the regime as a whole. In my view, frivolous and abuse of process claims impose unnecessary costs on the defending governments. Another reason why such claims are problematic is that they threaten credibility of the investment regime. In other words, why would governments commit to ISA if the regime has the reputation of permitting claims to go forward that manipulate the system or which *prima facie* lack legal merit?

The credibility concern is particularly acute given the range of possible strategic behaviours by investors. Foreign investors can use ISA claims to hold states to ransom or influence government decision-making. For example, recall that US diplomatic cables published by WikiLeaks[98] revealed that in the early ICSID arbitration *Alcoa v Jamaica*, the US company brought a claim against Jamaica for the purpose of gaining the upper hand in the process of negotiations that began in the aftermath of the newly adopted taxation measures by the Government of Jamaica. After bringing the claim, the company intentionally delayed the process of arbitration, so the arbitrators would not render an award before the negotiations were completed. The company thus used its investment claim to strengthen its position in negotiations with the Jamaican government. While this

[97] Deborah Rhode, "Frivolous Litigation and Civil Justice Reform: Miscasting the Problem, Recasting the Solution" (20004) 54: 2 Duke L J 447.

[98] WikiLeaks cable 1976STATE012599_b at para.2 (Microfilm, Alcoa Negotiations: Bureau of Inter-American Affairs). WikiLeaks materials have been cited as a legitimate source in both peer-reviewed publications and judicial proceedings. Taylor St John, *The Rise of Investor-State Arbitration: Politics, Law, and Unintended Consequences* (Oxford: Oxford University Press, 2018) at 212. Roberts McCorquodale, Wikileaks Documents are Admissible in a Domestic Court (2018), EJIL: Talk (blog), online:<https://www.ejiltalk.org/wikileaks-documents-are-admissible-in-a-domestic-court/>. ("the Court also held that any inviolability was lost due to the Wikileaks document coming into the public domain. This was the case even if it had been unlawfully extracted from the mission archive [para 21]. As Lord Sumption explained, once the documents have been published to the world, any confidentiality of them has been lost and there is 'nothing left to be preserved of the interest protected by Article 24").

conduct can be viewed positively as the attempt of a foreign investor, by all means, to protect its interests against a foreign government; in the context of frivolous and abuse of process claims, such strategic behaviour becomes a tool to influence a government's decision-making processes. The governments cannot rely on the system under which foreign investors can hold them to ransom by filing claims that lack merit or manipulate the system of investment protection. Without states' continued consent, the investment regime cannot function in principle.

1.3 Legal Borrowing: Learning from the Literature on Legal Transplants

It is not surprising that mechanisms for the dismissal of frivolous and abuse of process claims are currently reflected in the investment regime. Legal systems borrow mechanisms, rules and legal doctrines from each other.[99] Alan Watson coined the term "legal transplant" to describe this process.[100] Cross-fertilization in the legal field occurs

[99] Gilles Cuniberti, "Enhancing Judicial Reputation through Legal Transplants: Estoppel Travels to France" (2012) 60:2 Am J Comp L 383. Alan Watson, "The Transformation of American Property Law: A Comparative Law Approach" (1990) 24 Georgia L Rev 163.

[100] Alan Watson, *Legal Transplants: An Approach to Comparative Law* (Athens: University of Georgia Press, 1974). (Some critics find the term rather "awkward" and "ill-adapted to capturing the gradual diffusion of the law or the continuous nature of the process that sometimes leads to legal change through the appropriation of foreign ideas. Reportedly, the such terms as "reception", "transfer" and "circulation of legal models" were also used. In some instances, the term "diffusion of legal norms" is used as a term equivalent to legal transplants. Among many, Legrand voiced the most significant criticisms in his seminal article on impossibility of legal transplants. My reading of the article suggests that Legrand was not against legal transplantation per se. Instead, he remarked on impossibility of legal transplantation without appreciation of societal context of law. My reading of Legrand suggests that Legrand argued that the complex diffusion of legal norms, ideas and institutions is impossible without appreciation of the context of legal system (its culture, ideology and etc). For Legrand, societies of recipient systems can change how legal norms and ideas are interpreted and applied. In addition, Lagrand's critique of Watson's concept is built entirely on the presumption that only the legal norms (in a sense of statutory norms) can be transplanted. Edward Wise submits that "the original French title for this topic is «la circulation des models juridiques" […] refers to the movement, the continual flow of legal paradigms and ideas across national frontiers"). Edward Wise, "The Transplant of Legal Patterns" (1990) 38 Am J Comp L 1 at 22. Sue Farran & Christa Rautenbach, "Introduction" in Sue Farran, James Gallen & Christa Rautenbach, *The Diffusion of Law: The Movement of Laws and Norms Around the World* (London: Routledge, 2016) at 2-4 (discussing various terms that are used in the scholarship to define the phenomenon of transfer of legal norms, institutions and norms from one legal system to another). Michele Graziadei, "Comparative Law as the Study of Transplants and Receptions" in Mathias Reimann & Reinhard Zimmermann, eds, *The Oxford Handbook of Comparative Law* (Oxford: Oxford University Press, 2006) at 443. Roger Cotterell, "Is there a Logic of Legal Transplants? In David Nelken & Johannes Feest, eds, *Adapting Legal Cultures* (Oxford:

so frequently that Roscoe Pound famously characterized legal history as "largely a history of borrowings of legal materials". [101] The literature on legal transplants identifies "vertical" and "horizontal" patterns in inter-systemic borrowing.[102] Vertical legal transplants are those where "state law has inspired international rules",[103] while horizontal borrowing occurs between domestic jurisdictions.[104] According to Siems, "beyond legal rules, the object of a transplant can be general ideas and other elements of a country's legal culture".[105]

Borrowing may occur for variety of reasons, which include (1) transplantation by force, for example in the course of colonization[106] (2) transplantation in an attempt to legitimize domestic norms and institutions,[107] (3) transplantation as an attempt to save costs on conducting legal reforms,[108] and (4) transplantation for strategic reasons, for example, to simplify access to loans or to become a member of international

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Hart Publishing, 2001) at 70. Pierre Legrand, "The Impossibility of 'Legal Transplants" (1997) 4 Maastricht J Europ & Comp L 111, 121.

[101] Roscoe Pound, *The Formative Era of American Law* (New York: Peter Smith, 1938) at 94.

[102] Anna Dolidze, "Bridging Comparative and International Law: Amicus Curiae Participation as a Vertical Legal Transplant" (2015) 26:4 Eur J Intl L 851. Jonathan Wiener, "Something Borrowed for Something Blue: Legal Transplants and the Evolution of Global Environmental Law" (2001) 27 Ecology Law Quarterly 1295. Mathias Siems, *Comparative Law* (Cambridge: Cambridge University Press, 2018).

[103] Siems (2018), at 232.

[104] *Ibid*.

[105] *Ibid*.

[106] Ugo Mattei, "A Theory of Imperial Law: A Study on U.S. Hegemony and the Latin Resistance" (2003) 10 Ind J Global Leg Stud 383, 385.

[107] Jonathan Miller, "A Typology of Legal Transplants: Using Sociology, Legal History and Argentine Examples to Explain the Transplant Process" (2003) 51:4 Am J Comp L 839 at 859, 863 ("[a] comparatively straightforward example of a legitimacy-generating transplant is Argentina's decision at its 1994 Constitutional Convention to incorporate ten international human rights treaties and declarations into its Constitution, giving the instruments constitutional status". It was argued that the adoption "of the treaties would link Argentina to the rights-respecting countries of the world, giving it the moral legitimacy").

[108] Nuno Garoupa & Anthony Ogus, "A Strategic Interpretation of Legal Transplants" (2006) 35:2 J Leg Stud 339 at 346-347. Jonathan Miller, "A Typology of Legal Transplants: Using Sociology, Legal History and Argentine Examples to Explain the Transplant Process" (2003) 51:4 Am J Comp L 839 at 842. Ugo Mattei, "Efficiency in Legal Transplants: An Essay in Comparative Law and Economics" (1994) 14 Intl Rev L & Econ 3, 8.

organizations, trade or customs unions.[109] But, what legal norms, institutions and principles are borrowed from domestic legal systems into international law? How do the multiple actors decide what particular norms, mechanisms or institutions should be transplanted from domestic to international law?

Short concludes that "legal rules travel the globe not only […] through governmental channels, but rather via a complex web of private actors".[110] Transnational advocacy networks actively contribute to the process of legal transplantation.[111] This observation finds support in legal scholarship across numerous fields. Dezalay and Garth show that legal professionals can play the role of brokers who use their political and personal capital to shape rules and decision-making procedures.[112] Roberts also observes that legal professionals shape "the international law field" and facilitate the diffusion of ideas in international law.[113] Steer explains that legal norms, processes and institutions can "travel" from one legal system to another together with lawyers.[114] According to Steer, legal professionals often "choose the most familiar solution" when borrowing from domestic legal systems into international law.[115]

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[109] Daniel Berkowitz, Katharina Pistor & Jean- Francois Richard, "The Transplant Effect" (2003) 51 Am J Comp L 163.
[110] Jodi Short, "Transplanting Law in a Globalized World: Private Transnational Regulation and the Legal Transplant Paradigm" in Francesca Bignami & David Zaring, *Comparative Law and Regulation: Understanding the Global Regulatory Process* (Northampton: Edward Elgar Publishing, 2016) at 430.
[111] *Ibid*.
[112] Yves Dezalay & Bryant Garth, "Introduction: Constructing Transnational Justice" in Yves Dezalay & Bryant Garth, *Lawyers and the Construction of Transnational Justice* (London: Routledge, 2013) at 3-4. Yves Dezalay & Bryant Garth, *The Internationalization of Palace Wars: Lawyers, Economists, and the Contest to Transform Latin American States* (Chicago: University of Chicago Press, 2010) at 56-57, 198.
[113] Anthea Roberts, *Is International Law International?* (Oxford: Oxford University Press, 2017) at 69-70. John Flood, "Lawyers as Sanctifiers: The Role of Elite Law Firms in International Business Transactions" (2007) 14 Indiana Journal of Global Legal Studies 35.
[114] Cassandra Steer, "Legal Transplants or Legal Patchworking? The Creation of International Law as a Pluralistic Body of Law" in Elies van Sliedregt & Sergey Vasiliev, eds, *Pluralism in International Criminal Law* (Oxford: Oxford University Press, 2014).
[115] *Ibid*.

This explanation is illustrated by the example of Judge Gabrielle Kirk McDonald, the first female African-American judge to serve on the International Criminal Tribunal for the former Yugoslavia (ICTY). Judge McDonald had also served as an arbitrator on the Iran-United States Claims Tribunal. Judge McDonald undertook the drafting of the Rules of Procedure and Evidence for the ICTY. She recounts, "we used the American draft really as the 'working copy', and we all kind of all responded to it. And for me, I used the Federal Rules of Criminal Procedure".[116] Of course, this does not mean that the ICTY Rules of Procedure copied the US Federal Rules of Criminal Procedure entirely, but rather illustrates the point that legal professionals can facilitate the transfer of the legal solutions (both procedural and substantive that are most familiar to them from domestic to international law.[117] Legal professionals who have drafted IIAs and arbitration rules as well as adjudicated investment disputes have also adopted the "most familiar solution" in the context of the investment regime when contemplating how to dismiss frivolous and abuse of process claims. They, accordingly, have decided to empower the arbitrators to identify and dismiss frivolous and abuse of process claims akin to some domestic legal systems. This observation seems to be particularly reflective of the US approach to the dismissal of frivolous claims after *Methanex*.[118] As mentioned above in section 1.1, in the aftermath of the *Methanex* case, the USA introduced into its Model BIT a mechanism for the early dismissal of claims in which an award in favour of claimant could not be made. According to Vandevelde, the mechanism "is modelled in concept after Rule 12(b)(6) of the Federal Rules of Civil Procedure, which authorizes

[116] Interview Transcript with Gabrielle Kirk McDonald, at 4.
[117] Such transplantation is not always conscious; it may be that legal professionals or other actors employ the procedural solution that they know the best. Gregory Shaffer, "Transnational Legal Process and State Change" 37 Law & Soc Inquiry 229.
[118] Section 4.2.1.2.2.

dismissal of a claim upon which relief cannot be granted".[119] But application of the rule in the investment arbitration context has turned out to be overly narrow. After analysing *Renco v Peru* where the tribunal examined a preliminary objection seeking early dismissal of a frivolous claim, Johnson concluded that the "early-dismissal provision may be of much less use to respondent states than Rule 12(b)(6) (or any other 12(b) motion) is to defendants in US federal court proceedings".[120] This issue will also be examined in detail in Chapter Four.

Borrowing in itself is not problematic. In the context of foreign investment protection, it is even necessary because without such borrowing it may be difficult for states to "engage in international commerce or expect international investment without moving their legal regimes toward common standards".[121] For this reason, IIAs are often envisaged as instruments that promote the rule of law by establishing a predictable legal framework for foreign investors and providing them with recourse to an effective enforcement mechanism.[122] One example of such borrowing is *amicus curiae* submission. ISA tribunals permitted *amicus curiae* submissions to enhance the transparency of investment arbitrations that contribute to the overall sociological legitimacy of ISA.[123] The use of *amicus curiae* by courts, of course, originated in domestic legal systems.[124]

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[119] Kenneth Vandevelde, *U.S. International Investment Agreements* (Oxford: Oxford University Press, 2009) at 608.
[120] Lise Johnson, New Weaknesses: Despite a Major Win, Arbitration Decisions in 2014 Increase the US's Future Exposure to Litigation and Liability (Columbia Centre on Sustainable Development, 2015) at 11-12.
[121] Jonathan Miller, "A Typology of Legal Transplants: Using Sociology, Legal History and Argentine Examples to Explain the Transplant Process Source" (2003) 51:4 Am J Comp L 839 at 840.
[122] Jeswald Salacuse, *The Law of Investment Treaties* (Oxford: Oxford University Press, 2015) at 129. Thomas Ginsburg, "International Substitutes for Domestic Institutions: Bilateral Investment Treaties and Governance Authors" (2005) 25:1 Intl Rev L & Econ 107.
[123] Antony VanDuzer, "Enhancing the Procedural Legitimacy of Investor State Arbitration Through Transparency and Amicus Curiae Participation" (2007) 52 McGill LJ 683.
[124] Nigel Blackaby & Caroline Richard, "Amicus Curiae: A Panacea for Legitimacy in Investment Arbitration" in Michael Waibel, ed, *The Backlash Against Investment Arbitration: Perceptions and Reality* (The Hague: Kluwer Law International, 2010) at 257-260.

However, for such borrowing to be successful, the recipient legal system must show an ability to "internalize the rules, principles, and values of the donor system".[125] Inter-systemic borrowing is thus not a process of changing the wheels in a mechanical vehicle, where one element can be easily added or substituted but rather a process that is akin to the transplantation of an organ from one living organism into the other.[126] For transplantation to be successful, it is not only the qualities of the borrowed mechanism that matter but also the characteristics of the recipient legal system.[127]

The literature on legal transplants generally supports the presumption that incentives and structures within the recipient system matter for the successful reception of legal transplants.[128] For example, Langer shows that "legal ideas and institutions" cannot be "cut and pasted" from one jurisdiction to another.[129] He calls for a re-evaluation of how "we think about the circulation of legal ideas between legal systems".[130] Langer thus suggests avoiding the term "legal transplantation" because it

[125] Osvaldo Saldias, *The Judicial Politics of Economic Integration: The Andean Court as an Engine of Development* (London: Routledge, 2013) at 60.
[126] The term legal transplantation means "the movement of laws and legal institutions between states". Miller (2003), at 839. The analogy of legal transplant to the transplantation of kidney was first coined by Otto Kahn-Freund and later widely accepted in the literature. Otto Kahn-Freund, "On Uses and Misuses of Comparative Law" (1974) 37 Mod L Rev 1. John Cairns, "Watson, Walton, and the History of Legal Transplants" (2013) 41 Ga J Intl & Comp L 637 at 643. Edward Wise, "The Transplant of Legal Patterns" (1990) 38 Am J Comp L 1 at 16. ("la circulation des modeles juridiques". It refers to the movement, the continual flow, of legal paradigms and ideas across national frontiers). John Beckstrom, "Transplantation of Legal Systems" (1973) 21 Am J Comp L 557 at 558, 582.
[127] Maximo Langer, "From Legal Transplants to Legal Translations: The Globalization of Plea Bargaining and the Americanization Thesis in Criminal Procedure" (2004) 45 Harv Intl LJ 1 at 3-4 (discusses importance of structural differences in the legal systems for the transplant to be successful; the factors within the system can hinder reception of the transplant in the recipient legal system).
[128] Karen Alter & Laurence Helfer, *Transplanting International Courts: The Law and Politics of the Andean Tribunal of Justice* (Oxford: Oxford University Press, 2017) at 29-30. Alan Watson, "Legal Transplants and Law Reform" (1976) 97 Law Q Rev 79. Michele Graziadei, "Legal Transplants and the Frontiers of Legal Knowledge" (2009) 10:2 Theor Inq L 723 at 726-727.
[129] Langer (2004), at 5.
[130] *Ibid*.

"fails to account for the transformation that legal ideas and institutions may undergo when they are transferred between legal systems".[131]

According to Langer, "legal translation" is the more appropriate term. From a conceptual standpoint, this project concurs with Langer's observation that legal institutions and ideas must be borrowed from one system to another with full appreciation of systemic differences;[132] the borrowed concept is necessarily changed by the process of implanting it into the new system. I nevertheless use the term "transplantation" in order to connect this project to the rich body of comparative law scholarship on legal borrowing. Kahn-Freund's comparison of legal transplantation to the transplantation of kidney (rather than a mechanical process) shows that comparativists adhere to the idea that a legal transplant must be accepted by a recipient system that can have systemic and cultural features distinct from the donor legal system. Weiler and Trachtman also observe that "the dangers of borrowing are famous: the law of any polity is a construct embedded in a specific social and political culture and its transmutation to other polities is not easily achieved".[133]

To avoid any misunderstanding, it is important to clarify that in principle, the idea of introducing mechanisms to screen out frivolous and abuse of process claims early in the process is warranted. In other words, this thesis does not argue that any effort to

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[131] *Ibid*.

[132] This point seems to be reflected by Judge Fitzmaurice in Barcelona Traction. *Case concerning the Barcelona Traction Light and Power Company Limited* (Belgium v Spain), Judgment, 5 February 1970, ICJ Reports (1970) 3 (Fitzmaurice, J, concurring) 64, at 66–7. ("conditions in the international field are sometimes very different from what they are in the domestic, and […] rules which this latter's conditions fully justify may be less capable of vindication if strictly applied when transposed onto the international level. Neglect of this precaution may result in an opposite distortion—namely that qualifications or mitigations of the rule, provided for on the internal plane, may fail to be adequately reflected on the international—leading to a resulting situation of paradox, anomaly and injustice").

[133] Joseph Weiler & Joel Trachtman, "European Constitutionalism and its Discontents" (1997) 17:2 Northwestern J Intl L & Bus 354 at 355.

introduce such (or similar) mechanisms is futile. Instead, it simply suggests that any procedural mechanism must be viewed in the context of the incentives and structures of a specific system to understand how they can impact the functioning of the procedural mechanism.

The project is thus conceived as a case study of bottom-up vertical transplantation.[134] The metaphor "legal transplant" here "signals the need to consider the relationship between the part and the whole".[135] The coverage of bottom up transplantation in international law is limited, perhaps because the sociological legitimacy of the international public order generally rests on the claim of the universality of the legal norms, principles, and institutions.[136] As a result, professionals who practice in international law may be reluctant to acknowledge that international law is prone to influence by some legal systems more than others. In contrast, academics recognize that the diffusion of ideas, norms and legal principles occurs in accord with the paradigm of Westernization of international law.[137] For example, Anthea Roberts submits

[134] Wiener (2001), at 1301. Hersh Lauterpacht, "The So-Called Anglo-American and Continental Schools of Thought in International Law" (1931) 12 Brit YB Intl L 31 at 61,62. ("[u]nsurprisingly, international investment law has benefited from the insights of comparative law scholarship on legal transplants only in a very limited way. In part, academics, negotiators and other professionals in the field can explicitly deny a mere possibility of the vertical legal transplant because of "fear of undermining the perceived neutrality and legitimacy of their product". Hersh Lauterpacht, for example, denies that international law is anyhow influenced by two rival schools of intellectual thought, which are common law and continental law. Lauterpacht also submits that such rival influences will in principle be problematic in the context of international law from a "humanitarian perspective". The reason is that it will jeopardize "ultimate uniformity of the sense of right and justice which is the foundation of the legal ordering of the relations between states").

[135] David Nelken, "Towards a Sociology of Legal Adaptation" in David Nelken & Johannes Feest, eds, *Adapting Legal Cultures* (Oxford: Hart Publishing, 2001) at 19.

[136] Lauterpacht (1931), at 62 ("but present day international law at least constitutes a successful attempt at a common law of mankind, of relatively intensive and pervading universality and uniformity, in the limited field of relations between sovereign states").

[137] Roberts (2017), at 66-69. (Roberts provides a critical perspective and observes that Western ideas disproportionally influenced international law; and how graduates of "elite" schools in UK, US and France influence the construction of international law. Roberts suggests that similar pattern can be observed with regards to international judges and arbitrators who have to be "Westernized" in order to gain access to the international judicial bench and arbitral seat). Martti Koskenniemi, *The Gentle Civilizer of Nations: The*

international lawyers of certain nationalities and backgrounds can dominate the field of international law, and through this dominance shape how international law is interpreted and applied.[138]

Recently commentators in various subfields of international law have begun examining the bottom-up legal transplants, which occur wherever legal norms, processes, institutions, and rules are transplanted from domestic legal systems into international law. Steer's work on legal transplants in the context of international criminal law explains how prosecutors, academics, and practicing lawyers looked to domestic law when seeking normative solutions to issues that emerged in international criminal law, both with respect to criminal procedure and practice. Steer notes that domestic law often serves as "a direct source and an indirect influence on the development of ICL".[139] Jonathan Wiener examines vertical borrowing in the context of international environmental law.[140] Weiner demonstrates that international environmental treaties incorporate legal transplants from national environmental regimes.[141]

So far, international investment law scholarship has benefited from the insights of comparative law scholarship on legal transplants only in a very limited way. For example, Vadi's work addresses the question of the possible use of comparative law methods in international investment law.[142] She concludes that ISA tribunals should

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Rise and Fall of International Law 1870–1960 (Cambridge: Cambridge University Press, 2001) (discusses the Westernization of the concept of sovereignty in international law) at 174.

[138] Roberts (2017), at 118-119, 88-89 ("whereas international law was originally much more like civil law, it has shifted in last sixty years to become more like common law").

[139] Steer (2014).

[140] Wiener (2001), at 1295. Dan Tarlock, "The Influence of International Environmental Law on U.S. Pollution Control Law" (1997) 21 VT L Rev 759.

[141] *Ibid* at 1297.

[142] Valentina Vadi, "Critical Comparisons: The Role of Comparative Law in Investment Treaty Arbitration" (2010) 39:1 Denv J Intl L & Policy 67 at 99-100. Valentina Vadi, "The Migration of Constitutional Ideas: The Strange Case of Proportionality" in Andrea Bjorklund*, International Investment*

engage in analogies and judicial borrowing carefully in their legal reasoning, and only when the rules on treaty interpretation permit.[143] Overall, investment arbitration scholarship focuses predominantly on matters of substance, not procedure. For example, David Schneiderman argues that US domestic principles on expropriation inform the practice of ISA tribunals under NAFTA.[144] Eric Gillman submits that "trade and investment agreements between the US and Latin American countries intentionally represent the one way harmonization of commercial legal standards in the image of the US legal system".[145] This project aims to close the gap by addressing procedural mechanisms within the systemic context of the investment regime. The comparative law scholarship on legal transplants informs this project by introducing an appreciation of the systemic context and its relevance to the design of procedural mechanisms in international investment law.

1.4 Contribution of this Thesis to the Discourse on Frivolous and Abuse of Process Claims in Investment Arbitration Scholarship

The procedural mechanisms for the dismissal of frivolous and abuse of process claims have already been the subject of discussion in international investment law scholarship but only in a limited way. For example, Rosenfeld examined early dismissal of claims that manifestly lack legal merit and unfounded claims in the international

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Law and Arbitration in Yearbook on International Investment Law and Policy, 2013-2014 (Oxford: Oxford University Press, 2015) at 342 (advances similar ideas on a particular example of proportionality test).

[143] *Ibid*.

[144] *Council of Canadians v Canada* (AG), [2004] 1 ON (Affidavit, David Schneiderman)at 17-18. David Schneiderman, "Investment Rules and the New Constitutionalism" (2000) 25: 3 Law & Soc Inquiry 757 at 763. David Schneiderman, "NAFTA's Takings Rule: American Constitutionalism Comes to Canada" (1996) 46 U Toronto LJ 499.

[145] Eric Gillman, "Legal Transplants in Trade and Investment Agreements: Understanding the Exportation of US Law to Latin America" (2009) 41 Geo J Intl L 263 at 264-265.

investment regime.[146] While Rosenfeld's contribution is informative, his assessment of the mechanisms is rather confusing. Rosenfeld adopts the term "judicial" to describe the available mechanisms for the early dismissal of frivolous claims.[147]

Presumably, for Rosenfeld, the fact that the arbitrators (as adjudicators) exercise the power of early dismissal of frivolous claims is akin to the equivalent judicial function in the domestic legal systems. While an arbitrator is in the position of a judge with respect to the specific claim, the arbitrator is subject to different forces in comparison to judges in national courts. Thus, Rosenfeld fails to appreciate the implications of the different position of arbitrators and judges. Or perhaps he simply never considered any other possibility than that arbitrators should be empowered to identify and dismiss frivolous or abuse of process claims.

Potesta and Sobat examine the dismissal of frivolous claims by international tribunals and courts more generally.[148] They consider in detail the mechanism in the investment regime for the early dismissal of claims that are manifestly without legal merit in parallel with similar mechanisms that are applied by the European Court of Human Rights, the ICJ, and those under the *United Nations Convention on the Law of the Sea*.[149] Potesta's and Sobat's overview of these mechanisms is helpful for contextual purposes but the investment regime is so distinctive from those other regimes that lessons from other courts and tribunals have only limited relevance.

Potesta and Sobat focus on how investment tribunals have utilized the dismissal mechanisms, but do not situate their inquiry within the broader context of the regime's

[146] Friedrich Rosenfeld, "Early Dismissal of Claims in Investment Arbitration" in Andreas Kulick, ed, *Reassertion of Control over the Investment Treaty Regime* (Cambridge: Cambridge University Press, 2016) at 99-100.
[147] *Ibid*.
[148] Potestà & Sobat (2012), at 137.
[149] *Ibid*.

structures and incentives. Potesta and Sobat observe that the existing mechanisms "will allow states to commit time and resources only to the opposition of serious claims, while they will be dispensed with having to defend claims that do not deserve to be litigated".[150] However, they seem to forget that under the current rules the arbitrators (not states) are charged with distinguishing between "serious" and "not serious" claims, as well as having the power to determine what claims "deserve" to be litigated. As Chapter Four shows, arbitrators dismiss frivolous claims in overly narrow circumstances. This undermines the effectiveness of the rules, and Potesta's and Sobat's conclusion because *de facto* states may avoid costly defences in very rare instances.

So far, Gaillard's examination of abuse of process claims in the investment regime remains the most comprehensive.[151] (He does not address frivolous claims.) Gaillard sets the goal of identifying the circumstances in which ISA tribunals can dismiss claims as being abuses of process. Gaillard establishes three possible scenarios when the tribunals do so.[152] My thesis (in Chapter Four) adopts his categorization and adds a fourth scenario. Gaillard predicts that tribunals will expand their approach to the dismissal of claims as abuses of process. It is true that legal concepts can evolve, but I will argue that tribunals have applied abuse of process concept to justify dismissal only in an overly narrow set of circumstances and even permitted claimants to "cure" abuses of process. Such an approach can persist in arbitral practice due to the systemic features of the regime, for example, the case-specific mandate of arbitral tribunals and the arbitral duty to give parties a chance to air their arguments.

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[150] *Ibid*.
[151] Gaillard (2017), at 3-4.
[152] *Ibid*.

Eric De Brabandere has authored two articles related to the work in this thesis: one examines claims which are manifestly without legal merit and the other examines abuse of process claims in light of good faith principle.[153] It is worth considering De Brabandere's articles separately for two reasons. First, De Brabandere examines frivolous and abuse of process claims in isolation from each other. Second, De Brabandere does not seem to view such claims within a broader context of the backlash against the investment regime, and the regime's ongoing reform. In contrast, this thesis acknowledges the differences between the dismissal of frivolous and abuse of process claims yet makes an analytical choice to examine such claims together. The reason is that the thesis is primarily concerned with the existing mechanisms for dismissing such claims. In their turn, the mechanisms for dismissal are viewed in the broader context of the regime's legitimacy crises and ongoing reform.

On manifestly meritless claims, De Brabandere concludes that the existing rules do in fact deter investors from filing claims which are manifestly without legal merit and helps states to avoid costly litigation.[154] I agree with De Brabandere in principle. However, the mere existence of such mechanisms when investors (and their law firms) know that tribunals dismiss claims only in exceptional circumstances and generally set the threshold very high will only arguably serve as a deterrent. The presence of such a mechanism can be comforting to states but it has limited practical value. In this scenario, the mechanism for early dismissal only imposes additional costs on states. De Brabandere examines the mechanism without attempting to ask the question (that this thesis

[153] Eric De Brabandere, "Good Faith', 'Abuse of Process' and the Initiation of Investment Treaty Claims" (2012) 3:3 J Intl Disp Settlement 609. Eric De Brabandere, "The ICSID Rule on Early Dismissal of Unmeritorious Investment Treaty Claims: Preserving the Integrity of ICSID Arbitration" (2012) 9:1 Manchester Journal of International Economic Law 23.
[154] *Ibid*.

advances) whether it is appropriate for arbitrators to exercise the function of adjudicating claims for early dismissal.

In his article on abuse of process, De Brabandere argues that tribunals have the authority to "preserve the current system of investment arbitration from abuses" and even the "role to maintain the viability of the current system of investment arbitration" without asking whether it is appropriate for the arbitrators to serve as the "gatekeepers", one of the issues that this thesis addresses.

Finally, Céline Lévesque has produced a short note that proposes to utilize the hybrid mechanisms of mediation and arbitration to handle frivolous claims.[155] According to Lévesque, a preliminary mediation procedure may be useful to catch frivolous claims early in the dispute resolution process, especially "when a government first hears about a complaint only when investors deliver a notice of intent to submit a claim to arbitration under an IIA".[156] Lévesque observes that such a mechanism would promote efficient dispute resolution and save state resources. This thesis develops Lévesque's concept further by proposing a procedure of evaluating and screening out investors' claims that is based on the model of evaluative conciliation. It also compares such preliminary mechanisms with other potential alternatives for combating frivolous and abuse of process claims, such as cost-shifting and addition of an appeals process.

1.5 Theoretical Framework

This thesis will view the investment regime as a political system. The lens of the political system serves as a framing device to structure one's thinking on the investment regime and its participants, in particular the fluid relations between key participants in the

[155] Lévesque (2011), at 77-78.
[156] *Ibid*.

investment regime that lead to its constant evolution. To avoid confusion, it may be helpful from the outset to explain the relationship between the legal transplant framework and the political system theory. As has been mentioned, the legal transplant framework is an intellectually inspiring prompt to think about rules, principles, norms, and institutions in the systemic context of a given legal order. The political lens theory permits us to view the investment regime as a dynamic interaction between the regime's participants that through actions and reactions shape the legal rules within the system. In my view, the two frameworks are mutually supportive and reinforcing. Both frameworks are concerned with the appreciation of the systemic context but in a different way. The political system theory maps the interactions between the participants of the regime to show how legal rules emerge within the system through the actions and reactions of the regime's participants. The legal transplant framework works as a magnifying glass to examine how the rules operate when viewed within the regime's incentives and structures.

The political system lens was developed by Dupont and Shultz, who propose viewing the investment regime as a political system that "transforms the input of key actors (namely states, investors, arbitrators and arbitration institutions) into output (namely arbitral awards taken in the aggregate), with feedback loops from output to input, leading to or calling for adjustments or other reactions from these actors".[157] Through the lens of the political system, we see participants take actions or create demands for action ("inputs") that result in binding decisions (outputs). These outputs do not exist in a vacuum, but within an interactive environment where participants also introduce changes to the system, which are labelled "outcomes".[158] In this model,

[157] Dupont & Schultz (2016), at 56.
[158] *Ibid* at 3.

outcomes then generate demands for new inputs. Hence, the political system is a "mechanism that transforms certain types of input into certain types of output, thereby furthering certain goals by "authoritatively allocating values".[159]

This thesis is not particularly concerned with drawing a distinction between political processes and legal processes because any attempt to make such a distinction is "misguided".[160] Levin explains that "[n]o final distinction between law and politics is worth making, not because judicial decisions are mere dressing for naked political power, but because the requirements of constructing legal order involve an irreducible political element".[161] The investment regime is no exception, in part because it is a legal order that emerged for political reasons.[162]

Nevertheless, this thesis acknowledges a "sharp distinction between […] the political and the legal approaches to research".[163] According to Easton, "political research […] describes the way in which political organizations have arisen and the social forces behind them".[164] As per Easton's understanding, legal research "explains the legal provisions for the organization of the state and government".[165]

Thus, the political system lens focuses on dynamic interactions among the key participants of the regime (foreign investors, states, investment tribunals and arbitration centres). In particular, the political system lens helps to establish how, through action and

[159] *Ibid* at 5 and 19.
[160] Joel Levin, *How Judges Reason: The Logic of Adjudication* (New York: Peter Lang Publishing, 1992) at 27.
[161] *Ibid*. Similar logic in the context of international law you can see in Lauterpacht's differentiation between political and legal disputes. A division between political and legal disputes is artificial because "it is not the nature of an individual dispute which makes it unfit for judicial settlement, but the unwillingness of a state to have it settled by the application of law" in Hersch Lauterpacht, *The Function of Law in the International Community* (Oxford: Oxford University Press, 2011) at 369.
[162] St John (2018), at 120-124.
[163] David Easton, *The Political System*: *An Inquiry Into The State Political Science* (Chicago: Alfred Knopf, 1953) at 156.
[164] *Ibid* .
[165] *Ibid*.

reaction, these key participants contribute to rule development and the setting of legal norms. Thus, the key added value of the political system lens is that it helps demonstrate the evolution of legal rules via a series of political and economic reactions to legal outcomes.

To illustrate the interactions of the key participants, the claim of Phillip Morris against Australia is a helpful example. Philip Morris brought an ISA claim against Australia, arguing that Australia violated its international obligations under the *Hong-Kong-Australia BIT* when it adopted tobacco plain-packaging legislation.[166] The claim was problematic for at least two reasons. First, the claim challenged a public welfare regulatory measure in ISA. Second, Phillip Morris conducted a corporate re-structuring prior to launching the claim.[167] The ISA tribunal later determined that the corporate restructuring was an abuse of process, on the ground that Phillip Morris had attempted to take advantage of the *Hong Kong-Australia BIT* and, without such restructuring, it would have been inaccessible to the company.

Soon after the claim was filed (and well before the tribunal rendered its decision), Julia Gilliard, the Prime Minister of Australia, made a public declaration that her government would reconsider its approach to ISA. Instead of ISA, the government promised to favour state-to-state dispute settlement for resolving international disputes.[168]

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[166] *Philip Morris Asia Limited v The Commonwealth of Australia* (2012), Award on Jurisdiction and Admissibility PCA Case No. 2012-12 (United Nations Commission on International Trade Law) (Arbitrators: Karl-Heinz Böckstiegel, Gabrielle Kaufmann-Kohler, Donald M. McRae).

[167] Canada-EU FTA includes a clause that prevents submissions similar to Phillip Morris claim. The European Commission specifically indicated that claims similar to Phillip Morris are to be precluded.

[168] This position appears particularly before 2013. After 2013, there was change of governments in Australia after which a new government pursued a case by case approach to inclusion of ISA into IIAs. Austl, Commonwealth, Department of Foreign Affairs and Trade, Gillard Government Trade Policy Statement: Trading Out Way to More Jobs and Prosperity (April 2011), online:< http://blogs.usyd.edu.au/japaneselaw/2011_Gillard%20Govt%20Trade%20Policy%20Statement.pdf>. Australia later changed its approach and did not denounce its treaties. Possibly, ongoing elections in the country affected its policy trajectory. It is known, however, that the Parliament will be scheduled for the

The Australian parliament launched a series of consultations on ISA and its suitability for evaluating the consistency of domestic public policy regulations with international investment obligations.[169]

During the negotiations of CPTPP, Australia insisted that tobacco be carved out from the subject matter of the treaty, yet another illustration of how a claim by a foreign investor could trigger a change in a state's approach to investment arbitration.[170] Australia thus narrowed the scope of the definition of investment to exclude tobacco from investment arbitration.[171] It is noteworthy that after the Phillip Morris claim, Australia's actions have resulted in a strategic disadvantage to other investors, who now have to deal with a narrower definition of investment and, thus, are restricted in bringing their claims against Australia.

Similarly, in 2015 Australia negotiated an investment treaty with China that sets up "joint treaty party control" to dismiss investors' claims that target public welfare regulation at early stages in an arbitration. The *China–Australia Free Trade Agreement* (ChaFTA) provides that, if an investor challenges a regulatory measure, a host state may issue a "public welfare notice".[172] In this notice, the host state indicates that a challenged regulatory measure meets a welfare objective and is not discriminatory and launches a 90 days' consultation period with the home state of the foreign investor.[173] If the host state and home state agree that the measure pursues welfare objectives and is not

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second vote on Anti-ISA Bill and the Labour as well as the Green Party support the anti-ISA agenda in the Australian future treaties. Nottage (2016), at 5. Leon Trakman, "Investor-State Arbitration: Evaluating Australia's Evolving Position" (2014) 15:1 JWIT 152.

[169] *Ibid*.

[170] Andrew Mitchell & Tania Voon, *The Global Tobacco Epidemic and the Law* (Northampton: Edward Elgar Publishing, 2014) at 3.

[171] Nottage (2016), at 29.

[172] *China-Australia Free Trade Agreement* (ChAFTA).

[173] *Ibid*.

discriminatory, both states issue a binding decision requiring the tribunal to dismiss the claim.

"Joint treaty party control" is a mechanism that helps states to screen out claims by foreign investors that target their public welfare regulations.[174] Notably, the mechanism appeared in ChaFTA after Australia faced the Phillip Morris claim on plain packaging. Presumably, joint treaty party control represents Australia's reaction to previous claims targeting its pro-welfare regulatory measures, especially the Phillip Morris arbitration.[175] For its part, China may have agreed to enact joint treaty party control due to its own desire to insulate its regulatory policy making from challenges by foreign investors. This approach is consistent with China's generally "restrictive" position on ISA.[176]

Of course, claims are legal matters procedurally and substantively, with a formal structure and a certain substantive content of law and facts. Yet the political system lens

[174] Anthea Roberts & Richard Braddock, Protecting Public Welfare Regulation Through Joint Treaty Party Control:a ChAFTA Innovation (Report 2015), online:< https://academiccommons.columbia.edu/catalog/ac:201614>

[175] Luke Nottage, Trade and Foreign Investment (Protecting the Public Interest) Bill 2014, Submission 21, online:<https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Foreign_Affairs_Defence_and_Trade/Trade_and_Foreign_Investment_Protecting_the_Public_Interest_Bill_2014/Public_Hearings> at 4 (discussing the opposition to ISA in Australia predominantly from political left and "economic right"). Nottage (2016), at 3. ("The future of treaty-based ISA for Australia remains uncertain. Various parliamentary inquiries have raised concerns since 2014, on the part of increasingly well-organized civil society groups, as well as the opposition Labour Party and especially the Greens. A Greens senator from Tasmania has sponsored a bill that would preclude Australia from entering into any future treaties containing ISDS, although Coalition and even Labour senators have recommended against enactment […] The Labour Party eventually voted with the government regarding the Korea FTA, but it initially balked with respect to the China-Australia FTA (ChAFTA) (which also includes ISDS) and can be expected to do so regarding the expanded TPP"). *The Parliament of the Commonwealth of Australia, Joint Standing Committee on Treaties*, Report 154-Treaty Tabled on 17 June 2015: Free Trade Agreement between the Government of Australia and the Government of the People's Republic of China (Canberra, 2015), at para. 5.13. at 225. Tania Voon & Elizabeth Sheargold, "Australia, China and the Coexistence of Successive International Investment Agreements" in Colin Picker, Heng Wang & Weihuan Zhou, *The China-Australia Free Trade Agreement: A 21st-Century Model* (London: Bloomsbury Publishing, 2017) at 225.

[176] Juan Ignacio Stampalija, "Chinese Bilateral Investment Treaties: A Case of Internal Fragmentation" in C. L. Lim & Bryan Mercurio,eds, *International Economic Law after the Global Crisis* (Cambridge: Cambridge University Press, 2015) at 331.

offers a different perspective that helps to explain the implications of foreign investors' claims for the investment regime. The political system lens allows us to view investors' claims as an input that has ramifications beyond a particular dispute; the claims and the tribunals' outcomes thus can result in continuing effects on the host state directly engaged in the dispute, other states, and foreign investors.

Investment tribunals render awards that are binding only upon the participants of the particular dispute. Through the lens of the political system, we can see that these awards constitute outputs that provide feedback to other key participants of the investment regime.[177] Dupont and Shultz explain,

> [t]his output has feedback effects on the key actors of the system, who react to it, either by adjusting their input so as to maximise the realisation of their own preferences and perceived interests, or by adjusting their actions without seeking to alter the system itself, for instance by simply complying with it or by exiting it. These reactions create the system's dynamics.[178]

According to political system lens, the awards of investment tribunals play a crucial role in the dynamics of the investment regime by signalling to key participants what actions potentially to undertake in response to the output.

In my view, the political system lens is particularly helpful to view the emerging mechanisms for the early dismissal of frivolous and abuse of process claims within the broader context of the regime's reform. Interestingly, the procedural mechanisms for the dismissal of frivolous and abuse of process claims seem to have emerged consciously as one element of a broader response to "social demands"[179] from stakeholders affected

[177] Dupont & Schultz (2016), at 5.
[178] *Ibid*.
[179] Eric Stein, "Uses, Misuses and Non-uses of Comparative Law" (1977) 72 Nw UL Rev 198 at 206-207

(directly or indirectly) by the investment regime.[180] In particular, some governments, non-governmental organizations and mass-media have fuelled concerns over the regime's legitimacy deficits.[181] Among other issues, critics are chiefly concerned about the pervasive nature of ISA rulings against states' regulatory space, bias of investment arbitrators against states, and structural privileging of foreign investors over states in investment disputes.[182] This phenomenon is also known in the scholarship as the "backlash" against the investment regime.[183]

[180] "Behind Closed Doors; Investment, Arbitration and Secrecy", *The Economist* (25 April 2009), online:< http://www.economist.com/node/13527961>. James Surowiecki, "Trade-Agreements Troubles", New Yorker (22 June 2015), online:<https://www.newyorker.com/magazine/2015/06/22/trade-agreement-troubles>. Bret Gustafson & Natalia Guzman Solano, "Mining Movements and Political Horizons in the Andes: Articulation, Democratization, and Worlds Otherwise" in Kalowatie Deonandan & Michael Dougherty, eds, *Mining in Latin America: Critical Approaches to the New Extraction* (London: Routledge, 2016) (discussing the role of social movements in the anti-ISA).

[181] Gus Van Harten et al, *Public Statement on the International Investment Regimes - 31 August 2010*, available online:<http://www.osgoode.yorku.ca/public-statement-international-investment-regime-31-august-2010/>. [Public Statement on ISDS]. José Alvarez, *The Public International Law Regime Governing International Investment* (The Hague: Martinus Nijhoff Publishers, 2011) at 352. Amokura Kawharu, Amokura Kawharu, "Participation of Non-Governmental Organizations" in Michael Waibel, ed, *The Backlash Against Investment Arbitration: Perceptions and Reality* (The Hague: Kluwer Law International, 2010) at 285. Pia Eberhardt & Cecilia Olivet, Profiting From Injustice (Brussels: Corporate Europe Observatory and the Transnational Institute, 2012) at 15, online: <https://www.tni.org/files/download/profitingfrominjustice.pdft [Profiting from Injustice]. Argentina Rejects Azurix Claims on ICSID Award in Letter to Geithner", Inside U.S. Trade, 16 September 2011, http://www.embassyofargentina.us/v2011/files/20110825-geithnerazurix9.pdf. Sergey Ripinsky, Venezuela's Withdrawal From ICSID: What it Does and Does Not Achieve, online:< https://www.iisd.org/itn/2012/04/13/venezuelas-withdrawal-from-icsid-what-it-does-and-does-not-achieve/>.

[182] Gus Van Harten & Dayna Nadine Scott, "Investment Treaties and the Internal Vetting of Regulatory Proposals: A Case Study from Canada" (2016) 7:1 J Intl Dispute Settlement 92. Gus Van Harten, "Reforming the System of International Investment Dispute Settlement" in C. L. Lim, *Alternative Visions of the International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2016) at 113. C.L. Lim supports this argument and suggests that arbitrators are financially interested in the claim to proceed.

[183] Peter Muchlinski, "Regulting Multinationals: Foreign Investment, Development, and the Balance of Corporate and Home Country Rights" in Jose Alvarez & Karl Sauvant, eds, *The Evolving International Investment Regime: Expectations, Realities, Options* (Oxford: Oxford University Press USA, 2011) at 31. Asha Kaushal, "Revisiting History: How the Past Matters for the Present Backlash Against the Foreign Investment Regime" (2009) 50 Harv Int LJ 491 at 508.

Many states have responded to the backlash by proposing more vigourous "control" mechanisms.[184] Lauterpacht envisioned the need for such mechanisms years ago and made the following observation "[i]t is only at a rudimentary stage of legal development that society permits the unchecked use of rights without regard to its social consequences".[185] Among many proposals for reform are the establishment of a multilateral investment court,[186] the use of joint commissions to dismiss claims that target states' welfare regulations,[187] mechanisms for the early dismissal of frivolous claims, and provisions to restrict corporate restructuring.[188] In adopting such "control" mechanisms, states attempt to hinder access to ISA by adding multiple steps foreign investors must complete before they can initiate arbitration. There are purely pragmatic reasons for such an approach, which is obviously intended to reduce the claims states must face in ISA, along with the attendant costs.[189] The costs imposed by frivolous and abuse of process

[184] The Side-Letter between the Government of Vietnam and the Government of New Zealand to Comprehensive and Progressive Agreement for Trans-Pacific Partnership, online: <https://www.mfat.govt.nz/assets/CPTPP/New-Zealand-Viet-Nam-ISDS.pdf>. (excludes application of ISA). Michael Reisman is perhaps one of the first scholars who in detail discussed the mechanisms of control in the context of investor-state arbitration. For Reisman, "arbitration is delegated and restricted power" to render decisions. The mechanisms of control are essential to keep this power restricted within the boundaries and a "prerequisite condition" for "operation" of the whole system. Judicial review is one of such control systems in the domestic context. Michael Reisman, *Systems of Control in International Adjudication and Arbitration: Breakdown and Repair* (Durham: Duke University Press, 1992) at 3-4.

[185] Hersch Lauterpacht, *The Development of International Law by the International Court* (Cambridge: Cambridge University Press, 1982) at 162.

[186] Jonathan Bonnitcha, Lauge Skovgaard Poulsen & Michael Waibel, *The Political Economy of the Investment Treaty Regime* (Oxford: Oxford University Press, 2018) at 226-231. Stefan Griller, Erich Vranes & Walter Obwexer, *Mega-Regional Trade Agreements: CETA, TTIP, and TiSA: New Orientations for EU External Economic Relations* (Oxford: Oxford University Press, 2017) at 146.

[187] Anthea Roberts & Richard Braddock, Protecting Public Welfare Regulation Through Joint Treaty Party Control: a ChAFTA Innovation, online: <http://ccsi.columbia.edu/files/2013/10/No-176-Roberts-and-Braddock-FINAL.pdf>.

[188] M. Sornarajah, *The International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2010) at 329. Reportedly, the Dutch Foreign Ministry announced plans to limit foreign investors' use of the Dutch BITs. This is likely to have a profound impact because foreign investors frequently use Dutch BITs to bring claims against other states a practice that is known as the Dutch sandwich. Dutch set out plan to counter tax-haven reputation, Financial Times, online:< https://www.ft.com/content/ef9b87ac-1af5-11e8-aaca-4574d7dabfb6>.

[189] UNCTAD (2005), at para. 14. Profiting from Injustice at 22. Jarrod Hepburn & Mark Huber, An Assessment of Australia's Parliamentary Report on ISA in the TPP, 5 January 2017,

claims are not restricted to merely monetary expenses incurred by respondent states to defend the investor's claims in arbitration".[190]

As a result, investment arbitration claims may be burdensome for some developing states, yet these states may need foreign investment the most. In this context, perhaps the most alarming scenario is that developing states may be deterred from pursuing public welfare regulatory objectives for fear of a potential claim in ISA, or those states may refuse to pursue much-needed regulatory objectives to avoid discouraging foreign investors from investing in their economies.[191]

Another striking possibility is that national stakeholders, both in developed and developing states, will press through the available democratic fora for the elimination of ISA and a rejection of the investment regime overall.[192] Abandonment of the investment regime appears to be rather distressing because of the value of the investment regime for the international community, particularly for upholding the cornerstone UN principles of peaceful cooperation and dispute resolution.

As Chapter Three shows, many states have undertaken steps to change their IIAs and improve ISA as a dispute settlement mechanism more generally. Arbitration

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online:http://kluwerarbitrationblog.com/2017/01/05/reserved-an-assessment-of-australias-parliamentary-report-on-isds-in-the-tpp/ (According to a recently published Australian Parliamentary Report on ISA, the legal costs of the Australian defence in the Phillip Morris dispute reached 37 million US dollars).

[190] Profiting from Injustice at 7.

[191] Chapter 3, section 3.1.1.2 (on regulatory chill).

[192] These processes maybe of direct or indirect nature by virtue of participating in the national democratic systems. Now when investment and trade treaties are widely discussed in the media, public awareness on the investment regime considerably increased. As a result, the stakeholders including citizens may vote for the candidates that do not support international trade or investment treaties or directly scrutinizes such treaties. For example, the democratic processes in Wallonia resulted in a close scrutiny of investment arbitration in CETA. By 2017, we know that CETA passed Wallonian scrutiny yet the incident still has a great precedential value, showing that citizens could at minimum impede a governmental decision to sign an investment treaty. Gus Van Harten et al, *An Open Letter to the Parliament of Wallonia and Belgian Voters on the Proposed CETA and Its Foreign Investor Protection System*, online:< http://www.s2bnetwork.org/wp-content/uploads/2016/10/Canadian-academics-open-letter-on-the-CETA-and-Wallonia.pdf>

institutions, as independent participants in the investment regime, have also sought to introduce changes to increase the effectiveness of the dispute resolution process in ISA.[193] The dismissal of frivolous and abuse of process claims thus should not be considered in isolation but within a broader context of these ongoing dynamics of interaction between the participants within the investment regime (a goal that Chapter Two pursues).

The political system approach is also helpful in capturing the impact of factors from outside the ISA context, in particular the functional inequality of states. This functional inequality has particular implications where investment arbitration is concerned. Arbitration requires specialised legal expertise to adequately evaluate a claim.[194] Most states (including some developed states) lack such expertise in-house, but many states may also lack the resources to hire expert outside counsel. [195] For instance, Uruguay could withstand a challenge from Phillip Morris only due to funding from billionaire Michael Bloomberg.[196] Kyla Tienharra reports that without Bloomberg's support,

[193] Barbara Alicja Warwas, *The Liability of Arbitral Institutions: Legitimacy Challenges and Functional Responses* (The Hague: Springer, 2016) at 53-55.

[194] Importance of legal expertise is crucial, as the contrasting cases of *Philip Morris v Australia* and *Shell v Nicaragua* demonstrate. In *Philip Morris*, Australia approached the arbitration strategically and filed for bifurcation of the proceedings, a strategy that proved successful in helping Australia win the case on jurisdictional grounds while minimizing costs. In *Shell*, Nicaraguan officials admitted that they lacked expertise on matters relating to ISA. *Shell Brands International AG and Shell Nicaragua S.A. v. Republic of Nicaragua* (ICSID Case No. ARB/06/14). The case was settled. Online: <http://investmentpolicyhub.unctad.org/ISDS/Details/231>. Damon Vis-Dunbar, Shell launches claim against Nicaragua over seizure of intellectual property. Request for Arbitration, Shell Brands International AG & Shell Nicaragua S.A. v. The Republic of Nicaragua, May 17, 2006. Obiora Chinedu Okafor, "Critical Third World Approaches to International Law (TWAIL): Theory, Methodology, or Both?" (2008) 10:4 Intl Community L Rev 371 at 378. Michael Fakhri, "Law as the Interplay of Ideas, Institutions, and Interests: Using Polyani (and Foucault) to ask TWAIL Questions" (2008) 10:4 Intl Community L Rev 455.

[195] UNCTAD, International Investment Rulemaking: Note by the UNCTAD Secretariat. General. TD/B/COM.2/EM.21/2 (New York: UNCTAD 2007) at para. 17-19. Similar work has been done in the context of World Trade Organization (WTO). Joan Apecu Laker, *African Participation at the World Trade Organization: Legal and Institutional Aspects 1995-2010* (The Hague: Martinus Nijhoff Publishers, 2013) at 20.

[196] Krista Nadakavukaren Schefer, *Poverty and the International Economic Legal System: Duties to the World's Poor* (Cambridge: Cambridge University Press, 2013) at 217.

Uruguay could not have paid its legal fees.[197] The proposed mechanism for preliminary assessment of claims through an evaluative conciliation procedure can provide the governments with an opportunity to obtain independent legal assessment of the merits of the claim and participate in a less costly procedure that may facilitate settlement between an investor and a state.

Finally, the lens of political system helps to make these contextual details relevant to the debate on the legitimacy of investment arbitration. If the investment regime is viewed only (and exclusively) as the legal system, the discussed facts on Alcoa and its conduct are irrelevant from a legal perspective. The lens of political system provides an opportunity to appreciate these facts as environment in which foreing investors make their inputs.

1.6 Structure

This thesis is composed of Seven Chapters, including introduction and conclusion. Chapter One presents an overview of this thesis, discusses its theoretical framework and situates the project in the field of international investment law.

Chapter Two sets out the legal structure of the investment regime, describes its value for the international community, and explains why frivolous abusive claims are problematic. The objective of this chapter is to show that the investment regime is a complex legal system that embeds unique features that make it distinctive from any domestic legal system. To demonstrate this, the chapter focuses on discussing the legal structure of the investment regime and "logistics" of investment dispute settlement process.

[197] Kyla Tienhaara "The Dismissal of a Case Against Plain Cigarette Packaging is Good News for Taxpayers" *Sydney Morning Herald* (20 December 2015).

Chapter Three discusses the criticisms of the investment regime's legitimacy. This Chapter has two goals: to provide an extensive overview of the critical scholarship and to demonstrate that the regime's participants can change its legal structures to better fit their needs. The regime's development is thus a step-by-step "learning" process where the regime's participants introduce certain changes after gaining experience as respondents in disputes. This Chapter reinforces observations made by the proponents of the use of the political system as a theoretical framework. The mechanisms for the early dismissal of frivolous and abusive claims are thus elements of the broader dynamics of change within the international investment regime, which have arisen to cure perceived legitimacy deficits.

Chapter Four focuses on the existing mechanisms for the early dismissal of frivolous and abusive claims in the investment regime. This Chapter shows that the design of those mechanisms replicates the approaches in many domestic legal systems. The goal of this Chapter is to examine how ISA tribunals currently approach the dismissal of frivolous and abusive claims. This chapter thus presents the mechanics of dismissal i.e. the mechanisms as they function and it discusses the main features and characteristics of those mechanisms.

Chapter Five situates the mechanisms for the dismissal of frivolous and abusive claims within the broader context of the international investment regime, its incentives and structures. The objective is to show that those mechanisms must be viewed within the investment regime's systemic characteristics to determine their efficacy. Chapter Five examines the structures and incentives that characterize the investment regime to explain

why the current design of the mechanisms for the dismissal of frivolous and abusive claims is inappropriate.

Chapter Six discusses alternative approaches to the mechanisms for the early dismissal of frivolous and abuse of process claims. In particular, it proposes a mechanism of mandatory conciliation that can help to screen out claims before they enter the investment regime. Chapter Seven provides concluding remarks to map the way forward.

Chapter 2

The International Investment Regime: Overview and Background

Reflecting on the different methods of dispute resolution acceptable among states, Joseph Beale concluded that there are only two viable methods: "force and law".[198] According to Beale, "[e]ither the will of the physically strongest, or of the mentally alertest, must prevail — the way of the beast; or conflicting wills must be restrained by law-the way of organized human society".[199] The regime for the protection of foreign investment has a complex heritage. It emerged in the aftermath of the Second World War, as a response to large-scale nationalizations that signified the pursuit of independence (and in many cases socialist policies) by former colonial states, and as an alternative to gunboat diplomacy.[200] The investment regime may be viewed one aspect of the international community's aspiration to move from "the way of the beast" to "the way of law".[201]

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[198] Joseph Beale, *A Treatise on the Conflict* (1935) as cited in Jonathan Zasloff, "Abolishing Coercion: The Jurisprudence of American Foreign Policy in the 1920s" (1993) 102 Yale L J 1689 at 1698.

[199] *Ibid*.

[200] Gunboat diplomacy is a past policy of militarily superior states, which used their naval forces against weaker states to compel them by force of arms to commit to certain actions. James Cable, *Intervention at Abadan: Plan Buccaneer* (Berlin: Springer, 1991) at 1-2. Lucas Bento, "From Anarchy to Rational Design: Direction and Perception in International Investment Law" in Andrea Bjorklund, *Yearbook on International Investment Law & Policy 2014-2015* (Oxford: Oxford University Press, 2016) at 242. Barbara Torreon, Instances of Use of United States Armed Forces Abroad 1798-2013 (Washington D.C: Congressional Research Service, 2013) (this report includes all military campaigns of the USA abroad. The list of countries in this chapter includes only the military campaigns that required involvement of US military to protect US commercial interests abroad). Thomas Johnson & Jonathan Gimblett, "From Gunboats to BITs: the Evolution of Modern International Investment Law" in Karl Sauvant, ed, *Yearbook on International Investment Law & Policy 2010-2011* (Oxford: Oxford University Press, 2012) at 665.

[201] Before the investment regime emerged, there were, of course, many steps in between to facilitate transition from "force" to "law". The scope of this thesis precludes this discussion yet more on this issue can be found in the following sources. Kenneth Vandevelde, *The First Bilateral Investment Treaties: U.S. Postwar Friendship, Commerce, and Navigation Treaties* (Oxford: Oxford University Press, 2017) at 186. Herman Walker, "Modern Treaties of Friendship, Commerce and Navigation" (1957) 42 Minnesota L Rev 805 at 806. Pearce Higgins, *The Hague Peace Conferences* (Cambridge: Cambridge University Press,

Of course, such substitution is in itself valuable because it creates another potential avenue for peaceful resolution of disputes in the spirit of the UN Charter.[202] The legal structures that this regime puts in place, however, deserve detailed scrutiny in light of the emerging concerns of the regime's participants that relate to consistency of legal interpretations, lack of legal structures that ensure certainty of law, and skewed incentives generated by the party-driven appointment system, possibility of foreign investors bringing frivolous claims and gaming the system of investment protection, for example, by conducting corporate restructuring to gain investment protection. This chapter has a humble objective, which is to set the foundations. This chapter includes the following major sections. Section 2.1. provides an overview of the legal structures that exist in the investment regime to outline the key "pillars" of the legal frameowrk. Section 2.2. explains the "lifecycle" of investment arbitration process from filing the claim until a possible annulment or enforcement of the decision. Section 2.3. examines possible reasons why states have joined IIAs and ISA to provide readers with greater context necessary to appreciate the existing dynamics in the investment regime and reinforce a point on its decentralized nature.

2014) at 40-52. Christian Tietje & Emily Sipiorski, "The Evolution of Investment Protection Based on Public International Law Treaties: Lessons to be Learned" in Andrea Bjorklund & August Reinisch, eds, *International Investment Law and Soft Law* (Northampton: Edward Elgar Publishing, 2012) at 665. V. V. Veeder, "The Lena Goldfields Arbitration: The Historical Roots of Three Ideas" (1998) 47:4 ICLQ 747. [201] J. G. Merrills, *International Dispute Settlement* (Cambridge: Cambridge University Press, 2005) at 308. Chester Brown, "Resolving International Investment Disputes" in Natalie Klein & Natalie Klein, *Litigating International Law Disputes: Weighing the Options* (Cambridge: Cambridge University Press, 2014) (states that "many mixed claims commissions of the later 1800s and early 1900s largely concerned the treatment of foreign nationals and their property"). Lea Brilmayer, Chiara Giorgetti & Lorraine Charlton, *International Claims Commissions: Righting Wrongs after Conflict* (Northampton: Edward Elgar Publishing, 2017) (on mixed claims commissions, including Mexico-US and Panama-US commissions). Karen Alter, *The New Terrain of International Law: Courts, Politics, Rights* (Princeton University Press, 2014) at 170 ("during the nineteenth century, approximately eighty claims commissions adjudicated private litigant cases arising out of war and civil unrest").

[202] *Charter of the United Nations*, 26 June 1945, Can TS 1945 No 7. [*UN Charter*] Bardo Fassbender, *The United Nations Charter as the Constitution of the International Community* (BRILL, 2009) at 30.

2.1 What is the International Investment Regime?

The sections below introduce the main features and processes of the investment regime, to help contextualize a subsequent discussion on frivolous and abuse of process claims in the investment regime. This background information is essential to understand the "mechanics" of the investment regime, i.e. how the regime functions and why it is distinctive from domestic legal systems and systems of state-to-state adjudication under public international law.

2.1.1 The Legal Framework in the International Investment Regime

The most salient structural characteristic of the investment regime is its extreme decentralization. Karl-Heinz Bockstiegel, a well-known arbitrator, identifies three elements of the legal framework of the investment regime.[203] The first element is the existence of more than 3000 IIAs.[204] The second element is that it encompasses international law and municipal law.[205] The third element is the multitude of rules that determine the arbitral procedure.[206] The subsections that follow apply Bockstiegel's classification to discuss in greater detail the structure of the legal framework in the investment regime.

2.1.1.1. International Investment Agreements

The first element of the legal structure is presented by IIAs. The purpose of IIAs is to promote and protect foreign investment. [207] IIAs are intended to establish a more "stable and predictable" legal framework to guarantee the protection of international

[203] Karl-Heinz Bockstiegel, "The Role of the Arbitrators in Investment Treaty Arbitration" in Albert Jan van den Berg, ed, *International Commercial Arbitration: Important Contemporary Questions* (The Hague: Kluwer Law International, 2002) at 367.
[204] *Ibid*.
[205] *Ibid*.
[206] *Ibid*.
[207] UNCTAD, Investment Promotion Provisions in International Investment Agreements, UNCTAD Series on International Investment Policies for Development (New York: United Nations, 2008) at xi.

investments, for both individuals and companies.[208] IIAs come in variety of forms.[209] This thesis focuses on the two most common types of IIAs, (1) Free Trade Agreements (FTAs) and (2) Bilateral Investment Treaties (BITs).[210]

IIAs establish the substantive standards that govern the conduct of states with regards to foreign investors. In other words, under these agreements states promise each other that they will treat each other's foreign investors according to the set of independent legal standards. IIAs set out what these promises entail.[211] IIAs incorporate a variety of relatively standardized investment rules, such as Fair and Equitable Treatment (FET), Full Protection and Security (FPS), Expropriation, Most-Favoured Nation Treatment (MFN), national treatment, and umbrella clauses.[212]

Before examining the most common investment standards, two warnings must be made. First, IIAs are constantly evolving. More specifically, distinct "generations" of IIAs have been identified in the literature.[213] According to UNCTAD,

> [o]lder investment treaties have been described as imbalanced instruments; overly protective of investor interests at the expense of host states' normative flexibility […] [n]ew generation treaties attempt to remedy these

[208] *Ibid*.
[209] Salacuse mentions that IIAs exist typically in three forms. As BITs, as FTAs and as other "investment related agreements". Salacuse (2015), at 1.
[210] The modern trend in investment law-making shows that states negotiate more complex mega-national treaties such as the famous *Trans-Pacific Partnership* (CPTPP). Cin Lim, Deborah Elms & Patrick Low, eds, *The Transpacific Partnership. A Quest for Twenty First Century Agreement* (Cambridge: Cambridge University Press, 2012). UNCTAD, World Investment Report: Reforming International Investment Governance (New York: United Nations, 2016).
[211] Gus Van Harten*, Investment Treaty Arbitration and Public Law* (Oxford: Oxford University Press, 2008) at 82.
[212] Dolzer & Schreuer (2012), at 14. On umbrella clauses, Chrisoph Schreuer, "Travelling the BIT Route of Waiting Periods, Umbrella Clauses and Forks in the Road" (2004) 5:2 J World Investment & Trade 231 at 249, 233-256. (Shreuer explains "umbrella clauses have been added to some BITs to provide additional protection to investors beyond the traditional international standards. They are often referred to as 'umbrella clauses' because they put contractual commitments under the BIT's protective umbrella. They add the compliance with investment contracts, or other undertakings of the host State, to the BIT's substantive standards. In this way, a violation of such a contract becomes a violation of the BIT").
[213] UNCTAD Report 2015 at 121.

> issues by, for instance, including some 'state-friendly' or 'public interest-friendly' provisions.[214]

This generational change occurs incrementally and is associated with broader concerns that relate to the legitimacy of the investment regime, an issue in detail discussed in Chapter Three.

Second, IIAs do not always elaborate on the content of the standard or describe its elements. For example, a typical formulation of the obligation of FET states simply, "[e]ach Contracting Party shall at all times ensure fair and equitable treatment to investments".[215] In practice, ambiguously worded investment standards mean that states delegate authority to the arbitrators to determine the scope of the investment obligations in particular treaties. This approach reduces the *ex ante* costs of the IIA negotiations because a detailed substantive standard may be more difficult to table for the negotiators than a vague one-sentence provision.[216] Yet the ambiguity of investment standards can result in *ex post* costs when states face claims of foreign investors in ISA, since the tribunals can "interpret the law in unanticipated and unwanted ways".[217] The new generation of IIAs include investment standards of more precise nature.[218]

Such features of the investment regime as decentralization of IIAs and ISA tribunals, lack of appelate review, and ambiguity of legal standards perpetuate uncertainty within the system, and result in a situation where tribunals inevitably struggle

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[214] Catharine Titi, "Most-Favoured-Nation Treatment: Survival Clauses and Reform of International Investment Law" (2016) 33:5 J Intl Arb 425 at 426.
[215] *Agreement between the Government of Australia and the Government of the Argentine Republic on the Promotion and Protection of Investments, and Protocol* (1995), at art.4
[216] The multilateral treaty on foreing investment reportedly failed because states were not able to agree on the substantial terms of the treaty including the appropriate definition of property, the expropriation standard and the standard for compensation.
[217] Karen Alter, "Delegating to International Courts: Self-Binding vs. Other-Binding Delegation Law and Contemporary Problems" (2008) 71:1 Law and Contemporary Problems 37 at 39.
[218] Makane Moise Mbengue & Stefanie Schacherer, "Africa and the Rethinking of International Investment Law" in Anthea Roberts et al, eds, *Comparative International Law* (Oxford: Oxford University Press, 2018) at 558.

to assess the merits of the investor's claim early in the proceedings. The following sections will demonstrate ambiguity of substantive investment standards and explain how tribunals' diverging interpretations further the standards' uncertainty. The investment standards are described in order by the frequency of their appearance in IIAs as pointed out by Bonnitcha, Poulsen and Waibel. Accordingly, MFN and expropriation appear in 95% of treaties, FET appears in 90% of treaties, followed by the FPS in 70% of treaties, and umbrella clauses in 45% of treaties.[219]

2.1.1.1.1 Expropriation

The expropriation standard protects foreign investors from property seizures. It does not prohibit expropriations altogether, but rather sets standards for them.[220] To be lawful, expropriation must generally satisfy three requirements under international law. It must be undertaken for a public purpose, must be non-discriminatory, and the state must pay prompt, adequate and effective compensation.[221] If any of these elements is not met, the seizure constitutes an unlawful expropriation.[222] The distinction between lawful and unlawful expropriation is significant for the purposes of compensation, as established by the *Permanent Court of International Justice* (PCIJ) in the *Case Concerning the Factory at Chorzow*.[223] Salacuse explains that "compensation for illegal expropriation is governed by […[the principles of customary international law, as illustrated by the

[219] Bonnitcha, Poulsen & Waibel (2018), at Table 4.1.
[220] Rudolf Dolzer & Margrete Stevens, *Bilateral Investment Treaties* (The Hague: Martinus Nijhoff Publishers, 1995). Andrew Newcombe, *Regulatory Expropriation, Investment Protection and International Law: When is Government Regulation Expropriatory and When Should the Compensation be Paid?* (University of Toronto, 1999), online: <http://www.italaw.com/documents/RegulatoryExpropriation.pdf:>. Bonnitcha (2014), at 144.
[221] August Reinisch, "Legality of Expropriations" in August Reinisch, ed, *Standards of Investment Protection* (Oxford: Oxford University Press, 2008) at 176.
[222] *Ibid*.
[223] *Case Concerning the Factory at Chorzo´w* (*Germany v Poland*) (1928), PCIJ (Ser A) No 17 at 47. The USA-Iran Claims Tribunal arrives to the same conclusion in the *Amoco* case. *Amoco International Finance v Iran*, Award (1987), 15 Iran-US CTR 189, 246 at para. 192.

Chorzow Factory case, which requires that to the extent possible the offending state restore the investor to the situation that would have existed before illegal expropriation took place".[224] ISA tribunals also distinguish between lawful and illegal expropriation, for the purposes of determining the amount of compensation. For example, in *ADC v Hungary*, the tribunal concluded that the amount of damages to be paid for lawful and unlawful expropriation is different.[225] In absence of a means for calculating the quantum of compensation provided in the applicable BIT, the tribunal referred to the standard of customary international law reflected in *Chorzow Factory*, where the PCIJ found that "reparation must, as far as possible, wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed".[226]

Apart from its legality or illegality, expropriation may be direct or indirect.[227] Direct expropriation involves the actual taking or destruction of property by a state or its regulatory bodies.[228] Indirect expropriation is a more controversial concept.[229] Arguably, it can encompass any governmental action or series of actions that impair the value of an

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[224] Salacuse (2015), at 150.
[225] *ADC v Hungary* (2006), Award ICSID Case No. ARB/03/16 (International Centre for Settlement of Investment Disputes) (Arbitrators: Charles Brower, Albert Jan van den Berg, Neil Kaplan) at para.481. [*ADC v Hungary*]. August Reinisch, "Is Expropriation Ripe for Codification? The Example of the Non-Discrimination Requirement for Lawful Expropriations" in Andrea Bjorklund & August Reinisch, eds, *International Investment Law and Soft Law* (Northhampton: Edward Elgar Publishing, 2012) at 280.
[226] Chorzów Factory [PCIJ] at 47.
[227] Sergey Ripinsky & Kevin Williams, *Damages in International Investment Law* (London: BIICL, 2008) at 64. Rudolf Dolzer, "Indirect expropriation of Alien Property" (1986) 1 ICSID Rev 41 at 59. Yves Fortier &Stephen Drymer, "Indirect Expropriation in the Law of International Investment: I Know It When I See It, or Caveat Investor" (2004) ICSID Rev 293.
[228] *Ibid* at 64-65.
[229] Foreign investors sometimes allege so-called "creeping expropriation" which is a type of indirect expropriation "that occurs as a result of a series of measures taken over time that cumulatively have an expropriatory effect, rather than a single measure or group of measures that occur at one time". Andrew Newcombe & Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (The Hague: Kluwer Law International, 2009) at 343. Burns Weston, "Constructive Takings Under International Law: A Modest Foray into the Problem of Creeping Expropriation" (1975) 16 Va J Intl L 103 at 106.

investor's investment.[230] For example, the tribunal in the *Marvin Feldman v Mexico* concluded that there are many ways in which a state can "force a company out of business",[231] including such state measures as "confiscatory taxation, denial of access to infrastructure or necessary raw materials, imposition of unreasonable regulatory regimes, among others, have been considered to be expropriatory actions".[232] In *Marvin Feldman*, the tribunal observes that states should have ability to "act in the broader public interest" by adopting regulatory measures, a sovereign power well-recognized in international law.[233] According to the tribunal, it is problematic to distinguish a legitimate exercise of governmental authority from expropriation.[234] The distinction between these two categories has practical significance; upon it depends the international responsibility of states for violation of IIAs obligations as well as the amount of compensation for those violations.[235]

Ethyl v Canada illustrates this difficulty. In *Ethyl v Canada*, the US-based investor sued the Canadian government for introducing an import ban for a chemical compound that, Canada alleged, could cause severe environmental harm.[236] The tribunal had to decide whether the ban constituted expropriation or a legitimate regulatory

[230] *Ibid*. Ana Maria Daza-Clark, *International Investment Law and Water Resources Management: An Appraisal of Indirect Expropriation* (The Hague: Brill, 2016) at 101.
[231] *Marvin Feldman v Mexico* (2002), Award Case No. ARB(AF)/99/142 ILM 625 (International Centre for Settlement of Investment Disputes) (Arbitrators: Konstantinos Kerameus, Jorge Covarrubias Bravo, David Gantz) at para.103.
[232] *Ibid*
[233] *Ibid*
[234] *Ibid* at para. 104, 112.
[235] Caroline Henckels, "Indirect Expropriation and the Right to Regulate: Revisiting Proportionality Analysis and the Standard of Review in Investor-State Arbitration" (2012)15:1 J Intl Econ L 223 at 231-235 (discusses the Tecmed case and examines the "balance between host state and investor interests"). *Técnicas Medioambientales Tecmed S.A. v United Mexican States* (2003), Award ICSID Case No. ARB (AF)/00/2 (International Centre for Settlement of Investment Disputes) (Arbitrators: José Carlos Fernández Rosas, Carlos Bernal Verea, Horacio Grigera Naón).
[236] *Ethyl Corp v Canada* (1998), Award on Jurisdiction, 38 ILM 708 (United Nations Commission on International Trade Law) (Arbitrators: Karl-Heinz Bockstiegel, Charles Brower, Marc Lalonde). Sean Murphy, *United States Practice in International Law:1999–2001* (Cambridge: Cambridge University Press, 2003) at 234.

measure.[237] The dispute was eventually settled.[238] However, the tribunal's task to distinguish an indirect expropriation from a non-compensable regulatory measure has proven to be difficult. The report by Organization for Economic Cooperation and Development (OECD) explains:

> few legal texts attempted to address directly how to distinguish legitimate non-compensable regulations having an effect on the economic value of foreign investments and indirect expropriation, requiring compensation. Scholars recognized the existence of the distinction but did not shed much light on the criteria for making the distinction.[239]

In *Pope & Talbot v Canada*, the tribunal concludes that "mere interference is not expropriation; rather, a significant degree of deprivation of fundamental rights of ownership is required".[240] The tribunal in *S.D. Myers v Canada* concludes:

> expropriations tend to involve the deprivation of ownership rights; regulations [constitute] a lesser interference. The distinction between expropriation and regulation screens out most potential cases of complaints concerning economic intervention by a state and reduces the risk that governments will be subject to claims as they go about their business of managing public affairs.[241]

A variety of factors may be taken into consideration by the tribunals to distinguish between expropriation and legitimate regulatory measure. Salacuse concludes that the investment treaties do not establish criteria for distinguishing the indirect expropriation from non-compensable measures, and moreover the decisions of ISA tribunals provide

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[237] *Ibid*.
[238] *Ibid*.
[239] OECD, Directorate for Financial and Enterprise Affairs, *Indirect Expropriation and the Right to Regulate in International Investment Law*, Working Paper No 4, Doc No 2004/4 (2004) at 9.
[240] *Pope & Talbot, Inc v Canada* (2000), Interim Award (United Nations Commission on International Trade Law) (Arbitrators: Lord Dervaird, Benjamin Greenberg, Murray Belman) at para.99.
[241] *SD Myers, Inc. v Canada* (2000), Partial Award 40 ILM 1408 (United Nations Commission on International Trade Law) (Arbitrators: John Hunter, Bryan Schwartz, Edward Chiasson) at para.282.

limited guidance as to factors the arbitrators will take into consideration.[242] Salacuse suggests the following list of five factors that tribunals ought to consider in distinguishing between indirect expropriations and non-compensable regulatory measures: "(1) whether the measure is within the recognized police powers of the host state (2) the public purpose and effect of the measure (3) whether the measure is discriminatory (4) the proportionality between the means employed and the aim sought to be realized; and (5) the bona fide nature of the measure".[243] Salacuse acknowledges that "the application" of these criteria "to specific cases is by no means easy or automatic".[244] For example, according to Salacuse, the *S.D. Myers* tribunal considered "the economic impact of the government action, the extent to which the government action interferes with distinct, reasonable investment-backed expectations, the character of the government action".[245] Of course, the facts of a particular dispute and the conduct of a state in its relations with a foreign investor play a paramount role in establishing whether expropriation occurred. Notably, the new generation of treaties avoid

> explicit criteria on how to determine whether a particular regulatory measure amounts to an indirect expropriation […] the basic approach taken is to state the provision on expropriation in the traditional manner but then indicate that those provisions are to be interpreted in accordance with attached treaty annexes.[246]

The "quantum of compensation" in cases of expropriation is still a matter of controversy.[247] In particular, it is highly contested whether states should provide foreign investors with full compensation under international law and particularly what such "full

[242] Salacuse (2015), at 334-335.
[243] Salacuse (2015), at 335.
[244] *Ibid.*
[245] *Ibid*.
[246] Salacuse (2015), at 150.
[247] Sornarajah (2010), at 32.

compensation" entails.[248] In the aftermath of the Second World War and decline of colonialism, the issue of expropriation and compensation became a focal point of disagreement between the decolonized nations and their former colonizers.[249] In particular, the decolonized states openly disputed the Western formula "prompt, adequate, and effective compensation" that states must pay in case of expropriation.[250] Instead, the formerly colonized states advance the concept of "appropriate compensation" or "adequate compensation" where the host state is in charge of determining the "adequacy" of the compensation depending on the circumstances.[251] There is still disagreement among scholars whether there is an obligation under customary international law to provide compensation in accordance with such terms. For example, Sornarajah observes that it remains to be an open question of what is "the exact standard of which the compensation is to be paid".[252]

The standard for distinguishing expropriation from a non-compensable regulatory measure and the quantum of compensation thus remain matters of significant controversy in international investment law.[253] Most IIAs do not state criteria that tribunals must apply and, as a result, the ISA tribunals have broad discretion in characterizing the nature of an expropriation and determining the amount of compensation.

2.1.1.1.2 Most-Favoured Nation Treatment

[248] *Ibid* at 414-418.
[249] Sol Picciotto, *Regulating Global Corporate Capitalism* (Cambridge: Cambridge University Press, 2011) at 158.
[250] *Ibid*.
[251] John Linarelli, Margot Salomon & Muthucumaraswamy Sornarajah, *The Misery of International Law: Confrontations with Injustice in the Global Economy* (Oxford University Press, 2018) at 156.
[252] Sornarajah (2010) at 414-418.
[253] Ripinsky & Williams (2008), at 317. Santiago Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (London: Bloomsbury Publishing, 2009) at 234.

The goal of the MFN provision is to guarantee a level playing field for the investors of the party of IIAs in relation to other investors of any non-party state. MFN requires state parties to "treat each other's investors no less favourably than investors of any non-party".[254] For example, article 4 of the US Model BIT (2012) contains the following MFN clause:

> [e]ach Party shall accord to investors of the other Party treatment no less favourable than that it accords, in like circumstances, to investors of any non-Party with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory.[255]

This MFN clause is "far reaching"[256] because it potentially applies both before and after an investment.[257] Batifort and Heath emphasize that IIAs incorporate differently-worded MFN clauses.[258] Differences in wording may explain differences in outcomes, but it is not clear that tribunals actually adopt a treaty-by-treaty approach to interpreting MFN provisions in IIAs.[259] Batifort and Heath observe that tribunals,

> may not practice what they preach: one study observed in 2011 that decisions on the scope of MFN clauses depended less on the specific terms or context of the treaty at issue than on the tribunal's presumptions concerning the scope and effect of these clauses.[260]

The core of the disagreement on MFN is on the scope of the standard, in particular whether the standard applies only to substantial guarantees in IIAs or can be interpreted in a way that investor can rely on MFN to obtain the procedural guarantees. In

[254] Titi (2016), at 427.
[255] US Model BIT (2012) at art.4.
[256] Titi (2016), at 427.
[257] *Ibid*.
[258] Simon Batifort & Benton Heath, "The New Debate on the Interpretation of MFN Clauses in Investment Treaties: Putting the Brakes on Multilateralization" (2018) AJIL Unbound at 13-14.
[259] *Ibid*.
[260] *Ibid*.

its special submission to the UNCITRAL Working Group, EU explains that the scope and application of MFN continues to be an example of controversy,

> [o]ne example is the ongoing saga on the applicability of the most-favoured nation (MFN) clauses to procedural matters (i.e. dispute resolution). While some tribunals have held that the MFN clause extends to dispute settlement provisions contained in treaties between the respondent State and third States, other tribunals have reached the opposite conclusion.[261]

Bonnitcha *et al* agrees that "[t]he extent to which MFN provisions allow investors covered by one investment treaty to benefit from the more favorable substantive and procedural provisions of other treaties has been controversial".[262] For example, in the case of *Mafezzini v Spain*, the tribunal extended the application of MFN to the dispute settlement provisions of the IIA, not just its substantive provisions.[263] Maffezini brought its claim under the *Argentina-Spain BIT*.[264] The tribunal compared the provisions of the *Chile-Spain BIT* with the *Argentina-Spain BIT*.[265] The tribunal concluded that "arrangements" of the *Chile-Spain BIT* were "more favourable" for foreign investors.[266] Accordingly, the tribunal allowed Mafezzini to take advantage of the dispute settlement provisions in the *Chile-Spain BIT*.[267] In the aftermath of the *Mafezzini* controversy, the arbitral jurisprudence predominantly seem to settle on the view that MFN clauses can be invoked by investors only to claim benefit of substantive investment standards in other

[261] UN GA, Possible Reform of Investor-State Dispute Settlement (ISDS): Submission from the European Union (2018), A/CN.9/WG.III/WP.145 at para.23.
[262] Bonnitcha, Skovgaard Poulsen & Waibel (2018), at 100.
[263] *Emilio Agustín Maffezini v Spain*, (2000), Award ICSID Case No. ARB/97/7 16 ICSID Rev 212 (International Centre for Settlement of Investment Disputes) (Arbitrators: Francisco Orrego Vicuña, Thomas Buergenthal, Maurice Wolf) at para. 21.
[264] *Ibid*.
[265] *Ibid*.
[266] *Ibid*.
[267] *Ibid*.

