

A MODEL BIT FOR DEVELOPMENT

The Example of Jordan

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Developing countries are increasingly realizing the need to attract foreign direct investment to achieve economic and social welfare. Although the advantages of FDI are numerous and well documented, economic development through FDI has failed in most developing countries. Studies show that bilateral investment treaties (BITs) have not played a significant role in promoting and encouraging economic development for host states. By contrast, studies show that BITs have over-protected foreign investors and investments, at the expense of host country development. This is a result of the historical background and circumstances surrounding the formation of BITs in the 1950's. Recently, many countries and international organisations have expressed the need to effectuate the reciprocal nature of investment treaties, whereby BITs serve as a tool for economic development, in addition to investment protection.

States, as sovereigns, have the duty and right to pursue legitimate development goals and regulate matters of public concern without fear of liability to foreign investors. This requires a balanced approach to BITs, in which economic development objectives of the host country, and foreign investment protection are both addressed and equally preserved.

Model BITs are becoming an even more important tool to achieve development goals from FDI. A model BIT is an investment treaty designed specifically to address the needs and goals of a specific country. If the model BIT strikes the right balance between economic development and investment protection, then development through FDI should be possible.

This thesis takes Jordan as an example of a developing country that is striving to attract FDI, and does not have a model treaty specifically designed for its needs and objectives. The proposed BIT for Jordan shifts the focus from pure investment protection to balanced protection tied with economic development. Overly protective treatment standards and their innovative interpretations by arbitral tribunals, are analyzed, and guidelines are provided to help avoid past problems for developing countries. This doctrinal and comparative study draws on the case law of the International Centre for the Settlement of Investment Disputes (ICSID) and existing model BITs to develop an up-to-date BIT for Jordan that addresses the country's development goals.

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CHAPTER ONE

OVERVIEW

“What is the impact of foreign Direct Investment (FDI) on development? The answer is important for the lives of millions – if not billions- of workers, families, and communities in the developing world. The answer is crucial for policy makers in the developing and developed countries and multilateral agencies. The answer is central to the debate about the costs and benefits of the globalization of industry across borders.”¹

I. BACKGROUND TO THE PROBLEM

Economic development is an important goal for any country. It becomes *the* most important goal for developing countries whose standard of living and international power is fundamentally tied to their economic position in the world. Although there is no single definition of economic development, it is commonly described as the creation of jobs and wealth, and the improvement of the quality of life.² Economic development can also be described as a process that influences growth and restructuring of an economy to enhance the economic well-being of a community.³

¹ Edward Graham Theodore Moran, Magnus Blomstrom, Does Foreign Direct Investment Promote Development? 1 (Institute for International Economics 2005).

² The International Economic Development Council: Economic Development Reference Guide 3. Available at http://www.iedconline.org/clientuploads/Downloads/IEDC_ED_Reference_Guide.pdf.

³ Id. at 3. Available at http://www.iedconline.org/clientuploads/Downloads/IEDC_ED_Reference_Guide.pdf.

Each country has a unique set of challenges for economic development; therefore different countries address these challenges in different ways depending on their own needs and circumstances. However, if proper conditions exist, FDI can play an important role in securing the development needs of any state.⁴ The development process is accelerated by the spillover effect of transferred technologies, human capital enhancement, increased competitiveness in the host market which results in better and cheaper services and goods, the injection of foreign capital in the local economy, employment opportunities, management of resources, increased revenues to the host state government from the taxes and duties paid by the foreign investment, and many other advantages of FDI.

The use of FDI for development became increasingly significant after WWII, when states began to negotiate and sign Bilateral Investment Treaties (BITs). These treaties had three purposes: i) to enhance development through the attraction of FDI to the host state, ii) to protect the out-bound investors of the home state from the risks associated with investing in other countries, and iii) to clarify the rules and enforcement mechanisms otherwise existing in customary international law that would apply in the event of a dispute between an investor and the host state.⁵

The new trend of signing BITs came after the international community realized that other forms of development finance, such as foreign aid and loans, started to dry up and became harder to obtain.⁶ Thus, there was a need to find an alternative to such scarce development resources.

⁴ Leon Tarkman, *Foreign Direct Investment: Hazard or Opportunity?*, 41 GEORGE WASHINGTON INTERNATIONAL LAW REVIEW 5 (2009).

⁵ See in general, Genevieve Fox, *A Future For International Investment? Modifying BITs to Drive Economic Development*, 46 GEORGETOWN JOURNAL OF INTERNATIONAL LAW 231-32 (2014).

⁶ Jeswald Salacuse, *The Emerging Global Regime For Investment*, 51 HARVARD INTERNATIONAL LAW JOURNAL 441 (2010).

A. FOREIGN AID AND INTERNATIONAL LOANS AS A TOOL FOR DEVELOPMENT

Due to corruption, bad governance, or the lack of natural resources, among other problems, many developing states were, and still are, dependent on foreign aid and loans to secure funding for major domestic projects, cover budget deficits, and create jobs. This funding is provided to them by developed states and international development institutions, mainly the World Bank and the International Monetary Fund.

Although foreign aid can help a developing country with such needs in the short run, recent studies have found that financial aid has not proven to contribute significantly to the general development and welfare of countries in the long run.⁷ Donor governments also often seek to produce political benefit for themselves from conditions attached to foreign aid.⁸ In order to keep aid flowing, donor states often require that the subsidized state adopt political decisions and attitudes which might not be in the subsidized state's best interest, or which might go against the subsidized state's own policy. Any change in the subsidized state's political interest could jeopardize the financial aid given to it by these donor states.⁹

Dependency on foreign loans also has its negative effects. Loans provided to developing states by international development institutions impose heavy restrictions on the borrowing

⁷ See in general, Peter Boone, *Politics and the Effectiveness of Foreign Aid* 40 EUROPEAN ECONOMIC REVIEW (1995). See also, Daniel Ehrenfeld, *Foreign Aid Effectiveness, Political Rights and Bilateral Distribution*, THE JOURNAL OF HUMANITARIAN ASSISTANCE (2004).

⁸ See in general, Donald Hindley, *Foreign Aid to Indonesia and Its Political Implications*, 36 PACIFIC AFFAIRS (1963).

⁹ Boone, EUROPEAN ECONOMIC REVIEW, (1995). See also, Ehrenfeld, THE JOURNAL OF HUMANITARIAN ASSISTANCE, (2004).

government's operations, a feature known as "conditionality."¹⁰ Loans from international development institutions are continued based on requirements that the borrower undertake major policy changes and reforms that affect the governance of the country concerned.

In the 1980s and 1990s, these forms of development finance from developed countries and aid institutions started to dry up and became more difficult to obtain, thus "developing countries increasingly felt the need to promote foreign investment in order to foster economic development."¹¹ They saw their participation in investment treaties as a way to obtain alternative funding for their development goals and infrastructure, and therefore signed such treaties in increasing numbers.¹² Engaging in BITs with other countries was a way of signaling that a state would afford foreign investors with protections and guarantees, and that, in return, would attract foreign investors to the country, which would then lead to economic development.

B. FOREIGN DIRECT INVESTMENT AS A TOOL FOR DEVELOPMENT

"Developing countries, emerging economies and countries in transition have come increasingly to see FDI as a source of economic development and modernization, income growth and employment."¹³ FDI can be defined as an equity or ownership of more than 10 percent by an

¹⁰ For example, the International Monetary Fund (IMF) defines the term "conditionality" as follows: "When a country borrows from the IMF, its government agrees to adjust its economic policies to overcome the problems that led it to seek financial aid from the international community. These loan conditions also serve to ensure that the country will be able to repay the Fund so that the resources can be made available to other members in need." See IMF Factsheet, available at <https://www.imf.org/external/np/exr/facts/conditio.htm>.

¹¹ Nicholas P. Sullivan Jeswald W. Salacuse *Do Bits Really Work?: An Evaluation Of Bilateral Investment Treaties And Their Grand Bargain*, 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 77 (2005).

¹² See in general UNCTAD, World Investment Report 2003: FDI Policies for Development; National and International Perspectives. xv (2003).

¹³ Foreign Direct Investment for Development: Maximising Benefits, Minimising Costs (Overview). 5 (2002).

investor in one country (known as “the home country” or “capital-exporting country”), in an enterprise located in another country (known as “the host country” or “capital importing country”).¹⁴ Typically, such investment involves transferring capital, machinery, equipment, technology and other components related to the investment project, from the home country to the host country.¹⁵ FDI is distinguished from portfolio investments in which foreign entities invest only in the stock and shares of local companies, and thus there is no transfer of technology and equipment, nor is their real “control” by the foreign investor over the local entity.¹⁶

FDI is more effective than international aid and loans in fueling the development of countries. While foreign aid and loans bring the host country only money, FDI provides the host state with a package of vital elements for the creation of a productive economy.¹⁷ In fact, controversy has risen as to whether economic development is a criterion for, and part of the definition of, FDI and its eligibility for protection under international law.¹⁸

The rationale for increased attention to FDI stems from the belief that FDI has many advantages to the host state economy. These advantages include access to markets, technology transfers, the introduction of new processes and know-how to the domestic market, human resources training and enhancement, infrastructure development, and higher revenues resulting from taxes and duties paid by the foreign investor to the host state.¹⁹ These benefits, along with the direct capital financing FDI provides, offer strong incentives for states, especially developing ones, to compete for FDI and use it as a tool for development.

¹⁴ JESWALD W. SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 14 (Oxford University Press. 2013).

¹⁵ *Id.* at 15.

¹⁶ Tarkman, *GEORGE WASHINGTON INTERNATIONAL LAW REVIEW*, 5 (2009).

¹⁷ SALACUSE. 18 (2013).

¹⁸ SORNARAJAH, *THE INTERNATIONAL LAW ON FOREIGN INVESTMENT* 10 (Cambridge University Press 3 ed. 2012).

¹⁹ SALACUSE. 18-19 (2013).

To draw these advantages and other benefits from FDI, the host state is compelled to offer foreign investors and investments protections and treatment standards that mitigate the risks of investing in their territory and encourages the inflow of FDI. This is done via the conclusion of BITs, which provide protection and treatment standards to foreign investors. Thus, developing countries promote and encourage the inflow of foreign investment into their territory anticipating development through FDI.²⁰ This is the “grand bargain” of BITs; “a *promise* of protection of capital in return for the *prospect* of more capital in the future.”²¹ Hence, BITs have two main objectives: i) investment protection, and ii) host state development.

C. THE SUCCESS AND FAILURE OF BITS

BITs and investment agreements are not a new phenomenon; they can be traced back to the BCE era.²² However, the investment treaty we know today, the (BIT), emerged in the 1950’s when Germany signed the first BIT with Pakistan in 1959.²³ Since then BITs have proliferated at an extraordinary rate, reaching around 3300 BITs worldwide in less than 60 years.²⁴ The question is whether BITs serve their two main purposes (i.e., investment protection and economic

²⁰ Tarkman, GEORGE WASHINGTON INTERNATIONAL LAW REVIEW, 5 (2009).

²¹ Jeswald W. Salacuse HARVARD INTERNATIONAL LAW JOURNAL, 77 (2005).

²² Early investment treaties appeared in the old Babylonian period (2003-1595 BCE). See AMNON ALTMAN, TRACING THE EARLIEST RECORDED CONCEPTS OF INTERNATIONAL LAW: THE ANCIENT NEAR EAST (2500–330 BCE) § 8, at 67 (Randall Lesaffer ed., Martinus Nijhoff Publishers. 2012).

²³ TREATY BETWEEN THE FEDERAL REPUBLIC OF GERMANY AND PAKISTAN FOR THE PROMOTION AND PROTECTION OF INVESTMENTS (1959).

²⁴ Information taken from UNCTAD INVESTMENT POLICY HUB Website. Available at <http://investmentpolicyhub.unctad.org/IIA>

development). The BIT movement which started in the 1950's is a good starting point to answer this question.

As articulated by Lord Shawcross (a former Attorney General of the U.K.) and Herman Abs (Chairman of the Deutsche Bank in Germany):

[I]t is now widely recognized that major steps must be taken to buttress the economic position of the free-world nations, both as a measure against Soviet moves and as a means of resolving some of the demands being made by the peoples of the underdeveloped nations of the world, the notion of greater protection under international law for private investment takes on added importance.²⁵

From its inception, the BIT was designed and structured by capital exporting countries singularly focusing on one aspect of the investment process: to protect the investments of their outbound investors in less developed, newly independent, countries. BITs were not built to enhance or encourage development, although that was a projected goal by developing countries.²⁶ The BITs signed in the 1950's and 1960's are not very different in essence from those signed today. While investment protection has been a success, development through investment has failed in most countries.²⁷ This failure is due to the fact that BITs focus on investment protection singularly without consideration given to any other objective.²⁸

The current BIT system offers rights of protection to foreign investors without offering corresponding rights to the host state. Capital exporting countries impose overly protective, catch

²⁵ "The Proposed Convention to Protect Private Foreign Investment, A Round Table," Introduction by the Editors, *Journal of Public Law*, Vol. 9, p. 115, 1960.

²⁶ "Developing countries increasingly felt the need to promote foreign investment in order to foster economic development." Jeswald W. Salacuse *HARVARD INTERNATIONAL LAW JOURNAL*, 77 (2005).

²⁷ Aaron Cosbey Nathalie Bernasconi -Osterwalder, Lise Johnson, Damon Vis -Dunbar, *Investment Treaties and Why They Matter to Sustainable Development*, 8 (2012).

²⁸ As one commentator notes "[T]reaty-based investment arbitration – mainly under BITs and NAFTA – has been biased in favour of foreign investors to the detriment of the sovereign power and duty of host States to pursue the general interest for their populations of promoting their national development." Attila Tanzi, *On Balancing Foreign Investment Interests with Public Interests in Recent Arbitration Case Law in the Public Utilities Sector*, 11 *THE LAW AND PRACTICE OF INTERNATIONAL COURTS AND TRIBUNALS* 47, 48 (2012).

all, provisions that protect their outbound investors. Hence, host countries become restricted when regulating matters of public concern, such as public health, employment and environment. Also, the current BIT system does not provide the host country with an effective enforcement mechanism to ensure foreign investors' good conduct and contribution to the economic development of the host country. Nor does the current BIT template contain provisions that ensure that foreign investors effectively participate in the development process of the host country in order to be covered under the umbrella of treaty protection. Typically, BITs do not contain any requirements that oblige the foreign investor to import the latest technology into the country, for example, or require employment of host state nationals to facilitate the transfer of skills and know-how.

The magnitude of this problem has been increased by the novel application and interpretation of BIT treatment standards by arbitral tribunals, sometimes in a manner not intended by the treaty parties. For example, the MFN treatment standard has been used to import law from agreements to which the home state is not a party.²⁹ The national treatment standard has been used to challenge public policy laws introduced by host countries, on the basis that these laws have greater impact on foreign investors than competing domestic investors.³⁰ Such expansive interpretations of treatment standards have put host countries in a position where they become reluctant to take any regulatory action in the public good, fearing liability. Additionally, the amounts of money awarded as damages in investor-state arbitrations are becoming greater and disproportionate to the real damages sustained by the foreign investor. Some tribunals have awarded foreign investors massive amounts in damages which have become a concern and a

²⁹ *e.g.*, Emilio Agustín Maffezini v The Kingdom of Spain (Decision on Jurisdiction), (ICSID, 2000).

³⁰ *e.g.*, GAMI Investments, Inc. v The Government of the United Mexican States (Award), (NAFTA, 2004).

burden on host states. For example “in 2004, a U.S. investor won an arbitration against Ecuador . . . The award and claim amount relative to government expenditure were 1.92% and 7.5%. The importance of these numbers becomes clear in the light that Ecuador spends annually around 7% of their government expenditure on health.”³¹

In the light of these flaws, the BIT developed 70 years ago no longer fits the needs of many countries, even capital exporting countries. BITs are no longer concluded exclusively between developed and developing countries, in what is known as North-South relationship. In fact, BITs are now being concluded between developed countries (North-North), and between developing countries (South-South).³² Some developing countries are becoming capital exporting countries, such as China and Saudi Arabia, hence developed countries are increasingly becoming vulnerable to the BIT system they created over half a century ago. Accordingly, development through FDI is no longer a projected goal of developing countries only, nor is investment protection the only goal for developed countries. Rather, both goals are now a concern for both the North and South blocs.

These developments and concerns have raised the voices of many civic and not-for-profit organizations which call for the transformation of BITs, and the need to incorporate economic development and growth as an explicit purpose. Many international organizations have presented working papers and studies on the importance of re-balancing the purposes of BITs to include economic development.³³ For example, a recent initiative was taken by the UNCTAD Secretariat

³¹ Kevin P. Gallagher & Elen Shrestha (2011, May). Investment Treaty Arbitration and Developing Countries: A Re-Appraisal, Global Development and Environment Institute, Working Paper No. 11-01, p.10 (referring to *Occidental Exploration and Production Company v. Ecuador* (LCIA Case No. UN3467)).

³² UNCTAD - Bilateral Investment Treaties 1959-1999, at 2 (2000).

³³ See Investment Treaty Law, Sustainable Development and Responsible Business Conduct: A Fact Finding Survey. (2014). Also see David Gaukrodger, The Balance Between Investor Protection and the Right to Regulate in Investment Treaties: A scoping paper (OECD Working Papers on International Investment ed., 2017). Also See

in the “Investment Policy Framework for Sustainable Development (IPFSD),”³⁴ which is designed to promote a new generation of investment agreements that contain a development agenda.

D. A BIT FOR DEVELOPMENT

BITs have not addressed the need for development. By clarifying the obligations that often lead to a diminution of the right to regulate, they can better address reciprocal promise to both investors and states. Hence, the time is now ripe for a re-balancing of the interests protected by investment treaties. The rights of protection from government wrongdoings to foreign investors should not be affected, but also should not be over emphasized and expanded in a manner that is detrimental to host state development. Host countries must have the ability to act in their best interest and reach economic growth through FDI, as much as foreign investors have the right to protect their investments.

Equating the interests for host states and foreign investors and balancing the BIT requires tying treaty protection to foreign investments with host country development. This can be achieved by re-defining “foreign investment” and “foreign investors” so that treaty protection is given to those investments that are of quality and benefit to the host state. Also, BITs should incorporate the development challenges and objectives of the host country, and preserve that country’s right to regulate and pursue legitimate public policy and development objectives. In

HOWARD MANN AARON COSBEY, LUKE ERIC PETERSON, KONRAD VON MOLTKE, IISD MODEL INTERNATIONAL AGREEMENT ON INVESTMENT FOR SUSTAINABLE DEVELOPMENT: NEGOTIATORS’ HANDBOOK (International Institute for Sustainable Development (IISD) 2nd ed. 2006).

³⁴ Investment Policy Framework for Sustainable Development (2015).

addition, investor treatment standards must be clearly defined and framed so as not to allow innovative and unintended interpretations by arbitral tribunals.

Reforming the BIT template cannot be done via a single investment treaty adopted by all countries. Different countries have different economic, political and social circumstances, and development goals vary among countries. Therefore no single model BIT could be expected to suffice on a global basis. Given the range of states involved, and their distinctive circumstances, prior attempts for an international unified investment agreement have failed.³⁵ The concept of a uniform model investment agreement on a global basis is an obsolete one. The solution to this problem rests in reforming the bilateral investment treaty for each country alone, by drafting model BITs that are specifically designed to accommodate the needs and objectives of a specific country.

Country specific BITs (model BITs) are an important tool in obtaining the economic and development fruits of FDI. Contrary to developed countries, most developing countries do not have model BITs that are specifically designed to foster their economic development through investment. Nor do the BITs offered to them by other countries allow them the ability to act in their best interests and achieve development through FDI, as these BITs were designed to advance the interests of the capital exporting country. By preparing country specific BITs, host countries may have increased control in negotiating and imposing the terms and conditions that

³⁵ For example, in 1995 OECD took the initiative to establish a Multilateral Agreement on Investment (MAI). The negotiators from capital-importing and capital exporting countries had different views on the proposed MAI. “All the principle negotiating states had substantial investments abroad and so had a common interest in seeing that those investments received maximum protection.” OECD capital-importing countries, on the other hand, were concerned about the types of foreign investment they will have to accept in their territories under the MAI and the high level of protection proposed by capital-exporting states. The negotiators seemed not to find a common ground, and therefore the negotiations for the MAI failed. *See* JESWALD W. SALACUSE, *THE LAW OF INVESTMENT TREATIES* 118-22 (Oxford University Press 2 ed. 2015). *See also* SALACUSE, *The Three Laws of International Investment : National, Contractual, and International Frameworks for Foreign Capital.* 353-54 (2013).

are aligned with their own policies and development objectives. The threat of moving businesses offshore limits the ability of host countries to impose or introduce inefficient, or overly strict, provisions into the BIT.³⁶ Thus a balanced approach to protect both interests is vital for the success of a model BIT for any country.

By signing BITs and enacting investment laws and policies, developing states have increased control in negotiating and imposing the terms and conditions that are aligned with their own policies and development objectives. The most important challenge for a state that aims at achieving development through FDI is to strike a balance between protections and guarantees that increase FDI flows to its economy, and policies that secure and ensure the contributions of these inward investments on its economy and development. This is not an easy task, as strict legal regimes that impose heavy requirements on foreign investors will result in labeling a country as unattractive and unfriendly to foreign investors. On the other hand, a very liberal regime can have negative effects on the host state economy. Thus, finding a development-oriented balance is the challenge in the implementation and content of BITs. A legal system that is “premised on the notion that all foreign investment is uniformly beneficial is not one based on sound foundations.”³⁷

The fact that some countries are desperately in need of FDI to enhance their development, sometimes at any cost, creates the opportunity for the imposition of “treaty – contracts of adhesion,”³⁸ when BITs are entered by a developing state with a developed state. This happens when investor exporting states, usually developed, aim to facilitate the entry of

³⁶ ASSAF RAZIN & EFRAIM SADKA, *FOREIGN DIRECT INVESTMENT: ANALYSIS OF AGGREGATE FLOWS* 124 (Princeton University Press. 2008).

³⁷ SORNARAJAH. 230 (2012).

³⁸ Jose Alvarez, *A BIT On Custom*, 42 *INTERNATIONAL LAW AND POLITICS* 39 (2009).

their investors into developing markets and obtain for them the highest level of protection by drafting BITs and offering them to the developed countries on a take-it-or-leave-it basis.³⁹ Developing states may have no other choice but to accept the excessive investor protection standards and vaguely worded umbrella clauses drafted by the powerful party, anticipating economic advancement from the importation of foreign investments.⁴⁰ Some developing countries have fallen victim to their own actions when disputes regarding such BITs arise.⁴¹

Although having a modern legal framework which provides protection and incentives to the foreign investor is essential, this does not mean that the host state should not promote and create investment opportunities.⁴² An excellent example is Saudi Arabia after its discovery of large amounts of oil in the 1930's. At that time Saudi Arabia did not have the basics of a legal system, yet investors lined up to take part in this profitable investment opportunity.⁴³

The Saudi example does not mean that an investment opportunity is limited to investments in the extractive industry or investing in the natural resources of a state. Investment opportunities can result from the privatization of public entities, public-private-partnerships (“PPPs”), and concession agreements.⁴⁴ Investment opportunities can also result from a state's

³⁹ Jose Alvarez & Tegan Brink, Revisiting The Necessity Defense: *Continental Casualty v. Argentina* 361 (Karl Sauvant ed., Oxford University Press 2011), referencing, KENNETH VANDEVELDE, UNITED STATES INVESTMENT TREATIES: POLICY AND PRACTICE 82 (Kluwer Law and Taxation. 1992).

⁴⁰ See for example, Sarah Anderson, *Foreign Investors Gone Wild: Leaders of developing countries are often forced to work with institutions that promote and protect foreign investment -- with little regard for the costs to democracy and the environment.*, FOREIGN POLICY IN FOCUS 2007.

⁴¹ For example, due to the unclear language of the umbrella clause in the Switzerland – Philippines BIT, the arbitral tribunal in *SGS v. Philippines*, Decision on Jurisdiction, (ICSID January 29, 2004)., found that contractual breaches are considered treaty breaches for the purposes of ICSID jurisdiction.

⁴² Griffin Weaver, *The Underutilized Foreign Investor*, 5 CREIGHTON INTERNATIONAL AND COMPARATIVE LAW JOURNAL (2013).

⁴³ MOHAMED RAMADY, THE SAUDI ARABIAN ECONOMY: POLITICS, ACHIEVEMENTS, AND CHALLENGES (Springer 2nd ed. 2010).

⁴⁴ Silvano Domenico Orsi, *Arab Spring Brings Winds Of Change To The Maghreb And Mena Region: Does That Spell Opportunity For Infrastructure Development And Project Finance?*, 11 RICHMOND JOURNAL OF GLOBAL LAW & BUSINESS (2011). Also see, Andrew Hill, *Foreign Infrastructure Investment In Chile: The Success Of Public-*

adoption of different policies, or a state's focus on specific sectorial development. A good example of the latter is the increased change of policies, in many countries, to diversify their energy mix and be more reliant on clean and renewable energy sources.⁴⁵

To attract and maintain high levels of FDI, any country should take two steps. The first is to enact a balanced, well-developed and modern legal framework that addresses and incorporates the country's economic development issues and defines the objectives sought from FDI, while at the same time incentivizing foreign investment, and conforming to the international standards of foreign investment protection. The second step is to create investment opportunities that attract foreign investors by focusing on sectorial development and engaging the private sector in the establishment and operation of major and high value public facilities via privatizations and PPPs. The latter can be achieved by incentivizing FDI in particular sectors and offering those investments greater protections to encourage foreign their inflow. This may be furthered by a carefully-developed model BIT.

In the chapters which follow, I investigate and analyze how Jordan can successfully achieve these two steps through its future BIT network, in order to attract and maintain high levels of FDI and reach their economic development objectives. I conclude with a model BIT for Jordan that grounds the findings and recommendations of this thesis in a practical example.

Private Partnerships Through Concessions Contracts, 32 NORTHWESTERN JOURNAL OF INTERNATIONAL LAW AND BUSINESS (2011).

⁴⁵ Xiaodong Wang, *Legal and Policy Frameworks for Renewable Energy to Mitigate Climate Change*, 7 SUSTAINABLE DEVELOPMENT LAW & POLICY (2007).

II. RESEARCH OBJECTIVE

By taking Jordan as an example, I follow an analytical, empirical, and comparative methodology to answer the question: *How can developing countries draft model BITs that balance the protection of foreign investors with the host state's right to economic development?*

Jordan, like other developing countries, must enact a balanced, well-developed and modern legal framework that preserves the country's interests and incorporates its development goals, while at the same time providing incentives to foreign investors, and conforming to international standards of foreign investment protection. This can be achieved via drafting a model BIT for Jordan that takes into account the development challenges and goals of the country and reflects the latest developments in investor-state arbitration.

III. THESIS STRUCTURE:

This thesis will consist of (5) chapters. This chapter (Chapter 1) outlines the research problem, objective, and scope of the thesis. Chapter 2 provides a historical overview of international investment law, its sources, and how this field of law emerged and developed. It traces international investment agreements from their early beginnings in the old Babylonian period (2003-1595 BCE),⁴⁶ until modern time. The historical discussion focuses on the BIT movement and the development of international investment law in the twentieth century. It highlights how international investment agreements, throughout their history and development, have always had

⁴⁶ See ALTMAN. 67 (2012).

two objectives: protection of foreign investment, and enhancing host state development. This is also demonstrated through the historical background and motives behind the adoption of major international conventions that have contributed to the development of international investment law as it exists today. Most notable of these conventions are the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID),⁴⁷ and the Convention Establishing the Multilateral Investment Guarantee Agency (MIGA).⁴⁸

Chapter 3 elaborates on the thesis problem. Basically, whether BITs and their interpretation have equally served the two main purposes of BITs –i.e. investor protection and host state development. Chapter 3 provides evidence that investor protection has won out over host state development.⁴⁹ It illustrates how investor-state arbitration decisions have focused on the protection of investments “to the detriment of the sovereign power and duty of host States to pursue the general interest for their populations of promoting their national development.”⁵⁰ It explains how the failure to achieve host state development from FDI lies in the vague clauses of BITs and their interpretation by investor-state tribunals.⁵¹ Chapter 3 also discusses the different approaches taken by some countries to avoid unintended interpretations in future investor-state arbitrations and clarify their intent.

Chapter 4 offers a comprehensive review of the application and interpretation of different treaty provisions and treatment standards in BITs and in investor-state arbitration. It illustrates

⁴⁷ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965).

⁴⁸ The Convention Establishing the Multilateral Investment Guarantee Agency (1985).

⁴⁹ As one commentator notes “[T]reaty-based investment arbitration – mainly under BITs and NAFTA – has been biased in favour of foreign investors to the detriment of the sovereign power and duty of host States to pursue the general interest for their populations of promoting their national development.” See Tanzi, *THE LAW AND PRACTICE OF INTERNATIONAL COURTS AND TRIBUNALS*, 48 (2012).

⁵⁰ *Id.* at 48.

⁵¹ A recent UNCTAD report concludes -after reviewing different arbitral decisions- that “the outcome of many disputes hinged upon the wording of specific provisions in the applicable IIA.” See *Investor-State Dispute Settlement: Review of Developments in 2016*, at 29 (2017).

how BITs use vague and open-ended language for treatment standards which allows for expansive interpretations. This has resulted in arbitral tribunals expanding the protection of investments to the detriment of host state development. Chapter 4 also provides policy guidelines and recommendations that help developing countries in limiting the possibility of expansive interpretations that go against the host state's interests. These policy guidelines and recommendations are a reflection of the development and interpretation of such provisions and treatment standards by investor-state arbitral tribunals.

Chapter 5 grounds the findings in previous chapters' by applying the recommendations and policy guidelines to a specific country. Jordan is taken as an example of a country that does not have a model BIT designed for its needs and development challenges. Hence, this Chapter analyzes the development challenges in Jordan and demonstrates the role of FDI in overcoming these challenges. It then proposes a set of guidelines and suggested provisions for foreign investment lawmaking which serve as "design criteria" for a model BIT for Jordan. These guidelines and suggested clauses are based on Jordan's development challenges and are intended to ensure economic development through FDI in future BITs. They can serve as a reference point for legislatures and policymakers in formulating future national investment policies and negotiating BITs. Developments in investor-state arbitration regarding the application and interpretation of different treaty provisions are also reflected in these guidelines and suggested clauses.

CHAPTER TWO

THE HISTORY AND DEVELOPMENT OF INTERNATIONAL INVESTMENT LAW

INTRODUCTION

International investment law is a relatively new field of law that falls under the umbrella of international law. It has developed a myriad of principles and norms, mainly from international economic law, to become a distinctive set of legal rules worthy of its own category.¹

International investment law has its roots in international trade practices.² Prior to the emergence of the concept of “investment,” the international flow of capital happened primarily through trade. As merchants conducted business across borders they acquired property in foreign countries in order to create trade establishments.³ This form of acquiring property overseas, and the need to protect it from expropriation, is the foundation from which international investment

¹ RUDOLF DOLZER & CHRISTOPH SCHREUER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* 19 (Oxford University Press 2 ed. 2012).

² Kate Miles, *International Investment Law: Origins, Imperialism and Conceptualizing the Environment*, 21 *COLORADO JOURNAL OF INTERNATIONAL ENVIRONMENTAL LAW AND POLICY* 1 (2010).

³ JESWALD W. SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 13 (Oxford University Press. 2013).

law developed.⁴ Host countries saw this as an opportunity to benefit from the overspills of trade and thus were encouraged to grant protections to foreign merchants.

In order to gain protection for their property, foreign merchants would request guarantees from the sovereign to be treated with favoritism, and be protected.⁵ At the same time, sovereigns took this opportunity to expand foreign trade in their territory and strengthen their relations with groups of foreign territories.⁶ Thus the sovereign would ‘grant’ foreign merchants a ‘concession’ which provided for the protection of the merchant’s property as well as other privileges, such as reduced duty rates and rights of access.⁷ Although these grants were a unilateral act by the sovereign, they constituted the early beginnings of the current investment agreements which contain reciprocal benefits for both the foreign investor and the host country.

As trade relationships developed, traders and investors needed assurance from the sovereign that their property was protected from arbitrary acts. It would render any assurance given by the sovereign useless if, in the event of breach, the investor would have to seek redress through the sovereign’s own legal system. The sovereign who has the power to issue laws, has the power to repeal those laws in its favor when troubled by them.⁸ This explains the need to elevate investors’ claims from the realm of local laws and courts to a supranational and bias free domain, namely international law.

The contemporary practice of investment agreements, which are mostly in the form of bilateral investment treaties (BITs) concluded between two states, serve the goal of elevating

⁴ SORNARAJAH, *THE INTERNATIONAL LAW ON FOREIGN INVESTMENT* 11 (Cambridge University Press 3 ed. 2012).

⁵ JESWALD W. SALACUSE, *THE LAW OF INVESTMENT TREATIES* 89 (Oxford University Press 2 ed. 2015).

⁶ *Id.* at 89.

⁷ *Id.* at 89.

⁸ Thomas Hobbes reasons this principle as follows “*The sovereign of a Commonwealth, be it an assembly or one man, is not subject to the civil laws. For having power to make and repeal laws, he may, when he pleaseth, free himself from that subjection by repealing those laws that trouble him, and making of new; and consequently he was free before. For he is free that can be free when he will.*” See THOMAS HOBBS, *LEVIATHAN* ch. XXVI, at 2 (1651).

foreign investment protection from the host country's legal system to the international sphere. BITs provide foreign investors with substantive treatment standards, and a dispute settlement mechanism that ensures effective enforcement of these treatment standards, to encourage the inflow of FDI and achieve development. The treatment standards consist of a set of international legal principles that give protection to the foreign investor's property from arbitrary acts of the host government, such as expropriation. They also provide how the foreign investor is to be treated while performing his investment activity in the host country. The National Treatment standard ensures that the foreign investor is not discriminated against because of his foreign nationality,⁹ and the Most Favored Nation standard enables the foreign investor to enjoy the more favorable privileges and protections given to other foreign investors.¹⁰

Host countries are bound by the treatment standards offered in a BIT, and are subject to liability if they breach a commitment owed to the foreign investor. If a breach occurs, the foreign investor may invoke the dispute settlement mechanism contained in the investment treaty and resort to an international tribunal which will apply international law principles to the claim. In this manner, the foreign investor avoids the possibility of local bias and inefficiency in the host country's legal system.¹¹

The current investment regime thus offers two layers of protection to foreign investors. The first is the set of international treatment standards which the parties agree on applying in their BIT or investment contract. The second is an effective dispute settlement mechanism if the

⁹ Andrea K. Bjorklund, *National Treatment*, in STANDARDS OF INVESTMENT PROTECTION 29 (August Reinisch ed. 2008).

¹⁰ Andreas R. Ziegler, *Most-Favoured-Nation (MFN) Treatment*, in STANDARDS OF INVESTMENT TREATMENT 60 (August Reinisch ed. 2008).

¹¹ See in general regarding the barriers of recovery by foreign investors in the host country's legal system DON WALLACE JR. CHRISTOPHER DUGAN, NOAH RUBINS, BORZU SABAHI, *INVESTOR-STATE ARBITRATION* 13-18 (Oxford University Press. 2008).

host country breaches an obligation owed to a foreign investor. This dispute settlement usually occurs through arbitration under the auspices of the International Center for the Settlement of Investment Disputes (ICSID),¹² which is a dedicated Center for the settlement of investor-state disputes.

Although foreign investment law emerged from early trade practice, international investment law is now a field of its own dedicated to the protection of “investments” and “foreign investors” for economic growth of host countries. Therefore, it is essential to recognize the dual objective of modern investment treaties; providing protection to foreign investors to encourage their inflow, and consequently achieve economic development for the host state. However, to better understand the current investment regime and the dual objective of modern investment treaties, an understanding of the historical evolution of the current regime is helpful.

In this Chapter, I will provide that historical background to the current international investment regime. I will trace, in chronological sequence, the development of this field of law from its early beginnings, moving through the major development milestones, to its current state of affairs. I will identify the main sources of investment law, including the principal treaties that shape the current regime. Throughout the discussion, I will illustrate how the international regime governing FDI was built on development and economic growth of countries, along with investment protection to encourage its mobility into developing countries.

¹² Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965).

I. THE HISTORICAL EVOLUTION OF INTERNATIONAL INVESTMENT LAW

A. EARLY DEVELOPMENTS

The history of international investment law before the second half of the eighteenth century is not extensive.¹³ The term “investment” itself was not known in the English language until 1615.¹⁴ Trade was the dominant means of international flow of capital and goods in earlier times. Therefore most international treaties at that time were concerned with establishing and maintaining trade relationships.¹⁵ Nonetheless early trade treaties introduced many of the concepts and principles of the current international investment law regime.

Early trade treaties established the norm of protection of foreigners and their property in the host country. They contained an assurance from the sovereign that foreign merchants trading in his territory are protected from negative actions of the sovereign and local individuals.¹⁶ This section will provide highlights and examples of how international investment law originated and developed from international trade in early history.

¹³ LLUÍS PARADELL ANDREW NEWCOMBE, *LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT* 3 (Kluwer Law International, 2009). See also Lucja Nowak, *Kenneth J. Vandeveld, Bilateral Investment Treaties, History, Policy, and Interpretation, Oxford University Press, 2010 (Book Review)*, POLISH YEARBOOK OF INTERNATIONAL LAW 318 (2010).

¹⁴ The first known use of the word “investment” was in 1615. It was used specifically in the East India trade, to imply “*the employment of money in the purchase of Indian goods.*” It was not until 1740 when the term “investment” was used to mean “*the conversion of money or circulating capital into some species of property from which an income or profit is expected to be derived in the ordinary course of trade or business.*” See OXFORD ENGLISH DICTIONARY, “INVESTMENT, N.” (Oxford University Press.). <http://www.oed.com/view/Entry/99052?redirectedFrom=investment>

¹⁵ Kenneth J. Vandeveld, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 158 (2005).

¹⁶ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 332 (Oxford University Press, 2013).

1. The BCE Era: The Assyrian Example (2003-1595 BCE)

A good example of early trade treaties containing treatment standards similar to the current treatment standards are the treaties between the City of Ashur (Syria) and Kültepe (Turkey). These treaties date back to the old Babylonian period (2003-1595 BCE).¹⁷ In one of these treaties, the City of Ashur agreed with an unknown Ruler of Kültepe (Turkey) that he would safeguard Assyrian merchants' interests, among other matters, while trading in his territory. The treaty is in the form of an oath, taken by the Ruler and his dignitaries,¹⁸ where the Ruler and his dignitaries promised protection and trade routes to Assyrian merchants. In exchange for this protection, the Ruler was entitled to duty rates in silver and tin. The oath provided that the Ruler and his dignitaries would be killed if they failed to comply with their oath, which was:

There shall be no loss (of property belonging) to an Assyrian in your country, rope, peg or anything. If there occurs a loss in your country you shall search (the lost object) and you shall return it to us. If there occurs blood (shed) in your country you shall hand over the killers to us and we shall kill (them)... You shall not demand anything from us. Just like your father you may take 12 shekels of tin per (donkey) from a caravan on its way to Kaniš. You may consume, like your father, 1 1/4 shekels of silver per donkey from a return caravan. You shall not take anything in excess (of this)... He raised his hand towards (the gods) Aššur and Adad, to the Netherworld and to the spirits of his ancestors, he ... his table and his chair ... and he filled his cup and then emptied it; the ruler said: ... And

¹⁷ These are three commercial treaties concluded by the city of Ashur with the kings of Kaniš and Ḫaḫḫum, and of a city whose name was not preserved. See AMNON ALTMAN, TRACING THE EARLIEST RECORDED CONCEPTS OF INTERNATIONAL LAW: THE ANCIENT NEAR EAST (2500–330 BCE) § 8, at 67 (Randall Lesaffer ed., Martinus Nijhoff Publishers. 2012).

¹⁸ During the Babylonian era, treaties were concluded in two ways; either in writing, or by oath. If the treaty was concluded via an oath, the political heads of both contracting parties would get together and discuss the terms of the treaty. When an agreement is reached, certain rituals took place, “*in which an animal (a donkey is usually attested) was slaughtered, and the parties smeared its(?) blood. The parties then exchanged oaths regarding the terms of the agreement in front of the divine statues or symbols brought to the meeting for this purpose. A festive drinking (of the blood?) and exchange of gifts concluded the ceremony.*” For more details about treaty making and their rituals in the Babylonian era see id. at 69-75.

they (i.e. his dignitaries) said: “if we reject your sworn treaty our blood shall be shed like (the contents of) the cup!”¹⁹

Other treaties between Assyrians and Kültepe go even further to provide for the protection of movable and immovable assets of Assyrian merchants. These treaties provide that Assyrian merchants’ assets are not to be expropriated, or taken in payment of a lower price.²⁰ In case of dispute between an Assyrian and a local citizen the local ruler shall pass honest judgment on them. They also provided for the duty of the sovereign to secure the caravan road passing through his territory, as well as securing the water routes in the regions where river transportation was carried out. Any loss to Assyrian freight passing through designated trade routes is to be fully compensated by the sovereign.²¹ In exchange for these favorable rights and privileges, the Assyrian merchants would pay the kings and rulers of these territories taxes and duties.

It is clear from these treaties that Assyrians wanted to conduct their business in foreign territories with minimal risk. This is identical to what modern investors seek; minimal risk and preferential treatment in foreign countries. Commentators observe that Assyrians made treaties with the kings and rulers of other territories to get: i) protection and resident’s rights, ii) extraterritorial rights so that the foreign territories were in a sense political and juridical extensions of the city government of Ashur, and iii) protection of the roads and guarantees against losses due to robbery and other acts of the locals.²² These goals are similar to what the current BIT system offers to foreign investors. The international standards of treatment contained

¹⁹ The English translation adopted here is that of J.G. Dercksen, as in his “editor’s note” in the article of Günbatti 1994: p. 250, note 8. Cited by id. at 76.

²⁰ Id. at 76.

²¹ Id. at 76.

²² Id. at 75-78.

in BITs now, such as; national treatment, full protection and security, protection against expropriation, and elevating foreign investors from the local legal system to the international domain, are reflections of the ancient trade treaties concluded by the Assyrians with foreign territories. However, today foreign investors are given incentives, such as tax breaks and tax reduction, to encourage their investment in the host country. In the Assyrian treaties, foreign investors had to pay (in the form of duty rates) for the protection they receive. This is due to the historical attitude towards foreigners, who were always regarded with suspicion, if not fear, due to their differences from the native people.²³ The general attitude towards foreigners was hostility. Therefore it was only by agreements concluded with the sovereign, along with the payment of duties, that protection could be secured.

In the modern era, the effect of globalization has changed, to a large degree, the historically suspicious view of foreigners based on their difference. The hostility of some countries towards foreign investors in modern times is based on the fear of being exploited and harmed by foreign investors. This belief stems from the past experiences of developing countries which were dominated and exploited by the developed world. The effect of previous experiences on the attitude of some developing countries towards foreign investments will be dealt with below.

²³ Dharmendra Chatur, *Responsibility of States for Injury to Aliens*, From the Selected Works of Dharmendra Chatur KING & PARTRIDGE 7 (2009).

2. The Middle Ages

Some commentators attribute the origins of international investment law to trade treaties concluded by European countries during the Middle Ages.²⁴ As seen in the Assyrian treaties above, however, such a statement may be inaccurate. The treaties of the Middle Ages show that rulers and states understood the reciprocal benefits that result from protecting foreign traders in their territories. Thus the notion of using trade as a tool for development in the host country appeared and was explicitly mentioned in the trade agreements of this period.