IIAs, and not to claim procedural protection.[268] It does not, however, prevent foreign investors from submitting the claims where they allege a possibility to rely on MFN of an applicable treaty to benefit from the dispute settlement clauses in other IIAs.[269] The most recent example is the *Power Rental Asset v Australia,* in which foreign investor relies on MFN under the *Australia-United States Free Trade Agreement* (AUFSTA) to benefit from the more favourable dispute settlement provisions in the *Australia-Hong-Hong* BIT.[270]

The possibility of "transporting" substantial standards from one IIA to another has generated even more pointed polemics. The tribunal in *White Industries v India* applied MFN to permit investors to rely on the substantive provisions of another investment treaty.[271] By contrast, the tribunal in *İçkale v Turkmenistan* "refused to apply an MFN clause [in the Turkey-Turkmenistan BIT], thus preventing the claimants from relying on

[268] Stephen Schill, *The Multilateralization of International Investment Law* (Cambridge: Cambridge University Press, 2009) at 139–40. Schill explains that broadly worded MFN clauses "are usually broad enough to apply not only to more favourable substantive treatment but also to more favorable procedural rights and broader consent to arbitration". Schill cites the MFN clauses examined in Plama, Salini, Telenor, Berschader, Wintershall cases.

[269] *Power Rental Asset Co Two LLC (AssetCo), Power Rental Op Co Australia LLC (OpCo), APR Energy LLC v. the Government of Australia* (2016), Notice of Dispute Under United States-Australia Free Trade Agreement, online:https://www.italaw.com/sites/default/files/case-documents/italaw8748.pdf.

[270] *Ibid*.

[271] *White Industries v India*, Award (United Nations Commission on International Trade Law) (Arbitrators: Charles Brower, Christopher Lau, William Rowley) at para.11.2-11.3. (In White Industries, the investor referred to MFN in the Australia-India BIT to rely on the protection of the provisions in India-Kuwait BIT, an approach that the tribunal upheld). *Agreement between the Government of Australia and the Government of Republic of India on the Promotion and Protection of Investments* (1999), at art.4(2) ("[a] Contracting Party shall at all times treat investments in its own territory on a basis no less favourable than that accorded to investments of investors of any third country"). *Agreement Between the State of Kuwait and The Republic of India for the Encouragement and Reciprocal Protection of Investment* (2001), at art.4.5 ("[e]ach Contracting State shall maintain a favourable environment for investments in its territory by investors of the other Contracting State. Each Contracting State shall in accordance with its applicable laws and regulations provide effective means of asserting claims and enforcing rights with respect to investments and ensure to investors of the other Contracting State. the right of access to its courts of justice. administrative tribunals and agencies. and all other bodies exercising adjudicatory authority, and the right to employ persons of their choice, for the purpose of the assertion of claims and the enforcement of rights with respect to their investments").

the substantive protections of another bilateral investment treaty".[272] The Article II(2) of the *Turkey-Turkmenistan BIT* incorporates the MFN clause that requires each state party to afford "treatment no less favourable than that accorded in similar situations to investments of its investors or to investments of investors of any third country".[273] In particular, the tribunal in *Íçkale* engaged in the textual analysis of the term "similar situations" pursuant to article 31 of the *Vienna Convention on the Law of Treaties* (VCLT).[274] The tribunal concluded that,

> [t]he terms "treatment accorded in similar situations" therefore suggest that the MFN treatment obligation requires a comparison of the factual situation of the investments of the investors of the home State and that of the investments of the investors of third States, for the purpose of determining whether the treatment accorded to investors of the home State can be said to be less favorable than that accorded to investments of the investors of any third State. It follows that, given the limitation of the scope of application of the MFN clause to "similar situations," it cannot be read, in good faith, to refer to standards of investment protection included in other investment treaties between a State party and a third State. [275]

Accordingly, the tribunal's interpretation of the term "similar situations" limited the scope of the MFN clause in the applicable BIT and prevented claimant from "importing" the more favourable substantial standards.[276] What is crucial in *Íçkale* as

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[272] Donald McRae, "Introduction to the Symposium on Simon Batifort and J Benton Heath, The New Debate on the Interpretation of MFN clauses in Investment Treaties: Putting the Brakes on Multilateralization" (2018) AJIL Unbound 38 at 38.*İçkale İnsaat Limited¸ Şirketi v Turkmenistan* (2016), Award ICSID Case No. ARB/10/24 (Arbitrators: Veijo Heiskanen, Carolyn B. Lamm, Philippe Sands). [*İçkale İnsaat v Turkmenistan]*

[273] *Agreement between the Republic of Turkey and Turkmenistan Concerning the Reciprocal Promotion and Protection of Investments* (1992), at art. II (2) ("Each Party shall accord to these investments [i.e., investments permitted into its territory pursuant to Article II(1)], once established, treatment no less favourable than that accorded in similar situations to investments of its investors or to investments of investors of any third country, whichever is the most favourable").

[274] *İçkale İnsaat v Turkmenistan* at para.328.

[275] *Ibid* at para.329.

[276] *Ibid* at para. 332.

McRae, points out "the case that prompted this debate, was a relatively conventional MFN clause. If the MFN clause in Íçkale did not incorporate substantive standards of treatment, then perhaps no MFN clause will".[277]

Batifort and Heath analysed *Íçkale* and sought to demonstrate that if the MFN clauses in the applicable IIAs are interpreted appropriately under article 31 of VCLT, the clauses may not allow the import substantial provisions from other treaties.[278] Their position sparked a debate among academics, captured in a symposium issue of the American Journal of International Law Unbound where a number of prominent scholars diverged on the implications of the decision for the conventional application of MFN, i.e. whether MFN can be used by investors to rely on the substantive guarantees provided in other treaties.[279]

In *Plama v Bulgaria*, the tribunal warned that MFN can be used to "to pick and choose provisions from the various BITs".[280] Such a cherry-picking approach to using clauses from other IIAs undermines the nationality principle of the investment regime because a state may become bound by further obligations that it "has not specifically agreed thereto" with respect to the nationals of particular states.[281] UNCTAD explains that the broad interpretation of MFN clauses can serve to:

> potentially undermine individual treaty bargains and side-lining the base treaty […] treaty commitments may clash, or hard-won concessions in a negotiation (e.g. on flexibility in performance requirements) may be undone through the

[277] McRae (2018), at 40.
[278] Simon Batifort & Benton Heath, "The New Debate on the Interpretation of MFN Clauses in Investment Treaties: Putting the Brakes on Multilateralization" (2017) 4 AJIL 873.
[279] Symposium on Simon Batifort & Benton Heath, "The New Debate on the Interpretation of MFN Clauses in Investment Treaties: Putting the Brakes on Multilateralization" (2018) AJIL Unbound 38. The academics that contributed to the debate include Donald McRae, Andrea Bjorklund, Martins Paparinskis, Facundo Pérez-Aznar, Michael Waibel.
[280] *Plama Consortium* at para. 219.
[281] *Ibid*.

> application of a broadly worded MFN clause, as interpreted by arbitral tribunals.[282]

Accordingly, individual foreign investors can seek to obtain more expansive protection via MFN than what is available under their negotiated IIA.[283] In this regard, MFN clauses have potential to produce further controversies. For example, as Patrick Dumberry explains, if an IIA between two states does not incorporate an investment standard (for example, fair and equitable treatment (FET)), a foreign investor can use the MFN clause to "claim the benefit of a FET clause found in another treaty".[284] Dumberry examined 75 BITs that do not incorporate FET but include MFN clauses and concluded that in "almost all cases investors will indeed be able to benefit from FET clauses contained in other BITs".[285] There are two problems that arise out of such possibility. First, as Dumberry himself observes, the presence of a broadly worded MFN clause in IIA (even if FET is excluded) exposes states to claims of an FET violation. Second, if MFN is utilized by foreign investors as a device to claim an FET violation, foreign investors (in theory) can cherry-pick BIT with the most vaguely worded FET clause to allow the tribunal broad discretion in interpreting the standard.[286] Given that the FET standard (as will be discussed in subsection 1.1.1.4.) remains a subject of divergent interpretations by ISA tribunals, the possibility of "transportation" of substantial

[282] UNCTAD, *World Investment Report 2015* at 136.
[283] *Laurence Boisson de Chazournes' Dissenting Opinion in Garanti Koza L.L.P. v Turkmenistan* (2013), ICSID Case No. ARB/11/20, Decision on the Objection to Jurisdiction for Lack of Consent at para. 40. Boisson de Chazournes argues that MFN cannot be used before the tribunal established jurisdiction. Stern also makes similar argument that investors cannot use MFN to access the BIT. According to Stern, "[t]here are rights and there are fundamental conditions for access to the rights … an MFN clause can only concern the rights that an investor can enjoy, it cannot modify the fundamental conditions for the enjoyment of such rights, in other words, the insuperable conditions of access to the rights granted in the BIT" in Brigitte Stern's Concurring and Dissenting Opinion in Impregilo S.p.A. v. Argentina (2011), ICSID Case No. ARB/07/17, Award at para.47.
[284] Patrick Dumberry, "The Importation of the FET Standard through MFN Clauses: An Empirical Study of BITs" (2017) 32:1 ICSID Rev 116 at 117.
[285] *Ibid* at 136.
[286] *Ibid*.

standards in IIAs via the MFN provisions increases uncertainty of law. The newly negotiated treaties, such as CETA at article 8.7 (1) and (4), significantly limit the scope of MFN by excluding the possibility of importing dispute resolution procedures and substantive standards from other international investment and trade treaties.[287] CETA art. 8.7(1) provides that parties shall accord "an investor of the other Party and to a covered investment, treatment no less favorable than the treatment it accords in like situations, to investors of a third country and to their investments".[288] However, paragraph (4) of the same provision significantly limits the scope of this guarantee:

> the "treatment" referred to in paragraphs 1 and 2 does not include procedures for the resolution of investment disputes between investors and states provided for in other international investment treaties and other trade agreements. Substantive obligations in other international investment treaties and other trade agreements do not in themselves constitute "treatment", and thus cannot give rise to a breach of this Article absent measures adopted or maintained by a Party pursuant to those obligations.[289]

It seems that EU and Canada learned a lesson from a controversy that emerged in the arbitral practice and attempted to anticipate possible challenges by limiting the scope of MFN. CETA is yet to be ratified, and we only can guess if CETA-type MFN will become a new gold standard for MFN clauses in IIAs.

2.1.1.1.3 Full Security and Protection

The FPS standard in IIAs provides that "the host State is under an obligation to take active measures to protect the investment from adverse effects".[290] The scope of this

[287] CETA at article 8.7(4).
[288] *Ibid*.
[289] CETA at article 8.7(4).
[290] Christoph Schreuer, "Full Protection and Security" (2010)1:2 J Intl Disp Settl 353 at 353.

obligation continues to be a matter of controversy.[291] Some tribunals conclude that FPS includes only physical protection and does not "imply strict liability of the host State".[292] For example, *Rumeli v Kazakhstan* observes that under FPS, the state is obligated to "provide a certain level of protection to foreign investment from physical damage".[293] Other tribunals have held that the scope of FPS includes not only an obligation of physical protection but also of legal protection.[294] For example, in *Saluka Investments BV v the Czech Republic*, the tribunal emphasized that FPS imposes an obligation on a state to guarantee the physical integrity of an investment as well as an obligation to "take all

[291] *Ibid* (not all tribunals agree with this interpretation of FPS, since it might be regarded as overly broad in the sense that it "would result in equating the standard with fair and equitable teatment". Some tribunals agree that FPS and the fair and equitable treatment standards are two different standards under IIAs. Others do not draw a distinction between the two standards. Yet Schreuer observes that "the content of the two standards is distinguishable). Newcombe & Paradell (2009), at 311. A*zurix Corp. v The Argentine Republic* (2008), Award ICSID Case No. ARB/01/12 47 ILM 445 (International Centre for Settlement of Investment Disputes) (Arbitrators: Andres Rigo Sureda, Marc Lalonde, Hugo Martins) at para. 407 [*Azurix v Argentine*]. *Jan de Nul v Egypt* (2008), Award ICSID Case No. ARB/04/13 32 ILM 933 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gabrielle Kaufmann-Kohler, Pierre Mayer, Brigitte Stern) at para 269. *Siemens v Argentina* (2007), Award ICSID Case No. ARB/02/8 44 ILM 138 (International Centre for Settlement of Investment Disputes) (Arbitrators: Andrés Rigo Sureda, Charles Brower, Domingo Bello Janeiro) at para.302. ("although the parties have argued the application of this standard as a single standard, the Treaty provides for the fair and equitable treatment and full protection and security under two different Articles. The parties do not seem to have found this separation to be significant and the Tribunal will not dwell further on this point"). *Wena Hotels Ltd v Arab Republic of Egypt* (2000), Award 41 ILM 881 ICSID Case No. ARB/98/4 (International Centre for Settlement of Investment Disputes) (Arbitrators: Monroe Leigh, Ibrahim Fadlallah, Don Wallace) at para.84-85. [*Wena Hotels*]. Occidental *Exploration & Production Co. v Ecuador* (2004), Award LCIA Case No. UN3467 (London Court of International Arbitration Administered Case) (Arbitrators: Francisco Orrego Vicuna, Charles Brower, Patrick Barrera Sweeney) at para.180-192.

[292] Stephan Schill, *International Investment Law and Comparative Public Law* (Oxford: Oxford University Press, 2010) at 205. *Biwater Gauff v Tanzania* at para.729 (the tribunal interprets FSP as the standard that requires legal, physical and commercial protection). *National Grid v Argentina* (2008), Award (United Nations Commission on International Trade Law) (Arbitrators: Alejadro Miguel Garro, Judd Kessler, Andres Rigo Sureda) at para.189. ("[t]he Tribunal concludes that the phrase "protection and constant security" as related to the subject matter of the Treaty does not carry with it the implication that this protection is inherently limited to protection and security of physical assets"). *Ronald Lauder v The Czech Republic* (2001), (United Nations Commission on International Trade Law) (Arbitrators: Robert Briner, Philipe Cutler, Daniel Klein) at para.308 (establishes that FPS requires a state to protect investment from any possible loss of value caused by person whose acts cannot be attributed to the state").

[293] *Rumeli v Kazakhstan* (2008), Award ICSID Case No. ARB/05/16 (International Centre for Settlement of Investment Disputes) (Arbitrators: Stewart Boyd, Marc Lalonde, Bernard Hanotiau) at para 668.

[294] *Saluka Investments v The Czech Republic* (2006), Partial Award (United Nations Commission on International Trade Law) (Arbitrators: Arthur Watts, Yves Fortier, Peter Behrens) at para 483, 484. [*Saluka*].

measures necessary to ensure the full enjoyment of protection and security of its investments and should not be permitted to invoke its own legislation to detract from any such obligation".[295]

Most tribunals acknowledge that FPS includes physical protection, the tribunals however diverge on the question of who must supply that protection and from whom. For example, in *Eastern Sugar v Czech Republic*, the tribunal underscores that a host state has an obligation under FPS "to protect the investor from third parties", including "mobs, insurgents, rented thugs and other engaged in physical violence against the investor in violation of the state monopoly of physical force".[296] In another case, *Parkerings v Lithuania*, the tribunal indicates that FPS guarantees physical protection from the injury that is "committed either by the host State, or by its agencies or by an individual".[297] There however, the tribunal specified that the claimant must show that an injury committed by a third party "would have been prevented if the authorities had acted differently".[298]

Protection from legal harms under FPS is the subject of even greater controversy, as demonstrated in the *Azurix v Argentina* decision.[299] In that case the tribunal offered a broad view of the FPS obligation:

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[295] *Wena Hotels* at para. 84. *AAPL v Sri Lanka* (1990), Award ICSID Case No. ARB/87/3 30 ILM 577 4 ICSID Rep 250 (International Centre for Settlement of Investment Disputes) (Arbitrators: Berthold Goldman, Samuel Asante, Ahmed El-Kosheri) at para.77 (the tribunal indicated that FSP requires "a well-administered government" to uphold security of investment; "due diligence is nothing more nor less than the reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances"). [*AAPL v Sri Lanka*].

[296] *Eastern Sugar v The Czech Republic* (2004), Partial Award SCC Case No. 088/2004 (Arbitration Institute of the Stockholm Chamber of Commerce) (Arbitrators: Robert Volterra, Pierre Karrer, Emmanuel Gaillard) at para.203.

[297] *Parkerings-Compagniet AS v Republic of Lithuania* (2007), Award ICSID Case No. ARB/05/8, (International Centre for Settlement of Investment Disputes) (Arbitrators Julian Lew, Marc Lalonde, Laurent Levy) at para.355.

[298] *Ibid* at para.356-357.

[299] *Azurix v Argentine* at para.408.

> [t]he cases referred to above show that full protection and security was understood to go beyond protection and security ensured by the police. It is not only a matter of physical security; the stability afforded by a secure investment environment is as important from an investor's point of view […] when the terms 'protection and security' are qualified by 'full' and no other adjective or explanation, they extend, in their ordinary meaning, the content of this standard *beyond* physical security.[300]

The scope of FPS is important for a potential state's liability for a violation of an applicable IIAs. Some recently-negotiated treaties narrow the scope of the FPS standard. For example, CETA explicitly states that the state parties only hold obligations to guarantee physical protection to foreign investors.[301] This clarification helps to narrow the scope of the standard and thus constrains the discretion of the tribunals on this matter.

2.1.1.1.4 Fair and Equitable Treatment

The term FET originated from the treaty drafting practices following World War II.[302] The term "equitable treatment of foreigners" was coined even earlier, by the PCIJ.[303] Contemporary IIAs often mention FET but neither define the term nor set out explicit criteria for finding a violation of this obligation.[304] The formulation of FET can also vary from one treaty to another; these "generational" differences apparent between

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[300] *Ibid* [Emphasis added].
[301] Matthias Herdegen, *Principles of International Economic Law* (Oxford: Oxford University Press, 2016) at 469.
[302] Martins Paparinskis, *The International Minimum Standard and Fair and Equitable Treatment* (Oxford: Oxford University Press, 2013) at 84.
[303] *Ibid* at 86.
[304] Fulvio Maria Palombino, *Fair and Equitable Treatment and the Fabric of General Principles* (Berlin: Springer, 2017) at vii. Chester Brown, *Commentaries on Selected Model Investment Treaties* (Oxford: Oxford University Press, 2013) at 215. *Agreement Between the Government of Canada And The Government Of The Republic Of Argentina For The Promotion And Protection Of Investment* at article 2, para.4. (investments and investors must be "accorded fair and equitable treatment in accordance with principles international"). *Agreement between the Czech and Slovak Federal Republic and the Kingdom of Denmark for the Promotion and Reciprocal Protection of Investments* at art.3, para.1 ("Investments of investors of either Contracting party shall at all times be accorded fair and equitable treatment"). *Agreement between Australia and the Republic of Hungary on the Reciprocal Promotion and Protection of Investments* at art. 3, para.2 ("A Contracting Party shall ensure fair and equitable treatment in its own territory to investments").

older and newer IIAs.[305] Even when interpreting the same language, ISA tribunals have diverged in their interpretations of the scope and content of the FET standard.[306] According to UNCTAD, FET can include the following elements:

> (a) Prohibition of manifest arbitrariness in decision-making, that is, measures taken purely on the basis of prejudice or bias without a legitimate purpose or rational explanation; (b) Prohibition of the denial of justice and disregard of the fundamental principles of due process; (c) Prohibition of targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief; (d) Prohibition of abusive treatment of investors, including coercion, duress and harassment; (e) Protection of the legitimate expectations of investors arising from a government's specific representations or investment-inducing measures, although balanced with the host State's right to regulate in the public interest.[307]

OECD identifies that three categories of interpretations of FET clauses in IIAs. FET may be "a self-contained standard",[308] it can be linked to international law,[309] it can be limited more specifically to the customary international minimum standard of treatment (MST).[310] The rest of this section will examine the three interpretations of FET

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[305] Earlier treaties contain broad formulations of FET; the later IIAs contain FET with narrower formulations. For example, for the earlier treaties: *Agreement between the Government of Australia and the Government of the Independent State of Papua New Guinea for the Promotion and Protection of Investments* (1991) at art.3, para.3 ("Investments by nationals or companies of either Contracting Party shall at all times be accorded fair and equitable treatment"). For later generation of treaties, e.g. CETA includes the set of criteria that constitute a violation of FET at art.8.10, para.2.

[306] Ioana Tudor, *The Fair and Equitable Treatment Standard in the International Law of Foreign Investment* (Oxford: Oxford University Press, 2008) at 33. Alexandra Diehl, *The Core Standard of International Investment Protection: Fair and Equitable Treatment* (The Hague: Wolters Kluwer, 2012).

[307] UNCTAD, *Fair and Equitable Treatment: UNCTAD Series on Issues in International Investment Agreements II* (New York: United Nations, 2012) at 28. [*UNCTAD 2012*]

[308] OECD, Directorate for Financial and Enterprise Affairs, *Fair and Equitable Treatment Standard in International Investment Law*, Working Paper No 3, Doc No 2004/3 (2004).*China-Switzerland BIT* (2009) at art.4 ("[i]nvestments and returns of investors of either Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy full protection and security in the territory of the other Contracting Party").

[309] *Ibid*. *Croatia-Oman BIT* (2004), at art.3(2) ("Investments or returns of investors of either Contracting Party in the territory of the other Contracting Party shall be accorded fair and equitable treatment in accordance with international law and provisions of this Agreement").

[310] *Ibid*. NAFTA Free Trade Commission, "Notes of Interpretation of Certain Chapter 11 Provision" (adopted 31 July 2001), at para.2. [NAFTA Notes of Interpretation] ("Article 1105(1) prescribes the

that can be seen in the published awards, to demonstrate the level of uncertainty and divergence that persists.

First, let us examine FET in its linkage to MST. Some IIAs link MST to FET (and to FSP) in the hope that the connection will provide greater clarity and precision about the scope of the applicable standard.[311] For example, under NAFTA, the state parties issued a joint interpretation to clarify the scope of the FET standard,[312] which is mandatory for NAFTA tribunals to follow.[313] The joint interpretation determines that the state parties need not accord the foreign investors any rights beyond the MST standard under international law.[314]

However, the joint interpretation adds little to tribunals' understanding of the exact content of FET, since the scope of MST is itself uncertain,[315] leaving the joint interpretation "an unsuccessful attempt to solve the controversy".[316] According to UNCTAD, any "attempts to equate the two standards may be perceived as paying

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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. 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 the customary international law minimum standard of treatment of aliens"). Certain German Interests in Polish Upper Silesia, the PCIJ held that the governments have an obligation to respect the rights of aliens under international law. *Case Concerning Certain German Interests in Polish Upper Silesia* (*Germany v Poland*) (1926), PCIJ (Ser A) No 7 at 22 and 42. Newcombe & Paradell (2009), at 15.

[311] Marc Jacob & Stephan Schill, "Fair and Equitable Treatment: Content, Practice, Method" in Marc Bungenberg et al, eds, *International Investment Law* (Munich: Beck, 2015) (states that "a uniform and doctrinally clear vision of what limitations the standard precisely entails for State measures affecting foreign investors remains elusive") at 3. Andres Rigo Sureda, *Investment Treaty Arbitration: Judging Under Uncertainty* (Cambridge: Cambridge University Press, 2012) at 76 (FET "has been the subject of controversy, most importantly in relation to whether it reflects the customary law minimum standard of treatment of aliens or a higher level of protection"). *Agreement between Canada and the Czech Republic for the Promotion and Protection of Investment* (2012) at art.3, para.1(b) ("[t]he concepts of "fair and equitable treatment" […] do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens".)

[312] NAFTA Notes of Interpretation 249.

[313] NAFTA at art.1131, para.2.

[314] NAFTA Notes of Interpretation 249.

[315] Paparinskis (2013), at 83-105. Roland Kläger, *Fair and Equitable Treatment in International Investment Law* (Cambridge: Cambridge University Press, 2011) at 60-85. Rudolf Dolzer, "Fair and Equitable Treatment: Today's Contours" (2014) 12:7 Santa Clara J Intl L 7.

[316] Tudor (2010), at 43.

insufficient regard to the substantial debate in international law concerning the international minimum standard".[317] Moreover, UNCTAD submits:

> [the] difficulty with this line of thinking is that it presupposes the existence of a general consensus as to what constitutes the minimum standard of treatment of aliens under customary international law. The reality, however, is that the minimum standard itself is highly indeterminate, lacks a clearly defined content and requires interpretation.[318]

It is worth noting that the NAFTA parties issued their joint interpretation after a series of decisions by ISA tribunals that interpreted FET expansively but inconsistently. In *SD Myers v Canada*, Canada adopted a regulatory measure to prevent waste disposal in compliance with the Basel Convention.[319] SD Myers claimed that the measure *de facto* discriminated against investors from the USA.[320] The tribunal sided with the US investor and concluded that Canada violated the FET standard because *de facto* discrimination constituted a breach of FET under NAFTA.

In *Metalclad v Mexico*, the foreign investor approached the Mexican government to obtain permits for building a hazardous waste facility.[321] Initially, the federal authorities assured Metalclad that the permits would be granted without any obstacles. The local authorities, however, did not issue the required permits, in part because of protests by the local population against the waste facility. The tribunal sided with the foreign investor and concluded that Mexico violated FET standard. However, the interpretation of FET in *Metaclad* was different from the one in *S.D. Myers*. The tribunal

[317] UNCTAD, Fair and Equitable treatment (1999).
[318] *UNCTAD 2012* at 28.
[319] *SD.Myers Inc v Canada*, Partial Award (2000), (United Nations Commission on International Trade Law) (Arbitrators: Ian Hunter, Bryan Schwartz, Edward Chiasson). [*S.D.Myers Partial Award*].
[320] *Ibid*.
[321] *Metalclad Corporation v The United Mexican States* (2000), Award ICSID Case No. ARB(AF)/97/1, (International Centre for Settlement of Investment Disputes) (Arbitrators: Elihu Lauterpacht, Benjamin Civiletti, Jose Luis Siqueiros).

in *Metalclad* held that the FET standard is not linked to international law and constituted a standalone obligation.[322] In *SD Myers*, the tribunal concluded that FET under NAFTA must be understood not in isolation but as "treatment in accordance with international law".[323]

In *Pope & Talbot v Canada*, another NAFTA case, the tribunal adopted an even broader interpretation of FET than the one in *Metalclad*. It followed what it called "additive interpretation".[324] The *Pope & Talbot* tribunal held that the FET obligation under NAFTA must be interpreted as follows: "covered investors and investments receive the benefits of the fairness elements under ordinary standards applied in the NAFTA countries, without any threshold limitation that the conduct complained of be 'egregious' 'outrageous', 'shocking', or 'otherwise extraordinary'."[325] Thus, in these three cases, all of them interpreting the same IIA (NAFTA), the tribunals arrived at three different interpretations of the scope and content of FET. It was these inconsistent outcomes that spurred the NAFTA parties to issue a mandatory interpretation of the FET standard under NAFTA.

Even in the aftermath of the joint interpretation, tribunals have continued to generate controversy.The tribunal in *Merrill & Ring Forestry LP v Canada* concludes that the consensus on the meaning of MST does not exist in principle and the content of international minimum standard is a subject of "a broad and unsettled discussion".[326]

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[322] *Ibid*.
[323] *S.D. Myers, Partial Award* at para.262, 258.
[324] *Pope & Talbot v Government of Canada*, Award on the Merits of Phase 2 (United Nations Commission on International Trade Law) (Arbitrators: Lord Dervaird, Benjamin Greenberg, Murray Belman) at para.111-117.
[325] *Ibid* at para.118
[326] *Merrill & Ring Forestry L.P. v Canada* (2010), Award (International Centre for Settlement of Investment Disputes) (Arbitrators: Francisco Orrego Vicuña, Kenneth Dam, William Rowley) at para. 182. [*Merrill & Ring Forestry*]. David Collins, *An Introduction: International Investment Law* (Cambrdige:

What is often taken to be the customary international law standard for MST was articulated in *Neer v United Mexican States,* a decision of the US-Mexico General Claims Commission. According to *Neer*, a state violates MST only if "the treatment of an alien […] amount[s] to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency".[327] Some tribunals accept that the *Neer* case sets the limit for MST, the highest standard states may be held to.[328] Even among these tribunals, however, disagreement persists about what state actions are "shocking" or "outrageous".[329]

Other tribunals, however, have held that the interpretation of MST under *Neer* is only a starting point for analysing the scope of the standard.[330] According to this view, the MST standard is not static and has evolved throughout history.[331] For example, in *Clayton & Bilcon v Canada*, the tribunal concludes it is necessary to view MST-FET

Cambridge University Press, 2017) at 136 (argues that the linkage between MST and FET "presupposes the existence of a general consensus as to what constitutes the minimum standard of treatment, whereas in reality the minimum standard of treatment is in itself ambiguous").

[327] *LFH Neer and Pauline Neer v Mexico* (US v Mexico) (1926) 4 RIAA 60 at para. 61-62.

[328] *Waste Management v Mexico Phase Two* (2004), Award ICSID Case No ARB(AF)/00/3 43 ILM 967 (International Centre for Settlement of Investment Disputes) (Arbitrators: James Crawford, Benjamin Civiletti, Eduardo Magallón Gómez) at para. 98. [*Waste Management* 2, Award]. *International Thunderbird Gaming Corporation v Mexico* (2006), Award (United Nations Commission on International Trade Law) (Arbitrators: Agustín Portal Ariosa, Thomas Wälde, Albert Jan van den Berg) at para.194 [*International Thunderbird*]. *Glamis Gold, Ltd. v United States* (2009), Award 48 ILM 1038 (United Nations Commission on International Trade Law) (Arbitrators: Michael Young, David Caron, Kenneth Hubbard) at para.22 [*Glamis Gold*]. *Cargill v Mexico* (2009), Award ICSID Case No. ARB(AF)/05/2 (International Centre for Settlement of Investment Disputes) (Arbitrators: Michael Pryles, David Caron, Donald McRae) at para. 284–285. [*Cargill*].

[329] *Glamis Gold* at para. 616; *Cargill* at para. 285.

[330] *Merrill & Ring Forestry* at para.209.

[331] *ADF Group Inc. v United States of America* (2003), Award ICSID Case No. ARB(AF)/00/1 (International Centre for Settlement of Investment Disputes) (Arbitrators: Florentino Feliciano, Armand de Mestral, Carolyn Lamm) at para. 181 (the MST standard does not "automatically extendible to the contemporary context of treatment of foreign investors and their investments by a host or recipient State"). *Cargill* at para. 281-282, 284 (the MST standard has evolved and Neer should "adapt the principle underlying the holding of the Neer arbitration to the more complicated and varied economic positions held by foreign nationals today"). *Mondev v United States of America* (2002), Award ICSID Case No. ARB(AF)/99/2 42 ILM 85 (United Nations Commission on International Trade Law) (Arbitrators: Ninian Stephen, James Crawford, Stephen Schwebel) at para. 116.

under NAFTA though the lens of its historical development, with *Neer* only as a starting point, and observes that "the international minimum standard has evolved over the years towards greater protection for investors".[332] The words of the ISA tribunal in the *Merrill & Ring Forestry LP v Canada* case are illustrative:

> the restrictive *Neer* standard has not been endorsed or has been much qualified. The parties have extensively discussed whether the customary law standard might have converged with the fair and equitable treatment standard, but convergence is not really the issue. The situation is rather one in which the customary law standard has led to and resulted in establishing the fair and equitable treatment standard as different stages of the same evolutionary process.[333]

The tribunal in *Merrill & Ring* observes that "today's minimum standard is broader than that defined in the *Neer* case and its progeny"[334] and further characterizes the approach of other NAFTA tribunals as "an open and non-restricted approach".[335] Kinnear legitimately asks "how is a constantly evolving standard to be reconciled with certainty and predictability?"[336] Kinnear's response is that "[s]uch uncertainty may well be an inevitable result of the reasoning process in investor-State arbitration, which tends to decide cases on an ad hoc basis and by reference to previous cases dealing with similar fact situations".[337] In *Bilcon*, another NAFTA case, the arbitrators disagreed on the

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[332] *William Ralph Clayton, William Richard Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware Inc. v Government of Canada* (2009), Award on Jurisdiction and Liability PCA Case No. 2009-04 (United Nations Commission on International Trade Law) (Arbitrators: Bruno Simma, Donald McRae, Bryan Schwartz) at para. 434, 435. [*Clayton Bilcon*].
[333] *Merrill & Ring Forestry* at para.209.
[334] *Ibid* at 213.
[335] *Ibid*.
[336] Meg Kinnear, "The Continuing Development of the Fair and Equitable Treatment Standard" in Andrea Bjorklund, Ian Laird & Sergey Ripinsky, eds, *Investment Treaty Law: Current Issues. Remedies in International Investment Law Emerging Jurisprudence of International Investment Law* (London: BIICL, 2009) at 237.
[337] *Ibid*.

threshold to find a violation of FET-MST standard,[338] with McRae dissenting from the majority decision.[339] Clayton and Bilcon are US-based investors that brought a NAFTA claim against Canada for alleged mistreatment by the provincial authorities in Nova Scotia. The investors argued that the provincial authorities initially encouraged their investment project, the building of certain industrial projects on the coast.

Under Canadian law, before foreign investor can obtain a permit, it must pass an Environmental Impact Assessment (EIA) before an independent body; the assessment concluded that Bilcon's projects would negatively impact the environment in Nova Scotia, a decision that ultimately resulted in denial of the necessary permit. In *Bilcon*, the tribunal concluded that Canada violated the FET-MST standard. According to the *Bilcon* award, a violation of Canadian law is tantamount to a breach of the NAFTA FET-MST standard.[340] Arbitrator McRae dissented; he would have held that NAFTA sets a higher threshold to establish a breach of FET-MST.[341] To support his conclusions, McRae cited the *SD Myers* and *GAMI* cases, which held that a violation of national law does not necessarily amount to a violation of international law.[342]

Another controversial point is the FET element known as legitimate expectations (LE). Before examining the types of LE, it is worth noting that LE is considered an element of FET, or at least a part of the analysis to establish a violation of FET.[343] The

[338] Michael Carfagnini, "Too Low a Threshold: Bilcon v Canada and the International Minimum Standard of Treatment" (2016) 53 Can YB Intl L 244.
[339] *Clayton Bilcon*, Dissenting Opinion by Donald McRae, In the Matter of an Arbitration Under Chapter Eleven of the North American Free Trade Agreement and the UNCITRAL Rules of 1976 (UNCITRAL Rules) between William Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware Inc and the Government of Canada [McRae Dissenting Opinion for Bilcon].
[340] *Ibid*.
[341] McRae Dissenting Opinion for Bilcon at para.3,52-53.
[342] *Ibid*.
[343] Hector Mairal, "Legitimate Expectations and Informal Administrative Representations" in Stephan Schill,ed, *International Investment and Comparative Public Law* (Oxford: Oxford University Press) at 418.

roots of LE remain controversial, since IIAs usually do not specify whether FET encompasses protection of investors' LEs.[344] Bonnitcha identifies three relevant questions for establishing responsibility of a state for a violation of LE:

> 1.On what basis must an expectation rest to qualify for protection under the FET standard?
>
> 2.Of expectations that rest on a recognized basis, by what criteria are legitimate expectations identified?
>
> 3.To what extent must a claimant rely on a legitimate expectation to recover for its breach?[345]

According to Bonnitcha, there are four approaches in the relevant ISA cases to answering the first question.[346] These are,

> i) Expectations can only rest on specific rights that the investor has acquired under domestic law.
>
> ii) in addition to i), expectations may rest on specific representations made to the investor by government officials.
>
> iii) in addition to ii), expectations may rest on the regulatory framework in force in the host state at the time the investor made the investment.
>
> iv) in addition to iii), expectations may rest on the business plans of the investor.[347]

Bonnitcha eventually categorizes the case law into four distinct approaches that the tribunals follow i, which are: (1) the legal rights approach[348] (2) the representations

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[344] *Ibid* at 419-420.
[345] Jonathan Bonnitcha, *Substantive Protection under Investment Treaties* (Cambridge: Cambridge University Press, 2014) at 168.
[346] *Ibid* at 169.
[347] *Ibid*.
[348] *Ibid* at 170. The legal rights approach constitutes "[t]he narrowest interpretation of the doctrine of legitimate expectations is that is protects only specific, enforceable legal rights that have vested in the investor under domestic law. Further criteria then determine the circumstances in which an interference with a particular legal right will amount to a breach of legitimate expectations". This approach is followed in cases: *LG&E Energy v Argentina* (2007), Decision on Liability 46 ILM 40 (International Centre for

approach[349] (3) the stability approach,[350] and (4) the business plan approach.[351] It is beyond the scope of this thesis to discuss in detail LE as an element of FET in the ISA jurisprudence. Instead, this reference to the Bonnitcha's study is intended to show that at least four distinct approaches to the scope of LE can be found in the case law. The scope of the applicable standard on LE (as a matter of law) thus lacks legal certainty. Roberts reinforces this conclusion when she states that,

> one problem with attempting to develop a general international law principle of legitimate expectations is that not all states recognize the doctrine and, even when they do, disputes exist over whether it protects procedural expectations only (given the general sovereign right of states to change their laws and policies) or whether it can also protect substantive expectations in narrow circumstances (such as when a specific representation is made to a narrow class). Some investment tribunals have recognized the limited nature of this doctrine, while others

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Investment Disputes) (Arbitrators: Tatiana de Maekelt, Francisco Rezek, Albert Jan van den Berg) at para.130. [*LG&E Energy*] *Paushok v Mongolia* (2011), Award of Jurisdiction and Liability (United Nations Commission on International Trade Law) (Arbitrators: Marc Lalonde, Horacio A. Grigera Naón, Brigitte Stern) at para.253, 254. *Eureko v Poland* (2005), Partial Award ((Arbitrators: Yves Fortier, Stephen Schwebel, Jerzy Rajski) at para. 235.

[349] *Ibid* at 176. (This approach adopts "[a] broader view of the scope of the doctrine of legitimate expectations is that it protects investors from prior unilateral statements made by the state […] the principle that justifies this view is that representations amount to official 'position' taken by a host government, even when they are not legally binding"). This approach is followed in *International Thunderbird* at para.129; *Duke Energy Electroquil Partners & Electroquil S.A. v Republic of Ecuador* (2008), Award ICSID Case No. ARB/04/19 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gabrielle Kaufmann-Kohler, Enrique Gómez Pinzón, Albert Jan van den Berg) at para.340.

[350] *Ibid* at 184. (the stability approach "holds the FET standard grants investors a freestanding entitlement to the stability of the legal arrangements under which the investment was made». This approach reaffirms that investors have a legally enforceable right for stable "legal framework"). Followed in *Occidental Exploration & Production Co. v Ecuador* (2004), Award LCIA Case No. UN3467 (London Court of International Arbitration Administered Case) (Arbitrators: Francisco Orrego Vicuna, Charles Brower, Patrick Barrera Sweeney) at para.27-32. *Sempra v Argentina* (2007), Award ICSID Case No. ARB/02/16, (International Centre for Settlement of Investment Disputes) (Arbitrators: Francisco Orrego Vicuña, Marc Lalonde, Sandra Morelli Rico) at para.184. [*Sempra v Argentina*]. *Enron v Argentina* (2007), Award ICSID Case No. ARB/01/3 (International Centre for Settlement of Investment Disputes) (Arbitrators: Francisco Orrego-Vicuña, Albert Jan van den Berg, Pierre-Yves Tschanz) at para.261 [*Enron*]

[351] *Ibid* at para.193-194. (the business plan approach the business plan approach is the most expansive and "may be based on the business plans of the investor if the host state knew or should have known of those plans […] business plans must be reasonable to justify a legitimate expectation. However, a business plan is not unreasonable simply because it is premised on assumptions about the way the state will act in the future"). Followed in *MTD v Chile* at para.163, *Bogdanov v Moldova* at para.17, *Walter Bau v Thailand* at para. 2.36.

> have tended to overdraw it and related doctrines, treating them as akin to freezing the regulatory framework at the time of investment.[352]

The threshold for establishing a breach of MST-FET under NAFTA is only one of many issues where ISA tribunals disagree. Some tribunals acknowledge LE to be an element of MST, while others suggest that LE goes far beyond *Neer* and cannot be treated as an element of MST. In some cases, tribunals have required a foreign investor to show that it relied on explicit specific promises or representations made by the host state, otherwise there is no violation of IIA.[353] In other cases, tribunals hold that LE requires states to maintain a stable and predictable legal environment for the duration of an investment covered by an IIA.[354] Thomas Wälde wrote an influential separate opinion, in which he argued that LE constituted "a self-standing subcategory and independent basis for a claim under the 'fair and equitable standard' as under article 1105 of the

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[352] Anthea Roberts, "Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States" (2010) 104:2 AJIL 179 at 214-215.

[353] *International Thunderbird* at para.147 ("[t]he concept of legitimate expectations relates, within the context of the NAFTA framework, to a situation where a contracting party's conduct creates reasonable and justifiable expectations on the part of an investor (or investment) to act in reliance on said conduct, such that a failure by the NAFTA party to honor those expectations could cause the investor (or investment) to suffer damages"). *International Thunderbird,* Separate Opinion of Thomas Wälde at paras. 27-30. ("a significant growth in the role and scope of the legitimate expectation principle, from an earlier function as a subsidiary interpretative principle to reinforce a particular interpretative approach chosen, to its current role as a self-standing subcategory and independent basis for a claim under the "fair and equitable standard" as under Art. 1105 of the NAFTA. This is possibly related to the fact that it provides a more supple way of providing a remedy appropriate to the particular situation as compared to the more drastic determination and remedy inherent in concept of regulatory expropriation. It is probably partly for these reasons that "legitimate expectation" has become for tribunals a preferred way of providing protection to claimants in situations where the tests for a "regulatory taking" appear too difficult, complex and too easily assailable for reliance on a measure of subjective judgment"). *Clayton Bilcon* at para.148. *Glamis Gold* at para. 766 (in Glamis Gold, the tribunal emphasized that any representation made with a purpose to induce investment maybe treated as an attempt to create LE).

[354] *Técnicas Medioambientales Tecmed S.A. v United Mexican States* (2003), Award ICSID Case No. ARB (AF)/00/2 (International Centre for Settlement of Investment Disputes) (Arbitrators: José Carlos Fernández Rosas, Carlos Bernal Verea, Horacio Grigera Naón) at 154. [*Tecmed*] Michele Potesta, "Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept" (2013) 28:1 ICSID Rev 88 at 99. ("Tecmed Award has been said to provide 'the most far-reaching exposition of the principle underlying the developing notion of legitimate expectations as applied to fair and equitable treatment in investment law").

NAFTA".[355] In *Thunderbird Gaming Corporation v Mexico*, the tribunal adopted Wälde's approach to FET:

> the concept of legitimate expectations relates, within the context of the NAFTA framework, to a situation where a contracting party's conduct creates reasonable and justifiable expectations on the part of an investor (or investment) to act in reliance on said conduct, such that a failure by the NAFTA party to honor those expectations could cause the investor (or investment) to suffer damages.[356]

Yet it remains a subject of debate whether MST includes LE as a subcategory and what actions of states may in principle create or frustrate investors' LE. In particular, some commentators indicate that there is a "lack of rigorous explanation of how and why an investor's expectations intersect with FET".[357] For example, Bandali explains that many tribunals consider a violation of LE not as a stand-alone basis for a claim, but only as a factor that the tribunal takes into consideration when it examines whether a state has violated the FET standard.[358] In *Mobil Investments v Canada*, the tribunal specified that to assess whether a state violated the FET-MST standard under article 1105 of NAFTA,

> it will be a relevant factor if the treatment is made against the background of clear and explicit representations made by or attributable to the NAFTA host State in order to induce the investment, and were, by reference to an objective standard, reasonably relied on by the investor, and were subsequently repudiated by the NAFTA host State.[359]

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[355] *International Thunderbird Gaming Corporation v Mexico*, NAFTA/UNCITRAL, Award, 26 January 2006, Separate Opinion Thomas Wälde at para. 27-30.
[356] *International Thunderbird* at para.147.
[357] Sabrina Bandali, "Understanding FET: The Case for Protecting Contract-based Legitimate Expectations" in Ian Laird et al, eds, *Investment Treaty Arbitration and International Law* (Juris Publishing, 2014) at 143.
[358] *Ibid*.
[359] *Mobil Investments Canada &Murphy Oil Corporation v Canada* (2012), Decision on Liability and on Principles of Quantum ICSID Case No. ARB (AF)/07/4 (Arbitrators: Hans van Houtte, Merit Janow, Philippe Sands) at para.152.

In *Mobil Investments,* decided under NAFTA, the tribunal explicitly denies that NAFTA article 1105 requires a state to maintain a stable legal and business environment. According to the tribunal, the FET standard:

> does not require a State to maintain a stable legal and business environment for investments, if this is intended to suggest that the rules governing an investment are not permitted to change, whether to a significant or modest extent [and nothing precludes a state] from changing the regulatory environment to take account of new policies and needs, even if some of those changes may have far-reaching consequences and effects, and even if they impose significant additional burdens on an investor.[360]

When FET is not linked to MST in IIAs, the threshold for violating the standard seems to be lower.[361] According to Van Harten, "some tribunals have adopted a broad reading of the standard without even mentioning […] the customarily deferential position in international law".[362] This has resulted in rather "far-reaching" conclusions on "state liability".[363] The tribunal in *Tecmed v Mexico* held for the first time that a state must maintain the stability and predictability of its legal framework.[364] Other tribunals followed *Tecmed*. For example, in *CMS v Argentina*, the tribunal did not make any reference to the *Neer* case, nor to the standard under customary international law, instead concluding that FET requires states to "maintain a stable framework for investments and maximum effective use of economic resources".[365] Ultimately, the tribunal held that "a stable legal and business environment is an essential element of fair and equitable

[360] *Ibid* at para.153.
[361] *UNCTAD 2012* at 87.
[362] Van Harten (2008), at 89.
[363] *Ibid*.
[364] *Tecmed* at para.154. LG*&E Energy v Argentina* (2007), Decision on Liability 46 ILM 40 (International Centre for Investment Disputes) (Arbitrators: Tatiana de Maekelt, Francisco Rezek, Albert Jan van den Berg) at para.125.
[365] *CMS Gas Transmission Company v The Republic of Argentina*, ICSID Case No. ARB/01/8 (2005) Award (Arbitrators: Francisco Orrego Vicuña, Marc Lalonde, Judge Francisco Rezek) at 274.

treatment".[366] Pedro Nikken, an arbitrator in the *Suez v Argentine* case, characterized LE in his dissenting opinion as follows:

> the development of the doctrine of legitimate expectations is the result of the interaction of the claims of investors and their acceptance by arbitral tribunals, buttressed by the presumed moral authority of the decided cases. I believe that the standard of fair and equitable treatment has been interpreted so broadly that it results in arbitral tribunals imposing upon the Parties obligations that do not arise in any way from the terms that the Parties themselves used to define their commitments.[367]

From a practical standpoint, the tribunals' approach means that any change in the regulatory environment that results in adverse effects against foreign investors can potentially constitute a violation of FET.[368] Miles concludes that this approach can impose "a heavy burden on host states".[369] She admits that while "the obligation to maintain a stable legal and business environment does not mean that regulation can never change, it does have a potential to constrain host state policy space".[370]

In *Philip Morris v Uruguay*, however, the tribunal held that a simple change in the legal and business environment of the state is not sufficient to establish a violation of

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[366] *Ibid*. See also *Occidental Exploration and Production Co v Republic of Ecuador* (2004), (UNCITRAL, Case No. UN3467), Final Award at para.183.

[367] *Suez, Sociedad General de Aguas de Barcelona, S.A.and Vivendi Universal, S.A. v Argentina* (2010), Separate Opinion of Arbitrator Pedro Nikken ICSID Case No. ARB/03/19 (International Centre for Settlement of Investment Disputes) (Arbitrators: José Carlos Fernández Rosas, Carlos Bernal Verea, Horacio Grigera Naón) at para. 27.

[368] Trevor Zeyl, "Charting the Wrong Course: The Doctrine of Legitimate Expectations in Investment Treaty Law" (2011) 49 Alberta L Rev 203–235. Jason Haynes, "The Evolving Nature of the Fair and Equitable Treatment (FET) Standard: Challenging Its Increasing Pervasiveness in Light of Developing Countries' Concerns – The Case for Regulatory Rebalancing" (2013) 14 JWIT 114–146. Christopher Campbell, "House of Cards: The Relevance of Legitimate Expectations under Fair and Equitable Treatment Provisions in Investment Treaty Law" (2013) 30 J Intl Arb 361–379.

[369] Kate Miles, *The Origins of International Investment Law: Empire, Environment and the Safeguarding of Capital* (Cambridge: Cambridge University Press, 2013) at 169.

[370] *Ibid*.

FET.[371] The tribunal required the foreign investor to establish that Uruguay acted in bad faith when it adopted a new regulatory policy.[372] Philip Morris could not show bad faith and the tribunal dismissed its claim.[373] The responses of states against potentially broad interpretations of the investment standards will be examined in detail in Chapter Three.

2.1.1.1.5 Umbrella Clause

An umbrella clause is a provision found in some IIAs that "requires a host State to respect any obligation that it has assumed with regard to a specific investment (e.g. obligations undertaken in an investment contract or concession agreement)".[374] In short, umbrella clauses permit the foreign investor to argue that the breach of a contract constitutes a violation of the IIA.[375] In other words, an umbrella clause is an "intriguing obligation to observe obligations".[376] For example, the *Angola-United Kingdom BIT* incorporates a typical example of an umbrella clause. It requires that "[e]ach Contracting Party shall observe any obligation it may have entered into with regard to investments of nationals or companies of the other Contracting Party".[377] The varied and vague wording

[371] *Philip Morris v Republic of Uruguay* (2016), Award, (International Centre for Settlement of Investment Disputes) (Piero Bernardini, Gary Born, James Crawford) [Philip Morris v Republic of Uruguay] at 399. Deyan Draguiev, "Bad Faith Conduct of States in Violation of the Fair and Equitable Treatment Standard in International Investment Law and Arbitration" (2014) 5 J Intl L Disp Settlement 273.
[372] *Ibid* at para.433.
[373] *Ibid* at para.433-435.
[374] UNCTAD, World Investment Report 2015: Reforming International Investment Governance (New York: United Nations, 2015) at 144. Christoph Schreuer, 'Travelling the BIT Route: Of Waiting Periods, Umbrella Clauses and Forks in The Road' (2004) 5 J World Investment & Trade 231. Katia Yannaca-Small , Interpretation of the Umbrella Clause in Investment Agreements, OECD Working Papers on International Investment (OECD Publishing, 2006) at 9.
[375] Peter Muchlinski, *Multinational Enterprises and the Law* (Oxford: Oxford University Press, 2007) at 688-689.
[376] Shotaro Hamamoto, "Parties to the 'Obligations' in the Obligations Observance ('Umbrella') Clause" (2015) 30:2 ICSID Rev 449 at 450.
[377] *Angola-United Kingdom BIT*, at art.2(2).

of the umbrella clauses in different IIAs have permitted tribunals to exercise broad discretion over the interpretation of these provisions, resulting in divergent outcomes.[378]

The controversy over interpretations of the umbrella clauses began with the SGS cases: *SGS v Pakistan* and *SGS v Phillipines*.[379] These cases involve similar facts and similar investment rights but at least one different party. The SGS arbitrations illustrate the second scenario. In the SGS arbitrations, the ISA tribunals had to examine "umbrella clause" to determine whether the violation of a contract claim constitutes a violation of a treaty claim under the applicable IIA. The arbitrations occurred under different BITs. The facts of the cases are similar; in each, foreign investors contracted with state agencies and there was a breach of contract by those agencies. In both cases, SGS argued that the violation of contract can be transmuted via the umbrella clause into a violation of the treaty. In *SGS v Pakistan*, the investment tribunal concluded that a violation of contract cannot amount to the violation of a treaty.[380] In *SGS v Philippines*, the tribunal arrived at a drastically different conclusion, that it is possible for a contract claim to become a treaty claim.[381]

Admittedly, the different wording of the umbrella clauses must be duly taken into consideration. This factor, however, does not apply to the SGS arbitrations. There, the tribunals referred to the different IIAs but the treaties adopted similarly broadly-worded umbrella clauses. In *SGS v Pakistan*, the tribunal analysed article 11 of the *Agreement*

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[378] Sureda (2012), at 2-3.

[379] *SGS Societe Generale de Surveillance S.A. v Islamic Republic of Pakistan* (2003), Decision on Objections to Jurisdiction, ICSID Case No. ARB/01/13 8 ICSID Reports 406 (International Centre for Settlement of Investment Disputes) (Arbitrators: Christopher Thomas, André Faurès, Florentino Feliciano) at para.163-168, 171. [*SGS v Pakistan*]. *SGS Societe Generale de Surveillance S.A. v Republic of the Philippines* (2004), Decision on Objections to Jurisdiction ICSID Case No. ARB/02/6, 8 ICSID Reports (International Centre for Settlement of Investment Disputes) (Arbitrators: Ahmed El-Kosheri, James Crawford, Antonio Crivellaro) at para.121. [*SGS v Philippines*].

[380] *SGS v Pakistan* at para.163-168, 171.

[381] *SGS v Philippines* at para.121.

between the Swiss Confederation and the Islamic Republic of Pakistan on the Promotion and Reciprocal Protection of Investments, which contains the following umbrella clause: "either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party".[382] In *SGS v Philippines*, the tribunal applied article X, para.2 of the Swiss Confederation-Republic of the Philippines *Agreement on the Promotion and Reciprocal Protection of Investments*, which stipulates as follows: "each Contracting Party shall observe any obligation it has assumed with regard to specific investments in its territory by Investors of the other Contracting Party".[383] Admittedly, the wording of the two IIAs is not identical, but both BITs establish broadly-worded umbrella clauses. Jan Ole Voss concludes that "[a[lthough the wordings of the umbrella clauses in both applicable BITs did not differ considerably, the two tribunals issued contradictory judgments on the issue of the effect of the clause".[384] As the tribunal in *SGS v Philippines* has acknowledged, "there is no doctrine of precedent in international law, if by precedent is meant a rule of the binding effect of a single decision. There is no hierarchy of international tribunals, and even if there were, there is no good reason for allowing the first tribunal in time to resolve issues for all later tribunals".[385] The tribunal indicated that in "a long term […] the development of a common legal opinion or *jurisprudence constante* to resolve the difficult legal questions discussed by the *SGS v Pakistan* Tribunal and also in the present

[382] *Agreement between the Swiss Confederation and the Islamic Republic of Pakistan on the Promotion and Reciprocal Protection of Investments,* at art.11.
[383] *The Swiss Confederation-Republic of the Philippines, Agreement on the Promotion and Reciprocal Protection of Investments* (1997), at art. X, para.2.
[384] Jan Ole Voss, *The Impact of Investment Treaties on Contracts Between Host States and Foreign Investors* (The Hague: Martinus Nijhoff Publishers, 2010) at 222.
[385] *SGS v Philippines* at para.97.

decision".[386] Most notably, the tribunals in *SGS v Philippines* and *SGS v Pakistan* fundamentally disagreed on the matters of interpretation of the umbrella clause.

Crawford identifies the following approaches that tribunals use to interpret and apply umbrella clauses.[387] One approach is to consider that umbrella clauses can fully internationalize the contract claims.[388] At the other extreme, the second approach adopts the perspective that a breach of contract cannot ever result in a violation of international law.[389] The third approach suggests that breaches of contracts can be a violation of international law, but a mere contract breach is not automatically a treaty breach, however, it can become a treaty breach "even in the presence of a forum selection clause that the investor had specifically and freely entered into, the tribunal can exercise jurisdiction over claims under the umbrella clause".[390] Crawford concludes that,

> reflect a level of dissent that one may regard as disturbing: the carpet looks very much as if different people have started from different ends without many common threads- a crazy quilt rather than a Persian rug.[391]

Yannaca-Small suggests that this situation has not changed much since 2008, when Crawford wrote his seminal article.[392] After examining two recent cases, *BIVAC BV v Paraguay*[393] and *SGS v Paraguay*,[394] Yannaca-Small observes that the facts in *BIVAC*

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[386] *Ibid*.
[387] James Crawford, "Treaty and Contract in Investment Arbitration" (2008) 24:3 Arb Intl 351.
[388] *Ibid*.
[389] *Ibid*.
[390] Darius Chan, The High-Water Mark of an Umbrella Clause: SGS v Paraguay (2012), online:<http://arbitrationblog.kluwerarbitration.com/2012/04/18/the-high-water-mark-of-an-umbrella-clause-sgs-v-paraguay/>
[391] James Crawford (2008), as cited in Katia Yannaca-Small, *Arbitration Under International Investment Agreements: A Guide to the Key Issues* (Oxford: Oxford University Press, 2010) at 483.
[392] Katia Yannaca-Small, "The Umbrella Clause Still in Search of One Identity: Case Comment BIVAC BV v Paraguay versus SGS v Paraguay" (2013) 28:2 ICSID Rev 307.
[393] *Bureau Veritas, Inspection, Valuation, Assessment and Control, BIVAC BV v Republic of Paraguay* (2009), Decision of the Tribunal on Objections to Jurisdiction ICSID Case No ARB/07/9 (International Centre for Settlement of Investment Disputes) (Arbitrators: Rolf Knieper, L Yves Fortier; Philippe Sands).

and *SGS* are "almost identical" and "[t]he difference in language between the clauses in the two BITs in these cases was not the basis for the very different outcomes".[395] Yet the tribunals came to opposite conclusions:

> the two Tribunals' different assessments of whether a generally worded exclusive choice of forum clause in a contract subsequent to a BIT implicitly waives the party's umbrella clause right to invoke treaty arbitration or whether the parties would need to explicitly waive such recourse to treaty arbitration. This is a matter on which the two BIT umbrella clauses in question are entirely silent.[396]

Pereira de Souza Fleury also concludes that even similarly worded umbrella clauses may result in different interpretative outcomes.[397] According to Pereira de Souza Fleury, the controversial interpretations of the umbrella clauses has led to a trend where states either avoid umbrella clauses altogether or significantly modify them to ensure narrow application.[398] For example, Norway's 2015 Draft Model BIT "completely avoid[s] the use of an umbrella clause […] the US eliminated the customary umbrella clause and instead, the model BIT provides a strict limitation of investment agreements (Article 1) whose breach may be submitted to arbitration".[399]

2.1.2 International and Municipal Law

International and municipal law norms constitute the second pillar of the legal structure of the investment regime. The choice of law provisions in IIAs provide for the rules that tribunals must use when they adjudicate the dispute. It is important to

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[394] *SGS Société Générale de Surveillance SA v Republic of Paraguay* (2012), Award ICSID Case No ARB/07/29 (International Centre for Settlement of Investment Disputes) (Arbitrators: Stanimir Alexandrov, Donald Francis Donovan, Pablo Garcia Mexia).
[395] Yannaca-Small (2010), at 312.
[396] *Ibid* at 313.
[397] Rau´l Pereira de Souza Fleury, "Umbrella Clauses: a Trend Towards its Elimination" (2015) 31 Arb Intl 679 at 680-683. To illustrate de Souza Fleury's point, the example of *SGS v Phillipines* and *SGS v Pakistan* will be in detail discussed in Chapter Five of this thesis.
[398] *Ibid* at 688.
[399] *Ibid*.

distinguish the choice of law issue from the content of law. Choice of law provisions prescribe the sources of law that tribunals must rely on when they adjudicate the merits of investment disputes. The content of law refers to the meaning of the norms and principles that those sources of law impose.

It is worth beginning with the choice of law provisions in the ICSID Convention and the the *United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards* (New York Convention), as both conventions are widely used in the investment regime.[400] Under these treaties, tribunals are bound by choice of law provisions in the applicable IIAs, or else the award may not be enforceable.[401] Article 42(1) of the ICSID Convention provides:

> [t]he Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable.[402]

Accordingly, states can agree on the sources of applicable law; if they have not done so, the default rule of the Convention is that the tribunal must apply the law of the contracting state party to the dispute along with the applicable rules of international law. If the applicable IIA specifies both municipal and international law in its choice of law provisions, the tribunals must apply both. Two important caveats must be considered. First, as Karton puts it, the treaty "does nothing to guide the tribunal's interpretation of

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[400] *United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards* 10 June 1958, 330 UNTS 38 (entered into force 7 June 1959). [New York Convention].
[401] Karton (2017), at 228. ("t]he ICSID Convention and New York Convention do not directly bind arbitrators or arbitrants; rather, they are directed at national courts, which may be called upon to rule on the enforceability of arbitration agreements and arbitration awards").
[402] ICSID Convention at art.42(1).

national or international law".[403] Second, while it is true that the tribunals must apply the indicated treaty sources of law, it is up to the tribunal to decide "which rules of international law are applicable". The provisions of the Convention do not prescribe *how* the arbitrators must apply and interpret law, although the IIA may impose limits on tribunals' interpretive discretion. Karton explains that,

> [i]t is a common misconception that ISA tribunals have broad inherent discretion with respect to the governing law, for example to interpret IIAs in a restrictive or extensive manner […] when states conclude an IIA, they have the power to determine not only the set of rules that tribunals must apply, but also the way in which tribunals must interpret them.[404]

Notably, both the ICSID Convention and the New York Convention "say next-to-nothing about the actual decisions made by arbitrators" and only regulate "the way in which arbitrators reach those decisions".[405] When IIAs contain choice of law provisions, like ICSID Convention article 42(1), they typically refer to international law and/or the municipal law of the disputing state. Nevertheless, "the relevant rules on the law applicable in investment disputes are far from uniform".[406] Schreuer identifies three types of the choice of law provisions in IIAs, those that (1) require the tribunals apply both municipal and international law, (2) incorporate reference only to "applicable rules of international law", and (3) refer exclusively to the municipal law of host state.[407]

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[403] Karton (2017), at 231.
[404] *Ibid* at 226-227.
[405] *Ibid* at 228.
[406] *Ibid* at 231.
[407] Christoph Schreuer, The Relevance of Public International Law in International Commercial Arbitration: Investment Disputes, online:<http://www.univie.ac.at/intlaw/pdf/csunpublpaper_1.pdf> at 8-10. [Unpublished paper].

DR-CAFTA is an example of an IIA that requires the tribunals to apply both municipal and international law. DR-CAFTA article 10.22 provides that the governing law of the dispute may be:

> specified in the pertinent investment agreement or investment authorization, or as the disputing parties may otherwise agree […] if the rules of law have not been specified or otherwise agreed: the law of the respondent, including its rules on the conflict of laws; and such rules of international law as may be applicable.[408]

The choice of law provision in DR-CAFTA provides that the parties can specify the governing law of the dispute and if the parties did not establish it, the tribunal must apply the law of the respondent and the applicable rules of international law.

NAFTA exemplifies the category of treaties that require tribunals to adjudicate the disputes according to the applicable rules of international law without any mandatory reference to municipal law. Pursuant to article 1131(1), "[a] Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law".[409] The *Japan-Israel BIT* refers specifically to "customary international law" in defining the general treatment that the state parties must accord foreign investors.[410]

Even when not specifically referred in the applicable IIA, municipal law also constitutes a necessary part of the legal structure of the investment regime. In *AAPL v Sri Lanka*, the tribunal acknowledged that,

> the Bilateral Investment Treaty is not a self-contained closed legal system limited to provide for substantive

[408] DR-CAFTA at art.10.22. 2(b).
[409] NAFTA, art.1131(1).
[410] *Agreement between Japan and the State of Israel for the Liberalization, Promotion and Protection of Investment* at art.4, online:< http://investmentpolicyhub.unctad.org/Download/TreatyFile/5575>.

> material rules of direct applicability, but it has to be envisaged within a wider juridical context in which rules from other sources are integrated through implied incorporation methods, or by direct reference to certain supplementary rules, whether of international law character or of domestic law nature.[411]

Accordingly, IIAs are not self-contained legal mechanisms but rather elements of a broader "juridical context", as desmonstrated by the fact that IIAs usually contain choice of law provisions.[412] The integration of international law and municipal law to govern investment disputes corresponds to their "hybrid" nature.[413] For example, in *MTD v Chile*, the dispute arose out of a foreign investment contract that the Chilean Foreign Investment Committee entered into with MTD.[414] Although the applicable IIA did not mandate application of municipal law, the annulment committee in the case recognized that some issues in the dispute required tribunals to apply both municipal and international law.[415] The committee reasoned that "the meaning of a Chilean contract is a matter of Chilean law; its implications in terms of an international law claim are a matter for international law".[416] Choice of law provisions thus may introduce the interaction of municipal and international law in investment disputes, but even if application of international and municipal law are not mandated by the treaty, issues may arise in the course of a dispute that require reference to either or both.

2.1.3 The Rules that Determine Arbitral Procedure

[411] *AAPL v Sri Lanka* at para. 21.
[412] Joshua Karton, "Choice of Law and Interpretive Authority in Investor-State Arbitration" (2017) 3:1 CJCCL 217.at 240. (discusses six types of choice of law provisions in IIAs).
[413] Douglas Zachary, "The Hybrid Foundations of Investment Treaty Arbitration" (2004) 74:1 BYIL 151. Ivar Alvik, "The Hybrid Nature of Investment Treaty Arbitration- Straddling the National/International Divide" in Christof Eriksen & Marius Emberland, eds, *The New International Law: An Anthropology* (Leiden: Martinus Nijhoff Publishers, 2010).
[414] *Ibid*.
[415] *Ibid*.
[416] *Ibid* at para.75.

The third pillar of legal structure of the investment regime is the rules that determine arbitral procedure.[417] The rules of arbitral procedure may determine a variety of issues that arise from the commencement of arbitration until (non)enforcement of the award. For example, the rules of arbitral procedure encompass (but are not limited to) the rules for constitution of the tribunal, the rules that determine the order of arbitral appointments, the timelines for the arbitration disputes, filing preliminary objections including when the claim lacks merit.[418] Such rules may be produced by international organizations, arbitration institutions or agreed by the parties themselves. IIAs can also incorporate rules that regulate procedural matters.

Arbitration institutions that administer arbitrations, such as the International Chamber of Commerce (ICC),[419] the Stockholm Chamber of Commerce (SCC),[420] the London Court of Arbitration (LCIA)[421] develop, maintain and update the arbitration rules that determine how the arbitration process is conducted. In the context of the investment regime, the ICSID Arbitration rules and the *United Nations Commission on International Trade Law* (UNCITRAL) are the most widely used.[422]

2.2 The Lifecycle of the Investment Arbitration Process

An overview of the "lifecycle" of the arbitration process helps to appreciate how ISA tribunals function and where early dismissal of frivolous or abuse of process claims

[417] Barton Legum, "An Overview of Procedure in an Investment Treaty Arbitration" in Katia Yannaca-Small, ed, *Arbitration Under International Investment Agreements: A Guide to the Key Issues* (Oxford: Oxford University Press, 2010) 91 at 93-96.
[418] *Ibid* at 796.
[419] *International Chamber of Commerce Arbitration Rules Rules*, at art. 29, Appendix V [ICC Rules].
[420] *Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce*, at art..2 [SCC Rules].
[421] *London Court of International Arbitration Arbitration Rules*, at art. 2.1. [LCIA Arbitration Rules].
[422] Christopher Dugan el al, *Investor-State Arbitration* (Oxford: Oxford University Press, 2011) at 80. Edward Kehoe & Paul Maslo, "Trends in International Investment Agreements, 2009/2010: Recent Steps in the Evolution of Bilateral Investment Treaties and the UNCITRAL Arbitration Rules" in Karl Sauvant, ed, *Yearbook on International Investment Law & Policy 2010-2011* (Oxford: Oxford University Press, 2012) at 39.

might fit within the overall procedure. In the context of investment arbitration, the first step in the lifecycle of an arbitration is the state's consent to arbitration, typically expressed in an IIA. For example, article 9(4) of the *Netherlands-Venezuela BIT* includes the following provision that expresses consent of the state-parties to participate in arbitration:

> [e]ach Contracting Party hereby gives its *unconditional consent* to the submission of disputes as referred to in Paragraph 1 of this Article to international arbitration in accordance with the provisions of this Article.[423]

The consent to arbitrate expressed in IIAs is paramount because arbitral jurisdiction is founded on consent. By expressing its consent to arbitrate in the IIA, the state makes an open offer that can be accepted by a foreign investor; the investor's consent is demonstrated when it launches a dispute against a state. The foreign investors can bring claims under the umbrella of the arbitration institutions or submit their claims for *ad hoc* arbitration, depending on what is provided in the dispute resolution provision of the applicable IIA.[424] The choice between institutional and *ad hoc* arbitration is a significant issue, which may have serious implications for the arbitration procedure and its outcome.[425] Arbitration institutions play a curious role in the investment regime.[426] At the risk of oversimplifying, it can be said that the institutions administer and facilitate the investment dispute resolution in return for a fee; they supervise the integrity of the

[423] *Agreement on Encouragement and Reciprocal Protection of Investments Between the Kingdom of the Netherlands and the Republic of Venezuela* (1991), at art.9(4). [terminated]
[424] Jan Paulsson, *The Freshfields Guide to Arbitration and ADR Clauses in International Contracts* (The Hague: Kluwer Law International, 1999) at 6-8.
[425] Gary Born, *International Arbitration and Forum Selection Agreements: Drafting and Enforcing* (The Hague: Kluwer Law International, 2010) at 59 -62. (Gary Born for general discussion on the value of institutional arbitration and a choice between ad hoc and institutional arbitration).
[426] Remy Gerbay, *The Functions of Arbitral Institutions* (The Hague: Kluwer Law International, 2016).

arbitration processes and supply procedural rules.[427] Beyond these formal functions, arbitration institutions can play an important role behind the scenes; for example, the ICSID Centre currently advances gender parity in arbitral appointments by exercising its residual power to appoint female candidates to serve as arbitrators.[428] The ICSID Centre is currently the most popular venue to resolve investment disputes that also has important historical significance.

It is worth noting briefly here that the Centre emerged as a result of the World Bank's efforts to create international machinery of arbitration for resolution of disputes between investors and states over foreign property in response to the UN calls to resolve the disputes over foreign property via peaceful means.[429] Aron Broches, a former President of the Bank, personally played a significant role in negotiating the creation of such machinery.[430] The outcome of the Bank's proposal became the *Convention on the Settlement of Investment Disputes Between States and Nationals of Other States* (ICSID) Convention[431] was opened for signature in 1965 and became operational in 1966.[432] It introduced a unique mechanism: investor-state arbitration.[433] What made the ICSID Convention especially innovative was that it introduced "private standing" ie granted

[427] Warwas (2016), at 355.
[428] Margaret Moses, *The Principles and Practice of International Commercial Arbitration* (Cambridge: Cambridge University Press, 2017) at 6.
[429] UN, *International Flow of Private Capital*, ECOSOC, Resolution of 21 April 1960, No XXIX (1960) at 3-4. [ECOSOC International Flow of Private Capital]. ECOSOC, The Promotions of the International Flow of Private Capital: Further Report by the Secretary General Document E/3492 (1961) at para.259.
[430] Transcript Interview with Aron Broches at 35.
[431] *Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (1965), 5 ILM 532, 575 UNTS 159. [ICSID Convention]. ICSID, Paper by the General Counsel (18 February 1963) SID/63-2 at para.7 and 8. ("The Bank's approach to the problem is more modest than the other two efforts. While they aim at improving the investment climate, the proposals submitted to the Executive Directors neither contemplate rules for the treatment of foreign property nor compulsory adjudication of disputes. They would make available to foreign investors and host governments facilities for conciliation or arbitration of disputes between them. Use of these facilities would be entirely voluntary").
[432] Parra (2012), at 9.
[433] Elihu Lauterpacht, (2009) at ix.

direct rights to individuals and companies (non-state actors) to bring claims against states without prior requirement to exhaust local remedies.[434] The decisions of ISA tribunals under ICSID are enforced in the territories of state parties.[435] For foreign investors to use the ICSID system, both home and host state must be the parties to the Convention. In 1987, the World Bank created the "Additional Facility" mechanism, under which authorized investors may bring claims in circumstances when only one of the host and home states is a party to the Convention.[436]

The ICSID Arbitration Centre was established under the Convention to provide administrative support in the resolution of investment disputes.[437] The ICSID Centre is an international organization "with full international legal personality".[438] The Centre is an arbitration institution that does not itself adjudicate disputes. Instead, the Centre provides administrative services for managing investment claims. The Centre has a residual power to appoint the arbitrators when parties are unwilling or unable to do so.[439]

In the case of *ad hoc* arbitration, the dispute will not be administered by the arbitration institutions unless the parties agreed otherwise. The rules for *ad hoc* arbitration may be agreed upon by the parties of the dispute, or the parties can rely on the

[434] *Ibid*.
[435] *Ibid*.
[436] Lucy Reed, Jan Paulsson & Nigel Blackaby, *Guide to ICSID Arbitration* (The Hague: Kluwer Law International, 2011) at 18.
[437] Gerbay (2016).
[438] ICSID Convention at art.18-24
[439] Parra (2012), at 248-252. (These functions are particularly important in the context of the investment regime. The ability of the centres to update the rules permit to react to the requests of users of the arbitration system. For example, ICSID Centre updated the rules in 2006 to incorporate the mechanism for the early dismissal of manifestly meritless claims (see Chapter 3 of this thesis for more detailed discussion). Other centres, for instance ICC, SCC and LCIA incorporated the emergency arbitrator for expedient review of claims under certain amount).

set of already developed rules by international organizations, such as the UNCITRAL Rules, which were drafted for use in *ad hoc* arbitrations.[440]

Both institutional and *ad hoc* arbitration require the ISA tribunal to be constituted. The tribunals are convened *ad hoc* for each dispute.[441] ISA tribunals are typically composed of three arbitrators, with one arbitrator appointed by the respondent state, another by an investor while the third, who acts as president of the tribunal, is appointed by the agreement of both parties.[442] In arbitral practice, it is common for the two party-appointed arbitrators to select the chair. In circumstances where an investor and a state cannot agree on a possible arbitrator, the administering institution or another third party may be empowered to act as an appointing authority.[443]

Arbitrators do not hold tenure and are appointed separately for each arbitration.[444] This structure of arbitral appointments is perceived to guarantee the impartiality of arbitral tribunal.[445] The impartiality of the arbitrators is particularly important given that "the arbitrators rule on the legality of legislative choices, the fairness of regulation, the content of property rights, and the appropriate distribution of the costs of regulation between business and society".[446]

ISA tribunals are constituted to adjudicate the dispute between an investor and a state on its merits. However, before deciding the dispute on its merits, the tribunal has to

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[440] August Reinisch &Loretta Malintoppi, "Methods of Dispute Resolution in Peter Muchlinski, Federico Ortino & Christoph Schreuer, eds, *The Oxford Handbook of International Investment Law* (Oxford: Oxford University Press, 2008) at 710.
[441] Dolzer & Schreuer (2012).
[442] *Ibid*.
[443] Dupont & Schultz (2016), at 5.
[444] Trinh Hai Yen, *The Interpretation of Investment Treaties* (The Hague: Martinus Nijhoff Publishers, 2014) at 23.
[445] Giorgetti (2014), at 9.
[446] Van Harten (2008), at 81.

determine whether it has jurisdiction to adjudicate a dispute.[447] The claim must satisfy the requirements in the applicable IIA that respects the scope of its application: the definition of investor (i.e. jurisdiction *ratione personae*) and the definition of investment (i.e. jurisdiction *ratione materiae*).[448]

In addition to the jurisdictional requirements, other preconditions may have to be satisfied before an investor can proceed with its claim in ISA. For example, some treaties require exhaustion of local remedies prior allowing an investor to submit a claim to ISA.[449] Others may incorporate a "cooling off period", a period of time that must elapse before an investor may launch an arbitration.[450] Cooling off periods may be combined with requirements for the investor to participate in consultations and negotiations with the host state government.[451] Treaties may also contain temporal restrictions for submitting the claim.[452] If an investor does not submit the claim within the limitation period imposed by the applicable IIA, it loses the opportunity to make its claim in ISA.[453]

IIAs usually incorporate broad definitions of investment and investor. The definition of investment often encompasses every kind of asset, including tangible and intangible assets.[454] The definition of investor establishes the nationality requirements

[447] UNCITRAL Arbitration Rules, at art.23 para.1.
[448] Dolzer & Schreuer (2012), at 126. Mariel Dimsey, *The Resolution of International Investment Disputes: Challenges and Solutions* (Eleven International Publishing, 2008) at 64.
[449] Jan Ole Voss, *The Impact of Investment Treaties on Contracts Between Host States and Foreign Investors* (The Hague: Martinus Nijhoff Publishers, 2010) at 286.
[450] Eric De Brabandere, "The Settlement of Investment Disputes" in the Energy Sector Eric De Brabandere & Tarcisio Gazzini,eds, *Foreign Investment in the Energy Sector: Balancing Private and Public Interests* (The Hague: Martinus Nijhoff Publishers, 2014) at 145.
[451] Giorgetti (2014), at 35. ("the 2012 U.S.Model BIT as an example, the model includes several conditions precedent to arbitration. First, in accordance with article 23, the investor has a requirement of «consultation and negotiations» […] second, article 24(2) includes a ninety -day notice period before an investor may submit a claim to arbitration […] third,, in accordance with article 24(3), the investor must abide by a six-month cooling off period").
[452] *Ibid*.
[453] Vandevelde (2009), at 602.
[454] *Ibid*.

that individuals or companies must satisfy to get access to the investment protection under the applicable IIA.[455] Typically, IIAs require the investor to be a national of a state that has ratified the IIA, other than the state where it made the investment (the host state).[456]

After the tribunal determines that it has jurisdiction by addressing these requirements, the tribunal will proceed to adjudicating on the merits, which are determined in accordance with the applicable legal rules. IIAs and the arbitration rules do not always determine what rules exactly are applicable in the particular dispute. For example, article 35 (1) of the UNCITRAL Arbitration Rules stipulates that "[t]he arbitral tribunal shall apply the rules of law designated by the parties as applicable to the substance of the disputes".[457] In the circumstances, when the parties failed to produce such a designation, the tribunal will "apply the law which it determines to be appropriate".[458] The ICSID Convention contains similar provision in article 42 (1) that requires the ISA tribunal to adjudicate the dispute "in accordance with such rules of law as may be agreed by the parties".[459] The decisions of other tribunals formally have no precedential value.[460] However, the tribunals appear to refer to each other's decisions in a manner approximating *jurisprudence constante*.[461] In other words, while never binding

[455] UNCTAD, World Investment Report 2016: Investor Nationality: Policy Challenges (New York: United Nations, 2016) at 124-126.
[456] *Ibid*.
[457] UNCITRAL Arbitration Rules, at 35(1)
[458] *Ibid*.
[459] ICSID Convention at art.41(1).
[460] Andrea Bjorklund, "The Promise and Peril of Arbitral Precedent: The Case of Amici Curiae" 34 (2010) Association Suisse de L'arbitrage, Special Series 165 at 165. Black's Law Dictionary (6thedn, West Pub.Co., St. Paul, Minn., 1990) at 1406 *(stare decises* transplates as "to adhere to precedents, and not to unsettle things which are established").
[461] Andrea Bjorklund, "Investment Treaty Arbitral Decisions as Jurisprudence Constante" in Colin Picker, Isabella D Bunn & Douglas Arner, eds, *International Economic Law: The State and Future of the Discipline* (London: Bloomsbury Publishing, 2008) at 273.

on one another, different arbitral decisions may nonetheless have persuasive value to future tribunals, which helps to make their determinations more consistent.

The tribunal must render an award in writing and include a statement of facts, reasons for its decision on each question before it, and its decision on the costs.[462] It is worth noting that the remedies available under ISA are limited to awards of money damages.[463] The tribunals cannot compel a state-party to change its national laws; however in some recent cases, the ISA tribunals adopted measures that directly restrained states' actions.[464] The decision of the tribunal is final and binding upon the participants of the dispute.[465] After the award is rendered, the parties can seek enforcement of the award under the ICSID Convention or under the the New-York Convention.[466] The first applies to all investor-state arbitrations conducted under the auspices of ICSID, while the New York Convention applies to nearly all investor-state arbitrations conducted *ad hoc* or administered by other international arbitral institutions.[467]

For awards governed by the New York Convention, it stipulates that states must "recognize arbitral awards as binding".[468] McLaughlin and Genevro observe that states must "enforce the awards according to the State's own rules of procedure", another

[462] ICSID Arbitration Rules at Rule 47 (1) (g),(h),(i), (j). ICSID Convention at art.52 (1) (e). Vladimir Balas, "Review of Awards" in Peter Muchlinski, Federico Ortino & Christoph Schreuer,eds. *The Oxford Handbook of International Investment Law* (Oxford: Oxford University Press, 2008) at 1147.
[463]Sarah Farnham, "Claim Suspension and Issue Preclusion in Multiparty Investment Disputes: The Need for Autonomous, International Principles" in Ian Laird, Sabahi, Frédéric Sourgens & Todd Weiler, *Investment Treaty Arbitration and International Law* (Juris Publishing, 2015) at 225.
[464] *Found Alghanim & Sons Co. for General Trading & Contracting, W.L.L. and Mr. Foud Mohammed Thynyan Alghanim v Jordan* (2017), Award ICSID Case No. ARB/13/38 (International Centre for Settlement of Investment Disputes) (Arbitrators: L. Yves Fortier, Marcelo Kohen, Campbell Alan Mclachlan).(The majority of the tribunal requires the respondent to "refrain from prosecuting the Jordanian proceedings" and "otherwise desist from enforcing the Taxation Measures" against claimants).
[465] Laird, Sabahi, Sourgens & Weiler (2015), at 225.
[466] New York Convention at art.III. ICSID Convention at art.53-55.
[467] Karton (2017), at 228.
[468] Ripinsky & Williams (2008), (see generally on damages).

avenue where municipal law interacts with the international investment regime.[469] Article V of the Convention establishes an exhaustive list of grounds under which the national courts can refuse enforcement of arbitral awards.[470] The New York Convention, article V(1) establishes five procedural grounds for refusal enforcement of award, including that "[t]he party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case".[471] The two grounds for non-enforcement under Article V(2)—non-arbitrability and contradiction of public policy—can pertain to the substantive aspects of an award. In practice, however, courts would not invoke either of the grounds in Article V (2) simply because a tribunal misapplied the governing substantive law.

Refusal to enforce is possible in principle on substantive grounds, when "[t]he recognition or enforcement of the award would be contrary to the public policy of that country".[472] Non-enforcement on public policy grounds is only permissible in narrow circumstances,[473] as is continually repeated by courts in a variety of jusrisdictions.[474] Although a few national courts have expansively interpreted the public policy exception to enforcement,[475] "the grounds for refusal of enforcement are generally jurisdictional and procedural".[476] For this reason, arbitrators genuinely risk non-enforcement of an award on procedural grounds, but experience very limited oversight by national courts on

[469] Joseph McLaughlin & Laurie Genevro, "Enforcement of Arbitral Awards under the New York Convention - Practice in U.S. Courts" (1986) 3 Intl Tax & Bus L 249 at 252.
[470] New York Convention at art V.
[471] *Ibid* at art. V (1) (b).
[472] New York Convention at art.5(2)(b). The public policy ground invoked much criticism as a possible loophole for rendering awards not enforceable. Joel Junker, "The Public Policy Defense to Recognition and Enforcement of Foreign Arbitral Awards" (1977) 7 Cal W Intl LJ 228.
[473] McLaughlin & Genevro (1986), at 262-265.
[474] *Ibid*.
[475] Jenkins & Stebbings (2006), at 301-302.
[476] Karton (2017), at 228.

substantive legal grounds.[477] Since non-enforcement of an award can have reputational consequences for the members of the tribunal, arbitrators will exercise great caution to ensure that both parties have an opportunity to fully present their cases.

By contrast, ICSID awards do not require separate *exequatur.* According to article 53 (1) of the ICSID Convention, the award is "binding on the parties and shall not be subject to any appeal or to any other remedy except those provided for in this Convention".[478] State parties recognize and enforce an "award within its territories as if it were a final judgment of a court in that State".[479] In theory, the refusal of a state to comply with the terms of the ICSID Convention on enforcement can result in two types of sanctions:

> [t]he first is the exercise by the investor's national State of its right under customary international law to give diplomatic protection or to bring an international claim […] The second sanction is a statutory proceeding under Article 64 of the Convention, which provides for the referral to the International Court of Justice for disputes between Contracting States.[480]

In practice, refusal to enforce an award can result in diplomatic pressure. For example, states can suspend the trade benefits of countries that fail to enforce the ICSID awards.[481] When Argentina refused to enforce a number of awards rendered against it by the ISA tribunals in the aftermath of the 2008 financial crises, the Office of the US Trade Representative suspended the Argentina's status as a beneficiary developing country.[482]

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[477] *Ibid*.
[478] ICSID Convention at art.53 (1).
[479] ICSID Convention at art.54(1).
[480] Aron Broches, "Awards Rendered Pursuant to the ICSID Convention: Binding Force, Finality, Recognition, Enforcement, Execution" (1987) 2:2 ICSID Rev 287 at 294.
[481] Charles Rosenberg, "The Intersection of International Trade and International Arbitration: The Use of Trade Benefits to Secure Compliance with Arbitral Awards" (2013) 44 Geo J Intl L 503 at 520,530.
[482] *Ibid* at 524.

Rosenberg observed that suspension from a trade benefits scheme can serve as a "stick" to guarantee enforcement of ISA awards.[483]

However, the ICSID Convention provides an architecture that makes it almost impossible for states to refuse enforcement of the award. ICSID awards "inherit a twofold stability" that is guaranteed by two factors "firstly, they are not subject to any means of recourse before national courts of ICSID Member countries. […] Secondly, ICSID awards are not subject to *exequatur* proceedings and thus an effective enforcement is guaranteed".[484] Accordingly, the only option to prevent enforcement of the award is via the annulment procedure established by the ICSID Convention.

Article 52 ICSID Convention permits the annulment of an arbitral award.[485] The annulment can be accomplished by an annulment committee convened specifically for the dispute; the national or international courts cannot conduct the annulment procedure under the ICSID Convention.[486] Fundamentally, the ICSID annulment procedure fulfils the role of a controlling mechanism to avoid "arbitrary awards" that are manifestly "ultra vires".[487] The party to the dispute can file an application addressed to the Secretary General that requests the annulment of the decision.[488] The rules provide for limited grounds for the annulment, including that the Tribunal "was not properly constituted; manifestly exceeded its powers; had a member who was corrupt; seriously departed from

[483] *Ibid* at 525-526.
[484] Ole Voss (2010), at 63.
[485] ICSID Convention at art.52. Arbitration Rules at 50, 52-55.
[486] Antonio Parra, *The History of ICSID* (Oxford: Oxford University Press, 2012) at 187.
[487] Ahmed Sadek El-Kosheri, "ICSID Arbitration and Developing Countries" (1993) 8:1 ICSID Rev 104 at 113.
[488] ICSID Arbitration Rules, at Rule 50 (1).

a fundamental rule of procedure; or made an award but failed to state the reasons on which it was based".[489]

The Secretary General of ICSID accepts the application or refuses to register it.[490] Only claims that the Secretary General finds to be manifestly outside of the jurisdiction of the Centre may be refused.[491] The parties must be informed about the refusal of registration.[492] After the Secretary General registers the application for annulment, the Secretary General must request "the Chairman of the World Bank's Administrative Council to appoint the *ad hoc* committee".[493] The Committee is composed of three members and can annul the award fully or in part.[494] The ICSID Annulment procedure is unique to the investment regime.[495]

2.3 Why Do States Sign Up for International Investment Agreements?

States' motives for joining ICSID and concluding IIAs deserve scrutiny. The lack of conclusive evidence means there is no single straightforward answer to the question of why states sign up for ISA and IIAs. The literature suggests two categories of possible reasons: "rational choice" and "irrationality trap". The argument for "rational choice" proceeds as follows: states pursue ISA and IIAs for diplomatic, ideological or economic reasons. "Irrational trap" theories postulate that states sign up for ISA and IIAs without fully understanding the long-term implications of these legal instruments. On the BBC

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[489] *Ibid* at Rule 50 (3)(iii).
[490] *Ibid* at Rule 50 (2) and (3). ICSID Convention art.28(3) and 36(3).
[491] Parra (2012), at 158-160. (Parra explains that the refusals to register the claims were issued because the Centre began to "receive requests made, not on the basis of straightforward arbitration rules in investment contracts, but instead relying on consents said to be embodied in investment laws of the host state").
[492] ICSID Arbitration Rules, at Rule 50 (2) and (3). ICSID Convention art.28(3) and 36(3).
[493] ICSID Arbitration Rules, at Rule 52.
[494] *Ibid* at Rule 55.
[495] Irmgard Marboe, "ICSID Annulment Decisions: Three Generations Revisited" Christina Binder ed, *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (Oxford: Oxford University Press, 2009) at 200.

Radio Program "Company v Country", Poulsen discussed his interview with Makhdoom Ali Khan, a former Attorney General of Pakistan, in which Khan said that in 2001, when he received a notice that Pakistan was sued by the Swiss investor under the *Pakistan-Switzerland BIT*, he did not have "a clue" what this instrument was and what the claim meant for his country.[496] Reportedly, a number of other representatives from developing states expressed similar views. For example, "one East European negotiator explained, "[n]egotiators really didn't know that the treaties had any bite in practice. They were neither aware of the costs or the fact that it could lead to arbitration".[497]

While it is entirely possible that some countries fell into such a "trap", this account seems rather simplistic. Multiple factors may be relevant to understand why states signed up for IIAs and ISA Before examining these factors, it is important to note that to fully understand why states signed up for IIAs, it is important not only to account for multiple factors but also remain context-specific. Different states could be influenced by different factors, and no blanket approach to this issue can explain fully why states signed up for IIAs and ISA.

The adoption of IIAs "w[as] premised on a Grand Bargain: a promise of protection of capital in return for the prospect of more capital in the future".[498] Kaushal identifies the two premises of the "grand bargain" of IIAs.[499] She underscores the two assumptions behind the emergence and proliferation of the treaties: "[f]irst, BITs will lead to increased FDI flows; and second, increased FDI flows will lead to economic

[496] "Company v Country", BBC Radio at 8:20-9:00mm.
[497] Lauge Skovgaard Poulsen & Emma Aisbett, "When the Claim Hits: Bilateral Investment Treaties and Bounded Rational Learning" (2013) 65:2 World Politics 273 at 283. (also report that the representatives of Lybia, Thailand, South Africa and Dominican Republic expressed similar views).
[498] Jeswald Salacuse & Nicholas Sullivan, "Do BITs Really Work: An Evaluation of Bilateral Investment Treaties and Their Grand Bargain" (2005) 46 Harv Intl LJ 67 at 77.
[499] Kaushal (2009), at 508.

development".[500] Salacuse suggests that "nations create and join regimes out of a desire to reduce the relative costs of desired transactions [...] states have been led to sign investment treaties" to "reduce the perceived risks associated with investing in their territories and thereby lower their costs of obtaining needed foreign capital and technology".[501] Possibly some states genuinely believed that the adoption of IIAs would result in more significant capital inflows.[502] The most recent empirical evidence acquired by Taylor St John, however, debunks this theory at least in relation to developed states.[503] According to St John, in their internal correspondence, British and American public officials who were responsible for developing and negotiating early BITs acknowledged that investment treaties would *not* facilitate investment.[504] Similarly, the British officials recognized that the ICSID Centre will not result in "any additional stimulus" to "new" foreign investments.[505]

A second possible explanation is offered by Poulsen and Aisbett. They attribute the proliferation of IIAs to the phenomenon of diplomatic bureaucracy.[506] Poulsen and Aisbett argue that diplomats from developing states often negotiated IIAs out of personal self-interest. The treaty was "hard" evidence to justify trips abroad and for them to move up in the diplomatic hierarchy.[507] Of course, diplomats play an important role in treaty negotiations. However, the view that diplomats were solely responsible for the

[500] *Ibid*.
[501] Salacuse (2010), at 435
[502] Antony VanDuzer, Penelope Simons & Graham Mayeda, *Integrating Sustainable Development Into International Investment Agreements: A Guide for Developing Country Negotiators* (London: Commonwealth Secretariat, 2013) at 6-7.
[503] St John (2018), at 218. Arbitration Station, The History of ISDS, (27 February 2018) at 7:20-18:30mm. (Taylor St John discusses history of ISA in the interview).
[504] *Ibid*.
[505] *Ibid*.
[506] Lauge Poulsen & Emma Aisbett, "Diplomats Want Treaties: Diplomatic Agendas and Perks in the Investment Regime" (2016) 7 :1 J Int Disp Settlement 72.
[507] *Ibid*.

proliferation of IIAs is far too reductive. A narrow focus on the role of diplomats neglects the internal dynamics of how national governments develop foreign investment policy. Diplomats are only one constituency among many— and not even a particularly powerful one–that participates in the process of investment policy development.

Dupont and Schultz explain that states' reasons for joining IIAs and ISA may also have shifted over the years. In the early period i.e. "until the mid-to-late nineties, investment arbitration was used to a large extent both as a post-colonial instrument to strengthen the economic interests of the North and as a means to impose the rule of law in non-democratic states with a weak law and order tradition".[508] After this period international involvement shifted to upholding the "international rule of law".[509]

Whatever the precise reasons that motivated states to sign IIAs, they must all be understood in their specific political and historical contexts, which go beyond the ideology of post-war market liberalization. Karl Polany's work the *Great Transformation* helps untangle the philosophical underpinnings of state choices to conclude IIAs.[510] Polany's argument is essentially that markets constitute an embedded element of social systems.[511] From this viewpoint, any insulation of economic systems from social influences results in societal destruction.

[508] Cedric Dupont & Thomas Schultz, "Do Hard Economic Times Lead to International Legal Disputes? The Case of Investment Arbitration" (2013) 19:4 Swiss Political Science Review 564 at 565.
[509] Cedric Dupont, Thomas Schultz & Merih Angin, "Political Risk and Investment Arbitration: An Empirical Study" (2016) 7 Journal of International Dispute Settlement, 136 at 138. Thomas Schultz & Cedric Dupont, "Investment Arbitration: Promoting the Rule of Law or Overempowering Investors? A Quantitative Empirical Study" (2014) 25:4 Eur J Intl L 1147.
[510] Karl Polanyi, *The Great Transformation. The Political and Economic Origins of Our Time* (Boston: Beacon Press, 2001).
[511] *Ibid*.

Following the Second World War, trade and investment liberalization were seen as a panacea for "economic ills".[512] The International Monetary Fund (IMF) and the World Bank assisted in steering developing states into adopting particular types of policies that focused on privatization and diminution of state participation in the market economy.[513] In particular, the IMF and the World Bank agitated for elimination of national barriers that inhibited the flow of private capital, especially by giving loans only if the debtor-states follow the market liberalization programs.[514]

Martii Koskenniemi observes that, during this time, "domestic priorities and political choices have been routinely attacked as trade barriers and subsidies".[515] Schneiderman gives the example that Argentina followed the directives of the IMF and the World Bank in modernizing its economy, which resulted in "one of the most dramatic economic collapses in recent history".[516] These events led to a proliferation of the investment claims against Argentina, many of which resulted in substantial awards against the country.[517] Ideologically, adoption of IIAs was one tile in the mosaic of a broader trend towards investment and trade liberalization. IIAs and ISA were perceived as mechanisms to safeguard foreign investors from the non-business risks. In Polany's terms, IIAs and ISA *de facto* insulated foreign investors from social influences of the

[512] *Ibid*.
[513] *Ibid*.
[514] David Schneiderman, *Resisting Economic Globalization: Critical Theory and International Investment Law* (London: Palgrave Macmillan, 2013) at 50. (Privatization was one of the conditions to receive a loan. Shneiderman argued that Argentina's crises occurred because Argentina followed the liberalization program of the global institutions)
[515] Martti Koskenniemi, "Book Review Essay.It's not the Cases, It's the System M. Sornarajah, Resistance and Change in the International Law on Foreign Investment" (2017) 18 Journal of World Investment & Trade 343 at 344
[516] Schneiderman (2013), at 50.
[517] Roland Kläger, *Fair and Equitable Treatment' in International Investment Law* (Cambrdige: Cambridge University Press, 2011) at 79.

markets in which they invested, binding states under universal international standards set by developed states and promoted by the World Bank and IMF.

Whether or not states had full understanding of the implications of IIAs together with ISA remains an open question.[518] Van Harten suggests that some states were misinformed of the potential implications of entering the investment regime.[519] In particular, states may have failed to fully appreciate future implications of IIAs in constraining their policy options on the domestic level.[520]

The reasons why states participate in IIAs may be useful to summarize for future reference. In the aftermath of the Second World War, foreign direct investment (FDI) was marketed as the most effective path for economic development.[521] Accordingly, states concluded IIAs in the hope that such treaties would help them to attract more capital. It is possible that diplomatic bureaucracy and the officials of the international organizations contributed to reassuring states that IIAs could be a key for economic prosperity. In the context of the post Second World War environment, peaceful cooperation and dispute resolution of disputes have become buzzwords. Here, the general commitment of the international community[522] to peaceful dispute resolution also may

[518] Peter Muchlinski, "Corporations and the Uses of Law: International Investment Arbitration as a "Multilateral Legal Order"" 4:1 (2011) Oñati Socio-Legal Series at 5. Republic of South Africa 2009 Bilateral Investment Treaty Policy Framework Review Government Position Paper, Department of Trade and Industry, Pretoria.
[519] Gus Van Harten, "Five Justifications for Investment Treaties: A Critical Discussion" (2010) 2:1 Trade, Law & Development 19.
[520] *Ibid*. Parra (2012), at 238.As cited in Parra U.N. Global Compact: Corporate Citizenship in the World Economy, available at http://www.unglobalcompact.org. David Vogel, *The Market for Virtue: The Potential and Limits of Corporate Social Responsibility* (New York: Brookings Institution Press, 2007) at 156-158. (John Ruggie, the author of the corporate social responsibility (CSR) initiative and the Special Representative on Business and Human Rights, was among high-profile critics who warned that IIAs "could unduly constrain governments from introducing much needed reforms, including those concerning human rights").
[521] ECOSOC International Flow of Private Capital at 3-4. St John (2018), at 61.
[522] The notion of "international community" is subject of criticisms. Monica Hakimi, "Constructing an International Community" (2017) 111:2 AJIL 317 at 319-320.

have contributed to the popularity of IIAs and ISA. Finally, states may have underestimated the implications of joining IIAs and ISA. In other words, states knew that by signing the treaties they would give up some degree of sovereignty, but never fully appreciated how much of their sovereign policy space would be constrained by ISA and IIAs.

2.4 Concluding Remarks

Chapter Two provides an overview and background information on the investment regime as a *sui generis* legal system, subject to its own tensions and controversies. As Roberts observes, "[a] key problem in the investment treaty field is that the balance of power between treaty parties and tribunals concerning the authority to interpret investment treaties is askew".[523] In practice, this asymmetry produces tension between states and tribunals when tribunals' interpretations of IIAs diverge from the states' expectations on the scope of their investment obligations under IIAs.

In theory, states delegated to tribunals the authority to interpret IIAs as they see fit in the context of the circumstances of particular case.[524] In practice, the broad interpretations by tribunals result in states' attempts to restrain the arbitral interpretative power. The most prominent example discussed in this chapter is NAFTA MST-FET linkage introduced by the NAFTA FTC after the treaty entered into force. The *Pope & Talbot* tribunal "viewed the interpretation as an illegitimate attempt to amend the treaty

[523] Anthea Roberts, "Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States" (2010) 104:2 AJIL 179 at 179.
[524] Karen Alter, "Agents or Trustees? International Courts in their Political Context" (2008) 14:1 Eur J Intl L 33 at 35. (submits that "international Relations scholars are right that states are concerned about IC behaving in ways they did not intend, and do not want").

retroactively in order to interfere with an ongoing case".[525] This example illustrates tension that persists in the investment regime.[526]

As has been discussed in this Chapter, the investment standards in IIAs are often broadly formulated, so that they perpetuate and may even exacerbate the ambiguity and uncertainty of the scope of states' obligations towards foreign investors under IIAs. The decentralized nature of ISA, in particular the lack of hierarchy or formal precedent under independent, *ad hoc* tribunals, structurally reinforces this phenomenon. In addition, it induces greater risk of inconsistent interpretations.[527] As Schreuer explains, the *ad hoc*, decentralized nature of ISA "makes it considerably more difficult to develop a consistent case law than in a permanent judicial institution".[528] Inconsistent interpretations can persist because different tribunals can simultaneously adjudicate investment disputes that engage similar investment standards or even arise from the same state actions. Such tribunals would have no chance to examine each other's decisions.[529] Together, these systemic features imbue the system with uncertainty of legal standards, an issue that Chapter Five reviews in a greater detail.

[525] Roberts (2010), at 180.
[526] As Roberts concludes the states and the tribunals can still engage in the "interpretative dialogue". I agree with such possibility but both states and tribunals have to work out on what terms and under what framework such dialogue can exist in principle.
[527] Christoph Schreuer, "Diversity And Harmonization Of Treaty Interpretation In Investment Arbitration" in Malgosia Fitzmaurice, Olufemi Elias, Panos Merkouris, *Treaty Interpretation and the Vienna Convention on the Law of Treaties: 30 Years* (The Hague: Brill, 2010) at 145.
[528] *Ibid* at 129.
[529] *Ibid* at 146.

Chapter 3

Legitimacy Deficits in International Investment Regime

This Chapter maps the mechanisms for the dismissal of frivolous and abuse of process claims, viewed within the broader context of reforms to the investment regime in response to its perceived legitimacy deficits.[530] "Legitimacy" is an elusive term that can have different meanings depending on the context. For the purposes of this thesis, legitimacy is broadly understood in Max Weber's terms.[531] Participants in a legitimate system accept its authority because they *trust* the institution and *believe* that the exercise of such authority is just.[532] In the context of the investment regime, ISA tribunals adjudicate disputes, but they also contribute "to stabilizing and generating normative expectations in transborder social relations and therefore exercise transnational authority that demands justification in order to be considered as legitimate".[533] Hence, the deficit of trust may lead to noncompliance with tribunals' decisions. This eventually may lead to the collapse of the regime.[534] Legitimacy here is also a framing device to discuss the

[530] Leon Trakman, "The ICSID Under Siege" (2012) 45 Cornell Intl LJ 603.
[531] Wolfgang Mommsen, *The Political and Social Theory of Max Weber: Collected Essays* (Chicago: University of Chicago Press, 1992) at 21 (considering the Max Weber's sociological account of legitimacy).
[532] *Ibid*.
[533] Stephan Schill, "Conceptions of Legitimacy of International Arbitration" in David Caron et al, eds, *Practising Virtue: Inside International Arbitration* (Oxford: Oxford University, Press 2015) at 106. Stephan Schill, "Developing a Framework for the Legitimacy of International Arbitration" in Albert Jan van den Berg, ed, *Legitimacy: Myths, Realities, Challenges* (The Hague: Kluwer International, 2015). Charles Brower & Stephan Schill, "Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?" (2009) 9:2 Chicago J Intl L 471. Frank Garcia et al, "Reforming the International Investment Regime: Lessons from International Trade Law" (2015) 18:4 J Intl Econ L 861 at 862, 876. (explain that the treaties and the tribunals ""allocate rights, privileges, and burdens between investors and host states").
[534] Julie Maupin, "Public and Private in International Investment Law: An Integrated Systems Approach" (2014) 54 Va J Intl L 367 at 379. Stephan Schill, "Enhancing International Investment Law's Legitimacy: Conceptual and Methodological Foundations of a New Public Law Approach" (2011) 52 Va J Intl L 57 at 64.

ongoing criticisms of the investment regime. Frivolous and abuse of process claims undermine trust in the system, particularly when tribunals cannot efficiently dispose of such claims early in the process, and respondent governments have to defend those claims in full-fledged arbitration proceedings.

This chapter has two goals. First, it provides the literature overview to introduce the reader to the current discourse on the international investment regime. Second, it maps a broad picture of how the investment regime changes. The emerging mechanisms for the dismissal of frivolous and abuse of process claims constitute only one of the elements in this puzzle of changes. The actions and reactions of the regime's key participants shape legal norms and introduce novel legal mechanisms in a decentralized fashion. As a result, the norms in the regime "are processes, works in progress rather than finished products".[535] The existing mechanisms for the curtailment of frivolous and abuse of process claims are not an exception; they require critical assessment in the systemic context of the investment regime and in full view of the regime's legitimacy deficits.

Structurally this chapter proceeds in two steps. First, it examines the legitimacy deficits of the investment regime as described in the investment arbitration scholarship. To provide a structural framework for the in-depth conversation on legitimacy deficits, it employs Jose Alvarez's vertical, horizontal, ideological and rule of law rubrics.[536] Alvarez's categorization is helpful to map the reasons for backlash against the investment regime.

[535] Mona Krook & Jacqui True, "Rethinking the Life Cycles of International Norms: the United Nations and the Global Promotion of Gender Equality" (2012) 18:1 European Journal of International Relations 104 at 104.
[536] Alvarez (2011), at 75.

Second, this chapter addresses the responses of states to these legitimacy deficits. It employs Hirshman's theory of "exit", "voice" and "loyalty" to conceptualize state responses.[537] According to this theory members of organizations select among these options when building their relationships within organizations. In particular, members may exit the organization i.e. terminate their membership, or they potentially can stay loyal to the organization and voice their concerns to facilitate change. Hirschman's framework of "exit", "voice" and "loyalty" complements the political system lens. As has been mentioned, the lens of political system implies that participants in the investment regime contribute to the regime's evolution by means of actions and reactions, inputs, outputs, and outcomes. State actions that contribute to shaping and developing the investment regime can be understood by application of Hirschman's rubric. The application of Hirshman's theory to the investment regime is not novel and has proven useful for considering state responses to legitimacy deficits in the investment regime. [538]

3.1 Legitimacy Deficits in the Investment Regime

This section structures its exploration of legitimacy deficits of the investment regime through Alvarez's four categories of legitimacy critiques: vertical critiques, horizontal critiques, rule of law critiques and ideological critiques. Categorizing legitimacy deficits is important for three reasons. First, it examines the flaws within the regime in a structured way to provide a broader picture of the problems persisting within the investment regime. This is important to show that the system cannot be reformed through "quick fixes", since many concerns are structural.

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[537] Albert Hirschman, *Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States* (Cambridge: Harvard University Press, 1970).

[538] For example, Anna Katselas, "Exit, Voice, and Loyalty in Investment Treaty Arbitration" in Shaheeza Lalani & Rodrigo Lazo, eds, *The Role of the State in Investor-State Arbitration* (The Hague: Martinus Nijhoff Publishers, 2015) at 216.

Second, it explains where frivolous and abuse of process claims generally fit within the system's ongoing experience with legitimacy crisis and reform. From the outset, frivolous and abuse of process claims can be linked with the rule of law critiques. This linkage manifests itself in three ways. First, (as Chapter Four shows), the standards for dismissal of frivolous and abuse of process claims are ambiguous. Second, ISA tribunals have to employ mechanisms for dealing with frivolous and abuse of process claims within a context of systemic legal uncertainty. Third, the tribunals operate under procedural and sociological constraints that can prevent effective curtailment of claims early in the process. For example, the arbitrators must ensure enforceability of the award and for this purpose have to ensure that the parties have an opportunity to air their claims.

Finally, examination of the different critiques of the investment regime helps to explain why and how states have attempted to reform it. This explanation is valuable to draw the path forward for the regime's reform, including on how to deal with frivolous and abuse of process claims. Accordingly, this section proceeds by discussing the four categories of critiques identified by Alvarez. The categories overlap but the angle of critiques remains unique for each category.

3.1.1 Vertical Critiques

The label "vertical" refers to relations between the investment regime and domestic legal systems. Vertical critiques thus encompass two kinds of relations: the relationship between the international and national law, and the relationship between national and international authority.[539] The particular concern is "a vertical disconnect

[539] The problem of authority or "power delegation" in the investment regime i.e. how such authority is distributed between the participants of the investment regime (states and investors) is discussed in greater detail here. Andrea Bjorklund, "Constrains on Power and Authority in International Investment

between the supranational law that it produces and that was created by a country's elected representatives or enforced by local court".[540] To explain such "top-down" relations, this section discusses two related yet distinct issues. First, the investment regime authorizes investment tribunals to second-guess decisions of democratically elected governments.[541] Second, the investment regime establishes a "top-down" architecture, in which the ISA tribunals have an upper hand over national governments. The result is that national governments may be hesitant to regulate in the public interest. This section labels these two points as "the lack of democratic legitimacy" and "the regulatory chill concern".

3.1.1.1 Democratic Legitimacy

This section overviews the deficit of democratic legitimacy in the investment regime. Given the range and scope of scholarship, this section reviews only the key commentators and their core arguments to explain why the investment regime may face democratic legitimacy deficit. ISA tribunals "second-guess" the decisions of democratically elected state representatives, which has attracted strong criticisms in the investment arbitration scholarship.[542] Choudhury suggests that ISA tribunals "instigate democratic deficits" because "arbitrators make decisions that affect the public interest regulations of democratically elected governments" without taking into consideration "public input".[543]

Arbitration" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* 2013 (The Hague: Martinus Nijhoff Publishers, 2014) at 15.

[540] Alvarez (2011), at 75-76.

[541] *Ibid*.

[542] Thomas Ginsburg, "International Substitutes for Domestic institutions: Bilateral Investment Treaties and Governance"(2005) 25 Intl Rev L & Econ 107.

[543] Barnali Choudhury, "Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit?" (2008) 41 Vand J Transnatl L 775 at 779.

Similarly, according to Schneiderman, the investment regime imposes constraints upon democratically elected representatives even if they act to uphold public welfare.[544] In his discussion of *Metaclad v Mexico* case, Schneiderman shows that the Government of Mexico regulated to prevent a foreign investor from opening and operating "a hazardous landfill facility" in Guadalcazar, which led to an ISA claim from Metaclad for violation of investment standards.[545] The tribunal eventually upheld the claim.[546] Schneiderman underscores the point that the arbitrators were "deaf" to the public outcry and the protests of the civil society in Mexico, which demanded that the Government of Mexico shut down the landfill.[547] In this respect, the chief concern of Schneiderman is that the investment regime excludes "suffering voices from its institutional logic".[548]

Mouyal also argues that the investment regime lacks democratic legitimacy but approaches the problem from a human rights perspective. According to Mouyal, investment tribunals function in contradiction to the principle enunciated in the *Universal Declaration on Human Rights* that "*the will of the people* shall be the basis of the authority of the government".[549] Mouyal suggests that the regime inappropriately authorizes privately-appointed arbitrators to review the decisions of democratically

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[544] Schneiderman (2013), at 50.
[545] *Ibid*.
[546] *Ibid*.
[547] *Ibid*.
[548] *Ibid* at 93.
[549] Mouyal (2016), at 98 [emphasis original]. Andreas Kulick, "Investment Arbitration, Investment Treaty Interpretation, and Democracy" (2015) 4 Cambridge J Intl & Comp L 441. Kulick notes that not all tribunals ignore the will of democratically elected legislatures, he shows that *Paushok v. Mongolia* where the tribunal states "[t]he fact that a democratically elected legislature has passed legislation that may be considered as ill-conceived, counter-productive and excessively burdensome does not automatically allow to conclude that a breach of an investment treaty has occurred". Kulick, however, recognizes that formally IIAs grant the arbitrators an authority to review domestic policies adopted by the democratically elected institutions. Barnali Choudhury, "Recapturing Public Power: Is Investment Arbitration's Engagement of the Public Interest Contributing to the Democratic Deficit?" (2008) 41 Vand J Transnat'l L 776 at 822.

elected governments.[550] Accordingly, the democratic legitimacy critics amount to a concern of authority distribution within the regime generally and what actors are excluded from decision-making with the regime specifically.

3.1.1.2 Regulatory Chill

The other persistent vertical criticism relates to the "top-down" architecture of the investment regime, which can constrain the ability of states to regulate in the public interest. The argument is that the claims of foreign investors cause a "chilling effect",[551] but this hypothesis is vigorously contested in the scholarly discourse.[552]

Van Harten and Scott conducted interviews with governmental officials in Ontario to understand whether the ISA claims can potentially result in the regulatory chill.[553] This empirical inquiry shows that the ISA claims influence the governmental decision-making when adoption of national welfare policies is concerned.[554] Van Harten and Scott concede that more research is required to acquire evidence of the potential

[550] *Ibid*.
[551] David Schneiderman, *Constitutionalizing Economic Globalization: Investment Rules and Democracy's Promise* (Cambridge: Cambridge University Press, 2008) at 129–34 (discussing the case of plain-packaging regulation that the Government of Canada refused to adopt in fear of NAFTA claims). Baumgartner (2016), at 62-63 (examines the treaty and forum shopping practices in light of regulatory chill hypothesis). Leon Trakman & David Musayelyan, "Caveat Investors- Where Do Things Stand Now?" in Chin Lim, ed, *Alternative Visions of the International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2016) (discusses regulatory chill as an argument against arbitration) at 78. Thomas Johnson & Catherine Gibson, "The Objections of Developed and Developing States to Investor-State Dispute Settlement, and What They Are Doing About Them" in Arthur Rovine, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (The Hague: Nijhoff Publishers, 2014) (discusses regulatory chill concerns of states) at 261.
[552] Stephan Schill, "Do Investment Treaties Chill Unilateral State Regulation to Mitigate Climate Change?" (2007) 24 J Intl Arb 469 (examines three NAFTA cases where foreign investors challenged the environmental regulatory measures and argues that the states successfully maintained defence and won the arbitrations). Jack Coe & Noah Rubins, "Regulatory Expropriation and the Tecmed Case: Context and Contributions" in Thomas Weiler, ed, *International Investment Law and Arbitration: Leading Cases From the ICSID, NAFTA, Bilateral Treaties and Customary International Law* (London: Cameron May, 2005) at 597, 599 (Coe and Rubins argue that the main pitfall of the regulatory chill hypothesis is that the government bureaucrats are not always aware of international law. As a result, international law cannot influence on their decisions). Rohan Perera, *Technical Assistance and Capacity Building, Lessons Learned From Experiences and the Way Forward* (OECD, 2015).
[552] *Ibid*.
[553] *Ibid*.
[554] Van Harten & Scott (2016), at 92.

chilling effect. Yet their findings provide a valuable insight into how officials view potential ISA challenges when they make decisions.

According to Van Harten and Scott, ISA claims constitute a factor in states' risk-assessment process. For example, in the *Ethyl v Canada* case, the foreign investor sued Canada for its ban on Methylcyclopentadienyl manganese tricarbonyl (MMT), a gas that is hazardous to health, safety, and the environment.[555] Canada eventually settled the claim. Remarkably, one government official acknowledged that this case had a profound effect on the decision-making process, saying that it "really spooked officials and they became very, in my view, intimidated by Chapter 11 challenges ... […] they were just really fearful of developing any productive policy".[556] Lack of transparency in the investment arbitration process (particularly at the early stages of the process when the investor informally notifies the host government about a potential claim) makes it impossible to empirically analyze how the initiation or threat of initiation of an ISA claim influences governmental decision-making.

Tienhaara observes that there are two types of regulatory chill. The first is the effect as a "broad phenomenon", when "policy-makers take into account potential disputes with foreign investors before they even begin to draft a policy and prioritize avoiding such disputes over the development of efficient regulation in the public interest".[557] The second type of regulatory chill arises from "specific regulatory measures that have been proposed or adopted by governments […] [and] would emerge only when a government has been made aware of the risk of an investor–State dispute by an

[555] *Ibid*.
[556] *Ibid* at 111.
[557] Tienhaara (2011), at 606.

investor".[558] For Tienhaara, the first type is hard to measure and prove empirically, whereas the second type can be examined through case studies. Tienhaara acknowledges that in some instances "the mere threat of arbitration is sufficient to chill environmental policy development".[559] In developing her argument, Tienhaara points out that regulatory chill may be more problematic for developing countries "where there is less willingness to devote scarce resources to engage in arbitration".[560]

Miles examines regulatory chill in the light of environmental regulations.[561] As a case study, she considers an attempt by the Indonesian Government to enact a forestry law that "affected more than 150 mining companies".[562] Soon after the Indonesian Government enacted this law, it received advice that it may face ISA claims "in the realm of US31 billion if the forestry laws remained effective".[563] Miles concludes that regulatory chill "has the potential to frustrate initiatives designed to implement national and global environmental objectives".[564]

In his critical assessment of regulatory chill in the investment regime, Bonnitcha observes that "the extent of regulatory chill is likely to vary between decision-makers within and between states".[565] Bonnitcha emphasizes that some states have faced investors' claims multiple times and yet "have maintained permissible environmental and

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[558] *Ibid* at 607.
[559] Kyla Tienhaara, *The Expropriation of Environmental Governance: Protecting Foreign Investors at the Expense of Public Policy* (Cambridge: Cambridge University Press, 2009) at 3.
[560] *Ibid* at 263.
[561] Kate Miles, *The Origins of International Investment Law. Empire, Environment and the Safeguard of Capital* (Cambridge: Cambridge University Press, 2013) at 181-187.
[562] *Ibid* at 182. Stuart Cross, "Inordinate Chill: BITs Non-NAFTA MITs and Host State Regulatory Freedom- An Indonesian Case Study" (2003) 24 Mich J Intl L 849 (discusses the Indonesian case). Lone Mouyal, *International Investment Law and the Human Rights Perspective* (London: Routledge, 2016) at 67-68 (also makes an argument that regulatory chill may steer the governments' regulations on the basis of the Indonesian case).
[563] *Ibid*.
[564] *Ibid* at 187.
[565] *Ibid* at 132.

human rights measures".[566] As examples, he cites the cases of *Glamis Gold v USA*, *Chemtura v Canada* and *Lucchetti v Peru*, where "the respective respondent states maintained the impugned measures throughout arbitration proceedings and ultimately avoided liability".[567]

Phillip Morris v Uruguay also illustrates Bonnitcha's point.[568] In this case, Phillip Morris challenged Uruguay's public policy measures (including tobacco plain-packaging) to reduce smoking and improve public health.[569] The investor alleged a violation of FET, FPS and expropriation of its intellectual by Uruguay.[570] Uruguay is a developing country with limited capacity to respond to the claim, yet the government successfully defended the claim in ISA and continued its anti-tobacco policy.[571] According to the tribunal, Uruguay legitimately exercised its police power and acted in accordance with its international obligations when it adopted its regulatory measures on tobacco.[572] Accordingly, *Phillip Morris v Uruguay* shows that developing states are not necessarily victims of regulatory chill and are at least sometimes capable of defending investors' claims. It is essential, however, to acknowledge that Uruguay benefited from a third-party funding arrangement. It secured the financial support of Michael Bloomberg, the billionaire former mayor of New York City to combat the claim in ISA.[573] Bloomberg set up the Anti-Tobacco Trade Litigation Fund "to help low- and middle-income countries

[566] Bonnitcha (2014), at 125.
[567] *Ibid*.
[568] *Philip Morris v Republic of Uruguay* (2016), Award ICSID Case No. ARB/10/7 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gary Born, James Crawford, Piero Bernardini)..[Philip Morris v Republic of Uruguay]. *Agreement Between the Swiss Confederation and the Oriental Republic of Uruguay on the Reciprocal Promotion and Protection of Investments* (1976), UNTS 389.
[569] *Ibid*.
[570] *Ibid* at para.180, 308.
[571] Philip Morris Brands Sàrl v Oriental Republic of Uruguay Tribunal Holds that Uruguay's Anti-Tobacco Regulations Do Not Violate Philip Morris's Investment Rights (2017) Harv L R 1986.
[572] *Ibid* at para.287, 421, 158.
[573] Marc Margolis, Big Tobacco Gets Crushed by Tiny Uruguay, Bloomberg View, online:< https://www.bloomberg.com/view/articles/2016-07-18/big-tobacco-gets-crushed-by-tiny-uruguay>.

finance their defenses against tobacco companies' claims under investment treaties".[574] Not all states may be able to attract such support and thus can lack financial capacity to resist claims. The problem is particularly acute given that a frequently-proposed centre to assist developing states with defending investment claims has never materialized.[575]

However, Bonnitcha does not dismiss the regulatory chill argument outright. In his view, the case of New Zealand – where the government delayed adopting a tobacco plain-packaging law for fear of potential ISA claims – "is a clear case of regulatory chill".[576] Another alleged account of regulatory chill is presented by David Schneiderman in an affidavit submitted to a Canadian court in support of a constitutional challenge raised by the Community University Research Alliance Project (CURE).[577] CURE argued that the Canadian government violated the sections 7 and 15 of the *Canadian Charter of Rights and Freedoms* when it "conferred authority over the adjudication of investor-state disputes to NAFTA tribunals", international adjudicatory bodies that have no "competence or authority to consider or protect them".[578] Leave to appeal was refused by the Supreme Court. In his affidavit, Schneiderman alleges that Canada abandoned its plain-packaging regulatory initiative after the representatives of tobacco companies threathened to file a claim under NAFTA.[579]

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[574] Victoria Shannon Sahani, "Revealing Not-for-Profit Third-Party Funders in Investment Arbitration", (2017) *Investment Claims*, online:< http://oxia.ouplaw.com/page/third-party-funders/revealing-notforprofit-thirdparty-funders-in-investment-arbitration>.
[575] Eric Gottwald, "Leveling the Playing Field: Is it Time for a Legal Assistance Center for Developing Nations in Investment Treaty Arbitration?" (2007) 22:2 Am Un Intl L Rev 227 at 264. at 435. Lars Markert & Catharine Titi, "States Strike Back - Old and New Ways for Host States to Defend Against Investment Arbitrations" in Andrea Bjorklund, ed, *Yearbook on International Investment Law & Policy 2013-2014* (Oxford: Oxford University Press, 2015) at 401, 435.
[576] Bonnitcha (2014), at 126.
[577] *Charter of Human Rights and Freedoms*, C QLR c C-12, s 7,15. Bruce Porter, "Canadian Constitutional Challenge to NAFTA Raises Critical Issues of Human Rights in Trade and Investment Regimes" (2006) 3:1 Housing and ESC Rights Law Quarterly 2.
[578] *Ibid* at 3-4.
[579] *Council of Canadians v Canada* (AG), [2004] 1 ON (Affidavit, David Schneiderman) at para.11-12.

Another frequently-cited example of regulatory chill is *Vattenfall v Germany*.[580] Prislan and Zadvliet suggest that the regulatory chill concern should not be dismissed outright because "threats" to file a claim in ISA "are cheap" for foreign investors from a purely transactional perspective.[581] In other words, foreign investors have very little to lose from making such a threat, whereas the government may be hesitant to regulate, knowing the potential costs of arbitration proceedings, or that they may be forced to pay a large damages award. In some instances, particularly when third-party funding is available, bringing a claim in ISA becomes cheap for foreign investors.[582] In addition, the dynamics of participation in the disputes also matters, particularly when the investors are "one-shot" litigants and states have to respond to multiple claims.[583]

It is also clear that governments can take measures in response to regulatory chill when they draft their new treaties or revise their IIAs.[584] In my view, whether or not regulatory chill *de facto* exists, it seems clear that states *fear* that ISA could pervade and affect their regulatory space. The texts of the newly-negotiated IIAs provide evidence to support this perspective. For example, the CETA expressly re-affirms that states preserve their right to regulate to achieve environmental, public health and other objectives.[585] Such fear may in itself be sufficient for some governments, especially of developing

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[580] Jorge Viñuales, *Foreign Investment and the Environment in International Law* (Cambridge: Cambridge University Press, 2012) at 186.
[581] Vid Prislan & Ruben Zadvliet, "Labour Provisions in International Investment Agreements" in Andrea Bjorklund, ed, *Yearbook on International Investment Law and Policy 2012-2013* (Oxford: Oxford University Press, 2014) at 369.
[582] Anna Joubin-Bret, "Spotlight on Third-Party Funding in Investor-State Arbitration" (2015) 16 J World Investment & Trade 727.
[583] Jeffrey Dunoff & Mark Pollack, "Reviewing Two Decades of IL/IR Scholarship: What We've Learned, What's Next" in Jeffrey Dunoff & Mark Pollack, eds, *Interdisciplinary Perspectives on International Law and International Relations: The State of the Art* (Cambridge: Cambridge University Press, 2013) at 635.
[584] Armand de Mestral & Lukas Vanhonnaeker, "The Impact of the NAFTA Experience on Canadian Policy Concerning ISA" in Armand de Mestral, ed, *Second Thoughts: Investor State Arbitration Between Developed Democracies* (Montreal: McGill-Queen's Press, 2017) at 202.
[585] *CETA* at art.8.9, 8.10.

states, to alter their regulatory conduct to avoid a potential claim. Developing states can have less resources to be spent on arbitrations and thus might have a greater incentive to avoid engaging in costly proceedings. The structure of cost allocation in the aftermath of the disputes can contribute to these concerns. ISA tribunals do not always award the legal costs to the prevailing party; often, each party has to pay its own expenses.[586]

In the end, regulatory chill can affect decision-makers in some circumstances. It may be particularly important when foreign investors make governments aware of a potential claim if a specific regulatory policy is adopted.[587] The difficulty for proponents of the regulatory chill hypothesis is to show that states refuse to uphold a particular regulatory policy exclusively or mainly because they fear repercussions from investors. The hypothesis is difficult to prove empirically because governments do not publicize information if threats from foreign investors influenced their policy-making. Nevertheless, "the possibility of regulatory chill seems no less real because conclusive negative proof is logically impossible to deliver".[588] The cases of the Indonesian forestry law scenario and the New Zealand plain - packaging law, for example, present instances when concerns over regulatory chill appear to have been warranted.

For now, it suffices to say that regulatory chill may be a valid concern. Even if states simply *fear* that ISA claims will result from some regulatory action, this may

[586] Laurence Shore & Robert Rothkopf, "For Better or Worse, Is There a Common Law of Investment Arbitration" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers 2013* (The Hague: Martinus Nijhoff Publishers, 2014) at 296. (show that the ISA tribunals show "significant inconsistency in investment treaty awards" on "the allocation of costs between the parties").
[587] Freya Baetens, "The Kyoto Protocol in Investor-State Arbitration" in Marie-Claire Cordonier Segger, Markus Gehring & Andrew Newcombe, eds, *Sustainable Development in World Investment Law* (The Hague: Kluwer Law International, 2011) at 697.
[588] *Ibid*.

undermine the regime's legitimacy and result in states undertaking measures to safeguard their regulatory space.

3.1.2 Horizontal Critiques

Alvarez's definition of "horizontal" deficits suggests that IIAs and ISA constitute the "asymmetrical bargains struck along sadly familiar and predictable North/South lines".[589] In theory, the investment regime "was premised on putting all states on a "level playing field".[590] However, "as compared to the bad old days of gunboat diplomacy - it falls well short of that goal".[591] As a result, the regime is detrimental to "the principle of sovereign equality".[592] Horizontal deficits are deeply rooted in the history of the investment regime and echo the post-War tension between developing and developed states.[593] Developing states promoted resolutions that favored state sovereignty,[594] while developed states sought ways to further protect their nationals and assets abroad.[595] In short, these critics argue that the investment regime is a "one-way street" that favors developed states and continues colonial-style exploitation.[596]

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[589] Alvarez (2011), at 85.
[590] *Ibid*.
[591] *Ibid*.
[592] *Ibid* at 86.
[593] Kaushal (2009), at 510–514.
[594] Alvarez (2011), at 84-85.
[595] *Ibid*.
[596] Third World Approaches to Legal Scholarship (TWAIL) greatly contributes to the scholarly discourse in investment arbitration in bringing up the problems of functional inequality among states and by situating such inequality in a broader historical context of colonial politics and war capitalism. In particular, TWAIL approach is helpful to untangle the "horizontal critiques" because it explains a lack of participation of the developing states in the investment law-making by attributing it to a coordinated effort of developed states "normatively dominate international economic governance" and "maintain procurement of colonialism" over the newly independent states see e.g. Antonius Hippolyte, "Aspiring For a Constructive TWAIL Approach Towards the International Investment Regime" in Stephan Schill, Christian Tams & Rainer Hofmann, eds, *International Investment Law and Development: Bridging the Gap* (Northampton: Edward Elgar Publishing, 2015) at 199-200. Gus Van Harten, "TWAIL and the Dabhol Arbitration" (2011) 3 Trade, Law & Development 131. Obiora Chinedu Okafor, "Critical Third World Approaches to International Law (TWAIL): Theory, Methodology, or Both?" (2008) 10:4 Intl Community L Rev 371 at 378. Michael Fakhri, "Law as the Interplay of Ideas, Institutions, and Interests: Using Polyani (and Foucault) to ask TWAIL Questions" (2008) 10:4 Intl Community L Rev 455.

Vertical critiques cover the top-down relations between national and international authority. This section examines horizontal critiques, which instead focus on the relations between sovereign states. The first part shows that international rule-making in the investment regime is asymmetrical, followed by an analysis that shows participation in investment disputes is asymmetrical.

3.1.2.1 Asymmetry of Investment Rule Making

There are two key concerns about asymmetry in investment rule-making. First, there is an understanding that IIAs emerged for the protection of Western investments in the Global South. Second, developing states never had a chance to participate in negotiations of BITs under the equal arms principle; that is, developing states often had to agree on terms already offered by the developed states. Hence, the asymmetry in investment rule-making is a concept that encompasses two related but distinct problems, relating to (1) the content of IIAs, which focus on protecting foreign investors from developed states and (2) unequal participation in developing the IIA network.

3.1.2.1.1 Unequal Representation in Developing the Network of International Investment Agreements

This critique is built on the premise that developing countries played a limited role in the creation of the IIAs network.[597] The critics advance charges in three directions. First, during the process of the treaty negotiations, developed states often have the ability to impose pressure on developing nations to agree to provisions in IIAs that benefit investors and, by extension, capital-exporting states.[598] Alschner and Skougarevskiy empirically support this claim by showing that developed states over time were able to

[597] Jeswald Salacuse & Nicholas P. Sullivan, "Do BITs Really Work? An Evaluation of Bilateral Investment Treaties and Their Grand Bargain" (2005) 46 Harv Intl LJ 67 at 70.
[598] Elkins, Guzman & Simmons (2006), at 811–846, 822. (host states as "price takers").

achieve "consistent treaty networks" that "aligned with their preferences".[599] They conclude that this trend shows "underlying asymmetries in BIT negotiations".[600] Guzman submits that in the long-term some IIA provisions may actually hurt the least-developed states.[601] Second, developing states "stay in a subordinate role"[602] whereas developed states continue to dominate treaty making processes. Third, developing states continue to face capacity challenges that preclude their ability to fully participate in the investment rule-making.[603] Valerie Ruttenberg argues that developed countries possess greater bargaining power and illustrates this point by referring to US BIT negotiations;[604] she found that developing states that depended on US foreign aid were more inclined to accept the US Model BIT without amendments.[605]

The context of colonialism animates the dialogue of authors on contemporary asymmetric relations between developing and developed states and rule- making within the investment regime. [606] Sornarajah observes that early foreign investments were "largely made in the context of colonial expansion".[607] During the colonial period, investments were protected by the power of empires through their domestic

[599] Wolfgang Alschner & Dmitriy Skougarevskiy, "Mapping the Universe of International Investment Agreements" (2016) 19:3 J Intl Econ L 561 at 574
[600] *Ibid*.
[601] Andrew Guzman, "Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of Bilateral Investment Treaties" (1997) 38 Va J Intl L 639 at 682. (argues that "BITs sharpen the competition for investment among potential hosts. This forces LDCs to offer greater and greater concessions to potential investors, bidding away the gains the host would otherwise enjoy. In effect, BITs make the market for foreign investment much more competitive by allowing competition in the "price" of investment, that is, the terms under which investment takes place").
[602] Schill, Tams & Hofmann (2015), at 201.
[603] *Ibid* at 201.UNCTAD, World Investment Report: Transnational Corporations, Extractive Industries and Development United Nations (New York: Academic Foundation, 2008) at 18.
[604] Valerie Ruttenberg, "The United States Bilateral Investment Treaty Program: Variations of the Model" (1987) 9:1 University of Pennsylvania journal of international business law 121 at 141.
[605] *Ibid* at 125.
[606] Kaushal (2009), at 510–514.
[607] Sornarajah (2010), at 19.

parliamentary institutions, or by military capacity.[608] In the post-colonial period when many states seized independence, "capital-exporting countries […] were keen to devise some legal justification for pursuing the claims of their nationals" when foreign investments were concerned.[609] As a result, IIAs emerged in response.[610]

Mattias Kumm has a "darker story to tell" about colonial origins of the investment regime.[611] He argues that IIAs and ISA strikingly resemble the colonial institution of "consular jurisdiction", which ensured that "that certain nationals were exempted from the legal processes of the host country in favour of trial by officials more attuned to their interests".[612] Of course, during the colonial periods nations were not equal. States were as a matter of law divided into the subgroups of "civilized", "semi-civilized", or "barbaric" status.[613] The governments of what were called barbaric states could not legally prosecute foreign nationals of civilized states who otherwise fell under their jurisdiction.[614]

3.1.2.1.2 International Investment Agreements Can "Hurt" Developing States

IIAs include provisions that may visibly disadvantage developing and the least-developed states.[615] Lauge Poulsen observes that developing states do not favour the national treatment (NT) provisions because industries in developing states are still "infant" and thus require support from a state in order to compete with foreign

[608] *Ibid* at 20
[609] *Ibid*.
[610] Salacuse (2015), at 101. Surya Subedi, *International Investment Law: Reconciling Policy and Principle* (New York: Bloomsbury Publishing, 2016). Sornarajah (2010), at 210. Joseph Munoz, *Handbook on the Geopolitics of Business* (Northampton: Edward Elgar Publishing, 2013) at 237. (discusses a formula of "prompt, adequate and effective compensation" in a historical context and specifies that this is known as a Hull formula that the Latin American states and Mexico resisted through the legacy of Calvo doctrine that emphasized paramountcy of the self-determination and national sovereignty in relations with foreign investors).
[611] Mattias Kumm, An Empire of Capital? Transatlantic Investment Protection as the Institutionalization of Unjustified Privilege, online: http://www.esil-sedi.eu/node/944
[612] *Ibid*.
[613] *Ibid*.
[614] *Ibid*.
[615] Guzman (1997), at 666.

investors.[616] In contrast, developed states insist on including NT provisions in their treaties with developing states, to shield their investors from discriminatory practices.[617]

Another aspect of controversy is the clauses that permit the free transfer and repatriation of funds from a host state without restrictions or delays.[618] This mechanism constitutes an important tool for foreign investors to manage their capital.[619] Developing states often use these measures to restrict the transfer of fundsas part of a regulatory strategy to respond to financial crises.[620] Poulsen explains that most treaties include both of these types of provisions detrimental to developing states, while South-to-South IIAs either do not incorporate them, or enact a number of exceptions to them.[621]

Having examined "2100 IIAs and their 24 000 articles", Alschner and Skougarevskiy conclude that developed countries "tend to be IIA system's rule-makers, while developing countries tend to be its rule-takers".[622] Most importantly, their study helps to track trends within the investment regime. It supports the proposition of the political system framework that states tend to introduce changes in their IIAs to respond to adverse outcomes or the regime's broader deficits.

Similarly, Elkins *et al* observe that the developing and least developed countries are often "price-takers with respect to the terms of these treaties" because "they must compete with other potential hosts and, therefore, cannot demand changes to the core provisions of the treaties".[623] According to Alvarez, contemporary international law

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[616] *Ibid*.
[617] *Ibid*.
[618] *Ibid* at 194-195.
[619] *Ibid.*
[620] *Ibid* at 195.
[621] *Ibid* at 203-204.
[622] Wolfgang Alschner & Dmitriy Skougarevskiy, "Mapping the Universe of International Investment Agreements" (2016) 19:3 J Intl Econ L 561 at 562.
[623] Zachary Elkins, Andrew Guzman, & Beth Simmons, "Competing for Capital: The Diffusion of

restores colonial-style relations between states through the content of IIAs, which are said to reflect law among "civilized nations".[624]

Some authors insist that today's asymmetries are a holdover from, rather than an active continuation of, the colonial era. From this viewpoint, the investment regime currently reflects "a systemic bias […] of Northern superiority" and "inferiority of others".[625] Accordingly, IIAs are professed to be "one sided" instruments of neo-colonialism to protect investments from the Global North in the Global South.[626]

Dupont and Schultz argue that the investment regime served as "a sword in the hands of the economic interests of investors from rich countries against governments of poorer countries" only up to the "mid-to-late 1990s".[627] Dupont and Schultz submit that since the 1990s, IIAs focus on the promotion of the rule of law, rather than on reassertion of economic interests of developed nations.[628] On this basis, the investment regime was a tool of "rich" nations against the "poor" states only for a discrete and now-concluded period.

The asymmetry of the rule-making contributes to the undermining of the legitimacy of the investment regime by reinforcing inequality among states. The

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Bilateral Investment Treaties" (2006) 60 International Organization 811 at 822.

[624] Jose Alvarez, "The Once and Future Foreign Investment Regime" in Mahnoush H. Arsanjani, et al, eds, *Looking to the Future: Essays on International Law in Honor of W. Michael Reisman* (The Hague: BRILL, 2010) at 610.

[625] Muthucumaraswamy Sornarajah, *Resistance and Change in the International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2015). Muthucumaraswamy Sornarajah, "The Neo-Liberal Agenda in Investment Arbitration: Its Rise, Retreat and Impact on State Sovereignty" in Wenhua Shan, Penelope Simons & Dalvinder Singh, eds, *Redefining Sovereignty in International Economic Law* (London: Bloomsbury Publishing, 2008). Susan Franck, "Development and Outcomes of Investment Treaty Arbitration" (2009) 50 Harv Intl LJ 435.

[626] Wenhua Shan, "From North-South Divide to Private-Public Debate: Revival of the Calvo Doctrine and the Changing Landscape in International Investment Law" (2006-2007) 27 Nw J Intl L & Bus 631. David Schneiderman, "Legitimacy and Reflexivity in International Investment Arbitration: A New Self-Restraint?" (2011) 2:2 J Intl Disp Settlement 471.

[627] Thomas Schultz & Cédric Dupont, "Investment Arbitration: Promoting the Rule of Law or Over-empowering Investors? A Quantitative Empirical Study" (2014) 25:4 Eur J Intl L 1147 at 1149.

[628] *Ibid* at 1168.

horizontal critics argue that IIAs establish a system that privileges foreign investors from rich states over the interests of the poorer states.[629] Such privileges are exacerbated by the fact that poorer states historically could not actively participate in designing treaties due to various capacity challenges or dependence on developed states.[630]

3.1.2.2 Asymmetry of the Participation in the Disputes

Participation in investment disputes is also asymmetrical.[631] According to UNCTAD, there is a disparity among users of the investment arbitration system along the North/South line.[632] The most frequent respondent states from 1987-2017 were Argentina (60 claims), Venezuela (44 claims), Spain (43 claims), Czech Republic (35 claims), and Egypt (31 claims).[633] Accordingly, Spain is the only developed country at the top five most frequent respondents in ISA.

Developing countries face capacity challenges as the respondents in investment disputes.[634] Defending these claims requires substantial resources.[635] Disputes may also

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[629] Antony Anghie, *Imperialism, Sovereignty and the Making of International Law* (Cambrdige: Cambridge University Press, 2007) at 226-230.
[630] Jan Paulsson, "Third World Participation in International Investment Arbitration" (1987) 2:1 ICSID Rev 19 ("Legal concepts and processes introduced from abroad were historically imposed by colonial powers"). Gus Van Harten, "TWAIL and the Dabhol Arbitration" (2011) 3:1 Trade, Law and Development 131 at 134 ("international law disadvantages countries that were subjected to colonialism and benefits narrow elites who are especially based in the West"). Peter Drahos, "Weaving Webs of Influence: The United States, Free Trade Agreements and Dispute Resolution" (2007) 41:1 J World Trade 191.
[631] Yannaca-Small (2010), at 33-34.
[632] UNCTAD, IIAs Issues Note. Investor-State Dispute Settlement: Review of Development in 2017 (June, 2018) at 3. [IIAs Note 2017]. UNCTAD, World Investment Report 2016: Investor Nationality: Policy Challenges (United Nations, 2016) at 105-106.
[633] *Ibid* at 105-106. Victor Salgado, "Comment, The Case Against Adopting BIT Law in the FTAA Framework" (2006) Wis L Rev 1025 at 1053-59.
[634] UNCTAD at para. 17-19. Note: Similar work has been done in the context of World Trade Organization (WTO), Joan Apecu Laker, *African Participation at the World Trade Organization: Legal and Institutional Aspects 1995-2010* (The Hague: Martinus Nijhoff Publishers, 2013) at 20.
[635] Daniel Behn, "Legitimacy, Evolution and Growth in Investment Treaty Arbitration: Empirically Evaluating the State-of-the-Art" (2015) 46:2 Georgetown Journal of International Law 363 at 376. (arguing that an average of four years with the longest dispute 129 month (see Goetz v Rep. of Burundi, ICSID Case No. ARB/01/2 (June 21, 2012) After conducting an empirical research, Daniel Behn concluded that the investment regime is "geared" towards a particular type of foreign investor and that is MNE "that is likely attributable to the resources" that are required to file a claim and uphold it in ISA). Cecilia Olivet &

require high level of legal expertise which some states may not possess.[636] This is not to say that developing states cannot ever afford outside counsel to guarantee a high quality expert legal advice that may "cost several million dollars per case", yet it is essential to appreciate that hiring outside counsel may represent "a real burden" for some states.[637] Developing states sometimes rely on external support to fund their participation in a dispute.[638] However, developing countries have to secure support on the case-by-case basis.[639] To address the problem, Eric Gottwald even suggests establishing a 'legal aid centre' for developing states to assist them in managing the disputes.[640]

Some developed states like Canada now face multiple arbitration challenges.[641] However, of the 50 states that have been respondents in ISA arbitrations, 31 are developing states,[642] so it is fair to say that developing countries will "bear the brunt of a potential increase" in ISA proceedings, even if developed states are now respondents

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Alberto Villareal, "Who Really Won the Legal Battle Between Philip Morris and Uruguay?" *Guardian* online:< https://www.theguardian.com/global-development/2016/jul/28/who-really-won-legal-battle-philip-morris-uruguay-cigarette-adverts>.

[636] Thomas Stipanowich, "Arbitration: The "New Litigation" (2010) 1 U Ill L Rev 1 at 8 ([i]n characterizing arbitration one of the commentators notice that arbitration increasingly becomes "formal, costly, time-consuming, and subject to hardball advocacy"). Francis Higgins, William Brown, & Patrick Roach, "Pitfalls in International Commercial Arbitration" (1980) 35 Bus Lawyer 1035.

[637] Jeremy Sharpe, "Representing a Respondent State in Investment Arbitration" in Chiara Giorgetti, *Litigating International Investment Disputes: A Practitioner's Guide* (The Hague: Martinus Nijhoff Publishers, 2014) at 48-49.

[638] Brooks Daly & Sarah Melikian, "Access to Justice" in Krista Nadakavukaren Schefer, ed, *Dispute Resolution in Poverty and the International Economic Legal System: Duties to the World's Poor* (Cambridge: Cambridge University Press, 2013) at 247.

[639] *Ibid*.

[640] Eric Gottwald, "Levelling the Playing Field Is It Time For a Legal Assistance Center for Developing Nations in Investment Treaty Arbitration? (2007) 22:2 Am U Intl L Rev 227. Lars Markert & Catharine Titi, "States Strike Back - Old and New Ways for Host States to Defend Against Investment Arbitrations" in Andrea Bjorklund, ed, *Yearbook on International Investment Law & Policy* 2013-2014 (Oxford: Oxford University Press, 2015) at 435.

[641] Government of Canada, Cases Filed Against Government of Canada, online:< http://www.international.gc.ca/trade-agreements-accords-commerciaux/topics-domaines/disp-diff/gov.aspx?lang=eng>.

[642] UNCTAD (2005), at para. 9. (Argentina is an example, facing or having faced 37 claims arising out of actions taken to respond to its financial crises).

more often than in the past.[643] This trend shows that the asymmetry within the investment regime is slowly shifting.

Investment arbitration can be costly for investors as well. According to UNCTAD, high costs "limit access to international justice mainly to financially powerful investors" which predominantly come from developed states.[644] The high costs of ISA limits participation of small and medium size enterprises from developing states.[645]

Asymmetry in the participation in disputes enhances the legitimacy deficit of the investment regime and reinforces unequal participation in the regime. The claims arrive predominantly from the investors from developed states, whereas some developing states remain the most frequent respondents in investment disputes. Recent trends in dispute participation cannot be overlooked and now more developed nations face claims from foreign investors. However, developed states, do not face the same systemic capacity challenges compared to developing states in responding to claims

3.1.3 Ideological Critiques

At the risk of oversimplifying, ideological critiques fall into two broad categories. The first category focuses the structure of the investment regime that allegedly reinforces neoliberal ideology. The argument is that the structure of the investment regime embeds a particular ideological vision of relations between states and foreign investors. The second category focuses on the fact that the investment regime privileges the interests of foreign investors over those of other stakeholders. Critiques falling into this category argue that the interests of foreign investors are privileged over the interests of all other stakeholders. While distinct, there is a common thread that unites

[643] *Ibid* at para.21.
[644] UNCTAD, (2007) at 93.
[645] IIAs Note 2017 at 3.

these two broad categories, which is that both implicitly presume that a foreign investor and a sovereign state are unequal.

3.1.3.1 The Nexus of the Investment Regime and Neo-Liberal Ideology

This subsection examines two points that constitute the primary foci of the literature on ideological critiques. First, it provides an example of how the provisions of IIAs reflect neo-liberal ideology. Second, it explains that the investment regime is institutionally structured in favor of neoliberal ideology. Under the dominance of neo-liberal ideology, "[the] investment regime - both its substance and its procedures for interpretation and enforcement - are structurally biased in favour of the ideology of free market and privatization".[646]

IIAs constitute an ideological device that arranges the "relationship between politics and markets".[647] Vandevelde explains that the ideology of IIAs "was that the treaties should facilitate, rather than regulate market arrangements".[648] IIAs thus implement a particular *laissez-faire* ideological vision of the role that the government should play in its relations with the private enterprises. The example of this principle may be the so-called "performance provisions" in IIAs that directly prohibit states "from imposing performance requirements on investment".[649] These prevent states from demanding that foreign investors "purchase goods or services locally or export the goods produced".[650]

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[646] Alvarez (2011), at 89.
[647] Kenneth Vandevelde, "Of Politics and Markets: The Shifting Ideology of the BITs" (1993) 11:2 Intl Tax &Buss Law 159 at 161.
[648] *Ibid* at 164.
[649] *Ibid*.
[650] *Ibid*.

Another example is "competitive equality provisions", which prohibit the state parties to IIAs "from giving state owned or state-controlled investment a competitive advantage over the investments of nationals and companies of the other party".[651] That is to say, IIAs impose constraints upon states about how they use their regulatory power. They create an international law obligation to exercise regulatory power according to the rationale of an ideology of market fundamentalism under which the market forces (not regulatory intervention) should determine the affairs of private enterprise. This ideological approach has long informed the political and legal discourse on foreign investment and shaped negotiators' attitudes.[652] For example, in the Lima Declaration, the APEC states promote free and open economies and the removal of regulatory obstacles which inhibit free investment flows.[653]

Second, the ideology of free market embedded in IIAs is institutionally reinforced through the World Bank's and IMF's policies.[654] These international institutions can make governmental loans conditional upon particular performance requirements.[655] Sornarajah explains that the World Bank and IMF not only cultivated and promoted investment treaties, but also "made assistance through loans conditional on the signing of investment treaties".[656] Mourra and Carbonneau also indicate that IMF and the World Bank "began promoting "structural adjustment loans" and "hydro reform", essentially

[651] *Ibid* at 167.
[652] Donald Gibson, *Wealth, Power, and the Crisis of Laissez Faire Capitalism* (Berlin: Springer, 2011) at 215.
[653] *Lima Declaration*.
[654] Christian Tams, Stephan Schill & Rainer Hofmann, eds, *International Investment Law and the Global Financial Architecture* (Northampton: Edward Elgar Publishing, 2017) at 4-5. The book discusses the role of IMF and the World Bank in international investment law.
[655] *Ibid*.
[656] *Ibid* at 14. Sornarajah (2010), at 43.

conditioning loans and loan forgiveness upon a state's agreement to privatize its utilities companies".[657]

In some instances, privatization policies resulted in economic disasters. Schneiderman highlights the situation of Argentina, which followed the path of fundamental reforms under the directives of the World Bank and IMF.[658] These reforms contributed to the de-valuation of the Argentinian peso in 2008, which led Argentina's government to adopt robust economic measures to prevent the entire collapse of the national economy.[659] In response to these measures, Argentina faced more than 30 claims from foreign investors in ISA.[660] In this context, the loans are the "carrot" and ISA serves the "stick" to ensure that states comply with the demands of the international financial institutions.

Critics argue that another example of institutional linkages between investment regime institutions and neoliberal ideology is that ICSID "is not an autonomous body but the judicial arm of an international organization whose key stakeholders are developed countries. […] The US, which holds the largest percentage of the World Bank's shares significantly influenced the bank's lending policies in the 1990s".[661] During this period (as some commentators emphasize), the US still did not lose a single claim, although it faced more than 30.[662]

3.1.3.2 Privileging Foreign Investors

[657] Mourra & Carbonneau (2008), at 88.
[658] Schneiderman (2013), at 60-68.
[659] *Ibid*.
[660] *Ibid*.
[661] Schill, Tams & Hofmann (2015), at 205.
[662] Alvarez (2011), at 87.

One of the charges levied against the investment regime is that it privileges foreign investors at the expense of host states. It is important to distinguish the two most prominent approaches to this problem in the relevant scholarship. The first suggests that the regime structurally privileges foreign investors.[663] The justification for this approach has historical origins and requires an understanding of context, which includes the wave of expropriations of foreign property throughout the 20th century.[664]

The struggle of former colonies for independence and their attempts to re-establish control over natural resources contributed to a growing anxiety among foreign investors and their home states that faced unpredictable regulatory actions of the newly established governments.[665] In this context, IIAs played an instrumental role in limiting the regulatory powers of governments by establishing substantive guarantees for foreign investors and their investments. The central goal of IIAs was to "maximize the protection of the investor".[666] As a result, IIAs were conceived to prioritize the protection of private economic rights over the welfare policies of host states.[667]

The second approach suggests that the mere fact that IIAs set as their object and purpose the protection of foreign investors and their investments is not in itself problematic. What generates the deficit of legitimacy is that the ISA tribunals usually resolve ambiguities in IIAs in favor of foreign investors. The concern is that the tribunals

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[663] Van Harten (2007), at 137-138. Van Harten explains that the investment tribunals often make "explicit statements" that the "predominant aim of the system is to protect investors".
[664] E.g. Frederick Truitt, "Expropriation of Foreign Investment: Summary of the Post World War II Experience of American and British Investors in the Less Developed Countries" (1970) 1 J Intl Bus Stud 21, 23–30.
[665] Peter Muchlinski, "The Energy Charter Treaty: Towards a New International Order for Trade and Investment or a Case of History Repeating Itself" in Thomas Wälde, ed, *The Energy Charter Treaty: An East-West Gateway for Investment and Trade* (The Hague: Kluwer International, 1996) at 208.
[666] *Ibid*.
[667] Ruth Teitelbaum, "A Look at the Public Interest in Investment Arbitration: Is it Unique? What Should We Do About It?" (2010) 5 BJIL 54. Amr Shalakany, "Arbitration and the Third World: A Plea for Reassessing Bias Under the Specter of Neoliberalism" (2000) 41 Harv Intl LJ 419.

choose to prioritize the rights of foreign investors over the interests of host states when IIAs do not provide explicit guidance.[668]

Incentives embedded systemically in the institutions do appear to influence tribunals to favour investors.[669] For example, arbitrators are selected based of the choices of the parties. The party–driven appointment system creates incentives among arbitrators to further the system.[670] Park explains that the "argument seems to run as follows: arbitrators seek to promote the growth of investor-state proceedings in order to get future appointments".[671] Van Harten emphasizes that "the failings go beyond that of a rogue tribunal or cowboy arbitrator […] the problems with the current system are structural […] the system as a whole […] is open to a perception of bias so long as arbitrators earn appointments by the claim".[672]

3.1.4 Rule of Law Critiques

The rule of law principle has distinctive meanings in different contexts.[673] Investment arbitration scholars employ two aspects of the rule of law to argue that the

[668] Van Harten (2007), at 138. Van Harten explains that the tribunals resolve "doubts arising from ambiguity in the treaty in favor of investor protection".
[669] Mark Wu, "Trade's Influence in Shaping the Evolving International Investment Regime" in Zachary Douglas, Joost Pauwelyn & Jorge Viñuales, *The Foundations of International Investment Law: Bringing Theory into Practice* (Oxford: Oxford University Press, 2014) at 178 (see for general overview of the critique). Stavros Brekoulakis, "Systemic Bias and the Institution of International Arbitration: A New Approach to Arbitral Decision-Making" (2013) 4:3 Journal of International Dispute Settlement 553 at 557 (examines the influence of the "broader institutional context within which decisions are taken").
[670] Kaushal (2009), at 521. ("The creation of a competitive market in arbitration provides participants with an interest in furthering the system").
[671] Park (2010), at 213.
[672] Van Harten (2007), at 175.
[673] Duncan Kennedy, "The Stakes of Law, or Hale and Foucault!" (1991) 15 LS Forum 327. Thomas Buergenthal, "The Proliferation of Disputes, Dispute Settlement Procedures and Respect for the Rule of Law" (2006) 21 ICSID Rev at 126, 128. Brian Tamanaha, *On the Rule of Law: History, Politics, Theory* (Cambridge: Cambridge University Press, 2004). Tom Bingham, *The Rule of Law* (London: Penguin, 2011).

investment regime suffers from a crisis of legitimacy, namely "substantive" and "procedural" deficits of the rule of law.[674]

3.1.4.1 Substantive Deficits

Two critiques are prominent in relation to the content of the legal norms in the investment regime. First, the legal rules in IIAs are ambiguously formulated and produce uncertainty over the content of states' obligations to investors. Second, ISA tribunals enhance this uncertainty by adopting broad interpretations of IIAs. One result has been that ISA tribunals have generated contradictory decisions over time. These problems have been the subject of substantial scholarly attention.[675] For example, Garcia *et al* acknowledge the "shortcomings in the coherence and predictability of arbitral outcomes, two key rule of law desiderata".[676] This section examines the key arguments within this vein of scholarship to highlight how uncertainty over legal rules may result in legitimacy deficits.

With regard to the problem of ambiguity of legal rules in IIAs, Henckels observes that IIAs "typically contain broadly worded, open-textured obligations".[677] Reisman further explains that the provisions in IIAs have an "evaluative" character, meaning that they may require content to be filled in when they are implemented in each case.[678] In the

[674] Gus Van Harten, "Investment Treaty Arbitration, Procedural Fairness, and the Rule of Law" in Stephan Schill, ed, *International Investment Law and Comparative Public Law* (Oxford: Oxford University Press, 2010). Muthucumaraswamy Sornarajah, "Evolution or Revolution in International Investment Arbitration? The Descent into Normlessness" in Chester Brown & Kate Miles, eds, *Evolution in Investment Treaty Law and Arbitration* (Cambridge: Cambridge University Press, 2012) at 634.
[675] Schill (2009), at 281. Kidane (2017), at 139. Bonnitcha, Poulsen & Waibel (2018), at 250.
[676] Frank Garcia et al (2015), at 871.
[677] Caroline Henckels, "Protecting Regulatory Autonomy through Greater Precision in Investment Treaties: The TPP, CETA, and TTIP" (2016) 19:1 J Intl Econ L 27 at 28.
[678] Michael Reisman, "Canute Confronts the Tide: States versus Tribunals and the Evolution of the Minimum Standard in Customary International Law" (2015) 30:3 ICSID Rev 616 at 617.

investment regime, arbitral tribunals perform this content-filling function.[679] Menon observes that ISA tribunals often adopt broad interpretations of the meaning of legal rules in IIAs.[680] According to Menon, "some of the traditional concepts that underlay investment treaties might be stretched beyond what the parties to the treaties might have contemplated them to mean".[681]

The problem of overly broad interpretations is further complicated by the fact that ISA tribunals are not precluded from producing contradictory outcomes.[682] Franck's study on contradictory outcomes is one of the most widely cited works on this issue. She arrives at the following conclusions. First, Franck suggests that the contradictory decisions are not "occasional wrong[s]",[683] but rather a problem of greater magnitude, since inconsistencies are becoming more frequent.[684] Second, after considering a number of decisions that led to contradictory outcomes, Franck concludes if two awards that contradict one another entirely or in part, this must mean that "at least one of the awards (or a part thereof) was wrong".[685]

Franck's conclusions may have merit, but they fall short on taking into account the broader systemic context of the investment regime. Franck's statement that "one of the awards must be wrong" in the case of two contradictory outcomes fails to

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[679] Susan Franck, "The Role of International Arbitrators" (2006) 12 ILSA J Intl & Comp L 499, 504–13.
[680] Sundaresh Menon, "The Transnational Protection of Private Rights Issues, Challenges, and Possible Solutions" in David Caron et al, eds, *Practising Virtue: Inside International Arbitration* (Oxford: Oxford University Press, 2015) [emphasis added].
[681] *Ibid*.
[682] Schill (2009), at 284. ("in international investment law, there is abundant potential for inconsistent and conflicting decisions. This potential stems from the embryonic institutionalization of investor-state dispute settlement and the lack of *stare decisis*. Investment treaty arbitration therefore lacks internal as well as external control mechanisms that can ensure uniformity in the outcomes of the tribunals' decision-making processes").
[683] Susan Franck, "The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions" (2005) 73 Fordham L Rev 1521 at 1558.
[684] *Ibid* at 1559.
[685] *Ibid* at 1568.

acknowledge that the architecture of the investment regime permits two tribunals to consider similar issues and identical facts but still legitimately arrive at different conclusions. From a systemic point of view, both awards could be "right". Dolzer acknowledges that "the current system of investment arbitration has not been designed in order to promote uniformity or consistency of either rule-making or interpretation, with the sprawling consequences we have seen".[686]

Interestingly, not all commentators consider inconsistent decisions problematic. For example, Schultz argues that arbitrators are not law-makers, and so should cease any attempts to unify the application of the investment rules. As "law-makers they do more harm than good […] A bad rule applied consistently, in a predictable way, in highly regularized patterns, may do more harm than the same rule applied inconsistently, occasionally, in an unpredictable way".[687]

The methodological approaches to the inconsistency critiques are, thus, different. Schultz takes into account the macro perspective—systemic features of the investment regime, whereas Frank focuses on the micro perspective—outcomes of particular disputes. They appear to agree that the content of the investment legal rules is by no means certain, but according to Shill this uncertainty is embedded in the regime's architecture.[688]

It is worth noting that in the context of the early dismissal of claims the inconsistency and unpredictability in the application of legal norms hinders the ability of the arbitrators to understand (at the early stage) what claims can succeed on the merits.

[686] Rudolf Dolzer, "Fair and Equitable Treatment: Today's Contours" (2014) 12 Santa Clara J Intl L 10 at 15.
[687] Thomas Schultz, "Against Consistency in Investment Arbitration" in Zachary Douglas, Joost Pauwelyn, & Jorge Viñuales, eds, *The Foundations of International Investment Law: Bringing Theory into Practice* (Oxford: Oxford University Press, 2014) at 315.
[688] Schill (2009), at 281.

IIAs incorporate investment standards that may be the subject of broad and inconsistent interpretations.

3.1.4.2 Procedural Deficits

This section focuses on perceived deficits of procedural fairness in ISA proceedings. Two major concerns relate to the deficit of procedural fairness. First, the investment regime lacks procedural safeguards that guarantee independence and impartiality of arbitrators. Second, the arbitrators often appear to be biased in favour of foreign investors.

The procedural safeguards ensure independence of adjudicators in the national legal systems. For example, security of tenure protects the institutional and financial independence of judges from the parties. [689] In ISA, it is manifestly absent.[690] When the arbitrators are paid by the parties per day or per hour, they can have a strong incentive to "hear" cases in full rather than curtail them early in the process.

The party-driven appointment system can arguably incentivize rent-seeking behaviour when arbitrators act in such a way to be reappointed. [691] The party-driven appointment system and lack of procedural safeguards such as security of tenure foster a perception that arbitrators are biased.[692] This in itself is problematc for the legitimacy of the investment regime.

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[689] Michael Traynor, "Judicial Independence: A Cornerstone of Liberty" (2007) 37 Golden Gate UL Rev 487 at 492. Christopher Larkins, "Judicial Independence and Democratization: A Theoretical and Conceptual Analysis" (1996) 44 Am J Comp L 605 at 613–14.

[690] Gus Van Harten, "Five Justifications for Investment Treaties: A Critical Discussion" (2010) 2:1 Trade L & Dev 1 at 14. Susan Franck, "Foreign Direct Investment, Investment Treaty Arbitration, and the Rule of Law" (2007) 19 Global Bus & Dev LJ 337 at 340.

[691] Profiting from Injustice at 8.

[692] Van Den Berg highlights one of the most broadly cited neutrality concerns of the party appointed arbitrators is that the party appointed arbitrators issue the dissenting opinion that favors a party that appointed them). Van den Berg proposed to issue temporary stay in dissenting opinions. Yet the problem here is structural or may be categorized as a procedural rule of law problem, in particular that parties have a

In addition, under existing appointment procedures, parties to the dispute appoint most arbitrators. The chair of the tribunal may be appointed by the consent of the parties or, alternatively, by the two co-arbitrators. Van den Berg raises a concern about neutrality of the arbitrators within the current system. Van den Berg conducted a survey that showed "100% of the dissents were in favour of the party that appointed the dissenter in the investment arbitration".[693] He concludes that "the practice of dissents in investment arbitration may have reached the point where a party-appointed arbitrator is now expected to dissent if the party that appointed him or her has lost the case (the so-called 'mandatory dissent')".[694] Accordingly, Van den Berg argues that the current procedure for arbitral appointments may generate pressures for arbitrators to act in a certain way.[695] For example, Van den Berg acknowledges that the current procedure of appointments encourages arbitrators to compete for future appointments. This may incentivize arbitrators to issue dissenting opinions so as not to "disappoint" their appointer and to enhance a chance for future reappointments.[696]

This phenomenon generates a perception of arbitral bias, "a cognitive predisposition to favor the appointing party".[697] Admittedly, the investment arbitration literature does not offer any conclusive evidence of systematic bias. So far, only two

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right to appoint an arbitrator, that the arbitrators may be compete for future appointments and in order not to "disappoint" its appointer are ready to dissent in each case. This of course is relationship of dependency of the arbitrators from their appointers. Van Den Berg acknowledges it as well. Albert Jan van den Berg, "Charles Brower's Problem with 100%— Dissenting Opinions by Party-Appointed Arbitrators" in David Caron et al, eds, *Investment Arbitration in Practicing Virtue: Inside International Arbitration* (Oxford: Oxford University Press, 2015). Albert Jan van den Berg, "Dissenting Opinions by Party-Appointed Arbitrators in Investment Arbitration" in Mahnoush Arsanjani et al, eds, *Looking to the Future: Essays on International Law in Honor of W Michael Reisman* (The Hague: Martinus Nijhoff, 2011) at 821–43. Note:

[693] Van den Berg (2011), at 825-826.

[694] *Ibid*.

[695] *Ibid*

[696] *Ibid*.

[697] Sergio Puig & Anton Strezhnev, "Affiliation Bias in Arbitration: An Experimental Approach" (2017) 46:2 J Leg Stud 371 at 371.

empirical studies appear to show some alarming results. The first study, by Van Harten, suggests that arbitrators tend to affirm jurisdiction over disputes in an expansive fashion, a trend that favours investors.[698] The second, by Puig and Strezhnev, finds that "the frequent use of party-appointed arbitrators is likely to result in litigant-induced biases".[699] Disentangling selection effects (parties appointing friendly arbitrators) from affiliation effects (arbitrators changing their behavior in response to who appointed them) is particularly challenging using observational data".[700] These authors acknowledge some practical limitations of their studies. Van Harten's study cannot take into account all legal and factual differences in the investment disputes that may influence how the ISA tribunals determine jurisdiction. Puig's and Strezhnev's study admits an inability to "assess exactly how implicit biases of individual arbitrators affect outcomes of a body issuing a collective decision".[701] On the basis of previous social sciences studies, however, Puig and Strezhnev, observe that "in deliberations, biases tend to be reinforced—the bias-accentuation effect".[702] This means that "the implicit biases of the two party-appointed members may not simply cancel one another out, as often assumed, but rather may become further entrenched throughout the arbitration process".[703]

However, even the mere perception of bias may be detrimental to the credibility of the investment regime. In words of Lord Hewat, "it is not merely of some importance but is of fundamental importance that justice should not only be done, but should

[698] Gus Van Harten, *Sovereign Choices and Sovereign Constraints: Judicial Restraint in Investment Treaty Arbitration* (Oxford: Oxford University Press, 2013) at 107.
[699] Puig & Strezhnev (2017), at 393
[700] *Ibid*.
[701] *Ibid* at 392.
[702] *Ibid* at 393.
[703] *Ibid*.

manifestly and undoubtedly be *seen* to be done".[704] Grosstand and Black explain that "perceptions of procedural fairness strongly impact perceptions of substantive fairness, which results in a greater willingness to comply with the outcome and greater trust in and respect for the decision-maker".[705] When the parties question the neutrality of arbitrators, this jeopardizes the whole system of arbitration.