The guarantees of protection during the Middle Ages were often in the form of a unilateral “grant” or “concession” issued by the sovereign in a written document.²⁵ Various European sovereigns granted protection to foreigners using these grants. For example, in 991 AD the Byzantine Emperors Constantine VIII and Basil II granted the merchants of Venice rights to trade in their territory at reduced tax rates, protection, and a building (*domo*) in which to do business.²⁶ This grant by the Emperors was found in the form of a written document called “*chrysobull*.” The grant included the right of Venetian merchants to trade in the ports of the Byzantine Empire, as well as the right to “a quarter in the Constantinople, known as an *embolum*, for dwelling and trading.”²⁷

²⁴ See CHARLES LIPSON, *STANDING GUARD: PROTECTING FOREIGN CAPITAL IN THE NINETEENTH AND TWENTIETH CENTURIES* 11-12 (University of California Press. 1985). Also see Miles, 21 *COLORADO JOURNAL OF INTERNATIONAL ENVIRONMENTAL LAW AND POLICY* 3 (2010).

²⁵ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 332 (Oxford University Press. 2013).

²⁶ OLIVIA REMIE CONSTABLE, *HOUSING THE STRANGER IN THE MEDITERRANEAN WORLD: LODGING, TRADE, AND TRAVEL IN LATE ANTIQUITY AND THE MIDDLE AGES* 152-53 (Cambridge University Press. 2009).

²⁷ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 333 (Oxford University Press. 2013).

Another example of such grants was that given by the English King Henry II to German merchants in 1157 AD, providing protection of the German merchants' lives and property in London.²⁸ The purpose was mainly to encourage the inflow of German traders into England, which would reflect positively on the English economy.

Many other European countries started to realize the importance, and reciprocal benefits, of foreign trade and investment to their own economies. Therefore trade agreements were concluded in many parts Europe.²⁹ The grant issued by King Eric of Norway to the Hamburg merchants in 1296 AD explicitly articulated this goal. In his grant the Norwegian King granted the merchants of Hamburg extensive privileges and protection, for the purpose of “*the amelioration of our territories through trade.*”³⁰

Trade treaties of the Middle Ages also established the second main purpose of investment agreements, which is enhancing development of the host country, along with protection of outbound merchants and investors. These reciprocal benefits to both treaty parties accelerated and encouraged the conclusion of more detailed trade treaties in the sixteenth, and seventeenth centuries.

²⁸ Id. at 333.

²⁹ For a general discussion of the European role in the creation of International Investment law see Miles, 21 COLORADO JOURNAL OF INTERNATIONAL ENVIRONMENTAL LAW AND POLICY (2010).

³⁰ The original text stated “*ad meliorandum terran nostrum cum mercaturis*”, the English translation above is taken from SALACUSE, THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL 333 (Oxford University Press. 2013).

B. DEVELOPMENTS IN THE SIXTEENTH, SEVENTEENTH, AND EIGHTEENTH CENTURIES

As Europe emerged from the middle Ages, the new European countries acted in various ways to protect and advance the interests of their nationals in other countries. To that end, they negotiated trade and commerce treaties that regulated trans-border economic activity.³¹ This resulted in a series of bilateral treaties that would later become the basis for protection of aliens and their property. These treaties provided for national treatment, protection of property, and most-favored-nation treatment, along with other protections including access to courts, forming the base of the current investment protection regime.

Article VII of the Peace Treaty between Spain and the Netherlands in 1648 (also known as the *Peace of Münster*), provided for national treatment of aliens in both countries. It reads “*The Subjects and Inhabitants of the Lands of the aforementioned Lords King [Spain] and States [the Netherlands], trading in each other's Lands, shall not be required to pay more duties and imposts than the other side's own Subjects.*”³² The treaty also provided for the protection of aliens and their property in the host country, “*They [the subjects of each country] shall also be permitted to enter and remain in each other's lands and there conduct their business and trade in full security, on the sea, in other waters, as well as on land.*”³³ The parties of this treaty gave freedom of entry to the nationals of the other party, and undertakings not to interfere with their business: “*... commerce among the respective Subjects shall not be interfered with, and if any*

³¹ Id. at 333.

³² The text of the Peace of Münster was translated by Herbert H. Rowen, ed., *The Low Countries in Early Modern Times: A Documentary History 179-87* (New York, 1972), <http://www1.umassd.edu/euro/resources/dutchrep/14.pdf>

³³ Article IV of the Peace Treaty between Spain and the Netherlands (1648).

such interference occurs, it shall be removed in fact and deed.”³⁴ The treaty also provided for most-favored-nation treatment,³⁵ as Dutch merchants were accorded no less favorable treatment than that offered to English and Hanseatic merchants in Spain.³⁶

By the end of the seventeenth century most European countries had entered into economic agreements with other European countries.³⁷ Economic treaties came to be seen as a tool to spread European dominance and influence outside of Europe. Hence European countries would start concluding economic treaties with less developed countries, mainly in the Far-East Asia and the Middle East.³⁸ However these treaties differed from the ones concluded between European countries. The treaties between European countries offered equal rights to the nationals of each state. The new treaties with the developing world, although purporting to be of mutual benefit, were *de facto* “unequal” and “non-reciprocal.”³⁹ These new treaties granted non-reciprocal privileges and “extraterritorial jurisdiction” to the nationals of the European country trading in the territory of the less developed party.⁴⁰

The practice of concluding unequal and non-reciprocal agreements started with the Ottoman Empire, creating what became to be called the “capitulary system.”⁴¹ The first capitulary treaty was signed between King Francis I of France and the Ottoman Sultan Suleiman

³⁴ Article XI of the Peace Treaty between Spain and the Netherlands (1648).

³⁵ One of the earliest bilateral treaties that employed the term “most-favored-nation” was the Trade Treaty of Nijmwegan of 1679 between Sweden and Holland. H NEUFELD, *THE INTERNATIONAL PROTECTION OF PRIVATE CREDITORS FROM THE TREATIES OF WESTPHALIA TO THE CONGRESS OF VIENNA (1648-1815): A CONTRIBUTION TO THE HISTORY OF THE LAW OF NATIONS* 29 & 110 (Sijthoff. 1971).

³⁶ Articles XVI and XVII of the Peace Treaty between Spain and the Netherlands (1648).

³⁷ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 90 (Oxford University Press 2 ed. 2015).

³⁸ *Id.* at 90.

³⁹ *Id.* at 90.

⁴⁰ The term “extraterritorial jurisdiction” allowed foreign powers to apply their laws to their nationals in foreign states. See ANDREW NEWCOMBE, 11 (Kluwer Law International. 2009).

⁴¹ James B. Angell, *The Turkish Capitulations*, 6 *THE AMERICAN HISTORICAL REVIEW* 254 (1901).

I in 1535.⁴² This treaty gave French merchants in the Ottoman Empire privileges which included exemption from taxes and duties,⁴³ and extraterritorial jurisdiction. French judges were to hear the civil and criminal affairs of French subjects in the Ottoman Empire and apply French law to them.⁴⁴ Since then, other European countries obtained similar privileges, as those of “the Franks”, for their nationals trading in the Ottoman Empire.⁴⁵ England entered its capitulatory treaty in 1583,⁴⁶ the Netherlands in 1609, and Austria in 1615.⁴⁷

The capitulation system spread widely in the seventeenth, eighteenth and early nineteenth centuries, when traders from the West were spreading Western influence in non-Western and less developed countries by a process of infiltration rather than by annexation.⁴⁸ The extensive privileges and extraterritorial jurisdiction enjoyed by the Europeans under the capitulatory treaties created *imperium in imperio* in the Ottoman Empire, thus encouraging European countries to implement the capitulatory system in other parts of the world.

The Sino-British Supplementary Treaty of 1843 is an example of this extension of the capitulatory system.⁴⁹ This treaty granted the British subjects in China the right of extraterritoriality. It also established British courts on Chinese soil, where British subjects are to

⁴² It seems to have been in form, not a treaty, but a unilateral document, a grant or concession by the Sultan to his friend, the King of France. See *id.* at 254.

⁴³ “The substance of the treaty in the chief Capitulations was as follows: The Franks [French] were to have the liberty to travel in all parts of the Ottoman Empire. They were to carry on trade according to their own laws and usages. They were to have liberty of worship. They were to be free from all duties save customs duties. They were to enjoy inviolability of domicile.” See *id.* at 256.

⁴⁴ *Id.* at 256.

⁴⁵ *Id.* at 256.

⁴⁶ Queen Elizabeth of England attempted to sign a capitulatory treaty with the Ottoman Sultan in 1579. The Queen tried to persuade the Sultan to sign the treaty by reminding him that she, and her subjects, like him, reject the worship of images. The Queen’s effort to convince that Sultan to sign the treaty by showing the resemblance between Protestantism and Islam did not come to avail. *Id.* at 256.

⁴⁷ *Id.* at 256.

⁴⁸ Encyclopedia Britannica website, Capitulation, <https://www.britannica.com/topic/capitulation>

⁴⁹ Also called The British Supplementary Treaty of the Bogue (1843). More information about this treaty can be found at <https://www.britannica.com/biography/Qiying#ref251418>

be tried. The treaty granted the British “most-favored-nation” treatment, which promised that any concession granted later to other foreign powers would also then be granted to the British.⁵⁰ The treaty did not give any corresponding rights to Chinese residents in England.⁵¹ In 1844 China signed similar treaties with the United States and France, and in 1847 with Sweden and Norway.⁵²

After the end of the colonial era, most capitulation treaties ended. However, their exploitive and unequal nature would not be quickly forgotten by developing countries. The scare left from their injustice would carry on to modern times, when developing countries became skeptical about foreign investment.⁵³ It would be safe to conclude that developing countries, reflecting on their past experiences, saw modern investment agreements as instruments for exploitation by Western countries similar to the capitulation treaties. It can also be said that developing countries in modern times, which had recently gained their independence from colonial powers, were fearful that investment treaties are a tool for economic and political dominance; a threat to their recently acquired sovereignty.

⁵⁰ Encyclopedia Britannica website, Qiying – Chinese Official, <https://www.britannica.com/biography/Qiying#ref251418>

⁵¹ SALACUSE, THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL 334 n.20 (Oxford University Press. 2013).

⁵² Encyclopedia Britannica website, Qiying – Chinese Official, <https://www.britannica.com/biography/Qiying#ref251418>

⁵³ The different attitudes towards foreign investment in the modern era will be discussed later in this Chapter.

C. DEVELOPMENTS IN THE EIGHTEENTH, NINETEENTH, AND TWENTIETH CENTURIES

1. The Colonial Era (1700-Early 1900)

The Industrial Revolution, which began in England near the end of the eighteenth century, gradually transformed the industrial life of all the Western countries and played an important role in the expansion of Western countries through colonialism.⁵⁴ Industrialized countries needed markets for their machine-made products, and they also needed resources and materials for their growing industrial sector.⁵⁵ This need for new markets and resources encouraged the newly industrialized countries, mainly in Europe, to adopt a policy of annexation, or colonization, of territories in different parts of the globe, particularly in Africa, Asia, and South America.⁵⁶ Hence foreign investment, during the eighteenth and nineteenth centuries, was made mainly through the context of colonial expansion.⁵⁷

Colonized countries were an extension of the political and legal systems of the colonizing countries. Therefore investors did not need special protection for their property in the colonized country. They were, *de facto*, investing under their own legal and political systems.⁵⁸ Hence investment and trade treaties with the colonized countries were not needed. As for developing countries that were not colonized, a blend of force and diplomacy by the concerned developed

⁵⁴ Encyclopedia Britannica website, Western Colonialism, <https://www.britannica.com/topic/colonialism>

⁵⁵ PHILIP VAN NESS MYERS, MEDIAEVAL AND MODERN HISTORY 251-74 (Ginn and Company. 1905). Excerpts of the book can be found at http://www.shsu.edu/~his_ncp/EurImp.html

⁵⁶ *Id.* at 251-74.

⁵⁷ M. SORNARJAH, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT 19 (Cambridge University Press 3 ed. 2012).

⁵⁸ Vandeveld, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 158 (2005).

country ensured that the rights of its subjects were not infringed.⁵⁹ Some non-colonized countries were forced to sign treaties that gave European investors the right to be governed by their home country laws.⁶⁰ At the same time, developed countries were negotiating treaties among themselves that gave treaty parties greater equality, unlike the treaties concluded with less developed countries.⁶¹ The United States followed the path of concluding treaties with developed countries, these treaties were known as treaties of Friendship, Commerce and Navigation (FCN).⁶²

Modern investment treaties in their current form and content can be traced to the treaties of Friendship, Commerce and Navigation concluded by the United States in the eighteenth, and early nineteenth centuries. Although these treaties were they shifted through time to include investment protection, and later became the basis for investment treaties in the modern era.⁶³ Thus it is important to examine the evolution of FCN treaties in order to understand how the current BIT system evolved.

2. The American Treaties of Friendship, Commerce and Navigation

The United States concluded a series of bilateral treaties with other developed countries known as treaties of Friendship, Commerce and Navigation. The first FCN treaty was concluded with

⁵⁹ SORNARAJAH, 20 (Cambridge University Press 3 ed. 2012). See also SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 335 (Oxford University Press. 2013).

⁶⁰ SORNARAJAH, 20 (Cambridge University Press 3 ed. 2012).

⁶¹ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 335 (Oxford University Press. 2013).

⁶² For a detailed discussion about FCNs see *The Treaty of Friendship, Commerce and Navigation in the Modern Era*, 51 *COLUMBIA JOURNAL OF TRANSNATIONAL LAW* 302 (2013).

⁶³ *Id.* at 307-11. See also RONALD A. BRAND, *FUNDAMENTALS OF INTERNATIONAL BUSINESS TRANSACTIONS § II*, at 713-16 (Center for International Legal Education – University of Pittsburgh School of Law. 2015).

France in 1778,⁶⁴ and over the course of the next decade the United States would enter into additional FCN treaties with the Netherlands (in 1782), Sweden (in 1783) and Prussia (in 1785).⁶⁵ In 1815, an FCN treaty was signed with Great Britain, a treaty that is still in force today.⁶⁶ These treaties dealt with trade and diplomatic relations between the parties.⁶⁷ They contained MFN clauses for trade and navigation, and provided for very broad and “absolute” provisions that protected foreign ownership of property.⁶⁸ European states concluded similar treaties starting from the 1820’s, which dealt with matters relating to establishment, trade, and double taxation.⁶⁹

Starting from the mid-nineteenth century, the United States entered into FCN treaties with developing countries. These treaties escalated the level of protection for foreign owned property from the “national treatment” norm to a higher level. They required the host country to afford foreign investors with “special protection,” “full and perfect protection,” or “the most complete security and protection” to their property.⁷⁰ The protection to foreign ownership of property under these FCN treaties was restricted to those engaged in commercial activities, i.e. merchants and traders.⁷¹ For example, the 1903 U.S.-Ethiopia FCN treaty promised protection to

⁶⁴ *The Treaty of Friendship, Commerce and Navigation in the Modern Era*, 51 COLUMBIA JOURNAL OF TRANSNATIONAL LAW 302, 307 (2013).

⁶⁵ *Id.* at 307.

⁶⁶ *Id.* at 307.

⁶⁷ BRAND, § II, at 713 (Center for International Legal Education – University of Pittsburgh School of Law. 2015).

⁶⁸ *Id.* at 713. See also SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 336 (Oxford University Press. 2013).

⁶⁹ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 336 (Oxford University Press. 2013). See also KENNETH J. VANDELDE, *BILATERAL INVESTMENT TREATIES: HISTORY, POLICY, AND INTERPRETATION* (Oxford University Press. 2010).

⁷⁰ KENNETH J. VANDELDE, *UNITED STATES INVESTMENT TREATIES : POLICY AND PRACTICE* 15 (Kluwer Law and Taxation. 1992).

⁷¹ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 336 (Oxford University Press. 2013).

“those engaged in business and of their property.”⁷² Although the extent of protection was not explicitly mentioned in these treaties, they did implicitly require that foreign persons, and their property, are entitled to a minimum of respect and protection regardless of what the municipal law offers.⁷³ Thus, although FCN treaties were concerned with the protection of property rather than investment,⁷⁴ they did help in the formation of a new treatment standard for foreign investors; that is the “international minimum standard.”

FCN treaties also dealt with dispute resolution. The early FNC’s provided for dispute resolution between the injured foreigner and the host country through local courts. The foreigner was entitled to national treatment before the courts of the host country and the right to appoint a counsel of his choice. FCN treaties also provided for dispute settlement through arbitral tribunals between the state parties, including matters related to the confiscation of property.⁷⁵ However FCN treaties signed in the nineteenth century only provided arbitration for claims existing at the time of entry into the FCN treaty. Thus, FCN treaties of this time did not include any clause or method for settlement of disputes through binding third party procedures.⁷⁶

The move towards the use of FNC treaties by the United States had a major impact on the formation of international investment law as we know it today. They introduced the concept of bilateral agreements between two sovereign states that offered equal rights to its parties, contrary to the capitulatory system and former agreements which were exploitive of the weaker party. They

⁷² A Benton, *The Protection of Property Rights in Commercial Treaties of the United States*, 25 ZEITSCHRIFT FÜR AUSLÄNDISCHES ÖFFENTLICHES RECHT UND VÖLKERRECHT 50 (1965).

⁷³ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 336 (Oxford University Press. 2013).

⁷⁴ Vandeveld, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 159 (2005).

⁷⁵ The FCN Treaty between the U.S and Spain signed in 1795 provided for arbitration of claims by U.S. citizens for losses caused by Spain in its war with France. See VANDEVELDE, *BILATERAL INVESTMENT TREATIES: HISTORY, POLICY, AND INTERPRETATION* (Oxford University Press. 2010).

⁷⁶ *Id.* at n.40.

also introduced the international minimum standard of treatment, which was an innovative standard, to protect American interests abroad, especially in less developed countries where the rule of law and the administration of justice might be ineffective or inefficient.

The international minimum standard was later adopted by other developed countries in their treaties. European countries found the international minimum standard to be a convenient standard to adopt for the same reasons the Americans did. The international minimum standard later became recognized as a rule of customary international law.⁷⁷ However, developing countries resisted its application and challenged its existence as a rule of customary international law, and insisted on maintaining the national treatment standard which was incorporated in their constitutions.⁷⁸ To illustrate the controversy between developed and developing states on the question of treatment of aliens, it is important to discuss the concept of state responsibility for injuries to aliens. This concept is universally recognized, however, controversy arose in the second half of the nineteenth century as to when state responsibility to aliens arises. This responsibility depends on the standard of treatment which international law obliges that state to adopt.

3. State Responsibility for Injuries to Aliens

The rules of state responsibility for injuries to aliens is a body of international law which seeks to establish a standard of treatment to aliens who enter states for various reasons, including for the

⁷⁷ SORNARAJAH, 122 (Cambridge University Press 3 ed. 2012).

⁷⁸ *Id.* at 122.

purpose of doing business.⁷⁹ The host state is held liable when it breaches the treatment standard owed to aliens on its soil or fails to protect them from injury. Therefore a state is under an international obligation not to improperly treat foreign nationals residing on their soil. Violation of this obligation will incur international responsibility on the part of the host state.⁸⁰

The theory on which liability of the host state for injuries to aliens rests is the “mediate rule.” Under this rule, an alien is seen as a medium of his home country in the host state, thus making an injury to the alien an indirect injury to his home country. The mediate rule is the invention of the Swiss philosopher, diplomat, and jurist, Emerich de Vattel (1714-1767).⁸¹ In his writings, Vattel encouraged countries to adopt the mediate rule to protect their citizens abroad.⁸² Vattel declared that “whoever uses a citizen ill, indirectly offends the state, which is bound to protect this citizen; and the sovereign of the latter should avenge his wrongs, punish the aggressor, and, if possible, oblige him to make full reparation.”⁸³

According to Vattel’s theory, the home country may take measures against the host country if the host country breaches the standard of treatment owed to the home country’s citizen. These measures can range from the use of diplomacy – to remedy the injury through what is known as diplomatic protection – to international adjudication, or even the use of military force against the injuring country.

The Permanent Court of Justice explained the mediate rule as follows:

⁷⁹ *Id.* at 120-21.

⁸⁰ Chatur, *From the Selected Works of Dharmendra Chatur KING & PARTRIDGE* 7 (2009).

⁸¹ Emerich de Vattel, *The Law of Nations*, Book II, Chapter VI. Translated and Edited by Béla Kaposy and Richard Whitmore (2008), Liberty Fund. Can be found on http://lf-oll.s3.amazonaws.com/titles/2246/Vattel_1519_EBk_v6.0.pdf

⁸² *Id.* (Vattel) at 198.

⁸³ Emerich de Vattel, *The Law of Nations*, Book II, Chapter VI. Translated and Edited by Béla Kaposy and Richard Whitmore 198 (2008), Liberty Fund. Translation found on http://lf-oll.s3.amazonaws.com/titles/2246/Vattel_1519_EBk_v6.0.pdf

[I]n taking up the case of one of its nationals, by resorting to diplomatic action or international judicial proceedings on his behalf, a State is in reality asserting its own right, the right to ensure in the person of its nationals respect for the rules of international law. This right is necessarily limited to intervention on behalf of its own nationals because, in the absence of a special agreement, it is the bond of nationality between the State and the individual which alone confers upon the State the right of diplomatic protection, and it is as a part of the function of diplomatic protection that the right to take up a claim and to ensure respect for the rules of international law must be envisaged.⁸⁴

Although there was universal recognition on state responsibility for injuries to aliens, controversy arose in the second half of the nineteenth century as to when this responsibility arises. Whether a state is internationally responsible for its treatment to foreigners depends on the standard of treatment which international law obliges that state to adopt. The standard of treatment that should be afforded to aliens, which raises liability when breached, was the subject of considerable debate between capital importing and capital exporting countries.⁸⁵ This debate reflected the different political, economic, and social backgrounds of states, especially on matters related to state sovereignty, protection of national resources, and treatment of aliens.

Capital exporting countries favored an international minimum standard of treatment, which elevates the protection of foreign investors from the host country's local law, to an internationally accepted threshold of treatment that the host country must maintain with aliens.⁸⁶ Capital importing countries on the other hand, maintained the national treatment standard, where aliens are subject to the protection offered in the host country's municipal laws, in equality with the nationals of the host country.⁸⁷

⁸⁴ THE PANEVEZYS-SALDUTISKIS RAILWAY CASE (1939), Series A. /B, 16 (Permanent Court Of International Justice).

⁸⁵ Hussein Haeri, *A Tale of Two Standards: 'Fair and Equitable Treatment' and the Minimum Standard in International Law* 27 ARBITRATION INTERNATIONAL 27, 28 (2011).

⁸⁶ Alireza Falsafi, *Common Good and the Concept of Expropriation in International Law on Foreign Investment: Determinacy of Substance in Legitimacy of Structure* 203 (2010) McGill University).

⁸⁷ *Id.* at 201.

a. The International Minimum Standard vs The Doctrine of Equality Before the advent of an international minimum standard, the doctrine of equality was the dominant standard of treatment for aliens and their property. Under this doctrine the host state's international obligation towards the treatment of aliens and their property is fulfilled once aliens receive "treatment equal to that accorded to the nationals of the host state."⁸⁸ In other words, the standard of treatment under this doctrine was "national treatment." The treaties entered into by developed European countries in the seventeenth and eighteenth centuries offered national treatment to aliens from other European countries.⁸⁹

However in the nineteenth century, when developed countries gave up their colonies and the era of industrialization and globalization began, national treatment became ineffective in protecting the rights and property of aliens in host countries. The need for clear protection rules for outbound investors reached its peak, especially for those foreign investors in less developed countries. This was due to the fact that the legal and judicial systems of many developing countries were neither independent nor efficient. As described by the American Secretary of State, Elihu Root, "[t]he judges are removable at will; they are not superior, as they ought to be, to local prejudices and passions, and their organization does not afford to the foreigner the same degree of impartiality which is afforded to citizens of the country, or which is required by the common standard of justice obtaining throughout the civilized world."⁹⁰ Another reason was the need to protect the life and liberty of aliens' in situations of turmoil that frequently occurred in

⁸⁸ Id. at 201.

⁸⁹ See SORNARAJAH, 125 (Cambridge University Press 3 ed. 2012).

⁹⁰ Elihu Root, *The Basis of Protection to Citizens Residing Abroad*, 4 THE AMERICAN JOURNAL OF INTERNATIONAL LAW 526 (1910).

some developing countries.⁹¹ Thus there emerged a need for capital exporting countries to structure a new system of protection for their outbound investors. This required a higher standard of treatment than national treatment.

The International Minimum Standard Led by the United States, capital exporting countries advocated that aliens must be treated according to an international minimum standard. This standard of treatment is really a set of international legal principles recognized by developed countries, or the “civilized countries”, which set a “threshold” of treatment of aliens. If the host country’s legal system is below that internationally recognized “threshold” then that host country must maintain the international standard of treatment. In 1910, U.S. Secretary of State, Elihu Root, explained the international minimum standard, by stating:

*There is a standard of justice very simple, very fundamental, and of such general acceptance by all civilized countries as to form a part of the international law of the world. ... If any country’s system of law and administration does not conform to that standard, although the people of the country may be content to live under it, no other country can be compelled to accept it as furnishing a satisfactory measure of treatment of its citizens.*⁹²

The international minimum standard came to externalize the legal regime governing foreign investors only when the municipal legal system of the host country is below the international threshold of justice.⁹³ It is only when there is no hope to obtain justice from the laws and tribunals of the host country that an international standard applies and externalizes the legal regime governing the foreign investor. Otherwise the alien is subject to the laws and courts

⁹¹ SORNARAJAH, 123 (Cambridge University Press 3 ed. 2012).

⁹² Root, 4 THE AMERICAN JOURNAL OF INTERNATIONAL LAW 521-22 (1910).

⁹³ Falsafi, § D.C.L 203 (McGill University 2010).

of the host country. In 1850 Lord Palmerston spoke to the House of Commons in relation to the Don Pacifico Case,⁹⁴ and explained when the international minimum standard applies:

If our subjects abroad have complaints against individuals, or against the government of a foreign country, if the courts of law of that country can afford them redress, then, no doubt, to those courts of justice the British subject ought in the first instance to apply; and it is only on a denial of justice, or upon decisions manifestly unjust, that the British Government should be called upon to interfere. But there may be cases in which no confidence can be placed in the tribunals, those tribunals being, from their composition and nature, not of a character to inspire any hope of obtaining justice from them.

I say, then, that our doctrine is, that, in the first instance, redress should be sought from the law courts of the country; but that in cases where redress can not be so had – and those cases are many – to confine a British subject to that remedy only, would be to deprive him of the protection which he is entitled to receive.⁹⁵

The international minimum standard also gave foreign investors the right to seek dispute resolution before an international tribunal, if the remedies provided by the host state proved inadequate.⁹⁶ The home government, under this standard, may also intervene by way of diplomatic protection if the rights of its citizen have been infringed by the host government.⁹⁷

However the exercise of diplomatic protection by the host government should not be abused. The Venezuelan Claims Commission of 1885 commented on this issue by stating:

Strong and powerful governments must not take advantage of their superiority and exaggerate the duty of protection by exercising pressure upon weak

⁹⁴ “David Pacifico (known as Don Pacifico) was a Portuguese Jew who, having been born in Gibraltar in 1784, was a British subject. After serving as Portuguese consul in Morocco (1835–37) and then as consul-general in Greece, he settled in Athens as a merchant. In 1847 his house was burned down in an anti-Semitic riot, the police standing quietly by. Pacifico demanded compensation from the Greek government and was supported by Britain’s foreign secretary, Lord Palmerston. Palmerston sent a naval squadron to blockade the Greek coast (January 1850) and force the Greeks to meet Pacifico’s demands. This brought protests from the French and the Russians, with whom Britain shared a protectorate of Greece. Nevertheless, the Greeks acceded to the payment of £4,000, though, because of the loss of some papers, a commission awarded Pacifico only £150. He moved to London, where he died on April 12, 1854.” For more information see: Don Pacifico Affair – Encyclopedia Britannica, <https://www.britannica.com/event/Don-Pacifico-affair>

⁹⁵ Lord Palmerston speech to the House of Commons, quoted in Root, 4 THE AMERICAN JOURNAL OF INTERNATIONAL LAW 522 (1910).

⁹⁶ SORNARAJAH, 36 (Cambridge University Press 3 ed. 2012).

⁹⁷ Id. at 36.

*governments, in order to compel them to favor their citizens and exempt them from certain obligations or grant them privileges of any nature whatsoever.*⁹⁸

On the other hand, capital importing countries – mainly in Latin America – refused to apply the international minimum standard of treatment on foreign investors. These countries, which had recently gained their independence from colonial powers, were striving to encourage foreign investment in their economies.⁹⁹ To encourage foreign investment, the constitutions of these new countries' promised foreigners equality of treatment with nationals, along with other investment protection rights.¹⁰⁰ Latin American countries upheld that aliens are entitled to treatment not less, but also not better, than that afforded to the citizens of the host country.¹⁰¹ This maintained the “doctrine of equality”, which also became known as the Calvo doctrine, as the standard of treatment of aliens in developing countries.¹⁰²

The Doctrine of Equality Under this doctrine, relying on the principle of state sovereignty, no alien has the right to own property in a country other than his own.¹⁰³ Therefore an alien needs

⁹⁸ JACKSON HARVEY RALSTON, *THE LAW AND PROCEDURE OF INTERNATIONAL TRIBUNALS: BEING A RÉSUMÉ OF THE VIEWS OF ARBITRATORS UPON QUESTIONS ARISING UNDER THE LAW OF NATIONS AND OF THE PROCEDURE AND PRACTICE OF INTERNATIONAL COURTS* 271 (Stanford University Press. 1926).

⁹⁹ Christopher K. Dalrymple, *Politics and Foreign Direct Investment: The Multilateral Investment Guarantee Agency and the Calvo Clause*, 29 CORNELL INTERNATIONAL LAW JOURNAL 161, 164 (1996).

¹⁰⁰ Id. at 164.

¹⁰¹ TODD WEILER, *THE INTERPRETATION OF INTERNATIONAL INVESTMENT LAW: EQUALITY, DISCRIMINATION AND MINIMUM STANDARDS OF TREATMENT IN HISTORICAL CONTEXT* 111 (Martinus Nijhoff Publishers. 2013).

¹⁰² The doctrine of equality is associated with Carlos Calvo, an eminent Argentinian jurist and diplomat in the mid-1800's. “The doctrine's two basic principles are: (1) the ‘national treatment standard,’ which provides that foreigners should not be granted more rights and privileges than those accorded to nationals; and (2) the ‘diplomatic intervention’ provision that foreign states may not enforce their citizens' private claims by violating the territorial sovereignty of host states either through diplomatic or forceful intervention.” Dalrymple, 29 CORNELL INTERNATIONAL LAW JOURNAL 161, 163 (1996).

¹⁰³ A classical statement of the Calvo Doctrine is found in Art. 27 of the Mexican Constitution (1927), which provided that: *[o]nly Mexicans by birth or naturalization and Mexican corporations have the right to acquire ownership of lands, water and their appurtenance, or to obtain concessions for working mines or for the utilization of waters or mineral fuel in the Republic of Mexico. The Nation may grant the same rights to aliens, provided they agree before the Ministry of Justice to consider themselves as Mexicans in respect to such property, and bind*

to gain approval from the host government to invest and acquire property on its soil. If the alien is admitted to the host country, he is then entitled to non-discriminatory treatment. The host state's international obligation towards the treatment of aliens and their property is fulfilled once aliens receive "treatment equal to that accorded to the nationals of the host state."¹⁰⁴ No regard is given whether the alien, or his home state, are dissatisfied with the treatment received.¹⁰⁵ Thus the Calvo doctrine instituted a standard of "national treatment."

The foreign investor is subject to the laws and courts of the host country when seeking redress from state injuries, as is any local. This also meant that home governments of foreign investors cannot intervene by way of diplomatic protection in the claims of their subjects against the host state unless there was a denial of justice.¹⁰⁶ For Latin American countries, denial of justice was defined narrowly as: failure to provide access to domestic courts.¹⁰⁷

The logic used by Latin American countries in maintaining the doctrine of equality comes from their past experiences as colonies. Newly independent Latin America wanted to signal their new status as sovereign countries equal to other countries in the international arena.¹⁰⁸ They also wanted to signal that the era of domination by imperial powers was over. Hence, as sovereigns in the international system equal to other sovereigns, Latin American

themselves not to invoke the protection of their governments in matters relating thereto, under penalty, in case of non compliance, of forfeiture to the Nation of property so acquired.

¹⁰⁴ Falsafi, § D.C.L 201 (McGill University 2010).

¹⁰⁵ JESWALD W. SALACUSE, *THE LAW OF INVESTMENT TREATIES* 49 (Oxford University Press. 2010).

¹⁰⁶ Jonathan Gimblett O. Thomas Johnson Jr, *FROM GUNBOATS TO BITS: The evolution of modern international investment law in YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011*, at 656 (Karl P. Sauvant ed. 2011). See also Falsafi, § D.C.L n.587 (McGill University 2010).

¹⁰⁷ SANTIAGO MONTT, *STATE LIABILITY IN INVESTMENT TREATY ARBITRATION* 40-41 (Hart Publishing. 2009).

¹⁰⁸ Frank Griffith Dawson, *International Law, National Tribunals and the Rights of Aliens: The Latin American Experience*, 21 *VANDERBILT LAW REVIEW* 712, 721 (1967).

countries refused to be subject to any legislative authority other than their own.¹⁰⁹ They refused to apply any international standard or law on foreign investors on their soil. Moreover, out of the notion of fairness, they refused to give foreign investors a privileged position over their national investors. As articulated by the Mexican Foreign Minister Eduardo Hay:

*[T]he foreigner who voluntarily moves to a country which is not his own, in search of a personal benefit, accepts in advance, together with the advantages he is going to enjoy, the risks to which he may find himself exposed. It would be unjust that he should aspire to a privileged position.*¹¹⁰

When capital exporting countries called for the international minimum standard as a rule of customary international law in the second half of the nineteenth century, capital importing countries, mainly Latin American countries, challenged this rule and some denied its existence as a rule of customary international law.¹¹¹

International custom can be defined simply as “a general practice [of states] accepted as law.”¹¹² For an international customary rule to be formed, two criteria must be met. The first is continuous practice by states which must be “*both extensive and virtually uniform.*”¹¹³ The second criterion is that the practice should occur “*in such a way as to show a general recognition that a rule of legal obligation is involved.*”¹¹⁴ Latin American countries argued that both of these

¹⁰⁹ Id. at 721-22. See also SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 309 (Oxford University Press, 2013).

¹¹⁰ American Journal of International Law Supplement, 1938, vol. 32, at 188.

¹¹¹ SORNARAJAH, 123 (Cambridge University Press 3 ed. 2012).

¹¹² SALACUSE, *THE LAW OF INVESTMENT TREATIES* 54 (Oxford University Press 2 ed. 2015).

¹¹³ NORTH SEA CONTINENTAL SHELF CASES ((FEDERAL REPUBLIC OF GERMANY/DENMARK; FEDERAL REPUBLIC OF GERMANY/NETHERLANDS)), para. 74 (INTERNATIONAL COURT OF JUSTICE).

¹¹⁴ Id. at para. 74.

criteria were not present, as regional uniformity and practice regarding the international minimum standard was not established, let alone international recognition.¹¹⁵

However, international custom does not require universal recognition to form a rule of customary international law.¹¹⁶ The United States had introduced the international minimum standard in its early FCN treaties with many countries.¹¹⁷ In Europe, imperial powers adopted the international minimum standard in their bilateral treaties when they gave up their colonies in Asia and Africa.¹¹⁸ Capital exporting countries replied to the Latin American argument that the international minimum standard of treatment has been recognized between civilized nations, and does not require universal recognition to form part of international customary law.¹¹⁹

The continuous practice of the United States, and other European countries, of including the international minimum standard in their bilateral treaties during the twentieth century, along with the willingness of developing countries to accept such inclusion to encourage foreign investors leaves no room for further debate on this matter. The international minimum standard

¹¹⁵ Sornarajah agrees with this view. He also suggests that the United States, being a target of foreign investment arbitrations, especially under NAFTA, may change its position on the treatment of foreign investors and espouse the Calvo Doctrine. In 2002 the U.S. Congress mandated that future treaties should not grant foreign investors in the United States greater rights than U.S. investors making investments in the United States. See SORNARAJAH, 126 n.147 (Cambridge University Press 3 ed. 2012).

¹¹⁶ Article 38 (1) of the Statute of the International Court of Justice provides for “general practice” of an international custom – not universal practice. Another argument is that the ICJ Statute provides for the application of international principals of law “recognized by civilized nations” – not all nations. Outside of its scope, this thesis is of the opinion that the use of the phrase “civilized nations” in the ICJ Statute was unsound. What is a civilized nation? Are there any uncivilized nations? On what criteria is a nation considered civilized? Who are the civilized nations and who are not? All these theoretical questions are debatable.

¹¹⁷ VANDEVELDE, UNITED STATES INVESTMENT TREATIES : POLICY AND PRACTICE 15 (Kluwer Law and Taxation. 1992).

¹¹⁸ As M. Sornarajah puts it “The European states, once they gave up their colonies, had to structure a system of investment protection, and they found the existing American system a convenient one to adopt.” SORNARAJAH, 37 (Cambridge University Press 3 ed. 2012).

¹¹⁹ Alireza Falsafi, *The International Minimum Standard of Treatment of Foreign Investors' Property: A Contingent Standard*, 30 SUFFOLK TRANSNATIONAL LAW REVIEW 317, 320 (2007).

has now become an established rule of contemporary customary international law. Although the doctrine of equality may still find some support by some developing countries.¹²⁰

4. The Application and Enforcement of the International Minimum Standard

The treaties of the colonial era, although they elevated the level of protection and treatment to foreign investors, did not provide any legal means of enforcement in the event of violation by the host state. Foreign investors did not have the right to direct claims against the offending host country in international courts. Therefore the only path investors had was to rely on their home governments when seeking redress from host countries that infringed their rights. To that end, home governments used a blend of diplomacy and force to protect the interests of their nationals abroad.¹²¹ Initially, investment disputes in this era were solved by two means; either through diplomatic protection, or by the use of military force (gunboat diplomacy). Both of these customary means of enforcement proved to be inefficient.¹²² Hence, the use of mixed claims commissions, as a means of investment dispute resolution via arbitration, prevailed at a later stage and became the favored means of solving investment disputes for many countries.¹²³ These three models of investment dispute resolution and enforcement will be discussed below.

¹²⁰ Id. at 330-31.

¹²¹ VANDEVELDE, *BILATERAL INVESTMENT TREATIES: HISTORY, POLICY, AND INTERPRETATION* (Oxford University Press. 2010).

¹²² Vandeveld, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 160 (2005). See also ANDREW NEWCOMBE, 5 (Kluwer Law International. 2009).

¹²³ In 1907 the signatories of the Hague I Convention recognized arbitration as “the most effective, and at the same time the most equitable, means of settling disputes which diplomacy has failed to settle.” See article 16 of the Convention.

a. Diplomatic Protection The practice of diplomatic protection by states can be traced back to the Middle Ages, or earlier.¹²⁴ The rationale behind diplomatic protection rests on the mediate rule: an injury to a state's national is an injury to the state itself. Therefore the state has the right to protect itself from such injurious acts.¹²⁵ This gave home governments the right to pursue claims against other countries that injured their nationals.¹²⁶ To that end, capital exporting countries developed a notion of protecting their injured citizens through the use of diplomacy, what came to be known as "diplomatic protection."¹²⁷

The International Law Commission defines diplomatic protection as "the invocation by a State, through diplomatic action or other means of peaceful settlement, of the responsibility of another State for an injury caused by an internationally wrongful act of that State to a natural or legal person that is a national of the former State with a view to the implementation of such responsibility."¹²⁸

The exercise of diplomatic protection required the injured investor to request his home government to "espouse" his claim with the offending host government.¹²⁹ The injured investor should have exhausted all local remedies in the host country before requesting espousal for

¹²⁴ ANDREW NEWCOMBE, 5 (Kluwer Law International. 2009). See also O. Thomas Johnson Jr, *in* YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011, at 653 (Sauvant ed. 2011).

¹²⁵ ANDREW NEWCOMBE, 5 (Kluwer Law International. 2009).

¹²⁶ SALACUSE, THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL 311 (Oxford University Press. 2013).

¹²⁷ Although the term "diplomatic protection" gives the impression of peaceful means of dispute resolution between states, the practice of it was quite nasty. The use of diplomacy was associated with political, economic, and military pressure by the stronger country against the weaker. As Jan Paulsson notes "the diplomatic component of the expression 'diplomatic protection' was, in such circumstances, an ironic but subtle fiction." See JAN PAULSSON, DENIAL OF JUSTICE IN INTERNATIONAL LAW 15 (Cambridge University Press. 2005).

¹²⁸ Article (1) of the International Law Commission's (ILC's) Articles on Diplomatic Protection adopted by the ILC's at its fifty-eighth session, in 2006. See YEARBOOK OF THE INTERNATIONAL LAW COMMISSION: Report of the Commission to the General Assembly on the Work of its Fifty-Eighth Session 24 (2006).

¹²⁹ Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 160 (2005).

redress from his home government.¹³⁰ The home government is under no obligation to accept the espousal request and is free to reject espousing the claim without giving justification. However, if the home government accepts to espouse the claim against the country that caused injury, it is entitled to settle the dispute on the terms it deems suitable.¹³¹ In other words, the injured investor loses control over the claim, and will have to accept the outcome of the espousal process, whatever it may be.

Diplomatic protection was used continuously by home governments in the eighteenth and nineteenth centuries. This continuous and steady practice led the Permanent Court of International Justice (PCIJ) in 1924 to recognize the right of a state to exercise diplomatic protection over its nationals as an “*elementary principle of international law.*”¹³² The PCIJ affirmed that:

*[A] State is entitled to protect its subjects, when injured by acts contrary to international law committed by another state, from whom they have been unable to obtain satisfaction through the ordinary channels. By taking up the case of one of its subjects and by resorting to diplomatic action or international judicial proceedings on his behalf, a State is in reality asserting its own rights – its right to ensure, in the person of its subjects, respect for the rules of international law.*¹³³

However, the continuous practice of diplomatic protection by home governments to resolve investment disputes proved to be an inadequate remedy for investors. This is mainly because home governments are usually reluctant in accepting espousal of claims against host governments.¹³⁴ This hesitation arises from the possibility of disrupting diplomatic relations with

¹³⁰ Id. at 160.

¹³¹ Id. at 160.

¹³² THE MAVROMMATIS PALESTINE CONCESSIONS Series A-No. 2, at 12 (Permanent Court of International Justice).

¹³³ Id. at 12.

¹³⁴ Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 160 (2005).

the host state. Other reasons contributed to its ineffectiveness, such as the requirement to exhaust all local remedies under the local law of the host state before requesting espousal. This requirement entails a lengthy and costly process on the investors' part, and usually does not result in a satisfactory remedy to the investor. Another reason is the fact that the investor has no right to direct or interfere with the espousal process once taken by his government. The home government may settle the dispute on any terms it wishes, therefore the outcome of the espousal is unpredictable, and may also be unsatisfactory to the investor.

b. Gunboat Diplomacy: The Latin American Experience During the colonial era, when diplomatic efforts failed, the use of military force was the final arbiter in solving investment disputes.¹³⁵ Gunboat policy, or “diplomacy”, was used by capital exporting countries in the eighteenth, nineteenth, and early twentieth centuries.¹³⁶ Latin America is an example of a region that suffered from this policy when it defaulted on its commitments and obligations towards foreign investors.

In the early 1800s, Latin American nations eagerly sought foreign investment.¹³⁷ The effort by these countries to attract foreign investment was initially a great success. However, by 1833 “every Latin American bond issue was in default, and most of the foreign companies established to conduct business in the area had collapsed. In the following years, foreigners as well as nationals were exposed to economic losses.”¹³⁸ The inability of Latin American governments and judicial institutions to protect foreigners' property led home governments to

¹³⁵ SORNARAJAH, 20 (Cambridge University Press 3 ed. 2012).