3.2 "Exit", "Voice" and "Loyalty" in Responses of States

States respond to new developments in the investment arbitration case law with a variety of actions.[706] The lens of a political system reflects this reality in its concept of the feedback that states generate in response to the actions of other participants.[707] States can change their approaches to law-making as a result of "observing and interpreting experiencies" that surround them (Bayesian updating).[708] This learning curve "is biased

[704] R v Sussex Justices, ex p McCarthy [1924] 1 KB 256, 259. [Emphasis added]
[705] Jill Grosstand & Barbara Black, "When Perception Changes Reality: An Empirical Study of Investors' Views of the Fairness of Securities Arbitration" (2008) 2 J Disp Resol 349 at 356. See also Susan Franck, "Integrating Investment Treaty Conflict and Dispute System Design" (2007) 92:1 Minn L Rev 161 ("empirical evidence suggests that when stakeholders believe a system is procedurally just, they are more likely to buy into the result and the process, comply with the outcome, comply with the law in the future, increase commitment to the organization, accord respect and loyalty to the institution, and perceive the system to be legitimate").
[706] Wolfgang Alschner, "The Impact of Investment Arbitration on Investment Treaty Design: Myth versus Reality" (2017) 42:1 Yale J Intl L 1 ("states systematically react to arbitral case law points to the type of legal innovation that states do engage in. They fine-tune existing treaty commitments in light of legal developments, investing in the gradual adjustment of the field rather than its reinvention" […]The experience of the United States is the primary showcase for a strong impact of investment arbitration on rulemaking. In 1999, soon after it faced its first investment claim under NAFTA in Loewen, 142 the United States halted the negotiation of new investment treaties and initiated a policy review. The outcome of that review was the 2004 Model BIT) at 5, 40-41. Kenneth Vandevelde, "A Comparison of the 2004 and 1994 U.S. Model BITs: Rebalancing Investor and Host Country Interests" in Karl Sauvant, ed, *Yearbook on International Investment Law & Policy 2008-2009* (Oxford: Oxford University Press, 2009) at 283-285, 288-289 (submits that the Loewen case was a turning point for the US to recalibrate its Model BIT and the investment chapters in FTAs in full view that the US can be respondent in potential investment claims). José Alvarez, "The Return of the State" (2011) 20 Minn J Intl L 223 at 260 ("I am not suggesting that all states have been equally empowered, even within the changing investment regime. Sovereign equality, if it ever existed, has not miraculously returned. A more proper, but less catchy, title for this essay might be "the return of some states." The fact that an economic power like the United States is leading the drive to "re-balance" the investment regime is no accident. Moreover, even those states that are re-balancing their BITs are not necessarily doing so in the same way or to the same degree").
[707] Dupont & Schultz (2016), at 9.
[708] Poulsen & Aisbett (2013), at 274.

by cognitive shortcuts".[709] Such biases and shortcuts in principle explain the existing variability of the approaches to the law-making.[710] This section focuses on states' attempts to reassert control over the investment regime, based on their individual and collective experiences with ISA. The phrase "reassertion of control" is a term of art that encompasses the trend for states to rebalance IIAs in a way to safeguard regulatory protection and limit their exposure to investors' claims.[711]

State responses to legitimacy deficits can be conceptualized through Hirschman's theory of "exit, voice, and loyalty", which "serves as a method for understanding the pulls and pushes in and out of organizations".[712] In this approach, the members of an organization who have concerns about it have three options. First, they can leave the organization and cut ties to it. Second, members can stay loyal to the organization and not voice any concerns. Third, they can voice their concerns and demand the changes in the organization. It is worth noting that the members can potentially combine two options.[713]

In the context of the investment regime, Hirschman's theory means that states as participants in the investment regime can opt out from participating in the regime entirely, or in part. If the states choose the "exit" option, they can no longer influence,

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[709] *Ibid*.
[710] *Ibid* at 302. (particularly, level of administrative capacity and level of expertise may be the factors that influence the decision-makers incluindg in drafting and signing BITs)
[711] Andreas Kulick, *Reassertion of Control over the Investment Treaty Regime* (Cambridge: Cambridge University Press, 2016) at 6-7. Jason Yackee, "Controlling the International Investment Law Agency" (2012) 53 Harv Intl LJ 391, 434-436.
[712] Nancy Welsh, Andrea Schneider & Kathryn Rimpfel, "Using the Theories of Exit, Voice, Loyalty, and Procedural Justice to Reconceptualize Brazil's Rejection of Bilateral Investment Treaties" (2014) 45 Wash UJL & Policy 105 at 130.
[713] For example, the members can stay loyal to the organization in principle, but use available means in the organization to introduce the changes. Shareholders can fully abandon a company by selling all their shares, or they can stay loyal to the company, but vote for new directors to ensure that the company changes course. The "exit" option means that the members lose a chance to "voice" their concerns in order to improve the organization.

improve, or reform the regime.[714] The costs of withdrawal from the regime can be unduly high, signaling that a state is an "outsider" not committed to the protection of foreign investments, adversely impacting its eligibility for the development loans or foreign aid.[715]

Alternatively, states can stay loyal to the regime. In this case, loyal states have at least two options. First, they can attempt to reform the regime (i.e. "voice" their concerns). States have "numerous and powerful" options to raise their voices within the investment regime.[716]

Second, states can demonstrate full satisfaction with the regime and refuse to undertake any actions to change it. Such examples are rare but do exist. For example, Bernasconi-Osterwalder explains that despite significant changes in IIAs of many states, the approach of Switzerland to IIAs and their negotiations "remained in large part unchanged in the last decades".[717]

The task of this section is to examine how states have responded to legitimacy deficits of the investment regime. It has two limitations. First, it considers only state responses in treaties negotiated after Phillip Morris filed its claim against Australia. This

[714] Tanya Voon, Andrew Mitchell & James Munro, "Parting Ways: The Impact of Investor Rights on Mutual Termination of Investment Treaties" (2014) 29:2 ICSID Rev 451 at 452. Jane Kelsey, "Towards a New International Investment Paradigm? Taking the BRICS Seriously" (2015) 21:4 New Zealand Business Law Quarterly 328. Clint Peinhardt & Rachel Wellhausen, "Withdrawing from Investment Treaties but Protecting Investment" (2016) 7:4 Global Policy 571.

[715] Schneiderman (2013), at 41, 62.

[716] Anna Katselas, "Exit, Voice, and Loyalty in Investment Treaty Arbitration" in Shaheeza Lalani & Rodrigo Lazo, eds, *The Role of the State in Investor-State Arbitration* (The Hague: Martinus Nijhoff, 2015) at 216. (States can draft the provisions of the IIAs with greater precision to resolve ambiguities in investment standards. They can incorporate exceptions into IIAs to limit the scope of investment protection. They can establish an appeal mechanism to resolve the problem of contradictory decisions or incorporate procedural safeguards, such as security of tenure to protect the impartiality and independence of ISA arbitrators).

[717] Nathalie Bernasconi-Osterwalder, "Switzerland's Investment Treaties: Time for a Change" (2016) IISD, online:< https://www.iisd.org/itn/2016/05/16/resources-and-events-19/>. (It is worth noting that Switzerland had little experience as a respondent in the investment disputes. Accordingly, it is plausible to suggest that the experiences of states as the respondents influence their approaches to the investment regime, particularly whether they select "exit", "voice" or "loyalty" options).

does not mean that before the Phillip Morris claim, the regime had no legitimacy issues. However, it is logical to overview states' responses after the claim, because it generated a major public outcry against the investment regime.[718]

The next section will proceed by first examining the "exit" option, forcusing on the conditions under which states have decided to leave the investment regime. Second this section will examine the "voice" option to discuss the current approaches of states to reforming the investment regime.

3.2.1 Examining the "Exit" Option in the Practice of States

The "exit" option is a radical choice not to be taken lightly or frequently, but it remains an available option.[719] States can declare their exit from the regime by formally denouncing the ICSID Convention and by terminating their IIAs.[720] For example, in May 2007, Bolivia notified the ICSID Centre of its withdrawal from the ICSID Convention pursuant the procedure under article 71 of the Convention.[721] According to article 71, the state parties to the Convention "may denounce this Convention by written notice to the depositary of this Convention. The denunciation shall take effect six months after receipt

[718] Nottage (2009), at 20.
[719] Andrea Carska-Sheppard, "Issues Relevant to the Termination of Bilateral Investment Treaties" (2009) 26 J Int Arb 755. Norton Rose Fulbright, Indonesia Signal Intention to Terminate More than 60 Bilateral Investment Treaties (2014), online:<http://www.nortonrosefulbright.com/knowledge/publications/116101/indonesia-signals-intention-to-terminate-more-than-60-bilateral-investment-treaties>. Intl Inst Sustainable Dev, South Africa Begins Withdrawing from EU-Member BITs, Investment Treaty News (2012), https://www.iisd.org/itn/2012/10/30/news-in-brief-9.
[720] Tania Voon & Andrew Mitchell, "Denunciation, Termination and Survival: The Interplay of Treaty Law and International Investment Law" (2016) 31:2 ICSID Rev 413 at 416-417.
[721] Matilde Recanati, "Diplomatic Intervention State to State Arbitration" in Giorgio Sacerdoni et al, eds, *General Interests of Host States in International Investment Law* (Cambridge: Cambridge University Press, 2014) at 424. Julien Fouret, "Denunciation of the Washington Convention and Non-Contractual Investment Arbitration: "Manufacturing Consent" to ICSID Arbitration" (2008) 25:1 Intl Arb 71 at 72. José Carlos Bernal Rivera, "Life after ICSID: 10th anniversary of Bolivia's Withdrawal From ICSID" (12 July 2017), Kluwer Arbitration (blog), online:< http://arbitrationblog.kluwerarbitration.com/2017/08/12/life-icsid-10th-anniversary-bolivias-withdrawal-icsid/>.

of such notice".[722] Filing of such notice by Bolivia was a powerful political act that showed Bolivia's rejection of the investment regime as it currently stands.

A state's commitment to the "exit" option also depends on the ideological position of the domestic government. A change of government can result in dramatic and immediate shifts toward or away from the investment regime. For example, Ecuador chose to terminate its BITs after its experience as a respondent state in a dispute with Occidental Petroleum, which resulted in US$ 1,769,625,000 (plus interest) awarded in favour of the investor.[723] The President of Ecuador established the Commission for the Integral Citizens' Audit of the Treaties of Reciprocal Protection of Investments and of the International Arbitral System on the Subject of Investments (CAITISA), to conduct the comprehensive audit of Ecuador's international investment commitments.[724] Later, however, Ecuador's termination policy was revisited and the country reportedly began negotiations toward new BITs.[725]

The denunciation of the ICSID Convention under article 71 has a limited effect due to the provisions of article 72[726] which provides that the denunciation "shall not affect the rights or obligations under this Convention of that State […] arising out of consent to the jurisdiction of the Centre given by one of them before such notice was received by the depositary".[727] Ecuador and Venezuela followed the path of Bolivia and

[722] ICSID Convention at art.71.
[723] *Occidental Petroleum Corporation v Republic of Ecuador* (2012), Award ICSID Case No. ARB/06/11 (International Centre for the Settlement of Investment Disputes) (Arbitrators: Yves Fortier, David Williams, Brigitte Stern) at para.876 (v).
[724] IISD, Ecuador Denounces its Remaining 16 BITs and Publishes CAITISA Audit Report, online:< https://www.iisd.org/itn/2017/06/12/ecuador-denounces-its-remaining-16-bits-and-publishes-caitisa-audit-report/>.
[725] Tom Jones, "Ecuador Begins Talks Over New Bilateral Investment Treaties" Latin Lawyer (27 February 2018).
[726] Victorino Tejera, "Unraveling ICSID's Denunciation: Understanding the Interaction Between Articles 71 and 72 of the ICSID Convention" (2014) 20: 3 ILSA Journal of International & Comparative Law 423.
[727] *ICSID Convention* at art.72.

also denounced the Convention.[728] It is worth noting that "requests for arbitration have been filed against Bolivia and Ecuador, on the basis of Article 72, after their denunciations of the ICSID, and even after such denunciations became effective".[729]

It may be also that termination of BITs or exit from the ICSID Convention serves as a response to the concerns of the domestic constituencies. The termination of IIAs may be a politically powerful statement that shows states' unwillingness to cope with the existing regime's deficits. From a legal perspective, termination and denunciation of IIAs and ICSID have no immediate effect and thus are not a fast track exit from the investment regime. Most IIAs incorporate "survival clauses", provisions that keep IIAs alive for a period of 10-20 years after the IIA termination and that permit foreign investors to invoke the IIAs' protections for investments that existed prior to the termination.[730]

Not all states have made such extreme choices. The investment treaties permit both carve outs and exceptions that may be viewed (if adopted) as an intent to exercise partial "exit". Alternatively, such partial measures can be envisaged as the "voice" option

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[728] Matilde Recanati, "Diplomatic Intervention and State-to-State Arbitration as Alternative Means for the Protection of Foreign Investments and Host States' General Interests" in Giorgio Sacerdoti et al, eds, *General Interests of Host States in International Investment Law* (Cambridge: Cambridge University Press, 2014) at 424. Tolga Yalkin, Ecuador Denounces ICSID: Much Ado About Nothing?, online:< https://www.ejiltalk.org/ecuador-denounces-icsid-much-ado-about-nothing/>.

[729] Leonie Timmers, "The Protection Against Expropriations in Venezuela: a Right to Property in Theory?" in Freya Baetens, ed, Investment *Law Within International Law: Integrationist Perspectives* (Cambridge: Cambridge University Press, 2013) at 149.

[730] UNCTAD, Denunciation of the ICSID and BITs: Impact on Investor-State Claims, online:< http://unctad.org/en/Docs/webdiaeia20106_en.pdf> at 3-4. Tania Voon & Andrew Mitchell, "Ending International Investment Agreements: Russia's Withdrawal from Participation in the Energy Charter Treaty" (2017) 111 AJIL Unbound 461 (discussing survival clauses in the context of Russia's withdrawal from Energy Charter Treaty in light of Yukos case). "Latvia to Terminate Bilateral Investment Treaties with Poland, Czech Republic at EU Request", online:< http://www.baltic-course.com/eng/baltic_states/?doc=137320>. (in 2018, Poland and Czech Republic moved to terminate their reciprocal BITs to comply with the regulations of EU on investments. Interestingly, before the termination of their BITs, the states chose to amend the treaty by removing the "survival clause" to preclude the application of the BITs' provisions for a period of 10 years for pre-existing investments. The Poland-Czech Republic example presents a path for states who prefer a more expedient option of exit from the investment regime. It is, however, necessary to note that such an "exit" requires the consent of both state parties to accomplish).

because states remain committed to the investment regime but yet signal the need for change. For example, the Australian government exercised a "partial exit". In April 2011, the Government of Australia made a declaration that it will cease including the ISA clauses in its IIAs.[731] Kurtz explains the context of this decision.[732] According to Kurtz, at least three factors influenced the Australian Government. First, "the findings of the Australian Productivity Commission (Commission) in its November 2010 Research Report on Bilateral and Regional Trade Agreements" played an important role.[733] The Commission found that bilateral agreements are in principle problematic because they jeopardize the cooperation under multilateral frameworks such as WTO. Kurtz concludes that, "[c]onsistent with the Commission's analysis, the Australian Government is now sceptical of the latter as mechanisms to achieve meaningful trade liberalization".[734] Second, the Commission "received no feedback from Australian businesses or industry associations that ISDS [investor-state arbitration] was of much value or importance to them".[735] Third, "during the period of the Productivity Commission's inquiry, the Australian Government had announced its decision to introduce new public health regulations directed at cigarettes".[736]

After the Government introduced its regulatory measure, Phillip Morris "quickly launched investor–State arbitral proceedings against the Act under the *Hong Kong–Australia BIT* in late June 2011".[737] The initiation of the claim contributed to the "the

[731] Australian Government, Department of Foreign Affairs and Trade, Gillard Government Trade Policy Statement: Trading Our Way to More Jobs and Prosperity 14 (April 2011).
[732] Jurgen Kurtz, "Australia's Rejection of Investor-State Arbitration: Causation, Omission and Implication" (2012) 27:1 ICSID Rev 65.
[733] *Ibid* at 66-67.
[734] *Ibid* at 68.
[735] *Ibid*.
[736] *Ibid* at 70.
[737] *Ibid* at 71.

Australian Government's sudden hostility to investor–State dispute settlement".[738] However, after a change of government, the rigid position of the Australian Government on ISA shifted.[739] Australia now follows a case-by-case approach to incorporating ISA clauses in its IIAs.[740] As has been mentioned, Australia led the efforts to carve out tobacco products from the TPP.[741] The position of Australia is still a remarkable illustration of partial "exit" from the investment regime.

3.2.2 Examining the "Voice" Option in the Practice of States

In response to legitimacy deficits, states can recalibrate their IIAs.[742] First, this section discusses how states have clarified the scope of investment protection in IIAs. Second, it reviews institutional changes in some of the recently-negotiated treaties. Third, it examines the "filters" that many IIAs establish to limit access to the regime.

3.2.2.1 Clarifying the Scope of Investment Protection in Investment Treaties

This section briefly overviews four types of responses of states that aim to clarify the scope of investment protection in their investment treaties. First, states sometimes incorporate more meticulous language in IIAs to clarify (and usually narrow) the scope of investment standards. Second, states add carve-outs to exclude specific industries from access to the investment regime. Third, states can reinforce IIAs with right-to-regulate provisions. Finally, states empower joint treaty commissions to issue interpretations of

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[738] *Ibid* at 70.
[739] Trakman (2014), at 152. Leon Trakman, "Investor State Arbitration or Local Courts: Will Australia Set a New Trend?" (2012) 46:1 J World Trade 83 at 85.
[740] *Ibid*.
[741] Mikael Rask Madsen, "The European Court of Human Rights and The Politics of International Law" in Wayne Sandholtz & Christopher A. Whytock, eds, *Research Handbook on the Politics of International Law* (Northampton: Edward Elgar Publishing, 2017) at 330.
[742] Tomer Broude, Yoram Haftel & Alexander Thomson, "Who Cares About Regulatory Space in BITs? A Comparative International Approach" in Anthea Roberts et al, eds, *Comparative International Law* (Oxford: Oxford University Press, 2018) at 530. (state that some states (but not all) decide to recalibrate their treaties in the systemic way).

their IIAs. Of course, these measures may not be isolated from each other and IIAs could incorporate all of them. This section, however, reviews each of these measures separately to illustrate them clearly.

3.2.2.1.1 Greater Precision in the Content and Scope of Investment Standards

This section examines an emerging approach to drafting investment standards with "greater precision". As discussed in Chapter Two, many IIAs, especially the early ones, incorporated remarkably vague or ambiguous investment standards. For example, in the *Australia – Hong-Hong BIT* (1993), FET, simply required a state to treat foreign investor "fairly" and "equitably". This BIT never clarified what either term means.

As might be expected, such language creates practical problems. ISA tribunals have to interpret and apply the standards according to articles 31-33 of VCLT.[743] The VCLT requires treaties to be interpreted in good faith, according to the ordinary meaning of the terms and the object and purpose of the treaty. Of course, these are only general rules that guide tribunals to a limited extent. Accordingly, the ISA tribunals make their decisions on the basis of general rules and ambiguously formulated investment standards.

The more specific language in newly-negotiated treaties addresses the problem of the far-reaching discretion of ISA tribunals in determining the scope of the applicable investment standards. For example, CETA, TTIP, and TPP explicitly list what types of conduct may or may not constitute a violation of FET. Henckels explains that more precise language in IIAs places "greater constraints on the decision-making criteria that

[743] Joost Pauwelyn & Manfred Elsig, "The Politics of Treaty Interpretation: Variations and Explanations across International Tribunals" in Jeffrey Dunoff & Mark Pollack, eds, Interdisciplinary *Perspectives on International Law and International Relations: the State of the Art* (Cambridge: Cambridge University, 2013) at 448.

they [ISA tribunals] employ".[744] Conceptually the premise that justifies greater specificity in investment standards is that states will ensure that IIAs operates exactly as intended since tribunals will have no room to reach different interpretations.

More rigid formulations of investment standards may be undesirable to both states and investors.[745] First, the level of protection for foreign investors may decrease. More rigid investment standards mean that foreign investors may be declined protection under the investment regime, which they could have obtained under more flexible investment standards. From the perspective of home states whose investors frequently bring claims in ISA, such an outcome may be not desirable. Without access to treaty-based investment protection, investors will lobby the governments of their home states for protection, an approach that might herald a return to the era of gunboat diplomacy. Second, specific investment standards can signify an attempt to reverse the delegation of authority from the arbitral tribunals back to states. This echoes the early 20th century international relations theory of power politics, which viewed courts as mere state agents whose decisions reflected their national concerns.[746] Adoption of such power politics perspectives threatens the whole international rule of law and may result in the escalation of international tensions that will diminish the chance that states will be able to resolve disputes through peaceful means.

Despite changes in IIAs, commentators observe that *in practice* new ILAs still fall short in resolving ambiguities in the formulation of investment standards. For example, Van Harten suggests that the fact that FET in CETA is now linked to the international

[744] Henckels (2016), at 19, 27–50, 31-32.
[745] Reisman (2015), at 618-620.
[746] Alter (2014), at 113-115.

minimum standard of treatment is not a sufficient level of precision.[747] The content of MST is in itself a subject of vigorous debate in scholarship and arbitral practice. Hence, the linkage between MST and FET does not eliminate uncertainty and leaves tribunals plenty of room for maneuvering. It is worth noting that even if states exercise greater precision in the drafting process, the language of investment standards will always remain uncertain to some extent.[748] Judge Higgins notes that,

> [r]eference to the 'correct legal view' or 'rules' can never avoid the element of choice (though it can seek to disguise it), nor can it provide guidance to the preferable decision. In making this choice one must inevitably have consideration for the humanitarian, moral, and social purposes of the law.[749]

Judge Schwebel arrives at a similar conclusion, that "applying rules always involves a certain degree of choice".[750] This conclusion raises a number of issues worth examining. First, to what extent is greater precision in drafting investment rules *ex ante* are useful to specify the scope of the investment standards. The value of greater linguistic precision is that it limits "delegated interpretative authority".[751] Such delegation has political significance because "it introduces an independent outside actor with the legal authority to say what international law means".[752]

Second, there are limitations to any drafting exercise that aims to define the scope of legal norms. To some extent these legal norms will always remain imprecise as it is

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[747] *Ibid*.
[748] Karton (2017), at 247-248.
[749] Rosalyn Higgins, *Problems & Process: International Law and How We Use It* (Oxford: Oxford University Press, 1994) at 5.
[750] Stephen Schwebel, "The Outlook for the Continued Vitality, or Lack Thereof, of Investor-State Arbitration" (2016) 32:1 Arb Intl 1 at 7.
[751] Duncan Hollis, "Sources in International Theories: An Interdependent Relationship" in Jean D'Aspremont, Samantha Besson & Sévrine Knuchel,eds, *The Oxford Handbook on the Sources of International Law* (Oxford: Oxford University Press, 2017) at 438.
[752] Alter (2014), at 9.

impossible to predict and provide for all possible situations in which they might apply. However precisely drafted, legal norms will still require the adjudicators to exercise discretion. Without acknowledging that such limitations exist, our understanding of adjudication will be constrained by the inaccurate perception that adjudicators (judges or arbitrators) apply legal norms in a purely mechanical fashion.[753] As Karton aptly concludes, "[t]his view is at best misguided and at worst wilfully obtuse".[754]

3.2.2.1.2 Mandatory Interpretations of Joint Treaty Bodies

Joint commissions and committees are empowered by state parties to issue binding interpretations of IIA provisions. For example, CETA, NAFTA, TPP and ASEAN–*Australia–New Zealand FTA* (AANZFTA) establish specialized commissions that can issue binding interpretations of IIAs' standards.[755] Similarly, NAFTA establishes a joint commission empowered to render *ex post* interpretations of NAFTA's Chapter 11 provisions.[756] According to article 1131(2) of NAFTA, the interpretation notes issued by the Comission constitute governing law and are binding upon the tribunals.[757] However, even in absence of article 1131(2), the joint commission's interpretations would be binding upon the tribunal according to VCLT art.31(3)(a). Accordingly, for IIAs that contain no equivalent to NAFTAart. 1131(2), joint commissions would still be effective to bind tribunals to the interpretations they issue by virtue of the general interpretive provisions of the VCLT.[758]

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[753] Schwebel (2016), at 7.
[754] Karton (2017), at 248.
[755] Eleni Methymaki & Antonios Tzanakoupolous, "Masters or Puppets: Reassertion of Control Through Joint Investment Treaty Interpretation" in Andreas Kulick, ed, *Reassertion of Control over the Investment Treaty* (Cambrdige: Cambridge University Press, 2016) at 163.
[756] NAFTA at art.1131(2).
[757] *Ibid*. ("An interpretation by the Commission of a provision of this Agreement shall be binding on a Tribunal established under this Section").
[758] VCLT at art.31(3) (a).

These commissions are usually composed of senior public officials of the state parties to the treaty. All representatives must arrive at a common understanding of IIAs to issue a joint mandatory interpretation. The interpretations of the joint commissions useful for states to keep control over the meaning of the investment standards, after the IIA entered into force. It is worth noting that such Commissions are rare in practice. The reason may be that state parties to IIAs are unable or unwilling to agree unanimously on the scope of the standards or the approaches to their interpretation, and instead prefer to rely the tribunals as an independent source of interpretive authority. While the joint treaty bodies can potentially promote clarity in ISA, their very existence seems to create a tension with investment tribunals. The tribunals exercise their adjudicatory authority independently of the parties (at least in theory); through the joint treaty bodies, by contrast, the treaty parties retain for themselves the power to control how the tribunals interpret and apply the applicable treaty, so long as they are able to act in concert.[759] As soon as the tribunal exercises "too much independence" (in view of the state parties, of course), its authority can be immediately curtailed even with respect to pending cases via mandatory interpretation by the parties.[760]

3.2.2.1.3 Exceptions and Carve-Outs

In several recently-negotiated IIAs, the state parties included exceptions and carve-outs. Carve-outs exclude certain industries by preventing them from filing a claim in ISA. Exceptions exclude particular subject-matters, such as taxation, from investment

[759] Roberts (2010), at 180-181 (in her seminal article, "Power and Persuasion", Roberts discusses this tension between tribunals and states parties).
[760] Methymaki & Tzanakoupolous (2016), at 163-165. It can be argued that such situation puts guarantees of investment protection in jeopardy because the tribunals will essentially follow what states' parties mandate.

protection. For example, CPTPP includes a carve-out for the tobacco industry.[761] In some IIAs, states incorporate exceptions that exclude certain subject-matter from arbitrability in ISA. For example, article 2 of the *Nigeria-Singapore BIT* explicitly excludes tax matters from protection.[762] The *Agreement Between Canada and Mongolia for the Promotion and Protection of Investments* establishes that certain provisions such as Most-Favoured Nation (MFN) and National Treatment (NT) do not apply to matters of taxation.[763]

These exceptions permit states to avoid arbitrations over certain categories of regulatory measures. The issues covered by these exceptions are limited, and can include also prudential measures[764] and financial services.[765] Unsurprisingly, these policy areas are heavily regulated and, if they are not excluded from ISA, would easily expose states to multiple claims by investors. To limit such exposure, states can include exceptions for these subject-matters in their IIAs.

Under exceptions and carve-outs only certain policy matters and industries are excluded from the investment regime. In practice, this means that carve-outs and

[761] TPP at art. 29.5 of the TPP ("A Party may elect to deny the benefits of Section B of Chapter 9 (Investment) with respect to claims challenging a tobacco control measure of the Party. Such a claim shall not be submitted to arbitration under Section B of Chapter 9 (Investment) if a Party has made such an election. If a Party has not elected to deny benefits with respect to such claims by the time of the submission of such a claim to arbitration under Section B of Chapter 9 (Investment), a Party may elect to deny benefits during the proceedings. For greater certainty, if a Party elects to deny benefits with respect to such claims, any such claim shall be dismissed).
[762] *Investment Promotion and Protection Agreement between the Government of the Federal Republic of Nigeria and the Government of the Republic of Singapore* (2016), at art.2.
[763] *Agreement Between Canada and Mongolia for the Promotion and Protection of Investments* (2016), at art.16(7).
[764] Andrew Mitchell, Jennifer Hawkins & Neha Mishra, "Dear Prudence: Allowances under International Trade and Investment Law for Prudential Regulation in the Financial Services Sector" (2016) 19 Journal of International Economic Law 787 at 788, 798-81.("Prudential measures are regulatory tools employed to 'limit the accumulation of financial risks, in order to reduce the probability and mitigate the impact of a financial crash' […] Some typical examples of prudential measures include minimum capital requirements for banks, risk management tools for banks such as board/senior management oversight, collateral policies for individual lending, and capping loan-to-value ratios to minimize credit risks").
[765] Newcombe & Paradell (2009), at 507.

exceptions are limited in scope. However, these limitations do not mean that these measures are ineffective to preclude excessive ISA litigation. In addition, the carve-outs and exceptions show that states exercise an increased level of caution with respect to ISA. The tendency to include carve-outs and exceptions in recently-negotiated treaties represents an attempt to limit access to the regime.

3.2.2.2 Reinforcing Treaties with the Right to Regulate Provisions

"The right to regulate" has become a buzzword.[766] Catharine Titi explains that the right of states to regulate their economies and socieities "is well entrenched in customary international law" and is to a large extent based on the concept of sovereignty, i.e. the autonomy of states to determine the course of their external and internal affairs.[767] For the purposes of the investment regime, the right to regulate "denotes the legal right exceptionally permitting the host state to regulate in derogation of international commitments it has undertaken by means of an investment agreement without incurring a duty to compensate".[768] According to UNCTAD, most IIAs concluded in 2016 incorporate provisions intended to secure this "right".[769] Most of these IIAs reaffirm the right of state parties to regulate in their preambles and as a separate article.[770] For example, article 8.9 of CETA specifies that "the Parties reaffirm their right to regulate within their territories to achieve legitimate policy objectives",[771] and the Preamble of CETA contains a reference that states recognize that CETA intends "to stimulate

[766] Catharine Titi, *The Right to Regulate in International Investment Law* (London: Bloomsbury Publishing, 2014) at 33.
[767] *Ibid*.
[768] *Ibid*.
[769] UNCTAD 2017
[770] *The Reciprocal Promotion and Protection of Investments Between the Agrentine Republic and the State of Qatar* (2016), at art.10. *Reciprocal Investment Promotion and Protection Agreement between the Government of the Kingdom of Morocco and the Government of the Federal Republic of Nigeria* (2016), Preamble and art.23.
[771] CETA at art.8.9.

mutually‑beneficial business activity, without undermining the right of the Parties to regulate in the public interest within their territories".[772]

European democratic institutions have also weighed in on the matter. With regard to the right to regulate provision in CETA, the European Parliament made a public statement in which it distinguished CETA's approach from that of its predecessors.[773] According to the public statement, earlier treaties "required a state's regulations to be consistent with its obligations under the treaty, in other words the right to regulate did not justify violations of obligations under the treaty".[774] CETA departs from previous treaties by setting the right to regulate as a positive right "specifying that the mere fact of changing a law, adversely affecting the parties' expectations (of profits for example), does not amount to a breach of an investment protection obligation".[775]

However, not everyone is optimistic about the legal value of the right to regulate provisions in CETA.[776] According to Van Harten's commentary on the European Commission's statement, "[i]t is insufficient, indeed damaging, to affirm the right to regulate only as part of an aspirational statement in a preamble or elsewhere in the treaty […] the statement must be included in the treaty itself as a substantive right of the state which has been agreed by the states parties".[777] Radi expresses similar opinion. According to him, CETA is "not more protective of the right to regulate than mainstream arbitration practice".[778] Accordingly, reinforcing the right to regulate through the

[772] CETA at Preamble.
[773] European Parliament, CETA: Investment and the Right to Regulate. At a Glance (2017).
[774] *Ibid* at 2.
[775] *Ibid*.
[776] Gus Van Harten, *Comments on the European Commission's Approach to Investor-State Arbitration in TTIP and CETA* (July 3, 2014), Osgoode Legal Studies Research Paper No. 59/2014
[777] *Ibid*.
[778] Yannic Radi, "ESIL Reflection: Much Ado About Nothing'? An Appraisal of CETA's Investment Chapter", ESIL-Sedi (blog), online:< http://www.esil-sedi.eu/node/1743>.

declarations in the preambles and individual aspirational provisions may be not that effective from a legal standpoint.

So far, it is difficult to say whether the new IIAs will be more effective in safeguarding the right of a state to regulate, since there is no arbitral practice under CETA, CPTPP or TTIP. However, some tentative observations are possible. First, the right to regulate in the context of investment regime is both a legal and political matter. States equip their IIAs with the right to regulate provisions to safeguard their regulatory space. This may be a response to past arbitrations, where very sensitive issues of public policy were at stake. It is also worth remembering that some states face strong opposition to IIAs from civil society movements, NGOs and other interest groups. Consequently, the incorporation of right-to-regulate provisions in IIAs may be a way to acquire political capital, for example to "buy off" opposition with a symbolic provision. Second, new IIAs clearly show a shift in the attitudes of states in investment treaty-making, towards a more balanced approach in investment protection. The right to regulate provisions have symbolic value in demonstrating such attitudinal shift. While the preambles in IIAs do not generate binding obligations, the references to the right to regulate in the preambles can be considered by tribunals when they interpret the operative provisions of IIAs.[779]

3.2.2.3 "Filters" to Limit the Access of Foreign Investors to Investor-State Arbitration

This section examines mechanisms that limit access of foreign investors to ISA. These mechanisms include requirements for foreign investors to exhaust local remedies, the establishment of the joint commissions (or committees) for early dismissal of claims, filters against frivolous claims, and finally, restrictions on shell companies.

[779] VCLT at art.31(1)(2). Dolzer & Stevens (1995), at 20.

3.2.2.3.1 Exhaustion of Local Remedies

The requirement to exhaust local remedies is not novel or unique to international investment law.[780] Most international courts and tribunals require claimants to pass through tiers of national courts (and administrative tribunals, as the case may be) before allowing them to file a claim.[781] However, the investment regime has no requirement to exhaust local remedies to access ISA.[782] Historically, the exhaustion of local remedies was deemed ineffective in investment protection because a state that treated a foreigner unfairly would simply continue to do so, or even delay the process to prevent an investor from accessing the international forum.[783]

However, a few early treaties required foreign investors to exhaust local remedies.[784] According to the International Institute for Sustainable Development (IISD), the *Malta–Serbia BIT* (2010), *Bangladesh–UAE BIT* (2011), and *Indian Model BIT* (2015) establish an exhaustion of local remedies requirement for foreign investors.[785] Schreuer argues that this requirement has gone away "for good reasons" and states should "think twice" before including it in IIAs again.[786] According to Schreuer, the reason to

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[780] Chittharanjan Amerasinghe, *Local Remedies in International Law* (Cambridge: Cambridge University Press, 2004). Christopher Dugan et al*, Investor-State Arbitration* (Oxford: Oxford University Press, 2011) at 347.

[781] Jan Ole Voss, *The Impact of Investment Treaties on Contracts Between Host States and Foreign Investors* (The Hague: Martinus Nijhoff Publishers, 2010) at 286. (states that "diplomatic protection is contingent upon the exhaustion of local remedies").

[782] ICSID Convention at art.26 (unless specifically stated in the agreement of the state-parties).

[783] Sornarajah (2010), at 219-220. Voss (2010), at 286-287. UN, *Report of the International Law Commission* (New York: United Nations Publications, 2006) at 83. (The Commission explains that the respondent state may "obstruct" the person from "bringing such proceedings" and,hence, prevent the person from fulfilling the requirement to exhaust local remedies).

[784] *Agreement on Economic Cooperation Between the Kingdom of the Netherlands and Malaysia* (1971), at art.12. *Agreement on Economic Cooperation between the Government of the Kingdom of the Netherlands and the Government of the Republic of Singapore* (1972), at art.XI.
Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Republic of Korea (1974), at art.6.

[785] Martin Brauch, Exhaustion of Local Remedies in International Investment Law (Winnipeg: IISD, 2017).

[786] Christoph Schreuer, "Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration" (2005) 31 Law & Practice of Intl Courts and Tribunals 1 at 16.

fear the revival of the local remedies rule is that "once it is accepted that the investor should make an attempt to local remedies it is only a small step to require that the attempt should not stop at the level of the lowest court".[787] Schreuer's concern is that an investor may be struggling to achieve fair resolution of its case in domestic settings and will be wasting time in the attempts to achieve justice in the national judicial and administrative bodies. In general, the local remedies rule limits foreign investors' claims and allows states to restrict access to ISA.

3.2.2.3.2 Joint Comissions for Dismissal of Claims

This section will examine the provisions in IIAs that permit state parties to jointly dismiss a foreign investor's claim. One recent and remarkable example of this approach is ChaFTA. ChaFTA offers what is called "joint treaty party control" to dismiss claims that challenge public welfare regulations at an early stage in the dispute.[788] ChaFTA provides that if an investor challenges a regulatory measure, the host state may issue a "public welfare notice".[789] In this notice, a host state indicates that a challenged regulatory measure meets a welfare objective and is not discriminatory, and launches a 90 day consultation period with the investor's home state. In cases where both host and home state state agree that the measure pursues welfare objectives and is not discriminatory, they issue a binding decision requiring the tribunal to dismiss the claim.

In any event, "joint party control" is limited to public interest or welfare regulatory actions. In some instances, this mechanism may prove insufficient. If the claim is without merit or constitutes an abuse of process, but does not challenge a public welfare measure, the claim cannot be "filtered" out by the joint commission. Joint treaty

[787] *Ibid* at 15.
[788] Roberts & Braddock (2013).
[789] *Ibid*.

party control may also "serve to politicise investment disputes (negating one of the purported benefits of the system of ISDS)".[790]

3.2.2.3.3 Filters for Frivolous Claims

This subsection presents the mechanisms for early dismissal of frivolous claims as one of the measures that states have undertaken to respond to legitimacy deficits and reassert control in the investment regime. Some recently concluded IIAs feature mechanisms that permit the early curtailment of a claim where it "manifestly lacks legal merit" or is "unfounded as a matter of law". For example, CETA permits states to file preliminary objections to dismiss the claims that are "manifestly without legal merit" [791] and claims in which an award in favour of claimant cannot be made ("unfounded claims").[792] TPP adopts similar approach by allowing the tribunal to decide as a preliminary question whether "a claim submitted is not a claim for which an award in favour of the claimant may be made or [...] or that a claim is manifestly without legal merit".[793]

The rules of procedure of arbitration institutions may also incorporate the mechanisms for dismissing claims without merit early in the proceedings. In 2016, *Arbitration Rules of the Singapore International Arbitration Centre* (SIAC) included provisions on the early dismissals of the claims on the basis that the claim has no legal

[790] Kyla Tienhaara, Inquiry into the China-Australia Free Trade Agreement (ChAFTA), Joint Standing Committee on Treaties, Submission 36, at 8.
[791] CETA at 8.32. CETA sets a strict timeline for the claims by requiring the respondent to file an objection "no later than 30 days after the constitution of the division of the Tribunal, and in any event before its first session".
[792] *Ibid* at 8.33 para.1-2. ("According to CETA, a respondent can raise an objection that a claim is unfounded as a matter of law at "an appropriate time" but "no later than the date the Tribunal fixes for the respondent to submit its counter-memorial").
[793] CPTPP at 9.23.

merit. [794] In 2006, ICSID added to its arbitration rules mechanisms for the early dismissal of claims that manifestly lack merit. Of course, the arbitration institutions are independent participants of the investment regime according to the lens of political system, but it is worth mentioning the ICSID Centre incorporated the rules on the early dismissal of claims manifestly without legal merit only after assessing multiple complaints of governments. The mechanisms for the early dismissal of frivolous claims will be the subject of detailed discussion in Chapter Four of this thesis.

3.2.2.3.4 Restrictions on Claims by Shell Companies

"Shell" companies are frequent claimants in investment disputes. These are corporations controlled by an investor from another state and have no substantial business interest in the state of incorporation.[795] Some IIAs incorporate the denial of benefits clauses to prevent foreign investors from (ab)using corporate nationality planning. For example, the 2012 US Model BIT in article 17(2) establishes that shell companies cannot benefit from the BIT's protection.[796] The *Canada-China BIT* in article 16(2) and the TPP in article 9.14 also incorporate similar denial of benefits provisions.[797] Sornarajah explains that, "[d]enial of benefits provisions found in more recent investment treaties are reactions to the expansionary use of corporate nationality by arbitrators eager to increase

[794] *Arbitration Rules of the Singapore International Arbitration Centre* 2016, (SIAC), online:< http://www.siac.org.sg/our-rules/rules/siac-rules-2016> at Rule 29. Gus Van Harten, "Reforming the System of International Investment Dispute Settlement" in C. L. Lim, *Alternative Visions of the International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2016) at 113. (Van Harten suggests that arbitrators are financially interested in the claim to proceed and thus are not suitable to be in charge of early dismissal).
[795] Baumgartner (2016), at 108.
[796] US Model BIT art 17 (2), online:< https://ustr.gov/sites/default/files/BIT%20text%20for%20ACIEP%20Meeting.pdf>.
[797] Canada-China BIT 2012, online:< http://investmentpolicyhub.unctad.org/Download/TreatyFile/3476>.

the jurisdictional scope of investment arbitration".[798] According to Zaide and Melchionda, "to activate the denial of benefits clause, a state should show that the claimant is owned or controlled by a non-protected investor, ownership and control being disjunctive, not cumulative".[799]

In practice however, denial of benefits clauses have their limitations. Sornarajah explains that ISA tribunals have interpreted denial of benefits in an overly narrow way to permit greater protection of foreign investments.[800] According to Sornarajah, *Liman Caspian Oil v Kazakhstan* illustrates the limited effect of denial of benefits clauses. There, "the tribunal suggested that the respondent state should have been aware of the facts at the time of the request for arbitration and should have raised the issue of denial of benefits at that time and not one year later, during the jurisdictional phase".[801] Sornarajah submits (and I agree) that such reasoning is problematic because it reveals an approach that is "deliberately calculated to ensure that the investor benefits despite the fact that the denial of benefits provision itself was not specified to be time limited".[802]

Similarly, Baumgartner argues that denial of benefits provisions have only limited effect in ensuring that the "real nationals of the other treaty party benefit from the rights in the treaty".[803] It is possible that an entity with "qualifying nationality" under an applicable treaty will be effectively controlled by another person who has "host state

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[798] M Sornarajah, "Good Faith, Corporate Nationality, and Denial of Benefits" in Andrew Mitchell, M Sornarajah & Tania Voon, eds, *Good Faith and International Economic Law* (Oxford: Oxford University Press, 2015) at 137.
[799] Arthur Rovine, Ziade & Melchionda, "Structuring and Restructuring of Investment" in Arthur Rovine,ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (The Hague: Brill, 2015) at 397.
[800] *Ibid*.
[801] *Ibid*.
[802] *Ibid*.
[803] Baumgartner (2016), at 286.

nationality".[804] The key challenge is thus to identify the nationality of corporations where the named investor is an entity that may be owned and controlled by multiple nationals.

3.2.2.4 Institutional Changes: CETA in Focus

There are multiple proposals that advance institutional change of the conventional ISA mechanism.[805] For example, a multilateral investment court for resolution of investor-state disputes could be established,[806] and some commentators argue in favour of an appeal mechanism under the auscpices of the ICSID Centre.[807] This section examines the changes that CETA introduced to provide an example of institutional change. CETA establishes an appeal mechanism, changes the procedure for arbitral appointments, and changes how arbitrators are compensated. These changes can produce legal effects; an appeal mechanism, for example, can lead to greater consistency of arbitral jurisprudence.[808] Cecilia Malmström, a former European Comissioner on Trade, writes:

> My assessment of the traditional ISDS system has been clear - it is not fit for purpose in the 21st century. I want the rule of law, not the rule of lawyers. I want to ensure fair

[804] *Ibid*.
[805] Gabrielle Kaufmann-Kohler & Michele Potestà, The Composition of a Multilateral Investment Court and of an Appeal Mechanism for Investment Awards CIDS Supplemental (2017), online:< http://www.uncitral.org/pdf/english/workinggroups/wg_3/CIDS_Supplemental_Report.pdf >. Bonnitcha, Poulsen & Waibel (2018), at 202-206. Karl Sauvant, ed, *Appeals Mechanism in International Investment Disputes* (Oxford: Oxford University Press, 2008). Stefan Griller, Walter Obwexer & Erich Vranes, *Mega-regional Trade Agreements: CETA, TTIP, and TiSA: New Orientations for EU External Economic Relations* (Oxford: Oxford University Press, 2017).
[806] *Ibid*.
[807] *Ibid*. European Comission, CETA: EU and Canada Agree on New Approach on Investment in Trade Agreement (29 February 2016) Press Release. Stephan Schill, "Luxembourg Limits: Conditions for Investor-State Dispute Settlement under Future EU Investment Agreements" in Marc Bungenberg, August Reinisch, Christian Tietje, eds, *EU and Investment Agreements* (London: Blumsbury, 2013) at 37. August Reinisch, "The European Union and Investor-State Dispute Settlement: From Investor-State Arbitration to a Permanent Investment Court" (2016) CIGI Research Paper No.2 (2016) at 20.
[808] Freya Baetens, "Keeping the Status Quo or Embarking on a New Course? Setting Aside, Refusal of Enforcement, Annulment and Appeal" in Andreas Kulick, *Reassertion of Control over the Investment Treaty Regime* (Cambridge: Cambridge University Press, 2016) at 126 ("the creation of an appeal, which would allow appeals against all investment arbitration awards and which would result in binding, authoritative decisions, could increase the consistency of arbitral awards").

> treatment for EU investors abroad, but not at the expense of governments' right to regulate.[809]

The section below examines the appeal mechanism and the changes to the appointment and the remuneration procedures, which are the three most significant changes that CETA introduced.[810]

3.2.2.4.1 The Appeal Mechanism

The composition and status of appeal mechanisms under CETA deserve scrutiny. CETA authorizes the parties to investment disputes to bring appeals to an appellate tribunal.[811] The appellate tribunal has the power to overturn awards, including to address errors "in the application or interpretation of applicable law".[812] Such supervision may produce greater consistency in arbitral awards issued under the treaty.[813] Garcia *et al* emphasize that the appeal mechanism, if introduced, can generate "systemic and social benefits that would be profound and wide-ranging", for "enhancing consistency and coherence" within the investment regime.[814]

Nevertheless, the impact of the appeal mechanism under CETA may be limited because CETA is one treaty among numerous IIAs.[815] Since CETA is a recent treaty, it is

[809] Cecilia Malmström, Investments in TTIP and Beyond - Towards an International Investment Court, (2015), (blog).
[810] CETA at art.8.27 para 5.
[811] *Ibid* at art. 8.28.
[812] *Ibid* at art. 8.28, para.2 (a).
[813] In the international economic law context, the WTO Appeal Body gained scholarly praise for ensuring consistent case-practice in trade disputes. The constituency of arbitral practice of course serves for reinforcing the rule of law as the results become more predictable. In the context of frivolous claims, predictability in law's application plays an important role because it gives the tribunal a ground to assert that this particular claim has no chance to succeed on the merit due to the pattern in how legal standards are interpreted and applied. Peter Van den Bossche & Werner Zdouc, *The Law and Policy of the World Trade Organization* (Cambridge: Cambridge University Press, 2013) at 205.
[814] Garcia et al (2015), at 887.
[815] Henckels (2015).

still too early to make conclusions on the potential impact of the treaty on the institutional design of the regime more broadly.[816] It may prove influential or may remain an outlier.

If successful, CETA could serve as a model that may be implemented by other states in their IIAs. For example, the commentators in the field of investment arbitration often refer to the appeal mechanism under the World Trade Organization (WTO) as an example of an appellate body that positively contributes to consistent interpretations of international trade law.[817] The example of CETA's appeal mechanism will be particularly valuable in light of the multiplication of "socket provisions" in recent IIAs.[818] Such provisions allow parties to "plug" the appellate mechanism into existing IIAs if such a mechanism is established by a future agreement between the state parties. Legum explains that socket provisions in IIAs constitute "an "agreement to agree" to have a specified mechanism apply to the IIA following a potential future agreement to that effect.[819] For example, DR-CAFTA provides for "a negotiating group to develop an appellate body or similar mechanism to review awards rendered by tribunals".[820] To author's knowledge, the socket provision in CAFTA has never actually produced an appellate mechanism.

3.2.2.4.2 Appointments

[816] The discussions on the appeal mechanism are not novel. Previously, there were suggestions to incorporate the appeal mechanism clauses in the separate investment treaties and in the ICSID Convention. ICSID Secretariat, "Possible Improvements of the Framework for ICSID Arbitration", Discussion Paper, 22 October 2004; Karl Sauvant & M Chiswick-Patterson, eds, *Appeals Mechanism in International Investment Disputes* (New York: Oxford University Press, 2008).
[817] Raj Bhala, "The Myth About Stare Decisis and International Trade Law (Part One of a Trilogy)" (1999) 14 Am U Intl L Rev 845.
[818] Barton Legum, "Options to Establish an Appellate Mechanism for Investment Disputes" in Karl Sauvant,ed, *Appeals Mechanism in International Investment Disputes Columbia Program on International Investment* (Oxford: Oxford University Press, 2008) at 232.
[819] *Ibid*.
[820] DR-CAFTA at Annex 10.

CETA establishes a "permanent standing tribunal" that replaces the conventional arbitration model, whereby disputes between investors and states are resolved by *ad hoc* tribunals.[821] The adjudicators belonging to this permanent standing tribunal will be appointed by the CETA Joint Committee,[822] which in turn consists of representatives of the EU and Canada. It will appoint 15 adjudicators to renewable five-year terms.[823]

Under the conventional approach in ISA, the disputing parties (i.e. investors and respondent states) select the arbitrators. CETA departs from this approach and, instead, requires the president of the tribunal (a national of a third country) to select arbitrators from the standing tribunal to adjudicate disputes. CETA also changes the structure of compensation for adjudicators by providing that they will be paid a retainer to keep themselves available for adjudicating disputes. VanDuzer explains that "the Joint Committee is specifically empowered to transform the compensation arrangements into regular salary if it decides that would be more appropriate".[824] This means that these arrangements, while they differ from arbitration arrangements, do not transform the arbitrators into tenured judges. A retainer makes the arbitrators available for CETA's cases, but they would still "have a financial interest in substantial increases in the number of cases overall leading to more work for all members of the tribunal".[825]

3.3 Concluding Remarks

Deficits of legitimacy are perceived to persist at all levels of the investment regime. The vertical critiques question the suitability of the investment regime to

[821] Armand De Mestral & Lukas Vanhonnaeker, *The Impact of the NAFTA Experience on Canadian Policy Concerning Investor-State Arbitration* (2016), CIGI Research Paper No 13 at 5.
[822] CETA at art. 8.27 para.2.
[823] *Ibid* at 8.27 para.5. CETA provides that there will be 5 nationals of the EU, 5 nationals of Canada and 5 nationals of third countries. Individual cases are to be resolved by a panel of three arbitrators
[824] Antony VanDuzer, "Investor-State Dispute Settlement in CETA: Is it the Gold Standard?" (2016) C.D.Howe Institute Commentary No 459.
[825] *Ibid*.

constrain state choices in a "top-down fashion". Horizontal critiques show that the regime reinforces inequality among nations. Ideological critiques challenge the values of the investment regime that are perceived to be motivated by neo-liberal ideology, exemplifying the tension between private capital and public regulation. The rule of law critiques advance charges against procedural and substantial aspects of legal norms and structures within the investment regime.

Legitimacy deficits (perceived or real) have spurred state actions. Hirschman's "exit, voice, and loyalty" rubric is useful to conceptualize what paths states are currently undertaking with respect to the investment regime. Some states prefer to abandon the investment regime entirely; others remain loyal to it. Most states have moved to adopt measures to alter the *status quo* within the investment regime. It is important however to appreciate that states' conduct does not fit neatly in the "boxes" of Hirschman's categories. In particular, partial exit from the regime is a viable option.

Since the legitimacy crisis of the regime is a relatively recent phenomenon, it is hard to appreciate all of its potential effects generally and on individual states. Alschner and Skougarevskiy's study of 2100 IIAs shows that most states appear to follow the "voice-loyalty" option. In other words, most states continue to participate in the investment regime but also raise criticisms and develop different approaches to address gaps in its legitimacy.

For the purposes of this thesis, the overview of the ongoing reform of the international investment regime demonstrates that the materialization of mechanisms for the dismissal of frivolous and abuse of process claims in IIAs and the arbitration rules

constitutes only *one* aspect of many transformative initiatives undertaken by states to respond to the regime's legitimacy deficits.

Chapter 4

Existing Mechanisms for the Dismissal of Frivolous and Abuse of Process Claims in the International Investment Regime

Abuse of process and frivolous claims are well known in domestic legal systems around the world and in international law.[826] This chapter examines frivolous and abuse of process claims in the investment regime. Some IIAs and their arbitration rules incorporate procedural mechanisms for the early dismissal of frivolous claims. For example, the ICC Arbitration Rules permit the expedient dismissal of frivolous claims

[826] Vera Bolgar, "Abuse of Rights in France, Germany, and Switzerland: A Survey of a Recent Chapter in Legal Doctrine" (1975) 35 La L Rev 1015. Glenda Redmann, "Abuse of Rights: An Overview of the Historical Evolution and the Current Application in Louisiana Contracts" (1987) 32 Loy L Rev 946 at 977. Deborah Rhode, "Frivolous Litigation and Civil Justice Reform: Miscasting Problem, Recasting the Solution" (2004) 54: Duke LJ 447. Hersch Lauterpacht, *The Function of Law in the International Community* (Oxford: Oxford University Press, 2011) at 294. Potesta & Sobat (2012), at 137. *Convention for the Protection of Human Rights and Fundamental Freedoms*, opened for signature 4 November 1950, 213 UNTS 221 (entered into force 3 September 1953) (emphasis added). at article 35 (3) ("The Court shall declare inadmissible any individual application submitted under Article 34 if it considers that: (a) the application is incompatible with the provisions of the Convention or the Protocols thereto, manifestly ill-founded or an abuse of the right of individual application"). *Northern Cameroons (Cameroon v UK)* (Preliminary Objections) [1963] ICJ Rep 15, 97 (Separate Opinion Fitzmaurice) 106–07 ("In the general international legal field there is nothing corresponding to the procedures found under most national systems of law, for eliminating at a relatively early stage, before they reach the court which would otherwise hear and decide them, claims that are considered to be objectionable or not entertainable on some a priori ground. The absence of any corresponding 'filter' procedures in the Court's jurisdictional field makes it necessary to regard a right to take similar action, on similar grounds, as being part of the inherent powers or jurisdiction of the Court as an international tribunal"). *United Nations Convention on the Law of the Sea*, opened for signature 10 December 1982, 1833 UNTS 3, 21 ILM 1261 (entered into force 16 November 1994) at article 294 ("Preliminary proceedings" "1. A court or tribunal provided for in article 287 to which an application is made in respect of a dispute referred to in article 297 shall determine at the request of a party, or may determine *proprio motu*, whether the claim constitutes an abuse of legal process or whether prima facie it is well founded. If the court or tribunal determines that the claim constitutes an abuse of legal process or is prima facie unfounded, it shall take no further action in the case. 2. Upon receipt of the application, the court or tribunal shall immediately notify the other party or parties of the application, and shall fix a reasonable time-limit within which they may request it to make a determination in accordance with paragraph 1. 3. Nothing in this article affects the right of any party to a dispute to make preliminary objections in accordance with the applicable rules of procedure"). Tullio Treves, "Preliminary Proceedings in the Settlement of Disputes under the United Nations Law of the Sea Convention: Some Observations" in Nisuke Ando et al, eds, *Judge Shigeru Oda: Liber Amicorum* (The Hague: Kluwer Law, 2002) at 749–61, 751. Eric De Brabandere, "The ICSID Rule on Early Dismissal of Unmeritorious Investment Treaty Claims: Preserving the Integrity of ICSID Arbitration" (2012) 1:9 Manchester J Intl Economic L 23.

and defenses.[827] The ICSID Arbitration Rules authorize early dismissal of claims that manifestly lack legal merit.[828] Other IIAs and arbitration rules also contain provisions that authorize tribunals to dismiss frivolous claims as a preliminary matter. In contrast to frivolous claims, only a few IIAs and no arbitration rules explicitly set out the authority of ISA tribunals to dismiss abuse of process claims. As this Chapter shows, the ISA tribunals however developed a number of conceptual approaches to dismissal of abuse of process claims.

In the investment regime, arbitrators are the "gatekeepers" of the investment regime, in charge of policing frivolous and abuse of process claims.[829] Such design of the mechanisms for dismissal of frivolous and abuse of process claims replicates the design of similar mechanisms in the domestic legal systems where judges are in charge of identifying and dismissing such claims. When these mechanisms were introduced into IIAs, arbitration rules and ISA practice, the question of whether the arbitrators are the appropriate actors to exercise such policing never received critical scrutiny. But arbitrators are not judges and the investment regime structurally makes arbitrators the subjects of a distinct mix of structural tensions and incentives.

This Chapter examines the current state of affairs with regard to the dismissal of frivolous and abuse of process claims. Here, my goal is to underscore the challenges that arbitrators face in identifying frivolous and abuse of process claims in the investment regime and to highlight the cautious approach tribunals are taking on dismissal of such claims. The next chapter will examine the regime's structures and incentives to explain

[827] ICC Arbitration Rules, at art.22. "Note to the Parties and Arbitral Tribunals on the Conduct of the Arbitration under the ICC Rules of Arbitration", (2017) at para.59-64.
[828] ICSID Arbitration Rules at Rule 41(5).
[829] Diane Desierto, "Arbitral Controls and Policing the Gates to Investment Treaty Claims against States in Transglobal Green Energy v. Panama and Philip Morris v. Australia", (22 June 2016) EJIL:Talk (blog).

why, by simply replicating mechanisms from domestic legal systems, states are not likely to resolve the problem of frivolous and abuse of process claims in international investment regime.

This Chapter proceeds in three parts. First, it discusses frivolous and abuse of process claims in domestic legal systems from a comparative perspective. This section explains why legal systems aspire to limit such claims and examines the existing procedural devices that aim to prevent them in different jurisdictions. The objective of this section is to describe such mechanisms and support the argument that international investment law borrowed the design of these mechanisms from domestic legal systems. Second, this chapter examines the process by which ISA tribunals dismiss frivolous and abuse of process claims. Finally, it underlines continuing uncertainties in the investment regime that make the dismissal of such claims problematic. As this chapter shows, arbitrators need "a perfect case" to authorize the dismissal on frivolous and abuse of process grounds.

4.1 Frivolous and Abuse of Process Claims: Background

Frivolous claims and abuse of process claims are well known in civil and common law jurisdictions around the world. This section provides some examples of how domestic legal systems address the problem of frivolous and abuse of process claims. National legal systems employ various procedural mechanisms. This section has two objectives, which are (1) to describe the key features of domestic mechanisms for dismissal of frivolous and abuse of process claims and (2) to highlight that identifying and detecting such claims even in domestic legal systems may be problematic.

Before continuing, two warnings must be made. First, the following analysis is not a comprehensive scrutiny of the domestic legal mechanisms, a task interesting on its own but well beyond the objectives of this dissertation. The focus of this project remains on ISA; the existing legal mechanisms in the domestic jurisdictions are considered only to contextualize that discussion. Second, the rules for the early dismissal of frivolous and abuse of process claims are only presented as they exist "on the books"; no detailed investigation of such rules as they are applied "on the ground" will be attempted.

4.1.1 Frivolous Claims: Overview

This section provides an overview of the procedural tools available in domestic legal systems to curtail frivolous claims and explains why claimants choose to file such claims. The goal of this section is to highlight that the early dismissal of claims may be challenging for national legal systems and to briefly explain the reasons why.

4.1.1.1 Procedural Tools to Curtail Frivolous and Abuse of Process Claims in Civil and Common Law Jurisdictions

Common law jurisdictions employ several procedural devices to combat frivolous claims. These mechanisms include the right of courts to sanction attorneys and their clients for bringing frivolous submissions, to strike out frivolous claims or defences, and to grant summary judgement in cases that lack a legal foundation or where there is no genuine issue for trial.[830]

Frivolous claims are generally perceived as problematic and legal systems provide some procedural tools for early dismissal.[831] For example, in the USA, frivolous litigation

[830] Howard Erichson, *Inside Civil Procedure: What Matters and Why* (The Hague: Wolters Kluwer Law & Business, 2017) at 132. Ontario, *Ontario Rules of Civil Procedure*, RRO 1990, Reg 194, RS at 2.1.01(1), 2.1.01(1)(d), 2.1.02(1). Bernard Cairns, *Australian Civil Procedure* (Thomson Reuters, 2014).
[831] Mathias Reimann, *Cost and Fee Allocation in Civil Procedure: A Comparative Study* (Berlin: Springer, 2011) at 181.

is often perceived as pervasive.[832] In the US context, three provisions of the *Federal Rules of Civil Procedure* (FRCP) are the most relevant to frivolous claims.[833]

First, Rules 12(b)(6) and 12(f) empower defendants to move to dismiss a lawsuit for "failure to state a claim upon which relief can be granted".[834] Second, Rule 56 allows a party to request summary judgement.[835] These rules pursue one main objective, which is to curtail legally non-viable claims in a summary fashion, and thus present procedural devices that the US courts have at their disposal to manage the litigation process.[836] The application of the two rules exists within a broader domestic context of US "multistage" proceedings that enable more effective management of the judicial case load.[837] Kaplow explains that in the US context "the legal proceedings do not commence at the beginning of a trial. Instead, they involve multiple stages, both informal and formal. At various points along the path, a decision is made whether to terminate a case or allow it to continue to the next stage".[838]

Rule 12 and Rule 56 of FRCP must be properly distinguished for greater clarity. They differ both in the stage of the proceedings at which they may be invoked and in the standards for invoking them.[839] The standard for the Rule 12 (b)(6) is known as "plausibility standard for motions to dismiss".[840] To determine the plausibility of a case, the court needs to "(1)[i]dentify allegations that are conclusory, and disregard them for

[832] Alexandra Lahav, *In Praise of Litigation* (Oxford: Oxford University Press, 2017) (provides critical perspective on the outcry that relates to frivolous litigation and argues that curtailment of frivolous litigation may undermine democratic legitimacy).
[833] *Federal Rules of Civil Procedure*, Rule 12(b)(6), Rule 56 and Rule 11 (2017).[FRCP]
[834] FRCP at Rule 12(b)(6). Yoichiro Hamabe, "Functions of Rule 12(b)(6) in the Federal Rules of Civil Procedure: A Categorization Approach" (1993) 15 Campbell L Rev 119 at 125.
[835] Adam Steinman, "The Irrepressible Myth of Celotex; Reconsidering Summary Judgment Burdens Twenty Years After the Trilogy" (2006) 63 Wash & Lee L Rev 81 at 143.
[836] Lous Kaplow, "Multistage Adjudication" (2013) 126:5 Harvard L Rev 1179 at 1181-1183
[837] *Ibid*.
[838] *Ibid* at 1180.
[839] *Ibid*.
[840] *Ibid* at 1181.

purposes of determining whether the complaint states a claim for relief; (2) determine whether the remaining allegations, accepted as true, plausibly suggest an entitlement to relief".[841] Rule 12 (b)(6) provides that the party against whom a claim is brought may move to dismiss the claim at the initial stages of the dispute, before filing its pleading responsive to the claim.[842] Operating at this stage of the proceedings, the motion to dismiss is an important device to save costs because it prevents the claim from proceeding to full-fledged evidentiary discovery. The Rules also provide that "if not excluded by the court, the motion must be treated as one for summary judgement under Rule 56".[843]

Once it has filed its defense on the merits, a respondent can no longer avail itself of Rule 12(6)(b), but it still has an opportunity to rid itself of a frivolous claim. Rule 56 authorizes courts to grant summary judgment, "the procedure by which the court may decide a claim without a trial, where the claimant can show that the defendant has no real prospect of successfully defending the claim".[844] A court may grant summary judgment only "if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law".[845] Accordingly, the standard requires that "a reasonable jury would […] have a legally sufficient evidentiary basis to find for the party on that issue".[846] Rule 56 (b) provides that the "party may file a motion for summary judgment at any time until 30 days after the close of all discovery".[847]

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[841] Daniel Robertson, "In Defense of Plausibility: Ashcroft v. Iqbal and What the Plausibility Standard Really Means" (2010) 38 Pepp L Rev 111 at 159.
[842] *Ibid*.
[843] *Ibid*.
[844] Paula Loughlin Gerlis, *Civil Procedure* (London: Cavendish Publishing, 2001) at 249.
[845] FRCP at Rule 56.
[846] Kaplow (2013), at 1184.
[847] FRCP at Rule 56 (b).

Together, Rules 12(b)(6) and 56 provide respondents and courts with the means to curtail claims expediently at different stages of the process. Rule 12 (b)(6) allows plaintiff to bring the motion at the very outset of the proceedings to prevent discovery, which at least in US civil litigation is typically the most expensive stage of the proceedings. Rule 56 can be triggered at any time until 30 days after the close of discovery. The availability of both procedural devices reinforces the "multistage" approach to the proceedings, and permits more effective management of the caseload of the federal courts.

It is worth noting that application of the Rules 12 and 56 are not without controversy even in the national US context; the standards for disposing of claims have been described as "ambiguous" and employing "open-ended criteria".[848] Yet the courts are not left out entirely in a vacuum, but remain within a legal system that provides clarity through the multiple procedural stages where at each stage the parties can acquire more information, including by reference to prior appellate judgments that clarify the legal standards.[849] In all summary cases, courts must specify the reasons for granting summary judgment. It is worth noting that the summary judgment rule may be a subject of tactical abuse by the defendant, in particular "[a]t a very early stage of the litigation, a defendant might try to subject the claimant to pressure by requiring him to show that his claim can be sustained".[850]

The thid rule of the FRCP relevant to frivolous claims does not permit dismissal of these claims, but instead is intended to deter them. In particular, Rule 11 permits the

[848] Kaplow (2013), at 1185.
[849] *Ibid* at 1186.
[850] Neil Andrews, *English Civil Procedure: Fundamentals of the New Civil Justice System* (Oxford: Oxford University Press, 2003) at 507.

courts to sanction attorneys, law firms, and parties for bringing lawsuits that contain frivolous arguments, lack factual foundation, attempt to harass another party, or otherwise needlessly increase the cost of litigation.[851]

Similar provisions exist in other jurisdictions. For example, in Australia, courts can strike out "a frivolous […] statement of claim or defence".[852] The courts also can grant summary judgment if "there is no real substantial question to be tried".[853] In Canada, rules of civil procedure empower judges to decide whether a claim lacks legal merit or otherwise has no chance of success.[854] For instance, in Ontario, the court has power to dismiss the claim, sanction the attorney who brought frivolous submission, and order the costs against the party that initiated frivolous claim.[855] In Ireland, the court can also "strike out a pleading on the grounds that it discloses no reasonable cause of action or answer or where the action or the defence is shown by the leadings to be frivolous".[856]

Some other types of control powers are granted to courts in different jurisdictions. For example, in England and Wales, the courts possess an inherent power to "dispose of vexatious litigation".[857] Vexatious litigants can be prohibited from launching new claims without specific authorization. The Government of the United Kingdom also keeps a

[851] FRCP at Rule 11. See Jessica Winn, "A Firm Law for Sanctions: Taking a Stance on Whether 28 U.S.C. § 1927 Should Apply to Law Firms" (2016) 73:4 Washington and Lee L Rev 2135 at 2193.
[852] Bernand Cairns, *Australian Civil Procedure* (Sydney: Lawbook, 2002) at 403-404.
[853] *Ibid* at 387. *Australian Can Co Pty Ltd v Levin & Co Pty Ltd* [1947] VLR 332 at 333-334.
[854] Theodore Hirt, "A Second Look at Amended Rule 11" (1999) 48:5 Am Un L Rev at 1007-1052.
[855] *Thompson Bey v Iyer* [2016] FC 990 at paras 8-9. (frivolous and vexatious litigation "clogs the courts and uses up the judicial resources[…] the court has a duty to control access to the judicial system by these types of litigants"). *Ontario Rules of Civil Procedure*, RRO 1990, Reg 194, RS at r 2.1.01(1), 2.1.01(1)(d), 2.1.02(1). Paul Perell & John W Morden, *The Law of Civil Procedure in Ontario* (Markham: LexisNexis, 2010) at 354.
[856] Shelby Grubbs, *International Civil Procedure* (The Hague: Kluwer Law International 2003) at 320.
[857] Neil Andrews, *English Civil Procedure: Fundamentals of the New Civil Justice System* (Oxford: Oxford University Press, 2003) at 218. I.H.Jacobs, "The Inherent Jurisdiction of the Court" (1970) 23:1 Current Legal Problems 23.

written record of vexatious litigants available to the public.[858] From the outset, common law jurisdictions seem to provide tools for the early dismissal of frivolous claims within domestic law and traditionally the courts take the lead in curtailing frivolous claims early in the proceedings.

In civil law jurisdictions, the examination of a claim for its lack of merit is not an issue for summary procedures. Instead, the parties can raise a defence in the proceedings that the claim is frivolous or lacks legal merit. For example, the French legal system allows "a person" to "bring a civil action only if he has a right (*droit*), an interest (*intérêt*), capacity (*capacité*), and is a proper party – that is, has what the French call qualité".[859] The requirement of "intérêt" is "in essence a restatement in different form of the principle that every civil action must be based on substantive right. It is invoked mainly when the courts wish to reject a claim which is not supported by existing law".[860] Defendants may, at any time before the case is ready for judgment, advance a defence that the "plaintiff's action must be dismissed because it is *irrecevable et mal fondee*, thus indicating that defendant's action is procedurally defective and ill-founded on the merits".[861]

A most interesting approach is taken in Quebec in the *Quebec Code of Civil Procedure*.[862] According to the Code,

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[858] UK, UK Government: Vexatious Litigants, online:< https://www.gov.uk/guidance/vexatious-litigants>.
[859] Peter Herzog & Martha Weser, *Civil Procedure in France* (The Hague: Martinus Nijhoff, 1967).
[860] *Ibid* at 241.
[861] Peter Herzog & Martha Weser, *Civil Procedure in France* (The Hague: Martinus Nijhoff, 1967) at 268. *The French Code of Civil Procedure in English* (New York: Thomson Reuters, 2017) at art.122. (For the dismissal of non-meritorious claims, the two provisions of the Code appear to be particularly relevant. Article 122 Summary Declaration of Inadmissibility "the opponent's claim is inadmissible on the grounds that it does not show any cause of action, a locus standi or an interest, or that it is time barred, or is res judicata. Article 71 "any allegation which after an examination of the law on the merits tends to reject the claim of the opponent as being without justification, constitutes a defense").
[862] Rosalie Jukier, "The Impact of Legal Traditions on Quebec Procedural Law: Lessons From Quebec's New Code of Civil Procedure" (2015) 93 La Revue Du Barreau Canadien 2 at 18-19.

> [t]he courts may, *at any time*, *on an application and even on their own initiative*, declare that a judicial application or a pleading is abusive. Regardless of intent, the abuse of procedure may consist in a judicial application or pleading that is clearly unfounded, frivolous or intended to delay or in conduct that is vexatious or quarrelsome. It may also consist in a use of procedure that is excessive or unreasonable or that causes prejudice to another person, or attempts to defeat the ends of justice, particularly if it operates to restrict another person's freedom of expression in public debate.[863]

Accordingly, in Quebec, the judge is in charge of identifying and dismissing a claim as an abuse of process.[864] Most notably, the concept of abuse of procedure in Quebec seems to include frivolous submissions by the party. Three observations can be made about the procedures in Quebec. First, the court can declare the application or pleading to be abusive *at any time*, not only at the preliminary stage. Second, the court can act on an application or *on its own initiative*. This seems to establish the active role of a judge in the process that characterizes civil law systems.[865] The Code, however, does not contain a precise definition of abuse of process, only a list of instances where abuse of process might occur. Such an "absence of definitions of particular words, as found in the Common law statutory mode, is a usual feature of a Civil Code" .[866] Third, the Code appears to categorize frivolous and unfounded submissions as a kind of abuse of process, and does not draw any procedural distinction between the concepts.

It is also worth noting that both civil and common law jurisdictions employ cost-shifting strategies to curb frivolous litigation. For example, in Denmark "attorney's fees

[863] Code de Procédure Civile, at Article 51 Cpc (2016). [emphasis added]
[864] Jukier (2015), at 18.
[865] Geoffrey Hazard, "Discovery and the Role of the Judge in Civil Law Jurisdictions" (1997-1998) 73 Notre Dame L Rev 1017 at 1022.
[866] John Brierley, "The Renewal of Quebec's Distinct Legal Culture: The New Civil Code of Québec" (1992) 42:2 University of Toronto LJ 484 at 491-492.

are structured in a way to protect against frivolous proceedings".[867] The courts in England can make the claimant carry the full costs of the proceedings in case the claim was frivolous.[868] In Portugal, the cost shifting "guarantees access to the law and discourages frivolous […] claims in law and judicial practices".[869] In Canada, "costs sanctions […] are used as behavioural modification devices – to punish litigants who waste court time, party resources, take frivolous and vexatious actions".[870]

Cost-shifting strategies may to be effective because they remove pressure from the courts to identify the frivolity at early stages.[871] Yet such strategies do not clearly deter frivolous litigation altogether. Deborah Hensler explains that "economic theory produces ambiguous outcomes with regard to the effect of cost-shifting on the amount of litigation".[872] Accordingly, cost-shifting can be an effective strategy to handle frivolous claims; it also can increase litigation.

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[867] Christopher Hodges, Stefan Vogenauer & Magdalena Tulibacka, *The Costs and Funding of Civil Litigation: A Comparative Perspective* (London: Bloomsbury Publishing, 2010) at 279.
[868] *Ibid* at 12.
[869] *Ibid* at 467.
[870] *Ibid* at 259.
[871] *Best v Ranking*, [2016] ONCA 492 at para.35-36. (A recent Canadian civil case that imposed costs on the lawyer for advancing 'unreasonable' claims on behalf of the client).
[872] Deborah Hensler, "The United States of America: General Overview and Trends" in Christopher Hodges, Stefan Vogenauer & Magdalena Tulibacka, eds, *The Costs and Funding of Civil Litigation: A Comparative Perspective* (London: Bloomsbury Publishing, 2010) at 543. ("the best empirical test of the effect, the 1980 adoption of fee shifting for medical malpractices cases in Florida, found that fee shifting *increased* litigation, leading to the speedy reversal of the statute"). Clinton Becker & Ariel Katz, "The Incentive Effects of Litigation Fee Shifting When Legal Standards Are Uncertain" (1995) 15 Intl Rev L & Econ 205 at 206. (argues that "the economic literature on cost shifting has instead concluded that the effects of moving to the British rule are theoretically indeterminate, and that both the likelihood and total cost of litigation could increase if it is adopted. It is true that the British rule deters risk-averse litigants and penalizes those who overestimate their chances of victory, as Posner and Landes argued twenty years ago. But if litigants remain overly optimistic notwithstanding the penalty, the British rule will lead them to go to trial more often than under the American rule. Furthermore, the British rule encourages litigants to spend more in cases that they do bring, because the stakes of a lawsuit are higher when costs are included in the award, and because each litigant will discount the expected marginal cost of legal services by the probability that she will prevail"). Jackson Williams "Effects of Attorney Fee Shifting Laws on Claiming Behavior" (2001) 34 Policy Sciences 347-356.

Arguably, common law and civil law jurisdictions employ procedurally distinct approaches with regards to the disposition of frivolous claims *in limine*.[873] However, the common thread is that they all seek to limit such claims by empowering adjudicators to decide which claims are frivolous on a case-by-case basis. But what is the difference between a genuine claim and a frivolous one? How do adjudicators identify frivolous lawsuits and distinguish such lawsuits from other claims?

The precise characteristics of frivolous lawsuits are difficult to identify. In the US context, Yablon explains that these determinations are relative and subjective.[874] He suggests that "decisions to file lawsuits" are "probabilistic decisions made under conditions of uncertainty".[875] He further argues that potential litigants may differently estimate the probability of success of a claim, given that they participate in litigation where the outcome is uncertain and the judicial attitudes play a role in the process of decision-making.[876] Adjudicators can have different "views about the value of adjudication" and as a result "disagree about the conditions for legitimate suits".[877]

Bone submits that "we label a lawsuit 'frivolous' not simply to say something about its merits, but to express a normative judgment that suit should not be brought".[878] Levinson rather pessimistically concludes that "[t]he fascinating thing about the problem of frivolousness is that such cases can be recognized. What cannot be done, I have

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[873] "In limine" means "on or at the threshold; at the very beginning; preliminarily" Black's Law Dictionary, 2nd ed, sub verbo Black's Law Dictionary, 2nd ed, sub verbo, online:< http://thelawdictionary.org/in-limine/>.
[874] Charles Yablon, "The Good, the Bad, and the Frivolous Case: An Essay on Probability and Rule 11" (1996) 44 UCLA L Rev 65
[875] *Ibid* at 92.
[876] *Ibid*.
[877] *Ibid*. Benjamin Barton, *The Lawyer-Judge Bias in the American Legal System* (Cambridge: Cambridge University Press, 2010). Charles Yablon, "The Good, the Bad, and the Frivolous Case: An Essay on Probability and Rule 11" (1996) 44 UCLA L Rev 65 at 94 (arguing that "claims which appear frivolous and baseless in the eyes of one judge may seem respectable losers to others").
[878] Robert Bone, "Modeling Frivolous Suits" U Pa L Rev 519 at 531

discovered, is to explain (or teach to students) exactly what constitutes the frivolous case".[879] There are serious complications that arise in the process of determining whether the lawsuit is frivolous. First, claims may have "varying degrees of legal merit".[880] For example, in *Fox v Vice*, Justice Elena Kagan of the United States Supreme Court underscores that the standards for determining whether the claim is frivolous may be difficult to apply "in real world" where "litigation is more complex" and can include "multiple claims for relief that implicate a mix of legal theories and have different merits. Some claims succeed; others fail. Some charges are frivolous; others (even if not ultimately successful) have a reasonable basis".[881]

Some claims can rest on "fantastical factual allegations" or even "unrecognizable legal theories".[882] Other claims may be "long-shots" that make a somewhat persuasive argument as a matter of law and can succeed given the uncertainty of litigation process.[883] Guthrie makes a useful comparison of long-shot claims to lottery tickets because they offer to the litigant "a chance at greater wealth than the individual is likely to obtain all at once from any other source".[884]

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[879] Levinson (1986), at 378. In the context of criminal law, Hermann makes similar point. Robert Hermann, "Frivolous Criminal Appeals" (1972) 47 NYU L Rev 701 at 705 ("frivolousness, like madness and obscenity, is more readily recognized than cogently defined").
[880] Hersh Lauterpacht, *Development of International Law by International Court* (Cambridge: Grotious Publications, 1958) at 396-397.
[881] *Fox v Vice*, 131 S Ct 2205 (2011) at para.1988 as cited in Stephen Subrin, et al, *Civil Procedure: Doctrine, Practice, and Content* (The Hague: Wolters Kluwer Law & Business, 2016).
[882] Alexander Reinert, "Screening Out Innovation: The Merits of Meritless Litigation" (2014) 89:3 Ind LJ at 1191.
[883] Charles Yablon, "A Dangerous Supplement? Longshot Claims and Private Securities Litigation" (2000) 94 Nw U L Rev 567 at 568. Charles Yablon, "The Good, the Bad, and the Frivolous Case: An Essay on Probability and Rule 11" (1996) 44 UCLA L Rev 65 at 84-91. Charles Yablon, "Hindsight, Regret, and Safe Harbors in Rule 11 Litigation" (2004) 37 Loy LA L Rev 599 at 608.
[884] Chris Guthrie, "Framing Frivolous Litigation: A Psychological Theory" 67:163 Un Chicago L Rev at 205

Second, some legal claims that *once* were viewed as non-tenable could eventually become well-founded due to evolution of the law.[885] Michael Risinger explains that "today's frivolity may be tomorrow's law, and the law often grows by an organic process in which a concept is conceived, then derided as absurd (and clearly not the law), then accepted as theoretically tenable (though not the law), then accepted as the law".[886] Domestic courts have to determine the degree of a claim's legal merit at the outset of the proceedings or at the early stages. This task is particularly complicated when claimants do not assert fantastical theories, but rather present a case that, while made on the basis of existing legal norms and principles, cannot possibly succeed under the law as currently interpreted and applied.[887]

4.1.1.2 Why Claimants Bring Frivolous Claims

The literature on incentives affecting frivolous litigation in the domestic context reveals three possible explanations why a claimant may file a frivolous suit. First, a claimant can file a meritless claim to apply pressure in order to obtain a positive settlement.[888] Second, a claimant can use a lawsuit to acquire a competitive advantage by constraining the resources of a respondent or limiting its possible actions in the

[885] Michael Risinger, "Honesty in Pleading and Its Enforcement: Some 'Striking' Problems with Federal Rule of Civil Procedure 11" (1976) 61 Minn L Rev at 57. The civil rights cases and specifically women's rights cases present probably the best case-studies to illustrate the point on evolution of law and particularly how yesterday's case without merit tomorrow may have a solid legal ground.
[886] *Ibid*. Bolgár (1975), at 1016-1017 (arguing that "Hence the controversy on the abuse of rights turned around the old and the new: represented by those who held-that there. can be no abuse of rights if they were exercised within the limits of the law that granted these rights (le droit cesse droit abus commence) and by those who held that any exercise of rights which is contrary to the social functions of these rights constitutes abuse. The chief protagonist of the first theory, besides Planiol, was Georges Ripert, who feared that the emphasis on the social as against the individual orientation of law will gradually deprive the individual of his subjective rights").
[887] *Meads v Meads*, [2012] ABQB 571 at para. 67-78.
[888] Patent trolls may file lawsuits or threaten by litigation to obtain royalties and settlements. John Golden, "Patent trolls" and Patent Remedies" (2007) 85:7 Tex L Rev 2111 at 2157.

marketplace.[889] The second scenario is particularly widely applied by patent holders that file suits to constrain generic manufacturers. Third, claimants may bring "longshot" claims in the hope that under the pressure of uncertainty in the litigation process such claims will succeed.[890]

Frivolous claims will flourish if the legal system structurally creates a reasonable possibility for frivolous litigants to achieve one of these desired results. For example, it is possible to anticipate a victory in a longshot claim only where the applicable law is unacceptably uncertain. In other words, the frivolous litigant thrives in situations where the cost of filing a claim is marginal but the potential return is substantial, and the legal system creates a reasonable chance of achieving that return. Bowles explains that the rules on costs allocation determine the incentive structure.[891] "Under the 'English Rule', the loser of an action has to pay legal costs of both sides. This widens the difference in the payoffs associated with winning and losing compared with the 'American Rule' under which each side pays her own costs and changes the structure of payoffs associated with settlement relative to trial".[892]

The legal structures that encourage or discourage frivolous litigation have been studied in the most detail in the US context.[893] Two approaches are the most prominent. The first model is advanced by Rosenberg and Shavell. This model demonstrates that a claimant may fully understand that the claim is frivolous, but nevertheless have some

[889] Daryl Lim, *Patent Misuse and Antitrust Law: Empirical, Doctrinal and Policy Perspectives* (Northampton: Edward Elgar Publishing, 2013) at 136-137.
[890] Charles Yablon, "A Dangerous Supplement? Longshot Claims and Private Securities Litigation" (2000) 94: 2 Nw UL Rev 567.
[891] *Ibid*.
[892] *Ibid*.
[893] Robert Gertner, "Asymmetric Information, Uncertainty, and Selection Bias in Litigation" (1993) 1:1 University of Chicago Law School Roundtable 75 at 77.

confidence that it can extract a favourable settlement.[894] The reason is that the respondent will agree to pay a settlement equal to its defence costs to avoid having to defend the case. The key assumption that underpins this analysis is that the respondent has to spend a significant sum in the defence before a claimant is required to spend similar amounts to advance its claim. Rosenberg's and Shavell's model emphasizes that the structure of the costs' distribution, i.e. at what period of time claimant and respondent carry on the costs for upholding their positions in the process of litigation influence whether a frivolous litigant can obtain a favourable settlement.

Rosenberg's and Shavell's model has attracted some degree of criticism. According to Katz, the respondent can simply know that a claim is frivolous and "respond with a blanket denial of the plaintiff's allegations".[895] Katz criticizes Rosenberg's and Shavell's model because it fails to explain "why frivolous suits might settle for amounts greater than the cost of a minimal response".[896] Katz acknowledges that respondents rarely respond with a "blanket denial and refusal to negotiate" because they "rarely know the merits of the claim with certainty".[897]

In short, Katz arrives at the following conclusions. First, "the proportion of frivolous suits is directly related to both sides' trial costs […] the prospect of an expensive trial will make the defendant a softer bargainer".[898] Second, "frivolous suits lead to at least two sorts of social costs […] the first is the real resource cost involved in filing such suits. The second is the cost of the trials required because the presence of

[894] David Rosenberg & Steven Shavell, "A Model in Which Suits Are Brought for Their Nuisance Value" (1985) 5 Intl Rev L& Econ 3.
[895] Avery Katz, "The Effect of Frivolous Lawsuits on the Settlement of Litigation" (1990) 10 Intl Rev L & Econ 3 at 4.
[896] *Ibid*.
[897] *Ibid*.
[898] *Ibid*.

strike suitors prevents some genuine claims from settling".[899] Thus (at least in theory), claimants will pursue their claims only in the situations when the cost of pursuing frivolous lawsuit is lower than the benefit it may render.