¹³⁶ CHRISTOPHER DUGAN, 26 (Oxford University Press. 2008).

¹³⁷ Dalrymple, 29 CORNELL INTERNATIONAL LAW JOURNAL 161, 164 (1996).

¹³⁸ Id. at 164.

intervene by the use of force. The examples are many, but an interesting one is the intervention of France in Mexico, where the French invaded Mexico, overthrew its government, and appointed a “foreigner” as President of the country.

In 1860, the Mexican Government defaulted on a loan from J. B. Jecker & Company, a Franco-Swiss bank.¹³⁹ The original loan was for 75 million Francs, however the Mexican Government only borrowed 3.5 million of that amount. When the Mexican government defaulted on that amount, it was deemed to have defaulted on the whole contract amount.¹⁴⁰ This triggered the French Government to invade Mexico in 1861. It overthrew the government and maintained a puppet government there headed by Emperor Maximilian. The latter was the brother of the Austrian Emperor Francis Joseph I who accepted an offer by Napoleon III of France to rule Mexico. However in 1867 Emperor Maximilian was overthrown by the Mexicans and executed by a firing squad.¹⁴¹

Gunboat diplomacy stretched into the early twentieth century. The United States, for example, prevented the destruction of property owned by an American company, New York & Bermudez Company, in Venezuela, by sending a naval vessel.¹⁴² The Vessel’s mandate was to “*protect all existing rights and maintain the status quo*”,¹⁴³ of the American company in Venezuela.

The most notorious of all countries in using force in Latin America was Great Britain. The British “gunboat diplomacy” reached its peak in the 1840’s and 1850’s, during the tenures of

¹³⁹ Id. at 165.

¹⁴⁰ Id. at 165.

¹⁴¹ Id. at 165. See also Wikipedia – Maximilian I of Mexico, https://en.wikipedia.org/wiki/Maximilian_I_of_Mexico#Offer_of_the_Mexican_crown

¹⁴² CHRISTOPHER DUGAN, 27 (Oxford University Press. 2008).

¹⁴³ Letter from Mr. John Hay to Secretary of the Navy, Dated Dec 28, 1900, reprinted in 6 Moore’s International Law Digest 258 (1906).

Foreign Secretary and Prime Minister Lord Palmerston, who said “as the Roman, in days of old, held himself free from indignity, when he could say *Civis Romanus sum* [I am a Roman Citizen]; so also a British subject, in whatever land he may be, shall feel confident that the watchful eye and the strong arm of England, will protect him against injustice and wrong.”¹⁴⁴

The intervention in Latin America continued on repeated occasions during the first third of the twentieth century to protect foreign property, until the Franklin Roosevelt Administration ended the practice in 1933.¹⁴⁵ However, the main goal of these military interventions was to encourage Latin American countries to adjudicate disputes under terms that the invading powers deemed acceptable.¹⁴⁶ As a result, in the second half of the nineteenth century, the use of arbitration became the preferred method for solving investment disputes between countries. To that end, “mixed claims commissions” were established. These commissions helped in the evolution of international investment law and are the foundation to the current investor-state arbitration mechanism.

c. Mixed Claims Commissions By the second half of the nineteenth century, investment dispute resolution by states started to shift from the use of diplomatic protection and gunboat diplomacy to the use of arbitration. States formed *ad hoc* commissions that were vested with the responsibility of solving specific claims, or classes of claims, via arbitration.¹⁴⁷ The first commission of this kind was established between the United States and Great Britain in 1794 to

¹⁴⁴ *House of Commons Debates*, June 25, 1850, vol. 112, 16 (3rd Ser.) c. 444 (statement of Lord Palmerston). Quoted in PAULSSON, (Cambridge University Press. 2005).

¹⁴⁵ VANDEVELDE, *BILATERAL INVESTMENT TREATIES: HISTORY, POLICY, AND INTERPRETATION* (Oxford University Press. 2010).

¹⁴⁶ O. Thomas Johnson Jr, in *YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY* 2010-2011, at 653 (Sauvant ed. 2011).

¹⁴⁷ ANDREW NEWCOMBE, 7 (Kluwer Law International. 2009).

decide on matters relating to the treatment of nationals of both parties during and after the American Revolution.¹⁴⁸ Disputes were remitted to the arbitral tribunal which consisted of five commissioners; two appointed by each party and the fifth commissioner appointed via unanimous vote of the four appointed commissioners. This model became the standard of later mixed claims commissions which became the principle means of solving investment disputes between states.¹⁴⁹

Over sixty commissions were established between states between 1840 and 1940 by different states, and other *ad hoc* commissions were also established to decide on specific claims.¹⁵⁰ The mixed claims commission model for resolving disputes was built on the diplomatic protection model, meaning that only states can be parties before the commission. Therefore investors could not direct claims against the host country, and were still required to seek the approval of their home government to espouse their claims before the commission. Nonetheless, the mixed claims commissions proved to be a success in solving investment claims peacefully. Their success and efficiency was recognized by states as the best means for dispute settlement.¹⁵¹ This success and recognition helped in the evolution and development of investor-state arbitration as known today.

¹⁴⁸ The U.S.-British Mixed Claim Commission was established under the Treaty of Amity, Commerce, and Navigation of 1794. The Commission issued over 500 awards.

¹⁴⁹ O. Thomas Johnson Jr, in YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011, at 653 (Sauvant ed. 2011).

¹⁵⁰ ANDREW NEWCOMBE, 7 (Kluwer Law International. 2009).

¹⁵¹ In 1907 the signatories of the Hague I Convention recognized arbitration as “the most effective, and at the same time the most equitable, means of settling disputes which diplomacy has failed to settle.” See article 16 of the Convention.

II. THE POST-COLONIAL ERA

A. DEVELOPMENTS IN THE FIRST HALF OF THE TWENTIETH CENTURY

By the start of the twentieth century, states, as well as investors, realized the need to restructure the international legal regime governing foreign investment. Customary international law, which was the principal instrument in protecting the rights of foreign investors in earlier times, was proving deficient for several reasons. First, there was no universal consensus on the standard of treatment of foreign investors. Second, the content of the international minimum standard, in the countries where it existed, was vague and subject to varying interpretations.¹⁵² Third, there was no effective enforcement mechanism for investors' rights.¹⁵³ Home governments became even more reluctant to espouse claims due to the complex network of diplomatic and military alliances around the world. This network was vulnerable to disturbance should the inconsistent practice of diplomatic protection remain unchanged. Fourth, the use of gun-boat diplomacy had become internationally unacceptable. Developing countries pressured for the pacific settlement of disputes, after they suffered from uncivilized treatment by Western countries, which frequently invaded and destroyed their newly established and fragile countries. Finally, the success of mixed claims commissions in solving investment disputes demonstrated that arbitration was a

¹⁵² Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 159 (2005). See also Nicholas P. Sullivan Jeswald W. Salacuse *Do Bits Really Work?: An Evaluation Of Bilateral Investment Treaties And Their Grand Bargain*, 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 68 (2005).

¹⁵³ Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 69 (2005).

peaceful and effective dispute settlement mechanism that could replace other ineffective means such as diplomatic protection and gunboat diplomacy.

In 1907, the Convention for the Pacific Settlement of International Disputes was drafted (Hague I Convention).¹⁵⁴ This Convention prohibited states from the use of armed force in the settlement of disputes. The signatories of the Hague I Convention recognized arbitration as “the most effective, and at the same time the most equitable, means of settling disputes which diplomacy has failed to settle.”¹⁵⁵ Recourse to the use of force under the Hague Convention was allowed only if there was refusal to submit the claim to arbitration.¹⁵⁶

The Hague I Convention also encouraged signatories to conclude arbitration agreements amongst themselves, “with a view to extending obligatory arbitration to all cases which they may consider it possible to submit to it.”¹⁵⁷ This started a new phenomenon in the international arena where states began to rely on arbitration to solve disputes. From 1900-1914, more than 120 bilateral arbitration treaties entered into force.¹⁵⁸ The adoption of the Geneva Protocol on Arbitration Clauses in 1923,¹⁵⁹ by which the contracting states agreed to recognize the validity of arbitration agreements between private parties, added to this movement. This enforced the notion of arbitration as a means of alternative dispute resolution, and enabled private parties to submit their claims to an international impartial tribunal and be able to enforce their arbitral awards.

¹⁵⁴ CONVENTION (I) FOR THE PACIFIC SETTLEMENT OF INTERNATIONAL DISPUTES (HAGUE I) (1899). Available at http://avalon.law.yale.edu/19th_century/hague01.asp

¹⁵⁵ Id. at Article 16.

¹⁵⁶ ANDREW NEWCOMBE, 10 (Kluwer Law International. 2009).

¹⁵⁷ CONVENTION (I) FOR THE PACIFIC SETTLEMENT OF INTERNATIONAL DISPUTES (HAGUE I) (1899). Article 19.

¹⁵⁸ O. Thomas Johnson Jr, in YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011, at 654 (Sauvant ed. 2011).

¹⁵⁹ PROTOCOL ON ARBITRATION CLAUSES (Assembly Of The League Of Nations ed., 1923).

Another reason for the need to restructure the international legal regime governing foreign investment was the expansion in volume and scope of foreign investments worldwide. Customary international law was not able to accommodate the new trends and practices of foreign investment, nor did it take account of issues that were of concern to investors.¹⁶⁰

To that end, the American government undertook a project of reviewing its FCN treaties with the goal of including more detailed property protection provisions.¹⁶¹ The focus of FCN treaties started to shift from general consular and trade affairs to substantive investment protection.¹⁶² The FCN treaty signed with Japan in 1911 signaled that change in the American FCN treaty practice, becoming the first treaty to introduce important substantive protections for foreign investment, such as giving corporations' legal status in the host country and allowing them domestic court access.¹⁶³ It also provided for the protection of intellectual property rights and protection against exchange controls.¹⁶⁴ Further, it included a dispute resolution provision in which both states consented to the jurisdiction of the International Court of Justice for disputes involving the interpretation or application of the agreement.¹⁶⁵ The more favorable of national treatment and most-favored-nation treatment was offered to the foreign investor in the new FCN

¹⁶⁰ Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 68 (2005).

¹⁶¹ Dalrymple, 29 CORNELL INTERNATIONAL LAW JOURNAL 161, 308 (1996).

¹⁶² ANDREW NEWCOMBE, 23 (Kluwer Law International. 2009).

¹⁶³ BRAND, § II, at 713 (Center for International Legal Education – University of Pittsburgh School of Law. 2015). The American – Japan FCN Treaty stated in article VII that “*Limited-liability and other companies and associations, commercial, industrial, and financial, already or hereafter to be organized in accordance with the laws of either high contracting party and domiciled in the territories of such party, are authorized, in the territories of the other, to exercise their rights and appear in the courts either as plaintiffs or defendants, subject to the laws of such other party.*” *Treaty of Commerce and Navigation between the United States and Japan*, 5 THE AMERICAN JOURNAL OF INTERNATIONAL LAW, SUPPLEMENT: OFFICIAL DOCUMENTS (APR., 1911) 100 (1911); *id.* at .

¹⁶⁴ *Treaty of Commerce and Navigation between the United States and Japan*, 5 THE AMERICAN JOURNAL OF INTERNATIONAL LAW, SUPPLEMENT: OFFICIAL DOCUMENTS (APR., 1911) 100 (1911). See Article XV and Article XII.

¹⁶⁵ The Treaty provided that: “Any dispute between the Parties as to the interpretation or application of the present Treaty, not satisfactorily adjusted by diplomacy, shall be submitted to the International Court of Justice, unless the Parties agree to settlement by some other pacific means.” *Id.* at Article XXIV(2).

treaty. The new American FCN treaty was innovative, and provided a solid ground for investment protection.

The effect of the new FCN treaties did not last long. Two developments prevented the new FNC treaty from gaining momentum and adoption in other countries.¹⁶⁶ The first was the conclusion of the General Agreement on Tariffs and Trade (GATT) in 1947.¹⁶⁷ The GATT shifted international trade matters from bilateral negotiations and treaties to a multilateral framework, making bilateral “commerce” treaties no longer necessary.

The second development was the rise of the communist bloc, led by the USSR, and the start of the cold war era. The communist bloc, driven by its ideology, regarded foreign investment as a source of exploitation and interference in the affairs of the host state. Communist states embraced an unfriendly attitude towards foreign investment and expropriated investments on their soil.¹⁶⁸ They also encouraged their developing allies to view such agreements as a new form of colonialism by Western countries that should be resisted. The communist block advocated the notion of state control over natural resources, and that foreign investments should be heavily regulated and monitored by the state.¹⁶⁹

Therefore the United States FCN treaty nose-dived as a tool for investment protection. The communist bloc succeeded in spreading a speculative view, among developing countries, towards foreign investment. Hence capital exporting countries endorsed a new idea; a

¹⁶⁶ Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 72 (2005).

¹⁶⁷ THE GENERAL AGREEMENT ON TARIFFS AND TRADE (1947).

¹⁶⁸ O. Thomas Johnson Jr, in YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011, at 661 (Sauvant ed. 2011). See also Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 166 (2005). For more information about the expropriation of foreign owned property during this era see O. Thomas Johnson Jr, in YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011, at 661-67 (Sauvant ed. 2011).

¹⁶⁹ Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 167 (2005).

multilateral legal framework governing investment. This effort intended to harmonize the rules of investment protection internationally. However due to the speculative view developing states had on foreign investments, such efforts were always unsuccessful.¹⁷⁰

The first of these failed attempts to establish a multilateral legal framework for investment was the Havana Charter in 1948.¹⁷¹ The charter sought to establish an International Trade Organization (ITO) with a mandate to achieve the gradual liberalization of trade and investment.¹⁷² Subsequent efforts included the International Chamber of Commerce's ("ICC") International Code of Fair Treatment of Foreign Investment in 1949,¹⁷³ the International Convention for the Mutual Protection of Private Property Rights in Foreign Countries in 1957,¹⁷⁴ a private effort known as the Abs-Shawcross Convention,¹⁷⁵ and the Organization for Economic Cooperation and Development ("OECD") Draft Convention on the Protection of Foreign Property in 1967.¹⁷⁶ While none of these initiatives was fruitful, as a group, they did "inform and influence the development of the BIT movement that was to come."¹⁷⁷

As the multilateral legal framework attempts failed, along with the insecure climate for private capital in many parts of the world, there became an immediate and practical need to rely on bilateral treaties that are specifically designed for investment protection.¹⁷⁸ These treaties would set out the legal framework governing foreign investments between two state parties in a

¹⁷⁰ For a general survey of the failed attempts for a multilateral legal framework for investment see Franziska Tschofen, *Multilateral Approaches to the Treatment of Foreign Investment*, 7 ICSID REVIEW 384 (1992).

¹⁷¹ Vandevelde, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 162 (2005).

¹⁷² Legal Framework for the Treatment of Foreign Investment § I – Survey of Existing Instruments 66 (The World Bank Group 1992).

¹⁷³ *Id.* at 66.

¹⁷⁴ *Id.* at 67.

¹⁷⁵ *Id.* at 67.

¹⁷⁶ *Id.* at 68.

¹⁷⁷ Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 72 (2005).

¹⁷⁸ Ahmad Ali Ghouri, *The Evolution of Bilateral Investment Treaties, Investment Treaty Arbitration and International Investment Law*, 14 INTERNATIONAL ARBITRATION LAW REVIEW 189, 191-92 (2011).

clear, binding, and enforceable manner. Thus, the rules on treatment standards, expropriation, compensation, dispute settlement, and investor rights would no longer be subject to international customary law which was vague, scattered, and non-uniform.¹⁷⁹ Arbitration had already proved its success as a tool for dispute settlement for investment matters in the mixed claims commission model.¹⁸⁰ The opposing attitudes towards foreign investment around the world, along with the expropriation trend by many newly decolonized and independent countries,¹⁸¹ set the stage ready for BIT's to enter and reshape the international regime of foreign investment.

B. DEVELOPMENTS IN THE SECOND HALF OF THE TWENTIETH CENTURY:

1. The BIT Movement

By the end of World War II, capital exporting states realized the need to create bilateral treaties focused on investment protection and promotion. This came as a response to the uncertainties and inadequacies of customary international law in protecting foreign investment.¹⁸² The United States led this movement when it initiated a program to conclude a network of FCN treaties

¹⁷⁹ ANDREW NEWCOMBE, 41 (Kluwer Law International. 2009).

¹⁸⁰ O. Thomas Johnson Jr, *in* YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011, at 654 (Sauvant ed. 2011).

¹⁸¹ ANDREW NEWCOMBE, 18-19 (Kluwer Law International. 2009).

¹⁸² *Id.* at 41.

which, among other commercial and counselor matters, specifically sought to protect and facilitate U.S. investments overseas.¹⁸³

The new FCN treaty expanded and strengthened investment protection to be non-distinguishable from the modern BITs. This new FCN treaty was introduced in 1946, and became a success due to their strong protection of foreign investments. One of its main innovations was the protection of locally incorporated entities – by foreign investors – in the host country.¹⁸⁴ It also encouraged the use of commercial arbitration in the settlement of disputes between the foreign investor and other private parties in the host state, by including a clause providing for judicial enforcement of arbitration awards.¹⁸⁵ Other new provisions were also introduced in these FCN treaties which gave the foreign investor more rights, such as the right to currency and monetary transfers. The Hull doctrine was incorporated into these FCN treaties which provided for “prompt, adequate, and effective compensation” for expropriation. This formula expanded the previous requirement of “just compensation” and reinforced protection guarantees.¹⁸⁶

However the protectionist policies of many developing countries and their skepticism about foreign investment impeded the American FCN program. It is possible also that many developing countries, which were dependent on foreign aid, were reluctant to enter into a treaty of “friendship” with the United States. Signing such an agreement will impede any potential aid from the communist bloc, in addition to other measures of “disciplinary” nature, such as termination of economic relationships. By 1968 The United States had entered into 23 of these

¹⁸³ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 97 (Oxford University Press 2 ed. 2015).

¹⁸⁴ K. Scott Gudgeon, *United States Bilateral Investment Treaties: Comments on their Origin, Purposes, and General Treatment Standards*, 4 *INTERNATIONAL TAX & BUSINESS LAWYER* 105, 108 (1986).

¹⁸⁵ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 98 (Oxford University Press 2 ed. 2015).

¹⁸⁶ *Id.* at 98.

new FCN treaties with other countries.¹⁸⁷ After 1968, the United States did not enter into any FCN treaty with any other nation.¹⁸⁸

Although the United States FCN treaty was indistinguishable from modern BITs, the first document to hold the name “Bilateral Investment Treaty” was in 1959 between Germany and Pakistan.¹⁸⁹ It is hardly ever noted that the United States had signed a FCN treaty with Pakistan in the same year.¹⁹⁰ A comparison between the two treaties signed with Pakistan that year reveals that they both provide for the same degree of protection to foreign investors, and they both do not contain third party dispute resolution.

However the practice of concluding bilateral agreements focused solely on investment protection started to gain momentum, especially among European countries. By the end of the 1960’s, around 74 BITs were signed, almost half of them by Germany. Other countries such as the Netherlands, Sweden, and Switzerland had also signed a significant number of these BITs.¹⁹¹

During the 1970’s revolutionist regimes acquired power from post-colonial regimes in many developing countries, and a new wave of nationalizations started to take place. Also the communist bloc was still influenced by the notion of state control and state ownership of property. Hence developing and communist countries started a campaign at the United Nations General Assembly (UNGA) calling for recognition of their right to expropriate foreign

¹⁸⁷ Vandeveld, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 162 (2005).

¹⁸⁸ John F. Coyle, *The FCN Treaty in the Modern Era*, 51 COLUMBIA JOURNAL OF TRANSNATIONAL LAW 302, 309 (2013). The last, unsuccessful U.S. FCN treaty negotiation occurred with the Philippines in the early 1970s. See Gudgeon, 4 INTERNATIONAL TAX & BUSINESS LAWYER 105, 108 (1986).

¹⁸⁹ TREATY BETWEEN THE FEDERAL REPUBLIC OF GERMANY AND PAKISTAN FOR THE PROMOTION AND PROTECTION OF INVESTMENTS (1959).

¹⁹⁰ TREATY OF FRIENDSHIP AND COMMERCE BETWEEN THE UNITED STATES OF AMERICA AND PAKISTAN (1959).

¹⁹¹ Information obtained from UNCTAD Investment Policy Hub website: <http://investmentpolicyhub.unctad.org/IIA/AdvancedSearchBITResults>

investments without the payment of market value of the expropriated property. Relying on their numerical superiority in the UNGA, they were successful in passing the Declaration of the New International Economic Order (NIEO) in 1974.¹⁹² NIEO declared that states shall have “[f]ull permanent sovereignty” over their natural resources and other economic activities.¹⁹³ This includes “the right of nationalization or transfer of ownership to its nationals.”¹⁹⁴ The Declaration did not specify any obligation to pay compensation.

In December of the same year (1974), developing countries managed to pass another document that was critical to foreign investment protection; the Charter of Economic Rights and Duties of States (CERDS).¹⁹⁵ It declared that each state has the right “[t]o nationalize, expropriate or transfer ownership of foreign property, in which case appropriate compensation should be paid by the State adopting such measures, taking into account its relevant laws and regulations and all circumstances that the State considers pertinent.”¹⁹⁶ The Charter did not specify that compensation must be paid, nor did it specify that compensation should be calculated in accordance with international law. Thus the matter of calculating compensation was transferred to the municipal laws of the expropriating country.¹⁹⁷

These two documents let capital exporting countries to realize the importance of BITs as tools to protect their interests in less developed countries, especially from expropriation. The practical need for prompt, adequate, and effective compensation for expropriation in developing

¹⁹² Declaration on the Establishment of a New International Economic Order § A/RES/S-6/3201 (United Nations General Assembly – Sixth Special session ed., 1974).

¹⁹³ Id. at para. (4)(e).

¹⁹⁴ Id. at para. (4)(e).

¹⁹⁵ Charter of Economic Rights and Duties of States (United Nations General Assembly – Resolution 3281 (XXIX) ed., 1974).

¹⁹⁶ Id. at Article 2.2(c).

¹⁹⁷ Vandeveld, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 168 (2005).

countries required capital exporting states to engage in BITs that enforce this principle.¹⁹⁸ Therefore many capital exporting countries started to enter into BITs with other countries to secure the investments of their nationals. Belgium concluded its first BIT in 1970,¹⁹⁹ France in 1972,²⁰⁰ the United Kingdom in 1975,²⁰¹ Austria in 1976,²⁰² and Japan in 1977.²⁰³ The United States launched its BIT program in 1977 but did not enter into its first BIT until 1982.²⁰⁴ By end of the 1980's the number of BITs worldwide had increased six fold, from that of the 1960's, reaching almost 500 signed BITs.²⁰⁵ Another major event pushed the proliferation wheel even faster during the 1990's; the collapse of the Soviet Union and the fall of the communist economic ideology.²⁰⁶ After the fall of the Soviet Union in 1991, the over-protective, state-run, and speculative communist economy was no longer available as an alternative to the open market, capitalist economy. Hence many developing countries gave up their protectionist and highly restrictive legal regimes governing FDI and introduced new laws that were in the direction of greater liberalization.²⁰⁷ The 1990's decade witnessed the largest proliferation of BITs of any time, as over 2000 BITs were signed by the end of the year 1999.²⁰⁸ The

¹⁹⁸ Kenneth J. Vandeveld, *The Political Economy of a Bilateral Investment Treaty*, 92 THE AMERICAN JOURNAL OF INTERNATIONAL LAW 621, 627 (1998).

¹⁹⁹ The First BIT signed by Belgium was with Indonesia. Information obtained from UNCTAD Investment Policy Hub website: <http://investmentpolicyhub.unctad.org/IIA/AdvancedSearchBITResults>

²⁰⁰ The First BIT signed by France was with Tunisia. *Id.*

²⁰¹ The First BIT signed by United Kingdom was with Egypt. *Id.*

²⁰² The First BIT signed by Austria was with Romania. *Id.*

²⁰³ The First BIT signed by Japan was with Egypt. *Id.*

²⁰⁴ See Vandeveld, *The Political Economy of a Bilateral Investment Treaty*, 92 THE AMERICAN JOURNAL OF INTERNATIONAL LAW 621, 628 (1998). The First BIT signed by the United States was with Egypt. *Id.*

²⁰⁵ Information obtained from UNCTAD Investment Policy Hub Website, <http://investmentpolicyhub.unctad.org/IIA/AdvancedSearchBITResults> on October 30, 2016. See also Vandeveld, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 172 (2005).

²⁰⁶ Vandeveld, *The Political Economy of a Bilateral Investment Treaty*, 92 THE AMERICAN JOURNAL OF INTERNATIONAL LAW 621, 628 (1998).

²⁰⁷ UNCTAD World Investment Report: FDI Policies for Development: National and International Perspectives 20 (2003).

²⁰⁸ Information obtained from UNCTAD Investment Policy Hub Website, <http://investmentpolicyhub.unctad.org/IIA/AdvancedSearchBITResults> on October 30, 2016.

proliferation of the BIT network remained at an extraordinary rate in the twenty-first century. Today there are around 3300 signed BITs and investment agreements, involving almost every country in the world.²⁰⁹

2. The ICSID Convention

As illustrated earlier in this Chapter, historically foreign investors had limited options when seeking redress for damages caused by the acts or laws of host countries. Before the introduction of the investor-state dispute resolution mechanism, injured foreign investors had only four options: i) to accept the injury as a cost of doing business offshore and pass this cost to the secondary market, ii) seek diplomatic protection by petitioning their home governments to espouse their claims, iii) lobby their home governments to use military force to coerce the offending host country to make good to the offence, or iv) accept the remedies provided for by the host country's local courts. All of these options put the foreign investor at a disadvantage. The foreign investor had to choose between increasing the cost, and consequently the price, of his service or goods, or having to be subjected to the political considerations of the home government when requesting diplomatic protection, or having to ruin his relationship with the host country after his home country used military force against it, or having to accept the discriminatory treatment and inefficient legal systems of host countries.

Thus, there became a practical need to solve investment disputes in a peaceful, depoliticized, and impartial manner. The use of arbitration by the mixed claims commissions' to

²⁰⁹ Information obtained from UNCTAD Investment Policy Hub website: <http://investmentpolicyhub.unctad.org/IIA> on October 30, 2016.

solve investment disputes had great success, and encouraged the use of arbitration as a neutral and efficient method of solving investment disputes. However, although of its long use (1840-1940) the mixed claims commissions' model had its own shortcomings. Basically it did not allow foreign investors to directly press claims against the offending host country, but rather investors' claims had to be forwarded to the commission by the home government. Thus foreign investors were still subject to the discretion of their home government.

The use of commercial arbitration to solve investment disputes started in the early 1900's, when investment contracts were signed between states and private investors. However, international commercial arbitration is a system designed to solve private parties' disputes. It is not equipped to include a sovereign among its litigants, due to matters relating to state sovereignty and state immunity. Legal theorists, specifically from those of the positivist school of legal thought, criticized the use of arbitration to solve investor-state disputes.²¹⁰ The theoretical problem lays in that private natural and legal persons have no legal standing under international law to seek reparation from sovereigns. International law was seen as a field of law that governs the relations between states exclusively. Consequently, disputes arising out of contracts between sovereign states and private foreign investors were considered to be subject to the host state's municipal law. This was also supported by developing countries, especially those adopting the Calvo doctrine, were they resisted the notion of being brought into arbitrations by private foreign investors. The ICJ took a similar stance when it affirmed that a relationship

²¹⁰ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 414 (Oxford University Press 2 ed. 2015).

between a borrowing state and a private person is one that falls “*within the domain of municipal law*.”²¹¹

Hence there became a need for a system designed in particular to tackle the issue of investor-state dispute settlement. During the early years of the 1960’s international organizations realized even more the importance of FDI as a source of development for newly independent and economically weak countries. However, the immature and fragile legal systems of those countries constituted an impediment for FDI inflow. Foreign investors were hesitant to invest in countries where the local legal system might fail to protect them. Therefore it became increasingly clear that “if the plans established for the growth in the economies of the developing countries were to be realized, it would be necessary to supplement the resources flowing to these countries from bilateral and multilateral governmental sources by additional investments originating in the private sector.”²¹²

Consequently many international organizations started to consider different schemes that aimed at removing barriers and obstacles that hinder the flow of FDI into developing countries, and consequently hinder their development. The International Bank for Reconstruction and Development (the World Bank) proposed an international convention which establishes an institution that provides investor-state arbitration and conciliation facilities to settle investment disputes. The idea was proposed by the President of the Bank in 1961, who had frequently been requested to lend his good offices for the settlement of various types of financial disputes,

²¹¹ CASE CONCERNING THE PAYMENT OF VARIOUS SERBIAN LOANS ISSUED IN FRANCE 18 (Permanent Court of International Justice 1929).

²¹² History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States. (2009 Reprint), vol. 1, at 2.

including some between governments and private foreign investors.²¹³ The World Bank concluded that an institution specifically designed to deal with the special problems of settling investment disputes between foreign private persons and country governments would facilitate and enhance the international flow of capital, and hence development.²¹⁴

Drawing on the defaults of the customary means of investment dispute settlement, the Bank recommended that the proposed convention recognizes the following main principles: i) the possibility of direct claims by private investors against host governments, ii) recognition by states that arbitration agreements entered into with private investors are binding international instruments, iii) the provision of arbitration facilities, arbitrators, arbitration rules, and so forth, and iv) provide conciliation as an alternative to arbitration.²¹⁵

It took almost four years of deliberations, consultations, meetings, and many drafts to transform this project into its current form and content. On March 18th of 1965 the Executive Directors of the Bank took the resolution to adopt the draft text of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention or the Convention),²¹⁶ and instructed the President to transmit the Convention and the accompanying reports to all member governments of the Bank for their consideration and signature.²¹⁷ The Convention was soon signed by a number of States, and the twentieth ratification was deposited on September 14, 1966; pursuant to its Article 68(2), the Convention

²¹³ *Id.* at 2.

²¹⁴ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 417 (Oxford University Press 2 ed. 2015).

²¹⁵ *Id.* at 418.

²¹⁶ *Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (1965).

²¹⁷ *History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States* § 1, at 8-10 (ICSID 2009 Reprint).

thereupon entered into force 30 days later, on October 14, 1966.²¹⁸ Today 161 countries have signed the ICSID Convention, a 151 of which have deposited their instruments of ratification.²¹⁹

The Convention established the International Center for Settlement of Investment Disputes (ICSID or the Center); a dedicated institution for the settlement of investor-state disputes located in Washington, DC. The ICSID Center is on one of the five institutions that form the World Bank Group. The Center registered its first case in 1972, and has since become an international hub for investor-state dispute resolution with a caseload of 570 registered cases until today.²²⁰

The foundation on which the Convention was built on is: economic development of states through private foreign investment. The view of the founders of the Convention was that protection of investment enhances its mobility. For example; from 1980 until 1997 global FDI outflows increased at an average rate of about 13 percent a year.²²¹ Of course this success cannot be attributed only to the Convention, but providing a neutral and bias free venue to litigate investor-state disputes did encourage capital mobility from developed countries to less developed ones. However developing countries did not have major success in achieving economic growth from FDI. On the contrary, some developing countries are now denouncing the Convention,²²² or

²¹⁸ Id. at 8-10.

²¹⁹ LIST OF CONTRACTING STATES AND OTHER SIGNATORIES OF THE CONVENTION (as of April 12, 2016). Found on ICSID Website <https://icsid.worldbank.org/apps/ICSIDWEB/icsiddocs/Documents/List%20of%20Contracting%20States%20and%20Other%20Signatories%20of%20the%20Convention%20-%20Latest.pdf>

²²⁰ Based on cases registered or administered by ICSID as of June 30, 2016. See ICSID Caseload – Statistics, at ICSID Website [https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%2016-2%20\(English\)%20Sept%2020%20-%20corrected.pdf](https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%2016-2%20(English)%20Sept%2020%20-%20corrected.pdf)

²²¹ Karl P. Sauvant Padma Mallampally, *Foreign Direct Investment in Developing Countries*, FINANCE AND DEVELOPMENT 1999.

²²² Bolivia, Ecuador, and Venezuela have denounced the Convention. See in general Denunciation of the ICSID Convention and BITs: Impact on Investor-State Claims § December, No. 2 (United Nations UNCTAD ed., 2010).

have expressed their intention not to include ICSID arbitration clauses in their future BITs.²²³ The issue of why the Convention has not succeeded in fostering development for developing countries will be dealt with later in this thesis. However in brief it can be said that the inconsistent decisions and interpretations of the treatment standards, along with the expansive and innovative interpretations of BITs provisions by ICSID tribunals, have hindered the economic development of countries through FDI.

3. The MIGA Convention

Investing in less developed countries usually entails increased non-commercial risks and political uncertainties. These uncertainties, generally referred to as “political risks”, arise from the unpredictable behavior of the executive, legislative, and judicial authorities of the host country in the long-term. In essence, political risks are uncertainties related to the host country’s legislative and administrative acts, which “deny or restrict the right of an investor/owner (i) to use or benefit from his/her assets; or (ii) which reduce the value of the firm.”²²⁴ This can be the result of sudden change of government attitude towards foreign investors. For example a *coup d’état* in the host country might replace a liberal government with a nationalistic one. Thus expropriations, nationalizations dispossessions, or the alternation of property rights become government policies affecting foreign investors.²²⁵ Also some events of a political nature can

²²³ El Salvador and South Africa for example has expressed their intention to reconsider all BITs that contain ICSID Arbitration clauses.

²²⁴ See the definition of “Political Risk” in the *Glossary of Terms Used in the Political Risk Insurance Industry*, found MIGA’s website https://www.miga.org/Documents/Glossary_of_Terms_Used_in_the_Political_Risk_Insurance_Industry.pdf

²²⁵ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 245 (Oxford University Press. 2013).

have an adverse effect on foreign investment, which is compromised by situations of instability in the host country.²²⁶ Wars, revolutions, government seizure of property, and government actions that restrict the movement of profits or other revenues from or within the country, are just a few events that can place investor property and contractual rights in jeopardy.²²⁷

Economic growth and development of developing countries requires increased foreign capital to be injected into their economics. The latter objective can only be achieved if internal barriers' and risks in these countries are reduced to the minimum in order to encourage the inflow of foreign investment. Political risks are given great weight in the investment making decision process and can play a major role in deterring foreign investments into the host country.²²⁸

Based on its commitment to improve the investment climate of developing countries to achieve development, the World Bank initiated a project to establish a multilateral investment protection agency that would provide insurance against political risks to foreign investments in developing countries.²²⁹ Alden Clausen, President of the World Bank initiated the MIGA project based on the need "to improve the investment climate – for potential investors and potential recipients alike."²³⁰ The project materialized in 1985 when the Board of Governors approved the Convention establishing the Multilateral Investment Guarantee Agency (MIGA Convention). In

²²⁶ IBRAHIM F.I. SHIHATA, *MIGA AND FOREIGN INVESTMENT* 15 (Martinus Nijhoff Publishers. 1988).

²²⁷ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 245 (Oxford University Press. 2013).

²²⁸ SHIHATA, 16 (Martinus Nijhoff Publishers. 1988).

²²⁹ See Ibrahim I.F. Shihata, *Increasing Private Capital Flows to LDCs*, *FINANCE AND DEVELOPMENT* 1984, at 6.

²³⁰ *Id.* at 6.

1988 the required minimum ratifications and capital were reached and MIGA was officially created.²³¹

The MIGA Convention provides insurance against non-commercial and political risks to qualifying investments originating from developed member countries and invested in developing member countries.²³² Eligible investments for coverage are those which fall under two categories; i) equity interests, which include FDI and portfolio investments, and ii) non-equity direct investments, which include service and management contracts, franchising agreements, turnkey contracts, and the like; provided that they have terms of at least three years.²³³ MIGA provides eligible investment protection against four separate political risks. These risks are; host country restrictions on currency conversion and transfer, ii) expropriation and similar measures that deprive the foreign investor from effective control, ownership, or benefit from his investment, iii) breach of contracts by the host government, or is subject to procedural delays, or is unable to enforce decisions made in his favor, and iv) military action and civil disturbance.²³⁴

CONCLUSION

The history of international investment law reveals that the system of foreign investment protection was built on the notion of reciprocal benefits for the foreign investor and the host

²³¹ The MIGA Convention requires not less than five ratifications of developed signatory states, and not less than fifteen ratifications from developing signatory states; provided that total subscriptions of these states amount to not less than one-third of the authorized capital of the Agency. See Article 61 of The Convention Establishing the Multilateral Investment Guarantee Agency (MIGA) (1985).

²³² Id. at Article 14.

²³³ See Articles 1.02-1.13 of MIGA Operational Policies.

²³⁴ Article 11(a) of The Convention Establishing the Multilateral Investment Guarantee Agency (MIGA) (1985).

state. In early centuries, foreigners were perceived as invaders and thus confronted with an unfriendly attitude. However sovereigns realized their importance as sources of capital and products that fuel their economic development. Therefore they granted foreign traders in their territory protections and incentives to encourage and increase their inflow.

From the early beginnings until modern times the reciprocal benefits notion was central to the development of international investment law. The main conventions and multilateral agreements that govern this field (e.g. ICSID Convention and MIGA) were concerned with the development of host states as much as their concern with investor protection. In fact the protection of foreign investment was the tool to achieve capital mobility into developing countries, and hence achieve economic development around the globe. This goal, as mentioned above, is explicitly stated in the preparatory works and preambles of these multilateral instruments.

The BIT movement in the 1950's came as a "deal" between developed capital exporting states and developing capital importing states. By facilitating the entry of FDI and providing it with protection, and hence being exposed to liability, the developing state anticipated development by encouraging FDI inflows.

Therefore it can be concluded that economic growth and development was always a central objective in all international instruments that deal with overseas investment. Indeed the development of countries through FDI cannot be reached if FDI is not encouraged by guaranteeing its protection from harmful acts of host countries, thus protection of investment is the other central objective. All international conventions and BITs refer to economic development and investor protection as the driving force behind their enactment and adoption.

Nonetheless the current international legal regime of foreign investment is overlooking the historical and practical objective of FDI for state development. Instead, in the current state of affairs, the focus is on the protection of the investor. BITs are becoming stricter on investment protection in a manner that leaves little margin for the host country to benefit from FDI for its development. Concerns have been expressed about the balance between investment protection and the host country's public interest in regulating various matters of public concern, such as environmental protection, health protection, social and human rights, etc. Inconsistency in arbitral interpretation of investment treaty obligations and the expanding protective interpretation of treatment standards have led many countries and civil organizations to question the legitimacy and benefits of the entire system.

These issues have pushed investment treaties into the light of public scrutiny. That focus has turned up a number of concerns about how investment treaties operate, and the conflicts they can create between the goal of attracting investment and other public policy aims that may be impacted in the process. The concern is that investment treaties may be benefiting foreign investors and investments to the detriment of the goal of host state development through FDI.

CHAPTER THREE

THE MODERN INVESTMENT TREATY AND THE ISSUE OF DEVELOPMENT

INTRODUCTION

Foreign direct investment (FDI) is vital to the economic development of countries.¹ In the second half of the Twentieth Century, the international community realized that mobilizing capital from developed countries to developing countries, to assist the latter in their development, requires eliminating the risks for foreign investors in these countries.² Hence, the drafting and adoption of multilateral conventions governing international investment, such as ICSID and MIGA, were designed both to achieve the goal of minimizing investor risks in

¹ For example, UNCTAD notes: “At a time of pressing social and environmental challenges, harnessing economic growth for sustainable and inclusive development is more important than ever. Investment is a primary driver of such growth. Mobilizing investment and ensuring that it contributes to sustainable development objectives is therefore a priority for all countries and for developing countries in particular.” Investment Policy Framework for Sustainable Development 7 (2015). Also the Monterrey Consensus acknowledged the importance of FDI for development by stating: “Private international capital flows, particularly foreign direct investment, along with international financial stability, are vital complements to national and international development efforts. Foreign direct investment contributes toward financing sustained economic growth over the long term. It is especially important for its potential to transfer knowledge and technology, create jobs, boost overall productivity, enhance competitiveness and entrepreneurship, and ultimately eradicate poverty through economic growth and development.” See Monterrey Consensus of the International Conference on Financing for Development: The final text of agreements and commitments adopted at the International Conference on Financing for Development, para. 20 (Monterrey, Mexico, 18-22 March 2002) (United Nations 2003).

² See JESWALD W. SALACUSE, *THE LAW OF INVESTMENT TREATIES* 417 (Oxford University Press 2 ed. 2015).

developing countries and to demonstrate that “development is closely related to, and could be viewed as a core objective of, national and international investment law and policy.”³

The BIT movement in the 1950’s had a similar purpose. BITs came to fill a gap created by the inefficiency of customary international law in providing adequate protection to foreign investment.⁴ The rise of communist ideologies in many parts of the world, and the formation of newly independent developing states, created a climate of uncertainty for cross-border private capital which needed to be rectified.⁵ Developed countries wanted to create a stable international legal framework to facilitate and protect the investments of their nationals in developing countries.⁶ To that end, they drafted treaties that govern foreign investments in developing countries.⁷ As articulated by Lord Shawcross (a former Attorney General of the U.K.) and Herman Abs (Chairman of the Deutsche Bank in Germany) in 1960:

*[I]t is now widely recognized that major steps must be taken to buttress the economic position of the free-world nations, both as a measure against Soviet moves and as a means of resolving some of the demands being made by the peoples of the underdeveloped nations of the world, the notion of greater protection under international law for private investment takes on added importance.*⁸

³ Markus Gehring & Andrew Newcombe, *An Introduction to Sustainable Development in World Investment Law*, in *SUSTAINABLE DEVELOPMENT IN WORLD INVESTMENT LAW* 4 (Markus W Gehring Marie-Claire Cordonier Segger, Andrew Newcombe ed. 2011).

⁴ LLUÍS PARADELL ANDREW NEWCOMBE, *LAW AND PRACTICE OF INVESTMENT TREATIES: STANDARDS OF TREATMENT* 41 (Kluwer Law International. 2009).

⁵ See Asoka de Z. Gunawardana & José E. Alvarez, *The Inception and Growth of Bilateral Investment Promotion and Protection Treaties*, 86 *PROCEEDINGS OF THE ANNUAL MEETING (AMERICAN SOCIETY OF INTERNATIONAL LAW)* 544, 555 (1992).

⁶ Ahmad Ali Ghouri, *The Evolution of Bilateral Investment Treaties, Investment Treaty Arbitration and International Investment Law*, 14 *INTERNATIONAL ARBITRATION LAW REVIEW* 189, 191 (2011).

⁷ Kenneth J. Vandeveld, *The Political Economy of a Bilateral Investment Treaty*, 92 *THE AMERICAN JOURNAL OF INTERNATIONAL LAW* 621, 627 (1998).

⁸ *The Proposed Convention to Protect Private Foreign Investment, A Round Table*, Introduction by the Editors, *Journal of Public Law*, Vol. 9, p. 115, 1960.

The movement to conclude BITs was initiated and driven by Western, capital-exporting countries to protect their nationals' investment interests in developing countries.⁹ Most capital exporting countries created model BITs – prototypes – they would use when negotiating with developing countries.¹⁰ Although these treaties are formally reciprocal, they were developed by capital exporting countries to protect their nationals abroad, hence their obligations are asymmetrical.¹¹ Virtually all early BITs were entered into between developed countries on one hand, and developing countries on the other hand, providing what is called a North-South relationship.¹²

One might ask, then, why would developing countries, which do not have the surplus of capital and technology, sign agreements that impose a liability on them without any reciprocal benefit?¹³ Developing countries were inclined to sign such treaties to encourage the inflow of foreign investment into their economies.¹⁴ The host country sought to obtain the elements of

⁹ Jeswald W. Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, 24 *THE INTERNATIONAL LAWYER* 655, 665 (1990).

¹⁰ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 101 (Oxford University Press 2 ed. 2015). It is worth to mention that BITs nowadays are not exclusively signed between capital exporting and capital importing countries. Rather many developing countries have signed, and continue to sign, investment treaties between them (South-South) and many developed countries sign investment treaties between them (North-North). This shows that the benefits of FDI for economic growth (especially the transfer of technology) are no longer an issue attached to developing countries. See Alvarez, 86 *PROCEEDINGS OF THE ANNUAL MEETING (AMERICAN SOCIETY OF INTERNATIONAL LAW)* 544, 545 (1992).

¹¹ Andrew Newcombe, *Sustainable Development and Investment Treaty Law*, 8 *THE JOURNAL OF WORLD INVESTMENT & TRADE* 357, 363 (2007).

¹² UNCTAD-Bilateral Investment Treaties 1959-1999, at 1 (2000).

¹³ “For most of these [developing] countries, the promised reciprocity of the BIT – the promise that the treaty will permit their investors to enter the lucrative U.S. market – is for now an illusion. Few U.S. BIT signatories expect to be able to compete in the U.S. market. The truth is that these countries enter into BITs with the United States, as Professor Vandeveldel has suggested, as a symbolic announcement that they welcome U.S. investors and in the hopes that such investors are forthcoming.” Alvarez, 86 *PROCEEDINGS OF THE ANNUAL MEETING (AMERICAN SOCIETY OF INTERNATIONAL LAW)* 544, 552-53 (1992).

¹⁴ UNCTAD-Bilateral Investment Treaties 1959-1999, at 1 (2000). Also as on commentator puts it “developing countries, beset with economic difficulties, have come to realize that one of the best ways in which their economies can be developed is by encouraging foreign investments, and that the bilateral investment treaty is a fine instrument to achieve that objective.” Alvarez, 86 *PROCEEDINGS OF THE ANNUAL MEETING (AMERICAN SOCIETY OF INTERNATIONAL LAW)* 544, 546 (1992).

economic growth, which it lacked.¹⁵ Capital, technology, and know-how are the main economic growth elements that can be obtained through foreign investment.¹⁶ In addition, host countries sought to benefit from the spillover effects of foreign investments, such as; infrastructure development, employment opportunities and increased revenue from taxes and duties paid by the foreign investors.¹⁷

The dual objectives of investment protection and development stimulation are reflected in the titles and preambles of virtually all BITs.¹⁸ Typically a BIT is titled “Treaty Concerning the Reciprocal *Encouragement and Protection* of Investments.” The preambles acknowledge the parties’ desire to “*promote greater economic cooperation*” by creating a “*stable framework for investment*” that results in greater inflow of “*private capital and the economic development of the Parties.*”¹⁹ BITs were considered to be a “win-win” deal, or a “grand bargain,”²⁰ for both parties involved:

What should, after all, not be forgotten in this debate is that both capital-importing and capital-exporting countries derive benefits from increased flows of foreign investment. Apart from the transfer of technology connected to foreign investment, the creation of employment, additional tax revenue, etc., investment treaties create a legal infrastructure for the functioning of global market economy by protecting property rights, offering contract protection, establishing nondiscrimination as a prerequisite for competition through national and most-favored-nation treatment, and making effective dispute-settlement mechanisms.

¹⁵ Howard Mann Aaron Cosbey, Luke Eric Peterson, Konrad Von Moltke, *Investment and Sustainable Development: A Guide to the Use and Potential of International Investment Agreements* 1 (International Institute for Sustainable Development 2004).

¹⁶ Nicholas P. Sullivan Jeswald W. Salacuse *Do Bits Really Work?: An Evaluation Of Bilateral Investment Treaties And Their Grand Bargain*, 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 77 (2005).

¹⁷ SORNARAJAH, *THE INTERNATIONAL LAW ON FOREIGN INVESTMENT* 48 (Cambridge University Press 3 ed. 2012).

¹⁸ “BITs are agreements between two sovereign states. From the point of view of the capital importing country, their basic purpose is to help to attract FDI. From the point of view of the capital-exporting country, the basic purpose of BITs is to protect investors from political risks and instability and, more generally, safeguard the investments made by its nationals in the territory of the other state.” Lisa E. Sachs & Karl P. Sauvant, *BITs, DTTs and FDI flows: an Overview*, in *THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT: BILATERAL INVESTMENT TREATIES, DOUBLE TAXATION TREATIES, AND INVESTMENT FLOWS* 9 (Karl P Sauvant & Lisa E Sachs ed. 2009).

¹⁹ See for example the Preamble of the U.S. Model Bilateral Investment Treaty (2012).

²⁰ Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 77 (2005).

*Perfect market conditions presupposed, this leads to the efficient allocation of capital, economic growth, and development, and benefits both capital-exporting and capital-importing countries through an increase in overall well-being.*²¹

This chapter focuses on the question of whether BITs serve each of their two main purposes – i.e. investor protection and host state development – equally. Evidence shows that investor protection has won out over host state development.²² While this is demonstrated by economic studies,²³ that is not the focus here. Rather it is the individual clauses of BITs and their interpretation by investor-state arbitral tribunals that has demonstrated this failure.²⁴

Decisions in investor-state arbitration have focused on the protection of investments “to the detriment of the sovereign power and duty of host States to pursue the general interest for their populations of promoting their national development.”²⁵ As a result, BIT parties have responded to decisions in investor-state arbitrations by amending their model BITs in manner that preserves more regulatory flexibility for the host state via the addition of exceptions and reservations, “carve-outs,”²⁶ of certain state measures from treaty protection. These

²¹ Charles Brower & Stephan Schill, *Is Arbitration a Threat or a Boon to the Legitimacy of International Investment Law?*, 9 CHICAGO JOURNAL OF INTERNATIONAL LAW 471, 496 (2009).

²² As one commentator notes “[T]reaty-based investment arbitration – mainly under BITs and NAFTA – has been biased in favour of foreign investors to the detriment of the sovereign power and duty of host States to pursue the general interest for their populations of promoting their national development.” See Attila Tanzi, *On Balancing Foreign Investment Interests with Public Interests in Recent Arbitration Case Law in the Public Utilities Sector*, 11 THE LAW AND PRACTICE OF INTERNATIONAL COURTS AND TRIBUNALS 47, 48 (2012).

²³ For a full discussion on the impact of BITs on foreign investment inflows see Sauvart, *in* THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT: BILATERAL INVESTMENT TREATIES, DOUBLE TAXATION TREATIES, AND INVESTMENT FLOWS (Sachs ed. 2009). Also see Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, 24 THE INTERNATIONAL LAWYER 655 (1990).

²⁴ A recent UNCTAD report concludes – after reviewing different arbitral decisions – that “the outcome of many disputes hinged upon the wording of specific provisions in the applicable IIA.” See Investor-State Dispute Settlement: Review of Developments in 2016, at 29 (2017).

²⁵ Tanzi, 11 THE LAW AND PRACTICE OF INTERNATIONAL COURTS AND TRIBUNALS 47, 48 (2012).

²⁶ “Carve-outs are a popular tool in Mega-Regionals to protect host states’ regulatory freedom by ensuring that certain measures are not subject to investment treaty disciplines in the first place. Mega-Regionals may offer three main types of carve-outs: 1) carve-outs from the entire agreement; 2) carve-outs from specific treaty obligations; and 3) carve-outs for certain industries or areas of regulation. Notably, all three types of carve-outs can be found in U.S. and NAFTA practice.” Stephan W. Schill & Heather L. Bray, *The Brave New (American) World of International*

modifications and clarifications to model BITs are a reflection of the expansive pro-investor interpretations of treaty provisions in investor-state arbitrations. Other approaches to re-balancing investment treaties include issuing joint interpretations – by the state parties – for provisions of existing investment agreements.²⁷ This prohibits future tribunals from adopting expansive interpretations of treaty provisions that go beyond the intent and interest of the BIT parties. Moreover, a significant number of states have responded to these decisions by terminating their existing BITs,²⁸ and by rejecting investor-state arbitration in future BITs.²⁹

While this chapter will demonstrate that some arbitration decisions and the current BIT structure favor investor protection at the expense of host state development, Chapter 4 will demonstrate that it is not the arbitration process, but the fundamental substantive treaty provisions, which can best be changed to bring the system into place. There is no need to eject arbitration as a dispute settlement process when the rules can be clarified for proper application within that framework.³⁰

Investment Law: Substantive Investment Protection Standards in Mega-Regionals, 5 BRITISH JOURNAL OF AMERICAN LEGAL STUDIES 419, 429 (2016).

²⁷ For instance, following concerns by the NAFTA parties regarding interpretations of the “fair and equitable treatment (FET)” standard in NAFTA arbitrations, the NAFTA parties issued a joint interpretation of the FET standard. This joint interpretation is binding on future tribunals. Interpretation of the Free Trade Commission of Certain Chapter 11 Provisions, section B, July 31, 2001, available at <https://www.state.gov/documents/organization/38790.pdf>.

²⁸ See footnote 127.

²⁹ See footnote 128.

³⁰ See Investor-State Dispute Settlement: Review of Developments in 2016, at 29 (UNCTAD ed., 2017).

I. THE CONTENT OF BITs

Although there are over 3300 BITs worldwide, most BITs have a similar general structure and content. However, this does not mean that all BITs are identical, nor does it mean that BITs are not subject to constant developments. On the contrary, by looking into the details of each treaty one can distinguish a variety of approaches with regard to individual provisions.³¹ These differences exist as a result of the underlying rationale of the BIT, the degree of protection it offers, and the number of qualitative innovations.³² Below is a brief introduction to the basic structure and content of BITs. It does not discuss the individual differences or approaches, but rather gives a general overview of modern BITs and their basic provisions.

A. SCOPE OF APPLICATION

A BIT usually starts with a definitions article that basically outlines the treaty's scope of application.³³ The definitions of "investments," "investors," "companies," "nationals," and "territory" are of the essence, as they constitute the rules that determine the applicability of the BIT. Economic activities, and the foreign natural or legal persons conducting them, must fit the definitions given in the treaty to benefit from treaty protection. Consequently, these definitions play an important role in the negotiation and conclusion of treaties. Capital exporting countries

³¹ UNCTAD, BILATERAL INVESTMENT TREATIES 1995-2006: TRENDS IN INVESTMENT RULEMAKING § UNCTAD/ITE/IIT/2006/5, at xiii (United Nations 2007).

³² *Id.* at xiii.

³³ The preamble precedes the definitions provision in the BIT. The preamble expresses the objectives and purposes of the BIT, which usually are: to intensify economic cooperation between treaty parties, investment protection, and investment promotion to achieve economic development.

attempt to broaden these definitions to include all types of investments to protect all of their outbound investors. Capital importing countries on the other hand, especially those seeking economic development through FDI, should attempt to limit these definitions in a fashion that responds to their objectives and needs from FDI. It is well established that a legal system “premised on the notion that all foreign investment is uniformly beneficial is not one based on sound foundations.”³⁴ Currently, most BITs adopt an open asset-based definition for investment. Such a wide and inconclusive definition can encompass actives that are not “investments” within the meaning and intent of the host state seeking development through FDI. Thus, development through FDI requires that these definitions be both clear and limited, and that they encompass the development objectives of the host country so that treaty protection is given to FDI that contributes to economic development. A more detailed discussion of these definitions and their interpretation in investor-state arbitrations will follow in the next Chapter to demonstrate the need for new definitions in future BITs that incorporate the goal of host state development.

B. INVESTMENT LIBERALIZATION

One of the basic principles of state sovereignty is that aliens are not entitled to enter into a country and acquire property or conduct business in it unless the alien has gained explicit authorization from the host country to do so.³⁵ Every sovereign has the right to regulate the entry of foreign investment into its soil, and most countries have enacted national laws to that effect.

³⁴ SORNARAJAH, 230 (Cambridge University Press 3 ed. 2012).

³⁵ IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 520 (Oxford University Press 7th ed. 2008).

Depending on the state's economic ideology, its national laws can be protective, restrictive, or liberal towards FDI. After WWII many developing countries adopted conservative laws that restricted the entry of FDI into their economies. BITs circumvent these conservative national laws where the capital exporting country engages in a bilateral agreement that allows their nationals to access the markets of the otherwise conservative country. For example, the United States BIT program explicitly lists investment liberalization as one of its basic goals.³⁶ The American BIT encourages foreign countries to adopt "market-oriented domestic policies that treat private investment fairly."³⁷ Therefore, one of the aims of the BIT movement has been to reduce internal barriers for FDI, through treaty provisions on investment promotion, admission, and establishment.³⁸

The BIT obligations of a state owed to the foreign investor *before* entering the host country, or pre-establishment, are called "investment liberalization provisions."³⁹ The totality of obligations owed to him *after* entering the host country and establishing his economic project, post-establishment, are referred to as "treatment provisions."⁴⁰ Treatment provisions are the standards of treatment and protection that the foreign investor is entitled to after establishing his project, and which the state undertakes to preserve and maintain throughout the project term. The investment liberalization provisions are the obligations that the state undertakes in order to encourage and facilitate the admission of inbound investments coming from the other state party

³⁶ Jeffrey Lang, *KEYNOTE ADDRESS: The International Regulation of Foreign Direct Investment: Obstacles & Evolution (Symposium)*, 31 CORNELL INTERNATIONAL LAW JOURNAL 455, 457 (1998).

³⁷ *Id.* at 457.

³⁸ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 214 (Oxford University Press 2 ed. 2015).

³⁹ Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 82 (2005).

⁴⁰ *Id.* at 82.

to the BIT. Hence, investment liberalization provisions serve to encourage and promote foreign investment and facilitate its entry, rather than giving protection to the potential investment.

The investment liberalization goal of a BIT is usually expressed in its preamble where the contracting parties express their wish to “create favorable conditions for greater investment by investors of one country in the other country.”⁴¹ Thus, BITs place an obligation upon host countries to promote FDI from treaty partners by creating “favorable conditions” within their territories. However, BITs usually do not specify the practical measures that should be taken by the host country to create these “favorable conditions.” The notion of “favorable conditions” is very wide, and it can range anywhere from political, economic, and social conditions to the liberalization of laws, policies, and administrative decrees, to reforms in the judicial and administrative authorities. Consequently, this obligation is naturally vague and difficult to implement. The absence of a clear definition, or threshold, to determine when a state has reached that level of “favorability” or what constitutes an acceptable level of favorability, makes the applicability of such an obligation even harder.

Creating “favorable conditions” does not entail automatic admission of FDI into the host country. Under the principle of state sovereignty, no state is compelled to accept any foreign investments trying to enter its economy. On the contrary, a state is entitled to regulate all economic activity on its soil.⁴² It is hard to imagine, although possible, that a country will be

⁴¹ The Preamble of the AGREEMENT BETWEEN JAPAN AND THE KINGDOM OF SAUDI ARABIA FOR THE PROMOTION AND PROTECTION OF INVESTMENT (2013). See also Article 2 of the Agreement between the Government of the State of Israel and the Government of the Republic of the Union of Myanmar for the Reciprocal Promotion and Protection of Investments (2014).

⁴² RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 88 (Oxford University Press 2 ed. 2012).

willing to adopt an “open door” policy were it will accept any type of inward investment.⁴³ Many considerations restrain a country from doing so, such as public policy, national security, economic security, development objectives, social and cultural sensitivities, political motives, and others.

Investment liberalization aims to promote and encourage FDI, while preserving the host country’s right to regulate its admission. Hence, the contracting parties in most BITs usually stress that foreign investments are admitted to the host country only if they are made “in accordance with its laws and regulations.”⁴⁴ As a consequence of adopting such language in the BIT, only investments that comply with the host country laws are admitted and entitled to treaty protection. The host country will enact local laws that regulate, encourage, and prohibit inward investments in accordance with its national interests and development objectives. This allows the host country to retain control over the entry of foreign capital, in addition to the ability to screen and eliminate undesired FDI in accordance with its national laws.⁴⁵

Some countries have taken a different approach in their BITs in this regard. The United States, followed by Canada, Japan, and Turkey, require host countries to provide admission treatment that is not less favorable than the admission treatment given to the nationals of the host country, or to any third parties, in like circumstances. The purpose of such a provision is to

⁴³ China adopted an open-door policy in 1979 to attract FDI and develop an export-based economy. Indeed the open-door policy was a success and transformed the Chinese economy into one of the largest in the world. “In 1978, China was ranked thirty-second in the world in export volume. In 1989, it became the world’s thirteenth largest exporter. Its share of world trade almost doubled during this period. Between 1978 and 1990, the average annual rate of trade expansion was above 15 percent, more than three times higher than that of total world trade.” See Shang-Jin Wei, *The Open Door Policy and China’s Rapid Growth: Evidence from City-Level Data*, in GROWTH THEORIES IN LIGHT OF THE EAST ASIAN EXPERIENCE, NBER-EASE 74 (Takatoshi Ito & Anne O. Krueger ed. 1995).

⁴⁴ e.g. Article 2(1) of the Argentine-Qatar BIT (2016).

⁴⁵ SALACUSE, THE LAW OF INVESTMENT TREATIES 219 (Oxford University Press 2 ed. 2015).

equalize competitive conditions for market entry among potential investors.⁴⁶ The U.S. Model BIT states the national treatment standard for admission in Article 3, which reads:

*Each Party shall accord to investors of the other Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory.*⁴⁷

The Model BIT goes on in Article 4 to state the Most-Favored-Nation treatment for admission, which reads:

*Each Party shall accord to investors of the other Party treatment no less favorable 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.*⁴⁸

Whatever approach a country may take regarding the admission of FDI, once the foreign investment is admitted to enter into the host country and establishes his project, that investment becomes covered under the BIT. From this point on, the treatment standards in the BIT become applicable, and serve to protect the foreign investment from the wrongdoings of the host state, in addition to vesting the foreign investor with certain rights pertaining to his investment.

C. INVESTMENT PROTECTION AND TREATMENT STANDARDS

The protection of foreign investment and property is the core of, and the original idea behind, BITs. The provisions that obligate the host country to afford FDI on its soil certain “treatment” constitute the substantive part of the BIT as they determine what protection the foreign investor

⁴⁶ Id. at 222.

⁴⁷ Article 3 (1) of the U.S. Model Bilateral Investment Treaty (2012).

⁴⁸ Id. at Article 4 (1).

enjoys. The word “treatment” can be defined in the context of investment as “the rights and privileges granted and the obligations and burdens imposed by a Contracting State on investments made by investors covered by the treaty.”⁴⁹

The treatment provisions of a BIT define a standard to which the host country must conform when dealing with foreign investors and investments.⁵⁰ Failure by the host country to conform to these provisions will render it potentially liable to pay compensations for the injury it has caused to the foreign investor. Consequently, the treatment provisions of a BIT can be described as an economic bill of rights for foreign investors.⁵¹

Treatment standards can be categorized as “general” or “specific” depending on what they protect in the investment. The general treatment standards are those standards that apply to all aspects of the investment in the host country. They include the “fair and equitable treatment”, “full protection and security”, “most favored nation treatment”, “national treatment” and “international minimum standard.” The specific treatment standards, however, apply to particular matters of the investment, such as; monetary transfers, expropriation, investor rights in times of war and disturbance, and investor employment rights.

Different BITs offer some or all of these treatment standards depending of the level of protection the BIT parties wish to provide to foreign investors and investments. BITs can also offer similar, but not identical, versions of each of these treatment standards, to limit or expand their application and protection. For example, a BIT may offer investments “complete protection and security”, “full protection and security”, “full legal protection and security,” or simply

⁴⁹ Suez, Sociedad General de Aguas de Barcelona S.A., and Vivendi Universal S.A. v The Argentine Republic, para. 55 (DECISION ON JURISDICTION), (ICSID).

⁵⁰ SALACUSE, THE LAW OF INVESTMENT TREATIES 228 (Oxford University Press 2 ed. 2015).

⁵¹ Susan D. Franck, *Conflating Politics And Development? Examining Investment Treaty Arbitration Outcomes*, 55 VIRGINIA JOURNAL OF INTERNATIONAL LAW 13, 21 (2014).

“protection and security.” Additionally, a BIT may provide these treatment standards as standalone standards where they apply independently from each other, or they may tie their application with another treatment standard. For example, the U.S. Model BIT specifies that “full protection and security” treatment requires each party to provide “the level of police protection required under customary international law.”⁵²

Treatment standards are articulated vaguely in almost all BITs, which make their interpretation by arbitral tribunals difficult, inconsistent, and pro-investor. Thus, a balance between preserving and protecting investors’ interests, and, the host country’s ability to regulate and act in the public interest, is essential. The development objective of the BIT should be given the same weight as the investment protection objective when interpreting treatment standards.

A country that anticipates development through FDI, should modify the treatment provisions in their BITs to insure that these protection standards will not obstruct it from development, nor frustrate its ability to act in its best interest. The need to draft and include limitations regarding general treatment provisions in BITs is important to achieving development through investment. Chapter 4 will discuss in detail the inconsistent interpretations of some treatment standards in investor-state arbitrations, and will illustrate how redrafting these standards can illuminate inconsistent and over-protective interpretations in the future.

⁵² See Article 5 (2) (b) of the U.S. Model Bilateral Investment Treaty (2012).

D. DISPUTE SETTLEMENT

The treatment standards and protections contained in a BIT have no value if the foreign investor cannot enforce them when breached by the host country. Investor protection requires that host countries be bound to their treaty commitments, and responsible for their injurious actions towards foreign investors. Hence, an integral part of any BIT is the investor-state dispute settlement mechanism which enables foreign investors to enforce rights and treatment standards against the host state.

The investor-state dispute settlement mechanism depends on investment arbitration as a means of dispute settlement. Distinguishing investment arbitration from commercial arbitration can be difficult, as they both fall under the notion of international, binding, third-party, dispute settlement, outside of the ordinary constitutional route of court adjudication. However, some differences exist between the two systems of arbitration which makes them distinguishable from each other. The differences lay in the legal framework governing each of the two systems.⁵³

In commercial arbitration, generally, the relevant international law that applies is the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention),⁵⁴ which deals with the recognition and enforcement of arbitration agreements and arbitral awards. However in investment arbitration, international treaties play an important substantive role, particularly the vast network of BITs, and other multilateral agreements such as the ICSID Convention. The procedural law in commercial arbitration is chosen by the parties,

⁵³ For a more detailed comparison between commercial and investment arbitrations see Karl-Heinz Böckstiegel, *Commercial and Investment Arbitration: How Different are they Today?*, 28 *ARBITRATION INTERNATIONAL (LCIA JOURNAL)* 577 (2012).

⁵⁴ Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958).

whether it be a national law, institutional rules, or the parties own rules of procedure. Whatever the parties may agree on, the procedure in commercial arbitration must always respect and conform to the mandatory legal rules of the seat in order for the award to be enforceable.⁵⁵ In investment arbitration the procedural rules are usually provided in the international treaty that governs the investment arbitration process (i.e. ICSID Convention, or NAFTA, for example). The mandatory rules of the seat only become relevant in investment arbitration if the parties agreed to arbitrate their investment disputes at a conventional arbitration institution (ICC, SCC, LCIA ... etc.). In the latter situation the mandatory rules of the seat become relevant by virtue of the seat's arbitration law and the institutional rules, which require conformity of arbitration procedure with the seat's mandatory rules.⁵⁶

Another important distinction between commercial and investment arbitration is the enforceability of awards. Unlike commercial arbitral awards, arbitral decisions awarded under ICSID do not require domestic enforcement procedures in accordance with the New York Convention and, therefore, cannot be refused enforcement *inter alia* on public policy grounds.⁵⁷ An ICSID award is equivalent to “a final judgment of a court” in all of the ICSID contracting states, and therefore is directly executable.⁵⁸ However should the investment arbitration be

⁵⁵ Id. at Article 5.

⁵⁶ For example Article 33 of the ICC Arbitration Rules provides “*Before signing any award, the arbitral tribunal shall submit it in draft form to the Court. The Court may lay down modifications as to the form of the award and, without affecting the arbitral tribunal’s liberty of decision, may also draw its attention to points of substance. No award shall be rendered by the arbitral tribunal until it has been approved by the Court as to its form.*” See Rules of Arbitration of the International Chamber of Commerce (2012).

⁵⁷ Denunciation of the ICSID Convention and BITs: Impact on Investor-State Claims § December, No. 2, at 2 (United Nations UNCTAD ed., 2010).

⁵⁸ See Article 54(1) of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965).

conducted in any forum other than ICSID it would have to be enforced in accordance with the New York Convention.⁵⁹

As disputes between foreign investors and the host countries are foreseeable, and to ensure that the foreign investors' rights under the treaty are respected, virtually all BITs contain a dispute settlement section. Under the dispute settlement section of most BITs, a sequence of procedures has to be followed by the foreign investor to resolve the dispute with the host state.

The procedure usually starts by requiring the parties – the foreign investor and the host government – to initiate amicable negotiations for a specified period of time to attempt to solve the dispute.⁶⁰ Some BITs give the parties the option to resort to non-binding conciliation during this period.⁶¹ However, if the negotiations and the conciliation procedures fail, the foreign investor has the right to submit his claim to binding arbitration. Submitting to arbitration is usually governed by time bars. Many BITs specify the passage of a certain time period from the date of the event(s) giving rise to the dispute before the investor becomes eligible to submit his dispute to arbitration, usually six months.⁶² Also BITs usually specify a statute of limitations on submitting claims to arbitration; whereby the foreign investor can only submit claims to

⁵⁹ Some countries avoid the issue of enforcement under the New York Convention, and hence avoid the possibility of non-enforcement of the award based on public policy grounds, by including a provision in the BIT which provides for the immediate recognition and enforcement of any arbitral awards rendered by an independent arbitrator or arbitration center between the foreign investor and the host state. For example Article 10 (3) of the German Model BIT reads “*The [arbitral] award shall be binding and shall not be subject to any appeal or remedy other than those provided for in the Convention or arbitral rules on which the arbitral proceedings chosen by the investor are based. The award shall be enforced by the Contracting States as a final and absolute ruling under domestic law.*” German Model Treaty (2008).

⁶⁰ See Article 7 of France Model BIT (2006). Article 23 of U.S. Model Bilateral Investment Treaty (2012). Article 25 of Canada Model Foreign Investment Promotion and Protection Agreement (2004). Article 10 of German Model Treaty (2008).

⁶¹ For example, see Article 10 of the German Model Treaty (2008).

⁶² For example, see Article 26 of the Canada Model Foreign Investment Promotion and Protection Agreement (2004). Article 24(3) of the U.S. Model Bilateral Investment Treaty (2012). Article 10 of the German Model Treaty (2008). Article 7 of France Model BIT (2006).

arbitration within a specified time period from the date of the event(s) that raised the dispute, usually three years.⁶³

Arbitral proceedings under most BITs are not limited to ICSID arbitration. In fact, a single BIT may provide for several arbitral forums to settle investor-state disputes.⁶⁴ Under such BITs, the foreign investor can choose to settle his claims at conventional arbitration centers, such as the ICC or SCC, or via *ad hoc* arbitration conducted under the UNCITRAL Arbitration Rules, or via ICSID arbitration under the Convention, or ICSID arbitration under the Additional Facility Rules if one of the state parties of the concerned BIT is not a member of the ICSID Convention.⁶⁵ By providing for all these arbitral forums in the BIT, the state parties are simultaneously giving the consent needed to establish the jurisdiction of ICSID, or other arbitral forums, for future disputes with investors from the other contracting state.

II. THE SUCCESS AND FAILURE OF BITs

There is no doubt that investment treaties have been successful in securing protection to foreign investors. The global network of BITs has become the international legal framework governing economic activities conducted by nationals of one party on the territory of the other party. BITs set the rules and treatment standards which protect foreign investors from injurious acts by the host state, such as discrimination or unreasonable measures. They also govern the procedure to be followed when disputes arise between foreign investors and the host states. On numerous

⁶³ For example see Articles 22(2) and 23(2) of the Canada Model Foreign Investment Promotion and Protection Agreement (2004). Article 26 of U.S. Model Bilateral Investment Treaty (2012).

⁶⁴ E.g. Argentine-Qatar BIT (2016).

⁶⁵ See Article 2(a) of the ICSID Additional Facility Rules (2006).

occasions, foreign investors have been able to invoke their rights under BITs, and obtain compensation for damages caused by host states actions.⁶⁶ BITs have also complemented the encouragement of foreign capital inflow into less developed countries, by boosting investor confidence in the legal framework governing their investment in the host state.⁶⁷

While BITs succeeded in providing a legal framework for the protection of foreign capital in host countries, they have failed in their second objective (i.e. economic development).⁶⁸ The origin and structure of modern BITs provide the reason for this failure. BITs were drafted and structured by capital exporting countries singularly focusing on one aspect of the investment process: to protect their investors in less developed, newly independent, countries.⁶⁹ In fact, BITs signed in the second half of the twentieth century are not different from investment treaties signed in the colonial era, other than the addition of investment liberalization provisions.⁷⁰ Hence, they were not built to enhance or encourage development, although that was a projected goal by developing countries and the international community. BITs principally

⁶⁶ In 2016 foreign investors initiated 62 known investor-state arbitrations. This is higher than the 10 year average of 49 cases per year (2006-2015). Also, in 2016 at least 57 awards were rendered. It is reported that most of those awards rendered on the merits were in favor of the investor. For detailed statics and information see *Investor-State Dispute Settlement: Review of Developments in 2016*, at 2-5 (UNCTAD ed., 2017).

⁶⁷ Studies have found that BITs “act more as a complement to, rather than a substitute for, good institutional quality and local property rights. In host countries with weak domestic institutions, including weak protection of property, BITs have not acted as a substitute for broader domestic reforms. On the other hand, countries that ‘are reforming and already have reasonably strong domestic institutions, are most likely to gain from ratifying a treaty.’” See *THE ROLE OF INTERNATIONAL INVESTMENT AGREEMENTS IN ATTRACTING FOREIGN DIRECT INVESTMENT TO DEVELOPING COUNTRIES* 36 (UNCTAD ed., UNITED NATIONS 2009). Also see Jeswald W. Salacuse 46 *HARVARD INTERNATIONAL LAW JOURNAL* 67, 111 (2005).

⁶⁸ See in general Aaron Cosbey Nathalie Bernasconi-Osterwalder, Lise Johnson, Damon Vis-Dunbar, *Investment Treaties and Why They Matter to Sustainable Development*, (2012). Sornarajah inquires “[W]hy after such a long period of foreign investment flows, no economic development has taken place and resource rich countries remain abysmally poor.” SORNARAJAH, 48 (Cambridge University Press 3 ed. 2012).

⁶⁹ See Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, 24 *THE INTERNATIONAL LAWYER* 655, 665 (1990).

⁷⁰ Howard Mann, *Reconceptualizing International Investment Law: Its Role in Sustainable Development*, 17 *LEWIS & CLARK LAW REVIEW* 521, 523 (2013).

addressed the problem of investment protection rather than encompassing the developmental aspect of FDI for host countries.⁷¹

The surge in investor-state arbitrations in the past two decades reveals that BITs are not harmless documents, but rather they can “bite.”⁷² As will be shown below, the broad and vague provisions of BITs, coupled with their expansive interpretations by arbitral tribunals, has affected host state’s ability to benefit from FDI for its development.

A. BROAD AND VAGUE PROVISIONS

Investment agreements generally consist of three sections: definitions, substantive treatment obligations for host states, and provisions for binding investor-state dispute resolution. The definitions of investments and investors are broad and inconclusive, and thus bring a wide range of economic activities under the jurisdictional scope of the treaty.⁷³ This is a result of capital exporting states drafting open-ended definitions of “investment” that aim at capturing a wide variety of economic activities under the jurisdiction of the treaty. Hence, regular economic activities may qualify as “investments” that enjoy treaty protection, although they may not be the types of economic activities that contribute to the host state’s development, nor constitute an “investment” within the meaning intended by the developing host state.

⁷¹ Kenneth J. Vandeveld, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 179 (2005).

⁷² Reforming the International Investment Regime: An Action Menu 125 (2015).

⁷³ Claire Cutler, *Human Rights Promotion Through Transnational Investment Regimes: An International Political Economy Approach*, 1 POLITICS AND GOVERNANCE 16, 21 (2013).

The treatment standards, which are usually “open-ended and ambiguous”, have no unified meaning.⁷⁴ The vague formation of treatment standards has allowed foreign investors to challenge core domestic policies of the host state that serve its development.⁷⁵ For instance, the FET standard in its typical formation can be used by investors “to challenge any type of governmental conduct that they deem unfair.”⁷⁶ This is due to its “open-ended and largely undefined nature” as the notions of “fairness” and “equality” do not prescribe a clear set of rules and are open to subjective interpretation.⁷⁷ As a result, the scope of the FET standard has varied as to the governmental and administrative actions that can be reviewed under this standard.⁷⁸ Another challenge to the FET standard is its extension to cover the “legitimate expectations” of foreign investors. Concerns have been expressed that “the potentially far-reaching application of the concept of ‘legitimate expectations’ ... can restrict countries’ ability to change investment-related policies or introduce new policies – including those for the public good – if they have a negative impact on individual foreign investors.”⁷⁹

Similarly, the requirement of “like circumstances” under the national treatment (NT) and the most-favored-nation treatment (MFN) standards created controversy among different tribunals on what constitutes a suitable comparator.⁸⁰ The typical formation of these standards

⁷⁴ Thomas Walde and Stephen Dow, *Treaties and Regulatory Risk in Infrastructure Investment: The Effectiveness of International Law Disciplines versus Sanctions by Global Markets in Reducing the Political and Regulatory Risk for Private Infrastructure Investment*, 34 JOURNAL OF WORLD TRADE 1, 45 (2000).

⁷⁵ Reforming the International Investment Regime: An Action Menu 125 (United Nations 2015).

⁷⁶ *Id.* at 137.

⁷⁷ *Id.* at 137.

⁷⁸ UNCTAD, Fair and Equitable Treatment § II (UNCTAD Series on Issues in International Investment Agreements ed., United Nations 2012).

⁷⁹ Reforming the International Investment Regime: An Action Menu 137 (United Nations 2015).

⁸⁰ Andrea K. Bjorklund, *National Treatment*, in STANDARDS OF INVESTMENT PROTECTION 38 (August Reinisch ed. 2008).

does not provide whether comparison should be based on “market sector, production methods, or physical location.”⁸¹

The vague and broad formation of different treatment standards has also created an overlap effect between them. For instance, the NT standard protects against nationality based discrimination, while the FET standard encompasses a non-discrimination obligation.⁸² Some treaties specifically prohibit the contracting parties from according “arbitrary and discriminatory” treatment to foreign investors in a separate clause.⁸³ However, such a clause overlaps with the FET standard as “any measure that might involve arbitrariness or discrimination is in itself contrary to fair and equitable treatment.”⁸⁴ A detailed discussion of different treatment standards and their application and implications on state actions will follow in the next Chapter. However, it is evident that the typical definitions and treatment standards in investment treaties need to be revised and redrafted to reduce uncertainty and over-protection arising from their broadly worded provisions.⁸⁵

⁸¹ II Charles H. Brower, *Structure, Legitimacy, and NAFTA's Investment Chapter*, 36 VANDERBILT JOURNAL OF TRANSNATIONAL LAW 37, 61 (2003).

⁸² CMS Gas Transmission Company v The Republic of Argentina, Award, para. 290 (ICSID, 2005).

⁸³ E.g. Article II(3)(b) of the Jordan-USA BIT (1997).

⁸⁴ CMS Gas Transmission Company v The Republic of Argentina, Award, para. 290 (ICSID, 2005). Also the tribunal in *Saluka* noted that a violation of the non-arbitrary measures provision does not “differ substantially from the violation of the ‘fair and equitable treatment’ standard.” See *Saluka Investments BV (The Netherlands) v The Czech Republic*, para. 461 (Partial Award), (UNCITRAL, 2006).

⁸⁵ Investor-State Dispute Settlement: Review of Developments in 2016, at 29 (UNCTAD ed., 2017).

B. REGULATORY CHILL

Another issue of current BITs is their “regulatory chill” effect,⁸⁶ as they “make it difficult for host States to regulate in socially desirable areas.”⁸⁷ The vague provisions of modern BITs denies host states certainty as to the interpretation of the commitments they undertook in the investment treaty, and the possible outcomes of treaty claims.⁸⁸ A single provision such as the fair and equitable treatment (FET) provision can encompass endless possibilities of breach depending on its interpretation.⁸⁹ As such, “difficult legal questions about the borderline between permitted regulatory activities of the State and illegal interference with investor rights” arise.⁹⁰

The loss of regulatory space creates a situation where the host state is hesitant to regulate legitimate public matters fearing liability to foreign investors.⁹¹ This limits the regulatory flexibility of the host state to “pursue not only economic development policies but other public policies as well.”⁹²

⁸⁶ Mann, 17 LEWIS & CLARK LAW REVIEW 521, 532 (2013).

⁸⁷ Definition of “Regulatory chill” available on: <http://www.igi-global.com/dictionary/regulatory-chill/44758>. Mann suggests “It is extremely difficult to chronicle the so-called “regulatory chill impact” of investment treaties whereby threats of arbitration are used to try to fend off new regulations. But it is widely accepted that investors use such threats to “warn” governments of potential consequences if a planned measure is actually taken. Governments, however, generally do not state that the reason for not adopting a measure is due to such threats.” See *id.* at n.14.

⁸⁸ *Id.* at 532.

⁸⁹ Reforming the International Investment Regime: An Action Menu 125 (United Nations 2015).

⁹⁰ *Id.* at 124.

⁹¹ “[G]overnments are widely understood to be threatened with arbitration by foreign investors if a proposed new measure is adopted. What is certain is that investor-state arbitration has shifted from being a shield of last resort to a sword of first resort in many disputes, or potential disputes, between governments and foreign investors.” See Mann, 17 LEWIS & CLARK LAW REVIEW 521, 527 (2013).

⁹² Sauvart, *in* THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT: BILATERAL INVESTMENT TREATIES, DOUBLE TAXATION TREATIES, AND INVESTMENT FLOWS 9 (Sachs ed. 2009). To give an example on the effect of BITs on the regulatory space of the host state, Peterson & Gray argue that “host states may wish to regulate the economy, including foreign investors embedded therein, in a manner which seeks to promote or protect certain human rights interests.... Where bilateral investment treaties are in place, foreign investors will often enjoy the ability to challenge these human-rights inspired measures through international arbitration.” LUKE ERIC PETERSON & KEVIN R. GRAY, INTERNATIONAL HUMAN RIGHTS IN BILATERAL INVESTMENT TREATIES AND IN INVESTMENT TREATY ARBITRATION 5 (International Institute for Sustainable Development. 2003).

C. PRO-INVESTOR INTERPRETATIONS

The vague and ambiguous language of BIT provisions has had an effect on their interpretation in investor-state arbitrations. Arbitral tribunals in investor-state disputes have expanded the interpretation of treaty provisions in a novel, and sometimes contradictory, manner to serve the goal of investment protection.⁹³ The MFN standard is a good example of contradictory and inconsistent arbitral interpretations of treaty obligations.⁹⁴ Some tribunals interpreted the MFN standard to extend to the more favorable *procedural* provisions of other BITs (specifically more favorable dispute resolution provisions),⁹⁵ while other tribunals rejected that logic.⁹⁶ In some instances, tribunals have created meanings to treaty provisions rather than discovering the meaning consistent with the parties' intent.⁹⁷ For example, the Swiss government, in response to the tribunal's decision in *SGS v. Pakistan* and its reading of the "umbrella clause" in the Switzerland-Pakistan BIT, sent a letter to the ICSID Deputy Secretary-General attaching a three-page reaction to the tribunal's decision and interpretation of the provision. In that letter, "Swiss officials stated that they were 'alarmed' by the tribunal's reading and considered it to be 'counter' to the government's intent and the intent of other states."⁹⁸ Hence, there is a broadly

⁹³ Mann notes "There was the perception that investor treaties should be broadly interpreted to reflect the purpose of protecting investors, which created expansionary interpretations of what had been thought to be fairly limited understandings of international customary law on key issues. This perception is in fact reflected in a number of arbitral awards that expressly take this perspective." Mann, 17 LEWIS & CLARK LAW REVIEW 521, 526-27 (2013).

⁹⁴ Zachary Douglas, *The MFN Clause in Investment Arbitration: Treaty Interpretation Off the Rails*, 2 JOURNAL OF INTERNATIONAL DISPUTE SETTLEMENT 97 (2011).

⁹⁵ E.g. Emilio Agustín Maffezini v The Kingdom of Spain (Decision on Jurisdiction), (ICSID, 2000).

⁹⁶ E.g. Telenor Mobile Communications A.S. v The Republic of Hungary (Award), (ICSID, 2006).

⁹⁷ Douglas, 2 JOURNAL OF INTERNATIONAL DISPUTE SETTLEMENT 97, 99 (2011).

⁹⁸ See Lise Johnson & Merim Razbaeva, *State Control over Interpretation of Investment Treaties* 7 (VALE Colombia Center on Sustainable International Investment 2014). See Also Douglas, 2 JOURNAL OF INTERNATIONAL DISPUTE SETTLEMENT 97, 99 (2011).

shared view that treaty provisions “need to be clear and detailed, and drafted on the basis of a thorough legal analysis of their actual and potential implications.”⁹⁹

By prioritizing the goal of investment protection, arbitral tribunals have “broadly interpreted [treaty provisions] to reflect the purpose of protecting investors, which created expansionary interpretations of what had been thought to be fairly limited understandings of international customary law on key issues. This perception is in fact reflected in a number of arbitral awards that expressly take this perspective.”¹⁰⁰ Some tribunals have explicitly stated their pro-investor reading of the treaty, for example one tribunal stated:

*The BIT is a treaty for the promotion and reciprocal protection of investments. According to the preamble it is intended “to create and maintain favourable conditions for investments by investors of one Contracting Party in the territory of the other.” It is legitimate to resolve uncertainties in its interpretation so as to favour the protection of covered investments.*¹⁰¹

The inconsistent, pro-investor, and expansive interpretations of the broadly worded treaty provisions have added to the failure of BITs to accommodate for the interests of host states. Exaggeration in the protection of investors on the detriment of states undermines the overall aim of the treaty (i.e. to intensify the economic relations between treaty parties to reach development), as states will be discouraged to accept new FDI into its territory to avoid any

⁹⁹ Reforming the International Investment Regime: An Action Menu 126 (United Nations 2015).

¹⁰⁰ Mann, 17 LEWIS & CLARK LAW REVIEW 521, 526-27 (2013).

¹⁰¹ SGS Société Générale de Surveillance S.A. v Republic of the Philippines, para. 116 (Decision on Jurisdiction), (ICSID, 2004).

negative consequences.¹⁰² This can also lead states to refuse concluding new BITs or terminate their existing BITs.¹⁰³

Investment disputes touch on complex questions that can go to the heart of a state's public policymaking.¹⁰⁴ They impact the way host states govern, legislate, and adjudicate due to the significance and consequences of these disputes on the host government and society alike. The expansive interpretations add to the risk of regulatory chill; as governments seek to avoid regulating in the public good due to their uncertainty of what measures may expose them to liability, and consequently pay large amounts of compensation to foreign investors.¹⁰⁵ Hence, interpretation of treaty provisions plays an important role in furthering the benefits, or alternatively increasing the costs, of the BIT system.

The goal of “economic development of the Parties” in the preambles of virtually all BITs is generally overlooked.¹⁰⁶ Under principles of international law the preambles of agreements are not legally binding on the parties. Rather, the preambles provide a platform for the parties’ to express their objectives and purposes of concluding the treaty.¹⁰⁷ The Vienna Convention on the Law of Treaties (VCLT) provides that a treaty shall be interpreted in good faith and “*in*

¹⁰² The tribunal in *Saluka* pointed out the effect of pro-investor by stating that “[A]n interpretation which exaggerates the protection to be accorded to foreign investments may serve to dissuade host States from admitting foreign investments and so undermine the overall aim of extending and intensifying the parties’ mutual economic relations.” *Saluka Investments BV (The Netherlands) v The Czech Republic (Partial Award)*, para. 300 (UNCITRAL, 2006).