Bebchuk makes a similar argument, that when the parties carry on the costs in two or more stages (i.e. consecutively), the claimant has greater bargaining power to achieve a profitable settlement in between these stages, making a negative-value claim potentially worthwhile to pursue.[900] For his part, Gertner confirms that the systemic features of the regimes may lead to "different patterns of settlement".[901] It is worth noting that in the US context, costs are not normally recoverable, as the "American rule" on costs applies.[902]

In contrast, in Canada, the rule of thumb is that the loser pays at least some of the legal costs of the winner.[903] The application of rules on the allocation of costs is also a systemic feature that may be a factor in determining the structural incentives in bringing frivolous claims.[904] If the costs are not recoverable, a frivolous litigant can calculate the risks associated with litigation with greater certainty than the defendant.

Most notably, the cost of filing such a lawsuit may not be the same or even more than the cost of providing a legal response. In this case, it seems warranted to take into consideration the factor that claimants and respondents may be in substantially different bargaining positions. In other words, even though the costs of filing a lawsuit and defending it may be the same, for the defendant it may be more burdensome to defend

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[899] *Ibid* at 26.
[900] Arye Bebchuk, "A New Theory concerning the Credibility and Success of Threats to Sue" (1996) 25:1 J Leg Stud 1 at 1, 24-25.
[901] Andrés Villar Gertner, *Autonomy and Negotiation in Foreign Policy: The Beagle Channel Crisis* (London: Springer, 2016) at 77.
[902] Charles Bowles, "Prosecutorial Strategies" in Francesco Parisi, ed, *The Oxford Handbook of Law and Economics: Public Law and Legal Institutions* (Oxford: Oxford University Press, 2017) at 377.
[903] Canada follows the UK tradition. Peter McCormick, *Canada's Courts* (Toronto: James Lorimer Company, 1994) at 43.
[904] *Ibid*.

simply due to her financial circumstances. The relative burden of litigation must also be taken into consideration.

The phenomenon of asymmetrical information provides another reason why even claimants with weak cases may still file their claims. Hylton notes that the parties may have "have divergent expectations of the trial outcome or because one party has more at stake".[905] In part, such divergent expectations emerge as a result of asymmetric information that the parties possess before the trial, especially when the claimants have an informational advantagethat makes them more optimistic than the defendant.[906] Bones suggests that a weak claim might be pursued in hope that the defendant will "mistakenly believe that she has a strong case".[907] To uphold such a belief, the claimant will strategically "file the suit and mimic the meritorious claim" to obtain a profitable settlement.[908] Admittedly, the model of asymmetric information faces a number of criticisms as being "too simplistic" to reflect the reality of litigants' bargaining positions on the ground.[909] However, the theory of asymmetric information establishes a valid presumption that, in the reality of litigation, it is difficult to imagine a situation in which both claimant and respondent are equally well-informed.[910]

The structure of incentives to file and pursue frivolous claims thus depends on a number of systemic features such as the allocation of costs, funding of cases, and information that both parties possess (about each other, the lawsuit, and the applicable

[905] Keith Hylton, "Asymmetric Information and the Selection of Disputes for Litigation" (1993) 22:1 J Leg Stud 187 at 187.
[906] *Ibid*.
[907] Robert Bone, "Economics of Civil Procedure" in Francesco Parisi, ed, *The Oxford Handbook of Law and Economics: Public Law and Legal Institutions* (Oxford: Oxford University Press, 2017) at 152.
[908] *Ibid*.
[909] *Ibid* at 154.
[910] Michael Trebilcock, *The Law and Economics of Canadian Competition Policy* (Toronto: University of Toronto Press, 2003) at 293. (challenges the assumption that all actors act under the conditions of perfectly symmetric information).

law) before, during and after the proceedings. This review shows that these contextual factors contribute to increasing or decreasing filings of frivolous lawsuits.

4.1.2 Abuse of Process Claims: Overview

Abuse of process occurs when a party attempts to derive "an improper advantage, manifestly contrary to the objective" of the legal system.[911] The concept of abuse of process has its origins in rules of Roman law that prevented a claimant from misusing its rights.[912] The doctrine became prominent in the writings of French jurists in the 18th-19th century. During this period in France, two competing schools of legal thought influenced the development of the law. The formalists argued that all rights have an absolute character.[913] According to this school of thought, rights were defined as a "will" or an "entitlement"; individual rights were perceived as manifestations of "despotic power".[914] The representatives of the "relative" school of thought insisted that all rights have limitations.[915]

The concept of abuse of process emerged as a conceptual response to the absolutist vision of individual rights.[916] Josserand and Demogue, prominent French jurists, advanced this vision by arguing that "rights must be understood teleologically by

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[911] Arnaud Nuyts, "The Enforcement of Jurisdiction Agreements Further to Gasser and the Community Principle of Abuse of Rights" in Pascal de Vareilles-Sommieres, ed, *Forum Shopping in the European Judicial Area* (London: Bloosberry Publishing, 2007) at 68.
[912] *Houle v Canadian National Bank* [1990] 3 SCR 122. ("a closer analysis does demonstrate that the concept of abuse of rights was, to a certain extent, accepted in Roman law. While there are in the Digest formulas which, taken out of context, are such as to suggest that Roman jurists considered that a person could not be liable for damage caused to another while exercising a right, other texts show that these jurists refused to accept the use of a right so as to cause harm to another").
[913] James Gordley, "The Abuse of Rights in the Civil Law Tradition" in Rita de la Feria & Stefan Vogenauer Prohibition of Abuse of Law: A New General Principle of EU Law? (London: Bloomsbury Publishing, 2011) at 37-40.
[914] *Ibid*.
[915] *Ibid*.
[916] *Ibid*.

looking into finality and function".[917] Such teleological understanding of rights required the adjudicator in applying the abuse of process doctrine to look into the purpose that the particular legal institution had to serve.[918] This broad appreciation of abuse of process permitted adjudicators to employ the concept as a tool to prevent "individual choice from trumping social concerns".[919]

Fundamentally, abuse of process "is conceived as a restriction to liberty" for the common good.[920] The concept starts from a recognition that rights are not absolute and may be restricted in cases where parties misuse them. In practice, the application of the doctrine requires the adjudicator to draw a line between permissible and abusive conduct, a complex and potentially subjective determination. The challenge is that the legal rules do not explicitly prohibit such conduct. In the common law model of zealous advocacy, it may even be encouraged (within the limits of the law).[921] As a result, the adjudicator is put in a position where she has to normatively rationalize why particular conduct is or is not abusive, even when such conduct is not explicitly prohibited.

Civil law jurisdictions are familiar with the concept of abuse of process.[922] Voyame, Cottier, and Rocha identified three approaches to abuse of rights in the states of

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[917] Lous Josserand, De L'Esprit Des Droits et De Leur Relativite (Dalloz 2nd ed., 1939) as cited in Irene Calboli & Edward Lee, *Trademark Protection and Territoriality Challenges in a Global Economy* (Northampton: Edward Elgar Publishing, 2014) at 223. ("the goal and purpose of the theory of *abuse of rights* . . . is to ensure that the *spirit of the rights* prevails, and so to guarantee justice not only in statutory instruments and abstract formulas, this being relatively easy, but, what is a more substantial ideal, in their very application and even in daily life").
[918] *Ibid* at 245.
[919] Gordley (2011), at 39-40.
[920] Rita de la Feria & Stephan Vogenouer, *Prohibition of Abuse of Law: A New General Principle of EU Law?* (London: Bloomsbury Publishing, 2011) at vii.
[921] Monroe Freedman, "Henry Lord Brougham and Zeal" (2006) 34:4 Hofstra L Rev 1319.
[922] Hersh Lauterpacht, *Development of International Law by International Court* (Cambridge: Grotious Publications, 1958) at 295. Paul Perell, "Tort Claims for Abuse of Process" (2007) 33 Advoc Q 193 at 193. (explains that "the tort was recognized in 1883 in Grainger v. Hill 2 where a mortgagee of an ocean vessel sued to enforce the mortgage debt. The mortgagee's lawsuit was brought to coerce the mortgagor to turn over the ship's register, which the mortgagee wished to have because of concerns about the value of the

continental Europe. The first approach is conventional; it holds that "malicious intent was the sole essential element of the abuse".[923] According to Voyame *et al*, Italy, Austria and Liechtenstein follow the conventional approach by emphasizing malicious intent as the primary element of abuse of process in their civil codes.[924] There seem to be persistent differences among the states in this group with regard to the scope and legal effects of abuse of process.

The second group of countries "have toned down the requirement of harmful intent".[925] For example, in France, malicious intent is only a "subsidiary factor"; the primary element is a concept of fault. Under the fault factor, "what has to be determined is how a well-informed and well-intentioned person placed in the same circumstances would have acted".[926] The concept of abuse of process in France is closely interlinked with the concept known as "the social function of the law".[927] The social function of the law concept "rejects the vision of rights as absolute and justifies the limitations of individual rights by promoting social purpose or common good".[928]

Belgium and the Netherlands follow the French approach to a limited extent. In Belgium, the courts consider two criteria to establish abuse of process: "absence of legitimate interest",[929] and "the exercise of right for a wrongful purpose".[930] Finally, the

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security for the loan. 3 The mortgagee was liable for abusing the process of the law to achieve this improper purpose, which was extraneous to the enforcement of the mortgage"). Albert Mayrand, "Abuse of Rights in France and Quebec" (1974) 34 La L Rev 993 at 994,1014-1015.

[923] Council of Europe, Abuse of Rights and Equivalent Concepts: The Principle and Its Present Day Application (Strasbourg: Council of Europe, 1990) at 28. [Council of Europe: Abuse of Rights]. John Gaffney, "Abuse of Process in Investment Treaty Arbitration" 11 J World Investment & Trade 515 at 516-517.

[924] Council of Europe: Abuse of Rights at 28-29.

[925] *Ibid* at 30.

[926] *Ibid* at 32.

[927] *Ibid*.

[928] *Ibid* at 32-33.

[929] *Ibid* at 34.

[930] *Ibid*.

third group of states follows an objective approach to abuse of process. Their "courts focus their attention less on behaviour of the right holder – whether it be vexatious, excessive or unreasonable – than on the act itself and above all on its result."[931] Germany, Switzerland, Turkey, Spain, and Luxembourg belong to this group.[932] Voyame *et al*, emphasize that differences persist among the countries of the third group as well. For example, the courts of these states differently evaluate the weight of criteria such as "harmful intent" or "absence of legitimate interest".[933] After reviewing different legal traditions, these commentators conclude:

> the European states have very few points in common as regards the definition of abuse of rights, conditions of implementation, areas of application, and finally, legal effects […] so few, in fact, that it can be stated […] that there are almost as many conceptions of the abuse of rights as there are member states of the Council of Europe.[934]

Common law jurisdictions do not have a doctrine of abuse of rights in that form. In the common law of torts, "the use of any common right is subject to the duty of abstention from injuring others, of respect of their property, and of proper care to avoid causing harm".[935] The concept is construed narrowly. Gutteridge explains that "[t]he theory of abuse cuts across the line of many fundamental principles of the English law of torts […] A considerable portion of the area ascribed to the theory of abuse by continental law is already covered in English law either by the common law rules of tort

[931] *Ibid* at 35.
[932] *Ibid*.
[933] *Ibid*.
[934] *Ibid* at 23.
[935] Hersh Lauterpacht, *Development of International Law by International Court* (Cambridge: Grotious Publications, 1958) at 303.

or by statute".[936] Abuse of process exists as a freestanding tort, a source of liability not just a bar to recovery.[937]

As in civil law jurisdictions, the concept also may be a procedural device to prevent abusive conduct during judicial proceedings. According to the Supreme Court of Canada (SCC) in *Toronto (City) v CUPE Local 79*, "the doctrine of abuse of process is used in a variety of legal contexts"[938] including "to prevent the misuse of [the court's] procedure, in a way that would be manifestly unfair to a party to the litigation before it or would in some other way bring the administration of justice into disrepute".[939] The Australian courts follow a similar approach, identifying three categories of abuse of process: "the court's procedures are invoked for an illegitimate purpose, the use of court's procedures is unjustifiably oppresive to one of the parties, or the use of the court's procedures would bring the administration of justice into disrepute".[940]

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[936] Harold Gutteridge, "Abuse of Rights" (1933) 5 Cambridge LJ 22 at 44, 45.
[937] *Krieger v Law Society of Alberta*, [2002] 3 SCR 372, SCC 65 at para.32. (these attorneys can be brought before a court or a law society to be disciplined).
[938] *Toronto (City) v. CUPE, Local 79* [2003] SCC 63, 2003 Carswell Ont 4328 at para.36.
[939] *Ibid* at para.37. *Houle v Canadian National Bank* [1990] 3 SCR 122. (In Canada, the province of Quebec is a civil law jurisdiction has acknowledged the concept of abuse of rights (at least in the context of contract law). The SCC states "the doctrine of abuse of contractual rights is part of Quebec civil law. The doctrine serves the important social as well as economic function of controlling the exercise of contractual rights and is consistent with today's trend towards a just and fair approach to rights and obligations. Bad faith or malice in the exercise of a contractual right is no longer the only criterion for assessing whether such a right has been abused. The standard of the prudent and reasonable individual can also form the basis for liability resulting from an abuse of contractual rights. An abuse of rights may occur when the contractual right is not exercised in a reasonable manner, i.e. in accordance with the rules of equity and fair play. The abuse of a contractual right gives rise to contractual liability". The standard in Quebec was confirmed by SCC as follows "to summarize, then, it appears indisputable that the doctrine of abuse of contractual rights is now part of Quebec law. The standard with which to measure such abuse has expanded from the stringent test of malice or bad faith, and now includes reasonableness, as expressed by reference to the conduct of a prudent and diligent individual. This test could encompass a number of situations, including the use of a contract for purposes other than the ones contemplated by the parties. Consequently, the proper approach can be formulated as follows: were such rights exercised in the spirit of fair play?"). David Angus, "Abuse of Rights in Contractual Matters in the Province of Quebec" (1962) 8 McGill LJ 150.
[940] *Rogers v The Queen* [1994] HCA 42 at 286.

The abuse of process concept "remains controversial".[941] The above review reveals several aspects of this controversy. First, there appears to be lack of terminological consistency among commentators, courts, and legal systems. The concept is referred to as an abuse of process, abuse of rights, or abuse of law.[942] As a result, it appears difficult to crystalize "abuse" of what (law, process or right) has occurred. The lack of conceptual clarity is not resolved by references to transnational or supranational law. For example, the European Court of Justice "failed to pronounce […] a well-founded concept of abuse of law, at least in the context of company law".[943]

Second, there is a conceptual disaccord in the application of the concept. Some commentators view abuse of process as an element of tort law, while others insist that the concept is a procedural device to prevent misuse of courts procedures and ensure that the administration of justice is not put into disrepute.

Finally, the scope of the doctrine is not clear. There seem to be two main approaches. The first is to consider abuse of process as an element of a broader principle of good faith.[944] The second is to view the concept in isolation; as a tool to achieve dismissal on inadmissibility grounds only in narrow scenarios such as corporate restructurings.[945]

Three observations about domestic approaches to abuse of process are useful for our future discussion about the development of this concept in the context of the investment regime. First, the legal effects, the scope, and the implementation of abuse of

[941] Rita de la Feria & Stephan Vogenouer, eds, *Prohibition of Abuse of Law: A New General Principle of EU Law?* (Oxford: Hart Publishing, 2011) at vii.
[942] Stephan Vogenauer, "The Prohibition of Abuse of Law: An Emerging General Principle of EU Law" in Rita de la Feria & Stephan Vogenouer, *Prohibition of Abuse of Law: A New General Principle of EU Law?* (Oxford: Hart Publishing, 2011).
[943] Vogenauer (2011), at 115.
[944] *Abaclat* and *Phoenix* cases.
[945] Section 4.2.2.1.

process vary across jurisdictions, so there is no single concept of abuse of process in domestic law. Second, and on the other hand, there is a unifying theme, namely that abuse of process is "a corrective or limiting mechanism",[946] a device that may be employed to ensure the integrity of legal process. Abuse of process can also be a convenient device for preventing harm to third parties. The application of the concept may, however, result in increased volatility in the legal system because adjudicating an abuse of process claim forces adjudicators to resolve philosophical and even moral questions,[947] in particular whether the law allegedly abused has a definable purpose and whether the particular exercise of rights at issue undermines this purpose.[948] The questions raised by this overview open up the possibility for abuse of process to be regarded as "an instrument of dangerous potency in the hands of the demagogue and the revolutionary".[949]

Third, the common law and civil law systems appear to adopt two conceptually different visions of abuse of process. The civil law systems advance a broader concept of abuse of process that is interlinked with good faith and the idea that legal institutions have clear social purposes.[950] The common law systems consider abuse of process mainly

[946] Gambaro (1995), at 561.
[947] Pier Monateri, *Methods of Comparative Law* (Northhampton: Edward Elgar Publishing, 2012) at 112. Marcel Planiol and George Ripert criticized the abuse of rights concept exactly on this ground. They argued that "the doctrine was dangerous because it suggested that a court could set the law aside by an appeal to higher purposes whenever the application of a rule seemed to lead to an unfortunate result […] they claimed that such a doctrine would sacrifice individual rights to judicial conceptions of social needs."
[948] *Ibid* ("according to Louis Josserand, "to abuse [a right] is to proceed, intentionally or unintentionally, against the purpose of the institution of which one has misunderstood the finality and the function").
[949] Gutteridge (2016), at 44.
[950] Angelo Dondi, "Abuse of Procedural Rights: Regional Report for Italy and France" in Michelle Taruffo, ed, *Abuse of Procedural Rights: Comparative Standards of Procedural Fairness* (The Hague: Kluwer Law International, 1999) at 110-111.

as a procedural device to be employed in limited circumstances.[951] Such distinction between the common law and civil law raises an interesting question whether arbitrators with the distinctive educational background in civil law and common law identify and dismiss abuse of process claims differently.

A review of the cases where the tribunals upheld and rejected abuse of process allegations shows no correlation between the outcome of the case and the backgrounds of arbitrators. In other words, whether the arbitrators belong to common law or civil law background seems not to influence the dismissal of claims as abuses of process. In future research, it may be useful to identify how other factors in arbitrators' backgrounds (for example, the number of the arbitrator's previous appointments, their commercial/public law background, or their professional affiliations) correspond to the dismissal of abuse of process claims. Yet, one correlation between the arbitrators' backgrounds and their reasoning on abuse of process dismissals can be observed. In the three disputes (*Abaclat*, *Phoenix* and *Philip Morris*) where the tribunals offered the most detailed conceptual explanation of the factors can lead to the dismissal of the claim as an abuse of process, the majority of arbitrators had civil law backgrounds. Of course, these findings are only preliminary, and further research is needed in this area. It may also be necessary to control for other features of the arbitrators' backgrounds to identify whether they and how they may influence the dismissal of abuse of process claims.

[951] Neil Andrews, "Abuse of Process in English Civil Litigation" in Michelle Taruffo, ed, *Abuse of Procedural Rights: Comparative Standards of Procedural Fairness* (The Hague: Kluwer Law International, 1999) at 66-67.

4.2 Current Practices of Investor-State Tribunals on Dismissal of Frivolous and Abuse of Process Claims

This section examines the current state of affairs with regard to how and when ISA tribunals dismiss frivolous and abuse of process claims. This section provides an overview of the rules applicable to dismissal on these grounds and the way tribunals have applied those rules. As will be seen, the rules are vague and the volume of case law is small, so significant uncertainties remain.

4.2.1 Frivolous Claims in the International Investment Regime

The investment regime is not immune to frivolous claims. IIAs and arbitration rules include mechanisms for the dismissal of such claims early in proceedings. The following sections provide the historical context of such mechanisms, examine how they function, and set out the current state of affairs on the early dismissal of frivolous claims.

4.2.1.1 Context

The problem of frivolous claims in the investment regime has a history as long as the regime itself.[952] During the negotiations leading to the ICSID Convention, the problem of frivolous claims received attention from representatives of several of the negotiating states.[953] However, no provision was included in the Convention because the World Bank convinced the negotiators that the Secretary-General of the ICSID Arbitration Centre would convince foreign investors not to pursue frivolous claims.[954] Schreuer explains in his Commentary on the ICSID Convention that the Secretary-

[952] *OECD Draft Convention on the Protection of Foreing Property 1967*, reprinted in (1968) 7 ILM 117 at art.6 lit (c)(ii) (the tribunal can "dismiss the claim if, from the statements made by the national to the tribunal, the institution of the proceedings appears frivolous or vexatious". The Draft Convention however never came into force).
[953] Note by the General Counsel transmitted to the Executive Directions: Settlement of Investment Disputes, (19 January 1962), SecM 62-17. Consultative Meeting of Legal Experts: Settlement of Investment Disputes, (30 April 1964) Summary Record of Proceedings.
[954] *Ibid*.

General rejects requests for arbitration "only if the lack of jurisdiction is so obvious that the request does not deserve consideration by a tribunal.[955] It was not until 2005 that the ICSID Arbitration Centre revised article 41 of the ICSID Arbitration Rules to incorporate a mechanism for dismissing meritless claims *in limine*.[956]

Some recently-adopted IIAs and recently-revised arbitration rules have followed this trend and incorporated mechanisms for the early curtailment of meritless claims. [957] For example, CETA incorporates two provisions that aim to curtail frivolous claims early in the process.[958] Similarly, the SIAC Rules, revised in 2015, contain provisions permitting the early dismissal of claims on the basis of lack of legal merit.[959] Most notably, these two devices for dismissal of frivolous claims must be clearly distinguished from each other (at least on paper). The mechanisms for dismissal of unfounded claims and claims manifestly without legal merit have distinctive history of appearing in relevant treaties and arbitration rules. These procedural devices are also distinctively formulated. As the sections below show, the tribunals seem to acknowledge the difference between the two standards in theory, however, fail to clearly articulate precisely what are the differences between the standards for early dismissal and *how* the tribunals identify what claim must be dismissed under which standard.

It is worth noting that none of the arbitration rules or IIAs, however, give tribunals any direct guidance on how to distinguish legitimate claims of foreign investors from those that lack merit or are unfounded as a matter of law. IIAs and arbitration rules, thus, mimic the operation of domestic legal systems in this area; they authorize

[955] Christoph Schreuer, *The ICSID Convention: A Commentary* (Cambridge: Cambridge University Press, 2001).
[956] ICSID Arbitration Rules at art.41 (5).
[957] DR-CAFTA at 10.20. at para.4.
[958] CETA at art.8.32, 8.33.
[959] SIAC Arbitration Rules at Rule 29.

adjudicators to determine whether a claim is frivolous at some point early in the proceedings, before the evidentiary record may be complete. This exercise of discretion is largely unbounded, as no guidance is given to tribunals as to how to identify frivolous claims. one might therefore think that arbitrators dismiss claims freely. However, as will be discussed below, the opposite is true.

4.2.1.2 The Current State of Affairs: Available Procedural Devices to Dispose Frivolous Claims[960]

This subsection examines the criteria the ISA tribunals apply to identify the claims that manifestly lack legal merit (4.2.1.2.1), and claims that are unfounded or in which an award in favour of claimant cannot be made (4.2.1.2.2.). The goal of both mechanisms is to ensure administration of justice without unnecessary delays and to prevent extravagant costs of the full fledged arbitration process if the claim cannot stand as a matter of law.[961]

4.2.1.2.1 The ICSID Standard "Manifestly Without Legal Merit"

The standard "manifestly without legal merit" in the ICSID Arbitration Rules appeared in 2006 soon after the ICSID Secretariat received "recurring complaints" from a number of governments about a lack of procedural devices that will permit the arbitral tribunals to dismiss potentially meritless claim at the outset of the arbitral proceedings.[962]

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[960] The subsection 4.2.1. on claims manifestly without legal merit (the materials before *Ansung* and *Globex* cases) and the subsection 4.2.1.2.2. (the discussion on the *Pac Rim* case) build on my earlier publication in *Asper Review*. Ksenia Polonskaya, "Frivolous Claims in the International Investment Regime: How CETA Expands the Range of Frivolous Claims That May Be Curtailed in an Expedient Fashion" (2017) 17 Asper Rev. Int'l Bus. & Trade L. 1, 34. This publication was prepared during my doctoral work and I would like to express gratitude to the editor in chief of the journal Professor Bryan Schwartz.

[961] Deborah Rhode, "Frivolous Litigation and Civil Justice Reform: Miscasting Problem, Recasting the Solution" (2004) 54: Duke LJ 447. Charles Yablon, "The Good, the Bad, and the Frivolous Case: An Essay on Probability and Rule 11" (1996) 44 UCLA L Rev 65 at 94.

[962] Antonio Parra, "The Development of the Regulations and Rules of the International Centre for Settlement of Investment Disputes" (2007) 41 Int Lawyer 47.

In response, the ICSID Secretariat proposed a procedure for expedient rejection of investors' claims that manifestly lack legal merit. According to the Secretariat:

> by the introduction of a new paragraph (5), that the tribunal may at an early stage of the proceeding be asked on an expedited basis to dismiss all or part of a claim on the merits. The change would be helpful in addressing any concerns about the limited screening power of the Secretary-General.[963]

The ICSID Secretariat has amended Rule 41 that now provides that the respondent "may, no later than 30 days after the constitution of the Tribunal, and in any event before the first session of the Tribunal, *file an objection that a claim is manifestly without legal merit*".[964] Rule 41(5) is available only at the early stages and not throughout the process, akin to the mechanisms for dismissal available in common law jurisdictions.[965] Accordingly, the arbitrators must accept all facts as stated by the claimant. Under the Rule 41 (5) the tribunal has to address the legal merits as if all facts alleged by the claimant were true.[966] In *Trans-Global v Jordan*, the tribunal has observed that at the early stage in the proceedings when a rule 41(5) motion might be raised, "the tribunal is in no position to decide disputed facts alleged by the parties".[967] This feature makes the dismissal of meritless claims under Rule 41(5) similar to mechanisms that exist in common law jurisdictions. In Canada, Australia and the USA, courts may dismiss meritless claims, but may not at that stage resolve any factual disputes.[968] Courts in domestic legal systems, as well as ISA tribunals under ICSID,

[963] ICSID Secretariat, Suggested Changes to the ICSID Rules and Regulations (2005), at 7. [emphasis added]
[964] ICSID Arbitration Rules at art.41 (5). [emphasis added].
[965] Chapter 4, section 4.1.1.
[966] Trans-Global v Jordan at para. 93.
[967] Trans-Global v Jordan at para.97.
[968] Chapter 4, section 4.1.

must take the claimant's factual allegations as true. Most notably, the Rules do not explicitly state any criteria that can guide the tribunals in identifying such claims. The Rules, thus, allow the arbitrators full discretion in setting the standard for dismissal. From the outset, it is worth noting that given the lack of *stare decisis* in investment arbitration, future tribunals may adopt different interpretations of Rule 41(5).

Current arbitral practice demonstrates rather overly cautious approach to the dismissal of claims under the Rule 41(5). In past years, states have raised objections under rule 41(5) twenty-five times; only in three cases did the tribunal find that the claim manifestly lacked merit. In two other cases, the tribunals dismissed the investors' claims in part.[969]

The following four basic features in the application of the Rule 41 (5) can be identified from the arbitral practice. First, the tribunals explicitly stated that they will not deal with any novel issues of law under the standard "manifestly without legal merit". Apparently, the early dismissal procedure under Rule 41(5) applies only to cases without any dispute as to the meaning of the applicable rules of law. The case of *PNG Sustainable Development Program Ltd v Papua New Guinea* illustrates this point. In this case, the government of Papua New Guinea filed a preliminary objection, alleging that the claim did not satisfy the jurisdictional requirements of the applicable IIA and lacked legal merit as to its substance.[970] The tribunal has ruled that Rule 41 (5) "is not intended to resolve novel, difficult or disputed legal issues, but instead only to

[969] ICSID, Case –Law Rule 41(5), online:< https://icsid.worldbank.org/en/Pages/Process/Decisions-on-Manifest-Lack-of-Legal-Merit.aspx>.
[970] *PNG Sustainable Development Program Ltd. v Independent State of Papua New Guinea* (2014), Tribunal's Decision On The Respondent's Objection Under Rule 41(5) of the ICSID Arbitration Rules ICSID Case No. ARB/13/33 (International Centre for Settlement of Investment Disputes) (Arbitrators: Michael Pryles, Duncan Kerr, Gary Born) at para. 17, 30.

apply undisputed or genuinely indisputable rules of law to uncontested facts".[971] The tribunal in *PNG* thus dismissed the objection under Rule 41 (5), and emphisized that:

> [I]t would in principle be inappropriate to consider and resolve novel issues of law in a summary fashion, which would inevitably limit the Parties' opportunity to be heard and the Tribunal's opportunity to reflect.[972]

Accordingly, tribunals will not dismiss a claim as manifestly lacking merit if it implicates novel or otherwise unsettled legal issues. In *RSM* case, the tribunal has observed "[i]n cases of doubt or uncertainty as to the scope of a claimant's allegation(s), any such doubt or uncertainty should be resolved in favour of the claimant."[973]

The tribunal in *Mol Hungarian Oil and Gas Company Plc v Republic of Croatia* made somewhat similar point. In particular, the tribunal refused to dismiss the investor's claim and in doing so highlighted that both investor and state:

> have between them cited some half a dozen ICSID cases on the relationship between treaty claims and contract claims [...] [it] would seem to show that, whatever the merits of the Respondent's objection, it cannot be deemed "manifest" so as to meet the standard set by Rule 41(5).[974]

Second, the tribunals will not examine any allegations of bad faith under Rule 41(5). According to the tribunal in *Mol Hungarian Oil,* "when the claimant "is pursuing claims that it knows are baseless in order to obtain relief to which it knows it is not entitled", such conduct constitutes the "very definition of bad faith".[975] Such allegation

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[971] *Ibid* at para.89.
[972] *Ibid*.
[973] *RSM Production Corporation and others v Grenada* (ICSID Case No. ARB/10/6), Award at para.6.1.3.
[974] *Ibid* at para.49.
[975] *MOL Hungarian Oil and Gas Company Plc v Republic of Croatia*, ICSID Case No. ARB/13/32, Decision on Respondent's Application Under ICSID Arbitration Rule 41(5) (Franklin Berman, William Park, Brigitte Stern) at para.53. [*MOL Hungarian Oil*]

of bad faith cannot be adjudicated *in limine litis*.[976] The tribunal refused to adjudicate "imputations of bad faith" *in limine* presumambly because doing so would require resolving a factual dispute.[977] Under the current procedure, the facts as alleged by claimant are presumed to be true. This is likely to ensure that the claim is not dismissed simply because the claimant has not yet had a chance to obtain the evidence necessary to uphold its claim.

Third, it appears that ISA tribunals permit respondents to invoke Rule 41(5) at the jurisdictional stage or at the merits stage if the proceedings are bifurcated.[978] For example, the tribunal in *Brandes Investment Partners v Venezuela* observed:

> [r]ule 41(5) does not mention jurisdiction. The terms employed are "legal merit". This wording, by itself, does not provide a reason why the question whether or not a tribunal has jurisdiction and is competent to hear and decide a claim could not be included the very general notion that the claim filed is without legal merit.[979]

To satisfy the standard "manifestly", a respondent must demonstrate that the claim has no merit "on its face".[980] In *Trans-Global Petroleum, Inc. v Jordan*, the first dispute in which a tribunal applied Rule 41(5), a US investor concluded an agreement to explore oil deposits at the Dead Sea.[981] The Jordanian government then tried to prevent

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[976] *Ibid* at para.53.
[977] *Ibid* at para.53.
[978] *Global Trading Resource Corp. and Globex International, Inc v Ukraine*, Award ICSID Case No. ARB/09/11 (Arbitrators:Franklin Berman, Emmanuel Gaillard,Christopher Thomas) at para.31 (the tribunal permitted the tribunal to take advantage of Rule 41(5) in relation to either jurisdictional stage or a stage of merits as soon as "the objection is based on an issue (or issues) of law and does not involve disputed issues of fact"). [Globex v Ukraine]
[979] *Brandes* at para. 50.
[980] *Ibid* at para.25.
[981] *Trans-Global Petroleum, Inc. v Hashemite Kingdom of Jordan* (2009), Settlement Agreement and Release, ICSID Case No. ARB/07/25 (International Centre for Settlement of Investment Disputes) (Arbitrators: Donald McRae, James Crawford, VV Veeder) at para.48. [*Trans-Global v Jordan*]. In Trans-Global, the first time the Rule was cited in the ICSID arbitration.

the investor from participating in the project.[982] After Trans-Global initiated arbitration, Jordan invoked Rule 41 (5).[983] The tribunal held that the word "manifestly" means "self-evident", "clear", "plain on its face", or "certain".[984] Rule 41(5) only applies to "clear and obvious cases", given that time constraints require the tribunal to address the objection before or at the first session after the tribunal is constituted.[985]

In later awards, tribunals have concluded that the "manifestly" standard cannot be met where the disputing parties disagreed over the interpretation of the applicable legal rules. For instance, in *Mol Hungarian Oil and Gas Company Plc v Republic of Croatia,* the investor alleged that the Government of Croatia undertook a series of measures that impaired the claimant's investments in Industrija Nafte dd (INA), "Croatia's most significant enterprise in the field of energy".[986] Croatia filed a motion to dismiss the claim under Rule 41 (5) "based on allegedly preclusive effect of the forum selection clauses in the Shareholders Agreement […] the issue is essentially one of forum conveniens, a matter of considerable delicacy".[987]

Tribunals have dismissed claims entirely under Rule 41(5) in only three cases.[988] In *Global and Globex v Ukraine*, the tribunal examined the Ukranian government's

[982] *Ibid* at para. 52.
[983] *Ibid* at para.72.
[984] *Ibid* at para.83,84 and 105. The tribunal also addresses it as "test of clarity, certainty and obviousness" at para.105.
[985] *Ibid* at para.90.
[986] *MOL Hungarian Oil* at para. 14, 19.
[987] *Ibid* at para.48,49. Croatia cited two additional grounds for the dismissal. First, the objection relates to the treaty interpretation, in particular whether the "a state's listing in Annex IA is to be understood as a reservation to a treaty" that "expressly excludes reservations". Second, the objection related to the "preclusive effect of the forum selection clauses". Third, the objection was related to the criminal investigation against Mr Hernadi where both parties made "reciprocal allegations of bad faith". The tribunal refused to uphold Croatia's preliminary objections on all three grounds.
[988] In 2006-2018, there are total of 420 cases administered under the ICSID Convention and Additional Facility Rules. To author's knowledge, States invoked Rule 41(5) 25 times and only in three cases, the tribunal fully dismissed the claim as manifestly lacking merit. According to ICSID, only 0.7% of claims for past ten years were dismissed as claims that "manifestly lack legal merit". ICSID, The ICSID Caseload

preliminary objection that the investor's claims "represent nothing more than claims to payment under trading contracts, and do not therefore amount, in law, to investments".[989] In its turn, the claimant argued that its "poultry purchase contracts" constitute an investment.[990] The tribunal noted that the "concept of investment" remains "one of the most highly contested issues" in international investment practice.[991] Yet the tribunal refused to engage with this issue, and observed that its task in this case was more "straightforward", i.e. whether "the supplier's outlay of money in performing a contract for the transboundary purchase and sale of goods is capable of constituting an 'investment'?"[992] To answer this question, the tribunal examined the parties' written statements and held an oral hearing. The tribunal concluded that the "sale-purchase contracts" were "pure commercial transactions".[993] The contracts were "individual", "for limited duration", under "commercial trading terms", and provided for "delivery, the transfer of title, and final payment, before the goods are cleared for import into the recipient territory".[994] Therefore, the tribunal reasoned, "neither contracts of that kind,

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Statistics: Issue 2017-2, online:< https://icsid.worldbank.org/en/Documents/resources/ICSID%20Web%20Stats%202017-2%20(English)%20Final.pdf> at 7,14. For full record of the claims "manifestly without legal merit", see: ICSID, Decisions on Manifest Lack of Legal Merit, online:< https://icsid.worldbank.org/en/Pages/process/Decisions-on-Manifest-Lack-of-Legal-Merit.aspx>.

[989] Globex v Ukraine at para.41.

[990] *Ibid* at para.42. ("The Claimants contend that the claims do not arise solely from conventional trade transactions, and they do not involve only the cross-border sale of goods. Rather, the claims arise from "(a) the Ukrainian Prime Minister's entreaties that U.S. exporters assist the Prime Minister's efforts to break a domestic-producer monopoly, reduce prices, and curb inflation, and (b) the Prime Minister's explicit assurances that Ukraine would fulfill its obligations to those exporters willing to support the Prime Minister's economic-development efforts").

[991] *Ibid* at para.54.

[992] *Ibid* at para.55.

[993] *Ibid* at para.56.

[994] *Ibid*.

nor the moneys expended by the supplier in financing its part in their performance, can by any reasonable process of interpretation be construed to be investments".[995]

Another case where the tribunal upheld a preliminary objection under Rule 41 (5) is the *Ansung Housing v China* case. In *Ansung*, the claimant launched a development project (a golf course) in China for which it was granted rights of land use and necessary permits.[996] During the development stage, the government changed the conditions of the agreement, imposed additional requirements for using land, and (according to the claimant) harassed its employees.[997] As a result of these events, the claimant withdrew from the project and initiated arbitration. China filed a preliminary objection under Rule 41(5) on the basis that Ansung's claim was time barred.[998] According to the government, the period of three years for the claimant to bring an ISA claim elapsed, so that the tribunal did not have jurisdiction over the investor's claim.[999] The claimant invoked the MFN clause in the *China-Korea BIT* to avoid time-barring of the claim, since longer limitations periods applied in other IIAs entered into by China.[1000] The tribunal ruled that Ansung's claim was time barred under the *China-Korea BIT*, and the claim was not "protected by operation of the MFN Clause in Article 3(3) of the Treaty" because "[t]he plain reading of Article 3(3) and its interpretation leave no doubt that China has

[995] *Ibid*.
[996] *Ansung Housing Co v People's Republic of China* (2017), Award ICSID Case No. ARB/14/25 (International Centre for Settlement of Investment Disputes) (Arbitrators: Lucy Reed, Michael Pryles, Albert Jan van den Berg) at para.32-44.
[997] *Ibid* at 48-51.
[998] *Ibid* at para.59-61.
[999] *Ibid* at para.131. ("the Treaty context confirms that Article 3(3) does not cover dispute settlement").
[1000] *Ibid* at para.136. ("Ansung's alternative defense to China's Rule 41(5) Objection is that, because China has entered into other bilateral investment treaties with third States that do not prescribe a temporal limitation for an investor initiating an arbitration claim against the host State, Ansung is entitled to invoke the MFN Clause in Article 3(3) of the China-Korea BIT to disregard the three-year limitation period in Article 9(7) of the Treaty").

established its Rule 41(5) Objection with regard to the MFN Clause, "clearly and obviously, with relative ease and despatch".[1001]

In sum, tribunals will dismiss investors' claims under Rule 41(5) only in cases where lack of merit is "manifest". In *Globex*, the sale-purchase contracts were clearly commercial transactions with no "investment" element to them. In *Ansung*, the applicable BIT plainly barred the investors' claims. Interestingly, in *Ansung*, the tribunal did not consider the MFN claim as the contested legal issue particularly because of the explicit wording in the applicable BIT. Thus, the tribunals are likely to dismiss the claim only if the treaty explicitly (and without any doubt) sets a particular requirement for the claimant, or when there is no doubt as to the nature of the subject matter in the dispute. In contrast, tribunals are unlikely to dismiss claims if there are any disputed issues of law.

4.2.1.2.2 Claims Unfounded as a Matter of Law

In 2004, the US government included a provision for the dismissal of claims unfounded as a matter of law in its redrafted Model BIT.[1002] The USA continued to inject similar provisions in its subsequent treaties.[1003] This position is often explained by the USA's "bad experiences defending frivolous claims under *North American Free Trade Agreement Between the Government of Canada, the Government of Mexico and the Government of the United States* (NAFTA)".[1004] In particular, *Methanex v USA* seems to

[1001] *Ibid* at para.138-140. ("A plain reading of this Article does not extend to MFN treatment for a State's consent to arbitrate with investors and, in particular, not to the temporal limitation period for investor-State arbitration in Article 9(7) of the China-Korea BIT").
[1002] Salacuse (2015), at 116.
[1003] John Norton Moore, *International Arbitration: Contemporary Issues and Innovations* (The Hague: Martinus Nijhoff Publishers, 2013) at 159.
[1004] Arthur Rovine & Edward Kehoe, *Motions to Dismiss in International Treaty Arbitrations in Contemporary Issues in International Arbitration and Mediation: The Fordham Papers 2015* (The Hague: Brill, 2016) at 90. *North American Free Trade Agreement Between the Government of Canada, the Government of Mexico and the Government of the United States*, 17 December 1992, Can TS 1994 No 2 (entered into force 1 January 1994) [*NAFTA*].

have influenced the US government to incorporate "filters" against investors' claims in IIAs similar to those existing in the US legal system.[1005] In *Methanex*, the USA alleged that the investor's claim could not in principle succeed, even if all facts assumed by the claimant were true. The tribunal refused to dispose of the claim at the preliminary stages on the basis that the UNCITRAL Rules did not confer such authority.[1006] Kenneth Vandevelde explains that the claim in *Methanex* "consumed three years because of the absence of a mechanism for expeditiously challenging the legal sufficiency of the claim. Thus, US BIT negotiators sought to provide for expedited review of the legal sufficiency of claims".[1007]

Many US treaties borrow extensively from the US Model BIT. The *Dominican Republic-Central American* FTA (DR-CAFTA)[1008] incorporates the Model BIT's mechanism for the dismissal of legally insufficient claims.[1009] Article 10.20.4 of DR-CAFTA stipulates that "a tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favor of the claimant may be made.[1010] Most notably, the ICSID Arbitration Rule 41 (5) and the provision in DR-CAFTA incorporate drastically different language to authorize early dismissal.

The article 10.20.4 provides that the adjudicators must determine the legal viability of a claim at the early stages of the arbitration process. Under DR-CAFTA, the

[1005] Yannaca-Small (2010), at 25.
[1006] *Methanex* at para.88 ("The tribunal identified that it could not address the US objections as "based on "admissibility"; it does not qualify as a jurisdictional challenge; and even if it did qualify as a jurisdictional challenge (which in our view, it does not), it is so intertwined with factual issues in Methanex's case that we would have been minded to join that challenge to the merits").
[1006] Yannaca-Small (2010), at 25.
[1007] Vandevelde (2009), at 608.
[1008] DR-CAFTA at art.10.20.4.
[1009] Salacuse (2015), at 116.
[1010] DR-CAFTA. [emphasis added]

tribunal must decide at the stage of a preliminary objection if a claim can succeed as a matter of law. The respondent has a burden to convince the ISA tribunal that the claim is legally insufficient.[1011] DR-CAFTA provides that the tribunal does not examine facts at this preliminary stage; it must consider all facts alleged by the claimant to be true.[1012]

In *Pac Rim v El Salvador*, the tribunal determined the purpose of the provision and considered its scope. Pac Rim Cayman, a US-based company, brought a claim against El Salvador. According to Pac Rim's allegations, El Salvador violated its investment obligations under DR-CAFTA when it refused to issue an environmental permit and extend the license essential for for Pac Rim's operations.[1013] In response, El Salvador brought a preliminary objection under DR-CAFTA, describing Pac Rim's claim as one for which an "award in favour of claimant cannot be made". The tribunal explained that the purpose of the provision is to "to create, under CAFTA, an effective and flexible procedure for the swift and fair resolution of disputes between claimant investors and respondent host states, to be exercised reasonably by a tribunal according to all the circumstances of the particular case".[1014] The tribunal concluded that the standard of review under article 10.20.4 is not limited to "legally impossible" claims. According to the tribunal,

> [t]he Tribunal does not consider that the standard of review under Article 10.20.4 is limited to "frivolous" claims or "legally impossible" claims, contrary to the submissions of

[1011] *Pac Rim Cayman v The Republic of El Salvador* (2016), Decision on Preliminary Objection 10.20.4 and 10.20.5 ICSID Case No. ARB/09/12 (International Centre for the Settlement of Investment Disputes) (Arbitrators: Guido Santiago Tawil, Brigitte Stern, V.V. Veeder Esq) at para.111. ("the burden of persuading the tribunal to grant the preliminary objection must rest on the party making that objection, namely the respondent"). [*Pac Rim Cayman*]
[1012] *Ibid* at para.256. ("the Tribunal is legally obliged to assume that the Claimant"s factual allegations pleaded in the Notice of Arbitration, albeit disputed by the Respondent, are "true" in accordance with the express requirements of CAFTA Article 10.20.4(c) for the purpose of deciding these objections").
[1013] *Ibid* at para.60-64.
[1014] Ibid at para.116.

> the Claimant. These words could have been used by the Contracting Parties in agreeing CAFTA; but all are significantly absent. Moreover, the implied addition of these or similar words would significantly restrict the arbitral remedy under Article 10.20.4, when the structure of this provision permits a more natural and effective interpretation consistent with its object and purpose.[1015]

The tribunal specifically addressed the differences between ICSID Arbitration Rule 41 (5) and CAFTA article 10.20.4. It observed that "the Tribunal was also not materially assisted by comparisons […] with the New ICSID Arbitration Rule 41 (5), which ha[s] different wording and do[es] not share exactly the same object and purpose".[1016] The tribunal thus considered the standard under DR-CAFTA to be broader than the standard "manifestly without legal merit" under the ICSID Arbitration Rules. The tribunal held that, under DR-CAFTA,

> to grant a preliminary objection, a tribunal must have reached a position, both as to all relevant questions of law and all relevant alleged or undisputed facts, that an award should be made finally dismissing the claimant's claim at the very outset of the arbitration proceedings, without more..[1017]

Unfortunately, none of this actually articulates the standard. In fact, the tribunal suggests that the standard under 10.20.4 cannot be precisely identified and rationalized. Instead, the applicable standard appears to be decided in and intuitive manner of "I know it when I see it".[1018]

[1015] *Ibid* at para.108.
[1016] *Ibid* at para.118.
[1017] *Ibid* at para.110. [emphasis added]. The tribunal immediately safeguarded its full discretion over the matter ("depending on the particular circumstances of each case, there are many reasons why a tribunal might reasonably decide not to exercise such a power against a claimant, even where it considered that such a claim appeared likely (but not certain) to fail if assessed only at the time of the preliminary objection").
[1018] Paul Gewirtz, "On "I Know It When I See It" (1996) Faculty Scholarship Series 1023,1046. ("I cannot define it, but I know it when I see it" a famous phrase of Justice Potter Stewart that discussed the threshold for obscenity in Jacobelis v. Ohio. The judge attempted to categorize the parameters for identifying obscenity but instead presented a subjective opinion […] the central justification for that coercion is that it

In *Renco v Peru*, another ISA tribunal also examined the scope of article 10.20.4 after Peru made a preliminary objection that Renco's claim was not "a claim for which an award in favor of the claimant may be made". Peru's objections were:

> (1) presentation of an invalid waiver;
>
> (2) violation of the waiver;
>
> (3) lack of jurisdiction *ratione termporis*;
>
> (4) violation of the Treaty's three-year limitations period;
>
> (5) failure to state a claim for breach of the investment agreement; and,
>
> (6) failure to submit two factual issues for determination by a technical expert prior to commencement of the arbitration.[1019]

Peru argued that all these objections "fit within the broad scope" of the provision, given that article 10.20.4 allows "*any objection* by the respondent that, as a matter of law" the claim is not sufficient including the objections on competence of the tribunal to adjudicate the investor's claim.[1020] The tribunal disagreed, reasoning that the article "requires a tribunal to deal with a certain category of objections—namely, objections by a respondent to the legal sufficiency of claims".[1021] The tribunal also underscored that "there is a meaningful distinction between an objection that mounts a challenge to the sustainability of a legal claim, and an objection to a tribunal's competence to hear a

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is compelled, or at least constrained, by pre-existing legal texts and legal rules, and by legal reasoning set forth in a written opinion. From this perspective, the exercise of judicial power is not legitimate if it is based on a judge's personal preferences rather than law that precedes the case, on subjective will rather than objective analysis, on emotion rather than reasoned reflection" and suggesting to recognize "how central nonrational qualities are to both judging and lawyering, we in law teaching should be somewhat uneasy about what we are doing").

[1019] *Renco v Peru*, Decision as to the Scope of the Respondent's Preliminary Objections under Article 10.20.4 at para. 245.

[1020] *Renco v Peru*, Peru's Submission on the Scope of Preliminary Objections at para.3 [Emphasis original]

[1021] *Renco v Peru*, Decision as to the Scope of the Respondent's Preliminary Objections under Article 10.20.4 at para.185.

dispute".[1022] The difference is that a challenge to the "legal insufficiency" of a claim requires an examination of the merits, whereas the question of competence requires the tribunal to decide "whether the objection is "hearable" at all, irrespective of a party's substantive Treaty rights or the legal merit of the claim".[1023] The tribunal concluded that the "competence objections" of Peru cannot be reviewed and that only objection (6) was properly within its jurisdiction under the scope of article 10.20.4.[1024]

Two observations can help explain the scope of the standard under article 10.20.4. The first relates to the origins of the article, which some commentators note was informed by the US domestic rules on early claims dismissal there there is no real prospect of success.[1025] In its response to Peru's preliminary objections, Renco argued that the standard can be analogized to Rule 12(b)(6) of FRCP.[1026]

However, Peru argued against such a comparison.[1027] It noted instead that "there is "no reason to equate such common law court procedures to provisions in [the Treaty] agreed by Contracting Parties with different legal traditions and national court procedures".[1028] In my view, Peru's concern about applying standards developed in US domestic law in the international context is warranted. Even if the dismissal provision

[1022] *Ibid* at para. 205.
[1023] *Ibid* at para. 206.
[1024] *Ibid* at para. 246.
[1025] Edward Kehoe, "Motions to Dismiss in International Treaty Arbitrations" in Arthur Rovine,ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers 2015* (The Hague: Brill, 2016) at 90.
[1026] *Renco v Peru*, Claimant's Submission Challenging the Scope of Preliminary Objections at 7-8. Interestingly so, the tribunal in Pac Rim explicitly stated that it was not assisted by the comparisons of domestic rules of civil procedure with the provision in CAFTA. *Pac Rim Cayman* at para.117 ("The Tribunal was not materially assisted by comparisons between these provisions and national court procedures in one Contracting Party, the USA […] including the decisions of the US Supreme Court in *Neitzke v. Williams* and *Ashcroft v. Iqbal*. Not only is that message from one Contracting Party not replicated by other Contracting Parties to CAFTA, there is also no reason to equate such common law court procedures to provisions in CAFTA agreed by Contracting Parties with different legal traditions and national court procedures").
[1027] *Renco v Peru*, Peru's Submission on the Scope of Preliminary Objections at para.19.
[1028] *Ibid*.

was inspired by Rule 12(b)(c) of the FRCP, this does not mean that domestic rules should be used by the tribunal to interpret and apply the treaty.

The tribunal in *Renco* did not comment on the comparison in its interpretation of article 10.20.4. Instead, the tribunal concluded that Peru and the USA simply differed in their understandings of the "ambit" of article 10.20.4.[1029] Lise Johnson of the Columbia Centre on Sustainable Development observes that the tribunal's actions diminished the scope of the dismissal provisions,

> [b]y determining that all but one of Peru's objections were "competence" objections not within the scope of Article 10.20.4, the tribunal narrowed the provision beyond even the reach of Rule 12(b)(6) […] Similarly, under US law, defendants can use Rule 12(b)(6) motions for failure to state a claim to seek dismissal of claims when prerequisites to filing suit had not been met. According to the Renco decision, however, Peru's request for dismissal on the ground that certain prerequisites to suit had not been met were "competence" objections that could not be brought under Article 10.20.4. Assuming the Renco v. Peru tribunal's approach to the meaning of "competence" objections is followed in other decisions, that early-dismissal provision may be of much less use to respondent states than Rule 12(b)(6) (or any other 12(b) motion) is to defendants in US federal court proceedings.[1030]

On the basis of the first observation, two conclusions can be made. First, even if the similar clauses in IIAs were inspired by the US summary procedures for the early disposition of claims, the standard under the treaty is autonomous. Second, the

[1029] *Renco v Peru*, Decision as to the Scope of the Respondent's Preliminary Objections under Article 10.20.4 at para. 156, 169, 171. (The US Government confirmed that in its interpretation of the "according to the USG, paragraph 4 of Article 10.20 provides a further ground for dismissal, in addition to "other objections", such as preliminary objections to the tribunal's competence. The USG considers that in view of the "without prejudice" clause, a tribunal may also hear preliminary objections to competence asserted under the applicable arbitration rules". The tribunal read the US submission in the following way that led to the conclusion that "objections asserted under paragraph 4 [of Article 10.20] are distinct from objections to the tribunal's competence" and that "an objection that a dispute is not within the tribunal's competence" falls "outside the scope" of Article 10.20.4.").
[1030] Johnson (2015), at 11-12.

interpretation of the tribunal in *Renco* significantly narrows the range of preliminary objections that may be made under the scope of article 10.20. 4, by limiting objections only to those related to legal sufficiency. Peru, however, is correct in its observation that the civil procedure practice of the US courts has only limited relevance given that the investment regime constitutes a separate system of law distinct from any national legal systems.

The second observation relates to the silence of the *Renco* tribunal on the matter of how to identify whether a claim is legally sufficient. Throughout the decision, the tribunal mentioned that article 10.20.4 requires the arbitrators to consider objections "alleging the insufficiency of a claim as a matter of law",[1031] "an objection which is directed at the legal sustainability of a claim",[1032] and "the claimant's alleged failure to state the claim".[1033] The terminological inconsistency throughout *Renco* generates even greater confusion on the issue of what claims can be curtailed under the article. This inconsistency is particularly alarming in the context of international arbitration, when the claimants, respondents, and arbitrators may all come from different legal traditions and mean different things when they discuss legal concepts.

4.2.2 Abuse of Process Claims in the International Investment Regime

Hersch Lauterpacht offers the cornerstone doctrinal explanation of abuse of process in international law:

> The essence of the doctrine is that, as legal rights are conferred by the community, the latter cannot countenance their *antisocial use* by individuals […] there is such an abuse of rights each time *the general interest of the*

[1031] *Renco v Peru*, Decision as to the Scope of the Respondent's Preliminary Objections under Article 10.20.4 at para. 191 (1).
[1032] *Ibid* at para.207.
[1033] *Ibid* at para.255.

> *community is injuriously affected* as the result of the sacrifice of an important social or individual interest to a less important, though hitherto legally recognized, individual right.[1034]

Lauterpacht envisages abuse of process as "an instrument of change", and "one of the basic elements of the international law of torts" that has an "important function" in international law.[1035] It is important to emphisize that Lauterpacht does not distinguish between abuse of process as a rule of tort or a rule of procedure. In addition, Lauterpacht does not rationalize why abuse of process can be an element of international tort law not a matter of procedure. Two factors may explain what appear from the modern perspective to be deficiencies. First, Lauterpacht's seminal text was published in 1933, "well before the development of modern international procedural law".[1036] Second, my reading of the text suggests that Lauterpacht was primarily concerned with the public function of international courts, and how they can ensure that the administration of justice is not put into disrepute.[1037] Accordingly, while Lauterpacht's text is a cornerstone for the conceptual formulation of this doctrine in international law, it is not the final word on abuse of process largely because of the continuous development of international legal procedure and the emergence of new international courts and tribunals.

For Lauterpacht, thus, abuse of process is an instrumental device in the hands of the international community to ensure that "the rights are not exercised with an anti-social purpose".[1038] In this conception, abuse of process is a conceptually transformative

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[1034] Lauterpacht (1982), at 286. [Emphasis added].
[1035] *Ibid*.
[1036] Paul Gormley, *The Procedural Status of the Individual Before International and Supranational Tribunals* (London: Springer, 2012) at 57.
[1037] Chester Brown, "Inherent Powers in International Adjudication" in Cesare Romano, Karen Alter & Yuval Shany, *The Oxford Handbook of International Adjudication* (Oxford: Oxford University Press 2015) at 843.
[1038] Lauterpacht (1933), at 298.

mechanism, which symbolizes the development of international law. It moves law from a purely individualistic system that "refuses to interfere with the legally recognized self-assertion […] even if such conduct is contradictory to the principles of justice and social solidarity", to a more "advanced stage" characterized by "social integration of the community".[1039] In the absence of a single international legislature, this development is possible only via an international judiciary, which can employ abuse of process as one of its remedial devices to police that "rights are exercised with an anti-social purpose".[1040] This view of the spirit of abuse of process appears to reflect Josserand's broad view on abuse of process, who asserts that an exercise of an individual right cannot contradict a social function of a legal institution. Interestingly, the language of Lauterpacht's text echoes Josserand's appeals to abuse of process as an instrument of "civilized legal systems".[1041] Although such a view may be intuitively attractive (as much as choice between "civilized" and "uncivilized" is somewhat culturally predetermined for any scholar educated in the West),[1042] it is difficult to imagine the attainability of such a broad view of abuse of process in the context of international adjudication. The practice of ISA tribunals shows that arbitrators are rather cautious in utilizing this instrument for dismissal of claims.

[1039] *Ibid* at 299. András Sajó, *Abuse: The Dark Side of Fundamental Rights* (Eleven International Publishing, 2006) at 35. (This interpretation seems to follow Josserand's understanding of the legal systems. Andras Sajo explains "Josserand […] stated that "abuse of rights" is one of the eternal and fundamental ideas of all "civilized legal systems").
[1040] *Ibid* at 300. Brown (2015), at 843.
[1041] András Sajó, *Abuse: The Dark Side of Fundamental Rights* (Eleven International Publishing, 2006) at 35. (This interpretation seems to follow Josserand's understanding of the legal systems. Andras Sajo explains "Josserand […] stated that "abuse of rights" is one of the eternal and fundamental ideas of all "civilized legal systems").
[1042] Partha Chatterjee, *The Black Hole of Empire: History of a Global Practice of Power* (Princeton: Princeton University Press, 2012) at 191.

ISA tribunals contribute to the development of the investment regime by providing authoritative interpretations and generating legal outcomes that influence inputs and outputs of the regime's participants – foreign investors, states, and arbitration institutions.[1043] It is thus important to identify the contribution that ISA tribunals had made in developing abuse of process in international law. The sections that follow will examine how the tribunals applied this concept and identify the challenges they faced. This section adopts the categorization introduced by Emmanuel Gaillard, who identifies three scenarios in which dismissal of abuse of process claims may be warranted. This section further complements Gaillard's categorization by introducing the forth scenario.

The first category identified by Gaillard is "an abuse of process [that] arises exclusively in investment treaty arbitration and concerns the manner in which a corporate investor seeks to secure the jurisdiction of an arbitral tribunal".[1044] Second, abuse of process may occur when a foreign investor "initiates more than one proceeding to resolve the same or related disputes in order to maximize its chances of success".[1045] Third, abuse of process materializes when a foreign investor brings a claim to acquire a benefit "inconsistent with the purpose of investment arbitration".[1046] A fourth scenario that Gaillard does not mention explicitly is evident in the case law. This scenario encompasses conduct of the parties that violates the integrity of the arbitral proceedings.

Before further discussing these four scenarios, it is worth mentioning that, like national legal systems that employ the concept, the ISA tribunals also use imprecise and inconsistent terminology. For example, some tribunals refer to the concept as an "abuse

[1043] Dupont & Schultz (2016), at 3.
[1044] *Ibid* at 3.
[1045] *Ibid* at 6.
[1046] *Ibid* at 10.

of process",[1047] while others mention "abuse of rights" "abuse of system"[1048], or "abuse of treaty"[1049] instead; still other formulations include "abuse of the Convention purposes"[1050] and "abuse of the ICSID mechanism".[1051] Some tribunals view abuse of process as an element of a broader principle of bad faith, which is sometime further distinguished as either substantive or procedural bad faith.[1052] In my view, these inconsistencies complicate the categories that follow.

4.2.2.1 Corporate Restructuring

Many foreign investors who invoke ISA protection are transnational corporations that operate in multiple jurisdictions.[1053] Most investment treaties of early generation set no limitations on the mobility of companies that migrate from one jurisdiction to another in search of legal or economic benefits.[1054] Some foreign investors exploit this

[1047] *RomPetrol v Romania* at para. 59.
[1048] *Phoenix Action, Ltd v Czech Republic* (2009), Award ICSID Arbitral Tribunal Case No ARB/06/5 (International Centre for Settlement of Investment Disputes) (Arbitrators: Juan Fernández-Armesto, Andreas Bucher, Brigitte Stern) at para. 93, 143, 136-140. (the tribunal in *Phoenix* concluded that the claimant conducted restructuring of assets with a mere purpose to gain access to ICSID jurisdiction. The tribunal in detail analyzed the following factors: timeframe of the dispute, timeframe of the claim, nature of the restructuring).
[1049] *Tidewater v Venezuela* at para. 146–147. (Arbitrators: Campbell McLachlan, Andrés Rigo Sureda, Brigitte Stern).
[1050] *Autopista* at para. 81.
[1051] *RomPetrol v Romania* at para. 27.
[1052] *Abaclat and others (Case formerly known as Giovanna a Beccara and Others) v Argentine Republic* (2011), Decision on Jurisdiction and Admissibility ICSID Case No ARB/07/5 (International Centre for Settlement of Investment Disputes) (Arbitrators: Pierre Tercier, Albert Jan van den Berg, Santiago Torres Bernárdez) at para. 647–649. Eric De Brabandere, "'Good Faith', 'Abuse of Process' and the Initiation of Investment Treaty Claims" (2012) 3:3 Journal of International Dispute Settlement 609 at 613. De Brabandere traces relationship between good faith and abuse of process in the tribunals' practice. De Brabandere in detail analyses the Abaclat decision on conceptual distinction between material and procedural good faith. De Brabandere concludes in his analysis of Abaclat case as follows "The second category of 'good faith' claims, termed 'procedural good faith' by the Abaclat tribunal, concerns the invocation of 'good faith' in relation to 'the context and the way in which a party, usually the investor, initiates its treaty claim seeking protection for its investment"
[1053] Stephen Cohen, *Multinational Corporations and Foreign Direct Investment: Avoiding Simplicity, Embracing Complexity (*Oxford: Oxford University Press, 2007*)* at 268.
[1054] Baumgartner (2016), at 214.

flexibility.[1055] For example, in *Pac Rim v El Salvador*, Pac Rim re-incorporated in the USA, then invoked its US nationality when initiating arbitration under CAFTA. El Salvador argued that this change of nationality constituted an abuse of process because it was done solely to gain access to CAFTA. However, the tribunal held that in order to consider the corporate nationality planning as an abuse of process, the company must "foresee a specific future dispute as a very high probability and not merely as a possible controversy".[1056]

By contrast, in *Phillip Morris v Australia*, the ISA tribunal held that the corporate restructuring of Phillip Morris did constitute an abuse of process.[1057] There, the dispute revolved around Australian tobacco plain packaging legislation, which required cigarette companies to place public-health-promoting images on cigarette packs.[1058] The images took up more than 80% of the cigarette package, which, according to Phillip Morris, diminished the value of its trademark by undermining its appeal to customers.[1059] In

[1055] *Autopista v Venezuela* (2001), Decision on Jurisdiction ICSID Case No ARB/00/5 10 ICSID Reports 309 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gabrielle Kaufmann-Kohler, Karl-Heinz Böckstiegel, Bernardo Cremades) at para. 67, 130-131. [*Autopista*] *Aguas del Tunari SA v Republic of Bolivia* (2005), Decision on Respondent's Objections to Jurisdiction ICSID Case No ARB/02/3 16 ICSID Reports 3 (International Centre for Settlement of Investment Disputes) (Arbitrators: David Caron, Jose Luis Alberro-Semerena, Henri Alvarez) at para.331-332.
[1056] *Pac Rim Cayman v The Republic of El Salvador*, Decision on the Respondent's Jurisdictional Objections at para.2.99. *Tidewater v Venezuela*, Decision on Jurisdiction at para.148.
[1057] *Philip Morris Asia Limited (Hong Kong) v The Commonwealth of Australia* (2015), Award on Jurisdiction and Admissibility PCA Case No 2012-12 (Karl-Heinz Böckstiegel, Donald McRae, Gabrielle Kaufmann-Kohler). *Mobil v Venezuela* at para.202-205. [*Philip Morris Asia v Australia*]
[1058] Andrew Mitchell & Tania Voon, *The Global Tobacco Epidemic and The Law* (Northhampton: Edward Elgar Publishing, 2014).
[1059] *Philip Morris Asia Limited v The Commonwealth of Australia*, UNCITRAL, PCA Case No. 2012-12 ICSID (Gabrielle Kaufmann-Kohler, Donald McRae, Karl Böckstiegel, Arbitrators), *Notice of Arbitration* paras 6.5, 6.6. and 6.7 and the Notion of Arbitration at 37-40 "plain packaging legislation contravenes Australia's obligations under international trade treaties, in particular TRIPS […] which explicitly incorporates the minimum standards of protection provided for trade marks by the Paris Convention […]".

response to the plain packaging legislation, Philip Morris initiated domestic and ISA proceedings and successfully lobbied five governments to bring WTO claims.[1060]

In the arbitration, Phillip Morris alleged violation of multiple provisions of the *Hong Hong-Australia BIT*.[1061] Australia filed an application for bifurcation of the arbitral proceedings, to split jurisdiction and merits into two separate phases. At the jurisdictional stage, Australia submitted that Phillip Morris had "manipulated" the investment regime by undertaking a corporate restructuring in anticipation of the plain-packaging dispute, assigning its trademarks to a new Hong Kong-registered entity in order to take advantage of the *Hong Kong-Australia BIT*.[1062]

After five years of the arbitration proceedings, the ISA tribunal finally dismissed Phillip Morris's claims on the basis of an abuse of process.[1063] In short, the tribunal found that Phillip Morris had conducted its corporate restructuring for the sole purpose of gaining access to the *Hong Kong-Australia BIT*.[1064] The tribunal allowed that not every corporate restructuring constitutes an abuse of process.[1065] In some circumstances, corporate restructuring may be a legitimate way for a claimant to protect itself from non-business risks, including by incorporating subsidiaries in multiple jurisdictions to gain access to multiple IIAs should a dispute arise.[1066] This kind of strategic restructuring is common and permissible in view of the tribunal. The tribunal in *Phillip Morris* held that,

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[1060] Tania Voon, Andrew Mitchell & James Munro, "Legal Responses to Corporate Maneuvering in International Investment Arbitration" (2013) 1 J Intl Dispute Settlement at 4 – 8.
[1061] *Agreement Between the Government of Hong Kong and the Government of Australia for the Promotion and Protection of Investments* (1993), at art 1(e).
[1062] *Philip Morris Asia v Australia*.
[1063] *Ibid*.
[1064] *Ibid.*
[1065] Phillip Morris Jurisdiction and Admissibility at para.540
[1066] Baumgartner (2016), at 228.

in order to establish an abuse of process on the basis of corporate restructuring, it had to find that:

> … the abuse is subject to an objective test and is seen in the fact that an investor who is not protected by an investment treaty restructures its investment in such a fashion as to fall within the scope of protection of a treaty in view of a specific foreseeable dispute.[1067]

This is a rather narrow test with two distinct elements. First, the specific dispute must be foreseeable to the claimant. Second, a claimant must undertake corporate restructuring for the purpose for bringing a claim related to the dispute under an IIA. The *Phillip Morris* tribunal noted further that it "would not normally be an abuse of right to bring a BIT claim in the wake of a corporate restructuring, if the restructuring was justified independently of the possibility of bringing such a claim".[1068]

The tribunal concluded that the specific dispute was foreseeable to the company because it was aware of the commitment of the Australian government to introduce the plain-packaging legislation.[1069] The claimant also failed to persuade the tribunal that it had any reason for the corporate restructuring other than to gain access to the *Hong Kong-Australia BIT* and to bring a claim against Australia challenging the plain-packaging law.[1070]

In another corporate restructuring case, *Mobil v Venezuela*, the tribunal took a slightly different approach. It looked at the timing of the restructuring to determine whether Mobil's corporate restructuring was motivated by legitimate objectives, or to take advantage of the protection provided by a particular IIA. The tribunal concluded that

[1067] Phillip Morris Jurisdiction and Admissibility at para.539
[1068] *Ibid* at para.570.
[1069] *Ibid* at para.566-569.
[1070] *Ibid* at para.572-574.

a corporate restructuring is legitimate if conducted to protect corporate assets in case of a future dispute.[1071] The tribunal, however, reaffirmed that corporate restructuring for the sole purpose of gaining access to ISA for pre-existing disputes does constitute a manipulation of the system and therefore would be sanctioned by tribunals as an abuse of process.[1072] Interestingly, Schill and Bray criticized the tribunal's approach for relying on the "the vague concepts" of "abuse of process" that cannot be found "within the text of the treaty".[1073]

In *Pac Rim v El Salvador*, the tribunal followed the reasoning of the tribunal in *Mobil*. It held that corporate restructuring constitutes an abuse of process,

> when the relevant party can see an actual dispute or can foresee a specific future dispute as a very high probability and not merely as a possible controversy. In the Tribunal's view, before that dividing-line is reached, there will be ordinarily no abuse of process; but after that dividing-line is passed, there ordinarily will be.[1074]

The *Pac Rim* tribunal safeguarded its scope of discretion by holding that the determination of this "dividing line" will depend on the circumstances of each particular case.

This overview of arbitral decisions demonstrates that tribunals will consider claims of abuse of process on a case-by-case basis.[1075] Fukunaga similarly suggests that "careful

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[1071] *Mobil Corporation, Venezuela Holdings BV, Mobil Cerro Negro Holding, Ltd, Mobil Venezolana de Petroleos Holdings, Inc, Mobil Cerro Negro, Ltd, and Mobil Venezolana de Petroleos, Inc v Bolivarian Republic of Venezuela* (2010), Decision on Jurisdiction ICSID Case No ARB/07/27 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gilbert Guillaume, Gabrielle Kaufmann-Kohler, Ahmed Sadek El-Kosheri) at para.199-204. [*Mobil v Venezuela*].
[1072] *Ibid* at para.205
[1073] Stephan Schill & Heather Bray, "Good Faith Limitations on Protected Investments and Corporate Structuring" in Andrew Mitchell, M Sornarajah & Tania Voon, eds, *Good Faith and International Economic Law* (Oxford: Oxford University Press, 2015) at 112.
[1074] *Pac Rim Cayman,* Decision on the Respondent's Jurisdictional Objections at para.299.
[1075] *Tidewater v Venezuela* at para. 147.

reading of the decisions […] reveals that there is no settled case law in investment arbitration on the principle of abuse of process".[1076]

Two observations can be made with regards to corporate restructuring as an abuse of process category. First, the common (and decisive) factors in applying abuse of process seem to be the timing of and the motivation for the corporate restructuring. On the latter point, whether something is an abuse of process will turn on the question of whether it was undertaken specifically to gain the protection of a particular IIA for a particular investment.[1077]

Second, the application of abuse of process in corporate restructuring cases is narrow. Ziegler and Baumgartner found that "abuse of rights or abuse of process findings have thus been rare, probably in part due to the slightly differing foreseeability tests applied by arbitral tribunals".[1078] In this regard, the *Tokios Tokeles v Ukraine* case is illustrative.[1079] In *Tokios Tokeles*, the investors registered a corporation in Lithuania. The

[1076] Yuka Fukunaga, "Abuse of Process under International Law and Investment Arbitration" (2018) 33:1 ICSID Rev 181 at 182. (Fukunaga also adds that there is also no "clear and share understanding of the principle" which only exacerbates" the inconsistency that already exists in the interpretation and application of international investment law). Duncan Watson & Tom Brebner, "Nationality Planning and Abuse of Process: A Coherent Framework" (2018) 33:1 ICSID Review 302 at 303 ("The abuse of process doctrine is now well-entrenched in the jurisprudence; and it will likely play an increasingly important role in policing access to the investment treaty arbitration system. However, key aspects of the doctrine remain poorly defined").

[1077] *Tokios Tokeles v Ukraine* (2004), Decision on Jurisdiction ICSID Case No ARB/02/18 (International Centre for Settlement of Investment Disputes) (Arbitrators: Prosper Weil, Piero Bernardini, Daniel Price) at paras 55–56 ("the Claimant manifestly did not create Tokios Tokeles for the purpose of gaining access to ICSID arbitration under the BIT against Ukraine, as the enterprise was founded six years before the BIT between Ukraine and Lithuania entered into force").[*Tokios Tokeles*]. *Autopista* at para 122 ("The actual circumstances prevailing in this case confirm this finding. Indeed, the Tribunal has found no indication supporting Venezuela's assertions that Icatech would be a corporation of convenience exerting a purely fictional control for jurisdiction purposes or that Aucoven's conduct in the context of the share transfer would have been misleading"). *Mobil v Venezuela* at para. 183, 204-205 ("the aim of the restructuring of their investments in Venezuela through a Dutch holding was to protect those investments against breaches of their rights by the Venezuelan authorities by gaining access to ICSID arbitration through the BIT. The Tribunal considers that this was a perfectly legitimate goal as far as it concerned future disputes").

[1078] Andreas Ziegler & Jorun Baumgartner, "Good Faith as a General Principle of (International) Law" in Andrew Mitchell, M. Sornarajah & Tania Voon, eds, *Good Faith and International Economic Law* (Oxford: Oxford University Press, 2015) at 35.

[1079] *Tokios Tokeles* at para. 55-56.

shareholders of this entity were Ukrainian nationals who also held full control of the corporation in practice.[1080]

They subsequently brought a claim against Ukraine in ISA.[1081] In *Tokios Tokeles*, the majority of the tribunal ruled that "the origin of the capital is not relevant".[1082] The majority also held that "none of the Claimant's conduct with respect to its status as an entity of Lithuania constitutes an abuse of legal personality" and that there was "no evidence" that "the Claimant used its formal legal nationality for any improper purpose".[1083]

One arbitrator, Prosper Weil, dissented.[1084] Weil agreed with the majority that the claimant did not create the corporate entity in Lithuania solely to gain access to the system of investment protection or manipulate its nationality.[1085] He emphasized that the ICSID Convention and an applicable BIT govern disputes only between host states and foreign nationals.[1086] According to Weil, in *Tokios Tokeles*, this was not the case as the dispute concerned Ukraine and the Ukrainian investors.[1087] The majority of the tribunal failed to look "behind the legal structure chosen by the parties".[1088] Weil concluded that ICSID "is meant to protect – and thus encourage – international investment".[1089] In Weil's view, the *Tokios Tokeles* majority expanded the application of the Convention beyond its limits, to the point that it could "dissuade Governments […] from adhering to

[1080] *Ibid*.
[1081] *Ibid* at para.22.
[1082] *Ibid* at para.80.
[1083] *Ibid* at para.56.
[1084] *Tokios Tokeles v Ukraine*, Dissenting Opinion of Prosper Weil.
[1085] *Ibid* at para.21.
[1086] *Ibid*.
[1087] *Ibid*.
[1088] *Ibid* at para.16.
[1089] *Ibid* at para.30.

the Convention" or "from providing for ICSID arbitration in their future BITs or investment contracts".[1090]

The *Tokios Tokeles* case teaches two lessons in relation to abuse of process in the context of corporate restructuring. First, these determinations usually turn on whether the claimant corporation was created for the sole purpose of accessing the protections guaranteed under the investment regime. Second, it illustrates tribunals' narrow application of abuse of process, limited to situations of corporate restructuring in anticipation of foreseeable dispute[1091] and do not always apply to the cirumctances such as those in *Tokios Tokeles*, i.e. when the nationals of a state A control a corporation in a state B to sue a state A in ISA. Sornarajah concludes that "good faith has not triumphed" in *Tokios Tokeles* but,

> rather, a system has been created that enables fraud to be perpetrated on the respondent state so that funds originating from it can be cycled back with the protection of an investment treaty when such funds are channelled through a company incorporated in the treaty partner.[1092]

Perhaps Sornarajah's wording that the system "enables fraud" is too strict; rather the investment regime lacks a consistent and well-developed approach to prevent similar to situations to *Tokios Tokeles*.

4.2.2.2 Investor Initiates Multiple Investment Arbitration Proceedings

Gaillard describes an experience as arbitration counsel as follows,

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[1090] *Ibid*.
[1091] *Ibid* at para.102 ("[t]here is a line of consistent decisions of arbitral tribunals on objections to jurisdiction based on abuse of the investment treaty system"; the tribunal considers "the timing of the purported investment, the timing of the claim, the substance of the transaction, the true nature of the operation49, and the degree of foreseeability of the governmental action at the time of restructuring").
[1092] M Sornarajah, "Good Faith, Corporate Nationality, and Denial of Benefits" in Andrew Mitchell, M Sornarajah & Tania Voon, eds, *Good Faith and International Economic Law* (Oxford: Oxford University Press, 2015) at 133.

> I act as counsel in an on-going matter involving four parallel arbitrations concerning the same dispute […] Seeking to multiply their chances of obtaining recovery, these related parties dragged our clients through a series of four full-blown proceedings before four different tribunals, each with two-week hearings involving essentially the same fact witnesses and experts.[1093]

The problem of multiple proceedings is reinforced by the decentralized nature of the investment regime; "[t]he large number of BITs in place increases the risk of duplication of proceedings".[1094] To protect their assets, foreign investors often attempt to utilize different IIAs to maximize protection guaranteed under the investment regime. The multiplication of proceedings is an easy strategy to amplify claimants' chances to obtain recovery.

Tribunals do not always punish such strategies For example, in the *CME* and *Lauder* disputes, the *CME* tribunal declined to hold that the parallel proceedings constituted an abuse of process.[1095] The cases involve the same facts, related parties and similar investment rights. Ronald Lauder, an investor from the USA, expressed interest to

[1093] Gaillard (2017), at 1.
[1094] Loukas Mistelis & Julian Lew, *Pervasive Problems in International Arbitration* (The Hague: Kluwer Law International, 2006) at 347.
[1095] *Lauder* at para.43, 107-110. *CME v Czech Republic* (2001), Partial Award (United Nations Commission on International Trade Law) (Arbitrators: Wolfgang Kühn, Stephen M. Schwebel, Jaroslav Hándl) (United Nations Commission on International Trade Law) at para.40-47. [*CME*] Andreas Ziegler & Jorun Baumgartner, "Good Faith as a General Principle of (International) Law" in Andrew Mitchell, M Sornarajah & Tania Voon, eds, *Good Faith and International Economic Law* (Oxford: Oxford University Press, 2015) at 35. Campbell McLachlan, *Lis Pendens in International Litigation* (The Hague: Martinus Nijhoff Publishers, 2009) at 284-285 (discussing the arguments of the two tribunals on abuse of process and noting that Czech Republic, as respondent, did not seek to consolidate proceedings). Cameron Miles, *Provisional Measures before International Courts and Tribunals* (Cambridge: Cambridge University Press, 2017) at 383 ("the Lauder/CME debacle could have been avoided in three ways. In first place, as suggested by Crawford, the CME tribunal could have stayed its proceedings until the Lauder Tribunal determined that it lacked jurisdiction - an exercise of comity as between international tribunals. In the second, it could have determined that CME in bringing the case was engaged in a clear abuse of the Tribunal's process and deemed its claims inadmissible as a result"). Andrea Bjorklund, "Legitimacy of ICSID" in Harlan Grant Cohen et al, eds, *Legitimacy and International Courts* (Cambridge: Cambridge University Press, 2018) at 250 (discussing the pressing problem of parallel proceedings in the investment regime given the multiplicity of IIAs). Chester Brown, "The Relevance of the Doctrine of Abuse of Process in International Arbitration" (2011) 8:2 TDM 1at 1-3, 6 ("international courts and tribunals should be regarded as having the power summarily to dismiss proceedings as an abuse of process if they arise out of the same facts, and if they seek the same remedies as another international claim").

create a private TV company in the Czech Republic. After consultations, the Media Council of the Czech Republic approved a license under the condition that foreign investment will occur through the joint venture.[1096] The TV station launched broadcasting. After some time, the Czech Parliament introduced changes into the local law that negatively impacted the TV station. Subsequently, the government agencies launched a criminal investigation against Mr. Lauder and the joint venture that managed the TV station.

Eventually, Lauder and his investment vehicle CME brought two separate claims against the Czech Republic for violation of the FET, FPS, and expropriation standards under the applicable IIAs. Lauder in his personal capacity challenged the Czech Republic under the *Netherlands-Czech Republic BIT* and CME brought a claim under the *US-Czech Republic BIT*. Franck observes that both BITs have "similar prohibitions on the arbitrary and discriminatory treatment of investments".[1097] Nevertheless, the tribunals arrived at absolutely different conclusions.[1098] Specifically, the tribunals disagreed on what under the applicable BITs constitutes a discriminatory and arbitrary measure.[1099] The tribunals also had conflicting views on whether there was expropriation or a violation of FET on behalf of the Czech Republic.[1100] In short, they disagreed on just about everything.[1101] The Lauder arbitrations demonstrate that first, the tribunals can in

[1096] *Ibid*. [*Lauder*].
[1097] *Ibid*.
[1098] August Reinisch, "The Proliferation of International Dispute Settlement Mechanisms: The Threat of Fragmentation vs. the Promise of a More Effective System? Some Reflections from the Perspective of Investment Arbitration" in Isabelle Buffard & Gerhard Hafner, eds, *International Law Between Universalism and Fragmentation: Festschrift in Honour of Gerhard Hafner* (The Hague: BRILL, 2008) at 116.
[1099] *Ibid*.
[1100] Reinisch (2008), at 116. *Lauder* at para.292-293. *CME*, Partial Award at para. 611 (shows divergence on FET).
[1101] Reinisch (2008), at 116.

principle arrive at contradictory decisions without fear of any repercussions; and second, that tribunals can interpret and apply legal norms differently even when they deal with identical facts. The two issues are related yet distinct. The fact that tribunals can arrive at contradictory decisions even when the facts are the same shows that there is no structural corrective device or sanction against such contradictory decisions. In other words, the first issue relates not to the content of the decisions but to the structures of the regime. The second issue is concerned with the content of the applicable law, and showcases the potential for diverging interpretations in the investment regime, a major factor producing uncertainty over the content of the applicable law.

Most importantly for the purposes of this thesis, the *CME* and *Lauder* cases demonstrate the inability of tribunals to prevent the multiplication of proceedings by applying abuse of process. According to the tribunal in *CME*, "there is also no abuse of the Treaty regime by Mr. Lauder in bringing virtually identical claims under two separate Treaties".[1102] Interestingly, the tribunal never defined abuse of process. Brown points out that the *CME* tribunal "would have been well served by a more detailed examination of the concept of abuse of process" and could have employed abuse of process to manage the multiplicity of proceedings.[1103] In my view, the refusal of the *CME* tribunal to engage with abuse of process illustrates the overly cautious use of the doctrine by ISA tribunals.

The multiplication of proceedings puts a respondent in a disadvantageous position, having to waste resources to defend duplicative claims in various venues. But multiple proceedings are problematic not only from a respondent's perspective but also from a perspective of the investment regime as a political system. If the tribunals do not

[1102] *CME* at para.412.
[1103] Brown (2007), at 249.

preclude multiplication of proceedings and enable investors to seek double recovery, the states may lose confidence in credibility of the investment arbitration as an effective forum for resolving disputes.

In the absence of a hierarchy among ISA tribunals, multiple proceedings may result in conflicting outcomes. Reinisch explains that "[w]here investment tribunals produce inconsistent or even conflicting awards, one of the central values of any rule-based system of law, that is, predictability, is lost".[1104] This is not a merely hypothetical danger. Egypt recently faced two investment claims that were apparently brought for the benefit of a single foreign investor. Yosef Maiman, a dual national of Poland and Israel, filed a claim against Egypt under the ICSID Convention and the *Poland-Egypt BIT*.[1105] Simultaneously, the Ampal-American Israel corporation (controlled by Mr. Maiman) also initiated an ad hoc arbitration against Egypt under the UNCITRAL Arbitration Rules. The tribunal in *Ampal-American Israel Corporation v Egypt* set out the circumstances in which multiple proceedings would be tantamount to an abuse of process. According to the tribunal in *Ampal*, the "double pursuit of the same claim in respect of the same interest" may constitute an abuse of process only once both fora have affirmed jurisdiction.[1106]

In these proceedings, the bad faith of the claimant can be considered as a factor in tribunal's assessment of abuse of process. After finding that Ampal had no bad faith in

[1104] Reinisch (2010), at 115.
[1105] *Ampal-American Israel Corporation and others v Arab Republic of Egypt* (2016), Decision on Jurisdiction ICSID Case No ARB/12/11 (International Centre for Settlement of Investment Disputes) (Arbitrators: Yves Fortier, Campbell Mclachlan, Francisco Orrego Vicuña) at 331. [Ampal]
[1106] *Ibid* at para.333. ("The consequence of this finding, together with the balance of the present Decision on Jurisdiction, is that the abuse of process constituted by the double pursuit of the MAGL portion of the claim in both proceedings must now be treated as having crystallised. Both Tribunals have confirmed that they have jurisdiction. It follows from this therefore that there is no risk of a denial of justice occasioned by the absence of a tribunal competent to determine the MAGL portion of the claim. Both Tribunals are seised of the merits and neither Tribunal has yet reached a decision on the merits").

pursuing two parallel claims, the tribunal permitted the claimant to "submit the MAGL portion of the claim […] to the exclusive jurisdiction of the present Tribunal".[1107] The tribunal concluded that in so doing, Ampal will "relinquish" the MAGL portion of the claim in concurrent arbitration.[1108] Gaillard has criticized this decision on the ground that "[t]he tribunal's generosity towards the claimants sits somewhat uncomfortably with its concurrent finding that, pursuant to article 26 of the ICSID Convention, once the claimants had given their consent to ICSID arbitration, they had lost their right to seek relief in another forum".[1109]

Other tribunals have also held that multiple proceedings do not automatically signal an abuse of process. In *Waste Management*, the investor launched two separate proceedings under NAFTA.[1110] Mexico argued that such conduct constituted an abuse of process because "a disputing investor may have one but only one attempt at an international arbitration under Chapter 11".[1111] The tribunal rejected this interpretation, saying:

> [n]o doubt the concern of the NAFTA parties in inserting Article 1121 *was to achieve finality of decision and to avoid multiplicity of proceedings*. But where the first proceeding produces no decision on the merits because of a jurisdictional barrier, there is nothing in Chapter 11 which expressly or impliedly prohibits a second proceeding

[1107] *Ibid* at para. 334, 338. ("such an election would secure to Ampal in the present arbitration the advantages of the ICSID Convention, upon which it places special reliance, whilst removing the abuse constituted by the double pursuit of the same claim").
[1108] *Ibid*.
[1109] Emmanuel Gaillard (2017), at 9.
[1110] *North American Free Trade Agreement Between the Government of Canada, the Government of Mexico and the Government of the United States*, 17 December 1992, Can TS 1994 No 2 (entered into force 1 January 1994) [*NAFTA*]. *Waste Management, Inc. v United Mexican States Phase Two* (2002), Mexico's Preliminary Objection Concerning the Previous Proceedings Decision of the Tribunal ICSID Case No. ARB(AF)/00/3 (International Centre for Settlement of Investment Disputes) (Arbitrators: James Crawford,Benjamin Civiletti, Eduardo Magallón Gómez) [Waste Management 2].
[1111] *Ibid* at para.26.

> brought after the jurisdictional barrier has been removed.[1112]

Two conclusions can be drawn from the *Waste Management* approach. First, the tribunal in *Waste Management* signaled that multiple proceedings are problematic in the investment regime, as they inhibit "finality". Second, the tribunal concluded that multiple proceedings do not always constitute an abuse of process. In particular, the claim will not be an abuse of process if a claimant brings a claim after jurisdictional obstacles were removed on condition that the previous proceedings did not reach the decision on merits. Of course, strictly speaking, this tribunal's conclusion is relevant only to NAFTA and possibly to other treaties with similarly-worded provisions.

It is important to emphisize that tribunals typically permit claimants to "cure" an abuse of process. For example, in *Ampal,* the tribunal provided the claimant with an opportunity to select one forum in which to pursue its claim. In my view, such permissiveness removes any disincentives for claimants to engage in multiple proceedings. For claimants, the potential benefit of multiple proceedings is high—it increases the chances of obtaining relief—while the cost of engaging in simultaneous proceedings is comparatively low. Even if the claimant undertakes "double pursuit of the same claim in respect of the same interest",[1113] the tribunal can permit the claimant to cure the abuse of process by withdrawing from one proceeding. As has been discussed earlier in this thesis, structural incentives can influence litigation conduct and may encourage certain types of conduct if the cost for the claimant is low and possibility of

[1112] *Ibid* at para.27. [Emphasis added]
[1113] *Ampal* at para.331.

reward is high.[1114] The possibility to cure an abuse of process lowers the transactional costs of bringing the claim.

4.2.2.3 Claims that Contradict the Purpose of Investment Arbitration

The third category of abuse of process claims identified by Gaillard occurs where "parties have sought to instrumentalize the arbitral process by initiating one or more arbitrations for purposes other than the resolution of genuine disputes, in clear violation of the spirit of international arbitration law".[1115] As two examples of such conduct, Gaillard cites an unnamed ICC arbitration involving a German state-owned company, which brought an arbitration claim in order to to gain publicity,[1116] and *Rompetrol Group NV v Romania*, where the claimant allegedly launched the arbitration solely in order to "to terminate or to hinder legitimate criminal proceedings and investigations in Romania".[1117]

In *Rompetrol*, the tribunal refused to recognize that the claimant's conduct as constituting an abuse of process. The viability of Gaillard's third category may, however, be supported by the tribunal's decision in *Saipem SpA v The People's Republic of Bangladesh*. In *Saipem*, the tribunal noted that "[i]t is generally acknowledged in international law that a State exercising a right for a *purpose* that is different from that for which that right was created commits an abuse of rights".[1118] The tribunal in *Saipem* emphasized that the "purpose" of the legal right matters; an abuse of process occurs when a party invokes a legal right to achieve goals in contradiction to the "purpose" of the legal right.

[1114] Sections 4.1.1.2 and 1.1.1.2.
[1115] Gaillard (2017), at 10.
[1116] *Ibid*.
[1117] *RomPetrol v Romania* at para.59.
[1118] *Saipem* at 160. [emphasis added]

This interpretation of abuse of process seems to echo Josserand's approach, which has informed the understanding of the concept across many civil law jurisdictions.[1119] Calboli and Lee explain that Josserand's idea was that "private law is not simply about coordinating private interests but rather creating mechanics or instruments involved in the greater social engineering".[1120]

If applied in ISA, such an approach may result in serious challenges. The decentralized *ad hoc* nature of investment tribunals makes it difficult for the arbitrators to justify a reference to the overall purpose of the investment regime when they have a clear mandate to adjudicate a single dispute between two identified parties.As Schill and Kingsbury observe, "individual tribunals cannot easily have regard to system-level concerns given their mandate and primary responsibilities to solving an individual dispute submitted by the disputing parties in any single case".[1121] Tribunals' mandate to adjudicate a dispute between the parties – and no more[1122] – makes it difficult (and some argue undesirable in principle) for the tribunals to engage actively in any sort of "social engineering".[1123] If tribunals were to engage in such social engineering, the arbitrators

[1119] Eva Steiner, *French Law: A Comparative Approach* (Oxford: Oxford University Press, 2018) at 53.
[1120] *Ibid*.
[1121] Stephan Schill & Benedict Kingsbury, Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law, IILJ Working Paper 2009/6, online:<http://www.iilj.org/wp-content/uploads/2016/08/Kingsbury-Schill-Investor-State-Arbitration-as-Governance-IILJ-WP-2009_6-GAL.pdf> at 4.
[1122] *Glamis Gold* at para.3 (This Tribunal was constituted to address a particular dispute between Glamis and the United States of America. In this sense, the Tribunal sees its mandate under Chapter 11 of the NAFTA as similar to the case-specific mandate ordinarily found in international commercial arbitration […] Notwithstanding the likelihood that numerous arbitrations would arise under Chapter 11 of the NAFTA, the three states of North America did not establish a standing adjudicative body but rather chose to have arbitrations resolved by distinct arbitral panels. In this sense, it is clear that this Tribunal is asked to have a case-specific focus as it proceeds to address this dispute). *Saipem* at para. 67. (The Tribunal […] believes that, subject to the specifics of a given treaty and of the circumstances of the actual case, it has a duty to seek to contribute to the harmonious development of investment law and thereby to meet the legitimate expectations of the community of States and investors towards certainty of the rule of law). *Saluka* at para.299.
[1123] Michael Reisman, "Case Specific Mandates versus Systemic Implications: How Should Investment Tribunals Decide?:The Freshfields Arbitration Lecture" (2013) 29:2 Arb Intl 131 at 132. (argues that

would have to set aside the "case-specific and rule-text-based" approach in favour of "policy-and-context" based thinking.[1124] Although the "policy-and-context" approach may be desirable for permanent courts, tribunals of an *ad hoc* nature that function in the decentralized system can face serious obstacles, even if they wanted to pursue such an approach.[1125] For example, the *ad hoc* authority of the tribunal permits the arbitrators to discuss the purpose of the regime only in the context of a single dispute; among arbitrators, there may be disagreement as to the purpose of the investment regime, the purpose of the rights granted to investors under IIAs, or which particular actions might constitute a "clear violation of the spirit of international arbitration law".

4.2.2.4 A Party's Conduct Violates Integrity of Investment Arbitration Process

Gaillard completes his analysis of abuse of process with the above three categories. However, *Waste Management v Mexico* seems to identify a basis for abuse of process that does not fit into any of Gaillard's categories. The tribunal only mentioned that Chapter 11 of NAFTA, ICSID Convention or Rules do not explicitly confer any power to the tribunal to dismiss the claim as an abuse of process. The tribunal, however, observed that "if such a power exists*, it would only be for the purpose of protecting the integrity of the Tribunal's processes or dealing with genuinely vexatious claims*".[1126]The tribunal in *Waste Management* never identified which investment claims are "genuinely

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subject to narrow exceptions, the tribunals "should confine themselves to a case-specific methodology[…]Notwithstanding the likelihood that numerous arbitrations would arise under Chapter 11 of the NAFTA, the three states of North America did not establish a standing adjudicative body but rather chose to have arbitrations resolved by distinct arbitral panels. In this sense, it is clear that this Tribunal is asked to have a case-specific focus as it proceeds to address this dispute.").

[1124] *Ibid* at 133.

[1125] *East Timor* (*Portugal v Australia*), 1995 ICJ 90 (separate opinion of Judge Ranjeva) (citing Sir Robert Jennings, The Role of the International Court of Justice in the Development of International Environmental Protection Law). ("Ad hoc tribunals can settle particular disputes; but the function of the established 'principal judicial organ of the United Nations' must include not only the settlement of disputes but also the scientific development of general international law . . . there is therefore nothing strange in the ICJ fulfilling a similar function for the international community").

[1126] *Waste Management* 2 at para.49. [Emphasis added]

vexatious",[1127] nor did it specify what claims may interfere with the "integrity of the tribunal's processes" to the extent that it would require dismissal. However, another case, *Cementownia v Turkey,* sheds some light on this issue.[1128] In *Cementovina*, the claimant submitted fraudulent documents to show that the investment transaction had occurred. The tribunal "condemned" such conduct as "a manifest abuse of the international institutional arbitration system".[1129] The tribunal dismissed the claim and required the claimant to bear the respondent's legal fees and expenses.

A further example in this fourth category may be *Renco v Peru*. In *Renco*, the investor alleged that Peru's conduct in the proceedings constituted an abuse of process. In particular, Peru raised an objection to jurisdiction at a late stage in the proceedings.[1130] In its objection, Peru emphasized that Renco could only bring a claim against Peru on the basis of the *United States–Peru Trade Promotion Agreement* (TPA);[1131] TPA article 10.18.2(b) provided that an investor must accompany its request for arbitration with written waiver of "of any right to initiate or continue before any administrative tribunal or court under the law of any Party, or other dispute settlement procedures, any proceeding with respect to any measure alleged to constitute a breach".[1132] In short, Peru argued that Renco failed to comply with these requirements.

Peru did not raise its waiver objection until 2014, three years after Renco's application to arbitrate.[1133] The tribunal observed that it was "troubled […] by the *manner*

[1127] *Ibid* at para.49-50.
[1128] *Cementownia Nowa Huta S.A. v Republic of Turkey* (2009), Award ICSID Case No. ARB(AF)/06/2 (International Centre for Settlement of Investment Disputes) (Arbitrators: Pierre Tercier,Marc Lalonde, Christopher Thomas).
[1129] *Ibid* at para.162.
[1130] *Renco v Peru*, Partial Award on Jurisdiction at para.123-124.
[1131] *United States–Peru Trade Promotion Agreement* (2006), at art.10.18.2(b).
[1132] *Ibid*.
[1133] *Renco v Peru*, Partial Award on Jurisdiction at para.180

in which Peru's waiver objection arose in this arbitration".[1134] The tribunal concluded that "Peru has no duty to arbitrate Renco's claims under the Treaty unless Renco submits a waiver" in compliance with the applicable treaty.[1135] The tribunal noted that it would not "rule out the possibility that an abuse of rights might be found to exist if Peru were to argue in any future proceeding that the Renco's claims were now time-barred […] if that scenario should arise, Renco's submission that Peru's conduct with respect to its late invokation of the waiver objection constitutes an abuse of rights.".[1136]

As the above four scenarios demonstrate, ISA tribunals tend to find that an abuse of process has occurred in highly limited circumstances. The application of abuse of process remains flexible, and tribunals retain extensive discretion when to recognize the claim as an abuse of process. Yet the ISA tribunals appear to take a cautious approach in labelling a claim as an abuse of process and even permit claimants to "cure" abuse of process in some cases. The combination of a high threshold to establish abuse of process and the possibility to "cure" investor claims means that claimants may engage in manipulative strategies without any serious risk of being barred from gaining the investment regime's protections.

4.3 Preliminary Observations: Challenges

Chapter Four pursued a number of objectives. It explained why claimants bring frivolous and abuse of process claims. It revealed that arbitrators are overly cautious in dismissing investors' claims as frivolous or abuse of process. It showed that domestic legal systems put the judges in charge of identifying and dismissing frivolous and abuse of process claims, and that this basic model has been copied in the investment regime.

[1134] *Ibid* at para.123 (emphasis added).
[1135] *Ibid* at para.186.
[1136] *Ibid* at para.187-188.

Thus, the mechanisms for the dismissal of frivolous and abuse of process claims were as adopted from the "most familiar solution", rather than being conceived anew for the ISA context. While in principle there is nothing wrong with empowering the adjudicators to identify and dismiss frivolous and abuse of process claims early, in the context of the investment regime, such an exercise is complicated by several factors that relate to the systemic features of the investment regime. These will be discussed in greater detail in Chapter Five. As Chapter Five will show, these systemic features can hinder the effectiveness of the existing mechanisms for mechanisms for frivolous and abuse of process claims. The transplantation of the procedural mechanisms without appreciation of the systemic features of the legal system at hand, has resulted in ineffectiveness of the mechanisms for dealing with frivolous and abuse of process claims.

Chapter 5

The Mechanisms for Dismissal of Frivolous and Abuse of Process Claims in the Systemic Context of International Investment Regime

As Chapter Three has established, in the investment regime the arbitrators are in charge of dismissing frivolous and abuse of process claims. Once a tribunal is constituted, and not before, the respondent may bring a preliminary objection that a claim is frivolous and request the tribunal to dismiss such claim *in limine*. In law and even more so in practice, the respondent must meet a high threshold to succeed on either of these motions.[1137]

By contrast, under existing laws and rules, an abuse of process claim cannot be dismissed on the basis of the preliminary objection. To achieve the dismissal of an abuse of process claim, a respondent can pursue two strategies. First, a respondent can file for bifurcation of the proceedings into jurisdictional and merits stages. At the jurisdiction stage, the respondent can raise a defence that a claim constitutes an abuse of process. If the respondent can show an abuse of process, the claim will be dismissed as inadmissible and the tribunal will not proceed to consider the merits. Second, a respondent can raise a defence of abuse of process without filing for bifurcation. In this case, the tribunal proceeds by first establishing its jurisdiction and then examining whether the investor's claim is inadmissible as an abuse of process.

In a fashion similar to domestic legal systems, the mechanisms for the dismissal of frivolous and abuse of process claims put the adjudicators seized of the claim on the

[1137] *MOL Hungarian Oil* at para.44. (Tribunal observes "[t]here is no dispute between the Parties that the standard is a high one").

merits (i.e. the arbitrators) in charge of identifying and dismissing such claims. Arbitrators thus performs a gatekeeping function within the investment regime, keeping out frivolous and abuse of process claims. In practice, however, while arbitrators safeguard their discretion to exercise dismissal depending on the circumstances of each particular case, they actually dismiss claims as frivolous or abuses of process only in an overly narrow set of circumstances. From outset, it seems appropriate to delegate the assessment of allegedly of frivolous or abuse of process claims to a neutral third-party decision-maker like the arbitral tribunal. However, the question is whether the investment regime's incentives and structures enable the arbitrators to effectively fulfil this gatekeeping function.

The central goal of this chapter is to explain why the structures and incentives make actual dismissal of frivolous and abuse of process claims possible only in overly narrow circumstances under the current rules, and why even if the rules regarding dismissal were expanded in scope, claims would continue to be dismissed in overly narrow circumstances. There are two main reasons.

First, there is the meta-level problem of the decentralized institutional infrastructure of the investment regime within which arbitrators operate. In particular, the decentralized composition of authority makes inevitable a greater degree of legal uncertainty than can persist in domestic legal systems, with their unified executive, legislative, and judiciary and their hierarchical court structures. The lack of structures that encourage certainty, such as judicial hierarchy and systems of precedent, reinforce the ambiguity of legal norms within the regime. These factors combine to create a situation where arbitrators cannot be sure (particularly at a dispute's early stages) whether a claim

truly lacks merit altogether, and where even if they think it does, they would feel reluctant to dismiss the claim without a full hearing.

Moreover, the dismissal of an investor's claim as abuse of process requires tribunals to envision the broad purposes of the investment regime that such a claim subverts, an objective that is difficult to achieve for arbitrators (sometimes one-shot appointees) who preside in *ad hoc* tribunals within a decentralized system that lacks any single, overarching purpose. Even if the tribunals consier that such a purpose exists, they may be even more reluctant than national court judges to "legislate from the bench" or "make policy", and see their role to decide as narrowly as possible the particular dispute the parties have empowered them to adjudicate.

The second problem is the institutional incentives within the investment regime and, in particular, how the structural features of ISA, such as the party-driven appointment procedure, absence of tenure, and lack of rotation of assignments, perpetuate these incentives. Arbitrators are social actors subject to a variety of monetary and non-monetary incentives, which the current institutional set-up of the investment regime reinforces. These incentives influence the reluctance of the arbitrators to dismiss frivolous and abuse of process claims early in the proceedings and may even encourage them to dismiss claims only in the most glaringly obvious cases.

The intent of this chapter is not to criticize the mechanisms for the dismissal of frivolous and abuse of process claims on their own but to look at these mechanisms in the context of the system in which they have been deployed. As has been discussed in Chapter One, this approach is inspired by the comparative law literature on legal transplants. Langer's study on the transplantation of American plea bargaining into civil

law legal systems is illustrative. Langer shows that civil law jurisdictions set out to "transplant" American-style plea bargaining into their systems, but in fact "translated" plea-bargaining so that it diverged dramatically from the standard practices in the American legal system. To understand how plea bargaining was translated into various civil law systems, Langer examines the different ways in which legal systems "arrange powers and responsibilities between the main actors of the criminal process" within their distinctive procedural cultures.[1138] Langer concludes that to understand and evaluate these procedural mechanisms as they came to operate in different recipient legal systems, it is necessary to understand the arrangement of powers and responsibilities within those legal systems, their social dynamics, and the incentives these create for decision-makers.

Comparative law scholarship on legal transplants thus shows the need to maintain awareness of the system in which transplanted legal norms, institutions, and principles operate. Roberts explains that "[i]nvestment treaties have traditionally been short and vaguely worded, while the system as a whole is new and undertheorized. As a result, participants routinely draw on comparisons with other legal fields when seeking to fill gaps, resolve ambiguities, or understand the system's nature".[1139] According to Roberts, such comparisons are made on both the "micro" level, "with analogies being drawn using cases and principles from related legal areas", and the "macro" level, "with other legal fields being used as paradigms or frameworks for understanding the nature of the investment treaty system as a whole".[1140] The mechanisms for the dismissal of frivolous and abuse of process claims in the investment regime are not an exception, and have been

[1138] Chapter 1, section 1.3. Langer (2004), at 5.
[1139] Anthea Roberts, "Clash of Paradigms: Actors and Analogies Shaping the Investment Treaty System" (2013) 107:1 AJIL 45 at 46.
[1140] *Ibid*.

modelled after existing mechanisms from domestic legal systems. While borrowing of well-established legal mechanisms may have value, simply copying "off-the-shelf blueprints" can result in mechanisms with limited function. [1141]

This chapter does not argue that the existing mechanisms for early dismissal of claims do more harm than good. To the contrary, expediency in dismissing frivolous and abuse of process claims is a valuable procedural tool,[1142] particularly to reduce unnecessary costs that such claims may impose on the defending governments.[1143] The availability of such mechanisms is especially significant for developing and least developed states, which may lack capacity to uphold costly defences of investors' claims.[1144] In addition, the mere availability of the procedural mechanisms for the dismissal of frivolous and abuse of process claims, even if those mechanisms are invoked

[1141] Different legal systems need different mechanisms to ensure that functioning of such mechanisms is not hindered by systems' features. Randall Peerenboom makes similar point "one of the shortcomings of current rule of law promotion programs is that they tend to prescribe a common set of ―best practices‖ for all countries, notwithstanding the often repeated ―lesson learned about avoiding one-size-fits-all off-the-shelf blueprints". Randall Peerenboom, "Toward a Methodology for Successful Legal Transplants" (2013) 1:1 Chinese Journal of Comparative Law 4 at 4-5.

[1142] Aren Goldsmith, "Trans-Global Petroleum: 'Rare Bird or Significant Step in the Development of Early Merits-Based Claim Vetting" (2008) 26 ASA Bulletin 667.

[1143] Some investors raise a specific demand in their claims with regards to the state's regulatory measure. whether this concern is only perceived or real does not matter in our context, states change and alter the investment regime in **fear** that ISA could serve as a tool to threaten legitimate regulatory policies. For example, Phillip Morris demanded "an order for the suspension of enforcement of plain packaging legislation", later the company dropped this demand and focused on damages only. *Philip Morris Asia Ltd. v. The Commonwealth of Australia*, PCA Case No. 2012-12, Notice of Arbitration, UNCITRAL, 2011. Van Harten & Scott (2016), at 92. Kyla Tienhaara, "Regulatory Chill and the Threat of Arbitration: A View from Political Science" in Chester Brown & Kate Miles, eds, *Evolution in Investment Treaty Law and Arbitration* (Cambridge: Cambridge University Press, 2011) at 606. Vera Korzun, "The Right to Regulate in Investor– State Arbitration: Slicing and Dicing Regulatory Carve-Outs" 50:2 (2017) Vand J Transnatl L 355 at 373-380. Korzun suggests "[t]he concern is that international investment agreements and the ISDS regime have empowered foreign corporations to interfere with a state's ability to regulate for the benefit of the public at large". Gus Van Harten & Martin Loughlin, "Investment Treaty Arbitration as a Species of Global Administrative Law" (2006) 17 :1 Eur J Intl L 121 at 124. ("[t]his growth [of investment treaty arbitration] suggests that multinational enterprises are increasingly prepared to use investment arbitration to resolve disputes with states, indicating that investment arbitration has become an important method for foreign investors to resist state regulation and seek compensation for the costs that flow from the exercise of public authority"). Gus Van Harten et al, *An Open Letter to the Parliament of Wallonia and Belgian Voters on the Proposed CETA and Its Foreign Investor Protection System*, online:< http://www.s2bnetwork.org/wp-content/uploads/2016/10/Canadian-academics-open-letter-on-the-CETA-and-Wallonia.pdf>.

[1144] Gottwald (2007), at 227.

rarely, can enhance the effectiveness of arbitration as a dispute resolution mechanism.[1145] Finally, the availability of such mechanisms is important from a systemic perspective, to enhance the legitimacy of the investment regime, especially from the perspective of the states that constituted and perpetuate that regime.

However, it is difficult to overlook the problems that the operation of these mechanisms can produce in the context of the investment regime, particularly if the balance between the interests of an investor and a state is struck. The first concern is that foreign investors will lose their opportunity to air their claims fully, which may result in a re-politicization of disputes that ISA was intended to depoliticize,[1146] and which "may limit and frustrate access of investors to obtain a neutral and independent decision on their cases/claims".[1147] The former may be particularly relevant concern if the tribunals fail to strike an appropriate balance between the right of respondents to dispose of frivolous or abuse of process claims as early as possible in the proceedings and the right of claimants to receive due process.[1148]

[1145] UK, HC 804 Transatlantic Trade and Investment Partnership. Great Britain: Parliament: House of Commons: Business, Innovation and Skills Committee (London: Stationery Office, 2015) at 15.

[1146] Some investment tribunals also support a position that a central value of ISA is an insulation of law from politics i.e. depoliticization. *Banro American Resources, Inc. and Société Aurifère du Kivu et du Maniema S.A.R.L. v DRC* (2000), Award ICSID Case No ARB/98/7 (International Centre for Settlement of Investment Disputes) (Arbitrators: Carveth Harcourt Geach, Alioune Diagne, Prosper Weil) at para. 15-21. *Corn Products International, Inc v Mexico* (2008), Separate Opinion of Andreas Lowenfeld ICSID case No ARB(AF)/04/01 (International Centre for Settlement of Investment Disputes) (Arbitrators: Christopher Greenwood, Andreas Lowenfeld, Jesus Alfonso Serrano de la Vega) at para 1. [*Corn Products*, *Separate Opinion of Andreas Lowenfeld*]. Anthea Roberts, "Triangular Treaties: The Extent and Limits of Investment Treaty Rights" (2015) 56 Harv Intl LJ 353 at 390. (Roberts also discusses three most common understandings of depoliticization in the investment arbitration literature).

[1147] European Commission, Commission Staff Working Document: Report Online Public Consultation on Investment Protection and Investor-to-State Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership Agreement (TTIP), at 22 [EU Public Consultation]. Globex v Ukraine at para.33, 34 (the tribunal emphisized that in the application of Rule 41 (5) of the ICSID Arbitration Rules, it is concerned with providing the claimant "a proper opportunity to be heard, both in writing and orally". The tribunal also emphasized the need to maintain the balance between the due process and the right of the party file an objection to dismiss the claim under Rule 41(5)).

[1148] Friedrich Rosenfeld, "Early Dismissal of Claims" in Andreas Kulick, *Investment Arbitration in Reassertion of Control over the Investment Treaty Regime* (Cambridge: Cambridge University Press, 2016)

Second, the mechanisms further contribute to the process known as "formalization" of investment arbitration.[1149] Trakman and Montgomery warn that investment arbitration "laws and procedures increasingly replicate national judicial procedures, national laws and their legal intricacies".[1150] The concern is that further formalization through additional steps and procedures will result in delays that will make arbitration more adversarial and less efficient—that is, more like litigation. For example, in the context of CETA, the ICC expressed a concern that the inclusion of two provisions on the early dismissal of frivolous claims will "lead to unnecessary procedural delays".[1151]

This chapter proceeds in three parts. Part 5.1 discusses the meta-level problem that relates to the decentralized nature of the regime. Part 5.2 examines what incentives the institutional setup of the investment regime yields when arbitral decision-making is concerned. Part 5.3 focuses on social dynamics in the investment regime, and how such dynamics can potentially contribute to ineffectiveness of the mechanisms for the early dismissal of frivolous and abuse of process claims.

5.1 Institutional Features of Investment Regime

This section examines the institutional features of the investment regime and the implications of these features for the early dismissal of frivolous and abuse of process claims. It posits that the decentralized nature of authority within the investment regime,

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at 91. *Global Trading Resource Corp. and Globex International, Inc. v Ukraine* (2010), Award (ICSID Case No. ARB/09/11) (International Centre For Settlement of Investment Disputes) (Arbitrators: Franklin Berman, Emmanuel Gaillard, Christopher Thomas) at para.34

[1149] Leon Trakman & Hugh Montgomery, "The 'Judicialization' of International Commercial Arbitration: Pitfall or Virtue?" (2017) 30 Leiden J Intl L 405.

[1150] *Ibid* at 406.

[1151] European Commission, Commission Staff Working Document: Report, Online Public Consultation on Investment Protection and Investor-to-State Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership Agreement (Brussels, 2015), at 21.

general uncertainty over the content of investment obligations, and manifest lack of structures that promote greater certainty constitute institutional features of the regime that hinder tribunals' ability to dismiss frivolous and abuse of process claims at the early stages.

In particular, these features of the investment regime make inevitable legal uncertainty of a degree not found in well-regulated municipal legal systems. As Andres Rigo Sureda, an arbitrator and former Deputy General Counsel of the World Bank, explains: "uncertainty is not limited to international investment law or international law. It is common to many areas of law".[1152] However, in the investment regime, uncertainty persists at "two levels: the substantive content of the standards and the ad hoc nature of the arbitral tribunals".[1153] These features generate the "perpetual challenge"[1154] of legal uncertainty, characterised by serious disagreements on the content of applicable law in the investment regime. It is difficult to imagine how arbitrators can dismiss claims early in the process as lacking legal merit or abusing process, if they disagree on the standard of review, the content of applicable law, and in some instances even the purpose of IIAs, as well as the role that the tribunals themselves ought to play in the system.

This section discusses, first, the decentralized composition of authority in the regime. Second, it examines the general uncertainty over the content of substantive investment obligations. Third, it addresses the lack of institutional constraints that

[1152] Sureda (2012), at 139.
[1153] *Ibid*.
[1154] Andrea Bjorklund, "Constrains on Power and Authority in International Investment Arbitration" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (The Hague: Martinus Nijhoff Publishers, 2014) at 15 ("these include the scope of the fair and equitable treatment standard and its interaction with the minimum standard of treatment; the appropriate reach of the MFN clause; the definition of investment under the ICSID Convention (and perhaps the definition of investment under other rules as well" and etc).

promote consistent decision-making, such as hierarchy of tribunals and systems of precedent.

5.1.1 Decentralized Composition of the Investment Regime

The term "decentralized composition" is taken from Pauwelyn, who explains it as follows: "[the investment regime] is heavily decentralized and composed of a multitude of bilateral, regional and multilateral treaties (BITs, NAFTA, FTAs, the ECT etc) […] and a diversity of arbitral institutions […] *without* a central authority".[1155]

Decentralization persists in the investment regime on five inter-connected levels.[1156] First, the investment regime is characterized by decentralization of sources of law.[1157] The regime is built on thousands of IIAs, most of them bilateral, that include different parties and often distinctively worded investment standards. This stands in contrast to, for example, the WTO or EU, which are organized around one or a small set of multilateral treaties and a central international organization. Second, rulemaking authority belongs not to a single hegemon legislator, but rather is scattered among multiple states with disparate interests and economic and political positions.[1158] Third, ISA tribunals function without any central authority; there is no hierarchy among the

[1155] Joost Pauwelyn, "Rational Design or Accidental Evolution? The Emergence of International Investment Law" in Zachary Douglas, Joost Pauwelyn & Jorge Viñuales, eds, *The Foundations of International Investment Law: Bringing Theory into Practice* (Oxford: Oxford University Press, 2014) at 14.

[1156] In addition, the service providers that administer the investment disputes are highly decentralized. In particular, there are multiple arbitrations institutions that provide services to facilitate resolution of investment disputes. These institutions are in competition; yet the institutions show slow harmonization of the applicable arbitration rules and practices. SIAC, Proposal on Cross-Institution Consolidation Protocol, online:< http://www.siac.org.sg/69-siac-news/551-proposal-on-cross-institution-consolidation-protocol>. The arbitrators lack a single authority that supervises their activities similar to the bar associations in some domestic jurisdictions.

[1157] Moshe Hirsch, "Sources of International Investment Law" in Andrea Bjorklund & August Reinisch, eds, *International Investment Law and Soft Law* (Northampton: Edward Elgar Publishing, 2012) at 33-34.

[1158] Moshe Hirsch, "Conflicting Obligations in International Investment Law: Investment Tribunals' Perspective" in Tomer Broude & Yuval Shany, eds, *The Shifting Allocation of Authority in International Law: Considering Sovereignty, Supremacy and Subsidiarity* (London: Bloomsbury Publishing, 2008) at 334.

tribunals or a principle of *stare decisis* to ensure consistent application and interpretation of the applicable legal norms.[1159] Individual ISA tribunals are formed on an *ad hoc* basis for individual disputes. These tribunals produce decisions that may be contradictory, as none is bound to follow any other's decisions.[1160] Fourth, the system depends on domestic courts (and, for non-ICSID awards, on state legislation implementing the New York Convention) to enforce awards and for support during the arbitration process.

Finally, the decentralized composition of the regime reveals itself in the structure of authority delegation, in particular that states delegate authority to tribunals to resolve investment disputes.[1161] Accordingly, states and ISA tribunals share the domain of authoritative decision-making within the regime. Investors also participate in that authoritative decision-making, through contracts with states that can supersede treaty provisions and through their power to appoint arbitrators.[1162] Decentralization pervades the investment regime, including with respect to the meta-questions of *who* is empowered to generate authoritative decisions and *how*.

From the perspective of a political system, such decentralization is problematic; when a number of individual actors independently produce authoritative decisions, such

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[1159] *Ibid*.

[1160] UN, Reform of Investor-State Dispute Settlement: In Search of a Roadmap, IIA Issues Note No.2(June 2013), at 3 ("those arbitral decisions that have entered into the public domain have exposed recurring episodes of inconsistent findings […] [such as] divergent legal interpretations of identical or similar treaty provisions as well as differences in the assessment of the merits of cases involving the same facts"). Jaemin Lee, "Introduction of an Appellate Review Mechanism for International Investment Disputes: Expected Benefits and Remaining Tasks" in Jean Kalicki & Anna Joubin-Bret, eds, *Reshaping the Investor-State Dispute Settlement System: Journeys for the 21st Century* (Hotei Publishing, 2015) at 476 ("(consider […] contradictory decisions from recent investment arbitration proceedings relating to the key definitions of investment, investors or umbrella clause, or the scope of an MFN treatment obligation").

[1161] Andrea Bjorklund, "Constraints on Power and Authority in International Investment Arbitration" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (The Hague: Martinus Nijhoff Publishers, 2014) at 16.

[1162] Jan Ole Voss, *The Impact of Investment Treaties on Contracts Between Host States and Foreign Investors* (The Hague: Martinus Nijhoff Publishers, 2010) at 7-9. Christopher Dugan et al, eds, *Investor-State Arbitration* (Oxford: Oxford University Press, 2011) at 128.

decisions shape actions and reactions of other participants of the system in a contradictory fashion. As a result, there likely to be multiple authoritative approaches to a single legal issue within the system,[1163] an outcome that reinforces uncertainty as to what approach constitutes "good" law. As will be discussed below, the systemic features of domestic legal systems, such as the hierarchy of the courts, system of precedent, centralization of judicial review, and division of powers play an important role because "though the constraints on the judiciary, both imposed and self-imposed that, not only is the law spared an errant or aberrant judiciary, but also the law and legal process obtains coordination, coherence and direction".[1164] The following section examines how lack of judicial hierarchy and formal precedent encourage greater uncertainty over the content of investment obligations.

5.1.1.1.1. Lack of Judicial Hierarchy

This subsection briefly examines the institutional significance of judicial hierarchies for enhancing certainty of legal norms, and reviews the implications of the absence of such hierarchies in the investment regime. Adjudicators (both judges in national legal systems and arbitrators in the investment regime) do not operate alone, but function within the "structure of the legal system".[1165] In contrast to ISA tribunals,

[1163] Anthea Roberts argues that " [i]n theory, treaty parties are supreme when creating the law and tribunals are supreme when applying it in particular cases. In practice, this separation is never complete. How treaty parties interpret and apply the law affects what tribunals decide in particular cases. And tribunal awards in particular cases informally contribute to the interpretation, and thus the creation, of the law. As a result, some interpretive balance exists between treaty parties and tribunals, though neither enjoys ultimate interpretive authority in all circumstances". Anthea Roberts, "Power and Persuasion in Investment Treaty Interpretation: The Dual Role of States" (2010) 104:2 Am J Intl L 179 at 179. Since the ultimate interpretive authority is shared, there may be contradictions in approaches among the interpreters of what the legal standard actually means.

[1164] Edward Thomas, *The Judicial Process: Realism, Pragmatism, Practical Reasoning and Principles* (Cambridge: Cambridge University Press, 2005) at 242.

[1165] *Ibid* at 243.

domestic courts have a hierarchical organization.[1166] The hierarchy of courts is one of the typical features of domestic legal systems[1167] that constrains judicial discretion and ensures broad stability combined with incremental development of national law.[1168] In particular, the possibility of appeal constitutes an important institutional constraint upon judges, who must interpret and apply the law in a fashion that will survive the scrutiny of higher courts.[1169] The possibility of reversal on appeal means that the higher courts play a supervisory role over the lower courts to ensure consistent application and interpretation of the legal norms as well as their clarity.

This structure exists in many states, regardless of what kind of legal system they adopt. For example, in France, the possibility of appeal is realized though a two-tier system of appeal courts and the Supreme Court of Cassation, which may "quash a decision based on an incorrect interpretation" and "instruct the lower court as to the correct interpretation".[1170] In China, the national courts have a hierarchical structure, in which the upper courts review and may overturn the decisions of the lower courts.[1171]

[1166] Tim Koopmans, *Courts and Political Institutions: A Comparative View* (Cambridge: Cambridge University Press, 2003) at 35.

[1167] Ian Greene & James Lorimer , *Final Appeal: Decision-Making in Canadian Courts of Appeal* (Toronto: Lorimer Publishers, 1998) at 140. Gary Slapper & David Kelly, *The English Legal System* (London: Routledge, 2017). Raymond Youngs, *English, French & German Comparative Law* (London: Routledge, 2014) at 98-100. John Henry Merryman & Rogelio Pérez-Perdomo, *The Civil Law Tradition, 3rd Edition: An Introduction to the Legal Systems of Europe and Latin America* (Stanford: Stanford University Press, 2007).

[1168] .Ralf Rogowski & Thomas Gawron, *Constitutional Courts in Comparison: The U.S. Supreme Court and the German Federal Constitutional Court* (New York: Berghahn Books, 2002) at 30.

[1169] Richard Higgins & Paul Rubin, "Judicial Discretion" (1980) 9:1 J Leg Stud 129 at 129.

[1170] John Henry Merryman & Rogelio Pérez-Perdomo, *The Civil Law Tradition, 3rd Edition: An Introduction to the Legal Systems of Europe and Latin America* (Stanford: Stanford University Press, 2007). Eva Steiner, *French Law: A Comparative Approach* (Oxford: Oxford University Press, 2010) at 239. The same is true in Italy. Gianluca Esposito, Sergi Lanau & Sebastiaan Pompe, Judicial System Reform in Italy - A Key to Growth (International Monetary Fund, 2014) at 7.

[1171] Jianfu Chen, "Legal Institutions in the People's Republic of China" in Jianfu Chen, Yuwen Li & Jan Michel Otto, eds, *Implementation of Law in the People's Republic of China* (Hague: Martinus Nijhoff Publishers) at 202, 309. The court structure is similar in Vietnam, another country with a mixed civil law and socialist legal heritage. Nil Nicholson, "Access to Justice in Vietnam" in John Gillespie and Albert

Similarly, un Singapore, the system of courts is hierarchically structured.[1172] In Canada, judicial review is decentralized across the provinces, but is typically depicted as a pyramid with SCC as the court of final review.[1173] First, the hierarchical structure of courts permits greater consistency because the lower courts follow the higher courts. Second, the courts can clarify the legal standards through interpretation.[1174]

In addition to helping to maintain consistent interpretations of the laws through overturning of divergent lower court decisions, the hierarchical structure of the court system creates identifiable incentives for judges that also promote consistency. This pressure may be self-imposed among lower court judges, and emerges out of a desire to avoid criticism and reversals, and to improve their prospects for promotion. US Federal Judge Irving Kaufman explains the influence of social pressure generated by the existence of hierarchical court structures:

> [f]ew judges would long withstand the united importuning of their peers. Even if the judge is slow to accept the suggestion of his brethren, this method is sure to accomplish his ouster faster than a formal procedure. Peer pressure is a potent tool. It should not be underestimated because it is neither exposed to public view nor enshrined in law.[1175]

Anglin, in a comment-response to Kaufman's essay, observes that "Kaufman hints at the power appellate judges have over trial judges housed in the same building" and explains that "peer pressure, statutory removal authority, and appellate review"

Chen, eds, *Legal Reforms in China and Vietnam: A Comparison of Asian Communist Regimes* (London: Routledge, 2010) at 198.

[1172] Walter Woon, "The Doctrine of Judicial Precedent" in Kevin Tan, *The Singapore Legal System* (NUS Press, 1999) at 299-300.

[1173] Ran Hirschl, *Towards Juristocracy: The Origins and Consequences of the New Constitutionalism* (Cambridge: Harvard University Press, 2009) at 20-21.

[1174] Larry Alexander, "Constrained by Precedent" (1990) 63 S Cal L Rev 1.

[1175] Irving Kaufman, "Chilling Judicial Independence" (1979) 88:4 Yale LJ 681 at 709.

constitute powerful tools of influence within judicial community.[1176] In the US context, Klein points out that "consistency can be of indirect benefit to judges insofar as it bolsters the integrity and legitimacy of the judicial system […] even judges who cared nothing for consistency in itself might adopt consistency as an instrumental goal to avoid reversal by the Supreme Court".[1177] Of course, most judges aspire to avoid removals or reversals on appeal that may damage their reputations or their self-esteem. Venzke notes that "judges, like other people, get satisfaction from perceiving that other people view them positively. Judges care about the way they are seen in the eyes of their audiences".[1178] Thus, court hierarchy not only ensures consistency through direct means—reversals of lower court judgments—also by nudging judges to interpret and apply law in a consistent fashion.

The investment regime lacks any form of hierarchy, a feature that gives arbitrators a level of freedom that other adjudicators do not possess.[1179] The tribunals are convened *ad hoc* for each particular dispute between a foreign investor and a state. The arbitrators render a final decision and need not fear reversal of their decisions. Of course, there is the possibility of annulment of awards under the ICSID Convention and refusal of enforcement by the domestic courts pursuant to the New York Convention.[1180] However, the grounds for annulment or refusal of enforcement are strictly limited in comparison

[1176] James Flynn, "Interbranch Removal and the Court of Federal Claims: "Agencies in Drag" (2015) 125:1 Yale LJ 313 at 321.
[1177] David Klein, *Making Law in the United States Courts of Appeals* (Cambridge: Cambridge University Press, 2002) at 17.
[1178] Richard Posner, "What Do Judges and Justices Maximize? (The Same Thing Everybody Else Does)" (1993) 3 Supreme Court Economic Review 1. Ingo Venzke, Judicial Authority and Styles of Reasoning: Self-Presentation between Legalism and Deliberation in Joanna Jemielniak, Laura Nielsen & Henrik Palmer Olsen, eds, *Establishing Judicial Authority in International Economic Law* (Cambridge: Cambridge University Press, 2016) at 242.
[1179] Cornell Clayton & David May, "A Political Regimes Approach to the Analysis of Legal Decisions" (1999) 32:2 Polity 233 at 251.
[1180] Christoph Schreuer & Loretta Malintoppi, *The ICSID Convention: A Commentary* (Cambridge: Cambridge University Press, 2009) at 1042. Jane Jenkins & Simon Stebbings, *International Construction Arbitration Law* (The Hague: Kluwer Law International, 2006) at 301.

with domestic legal systems. The ICSID Convention at art. 52(1) lists an exhaustive legal grounds for annulment, which are limited to jurisdictional and procedural defects.[1181] The New York Convention in article V(1) also provides for strictly limited grounds on which domestic courts to refuse enforcement.[1182] In particular, neither the ICSID Convention nor the New York Convention permit annulment or refusal of enforcement of an award because the tribunal made an error of law. ISA tribunals are not subject to the kinds of pressures that arise out of hierarchical relations between courts in municipal legal systems. The lack of hierarchy means that there is no tribunal that can play a supervisory role over the consistent application of the investment standards that contributes to uncertainty over the content of the legal norms. Neither consistency through binding appellate review nor through the informal application of pressure to lower-level adjudicators occurs within the international investment regime.

5.1.1.1.2. Lack of Precedent

The systems of common and civil law have evolved different rules regarding precedent but, contrary to a common misconception, precedential authority exists in common law and civil law systems alike. The common law states recognize the formal binding power of previously-rendered judicial decisions, known as *stare decisis*. In common law jurisdictions, the principle of *stare decisis* requires courts to follow previously established interpretations of legal norms.[1183] Apex courts may overrule even a well-established precedent; however, they have to provide reasons why they will not

[1181] *Ibid*.
[1182] *Ibid*.
[1183] Rainer Arnold & José Ignacio Martínez-Estay, *Rule of Law, Human Rights and Judicial Control of Power: Some Reflections from National and International Law* (London: Springer, 2017) at 203.

follow it.[1184] The hierarchically superior courts can find that the lower courts err in law when it overruled a well-established legal rule.[1185] The lower courts can evade a precedent but have to establish that the precedential case was distinguishable. Anderlini, Felli and Riboni argue that the mere presence of *stare decisis* as the functional principle of a legal system "serves a disciplinary role" to prevent possible "one-shot deviations" and creates a sense of continuity in the law by linking "current judicial decisions to future ones", and thereby ensuring legal consistency.[1186]

Karton explains that there are two kinds of binding precedents. Under vertical precedent, "lower courts are required to follow the decisions of courts superior to them in the judicial hierarchy of their legal systems".[1187] Under horizontal precedent, "courts are required to follow the decisions of prior panels of the same court […] For example, panels of the various United States Courts of Appeals must follow the decisions of earlier panels from the same circuit, even if they believe them to be incorrectly decided".[1188] Together with the hierarchy of courts, *stare decisis* ensures consistency of law application that results in "incremental development of consistent substantive law".[1189]

The civil law countries do not recognize *stare decisis*, but do acknowledge various forms of binding precedent.[1190] For example, in France and Louisiana, there is "a

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[1184] Saul Brenner & Harold Spaeth, *Stare Indecisis: The Alteration of Precedent on the Supreme Court, 1946-1992* (Cambridge: Cambridge University Press, 1995).
[1185] *Ibid*.
[1186] Anderlini, Luca; Felli, Leonardo & Riboni, Alessandro, Legal Efficiency and Consistency, Paper, Georgetown University, online:< http://faculty.georgetown.edu/la2/Efficiency.pdf>
[1187] *Ibid* at 66.
[1188] *Ibid*.
[1189] Irene Ten Cate, "The Costs of Consistency: Precedent in Investment Treaty Arbitration" (2013) 51 Colum J Transnatl L 418 at 420. .Jeremy Waldron, "Stare Desis and the Rule of Law:A Layered Approach" (2012) 111 Mich L Rev 1.
[1190] John Henry Merryman & Rogelio Pérez-Perdomo, *The Civil Law Tradition: An Introduction to the Legal Systems of Europe and Latin America* (Stanford: Stanford University Press, 2007) at 47. There is no formal requirement for judges to follow the precedent but judges can still adhere to it by virtue of persuasive value. In France, the courts follow each others decisions.

consistent line of authority", *la jurisprudence constante*, which plays an analogous function to *stare decisis*, although it operates differently.[1191] Palmer and Borowski explain the similarities and differences between *stare decisis* and *jurisprudence constante*:

> the policy concern underlying *stare decisis* and *jurisprudence constante* is the same: stability in law and constancy of jurisprudence. However, unlike *stare decisis*, this latter doctrine does not mandate adherence to a principle of law announced and applied on a single occasion in the past. Adjudications assume the dignity of *jurisprudence constante*, and the rule of law they are based on becomes entitled to great weight in subsequent decisions, when the courts, by repeated decisions in a long line of cases, accept and apply that rule of law. […] In general, a compelling reason is necessary for a court to depart from *jurisprudence constante*.[1192]

In the context of investment arbitration, Crawford, Kaufman-Kohler, and Bjorklund have all advocated the position that, in practice, investment tribunals produce *jurisprudence constante*. However, the situation there should not be confused with that in France and other related jurisdictions. First, commentators disagree on *which* issues tribunals have generated consistent lines of authority. For example, Stern notes, "I heard James Crawford say that on fair and equitable treatment there is no *jurisprudence constante* and Gabrielle Kaufmann-Kohler says the contrary. So we already have a problem here."[1193] Stern concludes that in some areas *jurisprudence constante* emerges quickly, while in others it may emerge slowly or not at all.[1194] Of course, if there is no

[1191] John Bell, Sophie Boyron & Simon Whittaker, eds, Principles of French Law (Oxford: Oxford University Press, 2008) at 28.
[1192] Vernon Palmer, *Mixed Jurisdictions Worldwide: The Third Legal Family* (Cambridge: Cambridge University Press, 2012) at 304. [Emphasis added]
[1193] Brigitte Stern, "Cases and Commentaries" in Emmanuel Gaillard & Yas Banifatemi, eds, *Precedent in International Arbitration International Arbitration Institute* (Juris Publishing, 2008) at 149. [Emphasis original]
[1194] *Ibid*.

agreement whether a *jurisprudence constant*e has emerged on FET, it is difficult to imagine that how there can be certainty on the content, scope and standard of review for FET.

The second observation is that, since ISA tribunals function in a decentralized fashion, *jurisprudence constante* cannot emerge as it does in the courts of the French legal system, where it is tied to the judicial hierarchy. Steiner explains that in France, greater weight is accorded to higher courts' decisions because of "the law of imitation and the law of continuity".[1195] According to Steiner,

> judges in the lower courts usually find it expedient to follow the model offered by a decision of the courts above them in the hierarchy […] imitation is also forced upon judges in the lower courts in the sense that if they do not follow higher courts decisions their own decisions are likely to be reversed […] as far as the law of continuity is concerned, it rests on the assumption that continuity and consistency in judicial decisions are the most desirable features.[1196]

The precedential value of a particular case in the French system is thus determined by the courts that produce the decision – decisions of higher courts are more persuasive. The relationship within the system is thus of vertical authority that binds lower courts not formally (as in common law) but by virtue of imitation and continuity. The decisions of lower courts also have significance if they shape a consistent line of jurisprudence over time that is not overturned by higher courts. In France, therefore, the authoritative force of court decisions persists on both horizontal and vertical axes. Moreover, in the French system, jurisprudence generated by the courts "is subordinate to legislation", meaning that the legislature can always overturn the jurisprudence, a feature

[1195] Steiner (2010), at 95.
[1196] *Ibid*.

inspired by the separation of powers doctrine embedded in the French constitutional system.[1197] In the ISA context, there is no hierarchy among tribunals that might justify granting some decisions greater authority than others. In addition, not all IIAs permit for *ex post* control in form of mandatory interpretations by the specialized commissions akin to that established by NAFTA.

Third, as Karton points out, ISA tribunals often cite each other's decisions, but mostly to use "precedents for inspiration or information gathering".[1198] Where "adjudicators canvass precedents in such a manner, they slip too easily into 'cherry-picking' or fig-leafing' – that is deploying precedents to provide an authoritative gloss an already -determined position".[1199] For this reason, the citation of previous cases does not necessarily promote consistency.

As such, *jurisprudence constante* or *stare decisis* do not necessarily generate "good" law,[1200] they, however, produce important social benefit[1201] by encouraging consistency of legal interpretations.[1202] The roles of *stare decisis* and *jurisprudence constante*, thus, help "save" courts from the immediate pressure of political preferences of other participants in the legal system. The doctrines also limit partisanship in the decision-making process by (at least in theory) minimizing the influence of personal

[1197] Noelle Lenoir, "The Constitutional Council and the European Convention of Human Rights: the French Paradox" in Gordon Slynn et al, eds, *Judicial Review in International Perspective* (The Hague: Kluwer Law International, 2000) at 152.
[1198] Karton (2015), at 72-73.
[1199] *Ibid*.
[1200] Peters suggests that the rule stare decisis is also not perfect because it has a "cumulative effect" and,thus often reinforces injustice by requiring courts to follow the precedent. Christopher Peters, "Foolish Consistency: On Equality, Integrity, and Justice in Stare Decisis" (1996) 105:8 Yale LJ 2031. Waldron submits that *stare decisis* could have a serious social costs in terms of injustice and inefficiency of bad decisions. Jeremy Waldron, "Stare Desis and the Rule of Law: A Layered Approach" (2012) 111 Mich L Rev 1.
[1201] William Landes & Richard Posner, "Adjudication as a Private Good" (1979) 8:2 J Legal Studies 235 at 239.
[1202] Waldron (2012), at 3.

preferences of judges.[1203] When combined with the hierarchical structure of the courts, *stare decisis*, promotes certainty within the legal system.[1204]

Admittedly, ISA tribunals can generate *jurisprudence constante* on a horizontal level, and such jurisprudence could provide guidance for the tribunals as to what claims are viable or may be considered as an abuse of process.[1205] Yet the value of *jurisprudence constante* is limited for number of reasons. First, arbitral awards "can be hard to access and assess".[1206] Roberts explains that,

> there is no neat hierarchy or structure for sorting published decisions to identify seminal awards […] the awards are proliferating, which makes it time-consuming to stay abreast of developments […] without a strict doctrine of precedent, it takes a certain number of cases before states are likely to respond to apprehend the jurisprudential trends. Even then, states may wish to respond but lack the budget to do so effectively.[1207]

Second, arbitrators are free to ignore any findings (or even particular approaches taken to interpretation of investment rules) of their colleagues without risking any internal or external sanction, for exactly the reason that the international investment regime lacks any judicial hierarchy.[1208] Finally, *jurisprudence constante* in the investment

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[1203] Frank Cross & Emerson Tiller, "Judicial Partisanship and Obedience to Legal Doctrine: Whistleblowing on the Federal Courts of Appeals" (1998) 107:7 Yale LJ 2155 at 2156.
[1204] Lord Mance, Should the Law Be Certain? The Oxford Shrieval Lecture 2011, online:< https://www.supremecourt.uk/docs/speech_111011.pdf> para.7, 11.
[1205] Andrea Bjorklund, "The Promise and Peril of Arbitral Precedent: The Case of Amici Curiae" (2010) 34 Association Suisse de L'arbitrage, Special Series 165.
[1206] Roberts (2010), at 195. Andrea Bjorklund, *Investment Treaty Arbitral Decisions as Jurisprudence Constante* in Colin Picker, Isabella Bunn & Douglas Arner, *International Economic Law: The State and Future of the Discipline* (London: Bloomsbury Publishing, 2008) at 273.
[1207] Roberts (2010), at 195.
[1208] Reisman (1992), at 134. Joshua Karton, "Choice of Law and Interpretive Authority in Investor-State Arbitration" (2017) 3:1 CJCCL 217 at 239. ("Rather, the point is that the Saipem tribunal was asking the wrong question – how should tribunals conceive of their role? – while the Romak tribunal was asking the right one – what role have the parties assigned to the tribunal?"). *Romak* at para 171. ("the Arbitral Tribunal has not been entrusted, by the Parties or otherwise, with a mission to ensure the coherence or development of "arbitral jurisprudence." The Arbitral Tribunal's mission is more mundane, but no less important: to resolve the present dispute between the Parties in a reasoned and persuasive manner").

regime radically departs from its civil law based counterpart in France, as the regime lacks a vertical relationship among the tribunals or any subordination of arbitrators to the legislature under the umbrella of separation of powers. Arbitrators do not necessarily perceive themselves as actors who merely apply law, a cultural departure from how French judges perceive themselves.

Third, as Sornarajah points out, "[t]he great rush to argue that a *jurisprudence constante* has been developed in the area" may be foreclosed by the fact that common investment standards are worded differently in different treaties".[1209] In addition, investment disputes are fact-specific and the tribunals often emphasize that they render decisions on the basis of the circumstances in each particular case. This translates into awards' "diminished value as precedents".[1210]

To dismiss a claim early in the proceedings as an abuse of process or for lack of legal merit, the arbitrators must know with certainty what the law is. After all, before dismissing a claim, the arbitrators must assess its merits in a preliminary manner. Without knowing with certainty what the law is, or what actions of an investor potentially would impede the system's very purpose, such an assessment (especially at the early stages of a dispute) may be impossible to determine. The problem is not that arbitrators are biased in favour of investors; instead, the systemic features of the investment regime make it unlikely that frivolous or abuse of process claims will be dismissed except in the most obvious or egregious cases.

5.1.2. General Uncertainty Over the Content of Investment Standards

Saipem at para 90 ("it has a duty to seek to contribute to the harmonious development of investment law and thereby to meet the legitimate expectations of the community of States and investors towards certainty of the rule of law").

[1209] M. Sornarajah, *Resistance and Change in the International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2015) at 250.

[1210] Sureda (2012), at 140.

Some degree of uncertainty is inherent in any adjudicatory process. Even when the law is deemed to be settled, the legal rules still may require "reappraisal" simply because "life has a habit of throwing up circumstances" that call for such reappraisal.[1211] Benjamin Cardozo of the US Supreme Court observed: "in my first years upon the bench, to find how trackless was the ocean on which I had embarked, I sought for certainty. I was oppressed and disheartened when I found that the quest for it is futile".[1212]

The law may be inherently uncertain; the question is whether the legal system in question establishes structures and incentives that will ensure "a greater measure of predictability", for example through the application of formal precedent or the ability of the legislator to intervene and adjust the law.[1213] As has been mentioned, the lack of institutional features that promote certainty is exacerbated in the investment regime by drafting of the investment standards in a rather vague fashion, and by practices of the investment tribunals that may render inconsistent interpretations of the legal standards.

5.1.2.1. Open-Ended Formulations of the Investment Standards in IIAs: The Case of Fair and Equitable Treatment

As Chapter Two of this thesis shows, investment standards can be "evaluative",[1214] meaning rules where "those who apply it [have] to take account of a range of variables and to exercise judgment as to their contribution, in varying, idiosyncratic contexts, to realizing the goal or goals that have been specified".[1215] This

[1211] Edward Thomas, *The Judicial Process: Realism, Pragmatism, Practical Reasoning and Principles* (Cambrdige: Cambridge University Press, 2005) at 120.
[1212] Benjamin Cardozo, *The Nature of the Judicial Process* (New York: Cosimo, 2009) at 166.
[1213] Ginsburg (2003), at 1319.
[1214] Michael Reisman, "Canute Confronts the Tide: States versus Tribunals and the Evolution of the Minimum Standard in Customary International Law" (2015) 30:3 ICSID Rev 616 at 617.
[1215] *Ibid*.

ambiguity may be a result of the omission of the state parties[1216] or a deliberate decision necessary in the relevant domestic and international political context.[1217] Some level of ambiguity in treaties is inevitable and even desirable, for at least two reasons. First, ambiguity provides flexibility that may be needed at the stage of a dispute to ensure that various types of host state misconduct against foreign investors fall within the scope of an obligation in an applicable IIA. Second, from the perspective of a diplomat, states may deliberately choose vague or ambiguous language because reaching a deal is more important to them than the precise content of that deal. This phenomenon explains Philip Allot's famous definition of a treaty as "a disagreement reduced to writing".[1218]

It would be too vast a task to fully examine the more than 3000 IIAs and all of the broadly-worded substantive provisions in them. The section focuses on a few representative examples of investment standards, in particular the FET standard, to show the ambiguous nature of the obligations in IIAs.

[1216] Lauge Skovgaard Poulsen, *Bounded Rationality and Economic Diplomacy: The Politics of Investment Treaties in Developing Countries* (Cambridge: Cambridge University Press, 2015) at 141-142 (discussing a concept of bounded rational learning that developing states in particular did not know that the treaties "had bite in practice". Lack of understanding that IIAs can "bite" of course influenced how developing states approached the negotiation' process of the terms in such treaties).

[1217] Bonnitcha, Poulsen & Waibel (2018), at 201-202, 208 (noting that "the US BITs were consciously used as diplomatic symbols" and discussing the statement of President Nazarbayev of Kazakhstan that "described" its BIT with US as a "symbolic show of US regard for Kazakhstan". Reportedly, the Zimbabwean negotiator noticed "we were negotiating treaties to promote investment […] because we wanted to be the most competitive investment destination"). Guzman argues that developing countries competed for capital and attempted to signal foreing investors that they have friendly investment climate, Andrew Guzman, "Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of Bilateral Investment Treaties" (1997) 38 Va J Int'l L 639. Zachary Elkins, Andrew Guzman & Beth Simmons, "Competing for Capital: The Diffusion of Bilateral Investment Treaties" (2006) 60:4 International Organization 811. (Guzman,however, questions that BITs are anyhow credible tools to attract more investment. In later work with Elkins and Simmons, Guzman seemingly changes his position. The commentators point out that developing countries utilized IIAs strategically as tools to compete and attract foreign capital).

[1218] Philip Allott, "The Concept of International Law" (1999) 10 EJIL 31 at 43. Lauge Skovgaard Poulsen, *Bounded Rationality and Economic Diplomacy: The Politics of Investment Treaties in Developing Countries* (Cambridge: Cambridge University Press, 2015) at 44; Tarcisio Gazzini, *Interpretation of International Investment Treaties* (London: Bloomsbury Publishing, 2016) at 91. (arguing that "IIAs […] are intentionally or accidentally drafted in vague terms").

5.1.2.2. Investor State Tribunals Contribute to Uncertainty Via Inconsistent Decisions

It is worth considering (at least briefly) whether the practice of the ISA tribunals has introduced greater clarity and certainty on the scope of the FET. The following subsection shows that FET continues to be uncertain despite a relatively large volume of ISA case law. First, it examines the decisions of the NAFTA tribunals on FET as an example to illustrate the risk of inconsistent interpretations contributing to legal uncertainty. Second, it provides a macro perspective on the contradictory interpretations offered by ISA tribunals.

5.1.1.1.1 What Have Investor-State Tribunals Actually Done with FET?

ISA tribunals are empowered to apply the investment standards and clarify their content through interpretation of the governing IIAs. Article 1105 para.1 NAFTA states that "[e]ach Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security".[1219] The early NAFTA tribunals produced some notorious interpretations of FET. For example, in *Metaclad v Mexico*, the tribunal "based its conclusion that Mexico had breached the NAFTA on an apparently distinct obligation to provide a transparent and predictable framework for the operations of the the investor".[1220] As Weiler explains, the narrative of *Metaclad* is told in "dramatically different ways" depending on the circle to which the storyteller belongs.[1221] Puig

[1219] *Ibid*.
[1220] Viñuales (2012), at 351. The award was partially set aside.
[1221] Todd Weiler, Good Faith and Regulatory Transparency: The Story of Metaclad v Mexico in Todd Weiler,ed, *International Investment Law and Arbitration: Leading Cases from the ICSID, NAFTA, Bilateral Treaties and Customary International Law* (Cameron May, 2005) at 701. Marisa Yee, "The Future of Environmental Regulation After Article 1110 of NAFTA: A Look at the Methanex and Metalclad Cases" (2002) 9 Hastings W.-N.W. J. Env. L. & Pol'y 85. Jack Coe, Jr. & Clyde Pearce, "Arbitration Under NAFTA Chapter Eleven: Some Pragmatic Reflections Upon the First Case Filed Against Mexico" (2000) 23 Hastings Int'l & Comp. L. Rev. 311.

summarizes the issues in *Metaclad* as follows: "the question in dispute involved the determination of whether the municipality's denial of a construction permit and refusal of permission to operate a waste disposal facility was consistent with the obligations adopted by Mexico".[1222] The chief concern of the commentators on *Metaclad* was that the decision might chill states from adopting environmental regulations.[1223] For our purposes, *Metaclad* is important because it shows that the NAFTA tribunal interpreted the FET obligation (and also expropriation) remarkably broadly.[1224] Kate Miles explains that "the tribunal's 'effects-based' determination appeared to extend the meaning of expropriation well beyond its traditional scope and seemed to expose health and environmental regulations enacted for public welfare purposes to the risk of challenge from aggrieved foreign investors".[1225]

Decisions like *Metalclad* eventually led the NAFTA parties to issue a mandatory interpretation of FET.[1226] In 2001, the NAFTA Free Trade Commission (FTC) issued a binding interpretation that article 1105(1) "does not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens".[1227] NAFTA links FET to the international minimum standard of treatment (MST) in customary international law.[1228] The FTC's interpretation note constitutes a "subsequent recalibration of treaty practice" in response to overly expansive

[1222] Sergio Puig, "Is Investment Arbitration Good or Bad for Developing Countries? The Mexican Experience in the North American Free Trade Agreement" (2005) 4: Law and Practice of International Courts &Tribunals 61 at 65.
[1223] Miles (2013), at 158.
[1224] *Ibid*.
[1225] *Ibid*.
[1226] Patrick Dumberry, "The Prohibition against Arbitrary Conduct and the Fair and Equitable Treatment Standard under NAFTA Article 1105" (2014) 15 J World Investment & Trade 117 at 119.
[1227] NAFTA Notes of Interpretation at B(1)& (2). [Notes of Interpretation]. Florian Grisel, The Sources of Foreign Investment Law in Zachary Douglas, Joost Pauwelyn&Jorge Vinuales, eds, *The Foundations of International Law: Bringing Theory into Practice* (Oxford: Oxford University Press, 2014) at 221. (includes general discussion of the linkage between customary international law and FET)
[1228] *Ibid* at B(1).

(from the perspective of states) arbitral interpretations.[1229] Such state practice reinforces the dynamics envisaged by the political system's lens on how legal outcomes (ISA tribunals' decisions) generate feedback from the states, which in turn redraft IIAs. The MST's content in itself is a subject of ongoing development.[1230] Miles concludes that, "[i]n fact, tribunals have continued to afford expansive reading into the treaty standard".[1231] Specifically, Miles refers to the decision in *Pope & Talbot v Canada* (2002), the damages phase of which was resolved after FTC issued the interpretative note. Miles explains,

> [t]he tribunal chose to address the content of the customary international law standard. It determined that as the customary international law standard was not static, it had already evolved so as to encompass the treaty-sourced concept of fair and equitable treatment.It also held that the modern understanding of the customary international law rule had shifted to such an extent that the traditional minimum standard criteria of the Neer claim, 'egregious' conduct was not required-lesser degrees of conduct would trigger a breach of both the modern minimum standard and the fair and equitable treatment standard.[1232]

[1229] Lauge Skovgaard Poulsen, *Bounded Rationality and Economic Diplomacy: The Politics of Investment Treaties in Developing Countries* (Cambridge: Cambridge University Press, 2015) at 37.
[1230] James Crawford, "The ILCs Articles on Responsibility of States for Internationally Wrongful Acts: A Retrospect" (2002) 96 AJIL 874, 886. [emphasis added]. *Mondev International Ltd. v United States of America* (2002), Award, ICSID Case No. ARB(AF)/99/2 (Arbitration: Ninian Stephen, James Crawford, Stephen Schwebel) (International Centre for Settlement of Investment Disputes) at para.116 (the tribunal notes "Neer and like arbitral awards were decided in the 1920s, when the status of the individual in international law, and the international protection of foreign investments, were far less developed than they have since come to be. In particular, both the substantive and procedural rights of the individual in international law have undergone considerable development. In the light of these developments it is unconvincing to confine the meaning of "fair and equitable treatment" and "full protection and security" of foreign investments to what those terms – had they been current at the time – might have meant in the 1920s when applied to the physical security of an alien. To the modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious"). *Chemtura v Canada* (2010), Award (United Nations Commission on International Trade Law) (Arbitrators: Gabrielle Kaufmann-Kohler, Charles Brower, James Crawford) at para.120-123 ("each party puts forward different conclusions as to the impact of the FTC Note on the scope of Article 1105").
[1231] Miles (2013), at 321.
[1232] *Ibid*.

As Salacuse observes, the tribunal in *Pope & Talbot* actually criticized the FTC interpretative note—which was binding on the tribunal—on the grounds of its "incorrectness".[1233]

In *Waste Management v Mexico Phase Two* (2004), the tribunal formulated the MST standard as follows:

> the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.[1234]

The tribunals in two later cases, *Glamis Gold v USA* (2009) and *Merrill and Ring Forestry L.P. v Canada* (2010) (decided after the FTC note was issued), produced awards that resulted even in more controversy on the scope of MST-FET. In *Glamis Gold*, the Canadian-based foreign investor brought a claim against the US after the state of California adopted regulatory measures that resulted in interruption of the investor's open-pit mining operations. The tribunal examined whether the USA violated its obligations on expropriation and FET under NAFTA. In its award, the tribunal concluded that "Glamis fails to establish the evolution in custom it asserts to have occurred".[1235] According to the tribunal,

[1233] Salacuse (2015), at 248.
[1234] *Waste Management* 2, Award at para.98.
[1235] *Glamis Gold* at para.22

> an act must be sufficiently egregious and shocking—a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination, or a manifest lack of reasons—so as to fall below accepted international standards and constitute a breach of Article 1105(1).[1236]

In contrast, in the *Merrill and Ring Forestry* case, the tribunal simply acknowledged that "NAFTA jurisprudence has stiffened since the FTC Interpretation" and mentioned the *Glamis Gold* award's reliance on the traditional *Neer* standard.[1237] After a brief reference, however, the tribunal arrived at the opposite conclusion to the one in *Glamis,* that the MST standard has evolved and "is broader than that defined in the *Neer* case and its progeny".[1238] After this conclusion, the tribunal observed that the MST-FET standard under NAFTA:

> provides for the fair and equitable treatment of alien investors within the confines of reasonableness. The protection does not go beyond that required by customary law, as the FTC has emphasized. Nor, however, should protected treatment fall short of the customary law standard.[1239]

The tribunal thus decided—in accord with the NAFTA Free Trade Commission's interpretive note—that FET in NAFTA is not an independent standard, but is rather tied to states' obligations under MST. The tribunal, however, did not specify what is the scope of MST-FET standard or its content, except its observation that the standard evolved since *Neer*. Fundamentally, the tribunal also diverged in its interpretation from the award in *Glamis*, which explicitly held that FET-MST under NAFTA requires the treatment at the level established in *Neer*. As Ryan points out, *Merrill* "recognizes a

[1236] *Ibid*.
[1237] *Merrill & Ring Forestry* at para. 200.
[1238] *Ibid* at para.213, 200-212 (discussing the evidence on the evolution of MST).
[1239] *Ibid* at para.213.

more dynamic MST standard than *Glamis*".[1240] I agree with this observation, and can add that *Merrill* once again broadens the scope of the standard in comparison to *Glamis*. *Merrill* seems to be more in accord with the early NAFTA interpretations of FET from before the interpretive note.[1241]

In addition, the tribunal in *Glamis* imposed the evidentiary burden upon the foreign investor to prove an evolution of the MST, an approach that the tribunal in *Merrill* rejected. Instead, the tribunal in *Merrill* examined the evidence on the evolution of the MST standard on its own without requiring the claimant to show how the standard has evolved since *Neer*. This divergence has implications for claimant's ability to establish state liability under FET. In another case, *Clayton & Bilcon v Canada*, the arbitrators disagreed on the threshold to find a violation of FET-MST standard under NAFTA,[1242] leading to a dissent from arbitrator McRae on this issue.[1243] As has been discussed in Chapter Two, there seems to be continuing disagreement among the tribunals on a number of basic issues relating to the scope of the FET obligation in NAFTA, including (1) the scope of the standard in the context of the MST evolution since *Neer*, (2) the allocation of the burden of proof i.e. what party must prove whether the standard evolved (see above discussion on the *Glamis* and *Merill* cases), and (3) the threshold for breach of MST.

[1240] Margaret Clare Ryan, "Glamis Gold v The United States and the Fair and Equitable Treatment Standard" (2011) 56:4 Mcgill LJ 921 at 958.
[1241] *Pope&Talbot v Canada* (2002), Award on Damages, (Arbitrators Lord Dervaird, Benjamin Greenberg, Murray Belman) at para.58. (Compare with Pope& Talbot in which the tribunal says explicitly "the tribunal rejects this static conception of customary international law").
[1242] Michael Carfagnini, "Too Low a Threshold: Bilcon v Canada and the International Minimum Standard of Treatment" (2016) 53 Can YB Intl L 244.
[1243] Donald McRae, In the Matter of an Arbitration Under Chapter Eleven of the North American Free Trade Agreement and the UNCITRAL Rules of 1976 (UNCITRAL Rules) between William Clayton, Douglas Clayton, Daniel Clayton and Bilcon of Delaware Inc and the Government of Canada, online:<https://www.italaw.com/sites/default/files/case-documents/italaw4213.pdf>. [McRae Dissent for Bilcon]

Other questions are also pressing. Do the tribunals identify existing standard on the basis of customary law or do the tribunals *de facto* develop the content of the standard through their awards? As noted by the tribunal in *Sempra v Argentina,*"the evolution that has taken place is for the most part the outcome of a case-by case determination by courts and tribunals, as is evidenced by many investment treaty and NAFTA decisions, including the *Tecmed*, *OEPC*, and *Pope & Talbot* cases".[1244] Tribunals thus often refer to the previous decisions of other tribunals to determine the content of the standard on the case-by-case basis. The references and citations to previous decisions are, however, not sufficient to establish that MST has evolved.[1245] To establish the content of such an evolved international minimum standard, tribunals still must establish two elements (1) state practice and (2) *opinio juris*.[1246] Canada has repeatedly emphasized that "[t]he decisions and awards of international courts and tribunal do not constitute instances of State practice, but are relevant to the extent that they include an examination of State practice and *opinio juris*".[1247] The tribunal in *Cargill v Mexico* observes that the decisions of the ISA tribunals "do not create customary international law but rather, at most, reflect [international customary law] […]in both the case of scholarly writings and arbitral decisions, the evidentiary weight to be afforded such sources is greater if the conclusions

[1244] *Sempra v Argentina* at para.297. [Emphasis original]
[1245] There is an argument that IIAs reflect the development of international minimum standard and mere existence of the treaties is sufficient to satisfy practice of states and opinion juris. In its submission for *Loewen v USA*, the USA notes "it is impossible to infer from the existence of a large number of BITs alone that any particular provision therein represents a rule of customary international law merely by reason of its commonality". IIAs contain variety of different FET clauses that are often not linked to MST. Even when IIAs incorporate the FET in nexus with MST, the treaties rarely define what MST-FET is thus leaving the content to be interpreted by the tribunals. Response of the United States of America (27 June 2002) Submissions of the Governments of Canada and Mexico Pursuant to NAFTA Article 1128.
[1246] *North Sea Continental Shelf Cases*, 1969 ICJ 3 at para.73- 77. *Glamis Gold* at para. 602.
[1247] Submission of Canada Pursuant to Article 832 of the Canada-Peru Free Trade Agreement for *Bear Creek Mining Corporation v Republic of Peru*, ICSID Case No. ARB/14/21 (Arbitrators: Karl-Heinz Böckstiegel, Michael Pryles, Philippe Sands) at para.10. (The burden of proof for MST "rests with the party invoking the provision" at para.9).

therein are supported by evidence and analysis of custom".[1248] There is a risk that tribunals neither establish nor "reflect" the standards by such references, and instead engage in what ICJ Judge Sir Robert Jennings described as "use citations of selected passages from decisions" to give "the proposition […] the appearance of being vested with judicial authority".[1249]

5.1.1.1.2 What Do Investor-State Tribunals Actually Do? A Macro Perspective

This section shows that by producing inconsistent decisions and divergent interpretations, ISA tribunals contribute to uncertainty over the content and scope of the legal norms in the investment regime. The problem of inconsistent decisions and interpretations has been discussed at length in the literature. For example, Reinisch proposes to consider three "forms of inconsistencies" that persist in the investment regime.[1250] First, ISA tribunals can produce "divergent views on legal issues", in particular when the tribunals diverge on the interpretation of a single investment standard.[1251] Second, tribunals can generate "divergent assessments of identical facts".[1252] Third, tribunals can render "conflicting results in the same dispute" in instances "where the same dispute is litigated by a subsidiary and its parent".[1253] Reinisch's analytical framework is useful to envision a macro-picture of how ISA tribunals operate. Individual inconsistencies are driven by the structure of the investment

[1248] *Cargill, Inc v United Mexican States* (2009), Award ICSID Case No. ARB(AF)/05/2) (International Centre for Settlement of Investment Disputes) (Arbitrators: Michael Pryles, David Caron, Donald McRae) at para.277.
[1249] Robert Jennings, "Role of the International Court" (1997) 58 BYIL 1 at 41-42.
[1250] Reinisch (2010), at 115.
[1251] *Ibid* at 116.
[1252] *Ibid* at 116.
[1253] *Ibid* at 117.

regime, in particular by the *ad hoc* decentralized nature of the ISA tribunals and IIAs. The risk of inconsistency in such structure is "a given".[1254]

Susan Frank systematizes the case studies on inconsistency of tribunals' interpretations and outcomes into three categories. The first includes "cases involving the same facts, related parties, and similar investment rights".[1255] The second concerns "cases involving similar commercial situations and similar investment rights".[1256] The third category includes "cases involving different parties, different commercial situations, and the same investment rights".[1257] In her discussion of inconsistent decisions, Franck focuses on three sets of disputes that triggered serious turmoil among the regime's participants: the Lauder arbitrations,[1258] the SGS arbitrations,[1259] and a series of NAFTA arbitrations.[1260]

To illustrate inconsistencies of outcomes and interpretations, most commentators focus on specific case studies. For example, Burke-White and von Staden examine the series of cases against Argentina,[1261] in which the tribunals arrived at divergent

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[1254] *Ibid*.
[1255] Franck (2005), at 1558.
[1256] *Ibid*.
[1257] *Ibid*.
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[1259] *SGS Societe Generale de Surveillance S.A. v Islamic Republic of Pakistan* (2003), Decision on Objections to Jurisdiction, ICSID Case No. ARB/01/13 8 ICSID Reports 406 (International Centre for Settlement of Investment Disputes) (Ahmed El-Kosheri, James Crawford, Antonio Crivellaro) at para.163-168, 171. *SGS Societe Generale de Surveillance S.A. v Republic of the Philippines* (2004), Decision on Objections to Jurisdiction ICSID Case No. ARB/02/6, 8 ICSID Reports (International Centre for Settlement of Investment Disputes) (Arbitrators: Ahmed El-Kosheri, James Crawford, Antonio Crivellaro) at para.121.
[1260] *S.D.Myers, Partial Award* at para.262, 258. *Metalclad. Pope & Talbot,* at para.111-117, 118. *Clayton Bilcon* at para. 504, 436-437, 738, 740-741. Jarrod Hepburn, *Domestic Law in International Investment Arbitration* (Oxford: Oxford University Press, 2017) at 25. [Emphasis added]. ("Last, the more recent case of Clayton/Bilcon v Canada raises the role of domestic legality in FET perhaps most squarely of all the cases discussed here. Indeed […] the major point of criticism of the Clayton/Bilcon majority's award coming from the dissenting arbitrator was that the majority had impermissibly equated a breach of Canadian law with a breach of FET. […] The dissenting arbitrator viewed the majority's opinion as imposing international responsibility *for a mere breach of domestic law*").
[1261] *Enron* at para. 335-342. *Sempra v Argentine Republic* at para.390-397. *LG&E Energy* at para.266. *Continental Casualty v Argentina* (2008), ICSID Case No ARB/03/9 (International Centre for the

interpretations and applied different standards of review.[1262] In *Continental Casualty v Argentina*, the tribunal "gave considerable deference to Argentina's determination that its actions were necessary to protect essential security interests and maintain public order".[1263] By contrast, in *Gas Transmission Company v Argentine*, *Enron v Argentine* and *Sempra v Argentine*, the tribunals construed the defence of necessity in a narrow fashion and "essentially made Argentina's invocation of the NPM [Non-Precluded Measures] clause in the U.S.-Argentina BIT a legal impossibility and failed to take into consideration the broader policy context in which the arbitrations arose".[1264] Burke-White and von Staden conclude that the "ICSID tribunals reviewing Argentina's actions have generated inconsistent and incoherent jurisprudence".[1265]

Lévesque scrutinizes the trio of sweetener cases, *ADM v Mexico*, *CPI v Mexico*, and *Cargill v Mexico*.[1266] According to Levesque, these cases "provide an excellent case study on inconsistency" because they "display a number of commonalities: they involved

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Settlement of Investment Disputes) (Arbitrators: Giorgio Sacerdoti, V.V. Veeder, Michell Nader) at para.196-205.

[1262] William Burke-White & Andreas von Staden, "Private Litigation in a Public Sphere: The Standard of Review in Investor-State Arbitrations" (2010) 35 Yale J Intl L 283 at 323. ("First, each tribunal borrows different elements of the standards we discussed in Part IV, resulting in a review of state behavior that may not adequately balance the conflicting interests at stake. Second, these tribunals' approaches are far from uniform, resulting in continued ambiguity in and conflict over the applicable standard of review in similar public law settings").

[1263] *Ibid* at 299.

[1264] *Ibid* at 297.

[1265] *Ibid* at 299.