¹⁰³ See footnotes 127 & 128.

¹⁰⁴ Schill, 9 CHICAGO JOURNAL OF INTERNATIONAL LAW 471, 497 (2009).

¹⁰⁵ See Mann, 17 LEWIS & CLARK LAW REVIEW 521, 532 (2013).

¹⁰⁶ See Gabriele Gagliani, *The interpretation of general exceptions in international trade and investment law: is a sustainable development interpretive approach possible?*, 43 DENVER JOURNAL OF INTERNATIONAL LAW AND POLICY 559, 568 (2015).

¹⁰⁷ Max H. Hulme, *Preambles in Treaty Interpretation* 164 UNIVERSITY OF PENNSYLVANIA LAW REVIEW 1281, 1300 (2016).

*accordance with the ordinary meaning to be given to the terms of the treaty.*¹⁰⁸ Hence, the “terms” of the treaty are the substantive material to be relied upon when designating the obligations and commitments of the parties. The preamble on the other hand, serves as a supplement to the interpretation of those terms; Article 31 of VCLT states that the *terms* of the treaty shall be interpreted “*in light of its objective and purpose.*”¹⁰⁹ Thus the preamble, *per se*, is not a source for the imposition of obligations and commitments, and holds no significant binding power. In the context of investor-state arbitration, arbitrators have on many occasions disregarded the economic and development objectives found in the preamble of the investment treaty, and interpreted the terms solely from an investment protection lens.¹¹⁰ It is crucial to include the developmental objectives in the “terms” of future BITs, to give more binding power and enforceability to them.

Unlike most tribunals, the tribunal in *Saluka Investments v Czech Republic* took a balanced approach in its treaty interpretation.¹¹¹ In its interpretation of the FET standard, the tribunal acknowledged that protection of investment is not the sole goal of investment treaties, and that a balanced interpretation of treatment standards requires taking into account the diverse goals of investment treaties, including the goal of economic development. It stated:

The protection of foreign investments is not the sole aim of the Treaty, but rather a necessary element alongside the overall aim of encouraging foreign investment and extending and intensifying the parties’ economic relations. That in turn calls for a balanced approach to the interpretation of the Treaty’s substantive provisions for the protection of investments, since an interpretation which

¹⁰⁸ United Nations, *Vienna Convention on the Law of Treaties*, 23 May 1969, United Nations, Treaty Series, vol. 1155, p. 331. Article (31)(1).

¹⁰⁹ United Nations, *Vienna Convention on the Law of Treaties*, 23 May 1969, United Nations, Treaty Series, vol. 1155, p. 331. Article (31)(1).

¹¹⁰ “Interpretations giving significant weight to the object and purpose of investment treaties have been criticized as favouring investors to the detriment of host States.” J. ROMESH WEERAMANTRY, *TREATY INTERPRETATION IN INVESTMENT ARBITRATION* 191 (Oxford University Press. 2012).

¹¹¹ *Saluka Investments BV (The Netherlands) v The Czech Republic (Partial Award)*, (UNCITRAL, 2006).

*exaggerates the protection to be accorded to foreign investments may serve to dissuade host States from admitting foreign investments and so undermine the overall aim of extending and intensifying the parties' mutual economic relations.*¹¹²

However, the approach in Saluka is not the norm among other tribunals. As illustrated above, arbitral tribunals have generally prioritized the protection of investors' interests over the legitimate and essential interests of the host state.¹¹³ The excessive investment protection provisions in BITs, and their broad interpretation by arbitral tribunals, have denied host countries from reaping the benefits of FDI, and have restricted their ability to limit their potential risks or harms.¹¹⁴ This is demonstrated by the fact that after a long period of foreign investment flows, "no economic development has taken place and resource rich countries remain abysmally poor."¹¹⁵

D. REBALANCING INVESTMENT TREATIES

Different approaches have been taken by states to re-balance the provisions of investment treaties and limit their unintended interpretations by arbitral tribunals. Many countries have revised their model BITs and incorporated limitations and exceptions that preserve their policy making flexibility and reflect their stance on the developments in investor-state arbitration.¹¹⁶

¹¹² Id. at para. 300.

¹¹³ E.g. *SGS Société Générale de Surveillance S.A. v Republic of the Philippines (Decision on Jurisdiction)*, (ICSID, 2004).

¹¹⁴ Aaron Cosbey, at Executive Summary page (International Institute for Sustainable Development 2004).

¹¹⁵ SORNARAJAH, 48 (Cambridge University Press 3 ed. 2012).

¹¹⁶ PENELOPE SIMONS J ANTHONY VANDUZER, GRAHAM MAYEDA, *INTEGRATING SUSTAINABLE DEVELOPMENT INTO INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE OF DEVELOPING COUNTRY NEGOTIATORS 2* (Commonwealth Secretariat. 2013).

The usual 8-10 page model BIT has now become a complex document of over 50 pages.¹¹⁷ For example, in response to the interpretation of the tribunal in *Maffezini*,¹¹⁸ (that the MFN standard extends to the more favorable dispute resolution provisions found in other BITs) the Norwegian Model BIT was amended to include the following exception “*For greater certainty, treatment referred to in paragraph [MFN] does not encompass dispute resolution mechanisms provided for in this Agreement or other International Agreements.*”¹¹⁹ The United States and Canada, for example, drawing on their experience as respondents in NAFTA cases, have revised their model BITs to clarify the scope and meaning of different investment obligations.¹²⁰ South Africa revised its investment policy after it concluded that “BITs and international arbitration pose unacceptably high risks to the government's right to regulate in the public interest.”¹²¹ India's reconsideration of its BIT program was related to concerns about the imbalance between investment protection and the Indian state's regulatory power.¹²²

Other countries have issued joint interpretations of certain articles of their investment treaties, to unify their application and limit expansive interpretations by future tribunals. For instance, following concerns by the NAFTA parties regarding interpretations of the “fair and equitable treatment (FET)” standard, the NAFTA parties issued the following joint interpretation which is binding on future tribunals:

1) Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investors of another Party.

¹¹⁷ Andrew Newcombe, General Exceptions in International Investment Agreements: Draft Discussion Paper Prepared for BIICL Eighth Annual WTO Conference 13th and 14th May 2008, London 2 (2008).

¹¹⁸ Emilio Agustín Maffezini v The Kingdom of Spain (Decision on Jurisdiction), (ICSID, 2000).

¹¹⁹ Norway Model BIT (2015). Article 4(3).

¹²⁰ Reforming the International Investment Regime: An Action Menu 124 (United Nations 2015).

¹²¹ David Gaukrodger, The Balance Between Investor Protection and the Right to Regulate in Investment Treaties: A scoping paper 9 (OECD Working Papers on International Investment ed., 2017).

¹²² Id. at 9.

2) *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.*

3) *A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).*¹²³

Recent BITs now include language that permits the state parties to issue binding interpretations of treaty provisions. The Canada-China BIT, for example, enables the state parties to “take any action as they may jointly decide, including ... issuing binding interpretations of [the] Agreement.”¹²⁴ Some countries have exchanged diplomatic notes with their BIT partners to confirm their understanding of a treaty provision. Argentina and Panama took such a step when they exchanged diplomatic notes regarding their shared understanding that the MFN clause in their BIT “did not and never was intended by them to extend to dispute resolution clauses.”¹²⁵

All these efforts illustrate the growing need for a revised BIT system. A recent report notes that “the outcome of many disputes hinged upon the wording of specific provisions in the applicable IIA. This underlines the importance of balanced and careful treaty drafting and the need to reduce uncertainty arising from (broadly worded) provisions.”¹²⁶ The following chapter will discuss certain provisions and treatment standards of current BITs and their application and interpretation. It will also provide some policy guidelines on how to limit the expansive application and interpretation of these provisions in future BITs to achieve the goal of host state development.

¹²³ Interpretation of the Free Trade Commission of Certain Chapter 11 Provisions, section B, July 31, 2001, available at <https://www.state.gov/documents/organization/38790.pdf>.

¹²⁴ Article 18(2) of the Canada-China BIT (2012).

¹²⁵ Razbaeva, 6 (VALE Colombia Center on Sustainable International Investment 2014).

¹²⁶ Investor-State Dispute Settlement: Review of Developments in 2016, at 29 (UNCTAD ed., 2017).

CONCLUSION

Existing investment treaties do not address the issue of host state development. They do not contribute to the development of host countries because of the public policy constraints they impose on host countries. This is coupled with the expansive and unpredictable interpretations by some arbitral tribunals to different treaty provisions. Thus, the future of BITs is being scrutinized; as many countries are becoming more hesitant to enter in, or renew their, BITs.¹²⁷ Some countries have withdrawn from the ICSID Convention, while others have expressed their desire to exclude investor-state arbitration from their future BITs.¹²⁸ Accordingly, a backlash towards the use of investment treaties is foreseeable,¹²⁹ should they remain to be seen as a detrimental to state sovereignty to regulate and take measures that preserve its public interests.¹³⁰ A new generation of investment treaties that accommodate the interests of the host state equally with the interests of foreign investors need to emerge to maintain the current BIT system.¹³¹

¹²⁷ Some States have terminated certain agreements or refrained from concluding (new) investment agreements. Most recently are the decrees signed by President Correa of Ecuador on 16 May 2017 to terminate “16 Bilateral Investment Treaties (BITs), including with the US, Canada, China and eight European countries.” See news article on TNI website <https://www.tni.org/en/article/ecuador-terminates-16-investment-treaties>. Other countries have previously terminated certain of their BITs; “Venezuela (e.g., with the Netherlands in 2008), South Africa (e.g., with Germany, Switzerland and the Netherlands in 2013), Ecuador (e.g., with Cuba, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, the Dominican Republic and Uruguay in 2008), or the announcement of Indonesia to terminate its investment treaties (e.g., with the Netherlands as of 2015).” Andreas R. Ziegler, *Special Issue: Towards Better BITs? – Making International Investment Law Responsive to Sustainable Development Objectives*, 15 THE JOURNAL OF WORLD INVESTMENT & TRADE 803 (2014); id. at 804.

¹²⁸ “A variation has been the termination of the participation in the ICSID Convention or the negotiations of BITs without investor-State dispute settlement. Venezuela denounced the ICSID Convention in 2012, Bolivia had done so already in 2007 and Ecuador in 2010. Australia and the United States have concluded a comprehensive free trade agreement (Australia-United States Free Trade Agreement – AUSFTA) in 2004 that included an investment chapter, but did not contain an investor-State dispute settlement mechanism.” See id. at 804-05.

¹²⁹ Alvarez, 86 PROCEEDINGS OF THE ANNUAL MEETING (AMERICAN SOCIETY OF INTERNATIONAL LAW) 544, 555 (1992).

¹³⁰ Ziegler, 15 THE JOURNAL OF WORLD INVESTMENT & TRADE 803, 804 (2014).

¹³¹ “A key challenge is promoting investment in areas that make the greatest contribution to sustainable development. This requires a new generation of investment promotion and facilitation strategies, tools, institutions

Future BITs should respond and reflect the developments and jurisprudence of investor-state arbitrations. Their provisions should be well drafted in a manner that clearly details and indicates the parties' intent and interpretation of the treaty provisions.¹³² The treatment standards should be narrowed down by the use of exceptions and reservations that limit their application to their intended purpose. This will limit the potential of expansive interpretations by arbitral tribunals in future disputes. Future BITs should take a balanced approach towards the preservation of all parties' interests, by allowing the host country the flexibility to pursue its legitimate economic policy objectives without the fear of liability to foreign investors.

The next Chapter 4 will discuss certain sections of the modern BIT. It will discuss the application and interpretation of some of the most important provisions and treatment standards in modern BITs. Chapter 4 will also provide some policy guidelines and recommendations that limit the expansive interpretations that go against the host state's interests. These policy guidelines and recommendations are a reflection of the developments and interpretations of such provisions and treatment standards by investor-state arbitration tribunals.

and partnerships.” Investment Policy Framework for Sustainable Development, at Executive summary page (UNCTAD 2015).

¹³² See Razbaeva, 7 (VALE Colombia Center on Sustainable International Investment 2014).

CHAPTER FOUR

FOREIGN INVESTMENTS, INVESTORS, AND TREATMENT STANDARDS

INTRODUCTION

States, as sovereigns, have the right and obligation to ensure the security and development of the territories and societies they govern.¹ The development objectives and security concerns of a country dictate its policy on the entry of persons and capital. Foreign investors and investments are no exception. Host countries want to ensure that foreign investors entering their soil to establish economic projects will benefit the country's development agenda and will not cause harm to its economic security. Accordingly, states enact laws and regulations that aim at maximizing the benefits and minimizing the risks of incoming investments.²

One of the tools used by states to attract FDI is signing bilateral investment treaties (BITs) with other states. In a BIT, the two states agree on the types of investments and investors they aim to attract by offering those investments protections and incentives. In exchange for this protection, the host country anticipates a positive contribution by the foreign investment to its

¹ Emilio J. Cardenas, *The Notion of Sovereignty Confronts a New Era*, in *ECONOMIC DEVELOPMENT, FOREIGN INVESTMENT AND THE LAW* 13 (Robert Pritchard ed. 1996).

² JESWALD W. SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 18 (Oxford University Press. 2013).

economy and development. This relationship between foreign investments and host countries is referred to as the ‘grand bargain.’³ The host country provides protection to the foreign investor in exchange for the resources and spillovers from the foreign investments that help the host country in its development.

Although FDI can contribute positively to the host state economy and development, it may also cause damage. The notion that ‘all investment is good investment’ is absolute.⁴ Therefore, host countries seeking development through FDI should attract those investments that they deem beneficial to their development. To encourage the inflow of useful or beneficial investments to the host country, the latter should tailor the definitions of investments and investors in their BITs to that end.

A key element in any investment treaty is its provisions defining foreign “investment” and foreign “investor.”⁵ These definitions determine if an investment qualifies for protection under the investment treaty or enjoys incentives under local laws. They are also used to establish ICSID jurisdiction if a dispute arises between the foreign investor and the host country.

The treatment standards prescribed to the “investment” and “investor” under the BIT determine the scope of protection enjoyed by the foreign investor. They constitute a scale to evaluate what measures and actions by the host state infringe upon the foreign investor’s rights under the BIT. Thus, the treatment standards are the substantive part of any BIT.

In this Chapter, I begin with the definitions and interpretations of “investment” and “investors” in modern investment treaties, the ICSID Convention, and arbitral decisions. I then

³ See Nicholas P. Sullivan and Jeswald W. Salacuse *Do Bits Really Work?: An Evaluation Of Bilateral Investment Treaties And Their Grand Bargain*, 46 HARVARD INTERNATIONAL LAW JOURNAL 67 (2005).

⁴ See Howard Mann, *Reconceptualizing International Investment Law: Its Role in Sustainable Development*, 17 LEWIS & CLARK LAW REVIEW 521, 530 (2013).

⁵ SALACUSE, 365 (Oxford University Press. 2013).

explore how their broad definitions in the current system can allow harmful or undesirable investments in host countries, negatively affecting their economies. Next, I propose amendments that enable developing countries to promote development through foreign investment and attract quality investments that will effectively contribute to their development objectives. This can be achieved by amending the current standard definitions to avoid the arbitral controversy regarding their interpretation, and give more clarity to the economic activities, and persons, encompassed within them.

Later in the chapter, I discuss the scope, application and interpretation of treatment standards. I explore the current expression of these standards in BITs and their interpretation by arbitral tribunals and the controversies that arose in this context. I propose policy guidelines addressing the ambiguity of the scope and interpretation of these treatment standards. The proposed amendments will provide policy flexibility for host countries, allowing enhanced development without the fear of liability to foreign investors.

I. THE DEFINITION OF ‘FOREIGN INVESTMENT’

A. THE TERM ‘FOREIGN INVESTMENT’

The term ‘Investment’ or ‘to invest’ can be generally defined as the act of committing resources by a natural or legal person to a specific purpose in order to gain profit.⁶ It is derived from the

⁶ Id. at 1.

Latin word *investire*, which means “to clothe.”⁷ An investor “cloths” an enterprise with capital during the process of investment to gain revenue.⁸ In other words, the act of laying out money and other resources in such a manner that it may yield income is defined as an investment.⁹ An ‘Investor’ is the natural or legal person who commits resources to a project for the purpose of gaining revenue, or simply, the “one who cloths or invests.”¹⁰

The term “foreign investment,” on the other hand, has no unified definition. It is a term that has changed over time with the development of international economic relations.¹¹ Before the emergence of this term, international treaties used the term “foreign property,” which referred to property and financial interests owned by foreign nationals in the host state.¹² At that time, international law only protected the tangible property of aliens, and state responsibility for injuries to aliens arose only in the context of physical harm to the alien or his tangible property.¹³ Intangible property was not protected, presumably because the creation of intangible property was dependent on the extent to which the local laws of the host state recognized such rights.¹⁴

After the mid-twentieth century, investment forms evolved from simple ownership of land, plantations, vessels, bonds and the like, to more complex transactions that involved technology, consolidated business enterprises, complex financial instruments, trademarks, etc. These new types of property rights needed to be protected. The static notion of “property” is not broad enough to comprehend the latter developments in international investment. Hence the need

⁷ OXFORD ENGLISH DICTIONARY, "INVESTMENT, N." (Oxford University Press.).

⁸ SALACUSE, 1 (Oxford University Press. 2013).

⁹ Ballentine’s Law Dictionary: <https://advance.lexis.com/api/permalink/b52d31a3-10e7-431e-aa9f-0cc6055a653d/?context=1000516>.

¹⁰ OXFORD ENGLISH DICTIONARY, "INVESTOR, N." (Oxford University Press.).

¹¹ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 7-8 (2011).

¹² International Investment Law: Understanding Concepts and Tracking Innovations. 46-47 (OECD 2008).

¹³ SORNARAJAH, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT 11 (Cambridge University Press 3 ed. 2012).

¹⁴ Id. at 190-91.

to include a wider range of tangible and intangible property rights dictated the need to replace the term “foreign property” with the more dynamic and encompassing term “foreign investment.”¹⁵

B. THE TERM ‘FOREIGN DIRECT INVESTMENT (FDI)’

Before addressing the definition of FDI, an important distinction has to be made between the main types of foreign investment. Traditionally, foreign investments have been categorized as either direct investments (FDI) or portfolio investments (indirect investments).¹⁶ Foreign direct investment is the type of investment that most states aim at attracting and is the subject matter of bilateral investment treaties. Portfolio investments, however, have been controversial in respect to their protection under investment treaties.¹⁷ This distinction between direct and indirect (portfolio) investments stems from the different characteristics of each and their benefits to the host state.

1. Foreign Direct vs Indirect Investments

A foreign direct investment (FDI) results when a natural or legal person, usually a corporation, from one state (the “home state” or “capital exporting state”), commits resources and assets, whether tangible or intangible, in another state (the “host state” or “capital-importing state”) for the purpose of gaining profit. The foreign investor in direct investments exercises a degree of

¹⁵ P. Juillard, *L'évolution des sources du droit des investissements*, THE HAGUE ACADEMY OF INTERNATIONAL LAW 24 (1994). Referred to in [Understanding Concepts and Tracking Innovations. 47 (OCED 2008)].

¹⁶ International Investment Law: Understanding Concepts and Tracking Innovations 47 (OCED ed., 2008).

¹⁷ See below for a discussion on the issue of portfolio investments and their protection under BITs.

control and influence in the management of the enterprise.¹⁸ Hence, direct investments are physical, long-term investments where the foreign investor effectively manages and controls the enterprise in the host state.¹⁹ The foreign investor transfers capital, technology, know-how, trademarks, personnel and other resources to the host country. He employs local labor and provides a new service or commodity in the host economy. Consequently, direct investments provide the host state with new resources and enable the host state to benefit from the spillover effect of such imported resources for its economic development. For that reason, countries seek FDI and offer protection and incentives to foreign investments in their BITs and national laws to encourage their inflow.

Portfolio investments (indirect investments), on the other hand, are made by a resident of one country through the purchase of shares, or other financial instruments, in an enterprise located in another country.²⁰ Usually this purchase happens in international stock markets.²¹ Here, there is no direct linkage between the investor and the host country, as there is no transfer of resources, no physical presence, and no intention for a long-term relationship with that country. The investor does not control or have influence over the management of the enterprise; he is merely trading in shares to gain profit.²²

¹⁸ See the definition of the IMF Balance of Payments “A direct investment relationship arises when an investor resident in one economy makes an investment that gives control or a significant degree of influence on the management of an enterprise that is resident in another economy.” Balance of Payments and International Investment Position Manual para. 6.9 (BPM6). (2009).

¹⁹ See OECD Benchmark Definition of Foreign Direct Investment, 4th Edition, para. 11 (2008), where foreign investment is defined as “a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of *establishing a lasting interest* in an enterprise resident in an economy other than that of the investor (the direct investment enterprise). The motivation of the direct investor is *a strategic long-term relationship* between the direct investment and the enterprise which allows a *significant degree of influence* by the direct investor *in the management* of the direct investment enterprise.” [emphasis added].

²⁰ SORNARAJAH, 190 (Cambridge University Press 3 ed. 2012).

²¹ Id. at 9 & 190.

²² SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 29 (United Nations 2011).

There is a consensus in the field of international investment law that 10 percent voting power or more by a foreign investor in a local enterprise renders the investment a direct one.²³ The OECD Benchmark Definition of FDI characterizes a direct investment as one where the foreign investor owns a lasting interest in an enterprise located in an economy other than his own. This lasting interest “is evidenced where the direct investor owns at least 10 percent of the voting power of the direct investment enterprise.”²⁴ The IMF Balance of Payments Manual sets the threshold of control and influence required for a direct investment to be “10 percent or more of the voting power in the investment enterprise.”²⁵

Whether portfolio investments are protected investments under investment treaties is a controversial issue outside the scope of this Chapter. However, it is sufficient to say here that portfolio investments are not the type of foreign investments that the drafters of most investment treaties intended to cover and protect.²⁶ Unless the investment treaty contains explicit language that covers portfolio investments, any foreign investor holding less than 10 percent control in an enterprise is not a direct investor (*i.e.*, portfolio investor) and thus does not benefit from the investment treaty, which is normally aimed at foreign direct investments.²⁷

²³ SALACUSE, 6 (Oxford University Press. 2013).

²⁴ OECD Benchmark Definition of Foreign Direct Investment, 4th Edition, para. 11 (OECD ed., 2008).

²⁵ IMF Manual at para 6.12, in this regard it is important to note that the Manual considers indirect control or influence of an enterprise as direct investment. Indirect control or influence may be achieved when an enterprise has voting power in another enterprise that has voting power in the investment. *See* para 6.12 of the Manual.

²⁶ *See* the Legal Opinion of M. Sornarajah, In *El Paso Energy International Company v The Republic of Argentina*, Case No. ARB/03/15, Submitted to ICSID tribunal on 5 March 2007., (ICSID).

²⁷ Portfolio investors cannot invoke treaty protection for measures taken against the company in general. They can, however, invoke treaty protection if the host country measures are aimed towards the foreign shareholders directly, such as expropriation of their shares. Measures taken against the company in general or against the economic sector in which the company is involved in, even if they had a negative impact on the foreign portfolio shareholders, are not sufficient to give rise to treaty protection. In portfolio Investments, it is the ‘rights’ of the foreign shareholders that are protected, not their ‘interests.’ *See* SORNARAJAH, 190 (Cambridge University Press 3 ed. 2012).

The criterion used to differentiate between FDI and portfolio investments is the degree of control and influence enjoyed by the foreign investor in the local enterprise.²⁸ Control, for this purpose, does not mean owning the majority of shares in the enterprise, but rather having an effective right to participate in the management of the enterprise.²⁹ Accordingly, as a general rule, a direct investment is an equity interest in an enterprise that gives the foreign investor 10 percent or more voting power in an enterprise.³⁰ An investment that gives the investor less than 10 percent voting power is considered an indirect (portfolio) investment.

2. Equity Participation in Joint-Ventures

A distinction must also be made between portfolio investors and foreign investors who establish local enterprises in the host state to carry out the activities of their investments. Many national laws require foreign investors to establish a local company, or joint-venture, as a vehicle to carry out investment activities in the host state.³¹ In this case, similar to the concept of portfolio investments, the foreign investor owns shares in a local enterprise. However, contrary to portfolio investments, the foreign investor has control and influence over the management of that enterprise. The foreign investor usually transfers more than mere capital to the joint-venture enterprise, such as equipment, experts, and technology. The foreign investor also intends a long-

²⁸ *Id.* at 9. *See also* SALACUSE, 6 (Oxford University Press. 2013).

²⁹ Balance of Payments and International Investment Position Manual para. 6.12 (BPM6) (FUND ed., 6 ed. 2009).

³⁰ SALACUSE, 6 (Oxford University Press. 2013).

³¹ RUDOLF DOLZER & CHRISTOPH SCHREUER, *PRINCIPLES OF INTERNATIONAL INVESTMENT LAW* 50 (Oxford University Press 2 ed. 2012). For example, the Jordanian ‘Control of Foreign Investment Regulation of 2016’ categorizes the economic activities and sectors which foreign investors can investment in. The Regulation provides the economic sectors and activities were foreign investors can own up to 100% of the enterprise (article 3), the activities and sectors which foreign investors can own an equal share of 50% with a Jordanian partner (article 4), the activities and sectors which foreign investors can own only a minority share not exceeding 49% of the enterprise with a Jordanian majority partner (article 5), and activities and sectors were foreign investors are not allowed to invest in, *i.e.*, activities that are exclusive to Jordanians (article 6).

term stay in the host country, and is not simply trading in shares. Therefore, foreign shareholders of locally incorporated enterprises are protected under BITs and are not considered portfolio investors if they exceed the 10 percent threshold of control.

C. THE DEFINITION OF ‘INVESTMENT’ UNDER BITs

The state parties to an investment treaty define investment by enumerating the generic categories of assets and rights that are subject to the substantive protections of the treaty. Therefore, the scope of protection of the investment treaty is mutually determined by the contracting parties in the definition of “investment.” Yet whether a foreign investor acquires a particular right *in rem*, and the scope of that right, are matters determined by the municipal law of the host country.³² Thus the BIT definition of investment, which declares the general categories of protected investments, safeguards against unilateral change in the treaty’s scope by the host country via amending its national laws. However, the definition of investment in the BIT does not “detach the rights *in rem* that underlie those investments from the municipal law that creates and gives recognition to those rights.”³³

The definition of “investment” in a BIT has many implications - not only for the foreign investor, but also for the contracting states. Hence, treaty states should devote extra care and time when drafting the definition. The current practice in most BITs is to include an asset-based definition of investment. This type will be explored in further detail below. However, while the

³² See ZACHARY DOUGLAS, *THE INTERNATIONAL LAW OF INVESTMENT CLAIMS* 72-73 (Cambridge University Press, 2009).

³³ *Id.* at para. 123.

majority of investment treaties use the asset-based definition, albeit in various versions, other types of definitions exist.³⁴ For example, the *enterprise-based* definition defines “investment” as the establishment or acquisition of *a business enterprise*, or acquiring a controlling share in a business enterprise in the host country.³⁵ This type of investment is more akin to direct foreign investments and excludes portfolio investments.³⁶ This is in contrast to *asset-based* definitions, which define “investment” as *any asset* transferred to the host country. Asset-based definitions therefore do not necessitate the creation of an enterprise or participation in an already existing enterprise in the host country, as do enterprise-based definitions. The asset-based definition has three main versions:

1. Open Asset-Based Definitions

The definition of investment is found at the beginning of the BIT, usually in the definitions article. Most BITs adopt an asset-based definition for investment, which covers both tangible and intangible assets of the foreign investor. Such definitions tend to be broad in scope by defining investment as “every kind of asset”³⁷ or “any type of property.”³⁸ This broad definition of investment comes as a response to the complexity of modern international finance and the creativity of investors.³⁹

³⁴ For example, the enterprise-based definition which defines investment as the establishment or acquisition of a business enterprise, or acquiring a controlling share in a business enterprise.

³⁵ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 22 (United Nations 2011).

³⁶ See Note by the Chairman - DEFINITION OF INVESTOR AND INVESTMENT, Negotiating Group on the Multilateral Agreement on Investment (MAI) (OECD ed., 1995).

³⁷ For example, Japan - Uruguay BIT (2015). Article 1(a).

³⁸ For example, INVESTMENT COOPERATION AND FACILITATION AGREEMENT BETWEEN THE FEDERATIVE REPUBLIC OF BRAZIL AND THE REPUBLIC OF MALAWI (2015). Article 2(1).

³⁹ Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67, 80 (2005).

Capital exporting states prefer a broad definition of investment in their BITs to protect all types of outbound investments. They aim to capture most forms of investment, which continue to evolve rapidly, under the umbrella of treaty protection. Hence, they accompany the asset-based definition with a non-exhaustive list of generic categories that illustrate the forms an investment can take. The purpose of the non-exhaustive list is to make clear that the treaty's protection of investment does not depend on the particular form an investment takes,⁴⁰ and to illustrate that all forms of assets, whether tangible or intangible, are covered under the protection of the treaty. The U.K Model Investment Treaty may be taken as an example of what an open asset-based definition will generally include:

*“investment” means every kind of asset, owned or controlled directly or indirectly, and in particular, though not exclusively, includes: (i) movable and immovable property and any other property rights such as mortgages, liens or pledges; (ii) shares in and stock and debentures of a company and any other form of participation in a company; (iii) claims to money or to any performance under contract having a financial value; (iv) intellectual property rights, goodwill, technical processes and know-how; (v) business concessions conferred by law or under contract, including concessions to search for, cultivate, extract or exploit natural resources.*⁴¹

Most BITs adopt a similar open asset-based definition of investment, which gives protection to a wide variety of property both tangible and intangible.⁴² The transfer of technology and know-how, as well as the use of well-known trademarks, require that intangible rights be recognized as protected investments. Also, licenses, permits and concessions that are a matter of administrative law are also included in the definition of protected investments. This

⁴⁰ The tribunal in *Siemens v Argentina* noted that “*The specific categories of investment included in the definition are included as examples rather than with the purpose of excluding those not listed.*” *SIEMENS A.G. v THE ARGENTINE REPUBLIC* para. 137 (Decision on Jurisdiction), (ICSID 2004). See also *JESWALD W. SALACUSE, THE LAW OF INVESTMENT TREATIES* 177 (Oxford University Press 2 ed. 2015).

⁴¹ UK Model BIT (2008). Article (1)(a).

⁴² UNCTAD, *BILATERAL INVESTMENT TREATIES 1995–2006: TRENDS IN INVESTMENT RULEMAKING* § UNCTAD/ITE/IIT/2006/5, at 8 (United Nations 2007).

inclusion is not out of mere caution by the capital-exporting country, but rather recognition that some permits and licenses given by the host country's administrative authorities are vital to the foreign investment. In fact, the survival of some investment projects, such as those in the mining and extracting sectors, depend on the existence of such public law rights.⁴³

The asset-based definition approach is beneficial to the capital-exporting country, as it captures a very wide range of investment forms under the protection of the treaty. However, such an approach may be disadvantageous to the host country, which seeks the other end of the bargain when concluding a BIT: economic development. The asset-based definition gives protection to investments that may not contribute to the development of the host country, and may even give protection to some economic activities that caused harm to the host economy, such as those exploitive of the host state's natural resources. The wide range of protected investments in the asset-based definition may also result in unpredictability; as the host country will find it difficult to determine which investments qualify for protection, in order to comply with its obligations and avoid disputes. Finally, the phrase "every kind of asset" may give protection to economic activities that are not "investments" by their nature. As one commentator explains:

*If, by way of illustration, the legal characteristics of an investment were to be considered in isolation from the common sense economic meaning of that term, then, pursuant to some investment treaty definitions of an investment, a metro ticket might qualify as a 'claim to money or to any performance under contract, having a financial value' and thus as an investment.*⁴⁴

Hence some investment agreements add another dimension to the asset-based definition by requiring that the underlying asset must have "the characteristics of an investment."

⁴³ SORNARAJAH, 192 (Cambridge University Press 3 ed. 2012).

⁴⁴ DOUGLAS, 163 (Cambridge University Press. 2009).

2. Asset-Based Definitions Requiring Investment Characteristics

The U.S. Model BIT defines investment as “every asset that an investor owns or controls, directly or indirectly, *that has the characteristics of an investment*, including such characteristics as the *commitment of capital* or other resources, *the expectation of gain or profit*, or the *assumption of risk*.⁴⁵ The definition then proceeds to list a non-exhaustive list of investment forms.

By adding the three characteristics of an investment (capital, expectation of profit, and risk), the state parties of the investment treaty clarify that ordinary trade and purely financial transactions do not qualify as covered investments.⁴⁶ It provides objective criteria for interpreters when distinguishing between covered investments and ordinary trade transactions. It also provides host countries seeking development from foreign investment the assurance that only substantial investments that contribute to their development are protected, as short-term economic activities usually do not contribute to the host state’s development due to their instability and volatility.⁴⁷

Unfortunately, the characteristics of investment provided for in such treaties are neither exhaustive nor well-defined. Hence, they too do not provide certainty. For example, what is the minimum amount of capital or resources required for an economic activity to qualify as an investment? How is the risk to be assessed? Do all three characteristics (capital, profit, and risk)

⁴⁵ U.S. Model Bilateral Investment Treaty (2012). Article 1. *See also* AGREEMENT BETWEEN JAPAN AND THE ORIENTAL REPUBLIC OF URUGUAY FOR THE LIBERALIZATION, PROMOTION AND PROTECTION OF INVESTMENT (2015).

⁴⁶ Emmanuelle Cabrol, *Pren Nreka v. Czech Republic and The Notion of Investment Under Bilateral Investment Treaties*, in YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2009-2010, at 228 (Karl Sauvant ed. 2010).

⁴⁷ SALACUSE, THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL 181 (Oxford University Press. 2013).

need to exist for an investment to be identified or only some? As these questions do not have definite answers, some countries have opted for a more narrow, “closed asset-list,” definition of investment in their BITs.⁴⁸

3. Closed Asset-List Definitions

Some states adopt a “closed list” definition for investment in their BITs. The closed-list approach provides an extensive asset-based list of tangible and intangible property that is *exhaustive rather than illustrative*.⁴⁹ The closed list may also contain explicit exclusions of certain commercial transactions, such as sales contracts and financial loan agreements that involve no capital risk.⁵⁰

The use of closed-list definitions is emerging as a trend in investment treaty-making.⁵¹ This is due to the high level of certainty and control such a definition gives to contracting parties through the identification of economic activities that are covered under treaty protection. It also allows host countries seeking development through FDI to ensure that only desirable foreign investments will be protected. Hence for a developing country, the use of a closed-list definition in its BITs might be the most suitable option to manage its liability and protect desired investments.

Regardless of which definitional approach the contracting parties may decide to adopt in their investment treaty, certain limitations or additional requirements can be added to the definition. The purpose of these additional requirements is to limit the treaty’s protection to those

⁴⁸ For example *see* the Canada Model Foreign Investment Promotion and Protection Agreement (2004). Article 1.

⁴⁹ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 29 (United Nations 2011).

⁵⁰ *See* Canada Model Foreign Investment Promotion and Protection Agreement (2004). Article 1.

⁵¹ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 114 (United Nations 2011).

investments that fulfill the definition and also comply with the additional conditions imposed in the investment treaty.

D. LIMITATIONS ON THE DEFINITION OF INVESTMENT UNDER BITs

The limitations on treaty protection for foreign investments can take several forms. One form is the requirement that the investment is made in accordance with the national laws of the host state.⁵² Another form is the requirement that the foreign investment obtains approval from the host country's government.⁵³

1. Conformity with the Host State's Legislation

Most BITs condition treaty protection on compliance of the investment with the municipal laws of the host state. Thus, these treaties not only offer protection to investments that fit the treaty definition of an "investment," but also add that the investment must be made "*in accordance with the* [host country's] *laws.*"⁵⁴ Thus, if the investment violates the national legislation of the host state, it will automatically lose treaty protection. This requirement serves to ensure that foreign investors do not benefit from their own wrongdoing by not observing the host state's

⁵² See for example; Japan - Ukraine BIT (2015), Colombia - Turkey BIT (2014), Brazil - Chile BIT (2015), Azerbaijan - San Marino BIT (2015), Colombia-Israel FTA, Kuwait - Mauritius BIT (2013).

⁵³ This approach is followed, mainly, by Malaysia and Singapore in their investment treaties.

⁵⁴ For example the Canada – Slovenia BIT defines 'investment' as "*any kind of asset held or invested either directly or indirectly by an investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's laws and, in particular, though not exclusively, includes ...*" AGREEMENT BETWEEN CANADA AND THE SLOVAK REPUBLIC FOR THE PROMOTION AND PROTECTION OF INVESTMENTS (2010). Article 1(d).

national regulations.⁵⁵ Also, states have a fundamental interest in securing respect for their national laws by foreigners.⁵⁶ An arbitral tribunal explained this requirement by stating that the language found in BITs that requires an investment to conform to the laws and regulations of the host country “seeks to prevent the BIT from protecting investments that should not be protected, particularly because they would be illegal.”⁵⁷

An investment “made in accordance with the host country’s law” does not mean that the *existence* of the investment depends on whether the host country’s municipal law recognizes it as an “investment.” On the contrary, the investment treaty is the instrument that determines what types of economic activities are considered to be “investments.” Compliance with host country laws “refers to the validity of the investment and not to its definition.”⁵⁸ Hence, there becomes an absolute obligation on the investor to make his investment in compliance with the host state laws in order to benefit from the treaty protection.⁵⁹

2. The Requirement of Approval

Another requirement that is found in some BITs is that a foreign investment needs to obtain approval, or admittance, from the host country in order for the investment to be protected.⁶⁰ For example, the Sweden–Malaysia BIT defines investment as “any kind of asset;” however, it adds

⁵⁵ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 367 (Oxford University Press. 2013).

⁵⁶ *Alasdair Ross Anderson et al v Republic of Costa Rica*, para. 58 (ICSID, 2010).

⁵⁷ *Salini Costruttori S.p.A. and Italstrade S.p.A. v Kingdom of Morocco*, Decision on Jurisdiction para. 46 (2001), (ICSID 2001).

⁵⁸ *Salini v. Morocco*, Decision on Jurisdiction, para. 46 (ICSID, 2001).

⁵⁹ SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 187 (Oxford University Press. 2013).

⁶⁰ This approach has been followed, mainly, by Malaysia and Singapore in their investment treaties. *See* for example the Australia–Malaysia FTA (2012) at article 12.2 which defines covered investments as those investments which have been “*admitted by the host Party, subject to its relevant laws, regulations and policies.*”

that such an asset must, when invested in Malaysia, be “a project classified by the appropriate Ministry in Malaysia in accordance with its legislation and administrative practice as an ‘approved project.’”⁶¹

The approval requirement enables the host state to screen incoming investments and approve those that are beneficial to its economy and necessary for its development. It also enables the host country to prevent exploitive and unwanted investments from entering the country, or at least to not encourage their inflow by granting them treaty protection. Countries that impose such a requirement adopt one of two policies: either an “open door” policy where the host state allows all sorts of foreign investments, albeit only those that get approved enjoy certain privileges and treaty protection, or, a “restricted policy” where the host state requires approval for all incoming investments.⁶² Some treaties, however, impose both requirements in their definition; for example, the ASEAN Comprehensive Investment Agreement defines “covered investment,” with respect to a Member State as:

*An investment in its territory of an investor of any other Member State in existence as of the date of entry into force of this Agreement or established, acquired or expanded thereafter, and has been admitted according to its laws, regulations, and national policies, and where applicable, specifically approved in writing by the competent authority of a Member State.*⁶³

It must be noted that an investment made in accordance with the laws and regulations of the host country will not, without more, satisfy the approval requirement.⁶⁴ What is needed under

⁶¹ Agreement Between the Government of Sweden and the Government of Malaysia Concerning the Mutual Protection of Investments (1979). Article 1(i).

⁶² SORNARAJAH, 195 (Cambridge University Press 3 ed. 2012).

⁶³ ASEAN Comprehensive Investment Agreement (2009). Article 4(a).

⁶⁴ SORNARAJAH, 195 (Cambridge University Press 3 ed. 2012). See also YAUNG CHI 00 TRADING PTE LTD v GOVERNMENT OF THE UNION OF MYANMAR (Award), 42 ILM 540, (ASSOCIATION OF SOUTHEAST ASIAN NATIONS para. 58 (ASEAN) ARBITRAL TRIBUNAL, 2003).

the approval requirement is an approval in the form of a governmental document or contract.⁶⁵ Failure to satisfy the approval requirement will render the investment without treaty protection, since it is not an “approved project” within the meaning and requirement of the treaty.

The approval requirement can be used by countries seeking development as a tool to avoid the negative impacts of the foreign investment and harvest its benefits in accordance with its needs. For example, the host state can require the foreign investor to satisfy certain conditions, such as local employment quotas, transferring a minimum amount of capital for the project, or any other condition that it deems appropriate to advance its economy – so long as such a condition is not prohibited by the treaty’s terms.

There are other limitations that can be imposed on the definition of investment. Some treaties impose a “sectoral” limitation, whereby investments in certain sectors qualify for treaty protection.⁶⁶ Other investment treaties impose a “territorial” limitation on covered investments. Such a limitation requires the foreign investment to be made in the territory of the host country for the latter to enjoy treaty protection.⁶⁷ It requires the transfer of assets to the territory of the host country – and not to any other country. Thus, for example, a foreign investor who takes on a project to construct an embassy for the host country in a third country will not benefit from treaty protection.

⁶⁵ Philippe Gruslin v Malaysia para. 25.5 (Final Award), (ICSID, 2000).

⁶⁶ For example the AGREEMENT BETWEEN THE ARAB REPUBLIC OF EGYPT ON THE ONE HAND AND THE BELGO -LUXEMBOURG ECONOMIC UNION ON THE OTHER HAND, ON THE ENCOURAGEMENT AND RECIPROCAL PROTECTION OF INVESTMENTS (1977). This BIT defines ‘investment’ in Article III(1) as “every direct or indirect contribution of capital and any other kind of assets, invested or reinvested in enterprises *in the field of agriculture, industry, mining, forestry, communications and tourism.*” However this BIT was replaced with a new BIT in 1999. The new BIT removed the sectoral requirement imposed in the 1977 BIT.

⁶⁷ See SGS Société Générale de Surveillance S.A. v Republic of the Philippines para. 99 (Decision on Jurisdiction), (ICSID, 2004). “The language is clear in requiring that investments be made ‘in the territory of’ the host State ... In accordance with normal principles of treaty interpretation, investments made outside the territory of the Respondent State, however beneficial to it, would not be covered by the BIT.”

By inserting limitations on the definition of investment in the investment treaty, a host country can tailor the treaty protection to encourage the inflow of beneficial investments. However, this might not be an easy task, as capital-exporting states might not be willing to accept these limitations, which put their outbound investors at a disadvantage.

E. THE DEFINITION OF INVESTMENT UNDER ICSID

The purpose of having an investment within the definition and requirements of a BIT is to enjoy the treatment standards and protections given under that BIT. These substantive protections are of no value if there is no effective and reliable mechanism to enforce them against the host country when violated. Therefore, BITs traditionally contain a dispute resolution section, which uses international arbitration as a means to solve disputes that arise between the foreign investor and the host country. By resorting to international arbitration, the dispute is elevated from the host country's national legal system to the international domain. Thus, foreign investors are assured a fair and impartial review of their disputes through the application of international law.

Most BITs provide for arbitration under the ICSID Convention.⁶⁸ Article 25(1) of the ICSID Convention provides the subject matter jurisdiction of the Center to hear disputes. It reads as follows:

The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or

⁶⁸ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965). Hereinafter referred to as (the "Convention") or (the "ICSID Convention"). Alternatively Some Investment treaties refer to other arbitration venues, such as the International Court of Arbitration of the International Chamber of Commerce (ICC), the Arbitration Institute of the Stockholm Chamber of Commerce (SCC), or to *ad hock* arbitration under the UNCITRAL Arbitration Rules.

*agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.*⁶⁹

From this article, it is clear that access to ICSID arbitration depends entirely on the existence of an “investment.” However, the Convention does not define the term in any of its provisions. The drafters of the ICSID Convention considered adding a definition, but ultimately they decided that a fixed definition may limit the Center’s jurisdiction in the future due to the evolving nature of international investments.⁷⁰ Therefore, “the definition was left to be worked out in the subsequent practice of States, thereby preserving its integrity and flexibility and allowing for future progressive development of international law on the topic of investment.”⁷¹

The non-inclusion of a definition for “investment” in the Convention raised uncertainty among arbitrators on how the term should be interpreted when determining ICSID jurisdiction. Article 25(1) requires a “legal dispute arising directly out of an *investment*;²” therefore, tribunals have diverged on the question of what is an “investment” that satisfies the jurisdictional requirement of the Convention?

A survey of the ICSID case law in this respect shows two main lines of interpretation. The first, sometimes referred to as the deferential approach,⁷² uses the host state’s *ex-ante* consent to refer future disputes to ICSID arbitration as an indicator that the economic activity in question is an “investment” for purposes of ICSID jurisdiction.⁷³ The second line of

⁶⁹ Id. at art. (25)(1) [emphasis added].

⁷⁰ REPORT OF THE EXECUTIVE DIRECTORS ON THE CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES, para. 27 (1965).

⁷¹ *Mihaly International Corporation v Socialist Democratic Republic of Sri Lanka*, para. 33 (ICSID, 2002).

⁷² Julian Davis Mortenson, *The Meaning Of “Investment”: ICSID’s Travaux and the Domain of International Investment Law*, HARVARD INTERNATIONAL LAW JOURNAL 269 (2010).

⁷³ It should be noted that ICSID arbitration is available whenever both parties, the foreign investor and the host state, have consented to submit their dispute to the Center. This consent can raise in three ways; i) it can be a dispute

interpretation, sometimes referred to as the restrictive approach, uses a set of criteria to determine if an investment exists within the meaning required in Article 25(1) of the ICSID Convention.⁷⁴ These criteria, or “features” as described by Schreuer, are typical to most investment operations,⁷⁵ and thus render particular economic activities “investments” within the meaning required under the Convention. However, tribunals following this approach have not reached a consensus on the exact criteria that should be used to determine if an economic activity is an investment within the meaning of the Convention.⁷⁶

1. The Deferential Approach in Defining Investment for ICSID Jurisdiction

Under the deferential approach, consent of the parties to arbitrate their disputes at ICSID is the cornerstone of ICSID jurisdiction.⁷⁷ If the economic activity or asset fits the definition of an

settlement clause in an investment contract, designating ICSID as the forum for dispute resolution for claims arising out of that contract, ii) it can be in the form of a post dispute agreement to submit the claim to ICSID for settlement, or iii) it can be in the form of a standing offer by the host state to submit disputes with a class of investors to ICSID. The standing offer to submit disputes to ICSID is usually found in the host state’s BITs or national investment laws. The foreign investor accepts this standing offer by submitting his claim to ICSID when a dispute arises, or presents before the ICSID tribunal if he is the respondent.

⁷⁴ See Mortenson, HARVARD INTERNATIONAL LAW JOURNAL 271 (2010).

⁷⁵ CHRISTOPH SCHREUER, THE ICSID CONVENTION: A COMMENTARY 122 (2001).

⁷⁶ In *Saba Fakes v. Turkey* the tribunal noted that “no unanimous approach has emerged so far from the existing case law” regarding the definition of “investment.” The tribunal added that the “proposed solutions are inconsistent, if not conflicting, and do not provide any clear guidance to future arbitral tribunals.” *Mr. Saba Fakes v. Republic Of Turkey*, para. 97 (Final Award), (ICSID, 2010).

⁷⁷ See REPORT OF THE EXECUTIVE DIRECTORS ON THE CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES para. 23 (World Bank 1965). Also *LANCO INTERNATIONAL INC. v THE ARGENTINE REPUBLIC*, *Decision on Jurisdiction*, para. 41 (1998). “*This rule [Article 25(1) of the Convention] enumerates several requirements to determine ICSID’s jurisdiction, among which the fundamental and central consideration is the consent given by the parties to the dispute to submit their dispute to ICSID.*” Also in *Tokios Tokeles v Ukraine*, para. 19 (*Decision on Jurisdiction*), (ICSID, 2004). where the tribunal said “*The jurisdiction of the Centre depends first and foremost on the consent of the Contracting Parties, who enjoy broad discretion to choose the disputes that they will submit to ICSID. Tribunals shall exercise jurisdiction over all disputes that fall within the scope of the Contracting Parties’ consent as long as the dispute satisfies the objective requirements set forth in Article 25 of the Convention.*”

“investment” in the underlying consent document,⁷⁸ then ICSID jurisdiction is established. In other words, so long as the economic activity or asset falls within the definition of “investment” in the document that gives consent to ICSID arbitration (the BIT, contract, or national law),⁷⁹ then the jurisdictional requirement of having an “investment” under Article 25(1) of the Convention is fulfilled. According to this approach, any economic activity may be included or excluded from ICSID jurisdiction based on the parties’ agreement in the consent documents.

In *AG Frankfurt Airport Services v. Philippines*, the tribunal stated that its jurisdiction was determined by “the arbitration agreement, in the instant case, both the BIT and the Washington Convention.” The tribunal explained that:

*Article 25 of the Washington Convention, which provides, inter alia, parameters of jurisdiction ratione materiae, does not define ‘investment’, leaving it to parties who incorporate ICSID jurisdiction to provide a definition if they wish. In bilateral investment treaties which incorporate an ICSID arbitration option, the word ‘investment’ is a term of art, whose content in each instance is to be determined by the language of the pertinent BIT which serves as a lex specialis with respect to Article 25 of the Washington Convention.*⁸⁰

Tribunals following the Deferential Approach suggest that the Convention imposes no further jurisdictional limits.⁸¹ The tribunal in *SGS v. Pakistan* opined that the Convention does

⁷⁸ The term ‘Consent Documents’ means any legal instrument which expresses the consent of the parties (foreign investor and the host country) to refer current or future disputes between them to ICSID arbitration. Thus the consent documents to arbitration can be the BIT, or the investment contract.

⁷⁹ In ICSID arbitration, there must be an agreement to arbitrate -in writing- between the host State and the foreign investor. Article 25 of the ICSID Convention provides “The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, *which the parties to the dispute consent in writing to submit to the Centre.*” Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965). Consent is usually given as a standing offer in the BIT, or national law of the host state. In other instances that consent is given in the investment contract signed between the host state and the foreign investor. For more information see UNCTAD, Dispute Settlement: Consent to Arbitration 5-6 (UNCTAD ed., United Nations UNCTAD/EDM/Misc.232/Add.2 ed. 2003).

⁸⁰ *FRAPORT AG FRANKFURT AIRPORT SERVICES WORLDWIDE V. REPUBLIC OF THE PHILIPPINES*, para. 305 (Award), (ICSID, 2007).

⁸¹ “It has been suggested by some writers that where the parties have agreed that a dispute involves an investment, the ICSID tribunal is not required to check if the alleged investment is also an investment under the ICSID

not limit the definition of the investment, and that the parties are free to define the term in accordance with their needs and objectives.⁸²

Consent of the parties to refer disputes to ICSID can be as broad or narrow as the parties wish.⁸³ However, arbitral tribunals have indicated on several occasions that the parties' consent cannot be extended to activities that are clearly outside the scope of the Convention.⁸⁴ Thus, "tribunals should give effect to [the parties' consent], unless doing so would allow the Convention to be used for purposes for which it clearly was not intended."⁸⁵ Although tribunals have not elaborated on what activities would be ruled out of the Convention, it is agreed that a single commercial transaction (such as the import of one load of goods) will be outside the scope of the Convention regardless of how broad the parties' consent is.⁸⁶

Arbitrators following the deferential approach focus on the host country's *ex ante* policy of referring future disputes with foreign investors to ICSID arbitration. Therefore, the host

Convention," Kathigamar V.S.K. Nathan, *Submissions to the International Center for Settlement of Investment Disputes in Breach of the Convention*, 12 JOURNAL OF INTERNATIONAL ARBITRATION 30 (1995). See also Mortenson, HARVARD INTERNATIONAL LAW JOURNAL 269 (2010).

⁸² SGS Société Générale de Surveillance S.A. v Islamic Republic of Pakistan, Decision of the Tribunal on Objections to Jurisdiction, para. 133 (ICSID, 2003). "*The ICSID Convention does not delimit the term "investment," leaving to the Contracting Parties a large measure of freedom to define that term as their specific objectives and circumstances may lead them to do so.*"

⁸³ See Ceskoslovenska Obchodní Banka (CSOB) v. Slovak Republic, Decision on Objections to Jurisdiction, para. 68 (ICSID, 1999). Also see Tokios Tokeles v Ukraine, para. 39 (Decision on Jurisdiction), (ICSID, 2004), where the tribunal states "*We emphasize here that Contracting Parties are free to define their consent to jurisdiction in terms that are broad or narrow; they may employ a control-test or reserve the right to deny treaty protection to claimants who otherwise would have recourse under the BIT.*"

⁸⁴ See ENRON CORPORATION AND PONDEROSA ASSETS, L.P. v THE ARGENTINE REPUBLIC, Decision on Jurisdiction para. 42 (ICSID, 2004). "*... there is, however, a limit to this discretion of the parties because they could not validly define as investment in connection with the Convention something absurd or entirely incompatible with its object and purpose.*" See also Ceskoslovenska Obchodní Banka (CSOB) v. Slovak Republic, Decision on Objections to Jurisdiction, para. 68 (ICSID, 1999), where the tribunal states "*The concept of an investment as spelled out in that provision [Article 25(1) of the Convention] is objective in nature in that the parties may agree on a more precise or restrictive definition of their acceptance of the Centre's jurisdiction, but they may not choose to submit disputes to the Centre that are not related to an investment.*"

⁸⁵ Supra Tokios Tokeles v Ukraine, para. 39 (Decision on Jurisdiction), (ICSID, 2004).

⁸⁶ See SGS Société Générale de Surveillance S.A. v Islamic Republic of Pakistan, Decision of the Tribunal on Objections to Jurisdiction n.153 (ICSID, 2003).

country's objection to ICSID jurisdiction after the dispute arises is irrelevant.⁸⁷ The *ex-ante* policy of the host state creates a "legitimate expectation" to the foreign investor that his disputes with the host country will be adjudicated at ICSID. This legitimate expectation is protected under international investment law.⁸⁸ Hence, the only way for a host country to escape ICSID jurisdiction after a dispute arises is to prove that the economic activity or asset is not an "investment" within the meaning found in the consent document (*i.e.*, the BIT, contract, or national law).⁸⁹

2. The Restrictive Approach in Defining Investment for ICSID Jurisdiction

The restrictive approach gives supremacy to the Convention, not to the parties' consent.⁹⁰ In other words, tribunals following this approach apply a two-level jurisdictional analysis, otherwise referred to as the "double key-hole"⁹¹ or "double barrel" test.⁹² The first test requires the tribunal to investigate whether the economic activity in question is an "investment" within the definition given in the relevant investment treaty. Once that is satisfied, the tribunal moves to the second jurisdictional test, which is to determine whether the economic activity in question is

⁸⁷ See LORETTA MALINTOPPI CHRISTOPH SCHREUER, AUGUST REINISCH, ANTHONY SINCLAIR, *THE ICSID CONVENTION: A COMMENTARY* para. 130 (Cambridge University Press 2 ed. 2009).

⁸⁸ Legitimate expectations of foreign investors are protected under the fair and equitable treatment standard. See for example *Azurix Corp. v The Argentine Republic* para. 372 (Final Award), (ICSID, 2006).

⁸⁹ See Mortenson, *HARVARD INTERNATIONAL LAW JOURNAL* 269-71 (2010).

⁹⁰ "*the Washington Convention has supremacy over an agreement between the parties or a BIT.*" *THE CASE OF PATRICK MITCHELL V. DEMOCRATIC REPUBLIC OF CONGO* para. 31 (Decision on the Application for Annulment of the Award), (ICSID, 2006).

⁹¹ *Aguas del Tunari v. Bolivia*, para. 278 (Award on Jurisdiction), (ICSID, 2005).

⁹² *Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, para. 55 (Award on Jurisdiction), (ICSID, 2007).

an “investment” within the meaning of Article 25(1) of the Convention.⁹³ Hence, if the economic activity fits the definition of “investment” in the BIT (first test), but fails to pass the second test (an “investment” within the requirements of the Convention), the ICSID tribunal will not have jurisdiction.⁹⁴ The tribunal in the *Malaysian Salvors* case explained the restrictive approach in the following terms:

*Under the double-barrelled test, a finding that the Contract satisfied the definition of “investment” under the BIT would not be sufficient for this Tribunal to assume jurisdiction, if the Contract failed to satisfy the objective criterion of an “investment” within the meaning of Article 25.*⁹⁵

This is in contrast to the deferential approach, where only one jurisdictional determination is made based on the parties’ consent documents referring to ICSID arbitration. The restrictive approach is also in contrast with investment arbitrations outside of ICSID, where one level of jurisdictional determination is required (*i.e.*, under the investment treaty or contract), as the Convention itself is not applicable.⁹⁶ Therefore, ICSID arbitrators who follow this approach try to define the undefined term “investment” in the Convention to determine their jurisdiction. This has resulted in an array of different and inconsistent interpretations of the term. This uncertainty and confusion may indeed endanger the “whole ICSID system or at least jeopardize its development.”⁹⁷

⁹³ The tribunal in *ToTo Construzioni v Lebanon* made this clear by stating “*it is not sufficient that the dispute arises out of an investment as per the meaning of “investment” given by the parties in the Treaty, but also as per the meaning of “investment” under the ICSID Convention.*” *Toto Construzioni Generali S.P.A. v. Republic Of Lebanon* para. 66 (Decision on Jurisdiction), (ICSID, 2009). See also *International Investment Law: Understanding Concepts and Tracking Innovations* 59 (OECD 2008).

⁹⁴ *THE CASE OF PATRICK MITCHELL V. DEMOCRATIC REPUBLIC OF CONGO* para. 31 (Decision on the Application for Annulment of the Award), (ICSID, 2006).

⁹⁵ *Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, para. 55 (Award on Jurisdiction), (ICSID, 2007).

⁹⁶ DON WALLACE JR. CHRISTOPHER DUGAN, NOAH RUBINS, BORZU SABAHI, *INVESTOR-STATE ARBITRATION* 280 (Oxford University Press. 2008).

⁹⁷ Pierre - Emmanuel Dupont, *The Notion of ICSID Investment: Ongoing ‘Confusion’ or ‘Emerging Synthesis’?*, 12 *THE JOURNAL OF WORLD INVESTMENT & TRADE* 246 (2011).

The restrictive approach emerged after the prominent scholar and arbitrator, Christoph Schreuer, introduced a set of “features,” or “typical characteristics,” of an investment.⁹⁸ Schreuer suggested that these features can be used as a guide for arbitrators to determine whether an economic activity is an “investment” within the requirement of Article 25(1) of the Convention.⁹⁹ Schreuer’s five features of an investment are: i) a certain *duration*, ii) *regularity of profit and return*, iii) the assumption of *risk*, iv) a *substantial* commitment, and v) the operation’s significance for the *host state’s development*.¹⁰⁰ These features were not meant to be fixed or rigid requirements that would need to be satisfied in every activity to establish ICSID jurisdiction. On the contrary, Schreuer made clear that “these features should not necessarily be understood as jurisdictional requirements but merely as typical characteristics of investments under the Convention.”¹⁰¹

Many arbitral tribunals have used these features, subject to variation, as a rigid test to determine if an activity qualifies for ICSID jurisdiction.¹⁰² These “typical characteristics” of an

⁹⁸ Christoph Schreuer, Commentary on the ICSID Convention, ICSID Review - Foreign Investment Law Journal, Vol. 11, 1996, at pages 355-358. However after the *Salini v Morocco* case the features became known as the ‘Salini Test.’

⁹⁹ CHRISTOPH SCHREUER, 153 (Cambridge University Press 2 ed. 2009).

¹⁰⁰ *Id.* at para. 153.

¹⁰¹ *Id.* at para. 153.

¹⁰² For example *see*; *Fedax v. Venezuela*, Decision on Jurisdiction, (ICSID, 1997). The tribunal, in its decision, cited an early article of Schreuer published in 1997 (Christoph Schreuer: "Commentary on the ICSID Convention," ICSID Review - Foreign Investment Law Journal, Vol. 11, 1996, at pages 355-358.). The *Fedax* tribunal stated that “*The basic features of an investment have been described as involving a certain duration, a certain regularity of profit and return, assumption of risk, a substantial commitment and a significance for the host State's development.*” at para 43 of the decision. *See also Salini v. Morocco*, Decision on Jurisdiction, (ICSID, 2001). The tribunal used some of the features introduced by Schreuer, it said at para 52 “*The doctrine generally considers that investment infers: contributions, a certain duration of performance of the contract and a participation in the risks of the transaction ... In reading the Convention's preamble, one may add the contribution to the economic development of the host State of the investment as an additional condition.*” Also in *Joy Mining Machinery Limited v The Arab Republic of Egypt*, Award, para. 53 (ICSID, 2004), “*...the project in question should have a certain duration, a regularity of profit and return, an element of risk, a substantial commitment and that it should constitute a significant contribution to the host State's development.*” *See also Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, paras. 107-48 (Award on Jurisdiction), (ICSID, 2007). *See also Joy Mining Machinery*

investment have been transformed into a prescriptive list of requirements for ICSID jurisdiction.¹⁰³ This can be attributed to the repeated application of these criteria by arbitral tribunals, which has resulted in a perception that they were not merely “features indicative of investments,” but rather are mandatory rules.¹⁰⁴

The line of interpretation followed by the supporters of the restrictive approach in determining ICSID Jurisdiction goes against principles on which the Convention was founded. Basically, the drafters of the Convention believed that “adherence to the Convention by a country would provide an additional inducement for, and stimulate a larger flow of, private international investment into its territory, which is the primary purpose of the Convention.”¹⁰⁵ The Preamble to the ICSID Convention speaks of “the need for international cooperation for economic development, and the role of private international investment therein.” The deliberate omission of a definition of ‘investment’ in the Convention was to give Contracting States the discretion to determine what economic activity would be considered to be an “investment” according to their developmental needs.¹⁰⁶ Arbitrators following the restrictive approach impose a higher threshold on the definition of “investment” to find jurisdiction. This goes against the Convention’s main purpose, as it imposes a higher burden on foreign investors to establish ICSID jurisdiction by requiring their economic activity to satisfy a list of requirements that must be fulfilled in order to render their economic activity in question an “investment” within the

Limited v The Arab Republic of Egypt, Award, para. 53 (ICSID, 2004), “*the elements that an activity must have in order to qualify as an investment,*” and then proceeds to list the criteria.

¹⁰³ See CHRISTOPHER DUGAN, 265 (Oxford University Press, 2008); Mortenson, HARVARD INTERNATIONAL LAW JOURNAL 272 (2010).

¹⁰⁴ CHRISTOPH SCHREUER, 159 (Cambridge University Press 2 ed. 2009).

¹⁰⁵ REPORT OF THE EXECUTIVE DIRECTORS ON THE CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES para. 11 (World Bank 1965).

¹⁰⁶ Id. at para. 27. See also G. R. Delaume, *Convention on the Settlement of Investment Disputes Between States and Nationals of Other States*, 1 THE INTERNATIONAL LAWYER 64, 70 (1966).

meaning of the Convention. Hence it is perceivable that “foreign agents who doubt the qualification attributed to their transaction [will] turn away from ICSID arbitration (in spite of the advantages it presents) for the benefit of other available modes of dispute resolution, in order to discard the uncertainty concerning ICSID *ratione materiae* jurisdiction.”¹⁰⁷ This impacts the Convention’s purpose as an instrument of international policy for the promotion of economic development.¹⁰⁸ The ICSID Convention should not be seen merely as a means of dispute settlement, but rather as a tool to promote development through FDI.

Nonetheless, the typical features used by arbitrators under the restrictive approach are good indicators for drawing the line between regular commercial transactions and investments. Although they should be used as guidance and not as a mandatory list of requirements to establish ICSID jurisdiction, they are useful tools for determining whether a particular transaction falls in the grey area of ordinary commercial transactions that should be denied ICSID jurisdiction, or is an investment that falls within the reach of ICSID jurisdiction.

3. The Features of ‘Investment’ Under the Restrictive Approach

a. *Duration:* Investments, by their nature, are economic activities of extended duration. Host states attract foreign investments with the intention that the investments will be beneficial to the states’ development. The injection of capital and other resources into the host state’s economy for prolonged periods of time enables the host state to rely on such resources for development. This is contrary to short-term activities that are unpredictable and likely to withdraw from the

¹⁰⁷ Sébastien Manciaux, *The Notion of Investment: New Controversies*, 9 JOURNAL OF WORLD INVESTMENT & TRADE 448 (2008).

¹⁰⁸ CHRISTOPH SCHREUER, 4 (Cambridge University Press 2 ed. 2009).

host economy when conditions deteriorate, consequently “worsening financial volatility in the country rather than mitigating it.”¹⁰⁹ Therefore, the duration of an activity is key when differentiating between investments falling within the requirement of the Convention and other commercial activities that fall outside its scope.¹¹⁰ For example, a three-month servicing and maintenance contract for military airplanes, although the contract may be worth tens of millions of dollars, will not qualify as an “investment,” regardless of its major contribution to the economy. In this example, the duration of the transaction is too short to be considered an investment.

However, the issue that arises is not related to the necessity of a long duration for an activity to be considered an ‘investment’ within the meaning of Article 25(1) of the Convention. Rather, the issue is how long, or the minimum length of time, required for an activity to satisfy the ‘duration’ criterion.

In *Salini v. Morocco* the tribunal opined that “the minimal length of time upheld by the doctrine, ... is from 2 to 5 years.”¹¹¹ The tribunal in *Bayindir v. Pakistan* found that a three-year construction project, followed by a one-year defect liability period, satisfies the duration criterion, by stating, “contracts over similar periods of time have been considered to satisfy the duration test for an investment.”¹¹² The latter tribunal also ruled that guarantee periods should be taken into account when calculating the duration of an activity, as risks may arise during those

¹⁰⁹ CHRISTOPHER DUGAN, 266 (Oxford University Press. 2008).

¹¹⁰ See *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Islamic Republic of Pakistan* (Decision on Jurisdiction) (ICSID, 2005). The tribunal stated at para 132 “*The element of duration is the paramount factor which distinguishes investments within the scope of the ICSID Convention and ordinary commercial transactions.*”

¹¹¹ *Salini Costruttori S.p.A. and Italstrade S.p.A. v Kingdom of Morocco*, Decision on Jurisdiction para. 54 (2001), (ICSID 2001).

¹¹² *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Islamic Republic of Pakistan* para. 133 (Decision on Jurisdiction) (ICSID, 2005). (ICSID, 2005). It is worthy to note that the tribunal in this case opined that “guarantee periods” should be taken into account when calculating the duration feature of an economic activity. See para 133 in this regard.

periods.¹¹³ However, in *Consortium R.F.C.C. v. Morocco* a construction contract of 20 months did not meet this criterion.¹¹⁴ It is the fact that the parties had agreed to extend the contract for another six months that enabled the contract to satisfy “the minimal duration observed by the doctrine which are 2 to 5 years.”¹¹⁵ Hence, tribunals have reached a consensus on the minimum length of time required to satisfy the duration criterion: two years.

In *Saipem v. Bangladesh*, the construction of an oil pipeline contract of fourteen months was claimed by the defendant to not meet the two year minimum requirement.¹¹⁶ The tribunal held that duration should be calculated based on the “entire or overall operation,” thus “the entire or overall operation includes the Contract, the construction itself, the Retention Money, the warranty and the related ICC Arbitration.”¹¹⁷ The tribunal in this case reasoned that the duration criterion should be calculated based on the total duration of when risks to the foreign investor exist.¹¹⁸ The tribunal in *Joy Mining v. Egypt* also tied duration with risk.¹¹⁹ A contract for the sale of mining equipment was rejected as an “investment,” because payment had happened at an early stage in the contract.¹²⁰ Hence, the “duration of the commitment is not particularly significant,” as most risks of the sale had ended when payment was made.¹²¹

The *Saipem* and *Joy Mining* cases make clear that the minimum length of time required to satisfy the duration criterion is two years. Calculation of duration includes not only the duration of the project or contract, but also extends to periods where risk may exist. Thus, a one-

¹¹³ Id. at para. 136.

¹¹⁴ Consortium RFCC v Kingdom of Morocco, (ICSID, 2001).

¹¹⁵ Id. at 62.

¹¹⁶ SAIPEM S.p.A. v THE PEOPLE’S REPUBLIC OF BANGLADESH, Decision on Jurisdiction (ICSID, 2007).

¹¹⁷ Id. at para. 110.

¹¹⁸ Id. at para. 102.

¹¹⁹ Joy Mining Machinery Limited v The Arab Republic of Egypt , Award on Jurisdiction (ICSID, 2004).

¹²⁰ Id. at para. 57.

¹²¹ Id. at para. 57.

year project will not satisfy the duration criterion; however, a one-year project with a one-year defect liability period will satisfy the duration criterion.

A two-year minimum duration is reasonable and effectively filters out commercial activities from the jurisdiction of ICSID. However, the minimum duration requirement should not be strictly applied as in the cases above. Arbitrators following this approach should shorten the minimum length if all other characteristics of an “investment” exist, or if the nature and circumstances of the project at hand do not require a lengthy time to conclude. Also, arbitrators should respect the host country’s consent if that country had accepted to treat the economic activity as an “investment,” regardless of its short duration.

b. *Regularity of Profit and Return:* The driving force behind investors seeking opportunities overseas is to gain profit. Even if no profits eventually materialize, the expectation of profits is a typical element of any investment. In commercial transactions the profit, if any, materializes immediately after the merchant receives the payment for his goods or services. In investments, however, the return may not be profit, as the investor needs to first recover the costs of the investment, usually over several years. Thus, it is the ‘regularity’ of return that differentiates investments from other commercial transactions.

It can be said that the profit or regular return feature aims at keeping ‘not-for-profit’ organizations and companies outside the reach of ICSID.¹²² The issue of including not-for-profit

¹²² See CHRISTOPHER DUGAN, 305 (Oxford University Press, 2008). Some investment treaties explicitly include not-for-profit organizations in their definition of ‘investment.’ For example the Germany – Afghanistan BIT defines investor as “*any juridical person as well as any commercial or other company or, association with or without legal personality having its seat in the territory of the Federal Republic of Germany, irrespective of whether or not its activities are directed at profit.*” Treaty between the Federal Republic of Germany and the Islamic Republic of Afghanistan concerning the Encouragement and Reciprocal Protection of Investments (2005). At Article 1(3)(a). See

organizations in ICSID jurisdiction is controversial.¹²³ However, the satisfaction of this feature requires the demonstration of a ‘regular and steady’ return, or the expectation thereof, rather than proof of profitability.

In *Joy Mining v. Egypt*, a sales contract was considered not to meet the meaning of investment under the Convention, because “the duration of the commitment is not particularly significant, as evidenced by the fact that the price was paid in its totality at an early stage. *Neither is therefore the regularity of profit and return.*”¹²⁴ The tribunal considered the full payment of the contract price not to be a “regular” return. Other tribunals have described this feature as “immaterial” to the question of investment, and that its presence or absence is not determinative on this question.¹²⁵ Hence, the expectation of a regular return or profit will suffice for this purpose, if there is no actual return.

c. Assumption of Risk: Investments, as long-term projects with the expectation of profits, entail some form of risk assumed by both parties (*i.e.*, the host country and the foreign investor).¹²⁶ This risk is different from that associated with commercial transactions. The type of risk required for an activity to be considered an “investment” must be “*other than normal commercial risks.*”¹²⁷ It should not be an inherent risk in the contract, but rather “*a special feature of the*

also Agreement between Montenegro and The Kingdom Of Denmark Concerning the Promotion and Reciprocal Protection of Investments (2009). Article 1(4)(b).

¹²³ SCHREUER, 44 (Oxford University Press 2 ed. 2012).

¹²⁴ *Joy Mining Machinery Limited v The Arab Republic of Egypt*, Award on Jurisdiction para. 57 (ICSID, 2004).

¹²⁵ *See Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, 108 (Award on Jurisdiction), (ICSID, 2007).

¹²⁶ Schreuer considered the risk feature to be “a function of duration and expectation of profit.” *See* CHRISTOPH SCHREUER, 153 (Cambridge University Press 2 ed. 2009).

¹²⁷ *Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, para. 112 (Award on Jurisdiction), (ICSID, 2007).

Contract” that affects the investor’s decision to undertake the project.¹²⁸ Therefore, activities that entail regular commercial risks, such as the risk non-performance by one of the parties or the termination of contract, fall outside the scope of “investments” as required under the Convention.¹²⁹

One tribunal tried to define “risk” in this sense by stating that it is a situation where the investor “cannot be sure of a return on his investment, and may not know the amount he will end up spending, even if all relevant counterparties discharge their contractual obligations. Where there is ‘risk’ of this sort, the investor simply cannot predict the outcome of the transaction.”¹³⁰ Another tribunal identified this criterion as “an economic risk entailed, in the sense of an uncertainty regarding its successful outcome.”¹³¹

The tribunal in *Malaysian Historical Salvors v. Malaysia* considered the risk inherent in a salvage contract, which was on a ‘no-find-no-pay’ basis. The tribunal found that most salvage contracts are concluded on a ‘no-find-no-pay’ basis, hence:

*The risks assumed under the Contract were no more than ordinary commercial risks assumed by many salvors in a salvage contract. The Claimant has not provided any convincing reasons why the risks assumed under the Contract were anything other than normal commercial risks.*¹³²

The tribunal confirmed that ordinary commercial risks are not investments within the meaning of the Convention. It noted that the risk criterion should be satisfied in a qualitative, not

¹²⁸ Id. at para. 112.

¹²⁹ CHRISTOPHER DUGAN, 270 (Oxford University Press. 2008).

¹³⁰ ROMAK S.A. v THE REPUBLIC OF UZBEKISTAN, Award, para. 230 (PERMANENT COURT OF ARBITRATION, 2009).

¹³¹ THE CASE OF PATRICK MITCHELL V. DEMOCRATIC REPUBLIC OF CONGO para. 27 (Decision on the Application for Annulment of the Award), (ICSID, 2006).

¹³² *Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, para. 112 (Award on Jurisdiction), (ICSID, 2007). See also *Joy Mining Machinery Limited v The Arab Republic of Egypt*, Award on Jurisdiction (ICSID, 2004)., were the tribunal found that the commercial risks include the risk of termination of contract. It stated at para 57 that the risks associated with the contract in question to be “not different from that involved in any commercial contract, including the possibility of the termination of the Contract.”

quantitative, sense; therefore, even if the Claimant had satisfied the risk criterion “in a quantitative sense (*i.e.*, that there was inherent risk assumed under the Contract), the quality of the assumed risk was not something which established ICSID practice and jurisprudence would recognize.”¹³³

The tribunal in *Fedex v. Venezuela* found that “the very existence of a dispute . . . evidences the risk.”¹³⁴ Although this case was decided a decade before *Malaysian Salvors*, it is somewhat peculiar in its consideration of the existence of a dispute as an investment risk. Any transaction is under the risk of dispute for non-performance. Thus, this would easily fall under common commercial risks. Other tribunals have considered political and economic climates of a country to constitute an investment risk. In *Ioannis Kardassopoulos v. Georgia* the tribunal found that the political and economic climates in Georgia following its independence in 1991 constituted an investment risk.¹³⁵

d. *Substantial Commitment of Resources:* The term in “investment” in its most basic and simple definitions require the commitment of capital, or other resources, for a certain period of time to gain revenue. Thus, a substantial commitment of resources is key to differentiate between investments that fall within the scope of the Convention and other commercial transactions. However, a substantial commitment does not mean the financial value of the investment.

¹³³ *Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, para. 112 (Award on Jurisdiction), (ICSID, 2007).

¹³⁴ *FEDAXN.V. v THE REPUBLIC OF VENEZUELA* , Decision of the Tribunal on Objections to Jurisdiction para. 40 (ICSID, 1997).

¹³⁵ *IOANNIS KARDASSOPOULOS v GEORGIA*, Decision on Jurisdiction para. 117 (ICSID, 2007), “*the risk component is satisfied in light of the political and economic climate prevailing throughout the period of the investment.*”

The drafters of the ICSID Convention considered and rejected a minimum amount in dispute as a requirement for ICSID jurisdiction.¹³⁶ Therefore, monetary contribution in a project, while it constitutes a factor, should not be the only determinant of whether there is an ‘investment’ within the meaning of the Convention. In fact, it would be arbitrary to have monetary contribution as the main and only determinate, as monetary contributions have different values depending on the investor and the host country. To illustrate this point, an investment of USD 250,000 for a startup company might be substantial, however, it is a trivial amount for companies like Chevron or Microsoft. This also applies to where the investment is made. An investment project of USD 250,000 might be substantial in an underdeveloped country. However, such an amount is seen insignificant in well-developed and wealthy countries like the USA or UK.

Tribunals should consider several factors when deciding if there is a substantial commitment of resources. These factors should include the resources the foreign investor has committed and imported to the host country, such as know-how, employment opportunities, technology, and capital. The tribunal in *Bayinder v. Pakistan* acknowledged this by stating “to qualify as an investment, the project in question must constitute a substantial commitment on the side of the investor. In the case at hand, it cannot be seriously contested that Bayindir made a

¹³⁶ See *The History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States* 204 (2009 reprint). “*Consideration was given to fixing a lower limit for the value of the subject-matter of a dispute. It was, however, recognized that the parties would in practice be best qualified to decide whether, having regard to pertinent facts and circumstances including the value of the subject-matter, a dispute is one which ought to be submitted to the Center. The subject-matter of a dispute might be of insignificant pecuniary value, but might involve important questions of principle, thus justifying the bringing of a test case. In other instances the pecuniary value might not be readily ascertainable, as where a host government fails to implement a provision in an investment agreement conferring immunity from immigration restrictions on foreign personnel, or might not be ascertainable at all, as where an investor fails to implement an agreement with a host government to train local personnel.*”

significant contribution, *both in terms of know-how, equipment and personnel and in financial terms.*”¹³⁷

In *Malaysian Salvors v. Malaysia*, the tribunal held that the substantiality of an investment should not be determined solely on its economic contribution, even if it is the largest financial contribution in its respective industry. Rather, “to determine whether the Contract is an investment the litmus test must be its overall contribution to the economy of the host State.”¹³⁸ The *Malaysian Salvors* tribunal thus followed the line of reasoning adopted in *Bayinder v. Pakistan*; however, it clarified that assessment should be based on the “overall contribution to the economy.”¹³⁹

e. *Contribution to the Economic Development of the Host State:* While the other features relate to the economic activity itself (duration, risk, expectation of profits, and commitment of resources), this feature looks at the host state’s motivation to accept and protect the economic activity at question.¹⁴⁰ It is well known that countries attract foreign investments to benefit from the resources and expertise that foreign investors bring to their economies. In return of these benefits, and to encourage their inflow, the host country offers foreign investors protections and incentives under the investment treaty.¹⁴¹

¹³⁷ *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Islamic Republic of Pakistan* para. 131 (Decision on Jurisdiction) (ICSID, 2005) [emphasis added].

¹³⁸ *Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, para. 135 (Award on Jurisdiction), (ICSID, 2007).

Malaysian Salvors claimed that their contribution from the contract was the largest within the salvage industry (at least USD 3.8 million), and it is in that particular frame of reference within which its contributions and commitments must be measured. The tribunal rejected this method of measurement.

¹³⁹ *Id.* at 135.

¹⁴⁰ See CHRISTOPHER DUGAN, 272 (Oxford University Press, 2008).

¹⁴¹ See in general Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67 (2005).

This feature is the most controversial of all other features of an investment under the restrictive approach.¹⁴² The controversy arises from “the subjective character of this element and the resulting difficulty to ascertain its presence in a given investment.”¹⁴³

The ICSID Convention was founded on the vision that protection of foreign investments encourages capital flows around the globe, consequently boosting the economic development of countries. This view is explicitly expressed in the preamble of the Convention, which reads “*Considering the need for international cooperation for economic development, and the role of private international investment therein.*”¹⁴⁴ Therefore, some tribunals have adopted the view that this feature is essential when considering whether an economic activity qualifies as an investment within the meaning of the Convention. The tribunal in *Malaysian Salvors v. Malaysia* noted this feature to be “of considerable, even decisive importance.”¹⁴⁵

In *Patrick Mitchell v. Congo*, Mr. Mitchell, an American lawyer, established a law firm in Congo. In 1999, pursuant to a Military Court order, security forces raided the premises of the law firm, sealed it, and seized some of its documents and items. Some lawyers working in the firm were detained during the raid.¹⁴⁶ Mr. Mitchell filed an expropriation claim against the Government of Congo at ICSID. The first award was in favor of Mr. Mitchell.¹⁴⁷ However, this award was rejected by the Annulment Committee on the grounds of lacking merit, manifest

¹⁴² See *PHILIP MORRIS BRANDS SÀRL, PHILIP MORRIS PRODUCTS S.A. and ABAL HERMANOS S.A. v ORIENTAL REPUBLIC OF URUGUAY*, Decision on Jurisdiction, 207 (ICSID, 2013).

¹⁴³ *Id.* at para. 207.

¹⁴⁴ Preamble of the CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES (1965).

¹⁴⁵ *Malaysian Historical Salvors SDN, BHD v The Government of Malaysia*, para. 123 (Award on Jurisdiction), (ICSID, 2007).

¹⁴⁶ *THE CASE OF PATRICK MITCHELL V. DEMOCRATIC REPUBLIC OF CONGO* para. 1 (Decision on the Application for Annulment of the Award), (ICSID, 2006).

¹⁴⁷ *PATRICK H. MITCHELL v THE DEMOCRATIC REPUBLIC OF THE CONGO*, Award, (ICSID, 2004). In this Award Mr. Mitchell was awarded USD 750,000, plus arbitration costs and interest.

excess of powers, and failure of the tribunal to state reasons when they found that the legal practice was an investment under Article 25(1) of the ICSID Convention.¹⁴⁸ The Annulment Committee, in its effort to determine whether a law firm constitutes an “investment” within the meaning of the Convention, elaborated on the “contribution to the development of the host state” feature, and summarized the previous case law in this respect:

28. The Preamble of the Washington Convention sets forth a number of basic principles as to its purpose and aims, which imbue the individual provisions of the Convention, including Article 25...

29. It is thus quite natural that the parameter of contributing to the economic development of the host State has always been taken into account, explicitly or implicitly, by ICSID arbitral tribunals in the context of their reasoning in applying the Convention, and quite independently from any provisions of agreements between parties or the relevant bilateral treaty.

30. Indeed, in the Salini case, the contribution to the economic development of the host State was explicitly set as a ‘criterion’ for an investment which was subsequently taken into account in respect of the construction of a highway, which led to the conclusion that the highway was clearly of public interest. Similarly, in the Fedax case, which involved promissory notes issued by the Republic of Venezuela to guarantee a loan equivalent to their amount, the arbitral tribunal observed that: ‘It is quite apparent that the transactions involved in this case are not ordinary commercial transactions and indeed involve a fundamental public interest [...] There is clearly a significant relationship between the transaction and the development of the host State.’ Finally, in the CSOB case, which involved a ‘consolidation agreement’ between the Czech Republic, Slovakia, and the Czechoslovak bank CSOB, with each of the two new States guaranteeing the reimbursement of the loan granted by CSOB to its national Collection Company, the Arbitral Tribunal observed that: ‘Under certain circumstances a loan may contribute substantially to a State’s economic development [...] [The] undertaking involved a significant contribution by CSOB to the economic development of the Slovak Republic within the meaning of the Convention.’ While it is true that in these cases, where explicit reference was made to the “contribution to the economic development of the host State,” the concept of investment was somewhat ‘broadened,’ this does nothing to alter the fundamental nature of that characteristic. It is thus found that, in another group of cases where the contribution to the economic development of the host State had not been mentioned expressly, it was doubtless covered by the very purpose of the

¹⁴⁸ Id. at para. 40.

contracts in question – all of which were State contracts – which had an obvious and unquestioned impact on the development of the host State.

31. In addition to the foregoing, it bears noting that Professor Schreuer regards the contribution to the economic development of the host State as ‘the only possible indication of an objective meaning’ of the term ‘investment’ ...

32. ... the same Treaty [U.S. – Congo BIT] also recognizes clearly in its Preamble that agreement upon the treatment to be accorded such investment will stimulate the flow of private capital and the economic development of both Parties. Moreover, this is a provision that appears in all bilateral treaties signed by the United States, and was even emphasized in the Preamble to the 2004 Model BIT.

33. The ad hoc Committee wishes nevertheless to specify that, in its view, the existence of a contribution to the economic development of the host State as an essential – although not sufficient – characteristic or unquestionable criterion of the investment, does not mean that this contribution must always be sizable or successful; and, of course, ICSID tribunals do not have to evaluate the real contribution of the operation in question. It suffices for the operation to contribute in one way or another to the economic development of the host State, and this concept of economic development is, in any event, extremely broad but also variable depending on the case.¹⁴⁹

The Annulment Committee found that Mr. Mitchell’s law firm did not contribute to the development of Congo, thus it did not qualify as an ‘investment’ within the meaning of the Convention.¹⁵⁰ The cases cited in the Annulment Committee’s decision, and others, consider the “contribution to the development of the host state” as an important feature of an “investment” as required by the Convention. However, other tribunals have had an opposite view.

In *Phillip Morris v. Uruguay*, the tribunal noted that the preamble of the Convention and the preambles of BITs, referring to economic development, are “too general to permit the drawing of definitive conclusions regarding the need for the investment to contribute to the host

¹⁴⁹ THE CASE OF PATRICK MITCHELL V. DEMOCRATIC REPUBLIC OF CONGO paras. 28-33 (Decision on the Application for Annulment of the Award), (ICSID, 2006).

¹⁵⁰ Id. at para. 49.

State's economic development.”¹⁵¹ This aligns with the position taken in *Electrabel v. Hungary*, where the tribunal opined that the economic development of the host State “is one of the objectives of the ICSID Convention and a desirable consequence of the investment, but it is not necessarily an element of an investment.”¹⁵² The tribunal in *Saba Fakes v. Turkey* held the same position, noting that the preamble of the Convention referring to this goal is a desired consequence, but that it would be “excessive to attribute to this reference a meaning and function that is not obviously apparent from its wording.”¹⁵³ The latter tribunal opined that the economic development of the host state through foreign investment is an expected goal; however, “certain investments expected to be fruitful may turn out to be economic disasters. They do not fall, for that reason alone, outside the ambit of the concept of investment.”¹⁵⁴

The divergent views on this criterion show that there is far from a consensus among ICSID tribunals. From a host country's point of view, economic development is the main reason to attract foreign investors into their territory.¹⁵⁵ Hence it becomes natural that the host country will want to provide treaty protection to those investments that contribute to its development. The assessment of whether the investment project in question has contributed to the development of the host country should not be at the time of dispute. Indeed, as the tribunal in *Saba Fakes* noted, at the time of the dispute the investment project may not be a success story and may have caused harm to the host state's economy. Hence, a better proposition would be to assess the

¹⁵¹ PHILIP MORRIS BRANDS SÀRL, PHILIP MORRIS PRODUCTS S.A. and ABAL HERMANOS S.A. v. ORIENTAL REPUBLIC OF URUGUAY, Decision on Jurisdiction, para. 201 (ICSID, 2013).