[1266] Celine Levesque, "Inconsistency in Investor-State Awards and the Role of State Interpretations: The Example of the Mexican Sweetener Trio of Cases under NAFTA" in Andrea Bjorklund, ed, *Yearbook on International Investment Law & Policy 2013-2014* (Oxford: Oxford University Press, 2015) at 363. *Daniels Midland Co & Tate & Lyle Ingridients Americas* (2007), Award ICSID Case No (International Centre for Settlement of Investment Disputes) (Arbitrators: Bernardo Cremandes, Arthur Rovine, Eduardo Siqueiros). *Corn Products International, Inc. v Mexico* (2008), Decision on Responsibility, ICSID Case No ARB/(AF)/04/1 (International Centre for Settlement of Investment Disputes) (Arbitrator: Andreas Lowenfeld). *Cargill v Mexico* (2009), Award ICSID Case No. ARB(AF)/05/2 (International Centre for Settlement of Investment Disputes) (Arbitrators: Michael Pryles, David Caron, Donald McRae).

the same treaty, the same respondent, one common measure, very similar facts, and mostly common claims".[1267]

The disputes emerged after Mexico adopted a set of regulatory measures that impacted producers of high-fructose corn syrup, a sweetener commonly used in processed foods. These regulatory measures were the subject of disputes in the World Trade Organization (WTO) and under NAFTA Chapter 19.[1268] Foreign investors also challenged the regulatory measures adopted by Mexico, in particular a 20% tax on soft drinks, under Chapter 11 of NAFTA.[1269] In the end, the tribunals all held that Mexico was in breach of its obligations under NAFTA Chapter 11, but they did so for different reasons and awarded significantly different quanta of damages.[1270]

Lévesque concludes that the sweetener cases reveal two areas where fundamental inconsistency arises.[1271] The first "relates to the relationship between NAFTA's investment and trade obligations and resulting liability consequences".[1272] As Lévesque explains, "Mexico argued that they [regulatory measures] constituted damage to the claimants' US investment as opposed to their Mexican investment and as such fell outside the tribunals' jurisdiction. One tribunal agreed, but another disagreed".[1273] The second area where systemic inconsistency emerged "relates to the relationship between IIAs and the customary international law of countermeasures".[1274] Most important for our purposes is the fact the tribunals fundamentally diverged on the issue of "whether

[1267] *Ibid*.
[1268] *Ibid* at 374.
[1269] *Ibid*.
[1270] *Ibid* at 379, 389-399.
[1271] *Ibid* at 365.
[1272] *Ibid*.
[1273] *Ibid* at 365-366.
[1274] *Ibid* at 366.

countermeasures apply to NAFTA Chapter 11 as a matter of law".[1275] Interestingly, one of the claimants, Cargill, acknowledged in its memorial that "arbitral awards frequently conflict, an inherent hazard given party selection of arbitral tribunals and the private nature of arbitral resolution".[1276]

In addition to the risk of inconsistent outcomes and interpretations, there is no clear and consistent method or standard of review that arbitrators apply to render their decision on the host state's liability.[1277] Henckels observes the following two trends with regards to the standard of review applied by the ISA tribunals.[1278] First, ISA tribunals do not use a uniform method of review.[1279] Instead, they apply different standards of review, including "the proportionality-based approaches",[1280] "the legitimate objective as the test for legality",[1281] the so-called "suitability test",[1282] "review of unreasonableness"[1283] and,

[1275] *Ibid* at 366.
[1276] *Ibid* at 383. (United Mexican States v Cargill Incorporated, Respondent's Factum, The United Mexican States, Ontario Superior Court of Justice, Court File No CV-09-391935, 23 April 2010 at para.107 as cited in Levesque).
[1277] Henckels explains the difference between the two terms. According to Henckels, "conceptually the standard of review differs from the applicable method of review. Each serves a distinct purpose. […] A method of review is a technique used by adjudicators (such as proportionality analysis) to determine the permissibility of interference with a right or interest, whereas the standard of review refers to the intensity with which the method of review is applied- whether taking a strict or more deferential approach". Caroline Henckels, *Proportionality and Deference in Investor-State Arbitration* (Cambridge: Cambridge University Press, 2015) at 31.
[1278] *Ibid* at 70-129.
[1279] *Ibid* at 82-120.
[1280] *Ibid* at 83-115. Valentina Vadi, "A History of Success? Proportionality in International Economic Law" in Antonio Segura Serrano, ed, *The Reform of International Economic Governance* (London: Routledge, 2016) ("the proportionality analysis is not used consistently in investment treaty arbitration") at 183. Alec Stone Sweet, "Investor-State Arbitration: Proportionality's New Frontier" (2010) 4 L & Ethics Hum Rts 46 at 62,71. Armin Von Bogdandy & Ingo Venzke, *International Judicial Lawmaking: On Public Authority and Democratic Legitimation in Global Governance* (London: Springer, 2012) (argue "a prevalent model distinguishes three steps of a proportionality inquiry, or sub-principles of the principle of proportionality: suitability, necessity, and proportionality in a narrow sense (stricto sensu)") at 261.
[1281] *Ibid* at 115-116. ("several tribunals assessed the legitimacy of the state's regulatory objective as a means to determine whether the state had breached fair and equitable treatment or had undertaken expropriation").
[1282] *Ibid* at 116-117. (this test "involves testing the rationality of the connection between the measure and its objective").

finally, "review for arbitrariness".[1284] Second, even when where tribunals adhere to the proportionality-based approaches, they apply "the proportionality analysis […] inconsistently" and "the arbitrators have been less than clear with respect to the methodologies they have employed".[1285] What makes the situation even more obscure is that "references to proportionality […] do not always signal that a particular analytical process will be undertaken".[1286]

Another problem is that there is no consistency among the ISA tribunals in the degree of deference they afford to states when the arbitrators scrutinize a particular governmental policy. For example, in *Glamis Gold*, the tribunal took into consideration the US government's effort to balance the interests of different stakeholders,[1287] an approach that implicitly "reflects an understanding of the normative desirability of governments (rather than adjudicators) having primary responsibility for promulgating measures that deal with the competing interests of stakeholders in sensitive policy areas".[1288] In *Tecmed v Mexico*, however, the tribunal adhered to proportionality as a

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[1283] *Ibid* at 117-120. (the concept of reasonableness may be understood in search of equilibrium and appears to require a balancing of divergent interests. In absence of more detailed decision-making criteria,however, review for reasonableness risks impressionistic decision-making").
[1284] *Ibid* at 120-122. (" a number of other tribunals have held that fair and equitable treatment will only be infringed where the measure is arbitrary in the sense of there being a lack of substantial justification for the measure. […] the law is currently less than clear as to the actual circumstances in which state conduct will be arbitrary").
[1285] *Ibid* at 124.
[1286] *Ibid*. The application of proportionality requires "balancing" that in its turn sets demand for "certain normative background" and societal context. The investment regime that lacks centralized structure or any set of norms akin to the domestic constitutions is apparently distinctive from the domestic legal systems in this regard. Gebhard Bücheler, *Proportionality in Investor-State Arbitration* (Oxford: Oxford University Press, 2015) at 196. ("The caveat against the application of the principle of proportionality is that balancing requires a certain normative background; otherwise it risks being arbitrary and overly subjective.78 This does mean that the application of the principle of proportionality in the context of the FET standard presupposes a value system that displays all characteristics of a domestic constitution. But a certain value system that guides and structures the proportionality analysis is necessary"). Aharon Barak, "Proportionality and Principled Balancing" (2010) 4 L & Ethics Hum Rts 1 at 4-7.
[1287] *Glamis Gold* at para.762. ("To begin addressing this question, the Tribunal first notes that it is not for an international tribunal to delve into the details of and justifications for domestic law").
[1288] Henckels (2015), at 194.

method of review but did not afford any deference to the local government even though the government refused to issue the permits in an attempt to accommodate the opposition of the local community to the building of the landfill.[1289]

Inconsistency on the method and the standard of review has a direct bearing on the prospects for dismissal of frivolous and abuse of process claims. If tribunals have no consistent standard of review, how can they evaluate the investors' claims early in the process? Recall Chapter Four's discussion of the standards for dismissal as frivolous and abuse of process. The standard for dismissal, "manifestly without legal merit", allows the tribunals to dismiss only claims that are *prima facie* without merit.[1290] Recall that, for example, in the *Ansung v China* case, the tribunal dismissed the claim of investor as manifestly lacking merit only because the applicable IIA provided expressly that a right to make a claim elapses after a certain period.[1291] In *Mol Hungarian Oil and Gas Company Plc v Republic of Croatia*, the tribunal emphasized that it could not dismiss the claim because of ongoing disagreement as to the scope and content of the relevant state obligations in investment law.[1292]

Under the standard, "an award in favour of claimant cannot be made", the tribunals seem to act pursuant to the maxim "I know it when I see it" without clearly setting out the standard at all.[1293] In *Pac Rim* and *Renco* discussed in the section 4.2.1.2.2,

[1289] Caroline Henckels, "The Role of the Standard of Review and the Importance of Deference in Investor-State Arbitration" in Lukasz Gruszczynski & Wouter Werner, eds, *Deference in International Courts and Tribunals: Standard of Review and Margin of Appreciation* (Oxford: Oxford University Press, 2014) ("the tribunal did not appear to actually consider why it would have been appropriate to afford deference in the circumstances. This strict approach affected its conclusion as to the proportionality of Mexico's actions: the tribunal found that the authorities' objective was insufficiently important to outweigh the impact on the investor's interests").
[1290] *Trans-Global v Jordan* at para.105.
[1291] *Ansung* at para..141-143. [*Ansung*]
[1292] *MOL Hungarian Oil* at para.49. Chapter 4, section 4.2.1.2.1.2.
[1293] Chapter 4, section 4.2.1.2.2.

the tribunals never articulated a precise standard for the dismissal of the claim. With the method and the standard of review themselves uncertain, it seems to be possible for the arbitrators to dismiss investors' claims as frivolous only if those claims are based on truly fantastic legal theories.

As has been discussed in Chapter Four, abuse of process claims occur in principle whenever a right holder exercises the right "for a purpose that is different from that for which that right was created commits an abuse of rights".[1294] How can the tribunal identify such a purpose when even the state parties to the IIA may disagree about the goals of the system? If the tribunals offer different levels of deference to host governments, it may be nearly impossible to agree on the cases in which an investor's claim that challenges governmental regulation constitutes an abuse of process. The result is that the claims are dismissed as frivolous or abuse of process only in overly narrow set of circumstances, with the tribunals always reserving their right not to dismiss the claim at all.

What is more, the method and the standard of review are unlikely ever to become consistent under the current structure of the investment regime (individual IIAs and multiple non-hierarchical *ad hoc* ISA tribunals). In domestic legal systems (particularly civil law systems, from which the proportionality test seems to have been borrowed),[1295] systemic values play a role in determining how much deference the adjudicators afford to the executive:

> in the domestic legal order, it is the constitutional structure of the order that provides the basis upon which the courts determine whether to exercise constitutional restraint or to

[1294] *Saipem* at para.160. [Emphasis added]
[1295] Gebhard Bücheler, *Proportionality in Investor-State Arbitration* (Oxford: Oxford University Press, 2015) (discussing the establishment of the principle of proportionality in various legal orders).

> afford degrees of deference to the original decision-maker in the application of the principle of proportionality. Considerations of the "balance of power" among branches of the government in a constitutional system bear upon this question of the intensity of review to be applied by the courts and the level of deference to be afforded to the original decision-maker.[1296]

In the international investment regime, there is no explicit indication of what such a balance of power may be, whose powers are being balanced, or the requirements such a balancing exercise might impose on the intensity of review.

5.1.1.2 Legal Uncertainty in the Context of the Investment Regime

The combination of structural organization of the investment regime and imprecise treaty drafting "provides fertile ground for inconsistency in arbitral awards".[1297] From a systemic perspective, "there is a contradiction between the granting to *ad hoc* arbitral tribunals of the wide discretion that BIT standards entail and expecting consistency of their decisions".[1298] Based on the interpretation of the FET standard in NAFTA, we can make two observations. First, *how* exactly the ISA tribunals contribute to our understanding of MST (as well as other investment standards) may be in itself problematic. If the tribunals almost unanimously acknowledge that MST-FET is an evolving standard, the standard's scope will *always* depend on its interpretation by each individual ISA tribunal. If tribunals define the scope of the standard on a case-by-case basis, including by citing the decisions of prior tribunals and without clearly establishing

[1296] Jansen Calamita, "The Principle of Proportionality and the Problem of Indeterminacy in International Investment Treaties" in Andrea Bjorklund, ed, *Yearbook on International Investment Law & Policy, 2013-2014* (Oxford: Oxford University Press, 2015) at 177.
[1297] Celine Levesque, "Inconsistency in Investor-State Awards and the Role of State Interpretations: the Example of the Mexican Sweetener Trio of Cases under NAFTA" in Andrea Bjorklund, ed, *Yearbook on International Investment Law & Policy, 2013-2014* (Oxford: Oxford University Press, 2015) at 361.
[1298] Sureda (2012), at 139.

the mandatory elements of state practice and *opinio juris* in their decisions,[1299] tribunals' decisions will *de facto* create rather than reflect the international minimum standard. States never will be able to eliminate the impact of previous arbitral cases entirely, and, hence, would never be able to reassert full control over the meaning of FET except by eliminating it, treaty by treaty.

Second, the development of law within the investment regime is subject to different dynamics than the incremental evolution of legal norms within municipal legal systems, whether common law or civil law. As opposed to domestic legal systems, multiple ISA tribunals function on *ad hoc* basis and apply the decentralized sources of law. The tribunals operate under no legislative or administrative oversight or hierarchical structure to ensure consistent application and interpretation of the governing law. As a result, ISA tribunals can choose one interpretive approach or another without any systemic constrains.[1300] National judges "deliberate in a shadow of more constraining checks such as appellate review or legislative override".[1301] Arbitrators, by contrast, have significant flexibility in interpreting the rules without fear that their views may be overridden.[1302] These features make the process of law development and crystallization

[1299] In *Mondev* case, the tribunal for example referenced the "the numerous transmittal statements by the United States of BITs containing language similar to that of NAFTA" to determine opinion juris, see at *Mondev* at para.111. In *Mondev* at para. 117, the tribunal also underscored that "the vast number of bilateral and regional investment treaties (more than 200048) almost uniformly provide for fair and equitable treatment of foreign investments" constitute "a body of concordant practice will necessarily have influenced the content of rules governing the treatment of foreign investment in current international law". the tribunal thus arrived to the conclusion that such body of treaties represent state practice and thus expands the MST beyond *Neer*. It is worth noting that IIAs often do not define the meaning of FET or MST but simply require states to accord foreign investors such treatment. Such cross-reference is thus "empty" as it does not seem to add any content to defining the scope of the standard.

[1300] The tribunals can choose among the interpretative tools of art.31 of VCLT.

[1301] *Mondev* at para.111.

[1302] Armand de Mestral & Lukas Vanhonnaeker, "The Impact of the NAFTA Experience on Canadian Policy Concerning Investor-State Arbitration" in Armand de Mestral, ed, *Second Thoughts: Investor State Arbitration between Developed Democracies* (Montreal: McGill-Queen's Press, 2017).

different from the incremental development of legal norms within domestic legal systems.

The main implication of these differences is that it may be difficult to "deliver that degree of consistency without the factors that normally stabilize adjudication in national court systems".[1303] Of course, national legal systems also provide for some degree of divergence in legal interpretations; the domestic systems, however, possess systemic features capable of to correct divergencies if necessary.[1304] Karton explains that, "[o]n the global level, the factors that contribute to a lack of interpretative uniformity are multiplied. There is no comprehensive code, no global appellate court to strike aberrant interpretations, no system of binding precedent, and no share legal culture with common interpretative methods".[1305] As a result, arbitral tribunals may reach "multiple, equally reasonable interpretations" of the legal standards in IIAs.[1306] The next section shows how ISA tribunals not only fall short on clarifying the investment standards but also often generate even greater uncertainty over their content.

5.1.2 Institutional Incentives

This section examines the institutional features of the investment arbitration such as the party-driven appointment system, the lack of safeguards such as a security of tenure, and the collegiality of the arbitral profession, and the incentives these create for arbitrators. It argues that these systemic features incentivize arbitrators not to dismiss frivolous and abuse of process claims early in the proceedings.

[1303] Karton (2015), at 52.
[1304] *Ibid* at 58.
[1305] *Ibid*.
[1306] *Ibid*.

This section does not argue that ISA arbitrators, individually or as a group, are biased in favour of foreign investors or states. Rather, the goal is simply to describe the effects of incentives on arbitral decision-making, which operate systemically and separately from any kind of impartiality specific to a particular arbitrator. Arbitrators are rational actors that can be incentivized by promise of financial and reputational gains.[1307] The arbitrators also operate within the broader institutional context of the "political and legal system" [1308] that is the investment regime. Clayton and May explain that "judicial attitudes and strategies in decision making are both constituted and constrained by the broader context" of the legal and political system in which the adjudicators function.[1309]

Although the governing law (to the extent it is determinable) is no doubt the biggest factor in arbitral decision-making, arbitrators, like all humans, arrive at their decisions influenced by their self-interest, considerations of prestige, and intention to provide an expert legal opinion. Although part of a broader institutional framework, they also make decisions not only according to their own preferences but in response to the dominant values of the given political or legal system, which are in turn shaped by its participants.

Here, I focus on identifying how the investment regime's structures and procedures may influence arbitral incentives in the decision-making process with respect to frivolous and abuse of process claims. I argue that the current institutional arrangement of who makes arbitral appointments and how, along with some aspects of the social

[1307] Posner (1993), at 2.
[1308] Cornell Clayton & David May, "A Political Regimes Approach to the Analysis of Legal Decisions" (1999) 32:2 Polity 233. May and Clayton make this argument in the context of the US SC [*A Political Regimes Approach*]. Sotirios Barber, "Normative Theory, the New Institutionalism, and the Future of Public Law (1989) 3 Studies in American Political Development 56.
[1309] Mark Miller, *The View of the Courts from the Hill: Interactions between Congress and the Federal Judiciary* (University of Virginia Press, 2009) at 32. [*A Political Regimes Approach*].

dynamics of the arbitral role, embed incentives for arbitrators not to curtail claims early in the proceedings. First, I address the lack of protected tenure and the other job safeguards that apply to domestic judges. Second, I examine the party-driven approach to arbitral appointments. Finally, I discuss the issue of social dynamics within the community of arbitrators.

5.1.2.1 Lack of Safeguards

This subsection considers the lack of job safeguards for arbitrators in the investment regime. Institutionally, the investment regime does not establish the administrative and economic safeguards that guarantee judicial independence, such as security of tenure, rotation of case assignments, and prohibition on outside employment.[1310] The lack of safeguards is likely to make arbitrators more susceptible than national court judges to pecuniary and non-pecuniary incentives. As Schultz puts it, the pursuit of self-interest is an adequate "representation of human psychology", and the one who benefits from arbitration "as arbitrator, as counsel, as expert, as advisor to any of the proceedings" is subject to definable incentives.[1311] Accordingly, this thesis does not advance an argument that individual arbitrators are by default biased[1312] but suggests that

[1310] Thomas Schultz, "International Arbitration Scholarship: Forms, Determinants, Evolution" in Stavros Brekoulakis, Julian Lew & Loukas Mistelis, eds, *The Evolution and Future of International Arbitration* (The Hague: Walters Kluwer, 2016) at 448.
[1311] *Ibid* at 446-447. Thomas Schultz, "Arbitral Decision-Making: Legal Realism and Law & Economics" (2015) 6 JIDS 231. (discussing incentives in arbitration generally).
[1312] it is not to say that particular cultural/ background features of individual arbitrators (such as, age, gender, race, previous affiliation, current primary occupation) does not matter. They do. See more general discussion on how individual characteristics of judges impact judicial decision-making in Mark Cohen, "The Motives of Judges: Empirical Evidence from Antitrust Sentencing" (1992) 12:1 Intl Rev L & Econ 13 at 16. Kastellec Jonathan, "Racial Diversity and Judicial Influence on Appellate Courts" (2013) 57:1 American Journal of Political Science 167. More specific on this issue in investment arbitration context: Joost Pauwelyn, "The Rule of Law without the Rule of Lawyers? Why Investment Arbitrators are from Mars, Trade Adjudicators from Venus" (2015) 109:4 AJIL 761. David Schneiderman, "Judicial Politics and International Investment Arbitration: Seeking an Explanation for Conflicting Outcomes" (2010) 30:2 Nw J Intl L & Bus 761 at 385. Elena Helmer, "International Commercial Arbitration: Americanized, Civilized, or Harmonized" (2003) 19:1 Ohio St J Disp Resol 35.

the mere perception of arbitral bias can "arise from the institutional structure of investor-state arbitration".[1313] The following sections address security of tenure, the lack of restrictions on non-arbitrator employment, and the absence of rotation of case assignments to show how the lack of those features renders inadequate the existing mechanisms for the early curtailment of frivolous and abuse of process claims.

5.1.2.2 Security of Tenure and Compensation

This section will address the structure of arbitral compensation together with the guarantes established by security of tenure. Although the two issues are distinct, they are interrelated and thus will be addressed together. In national legal systems, judges typically possess security of tenure to ensure their independence from the parties.[1314] Fabien Gélinas explains that "security of tenure" has two dimensions.[1315] They are "personal" and "institutional".[1316] According to Gélinas, "[s]ecurity of tenure in its personal dimension demands a sufficiently long term of appointment, as well as safeguards against the consideration of past or future adjudicative orientation in any renewal process".[1317] In its turn, the institutional aspect entails "the institutional protection of established tribunals. It calls for safeguards against inappropriate institutional tampering by the political branches".[1318]

In the investment regime, there is no such structure but rather *ad hoc* appointment of arbitrators for each dispute. The lack of security of tenure makes arbitrators'

[1313] Gus Van Harten, Comments on the European Commission's Approach to Investor-State Arbitration in TTIP and CETA (2014) Osgoode Legal Studies Research Paper No. 59 at 40.
[1314] Enid Campbell, Hoon Phun Lee & Enid Mona Campbell, *The Australian Judiciary* (Cambridge: Cambridge University Press, 2013) at 250. H. P. Lee,ed, *Judiciaries in Comparative Perspective* (Cambridge: Cambridge University Press, 2011) at 15-20.
[1315] Fabien Gélinas, "The Independence of International Arbitrators and Judges: Tampered With or Well-Tempered?" (2011) 24:1 NY Intl L R 1 at 5-6.
[1316] *Ibid* at 6-7.
[1317] *Ibid*.
[1318] *Ibid*.

remuneration dependent on two factors: the hourly or daily rate paid by disputing parties and the length of the proceedings. Under such a such structure, "the arbitrators […] depend financially on whoever has the ability to make the claims and trigger the arbitrators' appointments".[1319] Puig observes that arbitrators can make "on average $200,000 per case", at least in investor-state disputes under ICSID.[1320]

Interestingly, judicial compensation was a matter of serious debate in England, France, and the United States from 17th to 19th centuries.[1321] Alexander Hamilton, Jeremy Bentham and Voltaire all advocated against collection of litigants' fees (the prevailing means of judicial compensation at the time) in favour of fixed salaries for the judiciary.[1322] For example, Bentham argued that the "fee gathering system" then prevalent in England created an "incentive for complicated procedures that multiply fees".[1323]He saw the payment of fixed salaries for judges, together with lifetime appointments, as necessary for judicial independence.[1324] In the Federalist Papers, Hamilton argued that "in the general course of human nature, a power over a man's subsistence amounts to a power over his will".[1325] Accordingly, most national legal systems have introduced "intstitutional safeguards" to guarantee judicial independence. These safeguards include "secure tenure for adjudicator instead of case-by-case appointment, set renumeration for the adjudicator instead of case-by-case (that is, for

[1319] Gus Van Harten, "The European Comission and UNCTAD Reform Agendas: Do They Ensure Independence, Openess, and Fairness in Investor-State Arbitration" in Steffen Hindelang & Markus Krajewski, *Shifting Paradigms in International Investment Law: More Balanced, Less Isolated, Increasingly Diversified* (Oxford: Oxford University Press, 2016) at 40.
[1320] Puig (2014), at 398. Compensation depends on the particular dispute and arbitrators can earn less or more; most scholars refer to the standard ICSID compensation rate to illustrate that the position of arbitrator can be lucrative.
[1321] David Gaukrodger, "Adjudicator Compensation Systems and Investor-State Dispute Settlement" OECD Working Paper (2017) at 9-11.
[1322] *Ibid*.
[1323] *Ibid*.
[1324] *Ibid*.
[1325] The Federalist Papers as cited in Gaukrodger (2017), at 10.

profit) payment, an objective method of case assignment such as lottery or rotation".[1326] In ISA, these institutional safeguards are absent, a fact that "gives rise to reasonable suspicion of bias".[1327]

Of course, this is not to say that arbitrators are motivated exclusively or even primarily by financial incentives.[1328] Rau underscores that the influences on arbitrators are "multiple and varied"[1329] and include "the opportunity to enhance one's education, one's familiarity with particular spheres of human endeavour, one's circle of contacts, or one's professional profile. For many, there may also be some sense of noblesse oblige or a desire to engage in public service. Nor should one neglect the pleasures of judging."[1330] To deny that arbitrators may be influenced by any of those incentives means to ignore that arbitrators are human. Yet, "our received wisdom is that none of these motives should be allowed to work in such a way as to call into question the impartiality of the decision-maker".[1331]

Moreover, arbitrators could usually earn more money working as legal counsel for governments or foreign investors, because counsel work can employ large teams of associate lawyers. Hence, while financial rewards from employment as an arbitrator are significant, they are unlikely to be the main factor directing arbitral conduct. The financial factor may be particularly influential in case of the so-called "professional class

[1326] Van Harten (2016), at 40.
[1327] *Ibid*.
[1328] Alan Rau, "Integrity in Private Judging" (1998) 14:2 Arbitration Intl 115 at 115.
[1329] *Ibid*.
[1330] *Ibid*.
[1331] *Ibid* at 116.

of arbitrators" who do little or no counsel work and depend on appointments for their livelihoods.[1332]

Since investment arbitrators are usually paid per hour or per day, they have a financial interest in prolonging the proceedings.[1333] Although money is hardly the only influence on arbitrators' decision-making, it is undeniable that the existing mechanisms put individuals who have an explicit financial incentive to prolong the proceedings in charge of the early dismissal of frivolous and abuse of process claims. In such a context, it should not be surprising that only the most blatantly unmeritorious or abusive are dismissed *in limine*.

5.1.2.3 Prohibition on the Outside Employment

In national legal systems, judges normally cannot accept outside employment. This limitation is in place to ensure that judges have no "network" of relationships outside of the court that will make them financially or otherwise dependent on disputing parties or others with an interest in the litigation. In the investment regime, arbitrators can be adjudicators in one dispute and simultaneously or consecutively counsel in others.[1334] The lack of any prohibition on outside employment may reinforce a pattern of strategic behaviour among arbitrators, whereby they are incentivized to resolve disputes before them in ways that strengthen their personal network to ensure their reappointment in future disputes.[1335] When the arbitrators in some disputes seek to serve as counsel for

[1332] David Branson, "Sympathetic Party-Appointed Arbitrators: Sophisticated Strangers and Governments Demand Them" (2010) 25:2 ICSID Rev 367 at 368, 375-377.
[1333] Profiting from Injustice at 51. David Schneiderman & Gus Van Harten, "Self-interested lawyers and the Canada-China FIPA" *University of Toronto* (blog). Cohen (1992), at 13.
[1334] Nassib Ziadé, "How Many Hats Can a Player Wear: Arbitrator, Counsel and Expert?" (2009) 24:1 ICSID Rev 49.
[1335] Sergio Puig, "Social Capital in the Arbitration Market" (2014) 25:2 EJIL 387 at 400. Puig also suggests that "arbitrators may perceive some indirect gains by agreeing or disagreeing with colleagues (i.e., an arbitrator may be simultaneously advising another party in other proceedings and therefore prefer a

foreign investors in other disputes,[1336] they may be reluctant to dismiss claims as frivolous and abuse of process because such dismissals may reflect on their personal records. Such decisions may signal to the parties that the arbitrator is apt to use the procedures for the curtailment of investors' claims and not to give the claimants a chance to proceed to a full-scale determination of the merits. There is also a risk of being labelled as a "pro-state" arbitrator if the arbitrator supports the dismissal of several claims as frivolous or abuse of process. Such a record is important because the parties scrutinize potential arbitrators' records prior to making appointments.[1337] Puig observes that "the trend of appointment by one type of litigant"[1338] is a strategic response of arbitrants (both states and investors) to political preferences signalled by the arbitrators.[1339] Pauwelyn concludes that parties appoint arbitrators "with a proven track record and prior disclosed preferences […] to maximize party's chances of success".[1340] Overall, most arbitrators share a "similar professional background".[1341] According to Bonnitcha, Poulsen, and Waibel, "of the 536 individuals appointed to ICSID tribunals at the time of writing, only 25 per cent have been public international lawyers; 11 per cent have been public lawyers;

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particular legal interpretation that benefits his client in such other proceedings)". Luke Peterson, "ICSID Tribunal Admits Counter-Claim in BIT Dispute. Outcome is a Setback for Counsel that Had Recently Sat as Arbitrator in Case Where Counter-Claims are Excluded" (2012) Investment Arb Reporter (blog).

[1336] This practice is known as "double hatting" meaning that arbitrators often participate in the investment proceedings as legal counsel. There is a significant overlap between the arbitrators and legal counsel. Malcolm Langford Daniel Behn & Runar Hilleren Lie, "The Revolving Door in International Investment Arbitration" (2017) 20:2 J Intl Econ L 301–332. Andreas Kulick, *Reassertion of Control over the Investment Treaty Regime* (Cambridge: Cambridge University Press, 2016) at 373.

[1337] Puig (2014), at 402.

[1338] *Ibid*.

[1339] *Ibid* at 404. Puig observes that some arbitrators, for example Stern was appointed 48 times and among them, 44 times by states; another arbitrator Bower held 25 appointments, 23 of which were made by foreign investors.

[1340] Joost Pauwelyn, Who Decides Matters: The Legitimacy Capital of WTO Adjudicators versus ICSID Arbitrators in Harlan Grant Cohen et al, eds, *Legitimacy and International Courts* (Cambridge: Cambridge University Press, 2018) at 230.

[1341] Bonnitcha, Poulsen & Waibel (2018), at 255.

whereas the remaining arbitrators have mostly specialized in commercial law".[1342] Bonnitcha, Poulsen, and Waibel explain that "[t]hese characteristics could matter when arbitrators look for answers to difficult and new questions, particularly when interpreting and applying open-ended standards of treatment such as indirect expropriation or FET".[1343] Specifically, arbitrators who share commercial law backgrounds may be "less sympathetic to interests outside their traditional domains, such as human rights, or less willing to consider the impact of their awards on other parts of the investment regime complex".[1344] Such "homogeneity among arbitrators" can potentially "create – in appearance or in reality – a pro-investor bias".[1345] These concerns are exacerbated by the "private standing" in the investment regime, whereby only investors may sue states, so ultimately investors generate all of the opportunities for arbitral appointments.[1346]

5.1.2.4 Rotation of Case Assignments

The random assignment of cases to adjudicators is another institutional feature that safeguards judicial integrity in national legal systems.[1347] Most jurisdictions follow random or quasi-random procedures for assigning cases.[1348] This helps to ensure that the "outcome of a specific case cannot be influenced through deliberate judge selection".[1349] Entin describes some attempts to influence random case assignments in the US courts, which resulted in severe sanctions; "people have gone to jail and lawyers have been

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[1342] *Ibid* at 256.
[1343] *Ibid*.
[1344] *Ibid*.
[1345] *Ibid*.
[1346] Jan Paulsson, *The Idea of Arbitration* (Oxford: Oxford University Press, 2013) at 278.
[1347] Robert Brown & Allison Herren Lee, "Neutral Assignment of Judges at the Court of Appeals" (2000) 78 Tex L Rev 1037, 1044.
[1348] Shimon Shetreet & Christopher Forsyth, *The Culture of Judicial Independence: Conceptual Foundations and Practical Challenges* (The Hague: Martinus Nijhoff Publishers, 2011) at 496-498.
[1349] *Ibid* at 496.

severely disciplined for trying to circumvent the assignment system".[1350] Implicit in these rules is an understanding that the identities of the adjudicators influence case outcomes.[1351] The circumvention of the random assignment process thus is viewed as an attempt to improperly influence the final outcome of a dispute. As a matter of principle, in the domestic legal context, for parties to choose their judge would contradict the basic due process guarantee of a "fair trial in a fair tribunal".[1352]

Of course, in the investment regime, parties select their "own judges" in every case. On the one hand, this arrangement benefits the parties (and the process itself) because it permits parties to select adjudicators with relevant expertise. On the other hand, the lack of random assignment in means that the parties can choose adjudicators with particular profiles, including those who are more or less willing to dismiss claims as frivolous or abuse of process. The lack of random case assignments must be viewed together with the party-driven appointment system in its effect on the dismissal of frivolous and abuse of process claims. The arbitrators may be cautious to take an overly broad approach to the dismissal of claims as frivolous or abuse of process for fear that they will be seen as "procedurally unfair" because they do not allow the parties to air their arguments. This label is a serious "hit" for arbitrators' profiles and their social capital in the community. Since an award may be challenged on these grounds, (for example, under art. V(1)(b) of the New York Convention), failing to provide each party an opportunity to present its case would mean that the tribunal has failed to fulfil its obligation to render an enforceable award. It is thus important for arbitrators to maintain

[1350] Jonathan Entin, "The Sign of `The Four': Judicial Assignment and The Rule of Law" (1998) 68:1 Mississippi L J 369 at 373.
[1351] *Ibid*.
[1352] *Ibid* at 374.

at minimum the appearance of procedural fairness; the easiest way to do this is to permit the parties to supply to the tribunal all materials they want, and to present all of the arguments they want during both jurisdictional and merits phases of the proceedings. If case assignments were randomized, the arbitrators would not have far less of an incentive to think about prospective appointments.

To sum up, the mechanisms for the early dismissal of claims in the investment regime replicate those existing in the national legal systems, but the investment regime lacks systemic safeguards such as security of tenure, prohibition of outside employment, and rotation of case assignments that protect the independence and impartiality of the domestic judiciary. Arbitrators are therefore vulnerable to incentives not to dismiss frivolous and abuse of process claims early in the proceedings. In addition, this makes the arbitrators vulnerable to suspicion, or as Van Harten puts it, "a reasonable perception of bias",[1353] that they may not utilize the mechanism for the early dismissal of claims because they have a financial interest in prolonging the proceedings. Such suspicion, even if entirely misplaced, is problematic in itself because it contributes to greater mistrust of participants of the investment regime in the fairness (and therefore legitimacy) of ISA.[1354]

5.1.3 The Party Driven Appointment Process

The previous section considered how arbitrators are appointed; this section considers who makes the appointments. In the investment regime, the arbitrators may be

[1353] Gus Van Harten, "Perceived Bias in Investment Treaty Arbitration" in Michael Waibel et al,eds, *The Backlash Against Investment Arbitration: Perceptions and Reality* (The Hague: Kluwer Law International, 2010). Gus Van Harten, "Arbitrator Behaviour in Asymmetrical Adjudication (Part Two): An Examination of Hypotheses of Bias in Investment Treaty Arbitration" (2016) 53:2 Osgoode Hall LJ 540 at 559.
[1354] William Park, "Why Bias Matters" in Michael Waibel,ed, *The Backlash Against Investment Arbitration: Perceptions and Reality* (The Hague: Kluwer Law International, 2010) at 208.

appointed by the parties to the dispute, by the party-appointed arbitrators, by the administering arbitral institution, or by an independent appointing authority.[1355] For example, the governing IIA can designate the appointment of the chairman to the President ICJ.[1356] This chapter focuses on the conventional ISA model but recognizes that some variety exists between cases in who appoints the members of the tribunal.[1357]

The party-driven appointment system in the investment regime (as well as in international commercial arbitration) has become a subject of intense scholarly debate. There are three major approaches to the issue. First, many critics of the investment regime argue that the current appointment procedure encourages arbitrators to "favour their appointing party in a self-interested effort to increase the likelihood of future appointments".[1358] For example, Branson argues that the party-driven appointment procedure creates "moral hazard", particularly "[i]f one party-appointed arbitrator sees a 'duty' to act for the benefit of the appointing party and the other follows the dictates of the law and remains neutral, then there is an imbalance, the process can be unfair and it can produce injustice".[1359] Yuval explains that the party-driven appointment procedure is

[1355] OECD, Appointing Authorities and the Selection of Arbitrators in Investor-State Dispute Settlement: An Overview, Consultation Paper, online:< https://www.oecd.org/investment/investment-policy/ISDs-Appointing-Authorities-Arbitration-March-2018.pdf> at para.16-17.
[1356] Anthony Aust, *Modern Treaty Law and Practice* (Cambridge: Cambridge University Press, 2000) at 294.
[1357] The newer investment treaties, such as CETA, prescribe a unique procedure for appointment of the arbitrators. David Schneiderman, Why CETA Is Unlikely to Restore Legitimacy to ISA Investor-State Arbitration Commentary Series No. 7 (2016), CIGI, online: <https://www.cigionline.org/publications/why-ceta-unlikely-restore-legitimacy-isds>. Van Harten (2014), at 40.
[1358] Catherine Rogers, "The Politics and Empirics of International Investment Arbitrators" (2014) 12:1 Santa Clara Intl L Rev 223 at 226.
[1359] Branson (2010), at 368. Paulson raised similar argument that "moral hazard is inherent in the system of party-driven appointment procedure. Paulson goes as far as to arguing for abandoning the party-driven appointment procedure. Jan Paulsson, "Moral Hazard in International Dispute Settlement" (2010) 25:2 ICSID Rev 339. Yves Derains, The Arbitrators Deliberation in Fifth Annual Lecture on International Commercial Arbitration, Presentation at American University Washington College of Law, Washington, D.C. (11 November 2010) (argues that the party-appointed arbitrators are often favouring the party that appointed them and sacrifice neutrality), online:< https://www.wcl.american.edu/arbitration/annuallecture.cfm>.

inherently predisposed to result in the appointment of "partisan" arbitrators.[1360] Van Harten concludes that the arbitrators are "repeat players" who, out of self-interest, seek future appointments and accordingly, favour those actors that can provide such appointments.[1361]

The second approach, associated with proponents of the regime, contests this speculation by positing that it is in arbitrators' interests to uphold their reputation as independent and impartial adjudicators, in that such a reputation is the most valuable asset in generating future appointments.[1362] Kapeliuk shows that "arbitrators do not have a tendency to render compromise awards. The results also clearly defy any claim that investment-arbitration tribunals tend to rule in favour of investors".[1363] Drahozal has made a similar argument.[1364] Richard Posner makes a general observation on arbitrators in any context, relevant to ISA as well, that "an arbitrator who gets a reputation for favouring one side or the other in a class of cases [...] will be unacceptable to one of the parties in any such dispute, and so the demand for his services will wither".[1365] Moreover an arbitrator with a reputation for partisanship may have little influence on other

[1360] Shany Yuval, "Squaring the Circle? Independence and Impartiality of Party-Appointed Adjudicators in International Legal Proceedings" (2008) 30:3 Loy LA Intl & Comp LJ 473. Catherine Rogers also underscores that some arbitrators have shown obvious favouritism towards their appointer. According to Rogers, the arbitrator from Saudi Arabia collaborated with his appointer to plan its case strategy; the arbitrator from India did not disclose that he represented its appointer in a number of cases previously. Canadian arbitrator once did not disclose that he was a director in the company. Catherine Rogers, "Regulating International Arbitrators: A Functional Approach to Developing Standards of Conduct" (2005) 41 Stan J Intl L 53 at 53-55.

[1361] Gus Van Harten, "Arbitrator Behaviour in Asymmetrical Adjudication: An Empirical Study of Investment Treaty Arbitration" (2012) 50:1 Osgoode Hall LJ 211 at 219-220. Similar issues are discussed by Catharine Rogers, "The Politics of International Investment Arbitrators" (2014) 223 12 Santa Clara J Intl L 223 at 236-237.

[1362] Michael Waibel, "Arbitrator Selection: Towards Greater State" in Andreas Kulick, ed, *Reassertion of Control over the Investment Treaty Regime* (Cambridge: Cambridge University Press, 2016) at 345.

[1363] Daphna Kapeliuk, "The Repeat Appointment Factor: Exploring Decision Patterns of Elite Investment Arbitrators" (2010) 96 Cornell L Rev 47 at 90.

[1364] Christopher Drahozal, "A Behavioural Analysis of Private Judging" (2004) 67 Law & Contemp Probs 127.

[1365] Richard Posner, "Judicial Behaviour and Performance: An Economic Approach" (2005) 32 Fla St UL Rev 1259 at 1261.

members of the tribunal. Without an ability to steer his or her colleagues, the arbitrator-partisan can end up producing many dissenting opinions without actually shaping enforceable outcomes.

The divergent outcomes of these studies are a result of different methodologies. For example, in her data sample Kapeliuk focuses only on arbitrators that were appointed four times or more (whom she calls "elite arbitrators"); it thus excludes other party-appointed arbitrators. The data sample also excludes rulings on preliminary objections, and does not specifically examine the awards in which the tribunals held claims to be an abuse of process. In her assessment, Kapeliuk focuses on the damages that the tribunals order without examining the particular approaches of the "elite" arbitrators to the scope of the substantive standards or the standard of review. In contrast to Kapeliuk, Van Harten shows a "tendency toward expansive resolutions where the claimant was from a Western capital exporting state".[1366] The difference may be due to different samples or to extra-legal factors such as cognitive bias, which are difficult to quantify.

As a result, the current empirical evidence on the matter of arbitral bias is inconclusive.[1367] The two camps make plausible but rather one-sided arguments. They either consider arbitrators to be "villains"[1368] and "ambulance chasers"[1369] who seek to enrich themselves instead of upholding justice,[1370] or instead to be wise, impartial, and

[1366] Van Harten (2012), at 214.
[1367] Rogers (2014), at 223.
[1368] Jan Paulsson, "What Authority Do International Arbitrators Have Over States" in Albert Jan van den Berg, ed, *New Horizons in International Commercial Arbitration and Beyond* (The Hague: Kluwer Law International, 2005) at 136.
[1369] David Schneiderman, "Investment Lawyers and Arbitrators" in C. L. Lim, ed, *Alternative Visions of the International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2016) at 134. Surya Subedi, *International Investment Law: Reconciling Policy and Principle* (London: Bloomsbury Publishing, 2016).
[1370] Van Harten (2010), at 213, 432. ("Investment treaty arbitration is characterized by an apparent bias in favor of claimants and against respondent states. This perception is reasonably held in light of structural features of the system, especially its use of arbitration to decide public law").

even immune to self-interest. These two approaches are not only inaccurate on their own terms, but they both miss the point by focusing more on arbitrators themselves than on the systemic context within which arbitrators work.[1371]

The third approach attempts to rationalize the two opposing camps. Brekoulakis argues that institutional processes shape and direct conduct of adjudicators.[1372] Specifically, the party-driven appointment procedure "provides the disputing parties with a unique opportunity to shape the judicial values of the tribunal".[1373] The appointment procedure is an element of the investment regime's institutional design that may influence adjudicators' conduct,[1374] – or at minimum, the parties often perceive it to be such.[1375] The problem of "double-hatting", of arbitrators switching between roles as arbitrator or counsel, contributes to a perception that the arbitrators' conduct may influenced by the political or personal considerations rather than the law alone.[1376]

[1371] Stavros Brekoulakis, "Systemic Bias and the Institution of International Arbitration: A New Approach to Arbitral Decision-Making" (2013) 5:3 Journal of International Dispute Settlement 553 at 560.
[1372] *Ibid*
[1373] *Ibid*.
[1374] New institutionalism helps to establish the link between "institutions and behaviour" in particular, "o how institutional arrangements shape purposive behaviour". Melinda Gann Hall and Paul Brace proved that "decision rules and judicial selection methods are related to dissent" in Melinda Gann Hall & Paul Brace, "A Neo-Institutional Approach to Judicial Consensus" (1989) 42:3 The Western Political Quarterly .391 at 392, 404.
[1375] Jan Paulsson explains "a certain perception of reality and a distaste for hypocrisy cause some practitioners to conclude that one should simply expect that a party-appointed arbitrator will behave as impartially as one appointed jointly or by a neutral authority […] they have a plausible argument. Why do arbitration agreements so often explicitly provide for two unilateral nominations unless each party expects something different from its nominee than from joint or neutral appointees" in Jan Paulsson, "Ethics, Elitism, Eligibility" (1997) 14:4 Arb Intl 13 at 13-14.
[1376] Malcolm Langford, Daniel Behn & Runar Hilleren Lie, "The Ethics and Empirics of Double Hatting ESIL Reflections" (24 July 2017) ESIL-Sedi (blog) at 8. (pointing out that "the key reason for the skepticism to the practice can be summarized in this dilemma. Philippe Sands asks: Can a lawyer that "spends a morning drafting an arbitral award that addresses a contentious legal issue" divorce themselves from their role in addressing the same or similar legal issue in the "afternoon" as counsel in a different case. And, even if they can, would they be able to convince a reasonable observer that such role bifurcation was maintained. The concern remains: an arbitrator's ability to shape legal precedent and evaluation of facts (or access confidential information) may assist them as legal counsel elsewhere. Another concern would be the inverse of the first: an arbitrator acting as legal counsel is colored by their arbitral role or uses his or her pleadings in one case for the purpose of being picked up and used by the same individual in their work as an arbitrator in another case".Phillipe Sands, "Conflict and Conflicts in Investment Treaty

Arbitrators are not evil, but they are not angels either, and they necessarily operate within the broader context of the regime's structures.[1377] The party-driven appointment procedure makes arbitrators heavily dependent on how the parties perceive the arbitrator's role. In other words, what the parties expect of the arbitrators can alter how they conduct themselves because the parties evaluate arbitrators' performance – and make decisions on future appointments – on the basis of such expectations. Karl-Heinz Böckstiegel, a well-known German arbitrator, underscores that "in investment treaty arbitration […] it does, of course, occur that a party-appointed arbitrator, though not challenged or challengeable for lack of impartiality, may in practice consider and use his role as having to represent the interest of the parties that appointed him within the tribunal".[1378] This does not imply a default bias or favouritism of arbitrators toward the appointing party. Yet the structure of appointments can influence what arbitrators actually do in their awards on the merits and what procedural choices they make. An example of such influence is the phenomenon of "mandatory dissents", whereby party-appointed arbitrators may feel obligated to issue a dissent if it appears that the party that appointed them will lose on the merits.[1379] According to Paulsson:

> we must confront an uncomfortable fact. Two recent studies of international commercial arbitrations have revealed that dissenting opinions were almost invariably (in more than 95% of the cases) written by the arbitrator nominated by the losing party [...] This troubling record is

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Arbitration: Ethical Standards for Counsel" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (New York: Brill, 2012) at 28-49. Langford, Behn & Lie, (2017) at 301.

[1377] Brekoulakis (2013), at 553. (Brekoulakis makes an argument that the investment regime institutionally and systemically reinforces bias).

[1378] Bockstiegel (2003), at 371.

[1379] Albert Van Den Berg, "Dissenting Opinions by Party appointed Arbitrators in Investment Arbitration" in Mahnoush Arsanjani et al, eds, *Looking to the Future: Essays on International Law in Honor of W. Michael Reisman* (The Hague: Martinus Nijhoff, 2010) at 821–43.

> duplicated in the newer field of treaty-based arbitrations brought by foreign investors against states.[1380]

There are two problems that arise from this state of affairs. First, "the appointing party has made an accurate reading of how its nominee is likely to view certain propositions of law or circumstances of fact".[1381] Second, the party-driven appointment procedure encourages arbitrators to respond to the expectations of their appointers in hopes of being reappointed.[1382]

Dissents can constitute a powerful tool for an adjudicator, in not only a legal but also a social sense.[1383] Dissents constitute a way for an arbitrator to signal their position on the legal issues implicated in the case. Dissents thus give arbitrators an opportunity to behave strategically, to signal their positions on issues that are likely to recur in future cases.[1384] Even where they do not affect the outcome of the instant case, dissents can affect future cases because they help parties to identify which adjudicators they want to appoint for which types of claims.

These observations align with the political system framework of Dupont and Shultz. According to the lens of political system, the participants have to interact with other participants in a broader context of the investment regime. Accordingly, investment arbitrators fully appreciate that "their fates depend on the preferences of the other actors

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[1380] Jan Paulsson, "Moral Hazard in International Dispute Resolution" (2010) 25:2 ICSID Rev 339 at 348.
[1381] *Ibid* at 349.
[1382] Paulsson (1997), at 14. ("whatever their motivation, arbitrators tend to want to be reappointed").
[1383] Howard Perry, *Deciding to Decide: Agenda Setting in the United States Supreme Court* (Cambridge: Harvard University Press, 2009) at 174, 213 (showing that dissent may be a form of communication). Tonja Jacobi, "The Judicial Signalling Game: How Judges Shape Their Dockets" (2008) 16:1 Sup Ct Econ Rev 1 at 4. (arguing that "Dissents are, among other things, common forms of signalling" it is important to understand what is the goal of such signalling. There will be systemic differences between domestic judges and arbitrators. For arbitrators (given the nature of party-driven appointments system, it is to attract future appointments).
[1384] Daphna Kapeliuk, "Collegial Games: Analyzing the Effect of Panel Composition on Outcome in Investment Arbitration" (2012) 31:2 Rev of Litigation 267.

and the choices they expect them to make (not just their own preferences)".[1385] In this context, it makes sense to ask: "what do the other participants in an investment dispute (the state and investor) expect from the arbitrators?" [1386]

In short, the answer is that both parties want the arbitrators to resolve the dispute between them.[1387] That is why they pay the arbitrators. Van Den Berg makes it clear that "the parties expect […] *a fair decision in their dispute.* They pay for it, not for developing the system. And I think they are right. Law schools should pay a professor for developing ideas, possibly contributing to the system, but parties should pay for a solution to their dispute".[1388] Of course, the expectation is that such a "fair" decision rendered by the tribunal will be enforceable, so the parties are also paying for the legal effect of the tribunal's decision.

The tribunal must be careful in making procedural decisions not to deprive a party of the opportunity to present its case.[1389] The *New York Convention* stipulates that a court may refuse to enforce an award if the losing party was not able to present its case.[1390] Similarly, the UNCITRAL Model Law incorporates a similar requirement: "[t]he parties

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[1385] Lee Epstein, ed, *Contemplating Courts* (Washington D.C.: SAGE, 1995) at 6.
[1386] White & Case, "International Arbitration Survey: Choices in International Arbitration (2010) at 3, 25. (White & Case reports that corporations have the following expectations of the arbitrators "Open-mindedness and fairness, prior experience of arbitration, quality of awards, availability, knowledge of the applicable law and reputation", in addition, "Respondents are also not strongly influenced by the arbitrator's disposition towards the issues in dispute, their organisation or their external counsel").
[1387] Henri Alvarez & Mark Friedman, "What Should Parties Expect from Arbitrators and What Should Arbitrators Expect from Parties?" (2009) 24:1 ICSID Rev 39. Douglas McLaren, "Party-Appointed vs. List Appointed Arbitrators: A Comparison" in Christopher Drahozal & Richard Naimark, *Towards a Science of International Arbitration: Collected Empirical Research* (The Hague: Kluwer Law International, 2005) at 162. ("Majority of of those who took the survey expect the arbitrators to be neutral (87%) but he party appointed arbitrator has to "see that it [the appointing party position] is property understood and fully considered by the Chair […] the party-appointed mechanism ensures that a party knows that at least one arbitrator truly understands the issues [from their point of view]").
[1388] Van Den Berg (2012), at 57.
[1389] ICC Arbitration Rules at art. 22 (5) ("In all cases, the arbitral tribunal shall act fairly and impartially and ensure that each party has a reasonable opportunity to present its case").
[1390] New York Convention at Art. V (b, e). Philip Chong & Blake Primrose, "Summary Judgment in International Arbitrations Seated in England" (2016) 33 Arb Intl 63 at 68.

shall be treated with equality and each party shall be given a full opportunity of presenting his case".[1391] Arbitration rules also impose the same due process requirement. For example, the ICC Arbitration Rules provide, "[i]n all cases, the arbitral tribunal shall act fairly and impartially and ensure that each party has a reasonable opportunity to present its case".[1392] Accordingly, when considering an application to set aside a claim before the claimant has had an opportunity to present all of its arguments and all of its evidence, arbitrators must be very careful. Karton explains the situation as follows: "there are significant legal consequences when arbitrators make poor jurisdictional or procedural decisions, but few legal consequences when they make poor decisions on the merits".[1393] One arbitrator interviewed by Karton repeated the phrase "you have to be extraordinarily cautious" fourteen times in a one-hour interview, each time with regard to procedural matters.[1394] The International Arbitration Survey (2015) confirms that issues of procedure—fairness and efficiency—preoccupy arbitrators.[1395] This level of caution with regards to procedural matters is not surprising, given that arbitrators are often under a positive obligation to ensure that "no jurisdictional or procedural choice they make will affect the enforceability of the award".[1396] If a procedural choice made by an arbitrator renders an award unenforceable, it may result in a serious blow to the arbitrators'

[1391] UNCITRAL Model Law at art.18.
[1392] ICC Arbitration Rules at art.22(4).
[1393] Joshua Karton, "Arbitral Role in Contractual Interpretation" (2015) Journal of International Dispute Settlement 1 at 19.
[1394] *Ibid* at 20.
[1395] White & Case, "International Arbitration Survey: Improvements and Innovations in International Arbitration" (2015), at 10.
[1396] *Ibid* at 19. ICSID Convention at art. 52 (1). Loukas Mistelis, Stefan Michael Kröll & Stefan Kröll, *Comparative International Commercial Arbitration* (The Hague: Kluwer Law International, 2003) at 280. (Enforceability may be less of the concern if the tribunal presented each party with a reasonable opportunity to present its case).

reputation, jeopardizing future appointments, or even influence intra-panel interactions, an issue in detail discussed in the following Section.

To sum up, under a party-driven appointment procedure, the arbitrators respond to the expectations of the parties. The parties expect that the tribunal will effectively resolve the dispute by issuing an enforceable award. If the award is annulled or is otherwise not enforceable, such an outcome could in theory impact the arbitrators' future appointments. This pressure to ensure enforceability makes arbitrators particularly careful with regard to procedural or jurisdictional choices, more so than with substantive decisions. Arbitrators may be more willing to give the parties a chance to air their claims in full, even if the arbitrators believe those claims to be frivolous, in order to ensure that both parties receive what they expect from the arbitration, and also to avoid the "black mark" that an unenforceable award would represent. This phenomenon has been observed in a variety of circumstances throughout the arbitral process, and has come to be called "due process paranoia". Gerbay and Al Raisi describe due process paranoia as:

> the perceived reluctance by arbitral tribunals to act decisively (for example by rejecting applications for extensions of time, refusing amendments to submissions, rejecting new evidence or declining to reschedule a hearing) for fear of the award being challenged on the basis of a party not having had the chance to present its case fully.[1397]

Overall, due process paranoia presents a tension in the mind of an arbitrator whether to sacrifice expediency when managing the proceedings. Berger and Jensen explain that the arbitrators act primarily as case managers, and often tend to decide so as to ensure that "their awards will not be set aside or denied enforcement—an unwelcome

[1397] Remy Gerbay & Badar Al Raisi, "Due Process Paranoia (Part 2): Assessing the Enforcement Risk under the English Arbitration Act" (20 February 2017) Kluwer Arbitration (blog). Reed (2017), at 361. (on due process concerns generally).

smudge on their track-record".[1398] Berger and Jensen conclude that arbitrators often overestimate the threat of annulment or non-enforcement of awards.[1399] Gerbay and Al Raisi report that the English courts "refused to enforce a New York Convention award in 6 instances, and adjourned the enforcement of awards in 7 instances [...] none of the instances […] arose out of a complaint that an arbitral tribunal had made an overly robust case management decision".[1400] They accordingly advised arbitrators to "proceed robustly".[1401]

By taking a cautious approach, arbitrators can arguably benefit personally over the long term. If arbitrators grant parties a chance to present their arguments fully, the parties can perceive these arbitrators as fair adjudciators who guarantee a fair procedure. The same arbitrators will be appointed repeatedly on the basis of this perception.

Such a potentially excessive caution in dismissing frivolous claims and abuse of process claims will systematically benefit claimants, and in particular will empower abusive or frivolous claimants because it will allow them to inflict greater costs on respondent states by launching meritless claims and appointing arbitrators likely to permit such claims to proceed to a full decision on the merits. By increasing the costs, they can impose on respondents, claimants can secure more profitable settlements or policy concessions in exchange for withdrawing their claims.

5.1.4 Social Dynamics: Peer-Pressure and Insider/Outsider Status

[1398] Klaus Peter Berger & Ole Jensen, "Due Process Paranoia and the Procedural Judgment Rule: A Safe Harbour for Procedural Management Decisions by International Arbitrators" (2016) 3:1 Arb Intl 415.
[1399] *Ibid*.
[1400] Gerbay & Raisi (2017).
[1401] *Ibid*.

Moshe Hirsch insights on the dynamics of social relations between arbitrators is helpful to frame how arbitrators interact.[1402] First, Hirsch conceptualizes the "investment arbitration community", which includes "lawyers, arbitrators, scholars, and other experts specializing in investment arbitration" as a social group.[1403] This step is important because it expands our understanding of arbitrators from strictly as legal professionals to individuals or "community members" who are "concerned about the opinions and respect of their colleagues, and peer pressure exerted by other members" that "operates to enforce the group's norms".[1404]

Second, Hirsch emphasizes that arbitrators as members of the social group experience a distinctive "socialization process" by the field, become a part of unique "collective narratives" that determine how the arbitrators see their role in deciding the disputes.[1405] For example, as Hirsch explains, most arbitrators are from developed states, they share a background in private law practice, and are "inclined to emphasize the importance of unimpeded flow of capital […] and market economy ideology".[1406] This section examines three aspects of "social dynamics" in the community of international arbitrators, (1) "insider status" in the arbitration community, (2) the role of intra-panel interactions and prestige in reinforcing insider status, and (3) lack of peer pressure to dismiss the claims early in the process.

First, the community of arbitrators is a "small club", into which outsiders may be difficult to find a point of "entry". The difficulty of entering the field may be exacerbated by the fact that majority of appointments are made by co-arbitrators who select chairs, by

[1402] Moshe Hirsch, *An Invitation to Sociology of International Law* (Cambridge: Cambridge University Press, 2015) at 110.
[1403] *Ibid*.
[1404] *Ibid*.
[1405] *Ibid* at 111-112.
[1406] *Ibid* at 109,110, 111-112.

the arbitration institutions whose governing bodies are often comprised of senior arbitration practitioners, or by the law firms (whose senior partners themselves may be arbitrators) that advise parties whom to appoint.[1407] In a way, "the arbitrators" keep the control over the "entry" into the system. The party-driven appointment system is thus linked to the social dynamics and contributes to reinforcing these social dynamics.

In principle, belonging to a social group is not in itself problematic; however, it may reinforce "insider"/ "outsider" dynamics within the given community. Accordingly, insiders may fear being "cast out", just as much as outsiders desire to join the inner circle. Hacking submits that "[a]ny grouping of professionals which becomes exclusive will tend to operate (intentionally and unintentionally) against the arrival of new persons into their ranks – in the case of arbitration against the arrival into the ranks of new arbitrators hopefully with new ideas and fresh approaches".[1408] Ginsburg makes an ideologically similar point: "[t]hose inside the relatively closed world of international arbitration can use claims of an "arbitration culture" to highlight their own expertise".[1409]

In particular, an arbitrator has to maintain "insider" status within the tightly networked international arbitration community because such status is essential to reappointment (recall that most appointments are made in one way or another by the co-arbitrators, senior practitioners in the field, or by the recommendations of the law firms representing parties).[1410] To maintain that status, the arbitrator has to reinforce the dominant paradigm in the field, which is currently "the commercial arbitration

[1407] Paulsson (2013), at 171-173.
[1408] David Hacking, "Ethics, Elitism, Eligibility: A Response" (1998) 15:4 Int Arb 73 at 75.
[1409] Tom Ginsburg, "The Culture of Arbitration" (2003) 36 Vanderbilt Journal of Transnational Law 1335 at 1344.
[1410] Arthur Rovine, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers 2014* (The Hague: Brill, 2015) at 450. Borzu Sabahi et al, eds, *Revolution in the International Rule of Law: Essays in Honor of Don Wallace* (New York: Juris Publishing, 2014) at 322.

paradigm".[1411] Conceptually, the commercial arbitration paradigm means that tribunals adopt the "*inter partes* model (which is prevalent in commercial arbitration) and grant precedence to their role as settlers of disputes between the particular parties".[1412] As Hirsch explains, such a restrictive perception of their role means that "most investment arbitrators are inclined to focus on the particular facts of the dispute" rather on the systemic implications of their decisions.[1413] This paradigm thus "shapes the inclinations of arbitrators" when they make "normative choices" as well as procedural choices.[1414] Prospective arbitrators who are "outside the culture" are less desirable.[1415] Puig and Stezhnev observe that,

> to remain a part of a professional community, arbitrators rely heavily on individual reputation and social capital. Once members of the profession develop a reputation, this information is passed on by other members of the profession and often translates into other nominations precisely because of such leanings.[1416]

Arbitrators are thus motivated by the structure of arbitral appointments and the field's social dynamics to make procedural choices that will maintain their "insider" status, reinforce their ability to influence others on the tribunal, and increase their prestige in the field.[1417] Arguably, by preventing the parties to present their case fully and dismissing the claim outright, or by constantly appealing to the broader systemic context or policy implications of their decisions (given that ad hoc tribunals have "a case specific mandate"), the arbitrators risk to inhibit due process that in its turn can undermine

[1411] Hirsch (2015), at 112-113.
[1412] *Ibid*. *Glamis Gold* at para.3,7. Hirsch presumambly means that the arbitrators focus on resolving a particular dispute between the two parties without looking beyond the scope determined by the parties.
[1413] *Ibid*.
[1414] *Ibid*.
[1415] Ginsburg (2003), at 1344
[1416] Puig & Strezhnev (2017), at 393.
[1417] *Ibid*.

enforceability of an award on procedural grounds. Such arbitrators seem to unlikely gain or maintain "insider" status that can be significant to secure future appointments.

Second, the issues of intra-panel interactions and prestige are worth examining separately as factors that can contribute to building an individual's insider/outsider status. Todd Tucker presents perhaps the most thorough exploration of intra-panel relations.[1418] He finds that party-appointed arbitrators display different types of behaviour in the investment proceedings:[1419] some are openly partisan; others operate indirectly in advocating outcomes that are in the interest of their appointers; still others are scrupulously neutral between the parties.[1420] Tucker concludes, "while partisanship goes against the supposed need for neutrality in arbitration, my interviewees admitted that it is a rational approach to take, as you are guaranteed a steady stream of appointments (so long as you are at least somewhat effective at influencing your peers)".[1421] Most importantly, "[t]he centre of 'tilt gravity' on the typical tribunal is thus closer to the investor interest from the outset. Moreover, state-friendly dictators are unlikely to survive in such a system, as they would be blocked by investor-side law firms and appointees".[1422] According to Tucker, "while states have incentives to make more moderate wingman appointments (to maximize influence with the other two, who are appointed totally or partially by the investors), investors do not. Indeed, investors are well served to pick vigorous partisans who have been known to vote or dissent in favour of investors".[1423] In the context of frivolous and abuse of process claims, the arbitrators'

[1418] Tucker (2016), at 183.
[1419] *Ibid*.
[1420] *Ibid*.
[1421] *Ibid*.
[1422] *Ibid*.
[1423] Tucker (2016), at 183. Tucker's observations are corroborated by the survey conducted by Queen's Mary's survey shows that foreign investors particularly value "the likelihood the arbitrator will be able to

choices may be sociologically limited dismissing claims only in extreme circumstances. Otherwise, arbitrators may be labelled "pro-state", limiting their prospects for reappointment.

Prestige may also be an influential factor in the social dynamics. Wilske and Raible explain that "traditionally, the profession of international arbitrator seems to be associated with prestige, exclusivity, and autonomy".[1424] Of course, the desire for prestige cannot be overlooked as an incentive that impacts arbitrators' behaviour. It is worth considering the possibility that arbitrators may view each claim they consider as an opportunity to enhance their prestige in the arbitration community and among arbitrants. The more the proceedings continue, especially to the issuance of an award on the merits, the more opportunities arbitrators have to increase their prestige.

Third, arbitrators in the investment regime are not subject to peer pressure to dismiss the claims early. Bronsteen suggests that the role of peer pressure should not be underestimated in the context of the early dismissal of claims.[1425] He argues that in the context of domestic legal systems, social pressure is placed on judges to dismiss claims early,[1426] and not to permit too many cases to proceed to trial.[1427] When a judge does not dismiss enough claims early, "more and more cases pile up on the judge's docket […] while these cases are piling up, other cases must be diverted by the judicial system's administrative staff to other judges whose dockets are less crowded, thereby imposing

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influence the Chair of the tribunal (which scored 47%)".[1423] Accordingly, investors will choose an arbitrator that will be able to influence his/her peers in the panel in the investor's favour. White & Case, "International Arbitration Survey: Choices in International Arbitration (2010) at 26.

[1424] Stephan Wilske & Martin Raible, "The Arbitrator as Guardian of International Public Policy? Should Arbitrators Go Beyond Solving Legal Issues?" in Catherine Rogers & Roger Alford, eds, *The Future of Investment Arbitration* (Oxford: Oxford University Press, 2009) at 257.

[1425] John Bronsteen, "Against Summary Judgement" (2006) 75 Geo Wash L Rev 522 at 540.

[1426] *Ibid*.

[1427] *Ibid* at 541.

work on those other judges".[1428] As a result, such intra-group social pressure can potentially "reduce backlogs" and "generate more vigorous management" of cases.[1429] Such peer pressure, of course, emerges because of the scarcity of judicial resources i.e. there are only so many judges that can resolve only so many cases in a given time, all of them paid from the public coffers. This is not the case in investment arbitration, where the arbitrators are paid by the parties and thus do not face such pressure; in their turn, the parties (especially claimants) value the opportunity to present their case fully (and do not hesitate to produce multiple submissions, expert reports, and the like to support their positions).

5.2 Concluding Remarks

This Chapter examined the structural features of the international investment regime and the incentives those structures create for arbitrators. The primary goal of this Chapter was to show that these structures and incentives will encourage arbitrators to follow overly cautious approach to the early dismissal of frivolous and abuse of process claims. First, arbitrators operate within a system with a high inherent level of legal uncertainty. To dismiss a claim as frivolous, a tribunal must have absolute certainty that the claim cannot succeed on the merits; to the extent that the law itself is uncertain, the necessary certainty may be out of reach.

In the international investment regime, in the vast majority of the cases (especially early in the proceedings) the necessary certainty is impossible to achieve, since the substantive obligations in IIAs are broadly worded, tribunals can interpret those obligations differently, there is no single standard of review, and the investment regime

[1428] *Ibid*
[1429] *Ibid*.

lacks the mechanisms to promote legal certainty such as hierarchy of courts or formal precedent. In short, adjudicators need to know the law with a fair degree of certainty to evaluate a claim early in the process and determine if the claim is frivolous or abusive. In the context of the investment regime, this seems to be problematic given persisting legal uncertainty that stems from the structural design of the investment regime: *ad hoc* tribunals that adjudicate disputes by applying ambiguously-formulated investment standards with few constraints on their discretion. Second, the party-driven appointment system and the structure of arbitral compensation may embed incentives for the arbitrators not to dismiss claims early. Instead, arbitrators may be more inclined to give the parties a chance to air their claims in full, particularly when the arbitrators get their remuneration per hour or per day, and are therefore interested in prolongation of the dispute.

Third, the reluctance of the tribunals to dismiss claims as abuse of process is easily comprehensible in the context of the regime's incentives and structures. The party-driven appointment system encourages the arbitrators to be overly concerned about their reputations and perpetuates incentives to be conservative on issues of procedure in order to ensure due process for the parties. This trend can be seen in at least two specific phenomena: first, arbitrators are concerned about their personal record and social capital (as it reinforces their ability to be reappointed by the parties); accordingly, they may want to avoid developing a reputation for dismissing claims as frivolous or abuse of process without giving parties a chance to present their case. Second, arbitrators have a responsibility to ensure due process for the parties on all aspects of procedure. If they fail to do so, the award can be set aside or refused enforcement, a significant reputational

blow. When ruling on the merits, however, arbitrators have no such concern given the absence of true appellate review in the international investment regime. For this reason as well, they have an incentive to permit claims to proceed to the merits without any early dismissal. In addition, the *ad hoc* nature of ISA as a method of dispute resolution can make it difficult for arbitrators to foresee the systemic implications of their decisions, or appreciate the purpose of the investment regime as a whole. Even if the arbitrators fully understand and appreciate the big picture, many arbitrators see it as their role not to take that big picture into account, and instead to "remain faithful to the parties' contract, not to create public policy".[1430] These factors can explain why arbitrators frequently permit claimants to cure an abuse of process, may be hesitant to characterize a claim as an abuse of process, or may apply the doctrine narrowly, limiting it to certain instances of corporate restructuring.

This Chapter did not argue that all arbitrators are biased, nor did it claim that bias is the source of tribunals' apparent reluctance to dismiss investors' claims as frivolous or abuse of process. Instead, this Chapter situated the procedural mechanisms for early dismissal of claims within the systemic context of the investment regime to explain why arbitrators are so careful in identifying and dismissing the claims as frivolous and abuse of process, what "pulls" and "pushes" may affect their decisions on these issues, and why the delegation of the authority to identify frivolous and abuse of process claims to arbitrators, a procedure adopted from domestic legal systems, may be not the best solution for ISA.

[1430] William Park, "Arbitration in Autumn" (2011) 2 Journal of International Dispute Settlement 287 at 297. Joshua Karton, *The Culture of International Arbitration and the Evolution of Contract Law* (Oxford: Oxford University Press, 2013) at 79-86.

Chapter 6

What Are the Alternative Options for Screening Out Frivolous and Abuse of Process Claims?

Previous chapters have demonstrated that states view frivolous and abuse of process claims in ISA as a problem that requires a legal solution. The text of IIAs and the practice of arbitral tribunals show that states and tribunals employ a variety of procedural mechanisms to limit frivolous and abuse of process claims in ISA. In particular, in recently-negotiated IIAs, states have incorporated provisions on the early dismissal of frivolous claims; they may also raise objections in the proceedings that investors' claims constitute an abuse of process.

As has been discussed in Chapter Four, such approach to handling frivolous and abuse of process claims seems to be borrowed from the mechanisms developed in some domestic jurisdictions. The investment regime is, however, radically different from domestic legal systems. The literature on legal transplants teaches us an important lesson, which is the necessity of appreciating the political, sociological, and institutional context of the donor and recipient legal systems when conducting legal reforms.[1431] The procedural solutions currently available within the investment regime are inadequate because the system within which they operate structurally embeds legal uncertainty, encourages personal and financial incentives of arbitrators to seek reappointments, and

[1431] Langer (2004), at 5. Jaap Haage, "Comparative Law as Method and Methods of Comparative Law" in Maurice Adams & Dirk Heirbaut, eds, *The Method and Culture of Comparative Law: Essays in Honour of Mark Van Hoecke* (Bloomsbury Publishing, 2014) at 59-60. Mathias Siems, "The Curious Case of Overfitting Legal Transplants" in Maurice Adams & Dirk Heirbaut, eds, *The Method and Culture of Comparative Law: Essays in Honour of Mark Van Hoecke* (Bloomsbury Publishing,2014) at 152

facilitates rather narrow interpretations of the procedural requirements to dismiss claims. Notably, these characteristics of the investment regime are not "flaws" per se, but rather must be perceived as "features" of the system that treaty-drafters and policy-makers should take into account when they advance any substantial legal reform in the investment regime.

With this perspective in view, this Chapter considers possible mechanisms for restricting frivolous and abuse of process claims. After reviewing various mechanisms that have already been proposed or adopted, it advocates for adoption of a new pre-screening mechanism for frivolous and abuse of process claims. Specifically, it proposes a mandatory evaluative conciliation that precedes the arbitration, within which an independent conciliator will seek to facilitate a negotiated settlement between the investor and state and, failing such a settlement, will provide an assessment of the investors' claims before it can proceed to arbitration.

In contrast to arbitration, the advantage of conciliation is that it offers "an attempt to resolve the looming conflict in a cooperative way" and provides the parties with "an accurate and objective assessment of the litigious situation, thus paving the way for an agreed solution of the conflict concerned".[1432] The conciliators can be appointed by the host state and the home state of the foreign investor, but the investor will have the ability to veto nominees. This feature ensures that investors still have a "say" in the process without tilting the balance of power too far into private hands. The conciliation process and its rationale will be examined further in this Chapter.

[1432] Christian Tomuschat, Riccardo Mazzeschi & Daniel Thurer, "Introduction" in Tomuschat, Riccardo Pisillo Mazzeschi & Daniel Thürer,eds, *Conciliation in International Law: The OSCE Court of Conciliation and Arbitration* (The Hague: Brill, 2016) at 3.

The conception behind the pre-screening conciliation mechanism is envisaged in this chapter as a system of control that helps states to manage access to ISA. In Reisman's seminal 1992 book, *Systems of Control in International Adjudication and Arbitration: Breakdown and Repair*, he observed that "arbitration is a delegated and restricted power to make certain types of decisions in certain prescribed ways".[1433] According to Reisman, "any restricted delegation of power must have some system of control", which he defines as "techniques or mechanisms in engineering artefacts, whether physical or social, whose function is to ensure that an artefact works the way it was designed to work".[1434]

Preliminary mechanisms of control can co-exist and co-function with other control mechanisms, such as (in the investment context) an appellate body or a cost-shifting rule that penalizes parties for bringing meritless claims. The proposed pre-screening mechanism may be a part of a multi-prong solution that can be combined with other reforms. Ultimately, only states – as the authors of IIAs – can decide what control mechanisms should be implemented; with respect to what categories of investments, and under what conditions. This Chapter examines the advantages and disadvantages of various mechanisms to address the problem of frivolous and abuse of process claims, and elaborates on the possible procedure and benefits of evaluative conciliation as means of pre-screening investors' claims.

6.1 Structural Changes in the Investment Regime

In recent years, most of the push for structural changes to the investment regime has come from the EU. Most recently, at a 2018 UNCITRAL working group meeting, the

[1433] Reisman (1992), at 1.
[1434] *Ibid*.

EU presented various potential benefits of a multilateral investment court.[1435] It continues to advance institutional reform in its IIAs, for example the quasi investment court introduced in CETA.[1436] The EU proposal seeks to respond to the legitimacy deficits of the investment regime by introducing a system of appeals to ensure consistency of arbitral jurisprudence, and by changing the arbitral appointment and compensation process.[1437]

Most notably, IIAs that include institutional changes are not yet in force.[1438] Consultations on a multilateral investment court are still ongoing".[1439] Accordingly, our discussion will be limited to the aspects of the project and treaties available to the public. First, this section examines institutional changes and discusses how they may potentially impact the dismissal of frivolous and abuse of process claims. Next, it makes a number of remarks on the practical attainability of such institutional reforms.

The European Commission suggest that the multilateral investment court project will "address all the main issues which beset the current system judges in such a court will enjoy some form of job tenure",[1440] which will free them "of any conflicts of interest or interest in the outcome of cases".[1441] The Commission hopes that appointing the judges will not only reduce bias but also contribute to the consistency of legal interpretations and

[1435] UN GA, Possible Reform of Investor-State Dispute Settlement (ISDS): Submission from the European Union (UNCTAD, 2018), A/CN.9/WG.III/WP.145 at para.7-11. [EU Submission, UNCITRAL]
[1436] Chapter 3, section 3.2.
[1437] EU Submission, UNCITRAL at para.5-6, 20. Andrea Bjorklund, "The Legitimacy of the International Centre for Settlement of Investment Disputes" in Harlan Grant Cohen, et al, eds, *Legitimacy and International Courts* (Cambridge: Cambridge University Press, 2018) at 242. (there are multiple proposals for such court in the scholarship). Surya Subedi, *International Investment Law: Reconciling Policy and Principle* (Bloomsbury Publishing, 2012). Van Harten (2008), at 180-181. Asif Qureshi, "An Appellate System in International Investment Arbitration?" in Muchlinski, et al, eds, *The Oxford Handbook of International Investment Law* (Oxford University Press, 2008) at 1165-1167.
[1438] Schill (2015), at 146.
[1439] European Commission, *A Multilateral Investment Court*, online:< http://trade.ec.europa.eu/doclib/docs/2017/september/tradoc_156042.pdf>.
[1440] *Ibid*.
[1441] *Ibid*.

outcomes.[1442] With or without the multilateral investment court, the Commission also advocates creation of an appellate body, to which each party is permitted to appeal a decision if it disagrees with the outcome of the first instance proceeding.[1443]

Both CETA's dedicated quasi-court and the proposal for a multilateral investment court eliminate the party-driven appointment system, create the possibility of random assignment of adjudicators to disputes, and introduce the kinds of employment safeguards that apply to judicial officers in domestic legal systems.[1444] As Chapter Three explained, CETA creates quasi-tenure by putting the arbitrators on retainer and requires appointment for a period of five years.[1445] The multilateral court proposal prescribes "permanent" appointments for judges.[1446] While the details are unclear, presumably judges will be appointed for a longer period of time and will have significant job protections during their terms.[1447]

For our purposes, such systemic changes are meaningful because they fundamentally shift the incentives and structures currently existing in the investment regime. First, the appeal mechanism is professed to create greater legal certainty by promoting consistency of legal interpretations and outcomes.[1448] When the adjudicators know the law with greater certainty, it may be easier for them to evaluate the merits of

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[1442] *Ibid*.
[1443] *Ibid*.
[1444] Christina Eckes, "International Rulings and the EU Legal Order: Autonomy as Legitimacy" in Marise Cremona, Anne Thies & Ramses Wessel, eds, *The European Union and International Dispute Settlement* (London: Bloomsbury Publishing, 2017) at 162.
[1445] *Ibid*.
[1446] Steffen Hindelang &Marcus Krajewski, "Conclusion and Outlook: Whither International Investment Law" in Steffen Hindelang & Markus Krajewski, eds, *Shifting Paradigms in International Investment Law: More Balanced, Less Isolated, Increasingly Diversified* (Oxford: Oxford University Press, 2016) at 388.
[1447] *Ibid*.
[1448] Barton Legume, "Options to Establish an Appellate Mechanism for Investment Disputes" in Karl Sauvant, *Appeals Mechanism in International Investment Disputes* (Oxford: Oxford University Press, 2008) at 231. Legume pinpoints that some US treaties include the so-called "socket" provisions i.e. the treaties recognize "the possibility to an appellate mechanism being established" [at 232].

the claims at the early stages and to conclude that claims lack all merit in a larger number of cases. In CETA, TTIP, and the *Vietnam-EU BIT*, we can find two provisions on the early dismissal of frivolous claims, pertaining to claims that manifestly lack legal merit and claims in which an award in favour of claimant cannot be made. By incorporating both provisions into the texts of their treaties, the state parties demonstrate their intention to expand the range of claims that can be dismissed as frivolous.

The EU's institutional reform proposals also change the structure of compensation and appointment of the adjudicators. As Chapter Five has shown, these changes would introduce safeguards akin to those that exist within the domestic legal systems. When adjudicators are not paid by hour or day (as usually occurs under the current system), they receive no direct gain from prolongation of the proceedings.[1449] Under CETA, the arbitrators receive remuneration in form of a retainer but still are paid by the parties while they preside over a particular dispute. Under the proposed multilateral court, judges will receive tenure and a regular salary, and thus will have no financial interest in the length of the proceedings. As Van Harten explains, CETA and other treaties with a CETA-like model of ISA "address the problem of frivolous ISDS claims by giving arbitrators the power to decide whether a case, in which they stand to earn significant income, should proceed. This creates an obvious conflict of interest; frivolous claims should be vetted by an actor who does not have a financial stake in the outcome of the decision to vet."[1450]

In addition, the long-term nature of appointments to these courts (as opposed to the current *ad hoc* appointment system) makes the adjudicators less concerned about

[1449] Van Harten (2010), at 446-447.
[1450] Gus Van Harten, "Reforming the System of International Investment Dispute" in C. L. Lim, ed, *Settlement Alternative Visions of the International Law on Foreign Investment* (Cambridge: Cambridge University Press, 2016) at 113.

rendering a procedural decision with the objective to seek further appointment in mind.[1451] Posner and Yoo explain that "a tribunal is independent when its members are institutionally separated from the state parties—when they have fixed terms and salary protection".[1452] Of course, such structures do not guarantee the independence of every adjudicator, especially when procedures for reappointment to a panel of judges or arbitrators create a "lever of state control".[1453] One-time appointments may be more suitable to ensure greater independence of the adjudicators.[1454]

To be sure, a judge with tenure can still be "indebted" for her "initial" nomination and appointment, or be influenced by her "post-bench prospects" in the public or private sectors.[1455] Even so, term-based judges in a permanent court are better situated than *ad hoc* arbitrators to preserve the integrity of the system or prevent the administration of justice from falling into disrepute.[1456] Judges will "hear whatever case is coming before

[1451] Karton (2013), at 55 ("arbitrators who seek repeated appointments by the same party present a particular problem. In the case of an arbitrator who considers that his only chance lies with the party which has already named him once, this might result in more or less dissimulated, but nevertheless systematic, favouritism").
[1452] Eric Posner and John Yoo, "Judicial Independence in International Tribunals" (2005) 93:1 California L Rev 1 at 7. Posner and Yoo argue that the standards of judicial independence useful in the domestic settings maybe not effective in international settings. ("because of the independence of the tribunal, states have little influence over how it resolves disputes. They cannot expect outcomes that are satisfactory to both parties, and thus they cannot expect widespread compliance. If compliance is likely to be weak, there is little point in using the Tribunal in the first place") at 72.
[1453] Tom Dannenbaum, "Regulation of the International Bench" in William Schabas & Shannon Brooke Murphy, *Research Handbook on International Courts and Tribunals* (Northampton: Edward Elgar Publishing, 2017) at 394. Ruth Mackenzie & Phillipe Sands, "International Courts and Tribunals and the Independence of the International Judge" (2003) 44 Harvard Intl L J 271 at 278, 279 (arguing that if states "put forward" judges, the most likely will appoint "as a candidate a person who shares (in general terms) the value systems of the nominating state"; the nomination and election process of judges by states can be also highly politicized, for example, ICJ, however, "once elected, international judges can only be removed by the court itself. In this respect, tenure is not subject to political interference".)
[1454] *Ibid*.
[1455] *Ibid*.
[1456] *Ibid* at 396.

them" and have an incentive to "further the rule of law", with the possibility of critical scrutiny at the appeal stage.[1457]

A restriction on double-hatting, individuals acting simultaneously or consecutively as arbitrators and advocates in different arbitrations, is imposed under the CETA model.[1458] As Langford, Behn, and Lie point out, double-hatting becomes a problem when,

> an arbitrator's ability to shape legal precedent and evaluation of facts (or access confidential information) may assist them as legal counsel elsewhere [and] an arbitrator acting as legal counsel is coloured by their arbitral role or uses his or her pleadings in one case for the purpose of being picked up and used by the same individual in their work as an arbitrator in another case.[1459]

Sands, for example, has cited own his experience in arbitral proceedings where the opposing side referred to a case "in which one of their counsel sat as arbitrator and handed down an award directly touching upon a legal issue that arose in our case".[1460] If in one case, as counsel, a legal professional argues that the claim requires a very high threshold to be dismissed as frivolous or abuse of process, and in another, similar case, the same legal professional as an arbitrator must decide whether to dismiss a claim as frivolous or abuse of process, it is difficult to imagine how such an individual can divorce

[1457] *Ibid*. John Mearsheimer, "The False Promise of International Institutions" (1995) 19 Intl Security 5 at 47 ("Many policymakers as well as academics believe that institutions hold great promise for promoting international peace. This optimistic assessment of institutions is not warranted" […] Not everyone agrees that international courts are effective. John Mearsheimer argues that international institutions (including courts) cannot achieve anything in principle as foreign relations are highly politicized.).
[1458] Anthea Roberts, "A Possible Approach to Transitional Double Hatting in Investor-State Arbitration", online:< https://www.ejiltalk.org/a-possible-approach-to-transitional-double-hatting-in-investor-state-arbitration/>.
[1459] Langford, Behn & Lie (2017).
[1460] Philippe Sands, "Conflict and Conflicts in Investment Treaty Arbitration: Ethical Standards for Counsel" in Chester Brown & Kate Miles, eds, *Evolution in Investment Treaty Law and Arbitration* (Cambridge: Cambridge University Press, 2011) at 22.

their opinion as an arbitrator on this matter from their opinion as a legal counsel; or convince the parties that they did.[1461]

Social capital in the party-driven appointment system is paramount for arbitrators because it has the greatest impact on their possibility of reappointment.[1462] What if a legal professional serves as legal counsel mostly for investors and is appointed as an arbitrator by investors?[1463] Given that the parties carefully examine the profiles of potential arbitrators, in particular their views on the legal issues involved in their dispute (and often pick them *because* of their views), for an arbitrator mostly appointed by investors, having a record of dismissing claims early would likely harm their prospects for reappointment. Even arbitrators who are appointed by both investors and states may be hesitant to dismiss frivolous or abuse of process claims because they may hope to avoid gaining a reputation as an aggressive arbitrator willing to their mandate (especially if they dismiss claims as abuse of process, an outcome that turns in large part on a finding of bad faith conduct by the claimant). As Puig points out, "arbitrators may perceive some indirect gains by agreeing or disagreeing with colleagues (i.e., an arbitrator may be simultaneously advising another party in other proceedings and therefore prefer a particular legal interpretation that benefits his client in such other proceedings)".[1464]

From a theoretical perspective, the path of institutional reform seems the most fruitful means to change the context of the investment system in such a manner as to better align the incentives on arbitrators with the objectives of the states that enact IIAs.