¹⁵² ELECTRABEL S.A. v. The Republic of Hungary para. 5.43 (Decision on Jurisdiction, Applicable Law and Liability), (ICSID, 2012).

¹⁵³ Mr. Saba Fakes v. Republic Of Turkey, para. 111 (Final Award), (ICSID, 2010).

¹⁵⁴ Id. at para. 111.

¹⁵⁵ TRENDS AND IMPACTS OF FOREIGN INVESTMENT IN DEVELOPING COUNTRY AGRICULTURE: EVIDENCE FROM CASE STUDIES (David Hallam Pedro Arias, Suffyan Koroma, Pascal Liu ed., Food and Agriculture Organization of the United Nations 9 (FAO). 2013).

contribution at the time when the foreign investment entered the host country and was established. The question should be: did the foreign investment project have the potential to contribute to the development of the host country at the time it entered? If the answer is in the affirmative then - even if it does not eventually materialize - the project should be regarded as an “investment” within the meaning of the Convention. The assessment should look at the impact the foreign investment was to make on the economy and community of the host country when it was entered.

It is important that an economic activity contributes, or is at least expected to contribute, to the development of the host country. In order for an investment to gain the protection and incentives given by the host country, it must fulfill its part of the “grand bargain.”¹⁵⁶

The expectation of return and profit feature is also one of the areas where investor-state tribunals have not reached an agreement, as some categorize it under the feature of risk.¹⁵⁷ Therefore, the features that are generally agreed upon by most arbitrators following the restrictive approach are: duration, risk, and the commitment of resources. There is a consensus between arbitrators that these features are intertwined, and that the satisfaction of one feature can indicate the satisfaction of other features.¹⁵⁸ For example, if a substantial amount of resources is committed to a project, that can serve as an indication of the satisfaction of the ‘contribution to the host state development’ feature, and so forth. However, these features, although usually considered individually, should be assessed collectively due to their interdependent nature.¹⁵⁹

¹⁵⁶ See in general Jeswald W. Salacuse 46 HARVARD INTERNATIONAL LAW JOURNAL 67 (2005).

¹⁵⁷ ROMAK S.A. v THE REPUBLIC OF UZBEKISTAN, Award, para. 230 (PERMANENT COURT OF ARBITRATION, 2009).

¹⁵⁸ Salini v. Morocco, Decision on Jurisdiction, para. 52 (ICSID, 2001).

¹⁵⁹ Id. at para. 52, where the tribunal stated “*these various criteria should be assessed globally even if, for the sake of reasoning, the Tribunal considers them individually here.*”

4. The Correct Approach?

As the definition of ‘investment’ is not found in the Convention, one should give considerable attention to the drafters’ objectives and purposes behind this omission. The omission of a definition was not due to the drafters’ inability to define the term, but rather it was deliberately left undefined.¹⁶⁰ The drafters of the Convention, after a long debate, opted to leave the term undefined to give the Convention a wide-open jurisdiction.¹⁶¹ Different countries have different purposes and perceptions on the matter of foreign investment; therefore, they are better positioned to define the term in accordance to their needs and objectives.¹⁶² Hence, the drafters transferred the burden of defining the term ‘investment’ from the Convention to individual countries.¹⁶³ This thereby gave them the ability to decide what activities they would consider as ‘investments’ worthy of ICSID arbitration in their national laws, investment contracts, and BITs.¹⁶⁴

The World Bank Executive Directors’ Report provides that “the Executive Directors did not think it necessary or desirable to attempt to define the term ‘investment’ given the essential requirement of consent of the parties and the fact that Contracting States could make known in

¹⁶⁰ History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States § 2, part 1, at 972 (ICSID 2009 reprint). See also Mortenson, HARVARD INTERNATIONAL LAW JOURNAL 251 (2010).

¹⁶¹ For extensive explanation on the negotiations and details that led to the adoption of this approach see Mortenson, HARVARD INTERNATIONAL LAW JOURNAL (2010). Also see the Report of the Executive Directors on the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965), which reads at para 27: “No attempt was made to define the term “investment” given the essential requirement of consent by the parties, and the mechanism through which Contracting States can make known in advance, if they so desire, the classes of disputes which they would or would not consider submitting to the Centre (Article 25(4)).”

¹⁶² See CHRISTOPH SCHREUER, paras. 113-17 (Cambridge University Press 2 ed. 2009).

¹⁶³ History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States § 2, part 1, at 710 (ICSID 2009 reprint).

¹⁶⁴ CHRISTOPH SCHREUER, para. 121 (Cambridge University Press 2 ed. 2009).

advance within what limits they would consider making use of the facilities of the Centre. *Thus each Contracting State could, in effect, write its own definition.*”¹⁶⁵

Given the fact that the drafters opted for a wide-open jurisdiction for the Center by not defining the term ‘investment,’ the drafters also created a set of opt-out mechanisms that individual countries can use to tailor the forms of investment eligible for protection in their particular circumstances.¹⁶⁶ In the latter option, states can notify the Center of any disputes they wish not to arbitrate under ICSID, even if those disputes arise from an “investment” under their national laws, contracts, or BITs.¹⁶⁷

Thus, an “investment” can be described as a “status” that a country consents to grant to certain foreign economic activities operating on its soil that enables them to enjoy the protection of international law. This status is given to foreign economic activities that fit certain criteria that the host country incorporates in its BIT or local laws. Any economic activity fulfilling that definition is considered an “investment,” which the state consents, in advance, to elevate to ICSID jurisdiction in case of dispute. While the State parties have a wide margin in defining the

¹⁶⁵ History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States § 2, part 1, at 972 (ICSID 2009 reprint) [emphasis added].

¹⁶⁶ Article 25(4) of the ICSID Convention sets the opt-out mechanism by contracting states, “*Any Contracting State may, at the time of ratification, acceptance or approval of this Convention or at any time thereafter, notify the Centre of the class or classes of disputes which it would or would not consider submitting to the jurisdiction of the Centre. The Secretary-General shall forthwith transmit such notification to all Contracting States. Such notification shall not constitute the consent required by paragraph (1).*”

¹⁶⁷ Until May 2016 seven countries have submitted their reservations in accordance with Article 25(4) of the ICSID Convention. Examples of these reservations are: (China: excludes all complaints not based on expropriation or nationalization), (Saudi Arabia: reserves the right not to submit any questions pertaining to oil, or pertaining to acts of sovereignty), (Turkey: will submit only disputes arising directly out of an investment which has been approved by the authorities). Other countries that made reservations are (Guatemala, Indonesia, Jamaica, and Papua New Guinea). See CONTRACTING STATES AND MEASURES TAKEN BY THEM FOR THE PURPOSE OF THE CONVENTION. (ICSID, 2016). At section 8-D (NOTIFICATIONS CONCERNING CLASSES OF DISPUTES CONSIDERED SUITABLE OR UNSUITABLE FOR SUBMISSION TO THE CENTRE). Available at: <https://icsid.worldbank.org/apps/ICSIDWEB/icsiddocs/Documents/ICSID%208-Contracting%20States%20and%20Measures%20Taken%20by%20Them%20for%20the%20Purpose%20of%20the%20Convention.pdf>.

term, they should always consider the objectives and purpose of the Convention, thus not including transactions that are clearly unrelated to the general concept of “investment.”¹⁶⁸

It is clear that the intention and goal of the drafters was to follow the deferential approach in defining “investment” under the Convention.¹⁶⁹ Tribunals should consider this historical background and respect state autonomy in this matter. Any economic activity fulfilling the definition of investment in the consent documents of the host state should be allowed access to ICSID arbitration. Access to ICSID should not be restricted to activities that are found to be “investments” in the arbitrators’ view (*i.e.*, the restrictive approach).¹⁷⁰ The only barrier to arbitration under ICSID should be where the definition of investment in the host country’s law or BIT is disconnected from the objective purpose of the Convention (*i.e.*, a definition that includes pure commercial transactions, or disputes arising from non-legal grounds). This is the position taken by the founders of the Convention; they stated that “Consent of the parties is the cornerstone of the jurisdiction of the Centre.”¹⁷¹ However, that consent should be within the objectives of the Convention, hence “While consent of the parties is an essential prerequisite for the jurisdiction of the Centre, consent alone will not suffice to bring a dispute within its jurisdiction. In keeping with the purpose of the Convention, the jurisdiction of the Centre is further limited by reference to the nature of the dispute and the parties thereto.”¹⁷²

¹⁶⁸ The parties of a BIT “have considerable freedom to determine for themselves whether, for the purpose of the ICSID Convention, their dispute arises out of an investment. That freedom is not, however, unlimited; it is not so extensive as to permit the parties to submit to arbitration under the ICSID Convention disputes that clearly do not relate to investments.” See Ibrahim F.I. Shihata & Antonio R. Parra, *The Experience of the International Center for Settlement of Investment Disputes*, 14 ICSID REVIEW 299, 307-08 (1999).

¹⁶⁹ SCHREUER, 74 (Oxford University Press 2 ed. 2012).

¹⁷⁰ *Id.* at 74-75.

¹⁷¹ REPORT OF THE EXECUTIVE DIRECTORS ON THE CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES para. 25 (World Bank 1965).

¹⁷² *Id.* at para. 25.

The features used under the restrictive approach should not be used as jurisdictional requirements as some tribunals have done. The definition of “investment” is not static and keeps evolving with the needs and objectives of both host countries and investors. Thus, the term investment under the Convention should be given a broad and flexible interpretation. The position taken by the tribunal in *Philip Morris v Uruguay* is probably the most clear and balanced, as the tribunal discussed the restrictive approach by stating that:

*“[the] Salini test has received varied applications by investment treaty tribunals and doctrinal writings. In the Tribunal’s view, the four constitutive elements of the Salini list do not constitute jurisdictional requirements to the effect that the absence of one or the other of these elements would imply a lack of jurisdiction. They are typical features of investments under the ICSID Convention, not ‘a set of mandatory legal requirements.’ As such, they may assist in identifying or excluding in extreme cases the presence of an investment but they cannot defeat the broad and flexible concept of investment under the ICSID Convention to the extent it is not limited by the relevant [investment] treaty.”*¹⁷³

The different views on the interpretation of Article 25(1) of the Convention have raised some serious concerns as to the Convention’s effectiveness in solving investment disputes. In *Saba Fakes v. Turkey* the tribunal voiced this concern by stating, “no unanimous approach has emerged so far from the existing case law” and that the “proposed solutions are inconsistent, if not conflicting, and do not provide any clear guidance to future arbitral tribunals.”¹⁷⁴ Renowned practitioners in the field have also voiced their concerns on this matter. For example, Professor Dolzer noted that “the diversity of reasoning of the tribunals make it difficult to predict the direction of future jurisprudence.”¹⁷⁵

¹⁷³ PHILIP MORRIS BRANDS SÀRL, PHILIP MORRIS PRODUCTS S.A. and ABAL HERMANOS S.A. v ORIENTAL REPUBLIC OF URUGUAY, Decision on Jurisdiction, para. 206 (ICSID, 2013).

¹⁷⁴ Mr. Saba Fakes v. Republic Of Turkey, para. 97 (Final Award), (ICSID, 2010).

¹⁷⁵ R. Dolzer, ‘The Notion of Investment in Recent Practice’, in S. Chamovitz, D. Steger, & P. Van Den Bossche (eds.), *LAW in the Service of Human Dignity: Essays in Honour of Plorentino Feliciano* 261-275 at 275 (2005).

It is clear that not reaching a consensus on this matter will affect the development and effectiveness of the whole ICSID system. The agents of the investor-state arbitration system may start to select other venues to arbitrate their disputes (such as the ICC or SCC) to avoid the issue of proving that their investments qualify for the jurisdictional requirement of Article 25(1) of the ICSID Convention.¹⁷⁶ They would save themselves the time, effort and money of doing so at ICSID if the tribunal reviewing their case follows the restrictive approach. Hence, there is a pressing need to harmonize the interpretation of “investment” under the Convention to preserve its role in international economic development.¹⁷⁷ Professor Emmanuel Gaillard has expressed his hopes that the current divergence between tribunals on the question of “investment” under the Convention “will be harmonized in a manner consistent with the all too often overlooked intentions of the Convention's drafters.”¹⁷⁸

F. POLICY GUIDELINES FOR THE DEFINITION OF INVESTMENT

To better serve the goal of development through FDI, a state should determine its development needs and the objectives it seeks from attracting foreign investment. Once that determination is made, the country would be better positioned to tailor the definition of “investment” to reach

¹⁷⁶ See in this regard Manciaux, 9 JOURNAL OF WORLD INVESTMENT & TRADE 443, para. 7 (2008).

¹⁷⁷ “The ICSID Convention and other investment protection treaties were created not for the sake of directing all private-public disputes into arbitration, but specifically in order to increase salutary economic activity and feed the engine of sustained development and prosperity around the world.” Noah Rubins, *The Notion of 'Investment' in International Investment Arbitration*, in ARBITRATING FOREIGN INVESTMENT DISPUTES: PROCEDURAL AND SUBSTANTIVE LEGAL ASPECTS 323 (Stefan Michael Kröll & Norbert Horn ed. 2004).

¹⁷⁸ Emmanuel Gaillard, *Identify or Define? Reflections on the Evolution of the Concept of Investment in ICSID Practice*, in INTERNATIONAL INVESTMENT LAW FOR THE 21ST CENTURY: ESSAYS IN HONOUR OF CHRISTOPH SCHREUER 416 (Ursula Kriebaum Christina Binder, August Reinisch, and Stephan Wittich ed. 2009).

those goals. For example, a country that is in need of foreign capital and hard currency can adopt an “open asset-based definition” of investment to cover a large array of investment forms and encourage their inflow. On the other hand, a country aspiring to develop its energy sector, for example, might want to emphasize this objective in the BIT by adopting a closed asset-based definition that provides treaty protection to energy related FDI.

The use of exceptions and exclusions in the definition of investment can be useful as well. By inserting exceptions in the definition of investment, the state will clarify, rather than narrow or restrict, the meaning of covered investments. Thus, a country might want to adopt an open asset-based definition to attract as much FDI as it can, but insert exceptions for some economic activities to exclude the latter from the ambit of that definition. For example, to clarify that it will not extend treaty protection to portfolio investments, a state can add an exception to that end while maintaining its open asset-based definition of investment, which provides treaty protection to “any kind of asset.”

The use of limitations on the definition of investment can further help the host country in managing its exposure to investor-state arbitration. For example, requiring that the FDI be established and operate “in accordance with the host country laws,” and that it “has the characteristics of an investment,” will narrow the range of economic projects that can claim treaty benefits and protection. Additionally, these limitations ensure that the investment conforms to the host country’s national policies and laws, thus limiting the risks of FDI on the host economy. A host country may want to limit the application of the treaty to “approved” investments. By doing so, the host country can evaluate the impact of the investment on its economy and development. On the basis of that determination, the host country can allow the

investment to enter its territory with grant of treaty protection, allow it to enter its territory without grant of treaty protection, or deny it entry.

It should be noted however, that a country seeking development should not adopt a single strategy or formula for defining “investment” in its investment treaties. Instead, the definition should be based on the desired types of FDI from each treaty partner. For example, the capital importing country might want to attract FDI in the mining and energy sectors from country (A), while not giving the latter access to its transport and infrastructure sectors. At the same time, the capital-importing country may want to attract investments in the field of transport and infrastructure from country (B), but not give it access to its energy sector. By adopting this strategy, the capital-importing country can control the types of FDI it wishes to attract from direct treaty partners. It will also be able to attract the best and most advanced technologies and know-how from capital-exporting countries that are known for their advancement in a specific sector. For example, attracting investments in the nuclear energy sector from North American or Western European countries, where such sector is highly advanced, might be better than attracting this type of investment from Asian or African countries, where the same sector is not as advanced.

Another issue related to the definition of investment can be the inclusion of certain requirements to the definition. These requirements enable treaty protection only when they are satisfied by the foreign investor. For example, a country with high unemployment rates can require foreign investors to employ a certain quota of nationals. The host country can be stricter in this regard by requiring employment of its nationals in specific levels of management and technical positions to ensure the transfer of know-how and managerial skills. The host country can also require that the assets covered under the investment treaty must be used in a commercial

or business operation. Thus, vacation assets or other personal assets of the foreign investor in the host country will not be covered by treaty protection. The requirement of physical presence in the host country can ensure that only real investments that contribute to the development of the host country will be covered under the treaty.

Many BITs provide in their preambles that the objective of the BIT is to enhance economic relations and economic development of its parties. However, they do not include this objective in the definition of covered investment. Hence, host countries might want to include a “contribution to development” requirement in their definition.¹⁷⁹ This will be a useful way to target and encourage those investments that provide development benefits to the host country. It will also clearly indicate that the protection of the investment treaty should be balanced with the host country’s expectation of development from the foreign investment. This will allow the host country to raise this as a defense in investor-state arbitration should future disputes arise.

II. THE DEFINITION OF ‘FOREIGN INVESTORS’

International investment law is designed to protect natural and juridical foreign investors who invest their resources overseas. Therefore, not only should the economic activity in the host state fit the definition of “investment” under the investment treaty to enjoy protection, but it should also be conducted by a “foreign investor.” Similarly, for investor-state dispute resolution under

¹⁷⁹ UNCTAD supports a including a development-based definition for “investment” in future BITs. SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 119-22 (United Nations 2011).

the ICSID Convention, “a national of another Contracting State” is required to enable ICSID jurisdiction to review the dispute.¹⁸⁰

The foreignness of an investor, whether it be a natural or juridical person, is determined via its nationality.¹⁸¹ Determining the investor’s nationality can be a complex issue, especially when the foreign investor is a juridical person incorporated in several countries and consisting of different layers of ownership.¹⁸² This section will discuss the definition of “investor” and the related qualifications for rights under investment treaties and the ICSID Convention.

A. FOREIGN INVESTORS UNDER INVESTMENT TREATIES

Almost uniformly, investment treaties will contain a definition of either “investors”¹⁸³ or “nationals,”¹⁸⁴ and in some instances a definition of both terms.¹⁸⁵ A typical definition is wide enough to include both natural and juridical persons. The U.S. Model BIT defines ‘investor of a party’ as:

*[A] Party or state enterprise thereof, or a national or an enterprise of a Party, that attempts to make, is making, or has made an investment in the territory of the other Party.*¹⁸⁶

¹⁸⁰ See Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965). Article 25(1).

¹⁸¹ Dolzer and Schreuer suggest that “it is most appropriate to refer to investors in general not as ‘she’ or ‘he’ but as ‘it’” due to the fact that most investors are companies. See SCHREUER, 44 n.3 (Oxford University Press 2 ed. 2012).

¹⁸² CHRISTOPHER DUGAN, 291 (Oxford University Press. 2008).

¹⁸³ e.g., Agreement between the Federal Republic of Germany and the Hashemite Kingdom of Jordan concerning the Encouragement and Reciprocal Protection of Investments (2007). Article 1(3).

¹⁸⁴ e.g., Between The Government of the United Kingdom of Great Britain and Northern Ireland and The Federal Democratic Republic of Ethiopia for the Promotion and Protection of Investments (2009). Article 1(c).

¹⁸⁵ e.g., U.K. - U.A.E. BIT, (1992). Article 1(e).

¹⁸⁶ U.S. Model Bilateral Investment Treaty (2012). Article 1.

This definition includes three categories of foreign persons which, for purposes of the BIT, are “foreign investors” eligible for treaty protection. The first category is states and state enterprises; here, the BIT gives “foreign investor” status to the state itself and its administrative agencies, if they invest in the other party’s territory.¹⁸⁷ The second category is natural persons investing in the territory of the other contracting party.¹⁸⁸ The third category is legal, or juridical, persons from one party investing in the territory of the other treaty party.¹⁸⁹

The three categories of investors in the U.S. Model BIT definition are commonly found, with variation, in most BITs. However, the issue of whether the investor is eligible to claim treaty protection depends on the existence of a *link* between the investor and one of the contracting parties of the BIT.¹⁹⁰ Proving the existence of this link depends on whether the investor is a natural or legal person, and also depends on the requirements of the investment treaty in this regard. This link between the natural person and one of the investment treaty parties is established via the investor’s nationality.

1. Natural Persons as ‘Investors’

The issue of establishing a link between a natural investor and one of the treaty parties does not entail much complexity. This link is determined via nationality; the natural investor should be

¹⁸⁷ See Mark Feldman, *The Standing of State-Owned Entities Under Investment Treaties* in YEARBOOK ON INTERNATIONAL INVESTMENT LAW & POLICY 2010-2011, at 633 (Karl P. Sauvant ed. 2012). Also, the U.S. Model Treaty defines ‘State enterprise’ as “*an enterprise owned, or controlled through ownership interests, by a Party [state].*”

¹⁸⁸ The U.S. Model Treaty defines a ‘National’ in regards to the United States as “*a natural person who is a national of the United States as defined in Title III of the Immigration and Nationality Act.*”

¹⁸⁹ The U.S. Model Treaty defines a ‘enterprise’ as “*any entity constituted or organized under applicable law, whether or not for profit, and whether privately or governmentally owned or controlled, including a corporation, trust, partnership, sole proprietorship, joint venture, association, or similar organization; and a branch of an enterprise.*”

¹⁹⁰ SALACUSE, THE LAW OF INVESTMENT TREATIES 207 (Oxford University Press 2 ed. 2015).

endowed with the nationality of one of the contracting parties, and make an investment in the territory of the other party.¹⁹¹ Consequently, the natural person should be foreign in the host country.

Investment treaties usually refer to natural and juridical persons as “nationals.”¹⁹² A national of a country is one who holds its nationality.¹⁹³ Hence, the general meaning of the term “national” - in the context of natural persons - is limited to those who hold the nationality of that country. However, some BITs explicitly extend the meaning of this term to include permanent residents.¹⁹⁴ Thus, the contracting parties agree to offer permanent residents of one country, even though not citizens, the advantage of benefiting from the treaty if they make an investment in the other party’s territory.

As a principle, the acquisition or loss of nationality is a matter of domestic jurisdiction.¹⁹⁵ Thus, arbitral tribunals, and interpreters of the investment treaty, should accord great weight to the national laws of the country whose nationality is claimed to rule on the question of nationality.¹⁹⁶ Investment treaties usually express this principle by stating that a “national” of one party is one who holds that nationality, or permanent residency status, in accordance with its domestic laws.¹⁹⁷ Even in scenarios where this principle is not explicitly expressed in the

¹⁹¹ CHRISTOPHER DUGAN, 296 (Oxford University Press. 2008).

¹⁹² e.g., UK Model BIT (2008). U.S. Model Bilateral Investment Treaty (2012).

¹⁹³ See OXFORD ENGLISH DICTIONARY, "NATIONAL, ADJ. AND N." (Oxford University Press.). “A citizen or subject of a (usually specified) state; a person whom a state is entitled under international law to protect in its relations with other states.”

¹⁹⁴ e.g., North American Free Trade Agreement (NAFTA) (1992). At Article 201(1) which defines a “national” as “a natural person who is a citizen or permanent resident of a Party.” See also Canada - Argentina BIT (1991). At Article 1(b) which defines ‘investor’ as “any natural person possessing the citizenship of or permanently residing in a Contracting Party in accordance with its laws.”

¹⁹⁵ See CHRISTOPH SCHREUER, para. 642 (Cambridge University Press 2 ed. 2009).

¹⁹⁶ Hussein Nuaman Soufraki v The United Arab Emirates para. 55 (Final Award), (ICSID, 2004).

¹⁹⁷ E.g., The U.K. - Colombia BIT (2014). Defines an ‘Investor’ as “in respect of the United Kingdom: Physical persons deriving their status as United Kingdom nationals from the law in force in the United Kingdom.” See also U.S. Model Bilateral Investment Treaty (2012).

investment treaty,¹⁹⁸ it is accepted in international law “that nationality is within the domestic jurisdiction of the State, which settles, by its own legislation, the rules relating to the acquisition (and loss) of its nationality.”¹⁹⁹

An issue arises when a natural investor holds the nationalities of both contracting parties of the investment treaty. BITs usually offer a solution to this issue by explicitly stating that “a natural person who is a dual national shall be deemed to be exclusively a national of the State of his or her dominant and effective nationality.”²⁰⁰

The doctrine of effective nationality appeared and developed in the context of diplomatic protection.²⁰¹ A country cannot espouse a claim of an injured individual unless the latter was a national of that country.²⁰² However, if the injured individual is a national of both countries (the home and the host states), then the state that holds the right to espouse his claims is the state of his effective nationality. The ICJ affirmed this customary rule in the *Nottebohm* case,²⁰³ where it said that international tribunals have “given their preference to the real and effective nationality.”

The ICJ provided indicators for determining the effective nationality of a dual citizen:

Different factors are taken into consideration, and their importance will vary from one case to the next: the habitual residence of the individual concerned is an

¹⁹⁸ e.g., *The France - Mexico BIT*, (1998). Defines ‘investor’ as “nationals, i.e., physical persons possessing the nationality of either Contracting Party.”

¹⁹⁹ *Hussein Nuaman Soufraki v The United Arab Emirates* para. 55 (Final Award), (ICSID, 2004).

²⁰⁰ e.g., *United States - Rwanda BIT* (2008). Other investment treaties provide that “a natural person who is a dual citizen is deemed to be exclusively a citizen of the State of their dominant and effective citizenship; a natural person who is a citizen of a Party and a permanent resident of the other Party is deemed to be exclusively a national of the Party of which that natural person is a citizen.” *Canada - Honduras FTA* (2013). Yet another form can be “this Agreement shall not apply to investments of natural persons who are nationals of both Contracting Parties unless such natural persons have at the time of the investment and ever since been domiciled outside the Area of the Contracting Party in which they made such investments.” *Japan - Colombia BIT* (2011).

²⁰¹ CHRISTOPHER DUGAN, 292 (Oxford University Press, 2008).

²⁰² See Craig Forcese, *The Capacity to Protect: Diplomatic Protection of Dual Nationals in the ‘War on Terror’*, 17 THE EUROPEAN JOURNAL OF INTERNATIONAL LAW 369, 379 (2006). See also Article 4 of the Convention on Certain Questions Relating to the Conflict of Nationality Laws (1930). “A State may not afford diplomatic protection to one of its nationals against a State whose nationality such person also possesses.”

²⁰³ *Nottebohm Case* (second phase), (ICJ, 1955).

*important factor, but there are other factors such as the center of his interests, his family ties, his participation in the public life, attachment shown by him for a given country and inculcated in his children etc.*²⁰⁴

2. Natural Investors under ICSID

The requirements for ICSID jurisdiction over “investors” are similar to those of “investments.” Foreign investors that wish to invoke dispute settlement under the Convention must pass a dual test. First, they have to fit within the definition ascribed to “investors” in the documents giving consent to ICSID arbitration (usually in the BIT). Second, the foreign investor must meet the nationality requirements under the ICSID Convention. Under the ICSID Convention, natural persons must meet the conditions specified in Article 25(2)(a), which stipulates that a “national of another contracting state” means:

*Any natural person who had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration as well as on the date on which the request was registered pursuant to paragraph (3) of Article 28 or paragraph (3) of Article 36, but does not include any person who on either date also had the nationality of the Contracting State party to the dispute.*²⁰⁵

This provision conditions qualification for ICSID jurisdiction by requiring that a natural investor must be i) a national of a signatory state to the Convention, and ii) not a national of the host state, or a dual national holding the nationality of the host state. Hence, the question of ICSID jurisdiction also relies on determining the nationality of the natural investor.

The ICSID Convention does not provide any guidance on the question of nationality. Thus, arbitral tribunals ruling on the question of nationality should, referring to the general rule

²⁰⁴ Id. at 22.

²⁰⁵ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965), Article 25(2)(a).

under the law of diplomatic protection, apply the national laws of the country whose nationality is claimed.²⁰⁶ This customary rule is incorporated in the Convention on Certain Questions Relating to the Conflict of Nationality Laws, which provides that: “[any] question as to whether a person possesses the nationality of a particular State shall be determined in accordance with the law of that State.”²⁰⁷

However, the international law of diplomatic protection limits the weight that tribunals should accord to the national laws of the country of nationality.²⁰⁸ The ICJ tribunal in the *Nottebohm* case explained this limitation by stating that whether a country is entitled to exercise diplomatic protection “does not depend on the law or on the decision of ... that State,” but rather “[i]t is international law which determines whether [it] is entitled to exercise [diplomatic] protection and to seise the Court.”²⁰⁹ Therefore, international tribunals should give substantial difference to the national laws of the country whose nationality is claimed; however, this shall not be conclusive on the question of nationality.

The tribunal in *Soufraki v. U.A.E.* affirmed this doctrine.²¹⁰ Mr. Soufraki brought an ICSID case under the Italy-UAE BIT.²¹¹ The UAE objected to the jurisdiction of the tribunal on the grounds that Mr. Soufraki was not a national of Italy. Soufraki provided the tribunal with several certificates of nationality and passports to prove his Italian nationality. The tribunal

²⁰⁶ e.g., Hussein Nuaman Soufraki v The United Arab Emirates para. 55 (Final Award), (ICSID, 2004). See also CHRISTOPH SCHREUER, para. 642 (Cambridge University Press 2 ed. 2009).

²⁰⁷ Article 2 of the Convention on Certain Questions Relating to the Conflict of Nationality Laws (1930).

²⁰⁸ CHRISTOPHER DUGAN, 298 (Oxford University Press. 2008).

²⁰⁹ *Nottebohm* Case 20-22 (second phase), (ICJ, 1955).

²¹⁰ Hussein Nuaman Soufraki v The United Arab Emirates (Final Award), (ICSID, 2004).

²¹¹ Italy - U.A.E. BIT (1995).

examined these documents and ultimately decided that Mr. Soufraki did not provide sufficient evidence to prove his Italian nationality.²¹² In its analysis of the matter, the tribunal stated:

*It is accepted in international law that nationality is within the domestic jurisdiction of the State, which settles, by its own legislation, the rules relating to the acquisition (and loss) of its nationality. Article 1(3) of the BIT reflects this rule. But it is no less accepted that when, in international arbitral or judicial proceedings, the nationality of a person is challenged, the international tribunal is competent to pass upon that challenge. It will accord great weight to the nationality law of the State in question and to the interpretation and application of that law by its authorities. But it will in the end decide for itself whether, on the facts and law before it, the person whose nationality is at issue was or was not a national of the State in question and when, and what follows from that finding. Where, as in the instant case, the jurisdiction of an international tribunal turns on an issue of nationality, the international tribunal is empowered, indeed bound, to decide that issue.*²¹³

Dual nationals holding the nationality of the host state are explicitly barred from ICSID jurisdiction by virtue of article 25(2)(a) of the Convention.²¹⁴ The Executive Directors' Report notes that "a natural person who was a national of the State party to the dispute would not be eligible to be a party in proceedings under the auspices of the Centre, even if at the same time he had the nationality of another State. This ineligibility is absolute and cannot be cured even if the State party to the dispute had given its consent."²¹⁵ Hence, host state nationals cannot use the ICSID Convention to sue their governments, because such individuals receive protection from the legal system of the state of which they are nationals.²¹⁶ However, a situation can be imagined where a natural person may be a dual citizen holding the nationality of the host country by virtue

²¹² Hussein Nuaman Soufraki v The United Arab Emirates para. 81 (Final Award), (ICSID, 2004).

²¹³ Id. at para. 55.

²¹⁴ The tribunal in *Champion Trading Company v Arab Republic of Egypt* 16 (Decision on Jurisdiction), (ICSID, 2003). stated that "According to the ordinary meaning of the terms of the Convention (Article 25 (2)(a)) dual nationals are excluded from invoking the protection under the Convention against the host country of the investment of which they are also a national."

²¹⁵ History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States. 1078 (2009 Reprint).

²¹⁶ SALACUSE, *THE LAW OF INVESTMENT TREATIES* 207 (Oxford University Press 2 ed. 2015).

of the *jus sanguinis* principle,²¹⁷ but have no real ties to the host country. It appears that international tribunals deal with this matter in a formalistic fashion and forbid the dual national from recourse to ICSID.²¹⁸

To qualify for ICSID Jurisdiction, the foreign investor must not be a national of the host country, but must be a national of a signatory country to the Convention, on two critical dates: on the date when the foreign investor and the host country consent to ICSID arbitration,²¹⁹ and on the date when the foreign investor officially registers its arbitration request. The Convention, from its wording, does not require continuity of nationality between these two dates.²²⁰ Accordingly, if the foreign investor acquires the nationality of the host state during the proceedings of the ICSID arbitration, this shall not affect jurisdiction.

B. JURIDICAL PERSONS AS “INVESTORS”

Most foreign investments are made by juridical persons. Whether a juridical person qualifies as an “investor” under the investment treaty is more complex. This is due to the nature of

²¹⁷ *Jus sanguinis* refers to the acquisition of citizenship by birth to parents of a particular nationality. See CHRISTOPHER DUGAN, 297 (Oxford University Press, 2008).

²¹⁸ See *Champion Trading Company v Arab Republic of Egypt* (Decision on Jurisdiction), (ICSID, 2003). The ICSID Working Group had raised this question, however it expressed its “unwillingness to deal in the Convention with the problem of involuntary acquisitions of nationality, feeling that it would be up to the Tribunals concerned to decide whether forced nationality would have to be taken into account or could be disregarded.” See *History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States* § 2, Part II, at 868 (ICSID 2009 Reprint).

²¹⁹ This consent must be in writing and can be in the form of a standing offer in a BIT or national investment law, a clause in an investment contract or in an arbitration agreement between the parties. See CHRISTOPH SCHREUER, 191-92 (Cambridge University Press 2 ed. 2009).

²²⁰ *Id.* at 276.

corporations, which can be incorporated and owned by various stockholders, in several layers of ownership, and in multiple countries.

Investment treaties usually define juridical investors in a broad sense to include various types of legal entities.²²¹ The definitions are wide enough to encompass both commercial and not-for-profit entities.²²² The inclusion of not-for-profit organizations comes from the fact that they, in some cases, provide the host country with resources and capital, such as building and operating schools and hospitals. Also, these organizations may invest their capital in commercial projects to gain revenue for their not-for-profit projects. Hence, their contribution to the host state's economy and development via the injection of capital, resources, and expertise is similar to that of foreign investors. Consequently, their status as 'not-for-profit' organizations seems of little significance, and they are therefore given treaty protection.²²³

The broad definition of juridical investors in investment agreements is also wide enough to include both privately-owned and governmentally-owned enterprises. This is due to the fact that many countries create enterprises with their surplus capital to conduct investment projects abroad. These governmentally owned or controlled enterprises are usually "indistinguishable from the completely privately owned enterprise both in their legal characteristics and in their activities."²²⁴ Hence, the distinction between private versus government-owned enterprises

²²¹ e.g., "any legal person or any other entity duly constituted or organized ... whether or not for profit, and whether private or government owned or controlled, including any corporation, trust, partnership, sole proprietorship, joint venture, association, organisation or company." Japan - Oman BIT (2015). Article 1(c).

²²² CHRISTOPHER DUGAN, 305 (Oxford University Press. 2008).

²²³ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 81 (United Nations 2011).

²²⁴ Aron Broches, *The Convention on the Settlement of Investment Disputes between States and Nationals of Other States* in COLLECTED COURSES OF THE HAGUE ACADEMY OF INTERNATIONAL LAW 354-55 (The Hague Academy of International Law ed. 1972).

becomes trivial and outdated, as their investments appear to be no different from investments made by private investors.²²⁵

Similar to the situation with natural investors, the link between the juridical investor and one of the treaty parties is established via nationality. However, in contrast to natural investors, most investment agreements use one of the two main standards for determining nationality of juridical investors. These standards are: i) the country of organization or incorporation,²²⁶ and ii) the country of the seat.²²⁷ Many investment treaties use a combination of these standards.²²⁸ Some investment treaties use the standard of “the country of ownership or control,” or include it as an additional standard, to widen - or in other cases to narrow - the scope of covered investors.²²⁹

The preference for a particular nationality standard in an investment treaty depends on the various interests of the contracting parties and on legal, cultural, economic and political factors.²³⁰ Hence all choices are valid, and it is not appropriate to establish a general rule, as

²²⁵ SORNARAJAH, 68-69 (Cambridge University Press 3 ed. 2012).

²²⁶ *e.g.*, Japan - Oman BIT which defines an “enterprise of a Contracting Party” as “any legal person or any other entity duly constituted or organised under the applicable laws and regulations of that Contracting Party, whether or not for profit, and whether private or government owned or controlled, including any corporation, trust, partnership, sole proprietorship, joint venture, association, organisation or company.” See Japan - Oman BIT (2015). Article 1(c).

²²⁷ *e.g.*, Germany - Afghanistan BIT which defines an “investor” as “any juridical person as well as any commercial or other company or, association with or without legal personality having its seat in the territory of the Federal Republic of Germany, irrespective of whether or not its activities are directed at profit.” See Germany - Afghanistan BIT (2005). Article 1(3)(a).

²²⁸ *e.g.*, Azerbaijan – San Marino BIT which defines an “investor” as “a company or other legal entity incorporated or duly constituted in accordance with applicable national legislation of one Contracting Party and having its seat and conducting substantial business activities within the state territory of that Contracting Party who makes an investment in the state territory of the other Contracting Party. See Azerbaijan - San Marino BIT (2015). Article 1(3)(b). See also SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 81 (United Nations 2011).

²²⁹ *e.g.*, Switzerland – Georgia BIT allows “legal entities not established under the law of that Contracting Party but effectively controlled by natural persons ... or by legal entities ...” of the treaty party to qualify as “investors.” See Switzerland – Georgia BIT (2014). Article 1(1)(c).

²³⁰ “There are two standard tests of the “nationality” of a corporation. The place of incorporation is the test generally favoured in the legal systems of the common law, while the *siège social* is more generally accepted in the

different states take different approaches on the question of qualifying investors for treaty protection.²³¹ Nonetheless, the consequences of these approaches vary and lead to different results. A country seeking development from FDI should thus consider whether it prefers a wide range of qualifying investors, in order to attract as much FDI as possible, or a narrow and specific range of investors, in order to focus its efforts on quality investments.

1. The country of organization or incorporation

Under the place-of-incorporation standard, “a company, partnership or other business association is deemed to be attached to the legal order under which it was incorporated, irrespective of the place and seat of its economic activities.”²³² This standard is the most common method for defining the nationality of juridical investors in investment treaties.²³³ This standard provides simplicity and certainty in determining a juridical investor’s nationality. It also allows a capital-importing country an easy-to-satisfy standard in order to provide treaty coverage to a wide variety of investors and thus attract more foreign investments into its economy.

On the other hand, the place-of-incorporation test may lead to disadvantageous results for both treaty parties. It is foreseeable, under such a standard, that nationals of the host state or nationals of non-contracting states would incorporate shell or mailbox companies in the territory

civil law systems.” See SEPARATE OPINION OF JUDGE JESSUP in the Barcelona Traction Decision of 1970, at para. 39.

²³¹ See Anthony C. Sinclair, *The Substance of Nationality Requirements in Investment Treaty Arbitration*, 20 ICSID REVIEW 357, 367 (2005).

²³² RUDOLF DOLZER & MARGRETE STEVENS, *BILATERAL INVESTMENT TREATIES* 35 (Kluwer Law International, 1995).

²³³ The tribunal in *Tokios v Ukraine* observed that “reference to the state of incorporation is the most common method of defining the nationality of business entities under modern BITs and traditional international law.” See *Tokios Tokeles v Ukraine*, para. 63 (Decision on Jurisdiction), (ICSID, 2004).

of the other treaty party to create artificial links with the home country. The shell company will not have any real or significant economic ties with the home country, nor will it bring any new capital or resources to the host country, as the shell company is just a cover for nationals of the host country to enjoy treaty protection. At the same time, host countries trying to manage their exposure to investor-state claims may not want to grant treaty protection to investors that do not have real economic ties with their home country, or to nationals of third countries that do not grant the nationals of the host country any similar protections or privileges. Hence, the country of incorporation test can be an enticement for treaty shopping - where foreign investors from third states, or from the host state, establish companies in the other treaty party to enjoy treaty protection. Although the latter practice is not illegal *per se*,²³⁴ it does go against the purpose of granting benefits for FDI.

To avoid treaty shopping under the “place-of-incorporation” standard, a development-seeking country may include a “denial of benefits” clause in its investment treaties.²³⁵ This allows the contracting parties to ensure that the protections of the investment treaty are only available to those juridical investors that have sufficient economic ties with the home state.²³⁶ A typical denial of benefits clause reads as follows:

Subject to prior notification and consultation, a Contracting Party may deny the benefits of this Agreement to an investor of the other Contracting Party that is an

²³⁴ The tribunal in *Aguas de Tunari v Bolivia* stated that “It is not uncommon in practice and –absent a particular limitation- not illegal to locate one’s operations in a jurisdiction perceived to provide a beneficial regulatory and legal environment in terms, for example, of taxation or the substantive law of the jurisdiction, including the availability of a BIT.” *Aguas del Tunari S.A. v Republic of Bolivia* para. 330(d) (Decision on Jurisdiction), (ICSID, 2005). See also Christoph Schreuer, *Nationality of Investors: Legitimate Restrictions vs. Business Interests*, 24 ICSID REVIEW 521, 524 (2009). “The establishment of companies so as to obtain benefits from domestic law and treaties is neither unethical nor illegal and is standard practice in international economic relations. Nationality planning has become as much a standard feature of diligent management as tax planning.”

²³⁵ Japan - Oman BIT (2015). Article 23(2).

²³⁶ DAVID COLLINS, AN INTRODUCTION TO INTERNATIONAL INVESTMENT LAW 87 (Cambridge University Press, 2017).

*enterprise of the other Contracting Party and to its investments if the enterprise is owned or controlled by an investor of a non-Contracting Party and the enterprise has no substantial business activities in the Area of the other Contracting Party.*²³⁷

Such a denial of benefits clause creates a twofold test. The first test entails evidencing that the juridical investor maintains business activities in its home country. This requires more than a “brass plate” office with an address.²³⁸ The second test entails the possibility of piercing the corporate veil to determine the real owners and controllers of the juridical investor.²³⁹ If the owners and controllers of the juridical investor are nationals of a non-contracting country to the investment treaty, or are nationals of the host country, then the parties of the treaty have the right to refuse to extend treaty protection to that juridical investor.

The incorporation of a denial of benefits clause in an investment treaty is an effective method to shape the contours of the definition of investor based on “a holistic rather than scientific (voting shares and place of incorporation) [one].”²⁴⁰ Therefore, the use of denial of benefits clauses in investment treaties, and their effect in investor-state arbitrations, is growing.²⁴¹

²³⁷ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 93 (United Nations 2011).

²³⁸ *Id.* at 93.

²³⁹ Some investment treaties define ‘ownership’ and ‘control’ of juridical investors. For example the Swiss – Trinidad and Tobago BIT extends treaty protection to “*juridical persons not established under the law of that Contracting Party (i) in which more than 50 per cent of the equity interest is owned by persons of that Contracting Party; or (ii) in relation to which persons of that Contracting Party have the power to name a majority of their directors or otherwise legally direct their actions.*” Swiss – Trinidad and Tobago BIT (2010). Article 1(1)(c).

²⁴⁰ COLLINS, 88 (Cambridge University Press. 2017).

²⁴¹ *See id.* at 87-88.