[1461] *Ibid* at 28-49. ("the appearance of bias rather than actual bias can implicate the case").
[1462] Puig (2014), at 400 ("The incentives for re-appointment may also affect an arbitrator's behaviour. Securing a reputation, for example, as 'conservative', 'progressive', or 'independent' (using Waibel and Wu's terminology) may trigger strategic decisions of an arbitrator either to ensure future appointments or otherwise to advance his/her prior decisions or view of the world").
[1463] *Ibid* at 404.
[1464] *Ibid*.

At this stage, it is difficult to predict whether the CETA arbitrators, or judges of the multilateral investment court (if such a court is ever created) will dismiss frivolous or abuse of process claims with greater frequency than arbitrators do now.[1465] However, based on the political system lens adopted in this thesis, the appellate structure *should* introduce greater predictability and consistency into the system and giving judges some form of tenure presumably will divorce them from the incentives that current ISA system perpetuates (for example, seeking reappointments). In principle, these systemic changes should impact the rate at which frivolous and abuse of process claims are dismissed. \

A permanent court could also provide clarity and consistency as to what claims constitute an abuse of process, and under what circumstances. For example, the court could clarify which of the following actions constitute abuse of process: a party intentionally delays the proceedings, employs guerrilla tactics to jeopardize the process, submits the claim to intimidate the respondent when the claim has no opportunity to succeed, launches a claim in parallel with informal negotiations process in order to have an upper hand in the negotiations.[1466] As Emmanuel Gaillard puts it, an adjudicator can employ abuse of process to dismiss claims "initiated for purposes ulterior to the resolution of a genuine dispute, such as for media attention or in order to harass or exert pressure; something that results in the misuse of the arbitral procedure".[1467]

However, while institutional reform may be beneficial, it is necessary to acknowledge that such reform may not be politically attainable as history of the

[1465] ICJ is a permanent court but the judges applied abuse of rights or abuse of process in very limited number of cases. This, however, does not mean that investment court will follow this path. The litigation dynamics in the investment court will be very different from ICJ because the private parties can file the claims. Private parties make arguments and use litigation differently in comparison to the states, even in international proceedings.
[1466] Robert Kolb, *The International Court of Justice* (London: Bloomsbury Publishing, 2013) at 948.
[1467] Gaillard (2017), at 20.

multilateral investment negotiations demonstrates.[1468] The current round of institutional reforms may face the stumbling blocks of its own. The first reason is purely pragmatic and relates to the costs of such a court. Over a span of years, maintenance of the international court with tenured judges may be more expensive than to participate in the *ad hoc* arbitrations.[1469] Second, the permanent court may develop a line of consistent jurisprudence in which it interprets the legal norms in a way that some states disagree with. Under the current system of *ad hoc* tribunals, some states can benefit from the prevailing uncertainty within the system because it permits greater flexibility.[1470] Other states may view such a court as a "trustee" rather than an "agent", with its judiciary as too empowered.[1471] The United States, for instance, historically opposes the creation of any new permanent international courts, and seems to prefer *ad hoc* arbitration.[1472]

6.2 Cost Shifting

Many legal systems use cost allocation in dispute resolution as a tool to create or alter litigants' incentives, including to deter claimants from bringing frivolous and abuse

[1468] St John (2018), at 250. Abs &H Shawcross, "The Proposed Convention to Protect Private Foreign Investment" (1960) 9 J Public L115. Schwarzzenberger (1969), at 147.

[1469] Kolb (2013), at 1190. ("the ICTY, for example, costs the UN hundreds of millions of dollars each year […] apart from the salaries of the regular registry staff, there are overheads: the remuneration of temporary personnel, travel and consultancy costs, overtime, and the costs of representation").

[1470] Ehud Guttel & Alon Harel, "Uncertainty Revisited: Legal Prediction and Legal Postdiction" (2008) 107 Mich L Rev 467 at 496 (discussing how past and future uncertainty differently influence conduct). Richard Craswell & John "Calfee, Deterrence and Uncertain Legal Standards" (1986) 2 J L Econ & Org 279 at 279 ("Uncertainty creates a positive chance that someone who violates the legal standard will not be punished, thus reducing incentives to comply"). Gillian Hadfield, "Weighing the Value of Vagueness: An Economic Perspective on Precision in the Law" (1994) 82 Cal L Rev 541 at 545 (arguing that " courts and legislatures should sometimes fashion vague standards rather than bright line").

[1471] Theresa Squatrito, "A Comparative Analysis of Formal Independence" in Robert Howse et al, eds, *The Legitimacy of International Trade Courts and Tribunals* (Cambridge: Cambridge University Press, 2018) at 410.

[1472] Stephan Schill, "Authority, Legitimacy, and Fragmentation in the (Envisaged) Dispute Settlement Disciplines" in Stefan Griller, Walter Obwexer & Erich Vranes, eds, *Mega-Regionals in Mega-regional Trade Agreements: CETA, TTIP, and TiSA: New Orientations for EU External Economic Relations* (Oxford: Oxford University Press, 2017) at 147.

of process claims.[1473] Costs in ISA can "take the form of fees and expenses of the institution and the arbitral tribunal ('tribunal costs' or 'arbitration costs'), and the fees and expenses of counsel, experts, and witnesses ('party costs' or 'legal fees')".[1474] This section examines the allocation of costs as an means to deter frivolous and abuse of process claims. It does not consider the broader social costs of investment disputes; just the arbitration costs and legal fees.[1475] First, this section examines the existing trends on cost allocation in ISA to demonstrate that tribunals have broad discretion on cost allocation but are not consistent in their cost-shifting practices. Second, this section shows how the ISA tribunals allocate costs in cases where the claim was frivolous or an abuse of process. Finally, it explains the limitations of this option as a solution for the problem of frivolous and abuse of process claims in the international investment regime.

6.2.1 Allocation of Costs: Overview

All arbitral rules of procedure contain rules on cost allocation. For example, article 42(1) of the UNCITRAL Rules provides that "[t]he costs of the arbitration shall in principle be borne by the unsuccessful party or parties […] the arbitral tribunal may apportion each of such costs between the parties if it determines that apportionment is reasonable, taking into account the circumstances of the case".[1476] Article 61(2) of the

[1473] Thomas Webster, "Efficiency in Investment Arbitration: Recent Decisions on Preliminary and Costs Issues" (2009) 25:4 Arb Intl 469 at 470-471.
[1474] Kateryna Bondar, "Allocation of Costs in Investor-State and Commercial Arbitration: Towards a Harmonized Approach" (2016) Arb Intl 45 at 45.
[1475] Such social costs may include the need of a host state to change its national policy to avoid ISA, the need of a state to raise taxes to afford to participate in the disputes and costs that are associated with the host state reputation because the disputes may affect the state's ratings with the credit agencies. Frank at 783. Luke Eric Peterson, "Czech Republic Hit With Massive Compensation Bill in Investment Treaty Dispute Investment Law and Policy" (21 March 2003) Weekly News Bulletin (arguing that "for an Administration already running a record budget deficit of some 360 million dollars (US), the Tribunal's decision threatens to double the Czech Republic's budget shortfall this year. As the government scrambles for solutions, one proposal mooted by some officials is for an increase in value-added tax on goods and services which would see all taxpayers absorbing the cost of the investment treaty arbitration").
[1476] UNCITRAL Arbitration Rules (2010) at 42 (1)

ICSID Convention gives the ISA tribunals almost unlimited discretion on the allocation of costs, providing:

> [i]n the case of arbitration proceedings, the Tribunal shall, except as the parties otherwise agree, assess the expenses incurred by the parties in connection with the proceedings, and shall decide how and by whom those expenses, the fees and expenses of the members of the Tribunal and the charges for the use of the facilities of the Centre shall be paid. Such decision shall form part of the award.[1477]

The ICSID Convention prescribes no default rule on cost allocation, while UNCITRAL Rules article 42(1) provides "a default rule on fees—albeit a weak one"[1478] The default rule is weak because it permits cost shifting but is worded is a way that does not require the tribunal to consider the allocation of costs. However, both UNCITRAL and ICSID grant tribunals effectively complete discretion on cost allocation.[1479] So far, ISA tribunals have followed three approaches: "loser pays", "pay your own way", and "allocation *pro rata*".[1480]

In national jurisdictions and in the investment regime, the application of each rule has its own policy rationale in creating incentives for litigation, settlement, and filing of frivolous claims.[1481] When a claimant choses whether to bring the claim and what steps to

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[1477] ICSID Convention at art. 61(2)
[1478] David Smith, "Shifting Sands: Cost-and-Fee Allocation in International Investment Arbitration" (2011) 51 Va J Intl L 749, 451.
[1479] *Ibid*.
[1480] Lucy Reed, "Allocation of Costs in International Arbitration" (2011) 26:1 ICSID Rev 76 at 78 [italic original].
[1481] Edward Snyder & James Hughes, "The English Rule for Allocating Legal Costs: Evidence Confronts Theory" (1990) 6:2 Journal of Law, Economics, & Organization 345 ("An extensive theoretical literature has analysed how the allocation of legal costs may affect the litigation process" […] We have found empirical support for one of the primary predictions of the theoretical literature on alternative methods for allocating legal costs: Fee shifting encourages parties to litigate rather than settle their claims. This change in behaviour is consistent with the view that optimistic litigants anticipate shifting their fees to their opponent, which reduces the settlement gap"). Thomas Miceli, "Dispute Resolution" in Jürgen Backhaus, ed, *The Elgar Companion to Law and Economics* (Northampton: Edward Elgar Publishing, 2005) at 396.

undertake during the proceedings (i.e. continue to arbitration or settle), it makes an "ex-ante evaluation",[1482] which encompasses predictions of the chance of prevailing, the likely size of a judgment, the costs of pursuing a claim, and the method by which costs may be allocated.[1483] Laird *et al* report that in "fewer than half of the 19 decisions in 2012 which addressed costs awarded them against a party for some portion of either the other party's cost of the arbitration or the costs of legal representation".[1484]

The "loser pays" rule requires a loser to pay the costs of the arbitration and all of the legal costs of the prevailing party.[1485] The "loser pays" rule is also known as the

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Rupert Jackson, *Review of Civil Litigation Costs* (London: The Stationery Office, 2010) at 93 ("cases under the English rule were less likely to settle than cases under the US rule").

[1482] Steven Shavell, "Suit, Settlement, and Trial: A Theoretical Analysis Under Alternative Methods for the Allocation of Legal Costs" (1982)11:1 J Leg Stud 55.

[1483] *Ibid* at 56.

[1484] Ian Laird *et al*, "International Investment Law and Arbitration: 2012 in Review" in Andrea Bjorklund, ed, *Yearbook on International Investment Law & Policy 2012-2013* (Oxford: Oxford University Press, 2014) at 189.

[1485] *Southern Pacific Properties v Egypt* (1992), Award ICSID Case No ARB/84/3 (International Centre for Settlement of Investment Disputes) (Arbitrators: Robert Pietrowski, Mohamed Amin Elabassy El Mahdi, Eduardo Jimenez De Arechaga) at para 207. ("[a]lso known as "the costs follow the event" or "English Rule". The tribunals in Southern Pacific Properties v Egypt supported this approach by declaring that "there is little doubt that the legal costs incurred in obtaining the indemnification must be considered part and parcel of the compensation, in order to make whole the party who suffered the loss and had to litigate to obtain compensation"). *International Thunderbird Gaming Corporation v Mexico* (2006), Award (United Nations Commission on International Trade Law) (Arbitrators: Agustín Portal Ariosa, Thomas Wälde, Albert Jan van den Berg) at para. 214 (adopted the loser pays principle but noted that "[i]t is indeed true that in many cases, notwithstanding the fact that the investor is not the prevailing party, the investor is not condemned to pay the costs of the government. The Tribunal fails to grasp the rationale of this view, except in the case of an investor with limited financial resources where considerations of access to justice may play a role. Barring that, it appears to the Tribunal that the same rules should apply to international investment arbitration as apply in other international arbitration proceedings"). *ADC v Hungary*. *Scimitar Exploration Limited v Bangladesh and Bangladesh Oil, Gas and Mineral Corporation* (1994), Award ICSID Case No. ARB/92/2 5 ICSID Report 4 (International Centre for Settlement of Investment Disputes) (Arbitrators: Edward C. Chiasson, Ian Brownlie, Keith Highet). *CDC Group plc v Republic of Seychelles* (2005), Decision on Annulment ICSID Case No. ARB/02/14 (International Centre for Settlement of Investment Disputes) (Annulment Committee members: Charles Brower, Michael Hwang, David Williams). *Telenor Mobile Communications AS v Republic of Hungary* (2006), Award ICSID Case No. ARB/04/15) (International Centre for Settlement of Investment Dispute) (Arbitrators: Nicholas Allard Arthur Marriott Roy Good). David Riesenberg, "Fee Shifting in Investor-State Arbitration: Doctrine and Policy Justifying Application of the English Rule" (2011) 60:4 Duke LJ 977 (arguing that the English rule should be controlling in ISA).

English Rule.[1486] It has both benefits and disadvantages. Glenn explains that "[s]ome maintain that a further justification for the rule would be its deterrent effect on litigation, in the form of the down-side risk of having to cover costs of the other side in addition to one's own costs".[1487] Hughes and Snyder, studying litigation within England, find "(i) a significantly higher percentage of dropped claims under the English rule and (ii) a net increase the relative frequency of settlements versus litigated cases".[1488] They conclude that the English rule effectively "censors" claims that have little legal merit.[1489] However, the English rule makes it more difficult for the claimants with "innovative claims" to reach the appellate courts, and thus, generate new precedents.[1490] Accordingly, the English rule may hinder development of the law.

In the ISA context, Schill rationalizes the "loser pays" rule as follows: "[t]he higher the (potential) liability for costs, the higher the risk of arbitration, the lower the incentive to bring claims, in particular if the outcome is difficult to predict in view of the vagueness of many investors' rights and the relative novelty of investor-state dispute settlement".[1491] Given that in the investment regime, the level of legal uncertainty is high (in part because of the ambiguity of the investment standards and in part due to the decentralized nature of dispute settlement), the application of the English rule can

[1486] Patrick Glenn, "The Irrelevance of Costs Rules to Litigation Rates: The Experience of Quebec and Common Law Canada" in Mathias Reimann, ed, *Cost and Fee Allocation in Civil Procedure. Ius Gentium: Comparative Perspectives on Law and Justice* (London: Springer, 2011) ("the "loser pays" rule was received in Canada through reception of French and English law and rests on the traditional justification, that a successful party should not have to bear the cost of establishing their right against an unjust claim or defense") at 100.
[1487] *Ibid*.
[1488] James Hughes & Edward Snyder, "Litigation and Settlement under the English and American Rules: Theory and Evidence" (1995) 38:1 J L & Econ 225 at 225.
[1489] *Ibid* at 248.
[1490] *Ibid* at 249.
[1491] Stephan Schill, "Arbitration Risk and Effective Compliance: Cost Shifting in Investment Treaty Arbitration" (2006) 7 J World Invest & Trade 653, 654 (explaining "the decision to arbitrate will depend on a cost-benefit analysis' and '[a]n important aspect of this cost-benefit analysis is the allocation of the costs of arbitration, both the costs of the proceedings... and the costs of legal representation").

discourage investors from bringing even valid claims against governments. For Franck, the application of the English rule is therefore "less desirable" because it generates more uncertainty than it resolves:

> [g]iven the inconsistency and breadth of the case law, it may be difficult to know in advance which party will "win" and which party will "lose." This makes a "loser-pays" approach susceptible to variance and injects an avoidable (and arguably unnecessary) degree of uncertainty into ITA, which creates greater challenges in predicting costs.[1492]

The "pay your own way" approach requires each party to pay its own expenses; it is also known as the American rule.[1493] The SCOTUS articulated three reasons for maintaining the American rule in the US context. According to SCOTUS, the American rule is essential:

> (i) because legal outcomes are uncertain, requiring losing parties to pay for the winning party's fees and expenses can be viewed as unjust punishment; (ii) the poor might be deterred from bringing a meritorious cause of action if they face the risk of paying their opponents fees; and (iii) allocating costs and fees may decrease efficiency by increasing costs, prolonging cases and imposing more administrative hardship.[1494]

In contrast to the English rule, "under the American system, the plaintiff will bring suit if and only if his expected judgment would be at least as large as his legal costs".[1495] In the context of international law, the "pay your own way" principle is

[1492] Susan Frank, "Rationalizing Costs in Investment Treaty Arbitration" (2011) 88:4 Wash Un L Rev 769
[1493] The tribunals applied the American rule in a number of cases LESI v Algeria, Anderson v Costa Rica, Pantechniki v Albania, Metalpar v Argentina and Impregilo v Argentina, Alasdair Ross Anderson v Costa Rica.
[1494] Acrambel v Wiseman, 3 US 306 (1796) as decribed in John Gotanda, "Consistently Inconsistent: The Need for Predictability in Awarding Costs and Fees in Investment Treaty Arbitrations" (2013) 28:2 ICSID Rev 420 at 424.
[1495] Steven Shavell, "Suit, Settlement, and Trial: A Theoretical Analysis Under Alternative methods for the Allocation of Legal Costs" (1982)11:1 J Leg Stud 55 at 58.

broadly applied, particularly in state-to-state dispute settlement.[1496] Sabahi reports that "a survey of 158 decisions shows that in majority of the cases the parties have been ordered to bear their own costs, following the American rule".[1497] Rovine provides more recent statistics on the application of the cost allocation rules. Rovine examined eighty eight ICSID awards issued from 2006 to 2015, and found that:

> most awards provide little or no explanation for either shifting costs or requiring the parties to bear their own costs. Only 53% (forty-seven awards) of the eighty-eight awards since 1 June 2006 can be clearly placed in either the American or English camps (twenty-six awards in American Rule categories […] and twenty-one awards in English Rule categories.[1498]

Rovine's results show "the apparent ambivalence" that infuses the "debate about the appropriate rules for costs in the investment arbitration context".[1499] The dynamics of inter-state dispute settlement are different from ISA in ways that may justify blanket application of the American rule. First, the volume of disputes in ISA is significantly higher than under state-to-state dispute resolution mechanisms. Investors can make arguments different from those of states because they need not fear that they have to defend their regulatory actions in a future dispute.[1500] Dreyfuss and Frankel explain that "once a challenge is brought, states retain the power to decide which arguments to make. A state may, for example, desist from challenging another state's use of a flexibility in an

[1496] Juan José Quintana, *Litigation at the International Court of Justice: Practice and Procedure* (The Hague: Brill, 2015) at 543. (discusses that in ICJ Statute, the default rule is that each party carries on the costs unless decided by the court otherwise).
[1497] Borzu Sabahi, *Compensation and Restitution in Investor-State Arbitration: Principles and Practice* (Oxford: Oxford University Press, 2011) at 162.
[1498] Arthur Rovine, "Allocation of Costs in Recent ICSID Awards" in David Caron, et al, eds, *Practising Virtue: Inside International Arbitration* (Oxford: Oxford University Press, 2015) at 667.
[1499] *Ibid* at 668.
[1500] Rochelle Dreyfuss & Susy Frankel, "From Incentive to Commodity to Asset: How International Law is Reconceptualizing Intellectual Property" (2015) 36 Mich J Intl L 557 at 572-573.

agreement that it also wishes to use".[1501] Foreign investors can also employ various creative tactics to frustrate the process by causing delay, or conducting corporate restructuring to alter their nationality and thereby gain access to the investment protection through the investment treaties of another state.[1502] Such tactics are anti-social and should be deterred, but the "pay your own way" rule typical in state-to-state dispute settlement provides no disincentive.

Under a "pro rata" approach, the tribunal assesses costs depending on each party's conduct in the dispute and the degree of their success on the merits.[1503] In the context of ISA, the *pro rata* rule may promote uncertainty. Different tribunals may examine different aspects of the parties' conduct during the arbitration proceedings, and may weigh those aspects differently. Such uncertainty may deter even meritorious claims. Frank explains that "the lack of certainty and predictability about total costs, which party will have liability for which costs, and the justification for those cost decisions diminishes the effectiveness of investment treaty arbitration".[1504] The pro rata approach may, however, be useful because it "permits stakeholders to prioritize behaviours that they wish to encourage and to nudge efficient and desirable conduct".[1505] States can limit arbitral discretion by prescribing what types of behaviour in the arbitration process should be taken into consideration during the assessment of costs.[1506]

[1501] *Ibid* at 573.
[1502] Gaillard (2017), at 1.
[1503] *EDF v Romania* (2009), Award ICSID CASE NO. ARB/05/13 (Arbitrators: Piero Bernardini, Arthur Rovine, Yves Derains) at para.329. *Occidental v Ecuador* II (2004), Award on Costs, LCIA No. UN3467 (Arbitrators: Francisco Vicuna, Charles Brower, Patrick Sweeney) at para.12.
[1504] Susan Frank, "Rationalizing Costs in Investment Treaty Arbitration" (2011) 88:4 Wash Un L Rev 769 at 772-773.
[1505] *Ibid*.
[1506] *Ibid*.

The existing literature helps to explain which of these three approaches is adopted in which circumstances. Before proceeding with this analysis, it is worth emphasizing that ISA tribunals demonstrate "consistent inconsistency" in exercising their powers over cost allocation.[1507] According to Schreuer, tribunals' practices on costs are "neither clear nor uniform".[1508]

Tribunals take into consideration a number of factors when they choose an approach on the allocation of costs.[1509] According to Bondar, these factors include "an interplay between claim and counterclaims and the amount claimed versus the amount actually awarded", "bad behaviour of one of the parties",[1510] "complexity and arguability of certain claims and novelty of legal issues".[1511] Rubins observes that the tribunals consider the following factors when they decide on costs: (1) proportion of success (i.e. ratio between the amount claimed and amount awarded), (2) conduct during the proceedings, (3) and novelty of legal issues.[1512]

Bosh v Ukraine is helpful to untangle tribunals' decision-making process. In *Bosh*, the tribunal took into consideration delays incurred due to various procedural

[1507] John Gotanda, "Consistently Inconsistent: The Need for Predictability in Awarding Costs and Fees in Investment Treaty Arbitrations" (2013) 28:2 ICSID Rev 420. Bondar (2016), at 45.
[1508] Schreuer (2009), at para.18.
[1509] Burkhard Hess & Rudolf Huebner, "Cost and Fee Allocation in German Civil Procedure" in Mathias Reimann, ed, *Cost and Fee Allocation in Civil Procedure. Ius Gentium: Comparative Perspectives on Law and Justice* (London: Springer, 2011). Patrick Glenn, "The Irrelevance of Costs Rules to Litigation Rates: The Experience of Quebec and Common Law Canada" in Mathias Reimann, ed, *Cost and Fee Allocation in Civil Procedure. Ius Gentium: Comparative Perspectives on Law and Justice* (London: Springer, 2011) at 102. (The domestic courts are also responsible for the assessment of costs. The judges do so on the basis of multiple factors including (but not limited to) "the complexity of the case, time actually spent, hourly rates and other factors". In some domestic systems, the courts are bound by strict mandatory rules in assessing costs. For example, in Germany "the allocation of costs is based on mandatory legal provisions which exclude any discretionary fee shifting by the court. Despite some recent deregulations, the German system is based on a highly regulated framework of legal provisions which mainly provide for fixed tariffs for all major cost positions").
[1510] Bondar (2016), at 47.
[1511] *Ibid* at 53-56.
[1512] Noah Rubins, "The Allocation of Costs and Attorney's Fees in Investor-State Arbitration" (2003) 18:1 ICSID Rev 109 at 126-217.

requests by the claimant, including its insistence on scheduling the proceedings in Washington DC, "when most of the witnesses were located in Europe", and its abandonment of several claims it initially raised, all of which had to be addressed by the respondent.[1513] The tribunal observed that the claimant's case was not an "abuse of process", and that the "[c]laimants' counsel represented their clients in a professional manner at the hearings".[1514] However, it recognized that the respondent had to bear additional costs because of the delays for which the claimant was responsible. The tribunal eventually concluded that the "costs follow the event" principle cannot be applied "in a blanket way in this case".[1515] After evaluating all the factors, the tribunal ordered "the Claimants to make a contribution to these additional costs that would not have been incurred but for the actions of the Claimants" and determined that "a reasonable sum in this respect, excluding the Respondent's share of ICSID's fees, is one-sixth of the Respondent's costs."[1516] The *Bosh* case is illustrative because it demonstrates that a tribunal's assessment of costs depends on the circumstances of each particular case, and that different factors will be most influential in different cases. Delays in the proceedings (even if they are due to the fault of one party) are not necessarily tantamount to abuse of process, and do not automatically result in costs being assessed against the party that triggered the delay.

As has been mentioned, there is no clear rule on cost allocation in the investment regime, which leaves tribunals with wide discretion to exercise their powers.[1517]

[1513] *Bosh International v Ukraine* (2012), Award, ICSID Case No ARB/08/11 (International Centre for Settlement of Investment Disputes) (Arbitrators: Gavan Griffith, Philippe Sands, Donald McRae) at para.290.
[1514] *Ibid* at para.291.
[1515] *Ibid* at para.291.
[1516] *Ibid* at para. 292.
[1517] Rubins (2003), at 125.

Although tribunals appear to examine similar factors, they attribute different weight to different factors depending on the circumstances of each particular case.

6.2.2 Allocation of Costs for Frivolous and Abuse of Process Claims

This section examines how ISA tribunals have approached the allocation of costs in cases where they held the investor's claim to be frivolous or an abuse of process.

6.2.2.1 Frivolous Claims

As with the more general trends on cost allocation, tribunals do not follow a consistent approach when they rule on the costs in cases where the investors' claims are frivolous. In some earlier decisions, the tribunals applied the American rule. For example, in *Globex v Ukraine*, the tribunal ruled that the investor's claim was manifestly without legal merit yet required both parties to pay their own costs, on the principle that "the costs of the procedure lie where they fall".[1518] In *Trans-Global v Jordan*, the tribunal decided that "[t]he Claimant and Respondent will each bear their own legal costs and expenses and pay in equal shares the fees and expenses of the Tribunal and ICSID".[1519] Notably, in *Trans-Global Petroleum,* the tribunal ruled that only one of three claimant's submissions manifestly lacked legal merit, whereas other two claims could not be ruled out at a preliminary stage.

In one of the more recent arbitrations involving a frivolous claim, the tribunal did not follow the American rule. In *Ansung v China*, the tribunal confirmed that it must take into account the circumstances of each particular dispute and is not obligated to allocate the costs between the parties even if the claim manifestly lacks legal merit.[1520] After

[1518] *Global Trading Resource Corp. and Globex International v Ukraine* (2010), Award ICSID Case No. ARB/09/11 (Arbitrators: Franklin Berman, Emmanuel Gaillard, Christopher Thomas) at para.59.
[1519] *Trans-Global v Jordan*, Settlement Agreement and Release at para.5.
[1520] *Ansung* at para.162.

making this disclaimer, the tribunal decided to "assess all of the direct costs of the proceeding and 75 percent of Respondent's legal fees and expenses against Claimant".[1521] Helpfully, the tribunal laid out the factors it considered to be important to the assessment of costs when the claim manifestly lacks legal merit. It cited the fact that "Ansung is a small investor in an unfortunate position, proceeding in good faith against China", as well as "efficiency in an Arbitration Rule 41(5) objection procedure" because the "[a]rbitration Rule 41(5) objection procedure is by definition designed to promote efficiency".[1522] The tribunal concluded that it determination that "Ansung's claim manifestly lacks legal merit as time-barred necessarily means that the claim should not have been brought, and China should not bear the reasonable costs for successfully defending the claim at the Rule 41(5) stage".[1523]

In contrast to *Ansung*, the tribunal in *Accession Mezzanine Capital L.P. and Danubius Kereskedohaz Vagyonkezelo Art v Hungary* ordered the parties carry their own costs and to share equally in paying the arbitration costs.[1524] In *Accession*, Hungary raised a preliminary objection that the claim was manifestly without legal merit. The tribunal refused to dismiss the claim at the preliminary stage, and decided that it would determine the costs at a later stage. Eventually, the tribunal held that it had no jurisdiction over the dispute, so Hungary prevailed.[1525]

To justify its ruling on costs, the tribunal reasoned that its decision on jurisdiction was "by no means straightforward" and "it cannot be said that either Party was advancing

[1521] *Ibid* at para.165.
[1522] *Ibid* at para.161.
[1523] *Ibid* at para.159.
[1524] *Accession Mezzanine Capital L.P. and Danubius Kereskedohaz Vagyonkezelo Art v Hungary* (2015), Award ICSID Case No. ARB/12/3, (International Centre for Settlement of Investment Disputes) (Arbitrators: Arthur Rovine, Marc Lalonde, Zachary Douglas) at para.202.
[1525] *Ibid* at para.191.

an extreme or untenable view of these issues during the proceedings. This was a close case in the sense of reaching or not reaching the merits."[1526] In the tribunal's view, its adoption of the American rule reinforced "broader considerations of fairness and justice in exercising its power to award costs under Article 61 of the ICSID Convention".[1527] The tribunal did not explain why the application of the American rule restores "fairness and justice" but did mention that the claimant had acted reasonably in pursuing its claim, particularly in light of the claimant's success "before the Hungarian courts in obtaining a declaration that the tender process through which Advenio had procured its broadcasting agreement was unlawful, only for the Hungarian Parliament to scupper the possibility of a new tender".[1528] In the tribunal's view, "there was no possibility for the Claimants to obtain justice in Hungary and it was natural for them to look to an international tribunal".[1529] Although the tribunal did not explain why it felt the claimant had no possibility of receiving justice in Hungary, this context clearly informed the tribunal's decision on costs.

It is also useful to consider how tribunals have assessed costs under the US FTA provisions that an award in favour of claimant cannot be made. In *Pac Rim v El Salvador*, the tribunal ruled that the claim against El Salvador was not frivolous.[1530] In assessing the costs, it took into account the complexity of the case and the conduct of the parties when it decided on the allocation of costs.[1531]

The tribunal also observed that El Salvador's preliminary objection was the first occasion on which CAFTA article 10.20.4 had been invoked, and thus "there was thus

[1526] *Ibid*.
[1527] *Ibid* at para.201.
[1528] *Ibid* at para.200.
[1529] *Ibid*.
[1530] *Pac Rim Cayman,* Final Award at para.11.14.
[1531] *Ibid* at para.11.14-11.19.

much to be learnt for all involved in this arbitration".[1532] The tribunal explained that "whilst the Claimant's case prevailed over the Respondent's case under the Tribunal's Decision on Preliminary Objections, it was perhaps, as the Duke of Wellington might have put it (as he did of the Battle of Waterloo), a 'near-run thing' with consequences for this third phase on the merits".[1533] The tribunal ordered the claimant to "pay to the Respondent the total amount of US$ 8 million towards the latter's Legal Costs", an amount that covered most of the respondent's costs.[1534]

6.2.2.2 Abuse of Process Claims

This section examines cost allocation in the few cases in which tribunals held that a claim constituted an abuse of process. This section shows that ISA tribunals have in fact been consistent on the issue of the costs' allocation in these cases. When tribunals find an abuse of process, they tend to award costs against the party that committed the abuse. For example, in *Cementownia v Turkey*, the tribunal found not only that the investor's claim was unfounded, but also that its conduct was fraudulent.[1535] In *Transglobal Green Energy, LLC and Transglobal Green Panama, S.A. v Republic of Panama*, the tribunal found that the claimant attempted to create "artificial international jurisdiction over a domestic dispute […] by inserting a foreign investor into the ownership of a domestic project, at a time when the project was already embroiled in a domestic dispute".[1536] The

[1532] *Ibid* at para.11.14.
[1533] *Ibid* at para.11.17.
[1534] *Ibid* at para.11.20.
[1535] *Cementownia* at para.178.
[1536] *Transglobal Green Energy, LLC and Transglobal Green Panama, S.A. v Republic of Panama* (2016), Award ICSID Case No. ARB/13/28 (International Centre for Settlement of Investment Disputes) (Arbitrators: Andrés Rigo Sureda, Christoph Schreuer, Jan Paulsson) at para. 85. [*Transglobal v Panama*]

tribunal ordered the claimant to carry the costs of the arbitration and the respondent's reasonable legal fees and expenses.[1537]

In *Phillip Morris v Australia*, the tribunal found that the investor's claim was a manipulation of the system of investment protection. The tribunal ordered the claimant to bear "the % of the Respondent's cost claim insofar as found reasonable […] the Claimant has to reimburse the Respondent: % of the Respondent's share of the arbitration costs".[1538] The award on costs is heavily redacted so it impossible to identify what percentage of Australia's costs Phillip Morris was ordered to pay. Still, it is clear that the tribunal supported the Australia's claim for reimbursement of at least part of its reasonable legal costs and its share of the costs of the arbitration.[1539] In *ST-AD GmbH v Republic of Bulgaria*, the tribunal held that "the Claimant's initiation and pursuit of this arbitration is an abuse of the system of international investment arbitration".[1540] It ruled that "the Claimant has to bear the costs of the Respondent".[1541]

Commentary supports an award of costs against parties that commit abuses of process. For example, Rovine states that "we also have general agreement that misconduct, such as fraud or abuse of process in the initiation of a claim or in the conduct of the proceedings […] will result in an award shifting some or all of the arbitration costs […] to the properly behaving party".[1542]

[1537] *Ibid* at para.12.
[1538] *Philip Morris v Australia* (2012), Final Award Regarding Costs PCA Case No. 2012-12 (Arbitrators: Karl-Heinz Böckstiegel, Gabrielle Kaufmann-Kohler, Donald McRae) at para.105.
[1539] *Ibid* at para. 105,106,107.
[1540] *ST-AD GmbH v Republic of Bulgaria* (2013), Award on Jurisdiction PCA Case No 2011-06 (United Nations Commission on International Trade Law) (Arbitrators: Brigitte Stern Christopher Thomas, Bohuslav Klein) at para. 423.
[1541] *Ibid* at para.423.
[1542] Rovine (2015), at 666.

This review appears to show a clear contrast in the allocation of costs in claims where the tribunal dismisses the claim as an abuse of process versus a frivolous claim. It may be that the tribunals want to deter claimants from manipulating the system, for example by conducting corporate restructuring in order to bring a claim against a state as in *Philip Morris v Australia*. The tribunals, however, may be reluctant to penalize claimants by shifting costs when the claims are frivolous because they do not want to over-deter claimants from making novel arguments and testing the permissible boundaries of litigation in ISA.[1543] The situation seems different in relation to abuse of process claims that display no novel interpretation of law or creativity of legal argument, but rather are "claims initiated for purposes ulterior to the resolution of a genuine dispute".[1544]

In principle, cost shifting can be an effective option to deter frivolous and abuse of process claims; however, current trends mean that it is not in fact effective to deter at least frivolous claims. Recall that ISA tribunals tend to dismiss claims as frivolous or abuse of process only in overly narrow scenarios. In this context, cost shifting to deter frivolous or abuse process claims (even if we assume that tribunals consistently pursue it) can only be applied *after* the tribunal finds that the claim is frivolous or an abuse of process. If investors have little fear that a claim will be dismissed, heightening the consequences of that dismissal will not be an effective deterrent, just as criminological studies have shown that stricter criminal penalties do not effectively deter crime if the chance of prosecution is very small. At minimum, further research is required to identify how cost shifting strategies influence the incentives of claimants to bring the claims in

[1543] Lahav (2017), at 18.
[1544] Gaillard (2017), at 20.

ISA context. However, the analysis presented in Chapter Five indicates that an effective strategy to combat frivolous and abuse of process claims must affect the identification of such claims, not just the consequences of such an identification.

6.3 A Proposal for Evaluative Conciliation as a Pre-Screening Mechanism

Under the classical model of international conciliation proceedings, "a conciliation commission, [was] normally composed of five persons, including conciliators appointed by each party […] The commission was to examine all the aspects of the dispute: the facts, but also the law and political consideration".[1545] The outcome of the proceedings is a conciliator's confidential report.[1546] In commercial disputes between private parties, conciliation has high success rates; for example, in the USA, one study showed that 85% of disputes submitted to mediation resulted in amicable settlement.[1547] The conciliation procedures, however, are little utilized in the context of investment disputes, although major institutions that handle such disputes provide for specialized conciliation rules. This subsection proposes the establishment of a conciliation procedure as a form of pre-screening of investors' claims.

At the outset, it is worth briefly to state the reasons why such a pre-screening mechanism may be beneficial not only for states, but also for investors and the ISA system overall. First, evaluative conciliation can provide both investors and states with a "reality check"; the independently-appointed conciliator will examine the investor's claim and (if no settlement is reached) produce a report stating the conciliator's

[1545] Jean -Pierre Cot, "Expectations Attached to Conciliation Reconsidered" in Tomuschat, Riccardo Pisillo Mazzeschi & Daniel Thürer,eds, Conciliation in International Law: The OSCE Court of Conciliation and Arbitration Christian (The Hague: Brill, 2016) at 9.
[1546] *Ibid*.
[1547] Joseph McLaughlin, "Resolving and Settling Claims in the Financial Services Industry through Mediation- An International Perspective" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (2011) (The Hague: Martinus Nijhoff Publishers, 2012) at 390.

assessment of the claim's merits. Most IIAs concluded since 2011 provide for voluntary amicable settlement prior to arbitration. Attempts at reaching a settlement can take the form of negotiations, consultations, good offices, resolution of disputes through diplomatic channels, or mediation.[1548] The timeframe for this preliminary stage varies from 90 days to 6 months, depending on the treaty.

This time may as well be used to conduct an evaluation of the investor's claim by a conciliator as an independent third party. When an investor is ready to bring a claim, its relationship with the host state may have deteriorated to the extent that constructive discussions between investor and state are no longer possible. Conciliation, unlike most adjudicative models, permits the conciliator to meet separately with the parties, both investor and host state. This procedure also stands in contrast to consultations or negotiations, where the investor has to deal with the governmental officials directly. From the perspective of an investor, it may be easier to communicate through an independent third party because a conciliator will be open to the views of both parties of the dispute and will be perceived by the investor as neutral.

The second general benefit of a pre-screening mechanism is that it gives states an opportunity to understand weaknesses in their regulatory agendas in a less adversarial context than arbitration. Foreign investors can serve states with claims without any prior notice or warning. Lévesque explains that there may be instances where a government first learns of a complaint only when investors deliver a notice of intent to submit a claim

[1548] *Agreement between the Government of the Republic of Belarus and the Government of the Republic of Estonia on the Promotion and Reciprocal Protection of Investments* (2009), at art.8. *Agreement Between Canada and the Federal Republic of Senegal for the Promotion and Protection of Investments*, at art.22. *Agreement Between Japan and the Oriental Republic of Uruguay for the Liberalization, Promotion and Protection of Investment* (2015), at art. 21. *Australia-Peru* FTA (2018), at art.8.19.

to arbitration under an IIA".[1549] The reasons for this circumstance vary. The conflict could develop at "the sub-national government level", "such that the investor has no relationship with the government other than through its regulations, preliminary discussions with the government "may not have led to a resolution of the conflict", which the investor then escalates without warning. Or there may be an unscrupulous investor trying to (ab)use the IIA dispute settlement regime".[1550]

The pre-screening mechanism thus gives states an opportunity to understand the claim and establish a line of communication with the investor. It can also provide for an additional step before an investor may resort to arbitration to limit the investors' ability to coerce states to pay damages or make policy changes by threatening to impose costs through a meritless suit. For their part, governments that have limited expertise or resources in dealing with investors' claims would have an opportunity to obtain an independent evaluation of their actions prior to arbitration that would help them to make an informed decision whether it is worth proceeding to arbitration, including by helping them to understand whether their regulatory policies leave them exposed to other claims by other investors.

Third, this additional mechanism of control can contribute to building trust in ISA as a whole, which is a particularly urgent objective given that "[f]or the first time, the number of effective treaty terminations [has] outpaced the number of new IIA conclusions".[1551]

In this chapter, the pre-screening mechanism is conceived under the model of conciliation to identify frivolous and abuse of process claims prior to arbitration. This

[1549] Lévesque (2011), at 77-79.
[1550] *Ibid*.
[1551] UNCTAD, Recent Developments in International Investment Regime (2018), at 1.

subsection will lay out the proposal in greater detail. It (1) provides an overview of the proposed conciliation process, (2) explains the possible outcomes of the conciliation process, and (3) describes some aspects of the conciliation process that may be valuable in the investment regime context.

6.3.1. Possible Outcomes of Conciliation Process: Overview

Like mediation of private disputes, the proposed conciliation process can result in three possible outcomes. First, the investor withdraws its claim because during conciliation it became clear that claim has little or no opportunity to succeed on merits. If the claim is truly unmeritorious, this outcome is clearly beneficial for all parties because it saves even the investor the costs of a full-fledged arbitration. (If investors who knowingly launch unmeritorious claims in order to extract money or policy concessions are deterred from proceeding to arbitration, this is a benefit, not a fault.) Second, during conciliation, the investor and state may reach a settlement. Of course, this outcome is beneficial because it is much more cost and time efficient than a full-fledged arbitration and leads to an outcome accepted by both parties to the dispute. It may even lead to improvements in states' regulatory landscape, in cases where the regulation in dispute was genuinely discriminatory or bad policy.

Third, if the conciliation concludes without a withdrawal or agreed settlement, the investor's claim may proceed to arbitration. In such cases, it may be argued that the conciliation was a waste of time and money since an arbitration occurred despite the conciliation. This scenario may be possible if the parties intentionally frustrate the conciliation process or are simply unwilling to compromise.

However, even in cases where the dispute proceeds to arbitration, the conciliation procedure nevertheless provides tangible benefits. First, the parties may still be better off in purely financial terms after completing the conciliation. The conciliators are able to narrow down the issues in dispute, and provide an independent evaluation of the parties' positions. Jack Coe suggests that early participation of conciliator will help to "induce refinements of various kinds in the theories advanced by the parties and generally help clarify issues".[1552] According to Coe, "the result should be higher quality submissions, and better use of the tribunal's time."[1553] In short, arbitrations that follow a purportedly unsuccessful conciliation (in the sense that it did not end the dispute) are likely to be more focused and therefore faster and cheaper than arbitrations that represent the first real engagement between the parties.

Second, the opponents of conciliation seem to focus on the worst-case scenario, where one party employs "guerilla tactics" to derail the conciliatoin. Such tactics may include requesting "[e]xtension after extension, postponing a hearing because a witness or client 'somehow' accepted a conflicting engagement, jettisoning the timetable to instruct 'necessary' new or additional counsel; [s]tubbornly pursuing a virtual death march of document disclosure disputes—each document more 'critical' to presenting its case than the last".[1554] These actions can significantly delay the proceedings. The arbitrators may be unwilling to take disciplinary action because the tribunal may be put in jeopardy. As Reed puts it "[i]f the tribunal says no, the applicant's due process flag goes up"; the party can even challenge the arbitrators (what Reed calls the "nuclear

[1552] Coe (2005), at 19.
[1553] *Ibid*.
[1554] Reed (2017), at 375.

option").[1555] Of course, the use of guerrilla tactics is possible in a pre-screening conciliation. But it is possible in any dispute settlement process, including ISA. The mere fact that some parties might abuse a system does not imply that the system should be dismantled.

In some cases, the parties may be simply unwilling to compromise and may approach the process with inflexible demands. This was the experience of Schwebel, a former ICJ judge and prominent arbitrator, when he served as conciliator in a dispute between a foreign investor and an African state.[1556] The investor demanded that the state revoke a regulatory measure; the state refused to respond. The process lasted around four days and yielded no result.[1557] The parties proceeded to arbitration, although they did later reach a settlement.[1558] Schwebel observes that "[w]hy the parties were prepared to settle upon that apparently sensible solution then, but not earlier, is unclear. Perhaps the exchange of written pleadings was salutary in demonstrating to the parties that the positions of each side had their infirmities".[1559] It seems that "the exchange of written pleadings" at the arbitration stage helped the disputing parties to realize the merits of each other's submissions, yielding a settlement at a later stage in the dispute resolution process.

Third, the success of conciliation process depends on the number of factors, including how the conciliator and the parties prepare for the procedure, the personality of conciliator, his/her expertise and willingness to manage the relationship between the

[1555] *Ibid* at 157.
[1556] Schwebel (2007), at 237.
[1557] *Ibid*.
[1558] *Ibid* at 238-239.
[1559] *Ibid* at 238.

parties with the view to understand, narrow down, and assess the issues in the claim.[1560] The appointment procedure of the conciliator thus should be (1) tailored to the subject-matter of particular dispute so that the conciliator has the necessary expertise as well as an understanding of the process and (2) be conducted with the involvement of the disputing parties.

Whatever the outcome of the process, the conciliator should produce a report that includes his or her overview of the issues that were crystalized in the process assessment of the claims. The report will not be binding on a subsequent arbitral tribunal, but may be examined by the tribunal to understand the issues at stake. The conciliator should have the power to terminate the conciliation after consulting with the parties, in case the procedure reached one of the three above mentioned outcomes or has resulted in a stalemate. The conciliator should be in charge of terminating the process to avoid parties using threats to walk away as a bargaining chip.[1561]

6.3.2. Overview of the Pre-Screening Mechanism

This section describes the proposed pre-screening mechanism for the early dismissal of claims. It (1) explains the structure of the proposed conciliation process and (2) discusses some "logistics" of the process, including how the conciliators should be appointed and default rules on matters such as confidentiality and termination of the process. It is not intended to be a comprehensive justification of the proposed process, but only to show that it is plausible and explain how it might work in general.

6.3.1.1 Structure of the Pre-Screening Mechanism

[1560] Thomas Walde, "Pro-Active Mediation of International Business & Investment Disputes Involving Long-Term Contracts: From Zero-Sum Litigation to Efficient Dispute Management" (2004) 3 TDM 1.
[1561] Allan Stitt, *Mediation: A Practical Guide* (London: Cavendish Publishing, 2004) at 65.

The proposed mechanism for pre-screening of potentially frivolous and abuse of process claims combines evaluative conciliation with the approach adopted by some IIAs (such as in the ChaFTA, discussed above in Chapter Two) that set up committees for preliminary screening. First, it examines the ChaFTA approach to pre-screening of claims. Second, it explains why evaluative conciliation would be a valuable addition to these pre-screening mechanisms.

As discussed in Chapter Two, states have taken various measures in response to the legitimacy deficits of the investment regime. In ChAFTA, China and Australia agreed to set up a committee that fulfils a pre-screening function. The committee is to decide whether each claim filed by a foreign investor challenges a non-discriminatory regulatory measure of the host state. If the Committee finds that the measure is not discriminatory, it can dismiss the claim. The committee includes representatives appointed by the two governments. Presumably, the participation of the home state ensures that the interests of foreign investors are well represented. The committee fulfils the function of pre-screening investors' claims, but only on the basis of the non-discriminatory character of the challenged government measure. The problem with this pre-screening mechanism is that if the committee (i.e. the home and host states) finds that the regulatory measure is not discriminatory, the tribunal must dismiss the claim of foreign investor even if in substance it is meritorious. The mechanism seems to be a response to the vertical legitimacy concerns, including on regulatory chill. However, the note issued by the two state parties is *ex post*, meaning that states can adopt it retroactively, i.e. after they receive an investor's claim. It is also problematic because states, not independent third parties, make the decision. Even if, in a given case, the investor's home state might want

to help the investor, all states have a shared interest in safeguarding their regulatory flexibility. The ChaFTA example introduces the conceptually attractive option of pre-screening claims before an investor can access arbitration. In this context, it may be useful to consider mandatory evaluative conciliation that will evaluate whether a claim is frivolous or an abuse of process, rather than dismissing investors' claims according to an *ex post* notice issued by the two state parties.

Coe explains the value of mandatory conciliation as follows: "[m]aking attempted conciliation part of a normal routine […] each side can anticipate and more fully engage the process".[1562] Of course, conciliation/mediation is more likely to be successful when the parties voluntarily launch the process because both parties must buy in to the conciliation procedure for it to yield an acceptable settlement. Bühring-Uhle, Kirchhoff, and Scherer, however, observe that it may be difficult to "get the parties to participate".[1563] The reasons may be that "confidence of the parties to reach an agreement is lost", or "the parties fail to perceive their interest in settlement because they simply miscalculate the benefits of pursuing litigation".[1564] When the conciliation procedure is mandatory, it can become "an eye-opener" for both parties, particularly when the conciliator provides an independent assessment of the merits of the claim and assists in clarifying and narrowing the issues.[1565]

[1562] Jack Coe, "Toward a Complementary Use of Conciliation in Investor-State Disputes" (2005) 12 U Cal Davis L Rev 7 (2005) at 38. Some domestic legal systems reportedly adopted mandatory mediation prior to the formal dispute resolution process. David Spencer, "Mandatory Mediation and Neutral Evaluation: A Reality in New South Wales" (2000) 11 ADRJ 237.
[1563] Christian Bühring-Uhle, Lars Kirchhoff & Gabriele Scherer, *Arbitration and Mediation in International Business* (The Hague: Kluwer Law International, 2006) at 229.
[1564] *Ibid*.
[1565] *Ibid*.

The concept of evaluative conciliation deserves some unpacking.[1566] In short, evaluative conciliation is a procedure that permits "condensed exchange of data, arguments and evidence, and that makes it possible [...] to gain neutral evaluation of the merits".[1567] This procedure "has a great potential for bringing about mutually satisfactory solutions or at least for narrowing the issues and focusing the dispute, thus enhancing efficiency of any subsequent binding procedures".[1568] According to Riskin,

> a principal strategy of the evaluative-narrow approach is to help the parties understand the strength and weaknesses of their positions and the likely outcome of litigation […] Before the mediation starts, the evaluative-narrow mediator will study relevant documents, such as pleadings, depositions, reports, and mediation briefs. At the outset of the mediation, such a mediator typically will ask the parties to present their cases […] in a joint session. Subsequently, most mediation activities take place in private caucuses in which the mediator will gather additional information.[1569]

An evaluative conciliator employs several evaluative techniques and strategies. Specifically, they may "assess the strengths and weaknesses of each side's case, predict outcomes of court or other processes, propose position-based compromise

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[1566] John Bickerman, "Evaluative Mediator Responds" (1996) 14 Alternatives to High Cost Litig 70. Scott Hughes, "Facilitative or Evaluative Mediation: May Your Choice Be a Wise One" (1998) 59 Alabama Lawyer 246. John Collier & Vaughan Lowe, *The Settlement of Disputes in International Law: Institutions and Procedures* (Oxford University Press, 2000) at 30. Javier Yeo, "The Facilitative–Evaluative Divide: Have We Lost Sight of What's Important?" in Joel Lee and Marcus Lim, eds, Contemporary Issues in Mediation: Volume 1 (World Scientific, 2016) at 37-39. (Yeo explains that there is a divide between proponents of facilitative and evaluative mediation. The proponents of facilitative mediation ("purists") argue that evaluative mediation is "oxymoron" that "has no place in mediation". The proponents of evaluative mediation are rather "pragmatists" that support overall "facilitative" nature of mediation, however, recognize that there is an inherent evaluative element in it. The key value of the mediation as a process is that it permits mediator together with the parties to explore their interests beyond legal rights. When the mediator helps the parties to see their interests beyond legal rights, the parties can "discover" solutions to their problems as well as understand shared interests/risks, including those they may discourage them from going to litigation, or those that will encourage settlement. The two continuum distinguish facilitative and evaluative mediation: the role of mediator and the problem solving. Riskin does not say "what the mediator will focus on" merely how s/he will do it).

[1567] Bühring-Uhle, Lars Kirchhoff & Gabriele Scherer (2006), at 170.

[1568] *Ibid*.

[1569] Leonard Riskin, "Understanding Mediators' Orientations, Strategies, and Techniques: A Grid for the Perplexed" (1996) 1 Harv Negot L Rev 7 at 27.

agreements".[1570] Most importantly, once the parties have an independent third-party assessment of their respective positions, they may want to reach settlement. Coe submits that in the context of international commercial arbitration, "the settlement rate was somewhat higher when the neutral gave an evaluation of the merits".[1571] Of course, investment arbitration is structurally different from the typical commercial context where only private parties participate, yet it seems plausible to at least test whether mandatory conciliation will result in greater settlement rates.

If the conciliation does not yield a settlement, the conciliator will issue a report that provides reasons for their assessment and predicts the likely outcome of the dispute if the claim is brought to a formal adjudication forum such as ISA. In *Tesoro Petroleum Corporation v Trinidad and Tobago* (the first ICSID conciliation case), the conciliator, Lord Wilberforce, examined the investor's claims as follows:

> [he] conceive[d] that his task in these proceedings is to examine the contentions raised by the parties, to clarify the issues, and to endeavour to evaluate their respective merits and the likelihood of their being accepted, or rejected, in Arbitration or Court proceedings, in the hope that such evaluation may assist the parties in reaching an agreed settlement.[1572]

Nurick and Schnably explain that Wilberforce "analysed in detail the merits of the arguments-both factual and legal-presented by the parties, and finally concluded with a proposed settlement (involving a suggested percentage of the amount sought by Tesoro) based on "[h]is estimate of the parties' chances of success on the issue in the dispute".[1573]

[1570] *Ibid* at 28.
[1571] Coe (2005), at 18.
[1572] *Tesoro Petroleum Corporation v Trinidad and Tobago* (ICSID Case No. CONC/83/1). Lester Nurick & Stephen Schnably, "The First ICSID Conciliation: Tesoro Petroleum Corporation v. Trinidad and Tobago" (1986) 1:2 ICSID Rev at 348.
[1573] *Ibid* at 348.

The key to such a procedure is explained by Lord Wilberforce himself: "evaluation may assist the parties in reaching an agreed settlement".[1574] Thus, a conciliation procedure permits for assessment and evaluation of the merits of an investor's claims, and such evaluation can steer parties into amicable settlement or encourage an investor to withdraw legally insufficient claim.[1575] According to Schwebel, "Lord Wilberforce thereafter advanced a proposed settlement based on "his estimate of the parties' chances of success on the issue in dispute […][t]he parties then negotiated for eight months on the basis of his recommendations and reached a settlement".[1576] Schwebel concludes that the parties reached the outcome "far more expeditiously and inexpensively than they could have if they had gone to arbitration".[1577]

The ultimate value of such an evaluation is to serve as a "reality check" for the parties with the purpose facilitating settlement, encourage an investor to drop its claim, or (if the investor decides to proceed with arbitration) clarifying and narrowing the issues.[1578] Wälde explains that the "disputing parties (and their counsel, in-house and external) habitually over-estimate their chances of success" because of the "pressures of social cohesion" and the intent of "pleasing the client will lead to unrealistic

[1574] *Ibid*.
[1575] The conciliators could take into account the *jurisprudence constante* practice of the tribunals to explain the claimant why its claim might be frivolous or constitute an abuse of process. In contrast to the arbitrators that are often cautious to admit the value of the previous jurisprudence not the create precedent, the conciliators do not have such a constraint.
[1576] Stephen Schwebel, "Is Mediation of Foreign Investment Disputes Plausible?" (2007) 22:2 ICSID Review 237 at 240.
[1577] *Ibid*.
[1578] David Spencer & Michael Brogan, *Mediation Law and Practice* (Cambridge: Cambridge University Press, 2007) at 269 ("ADR may assist in the narrowing of issues between parties - is a significant one that should not be understated despite the above mentioned philosophical problems arising from mandatory court-annexed ADR. […] If settlement is not achieved or even desirable, the opportunity to reduce the issues required to be litigated must be beneficial to the parties and the justice system").

perceptions".[1579] According to Wälde, "litigation teams develop into 'bands of brothers' opposing the evil foe" where "human nature creates pressures for cognitive harmony. Corporate, social, human loyalty prevails over challenging an organization's perception of a dispute".[1580] An independent third party thus will be able to provide credible (and most importantly rational) evaluation of the claim, "understand each party's internal assessment, but also influence it – usually in terms of combating unrealistic assessment and in terms of focusing each party's attention not only on the reward, but on the probability and magnitude of the litigation risk".[1581]

6.3.1.2 Logistics of the Proposed Pre-Screening Mechanism

This section describes the main logisitical features of the proposed evaluative conciliation process. First, it describes the appointment process for conciliators, and how the process can be launched. Second, it discusses some "table-setting" details of the procedure, in particular those relating to confidentiality and disclosure.

With regards to the appointment of the conciliator, the following matters should be addressed. First, the conciliator should be appointed with due regard to his or her expertise not only in conciliation, but also in the particular subject matter of the investment dispute, knowledge of international investment law, and knowledge of international civil procedure as well as public international law.

Second, the disputing parties should participate in the selection of the conciliator. As has been discussed, the party-driven appointment system in investment arbitration has been a subject of robust criticism. Some recently negotiated treaties, such as CETA, have

[1579] Thomas Walde, "Efficient Management of Transnational Disputes: Case Study of a Successful Interconnector Dispute Resolution" (2007) 4:1 TDM 1 at 6.
[1580] *Ibid*.
[1581] *Ibid* at 11.

moved away from the *ad hoc* party-driven appointment system and instead, empower the state parties to the IIA to appoint the arbitrators. In the context of conciliation as a pre-screening mechanism, the state party appointment system would need to be modified. The conciliation procedure cannot be in principle successful unless both parties trust the conciliator. Without trust, the disputing parties may be unwilling to participate in the process, or to reveal sensitive information relevant to the merits of the dispute.

With this context in view, I propose that the state parties to the applicable IIA will appoint the conciliator, but the investor will have a right to veto any candidate proposed by the state parties, as well as the right to propose a candidate for consideration to the state parties. If the investor vetoes all candidates proposed by the state parties, and if the state parties do not accept any candidates proposed by an investor within 30 days after the initial request for conciliation, the Secretary General of the administering institution (or their designate) should make the appointment. The IIA may also specify a neutral appointing authority for concilliators.

The pre-screening mechanism should be added as a mandatory step prior to arbitration. As has been mentioned above, many IIAs include "cooling-off" provisions that mandate a period of time before an investor can bring a claim against the host state to ISA. During the cooling-off period, the parties may enter into negotiations or consultations.[1582] Mandatory conciliation during the cooling-off period would embed the

[1582] Cooling off provisions in the treaties are not always enforced by the tribunals, particularly if an investor can show that consultation/negotiations are useless given the approach taken by the host state. Antonis Bredimas, Anastasios Gourgourinis & Georges Pavlidis, "Legal Countours of Sovereign Debt Restructuring under UNCTAD Principles" in Carlos Espósito, Yuefen Li & Juan Pablo Bohoslavsky, *Sovereign Financing and International Law: The UNCTAD Principles on Responsible Sovereign Lending and Borrowing* (Oxford: Oxford University Press, 2013) at 146. ("disagreement has in fact arisen between investment tribunals regarding whether non-compliance with cooling off/waiting clauses under IIAs constitutes a jurisdictional bar or merely procedural requirement").

procedure within the framework that already exists in many IIAs.[1583] ISA tribunals will need to reinforce the mandatory nature of conciliation by refusing jurisdiction before the parties go through the mandatory pre-screening procedure; the state parties may want to specify this criterion in the applicable IIA. Such a specification is necessary to avoid uncertain or inconsistent outcomes. Under existing IIAs, "arbitral tribunals have been divided over the question whether the non-compliance with an amicable settlement requirement affects the tribunal's jurisdiction".[1584]

Accordingly, if an IIA incorporates a conciliation mechanism as proposed here, it might specify that, during this period, the investor must submit a request for conciliation. The investor's request should include "an indication of the subject of the dispute as well as relevant supporting documents".[1585] It seems feasible for the conciliator to have freedom in determining the procedure. The UNCITRAL Conciliation Rules propose exactly this: "[t]he conciliator may conduct the conciliation proceedings in such a manner as he considers appropriate, taking into account the circumstances of the case, the wishes the parties may express […] and the need for a speedy settlement of the dispute".[1586] As with the conciliation procedure used by the Multilateral investment Guarantee Agency (MIGA), the conciliator may be "guided by ICSID's Conciliation rules".[1587] The IIA may also provide that the conciliator be bound by some other named set of rules.

[1583] Coe (2005), at 39.
[1584] August Reinisch, "Elements of Conciliation in Dispute Settlement Procedures Relating to International Economic Law" in Christian Tomuschat, Riccardo Pisillo Mazzeschi & Daniel Thürer, eds, *Conciliation in International Law: The OSCE Court of Conciliation and Arbitration* (The Hague: Brill, 2016) at 124.
[1585] Edouard Planche, UNESCO Mediation and Conciliation Procedure for Promoting the Return and Restitution of Cultural Property in Christian Tomuschat, Riccardo Mazzeschi & Daniel Thürer, eds, *Conciliation in International Law: The OSCE Court of Conciliation and Arbitration* (The Hague: Brill, 2016) at 111.
[1586] UNCITRAL Conciliation Rules (1980) at art.7(3).
[1587] Ibrahim Shihata, *Foreign Investment: Origins, Operations, Policies and Basic Documents of the Multilateral Investment Guarantee Agency* (The Hague: Martinus Nijhoff Publishers, 1988) at 266.

After the conciliation procedure is launched, the conciliator may determine the timeframe for the process, after consulting with the parties. The example of MIGA conciliation may be useful for our purposes, as the agency reports "a great success rate" in handling such cases.[1588] The state parties can set a "cut-off" date for the conciliator to issue their report, as is done in cases of disputes between MIGA and its state parties.[1589] For instance, the deadline for MIGA conciliation is "180 days unless parties agree to extend this period".[1590] After the conciliator's report is issued, each party has a period of time (60 days under MIGA) to comment on the report before the conciliator's role is terminated.[1591] The conciliator can also end the procedure earlier, in case the circumstances of the case do not permit them to evaluate the merits of the claim, the parties refuse to cooperate; or they employ so-called guerrilla tactics to delay the process. The conciliator may reflect on these issues in their final report. Under MIGA, parties cannot resort to arbitration if:

> the conciliator fails to submit his report within the required period, (ii) if, 60 days after both parties have received the report, they fail to accept it, (iii) if, within the same time limit, the parties fail to agree otherwise on a settlement of all controversial issues or (iv) if either party fails to express any views on the report in the specified 60-day period.[1592]

One might reasonably question "the usefulness and appeal of conciliation in an international context", particularly in relation to investment disputes.[1593] In response, it

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[1588] Ximena Bustamante, "Investor-State Mediation: Reflections of Its Feasibility From a Process Perspective" in Todd Weiler & Freya Baetens, eds, *New Directions in International Economic Law: In Memoriam Thomas Wälde* (The Hague: Martinus Nijhoff Publishers, 2011) at 287.
[1589] *Ibid*.
[1590] *Ibid* at 266.
[1591] *Ibid*.
[1592] *Ibid*.
[1593] Eric Scwartz, "International Conciliation and the ICC" (1995) 10:1 ICSID Review 98. Bustamante, (2011), at 284. (Opponents of ICSID Conciliation process suggest that it is similar to arbitration, "lacks principle of confidentiality" and usually is "conducted in adversarial frame". These factors together

may be useful to examine some significant advantages.[1594] For example, these procedures permit conciliators to meet with the parties either separately ("caucusing") or together to discuss their submissions, narrow down the issues, clarify the aspects of the claims, and provide the parties with preliminary evaluations of one or more substantive issues.[1595] In

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reportedly brought down the popularity of conciliation as opposed to arbitration. In my view, conciliation may be unpopular among investors if it is voluntary. Why would investor subject itself to additional procedure in some ways similar to arbitration without actually getting a binding outcome? If the conciliation is mandatory, an investor has to participate in the process). Bühring-Uhle, Kirchhoff & Scherer (2006), at 228. Recall that conciliation has been employed by the World Bank to resolve property disputes between investors and states since before the establishment of the ICSID Centre. The ICSID Convention itself created machinery for both conciliation and arbitration. Some prominent arbitrators, such as Thomas Wälde, report success in mediating investor-state disputes. It has also been successfully used in inter-state conflicts. Robert Asher, "The World Bank Group Archives Oral History Program: Transcript of Interview with Aron Broches" (18 April, 1984) at 29, 35, online: <http://documents.worldbank.org/curated/en/603371468151508966/pdf/789460v30TRN0B0ssion020May023001984.pdf>. Parra (2012), at 10. Thomas Walde, "Mediation/ Alternative Dispute Resolution in Oil, Gas, and Energy Transactions: Superior to Arbitration/Litigation from a Commercial and Management Perspective" (2003) 2 OGEL. Marieke Koopmans, *Diplomatic Dispute Settlement: The Use of Inter-State Conciliation* (Cambridge: Cambridge University Press, 2008). The most recent example is the conciliation between Timor Leste and Australia on maritime delimitation under the United Nations Convention on the Law of the Sea. Although some critics may say that this conciliation lasted as long as 2 years before concluding in the amicable settlement, it is worth noting that the dispute between Australia and Timor Leste lasted for 45 years *prior* to conciliation. The dispute involved potentially multimillion claims over possession of oil and gas resources in the Timor Sea. Both parties were significantly aggravated.

[1594] Eric Scwartz, "International Conciliation and the ICC" (1995) 10:1 ICSID Review 98. Bustamante, (2011), at 284. (Opponents of ICSID Conciliation process suggest that it is similar to arbitration, "lacks principle of confidentiality" and usually is "conducted in adversarial frame". These factors together reportedly brought down the popularity of conciliation as opposed to arbitration. In my view, conciliation may be unpopular among investors if it is voluntary. Why would investor subject itself to additional procedure in some ways similar to arbitration without actually getting a binding outcome? If the conciliation is mandatory, an investor has to participate in the process). Bühring-Uhle, Kirchhoff & Scherer (2006), at 228. Recall that conciliation has been employed by the World Bank to resolve property disputes between investors and states since before the establishment of the ICSID Centre. The ICSID Convention itself created machinery for both conciliation and arbitration. Some prominent arbitrators, such as Thomas Wälde, report success in mediating investor-state disputes. It has also been successfully used in inter-state conflicts. Robert Asher, "The World Bank Group Archives Oral History Program: Transcript of Interview with Aron Broches" (18 April, 1984) at 29, 35, online: <http://documents.worldbank.org/curated/en/603371468151508966/pdf/789460v30TRN0B0ssion020May023001984.pdf>. Parra (2012), at 10. Thomas Walde, "Mediation/ Alternative Dispute Resolution in Oil, Gas, and Energy Transactions: Superior to Arbitration/Litigation from a Commercial and Management Perspective" (2003) 2 OGEL. Marieke Koopmans, *Diplomatic Dispute Settlement: The Use of Inter-State Conciliation* (Cambridge: Cambridge University Press, 2008). The most recent example is the conciliation between Timor Leste and Australia on maritime delimitation under the United Nations Convention on the Law of the Sea.

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[1595] Coe (2005), at 40.

their preparations for the conciliation, conciliators "review legal documents, require pre-mediation submissions from the parties, and confer with the lawyers (and even the parties) beforehand to learn about the dynamics of the dispute and the interests of the parties that will be relevant in customizing the process".[1596]

These features of conciliation may be particularly helpful in dealing with frivolous and abuse of process claims. The conciliators will be familiar with the dynamics of the dispute and the extra-legal interests of the parties, which will help them to narrow down the issues and to appreciate the merits of each other's positions.

Another key advantage of caucusing specifically and conciliation generally is confidentiality.[1597] Conciliation proceedings are usually kept entirely confidential from third parties.[1598] With respect to information divulged by one party to the conciliator during a caucus session, there are two approaches to the release of that information to the opposing party.[1599] The first is to keep all information from caucuses confidential from the other party (unless disclosure is expressly authorized by the party possessing the information). The second requires the conciliator to disclose everything to the other party unless the party expressly required them to keep all information from the caucus confidential.[1600] The difference in the two approaches lies in whether disclosure or confidentiality is the default position; under both approaches, parties that possess information can control whether it is disclosed to the other party.

[1596] Nancy Welsh & Andrea Schneider, "Becoming Investor-State Mediation" (2012) 1 Penn St JL & Intl Affairs 86 at 92.
[1597] Donna Ross, "Med-Arb/Arb-Med: A More Efficient ADR Process or an Invitation to a Potential Ethical Disaster" in Arthur Rovine, ed, *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers (2012)* (The Hague: Martinus Nijhoff Publishers, 2013) at 374.
[1598] American Arbitration Association, *Handbook on International Arbitration and ADR* (Juris Publishing, 2010) at 226.
[1599] *Ibid.*
[1600] *Ibid*

The confidentiality of the caucusing process and of conciliation generally permits parties to speak freely with conciliator without fear that their statements will impact the outcome of a possible future litigation or arbitration process.[1601] Of course, confidentiality can also create tension in the context of investment disputes, where one participating party is a state that may face pressure or even be subject to obligations to publicize matters of public interest. It is true that states have participated in inter-state conciliations where matters were kept confidential without much additional pressure from public constituencies. However, in investment arbitration, the confidentiality of conciliation can arguably produce even greater mistrust in the system and thus contribute to the backlash against the investment regime.

Coe suggests a compromise position: "[t]he delicate balance required might be struck by retaining privacy and confidentiality for caucuses and most joint sessions, while making public the terms of settlement, the opening joint session and any session at which agreement is announced".[1602] I endorse Coe's suggestion; the final agreement and the final session where the final agreement is reached should be made public but not any other statements, offers, or disclosures made during the course of the conciliation.[1603]

It may also be useful for states to be able to publicize the existence of a dispute and the general issues subject to conciliation, without disclosing the identity of the investor until the conciliation is concluded (with any of three outcomes listed in the previous section). But I would not expand transparency any further, for fear of disrupting the non-adversarial environment necessary to achiving amicable settlements. For example, Bustamante argues that it may be useful to invite observers to any joint sessions

[1601] *Ibid*.
[1602] Coe (2005), at 40.
[1603] *Ibid*.

during the conciliation.[1604] Although this may be useful in some cases, it would likely result in delays and procedural complications that would unnecessarily extend the process of pre-screening, and may inhibit settlements between states and investors.

The objection may be raised that conciliators will face the same difficulties that arbitrators face in evaluating the merits of the investors' claims, due to possible uncertainty of legal norms. It is true that the pre-screening mechanism is not a unique "cure" that will immediately resolve all problems of the investment system. The mechanism should be viewed only as a tool that provides certain benefits, and will not resolve the problem of legal uncertainty. However, it is worth noting that the third party conciliator, unlike arbitrators, will have no personal interest in prolongation of the dispute – that is, they are removed from at least some of the set of incentives discussed in Chapter Five that inhibit arbitrators from dismissing frivolous and abuse of process claims. In addition, the conciliation procedure may permit both states and investors to "save face", a culturally important aspect of dispute resolution that is frequently overlooked.[1605]

Critics also may also point out that claims fall at many different points along "the merits spectrum".[1606] Céline Lévesque explains that "[a]t one end of the spectrum are

[1604] Bustamante (2011), at 298.
[1605] Hi-Taek Shin, "An Ombudsman as One Avenue Facilitating ADR and Socio-Cultural Factors Affecting ADR in Investment Treaty Dispute Resolution" in UNCTAD, *Prevention and Alternatives to Arbitration* (New York: United Nations, 2011) at 100. ("[w]hile litigation has become a widely accepted way of resolving disputes between individuals and corporate entities, prematurely filing a legal action without putting in a bona fide effort to find a mutually acceptable solution is considered distasteful in Korean society […]During my years as a practitioner, I have observed from both private parties and government agencies that giving the counterparty a chance to save face is crucial to prevent an adversarial relationship from becoming acrimonious because, without that opportunity, it may be compelled to defend the case to the end (even if the cost of settling would have been rationally preferable to the negative outcome of litigation) for fear of losing face").
[1606] Lévesque (2011), at 78.

meritorious claims and, at the other end, those that are unmeritorious".[1607] But Lévesque highlights the possibility of a "middle zone", where claims are of "uncertain merit (either as matter of law, fact or mixed questions of law and fact)".[1608] In the "clear-cut" meritorious cases, the conciliator can produce a legal assessment that may impress on the state its high risk of liability. This evaluation can encourage a state to settle. When cases are unmeritorious, the conciliator will evaluate the claim, "and may conclude that the government faces a low risk of liability".[1609] Lévesque observes that early neutral evaluation" of the merits may discourage investors from proceeding with their claim.[1610]

In circumstances where the conciliator faces claims in the "middle zone" where the merits are uncertain due to, for example, the contradictory interpretations of relevant IIA provisions rendered by previous arbitral tribunals, the report still may be useful to "weigh the strengths and weaknesses of different claims and arguments. This analysis can in turn be used to tailor a more efficient dispute settlement process—that is "fitting the forum to the fuss".[1611] As Coe explains, the uncertainty of the final result in such claims may be the exact reason why the parties may prefer to reach an amicable settlement or withdraw the claim in the aftermath of conciliation.[1612]

In any case, this Chapter does not argue that the conciliation procedure should substitute for arbitration, or that conciliation is in principle a superior means for resolving investor-state disputes.[1613] Instead, it suggests that some features of the conciliation

[1607] *Ibid*.
[1608] *Ibid*.
[1609] *Ibid* at 78-79.
[1610] *Ibid*.
[1611] *Ibid* at 79.
[1612] Coe (2005), at 16.
[1613] This may be the case but I advance no such argument here.

procedure may be useful to deal with frivolous and abuse of process claims at the pre-arbitration stage.

After the conciliator is appointed, it is sensible for conciliator to "set the table" by explaining the ground rules of the conciliation, for example at what stage of the process the parties will have an opportunity to present their positions, what will be the schedule for caucusing, and how the parties will interact with each other (directly or indirectly).[1614] The conciliator should explain to the parties the confidentiality rules, in particular the legal status of facts disclosed or settlement offers made during the conciliation.[1615] The conventional rule of conciliation suggests that "discussions in mediations where litigation has been or could be commenced, like settlement discussions, are without prejudice".[1616] This means that information shared during the conciliation cannot be used in litigation, the conciliator cannot be called as witness, and his or her notes "cannot be produced as evidence".[1617] It seems reasonable to maintain this conventional approach in the proposed pre-screening process because it could facilitate cooperation by the parties, and permit the pre-screening to reach a settlement or for an investor to withdraw their claim, the most desirable outcomes.

6.3.2 Challenges for Conciliation

It is worth briefly addressing one of the most serious practical challenges that may jeopardize the success of a conciliation. The state representative at the conciliation process may have no authorization to make an offer, or there may be disagreement among the states' departments as to whether the state should make any offers to the

[1614] Stitt (2004), at 56-57.
[1615] *Ibid* at 58-59.
[1616] *Ibid*.
[1617] *Ibid* at 59.

investor without a binding third-party decision.[1618] It may be plausible to follow the example of Peru, which created a special committee composed of members from various government departments that is authorized to make proposals for settlements with investors.[1619]

Interestingly, opponents of conciliation prior to arbitration appear to assume that foreign investors will not want to engage in conciliation due to the additional expenses that may occur or bluntly disregard the process as another procedural hurdle on the way to obtaining a binding, enforceable decision. However, this is not necessarily the case. For instance, the CEO of Metalclad suggested that the mechanism of arbitration "was so dissatisfying that he wished he had merely entrusted his company's fate to informal mechanisms".[1620] Another example is provided by Thomas Wälde, who mediated the Vattenfall-PSE SwePol Dispute in 2003.[1621] Wälde submits that both parties' executives demonstrated robust professionalism and "commercial judgement" when they decided to "explore" the mediation process as a way to resolve the dispute despite possible pressures to "pass dispute to the lawyers" so they "move it into and through litigation".[1622] The mediation conducted by Wälde helped to produce an outcome that satisfied the parties at the expense of only 1 million Euros in costs; this includes the costs of both the mediation service and the costs incurred by the two parties.[1623] The mediation took 175 days to complete.[1624] From Daniel Behn, we know that the average length of an ISA arbitration is

[1618] Barton Legum, "The Difficulties of Conciliation in Investment Treaty Cases: A Comment on Professor Jack Coe's Toward A Complementary Use of Conciliation in Investor State Disputes" (2007) 1 TDM.
[1619] *Ibid*.
[1620] Coe (2005), at 9.
[1621] Walde (2007), at 27.
[1622] *Ibid* at 28.
[1623] *Ibid*.
[1624] *Ibid*.

four years,[1625] and the costs to a respondent state of defending a claim can exceed 10 million US dollars, which accounts only for arbitrators' and lawyers' fees and not the additional costs of experts, witnesses, investigations, and the like.[1626] For example, Poland and the Czech Republic spent US$6 million USD $10 million, respectively, defending single arbitrations.[1627] Accordingly, conciliation may be a way to reduce costs for both parties.

6.4 Concluding Remarks

Frivolous and abuse of process claims constitute a legal problem that requires a legal solution. This chapter examined three possible approaches to handling such claims in the investment regime: institutional reform, cost-shifting, and pre-screening mechanisms.

The proposed pre-screening conciliation procedure can successfully play the role of a control mechanism, and would be far more likely to achieve political support than a multilateral investment court or appellate body. The mechanism provides for three possible outcomes: the investor withdraws the claim, investor and state agree on a settlement, or the investor decides to proceed with arbitration. The first two outcomes are unambiguously beneficial if a frivolous or abusive claim is involved. And even under the third option, the independent conciliator will help the parties to narrow the issues, clarify them, and provide an independent assessment of the claim. The ultimate objective of such a mechanism is to serve as an "eye-opener" for the parties that, under conditions of asymmetric information, may not fully appreciate the legal merits of their claims.

[1625] Behn (2015), at 376.
[1626] UNCTAD (2005), at para. 14.
[1627] *Ibid*.

Accordingly, the pre-screening of claims can be a politically attainable and effective way to curtail frivolous and abuse of process claims.

Institutional reform can result in greater consistency in the interpretation of investment standards, and the changes in the structure of arbitrator remuneration and the appointment procedure can shift arbitrators' incentives. These factors may be effective in influencing arbitrators to dismiss more claims as frivolous or abuse of process. However, institutional reforms are the most difficult to achieve in practice, and may never be politically attainable.

Cost-shifting is in theory an effective strategy to deter investors from bringing frivolous and abuse of process claims. There are, however, two problems with this approach in the ISA context. First, the tribunals have not yet developed a consistent approach to cost allocation. Rovine's findings confirm that in the majority of cases, tribunals do not expressly adopt *ex ante* any particular rule on the cost allocation, instead preferring the standard of "ambivalence" and allocating costs without articulating the reasons why the costs were allocated in a particular way. Thus, for cost-shifting strategies to be successful in deterring frivolous and abuse of process claims, states should specify in IIAs the mode of cost allocation in case a claim is found to be frivolous or an abuse of process, so that investors may know in advance what scope of costs they will likely face. Second, even when tribunals are willing to allocate costs against a party that brought a frivolous or abuse of process claim, that will be ineffective as a deterrent if tribunals dismiss claims in overly narrow circumstances. Accordingly, changing the rules on cost-shifting without dealing with the broader structure of the investment regime and the incentives it creates is unlikely to make much of an impact.

None of the three types of measures described in this chapter would be a panacea for the problem of frivolous and abuse of process claims. They may be adopted concurrently or independently. In my view, the pre-screening mechanism presents a valuable option for the investment regime's participants not only because of its political attainability but also because it may help shift the parties' perspective away from thinking of investment disputes as legal cases to win or lose, but rather as practical problems that may be resolved through independent third-party assessment without the heavy costs associated with arbitration.

Chapter 7

Concluding Reflections

The practice of international investment treaty-making shows that states often "copy-paste" provisions in their IIAs.[1628] The mega-regional investment agreements such as CETA, TPP and TTIP all include provisions that permit tribunals to dismiss the claims in which "an award in favour of claimant cannot be made" or that are "manifestly without legal merit". Some other recent IIAs concluded in the last four years, for example by Australia and Peru,[1629] New Zealand and Korea,[1630] Korea and Turkey,[1631] Nigeria and Singapore,[1632] and Singapore and Burkina Faso[1633] all incorporate similarly worded provisions relating to the dismissal of frivolous claims. Investment tribunals continue to deal with allegations of the state parties that investors' claims constitute an abuse of process.

In all these treaties, the arbitrators remain in charge of identifying and dismissing frivolous and abuse of process claims. The application of these instruments in the investment regime context shows the lack of clearly articulated standards under which the claims can be dismissed. The arbitrators have full discretion over the dismissal, and so far have been overly cautious in dismissing the claims early. Unless some other systemic changes are made, no number of provisions empowering the dismissal of frivolous or abuse of process claims is likely to be effective in curtailing those claims.

[1628] Shotaro Hamamoto & Luke Nottage, "Japan: Introduction" in Chester Brown, ed, *Commentaries on Selected Model Investment Treaties* (Oxford: Oxford University Press, 2013) at 355.
[1629] Australia-Peru FTA at 8.20.
[1630] Republic of Korea-New Zealand FTA at art.10.26 (3).
[1631] Republic of Korea-Turkey BIT at art.1.17.
[1632] Nigeria-Singapore BIT at art.16(2).
[1633] Burkina Faso-Singapore BIT at art.14.

The idea that adjudicators should be in charge of identifying and dismissing frivolous and abuse of process claims in the investment regime context reflects the domestic legal approaches to handling such claims. It seems that the policy-makers, state parties, arbitrators, and investors have all accepted this approach without reflection, perhaps because it constitutes "the most familiar solution" from the domestic legal systems in which all of these participants were trained.[1634] Going with the "most familiar" option as an unexamined default shows that participants in the regime have given little thought to the structural and sociological differences between some domestic legal systems (where the rule seems to originate) and the regime of international investment protection. The regime drastically departs from the national legal systems in terms of its structures (especially decentralized system of dispute resolution without any sort of formal precedent or judicial hierarchy), and the incentives that those structures create for adjudicators (especially that where arbitrators are appointed by the parties and receive remuneration per hour or per day), they have multiple, overlapping incentives to permit even the least meritorious disputes to be pursued in full.

The purpose of this thesis has been to challenge this status quo and inject a contextual mode of thinking about accepting and importing legal solutions to resolve problems within the investment regime. As anyone familiar with the many failed legal transplants in national legal systems should know, the "most familiar solution" is not necessarily the most appropriate and effective one. The comparative law scholarship, particularly the literature on legal transplants, teaches us to appreciate the context of the system and

[1634] J. A Jolowicz, *On Civil Procedure* (Cambridge: Cambridge University Press, 2000) at 167. Lahav (2017) (provides critical perspective on the outcry that relates to frivolous litigation and argues that curtailment of frivolous litigation may undermine democratic legitimacy). Levinson (1986), at 359. Andrews (2003), at 507.

systemic differences before proceeding with a policy of legal borrowing. The contribution of this thesis, accordingly, has not only been to describe and assess the existing approaches to the early dismissal of claims, but more importantly to show *why* those approaches have been ineffective and *how* we should think about the reform of the investment regime more generally. Most significantly, it warns against transplanting legal solutions from national legal systems to the international investment regime without due appreciation of the regime's particularities. Such a warning is particularly timely in 2018, when the regime's participants are actively exploring new approaches to arbitration and introducing various initiatives in the administration of investor-state disputes.

This thesis aspires to direct the treaty drafters toward such as "contextual" way of thinking about the investment regime's reform. It thus adds to the comparative international law discourse recently highlighted by the volume on *Comparative International Law* edited by Roberts, Stephan, Verdier, and Versteeg. Roberts *et al* conceive of comparative international law as a way to "utilize […] insights and methods from comparative law in order to identify, analyze, and explain similarities and differences in how international law is understood, interpreted, applied, and approached by different national and international actors".[1635] The project also fits with earlier scholarship by David Kennedy, who examined "the roles comparativists, as legal specialists in difference, play in the broader international project of public and private governance".[1636] Kennedy concluded that we "should also see comparative law in relation

[1635] Anthea Roberts et al, eds, *Comparative International Law* (Oxford: Oxford University Press, 2018) at 6-7.
[1636] David Kennedy, "New approaches to comparative law: Comparativism and international governance" (1997) 2 Utah LR 545 at 551.

to the broader problems of governance in which it plays, often unwittingly to be sure, a number of important roles".[1637]

[1637] *Ibid*.

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