2. The country of the seat

Some BITs use the standard of the company seat or “*siège social*” to provide treaty protection. Under this standard, only those juridical investors with an effective center of administration of their business operations in the home country will qualify as investors when investing in the host country.²⁴² German BITs are notable for using this standard in their BITs;²⁴³ for example, the Germany–Jordan BIT provides that an “investor” means “any juridical person as well as any commercial or other company or association with or without legal personality *having its seat in the territory of the Federal Republic of Germany*, irrespective of whether or not its activities are directed at profit.”²⁴⁴

The seat of the company may not be as easy to determine as the “place-of-incorporation.” However, the seat standard reflects a more substantial economic relationship with the home country, thus avoiding the possibility of treaty shopping. Proof of a company seat requires that a business entity is effectively organized at that country. This can be established by evidencing that director and shareholder meetings are regularly held in that country, that there is top company management sitting within that country, that the company has a number of employees working in that country, that general expenses or overhead costs are incurred in that country for the maintenance of the physical location of the company in that country, and an address with phone and fax numbers in that country.²⁴⁵

²⁴² See *Alps Finance and Trade AG v The Slovak Republic* para. 217 (Award), (UNCITRAL, 2011).

²⁴³ *e.g.*, Germany - Afghanistan BIT (2005). Germany - Antigua and Barbuda BIT (1998). Germany - Bahrain BIT (2007).

²⁴⁴ Germany - Jordan BIT (2007). Article 1(3)(a).

²⁴⁵ See *Alps Finance and Trade AG v The Slovak Republic* para. 217 (Award), (UNCITRAL, 2011).

Other BITs require the satisfaction of both standards (incorporation and seat) to qualify for coverage under treaty protection. For example, the Swiss–Georgia BIT defines “investor” as “legal entities, including companies, corporations, business associations and other organisations, which are *constituted or otherwise duly organised under the law of that Contracting Party and have their seat, together with substantial business activities, in the territory of that Contracting Party.*”²⁴⁶ It is noticeable that this definition requires “*substantial business activities;*” this is likely to strengthen the country of seat test further and avoid granting protection to shell companies.²⁴⁷

Finally, a few investment treaties use the “country of ownership or control” as the standard for determining corporate nationality. Under this standard, a juridical person will be considered an investor of the state whose nationals own or control it.²⁴⁸ However, determining control is not an easy task;²⁴⁹ hence, some treaties combine this standard with the country of incorporation or country of seat standards.²⁵⁰

²⁴⁶ Swiss – Georgia BIT (2014). Article 1(1)(b).

²⁴⁷ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 83 (United Nations 2011).

²⁴⁸ Id. at 84.

²⁴⁹ Id. at 84.

²⁵⁰ e.g., Swiss – Lebanon BIT defines juridical investors as “*legal entities, including companies, corporations, business associations and other organizations, which are established under the law of that Contracting Party, as well as legal entities not established under such law but effectively controlled by nationals or legal entities of that Contracting Party; these criteria also apply to holding and offshore companies.*” Swiss – Lebanon BIT (2000). Article 1(1)(b).

C. JURIDICAL INVESTORS UNDER ICSID

The ICSID Convention does not define the concept of juridical persons.²⁵¹ Although the concept is not defined, there are inherent characteristics in the term that should be present in a juridical claimant under ICSID. For example, a juridical investor must have legal personality under some legal system, normally the legal system of the state whose nationality is claimed.²⁵² Therefore, mere associations of individuals or of juridical persons would not qualify for ICSID jurisdiction, even if the investment treaty giving consent to ICSID arbitration extends protection to associations without legal personality in their definitions of “investor.”²⁵³

Article 25 of the Convention sets the requirement for ICSID jurisdiction over juridical investors. It requires that juridical investors have “the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration.”²⁵⁴ Thus, a juridical investor must be a national of country other than that involved in the dispute. ICSID tribunals have uniformly adopted the place-of-incorporation test or seat rather than control when determining the nationality of juridical claimants.²⁵⁵ The tribunal in *Tokios Tokeles v. Ukraine* noted that, “Although Article 25(2)(b) of the Convention does not set forth a required method for determining corporate nationality, the generally accepted (albeit implicit) rule is that the nationality of a corporation is determined on

²⁵¹ See Article 25(2)(b) of the ICSID Convention which defines a “National of another Contracting State” as “any juridical person which had the nationality of a Contracting State other than the State party to the dispute...”

²⁵² CHRISTOPH SCHREUER, 278, para. 693 (Cambridge University Press 2 ed. 2009).

²⁵³ e.g., Germany - Afghanistan BIT which defines an “investor” as “any juridical person as well as any commercial or other company or, association with or without legal personality ...” Germany - Afghanistan BIT (2005). Article 1(3)(a).

²⁵⁴ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965). Article 25(2)(b).

²⁵⁵ SCHREUER, THE ICSID CONVENTION: A COMMENTARY 281 para. 699 (2001).

the basis of its *siège social* or place of incorporation.”²⁵⁶ Tribunals have also agreed that the Convention does not require any further investigation in regards to the real controllers of the juridical person, or any other requirements, so long as the juridical claimant fits within the “reasonable” definition and requirements ascribed to “investor” under the consent documents.²⁵⁷ The tribunal in *ADC v. Hungary* affirmed the position by stating that, “the Tribunal cannot read more into the BIT than one can discern from its plain text.”²⁵⁸

Many national laws require foreign investors to undertake their investment in the host country via a nationally incorporated legal entity. This allows the host country to monitor and supervise the activities of the foreign investor in its territory. However, since the foreign investment is undertaken via a national company, that company is a national of the host country under the country of incorporation test. Consequently, this would exclude the foreign investor from the domain of ICSID jurisdiction. The drafters of the convention were aware that a large and important group of investors would be outside the Convention’s scope if this issue were not explicitly addressed in the Convention.²⁵⁹

Nationally incorporated companies controlled by foreign investors were thus added to the jurisdiction of ICSID as an exception to the general principle of the Convention, *i.e.*, that it deals

²⁵⁶ *Tokios Tokeles v Ukraine*, para. 42 (Decision on Jurisdiction), (ICSID, 2004).

²⁵⁷ The tribunal in *Tokios v Ukrain* stated that “*Contracting Parties are free to define their consent to jurisdiction in terms that are broad or narrow; they may employ a control-test or reserve the right to deny treaty protection to claimants who otherwise would have recourse under the BIT. Once that consent is defined, however, tribunals should give effect to it, unless doing so would allow the Convention to be used for purposes for which it clearly was not intended.*” See *id.* at para. 39. Also, The tribunal in *Romp petrol v Romania* commented on this issue by stating that “*the Tribunal cannot find any trace of justification for an argument that international law deprives the States concluding a particular treaty – whether a multilateral Convention like ICSID or a bilateral arrangement like a BIT – of the power to allow, or indeed to prescribe, the place and law of incorporation as the definitive element in determining corporate nationality for the purposes of their treaty.*” *The Rompetrol Group N.V. v Romania* para. 92 (Decision on Jurisdiction), (ICSID, 2008).

²⁵⁸ *ADC Affiliate Limited v The Republic of Hungary* para. 359 (Award), (ICSID, 2006).

²⁵⁹ CHRISTOPH SCHREUER, 296-97 (Cambridge University Press 2 ed. 2009).

exclusively with disputes between parties of diverse nationalities.²⁶⁰ Article 25(b)(2) of the Convention, which defines juridical nationals of other contracting states, can be divided into two clauses as follows:

- i) any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration and
- ii) any juridical person which had the nationality of the Contracting State party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention.²⁶¹

For the exception to apply, a national of the host country must meet two conditions as specified in the second clause of Article 25(b)(2). The first condition is the agreement of the host state to treat the national company as a foreign entity for purposes of the Convention. Without this agreement, ICSID jurisdiction will not exist. The second condition is the objective factor of foreign control. The tribunal will have to examine and establish foreign control of the national claimant to extend its jurisdiction to the dispute.

The two conditions found in the second clause of Article 25(b)(2) of the Convention (agreement of the host country and foreign control) are independent of each other. The sole agreement by the host country to treat the locally incorporated company – because of its foreign control - as a national of another state for purposes of the Convention will not be sufficient to extend ICISD jurisdiction. Rather, although the latter creates a rebuttable presumption of foreign control,²⁶² the tribunal will have to examine the facts of the case to determine whether foreign

²⁶⁰ TSA Spectrum de Argentina S.A v Argentine Republic para. 139 (Award), (ICSID, 2008).

²⁶¹ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965). Article 25(b)(2).

²⁶² The tribunal in *Vacuum Salt v Ghana* noted “*Nevertheless the words “because of foreign control” have to be given some meaning and effect. These words are clearly intended to qualify an agreement to arbitrate and the parties are not at liberty to agree to treat any company of the host State as a foreign national: They may only do so*

control exists *de facto*. The tribunal in *Vacuum Salt v. Ghana* explained the independence of these two conditions by stating:

The parties' agreement to treat Claimant as a foreign national "because of foreign control" does not ipso jure confer jurisdiction. The reference in Article 25(2)(b) to "foreign control" necessarily sets an objective Convention limit beyond which ICSID jurisdiction cannot exist and parties therefore lack power to invoke same no matter how devoutly they may have desired to do so.²⁶³

The requirement of obtaining the consent of the host country to treat the national company as a foreigner for purposes of the Convention does not entail much complexity. The Convention does not specify any form for that consent. A simple clause that explicitly or implicitly gives that effect in the BIT, national legislation, or investment contract would suffice.²⁶⁴ Determining foreign control, however, is more complicated.

The Convention does not define "foreign control." Giving a fixed definition of foreign control in the Convention would have frustrated its application, as corporate investors are usually complexly structured. However, neither should the question of foreign control be answered in a formalistic manner. A formalistic determination of foreign control would be based on the percentage of ownership alone. The percentage of ownership in shares or voting rights in a company is not a reliable indicator of control. Corporate lawyers know that in many situations minority shareholders can have more control over the management of a company than the majority shareholders. This is due to the various corporate structures and different schemes of voting rights and classes of shares. Therefore, the mere ownership of majority shares in a

"because of foreign control." The Tribunal concludes that the existence of consent to an arbitration clause such as paragraph 36(a) of the 1988 Lease Agreement in circumstances such that jurisdiction could be premised only on the second clause of Article 25(2)(b) raises a rebuttable presumption that the "foreign control" criterion of the second clause of Article 25(2)(b) has been satisfied on the date of consent." See Vacuum Salt Products Ltd v Republic of Ghana para. 38 (Award), (ICSID, 1994).

²⁶³ Id. at para. 36.

²⁶⁴ See SCHREUER, THE ICSID CONVENTION: A COMMENTARY 299-301 (2001).

company is not conclusive on the question of control. Consequently, foreign control is a factual element that should be determined objectively based on all the facts and circumstances present in a particular case. One tribunal noted the following in its interpretation of “foreign control”:

The Tribunal notes, and itself confirms, that ‘foreign control’ within the meaning of the second clause of Article 25(2)(b) does not require, or imply, any particular percentage of share ownership. Each case arising under that clause must be viewed in its own particular context, on the basis of all of the facts and circumstances. There is no ‘formula.’ It stands to reason, of course, that 100 percent foreign ownership almost certainly would result in foreign control, by whatever standard, and that a total absence of foreign shareholding would virtually preclude the existence of such control. How much is ‘enough,’ however, cannot be determined abstractly.²⁶⁵

Determining foreign control requires a factual and objective examination of several factors in their totality on case-by-case basis. These factors include the amount of equity participation, voting rights, and management combined.²⁶⁶ Tribunals reviewing this question should give considerable weight to the parties’ definition of “foreign control” in the consent documents to the extent that it does not go against the objectives of the Convention.²⁶⁷ For example, it has been noted that foreign control in this sense does not mean actual control, but rather *the legal capacity* to exercise control.²⁶⁸

²⁶⁵ Vacuum Salt Products Ltd v Republic of Ghana para. 43 (Award), (ICSID, 1994).

²⁶⁶ Schreuer observes “*On the basis of the Convention’s preparatory works as well as the published cases, it is possible to conclude that the existence of foreign control is a complex question requiring the examination of several factors such as equity participation, voting rights and management. There is no mathematical formula based on shareholding or votes alone.*” See SCHREUER, THE ICSID CONVENTION: A COMMENTARY 327 para. 864 (2001).

²⁶⁷ “*For purposes of ICSID’s jurisdiction, the concept of control should be treated with some flexibility.*” Id. at 327 para. 865.

²⁶⁸ Id. at 326-27 paras. 862-63.

D. POLICY GUIDELINES FOR THE DEFINITION OF “INVESTOR”

The approach a state takes when defining “investor” should be tied with the approach taken when defining “investment.” If the host country adopts an “open asset-based definition” of investments because of its policy of attracting a wide range of FDI, then it should adopt the “place-of-incorporation” definition for “investors.” This definition is easy to satisfy, giving a wide range of investors the ability to take advantage of the treaty; thus, it complements the approach followed in the definition of “investment.” The “state of incorporation” definition may create the opportunity for treaty shopping, but a capital-importing country striving for FDI might not consider this an issue, as long as it receives the investment.

A country that seeks specific investments in specific fields, on the other hand, may want to adopt a “country of seat” definition. This type of definition ensures that there is a genuine link between the investor and his home country, thus managing the host state’s exposure to investment arbitration in the future.

Similar to the situation in “investments,” the use of limitations and exceptions in the definition of “investor” can be beneficial. A capital-importing country seeking development from FDI may require foreign investors to have substantial business activities in the home country to benefit from treaty protection. It can require so by including a “denial of benefits” clause in the investment treaty. This will prevent treaty shopping and consequently manage its exposure to investment claims. Another limitation can be the requirement of “control;” under this requirement, the foreign investor must be controlled by nationals of the home country. Thus, a juridical investor not controlled by nationals of the home country, although incorporated or seated in the home country, will not qualify for treaty protection.

The definitions of “investment” and “investor” are key clauses in any investment treaty, as they will determine the scope and application of the treaty. Therefore, states should use their negotiation powers to tailor these definitions to target the kinds of “investments” and “investors” the state wants to attract to enhance its economic development. These definitions are also important for purposes of investor-state claims. Eventually, these definitions will become the cornerstone of jurisdiction for investor-state dispute settlement tribunals. Hence, a state that wants to manage its exposure to investment arbitration will have to be certain of the kinds of investments and investors it is willing to afford treaty protection.

III. NATIONAL TREATMENT

When investors commit large amounts of capital and resources in countries other than their own they are exposed to an array of risks. One of the risks is discriminatory treatment by the host country due to the investor’s foreign nationality. The host government may discriminate against foreign investors through laws, regulations or administrative decrees that favor its national investors. Eliminating the risk of discrimination based on foreign nationality is vital for the encouragement of FDI.

The need to avoid discrimination against foreign investors due to their foreign nationality is the foundation of the national treatment and most-favored-nation standards. While the former protects foreign investors from protectionist measures by the host state that favor its national investors, the latter protects the foreign investor from discrimination that favors investors from other countries. This section will discuss the national treatment standard, and the subsequent section will discuss the most-favored-nation standard.

A. DEFINITION AND EVOLUTION

The national treatment standard first appeared in trade agreements in the twelfth and thirteenth centuries,²⁶⁹ and has become a pillar of international trade law.²⁷⁰ Some commentators have found the national treatment concept to be evolved from the Calvo doctrine,²⁷¹ but the current national treatment clauses found in modern investment treaties have a different purpose than that of the Calvo doctrine.²⁷² In contemporary practice, national treatment connotes that foreign investors are to be given the benefits provided to national investors, and are not to be discriminated against because of their foreign nationality.²⁷³ The current interpretation of national treatment does not confine foreign investors to local remedies as did the Calvo clause.

The universal objective that emerged after WWII of promoting worldwide free flow of capital by liberalizing investment and trade required that FDI occur with the least amount of restrictions.²⁷⁴ To achieve this goal, the national treatment standard was incorporated into modern investment treaties to provide assurance that foreign investors will receive treatment no less favorable than nationals of the host state. Some states granted foreign investors equal

²⁶⁹ “National treatment obligations date back to Hanseatic League treaties of the twelfth and thirteenth centuries.” See Andrea K. Bjorklund, *National Treatment*, in STANDARDS OF INVESTMENT PROTECTION 30-31 (August Reinisch ed. 2008).

²⁷⁰ Together with the Most-Favoured-Nation principle, national treatment is one of the cornerstones of WTO trade law. It is found in all 3 of the main WTO agreements (GATT, GATS and TRIPS).

²⁷¹ Jian Zhou, *National Treatment In Foreign Investment Law: A Comparative Study From a Chinese Perspective*, 10 *TOURO INTERNATIONAL LAW REVIEW* 42, 85 (2000).

²⁷² SCHREUER, 198 (Oxford University Press 2 ed. 2012). In 1868 Calvo argued that foreign investors should not be granted more rights and privileges than those accorded to nationals of the host country. In case of injury, Calvo argued that foreign investors are limited to the remedies available in the domestic legal system of the host country, in equality with national investors who do not have access to international law and international litigation. See in general Christopher K. Dalrymple, *Politics and Foreign Direct Investment: The Multilateral Investment Guarantee Agency and the Calvo Clause*, 29 *CORNELL INTERNATIONAL LAW JOURNAL* 161 (1996).

²⁷³ SCHREUER, 198 (Oxford University Press 2 ed. 2012).

²⁷⁴ SORNARAJAH, 336 (Cambridge University Press 3 ed. 2012).

treatment with national investors on both the pre-entry and post-entry stages,²⁷⁵ while others limited it to the post-entry stage.²⁷⁶ Hence, the national treatment standard became an instrument of economic liberalization and a driver of FDI in developing and developed countries.²⁷⁷

The purpose of the national treatment standard is to provide a level playing field to foreign investors in the host country.²⁷⁸ It ensures that the host state will not make any negative differentiation between foreign and national investors through its laws or administrative actions.²⁷⁹ The host state commits to accord the foreign investor treatment “no less favorable” than the treatment it accords to similarly situated national investors.²⁸⁰ Hence it is a relative standard – one that requires comparison between the treatment received by the foreign investor and the treatment received by national investors operating in similar or identical circumstances.²⁸¹ The protection encompasses *de jure* discrimination, which happens through discriminatory legislation in the host country, and *de facto* discrimination, which happens via facially neutral state measures that are in fact discriminatory.²⁸²

Related to the national treatment standard, but different in focus, is the international minimum standard of treatment. If the treatment accorded to national investors is below the internationally accepted standards, then foreign investors are entitled to treatment that conforms

²⁷⁵ For example the United States and Canada give national treatment protection to foreign investors in the pre-entry and post-entry stages. *See* Article 3 of the U.S. Model Bilateral Investment Treaty (2012). Also *See* Article 3 of the Canada Model Foreign Investment Promotion and Protection Agreement (2004).

²⁷⁶ Most countries follow this approach which allows them to exercise some discrimination based on desired or undesired FDI and consequently admit or exclude incoming investments and/or investors.

²⁷⁷ SORNARAJAH, 336 (Cambridge University Press 3 ed. 2012).

²⁷⁸ *See* SCHREUER, 198 (Oxford University Press 2 ed. 2012).

²⁷⁹ COLLINS, 97 (Cambridge University Press. 2017).

²⁸⁰ *See* SCHREUER, 198 (Oxford University Press 2 ed. 2012).

²⁸¹ Bjorklund, *in* STANDARDS OF INVESTMENT PROTECTION 31 (Reinisch ed. 2008).

²⁸² *Id.* at 30. *See also* CHRISTOPHER DUGAN, 408 (Oxford University Press. 2008).

to the internationally accepted standards.²⁸³ Therefore, customary “international minimum standard” serves as a “floor below which treatment cannot fall, regardless of any relevant relative comparison.”²⁸⁴ Hence foreign investors receive *better* treatment than national investors, because their right to be treated equally with national investors is protected by international law and backed up by the international minimum standard.

The national treatment standard is widely used in modern investment treaties. It has been described as the “most important standard of treatment enshrined in international investment agreements.”²⁸⁵ At the same time, it is the most difficult to achieve, due to interference with public policy and sovereignty considerations of the host country. Some national economic goals and policies, such as the protection of infant industries, might require host countries to discriminate between foreign and national investors.²⁸⁶ Another dimension of the problematic application of the national treatment standard is its overlap with other investment protection standards. For example, the state’s obligation to provide “fair and equitable treatment” encompasses a non-discrimination obligation in some instances.²⁸⁷ Hence, national treatment is hard to achieve, and a few countries therefore choose not to include national treatment obligations in their investment treaties, which allows them more regulatory space with regards to foreign investors and national economic policies.²⁸⁸

²⁸³ Bjorklund, *in* STANDARDS OF INVESTMENT PROTECTION 31 (Reinisch ed. 2008).

²⁸⁴ *Id.* at 31.

²⁸⁵ UNCTAD, National Treatment § IV, at 1 (United Nations 1999).

²⁸⁶ *See* COLLINS, 97 (Cambridge University Press. 2017).

²⁸⁷ Bjorklund, *in* STANDARDS OF INVESTMENT PROTECTION 32 (Reinisch ed. 2008).

²⁸⁸ Indonesia, The Philippines, and Singapore typically do not grant national treatment in their investment treaties. Also earlier Chinese agreements did not include this obligation. *See* COLLINS, 97-98 (Cambridge University Press. 2017).

Nevertheless, most countries offer a national treatment standard either in their investment agreements, national laws, or both.²⁸⁹ Usually the standard itself will be stated in a short paragraph at the beginning of the treaty either as a standalone article or in combination with other treatment standards, such as the MFN clause.²⁹⁰ However, the national treatment standard is usually accompanied by a list of exceptions that enable the host country to exercise discrimination against foreign investors in specific sectors or situations.²⁹¹ For example, the host country might exclude subsidies and government supported loans from the ambit of national treatment to protect and support its fragile national entrepreneurs.²⁹²

B. NATIONAL TREATMENT IN INVESTMENT TREATIES

In investment treaties, contracting parties typically promise national treatment to foreign investors *after* the foreign investment is admitted and established in the host country (post-establishment stage). The post-establishment model of national treatment is the preferred model among developing countries, because it enables them to discriminate against foreign investors in the pre-establishment stage.²⁹³ A typical post-entry national treatment clause would state the following:

Each Party shall accord to a covered investment treatment no less favourable than that it accords, in like circumstances, to investments of its own investors with

²⁸⁹ UNCTAD, National Treatment § IV, at 14 (United Nations 1999).

²⁹⁰ *e.g.*, Article 5 of the Colombia - Turkey BIT (2014).

²⁹¹ *See* SALACUSE, THE LAW OF INVESTMENT TREATIES 274-75 (Oxford University Press 2 ed. 2015).

²⁹² *e.g.*, Article 3(2) of the Japan - Oman BIT (2015). “*The provision of paragraph 1 [national treatment] shall not apply to subsidies including grants, government supported loans, guarantees and insurance.*”

²⁹³ UNCTAD, National Treatment § IV, at 19-21 (United Nations 1999).

respect to the expansion, management, conduct, operation and sale or other disposition of an investment in its area.²⁹⁴

The post-entry model enables the host country to impose higher licensing burdens and requirements on foreign investors, and reserves the host country's right to reject and deny undesired or harmful FDI from entering its territory.²⁹⁵ Some treaties make the application of the national treatment standard conditional even after the entry of the foreign investment on its soil.²⁹⁶ In such treaties, the contracting parties stress that national treatment is subject to "the laws and regulations" of the host country.²⁹⁷ Such language offers the host country the flexibility to enact national laws that discriminate against foreign investors to advance its national interests.²⁹⁸ Even if the treaty does not contain such language, it is agreed under customary international law that "a degree of discrimination in the treatment of aliens as compared with nationals is, generally, permissible."²⁹⁹ However, such discrimination should not go below the international minimum standard of treatment owed to aliens,³⁰⁰ and the host country should be able to provide rational grounds that justify its discrimination.³⁰¹

A few investment agreements, mainly those signed by the United States and Canada, extend national treatment to the pre-establishment stage as well (*i.e.*, before the investment is admitted and established in the host country).³⁰² Under this model, the host country is obliged to provide foreign investors –in the pre-establishment stage- treatment no less favorable than that of

²⁹⁴ Article 4(2) of the Hong Kong - Chile BIT (2016).

²⁹⁵ See COLLINS, 100 (Cambridge University Press. 2017).

²⁹⁶ *e.g.*, India - Indonesia BIT (1999). Article 4(3) states "Each Contracting Party shall, subject to its laws and regulations, accord to investment of investors of the other Contracting Party treatment no less favourable than that which is accorded to investments of its investors."

²⁹⁷ *Id.* at art. 4(3).

²⁹⁸ See SALACUSE, THE LAW OF INVESTMENT TREATIES 276 (Oxford University Press 2 ed. 2015).

²⁹⁹ Peace in OPPENHEIM'S INTERNATIONAL LAW 932 (Robert Jennings & Arthur Watts ed. 1996).

³⁰⁰ See Bjorklund, in STANDARDS OF INVESTMENT PROTECTION 31-32 (Reinisch ed. 2008).

³⁰¹ See COLLINS, 103 (Cambridge University Press. 2017).

³⁰² *e.g.*, Article II(1) of the Jordan - USA BIT (1997).

its own investors in “like circumstances.” Thus the host state grants foreign investors a right of entry into its territory as if they were domestic investors.³⁰³ The United States Model BIT, for example, provides that national treatment shall extend to the “*establishment*, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory.”³⁰⁴

Although countries vary on the issue of extending national treatment to the pre-establishment stage, all countries seem to agree that the national treatment standard, in both models, should be subject to certain exceptions. The need to protect local infant industries in the host country requires a degree of flexibility in the treatment of national investors in specific economic sectors.³⁰⁵ Also, the need to preserve the host country’s ability to disable national treatment when matters of essential interest are affected requires an exception to that end.³⁰⁶ These national interests include public health, morals, environment, national security, and economic and social policies. Hence, most investment treaties accompany the national treatment standard with a list of general and/or specific exceptions that exclude certain types of enterprises, activities or industries from the operation of national treatment.³⁰⁷ These exceptions serve to enhance the economic development of the host country by striking a balance between the interests of the host country and the interests of foreign investors. The host country thereby maintains a degree of flexibility and discretion to nurse its growing local industries and national

³⁰³ COLLINS, 101 (Cambridge University Press. 2017).

³⁰⁴ Article 3(2) of the U.S. Model Bilateral Investment Treaty (2012). [emphasis added].

³⁰⁵ *e.g.*, U.S. - Rwanda BIT (2008). This treaty excludes certain investment activities from the ambit of the national treatment standard. *See* Annex I, II, and III. *See also* UNCTAD, National Treatment § IV, at 2 (United Nations 1999).

³⁰⁶ *e.g.*, NAFTA contains a general national security exception in Article 2102. North American Free Trade Agreement (NAFTA) (1992). *See also* UNCTAD, National Treatment § IV, at 12-13 (United Nations 1999).

³⁰⁷ UNCTAD, National Treatment § IV, at 12 (United Nations 1999).

interests, while simultaneously committing to the basic principle of national treatment to foreign investors.

C. THE APPLICATION OF THE NATIONAL TREATMENT STANDARD

The national treatment standard is a relative, rather than absolute, standard.³⁰⁸ Therefore, the determination of whether the standard is infringed is not dependent on a set of objective criteria. Instead, it depends on a factual analysis of the treatment received by the foreign investor in comparison with a similarly situated local investor.³⁰⁹

Arbitral tribunals have developed a three-step test to rule on the question of national treatment infringement.³¹⁰ First, the arbitral tribunal must determine if the foreign investor is in a comparable setting, or in “like circumstances,” with the alleged more favored domestic investor. Second, it will need to determine whether the treatment accorded to the foreign investor is less favorable than that accorded to the domestic comparator. Finally, the tribunal will have to determine whether the less favorable treatment is justified on rational grounds.³¹¹

³⁰⁸ COLLINS, 105 (Cambridge University Press. 2017).

³⁰⁹ Id. at 105.

³¹⁰ The tribunal in *UPS v Canada* noted the following in this regard “*The Tribunal notes that there are three distinct elements which an investor must establish in order to prove that a Party has acted in a manner inconsistent with its obligations under article 1102. These are:*

- a) *The foreign investor must demonstrate that the Party [Canada] accorded treatment to it [the Claimant or UPS Canada] with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.*
- b) *The foreign investor or investment must be in like circumstances with local investors or investments; and*
- c) *The NAFTA A Party must treat the foreign investor or investment less favorably than it treats the local investors or investments.” See United Parcel Service of America Inc v Government of Canada para. 83 (Award), (ICSID, 2007).*

³¹¹ See SCHREUER, 199 (Oxford University Press 2 ed. 2012).

1. Like circumstances

The infringement of the national treatment standard requires identifying a similarly situated domestic comparator who has received more favorable treatment.³¹² Even when the national treatment clause of an investment treaty does not specifically require “like circumstances,” arbitral tribunals seem to agree that comparison with a national investor who is in a similar position is required.³¹³ However, the determination of what constitutes “like circumstances,” or of the appropriate domestic comparator, is no easy task. Should the foreign investment be in the exact same business as the national comparator to satisfy the “like circumstances” requirement? Or is it sufficient to find a comparator from the same economic sector without being in the same line of business?

In order to preserve the purpose of the national treatment standard, arbitral tribunals have construed the like circumstances requirement in a broad and flexible manner depending on the context and facts of each case.³¹⁴ For example, the tribunal in *Occidental v. Ecuador* stated its view that “in like situations” cannot be interpreted in the narrow sense, “as the purpose of national treatment is to protect investors as compared to local producers, and this cannot be done by addressing exclusively the sector in which that particular activity is undertaken.”³¹⁵ Similarly, the tribunal in *Pope & Talbot v. Canada* opined that:

‘circumstances’ are context dependent and have no unalterable meaning across the spectrum of fact situations. And the concept of ‘like’ can have a range of meanings, from ‘similar’ all the way to ‘identical.’ In other words, the application

³¹² Bjorklund, in *STANDARDS OF INVESTMENT PROTECTION* 38 (Reinisch ed. 2008).

³¹³ *Id.* at 38.

³¹⁴ SCHREUER, 200 (Oxford University Press 2 ed. 2012). *See also* CHRISTOPHER DUGAN, 408 (Oxford University Press. 2008).

³¹⁵ *Occidental Exploration and Production Company v The Republic of Ecuador* para. 173 (Award), (LCIA, 2004).

of the like circumstances standard will require evaluation of the entire fact setting surrounding, in this case, the genesis and application of the Regime.³¹⁶

To achieve the purpose of the standard, which requires equality of competitive conditions, like circumstances should be construed broadly.³¹⁷ However, equality of competitive conditions does not necessarily mean equality in competitive opportunities. The tribunal in *Methanex Corporation v. USA* ruled that if an identical comparator is available, then this is the comparison through which the meaning of like circumstances should be derived.³¹⁸ However, if no identical comparator, or competitor, exists, then the most similar and in equal conditions comparator is used, which might not be a competitor.³¹⁹

Evaluating “like circumstances” should also take into account the overall legal context of the instrument in which the national treatment standard exists.³²⁰ The tribunal in *Pope & Talbot v. Canada* took into consideration the objectives of NAFTA in its assessment of the complained against measure, and pronounced that “[d]ifferences in treatment will presumptively violate Article 1102(2), unless they have a reasonable nexus to rational government policies that (1) do not distinguish, on their face or de facto, between foreign-owned and domestic companies, and (2) do not otherwise unduly undermine the investment liberalizing objectives of NAFTA.”³²¹ The tribunal opined that the liberalizing objectives of NAFTA, to which the parties of the treaty had

³¹⁶ *Pope & Talbot Inc v The Government Of Canada* para. 75 (Award on the Merits of Phase 2), (NAFTA, 2001).

³¹⁷ See COLLINS, 106 (Cambridge University Press. 2017).

³¹⁸ *Methanex Corporation v United States of America*, Part IV, ch. B, 8, para. 17 (NAFTA, 2005).

³¹⁹ The tribunal stated “Given the object of Article 1102 and the flexibility which the provision provides in its adoption of “like circumstances,” it would be as perverse to ignore identical comparators if they were available and to use comparators that were less “like,” as it would be perverse to refuse to find and to apply less “like” comparators when no identical comparators existed. The difficulty which Methanex encounters in this regard is that there are comparators which are identical to it.” *Id.* at Part IV, ch. B, 8, para. 17.

³²⁰ The tribunal in *Myers v Canada* stated “In considering the meaning of “like circumstances” under Article 1102 of the NAFTA, it is similarly necessary to keep in mind the overall legal context in which the phrase appears.” See *S.D. Myers Inc. v Government of Canada* para. 245 (Partial Award), (NAFTA, 2000). See also *Pope & Talbot Inc v The Government Of Canada* paras. 78-79 (Award on the Merits of Phase 2), (NAFTA, 2001).

³²¹ *Pope & Talbot Inc v The Government Of Canada* para. 79 (Award on the Merits of Phase 2), (NAFTA, 2001).

agreed, should be respected by the tribunal and should not be undermined by the national treatment standard.³²²

Assessment of like circumstances should also take into account the exceptions of national policy and essential interests of the host country.³²³ If the measure complained against is justified on rational grounds that serve a public policy goal or protect essential state interests, then national treatment is not infringed. The tribunal in *S.D. Myers v. Canada* stated that the “assessment of ‘like circumstances’ must also take into account circumstances that would justify governmental regulations that treat them differently in order to protect the public interest.”³²⁴ The tribunal in *Pope & Talbot v. Canada* also raised this point by stating that the like circumstances test requires the tribunal to address “any difference in treatment, demanding that it be justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investments.”³²⁵

The national interests’ exception should not be used as a pretext for host governments to discriminate against foreign investors. It is important that the host country has genuine public goals that it wishes to serve from its unequal treatment to avoid liability.³²⁶ The tribunal in *GAMI*

³²² Id. at para. 72 [emphasis added]. See also *S.D. Myers Inc. v Government of Canada* para. 250 (Partial Award), (NAFTA, 2000). “The Tribunal considers that the interpretation of the phrase “like circumstances” in Article 1102 must take into account the general principles that emerge from the legal context of the NAFTA, including both its concern with the environment and the need to avoid trade distortions that are not justified by environmental concerns. The assessment of “like circumstances” must also take into account circumstances that would justify governmental regulations that treat them differently in order to protect the public interest.”

³²³ COLLINS, 103-04 (Cambridge University Press. 2017).

³²⁴ *S.D. Myers Inc. v Government of Canada* para. 250 (Partial Award), (NAFTA, 2000).

³²⁵ *Pope & Talbot Inc v The Government Of Canada* para. 79 (Award on the Merits of Phase 2), (NAFTA, 2001).

³²⁶ e.g., *GAMI Investments, Inc. v The Government of the United Mexican States* para. 114 (Award), (NAFTA, 2004). “The arbitrators are satisfied that a reason exists for the measure which was not itself discriminatory. That measure was plausibly connected with a legitimate goal of policy (ensuring that the sugar industry was in the hands of solvent enterprises) and was applied neither in a discriminatory manner nor as a disguised barrier to equal opportunity.”

Investments v. Mexico,³²⁷ for example, found the measure of expropriating some sugar mills not discriminatory to the foreign investor (GAMI), because the expropriation was “connected with a legitimate goal of policy”³²⁸ and was “applied neither in a discriminatory manner nor as a disguised barrier to equal opportunity.”³²⁹

The “like circumstances” test is a factual and legal question that requires separate examination in each case. Hence, no unified definition or approach can be reached. However, it can be concluded that tribunals need to find an identical comparator, or, if an identical one is not found, at least the most similar comparator. The tribunal should give considerable attention to the state’s right to impose reasonable, non-discriminatory policies that preserve its national interests. Thus the objective of most investment treaties - to enhance economic development - should be balanced with the foreign investor’s right of national treatment. Nonetheless, when the tribunal finds a suitable comparator, the question is then: has the foreign investor received less favorable treatment?

2. Less Favorable Treatment

Discriminatory treatment of foreign investors can happen in two ways: *de jure* or *de facto*. The host country may introduce new laws that *explicitly* discriminate against foreign investors by denying them certain advantages or benefits offered to their domestic counterparts. *De facto* discrimination occurs when the host state introduces measures that are neutral on their face, yet

³²⁷ Id. at .

³²⁸ Id. at para. 114.

³²⁹ Id. at para. 114.

they *effectively* discriminate against foreign investors and their investments.³³⁰ The national treatment protection covers both forms of nationality-based discrimination and provides protection to foreign investors from explicit or implicit discriminatory state measures.

Arbitral tribunals seem to agree that the less favorable treatment test, whether the discrimination is *de jure* or *de facto*, does not require that discriminatory treatment be attributable to the “nationality” of the foreign investor to succeed in a national treatment claim.³³¹ In other words, in order to satisfy the less favorable treatment test, the foreign investor need not prove that the differentiation in treatment is due to his foreign nationality. For example, the tribunal in *Thunderbird v. Mexico* stated that “[i]t is not expected from Thunderbird that it show separately that the less favourable treatment was motivated because of nationality.”³³²

However, eliminating the question of whether the less favorable treatment is attributed to the foreign nationality of the investor renders the national treatment standard redundant and hollow of its purpose. Other investment protection standards, such as the fair and equitable treatment standard, and the protection from arbitrary and unreasonable measures standard, deal with discriminatory treatment not based on nationality. Hence, the foreign investor should have to prove that the differential treatment it received was due to its “foreignness,” by demonstrating the measure was motivated on the basis of nationality. If the claimant fails to prove that the less favorable treatment was motivated by nationality, then national treatment is not breached. This is the position taken by some tribunals. The tribunal in *Noble Ventures v. Romania* considered

³³⁰ See CHRISTOPHER DUGAN, 408 (Oxford University Press, 2008).

³³¹ See SALACUSE, THE LAW OF INVESTMENT TREATIES 277 (Oxford University Press 2 ed. 2015).

³³² International Thunderbird Gaming Corporation v The United Mexican States para. 177 (Award), (NAFTA, 2006). See also Marvin Roy Feldman Karpas v United Mexican States para. 183 (Award), (ICSID, 2002): “*requiring a foreign investor to prove that discrimination is based on his nationality could be an insurmountable burden to the Claimant, as that information may only be available to the government.*”

“nationality based discrimination” to be an important component necessary to a national treatment claim. It stated that discriminatory measures should be “directed specifically against a certain investor by reason of his, her or its nationality.”³³³ The tribunal in *GAMI v. Mexico* took a similar position, although not so clearly. It noted that the expropriation of some national sugar mills for a legitimate public purpose,³³⁴ in which an American investor had a minority share, did not offend the national treatment standard under NAFTA.³³⁵ It reasoned that the expropriation measure by Mexico was not motivated by the foreign nationality of the minority shareholder,³³⁶ thus “[i]t is not conceivable that a Mexican corporation becomes entitled to the anti-discrimination protections of international law by virtue of the sole fact that a foreigner buys a share of it.”³³⁷

Likewise, if domestic and foreign investors alike receive the less favorable treatment, then no differential treatment exists to give way to a national treatment claim. However, the foreign investor in the latter case may avail itself of other protection standards, such as the international minimum standard and the fair and equitable treatment standard.

The foreign nationality of the investor should be the reason behind the less favorable treatment it received in order to sustain a national treatment claim.³³⁸ However, proving “protectionist intent” by the host state is not required. The tribunal in *S.D. Myers v. Canada* correctly stated that “[i]ntent is important, but protectionist intent is not necessarily decisive on

³³³ *Noble Ventures, Inc. v. Romania* para. 180 (Award), (ICSID, 2005).

³³⁴ The purpose was to ensure “that the sugar industry was in the hands of solvent enterprises.” See *GAMI Investments, Inc. v. The Government of the United Mexican States* para. 114 (Award), (NAFTA, 2004).

³³⁵ *Id.* at para. 112.

³³⁶ *Id.* at para. 114.

³³⁷ *Id.* at para. 115.

³³⁸ See also Bjorklund, in *STANDARDS OF INVESTMENT PROTECTION* (Reinisch ed. 2008).

its own.”³³⁹ Proving “intent” is burdensome on the foreign investor, as it requires information that may not be accessible, or may be hard to obtain, in developing countries that lack transparency.³⁴⁰ Requiring proof of intent would effectively limit the national treatment claim to *de jure* violations and would limit the effectiveness of the obligation.³⁴¹ In addition, “[t]he word ‘treatment’ suggests that practical impact is required to produce a breach ... not merely a motive or intent.”³⁴² Therefore, even if protectionist intent is proven, it would not suffice to breach the national treatment standard, unless it was associated with practical discriminatory measures.

Lastly, a foreign investor may not rely on the national treatment standard to escape liability for conducting illegal activities in the host state, even if the foreign investor receives less favorable treatment in the enforcement of the law. In other words, the national treatment standard does not apply in situations where the host country affords the foreign investor less favorable treatment than domestic investors if the investment activities are illicit under the host state’s national law. In *Thunderbird v. Mexico*, Thunderbird operated gambling devices (skill machines) that were prohibited under Mexican law.³⁴³ When Mexico seized Thunderbird facilities with the devices, Thunderbird argued that some domestic facilities were not seized and were still operating, and thus this conduct by the Mexican State was a breach of the national treatment standard under NAFTA. The tribunal, in its findings on this issue, stated:

In any event, even if Thunderbird had established without doubt that Mexico’s line of conduct with respect to gambling operations was not uniform and

³³⁹ S.D. Myers Inc. v Government of Canada para. 254 (Partial Award), (NAFTA, 2000).

³⁴⁰ Marvin Roy Feldman Karpa v United Mexican States para. 183 (Award), (ICSID, 2002).

³⁴¹ Bjorklund, in STANDARDS OF INVESTMENT PROTECTION 49 (Reinisch ed. 2008).

³⁴² S.D. Myers Inc. v Government of Canada para. 254 (Partial Award), (NAFTA, 2000). See also Siemens A.G. v The Argentine Republic para. 321 (Award), (ICSID, 2007): “*intent is not decisive or essential for a finding of discrimination, and that the impact of the measure on the investment would be the determining factor to ascertain whether it had resulted in non-discriminatory treatment.*”

³⁴³ International Thunderbird Gaming Corporation v The United Mexican States para. 171 (Award), (NAFTA, 2006).

consistent, one cannot overlook the fact that gambling is illegal in Mexico. In the Tribunal's view, it would be inappropriate for a NAFTA tribunal to allow a party to rely on Article 1102 of the NAFTA [National Treatment] to vindicate equality of non-enforcement within the sphere of an activity that a Contracting Party deems illicit.³⁴⁴

D. POLICY GUIDELINES FOR NATIONAL TREATMENT

By providing national treatment to foreign investors, a host country is committing itself to not favor its domestic investors to the detriment of foreign investors in similar circumstances. By eliminating the risk of nationality based discrimination through the national treatment standard, FDI is encouraged in the host country. Hence, the national treatment standard has a liberalization effect that increases the developing country's chances of attracting FDI for its development.³⁴⁵

However, the national treatment obligation may present a hurdle to the economic development in the host state. The national treatment obligation can decrease the regulatory space of the host state, impeding its development policy goals. These negative effects can be summarized as follows:

- i) The national treatment standard is a relative standard; the application and breach of this standard is fact specific. Hence, a host country must carefully examine the effects of any measures it wishes to introduce on foreign and domestic investors to determine if the proposed measures result in differential treatment. In addition to taking significant time, this assessment increases the administrative costs and resources required of the host country to determine whether a measure breaches

³⁴⁴ Id. at para. 183.

³⁴⁵ See SORNARAJAH, 336 (Cambridge University Press 3 ed. 2012).

the national treatment obligation. This may also result in the measure not being adopted in due time. The host state's ability to regulate in the public interest becomes limited from fears of breaching the national treatment obligation.

- ii) The national treatment standard requires comparison with domestic investors; however there are no objective criteria that an arbitral tribunal may rely on to find a suitable comparator. Thus, it is important that host countries, when negotiating investment treaties, incorporate objective criteria that help an arbitral tribunal to find an appropriate comparator. This can be achieved by adding the following elements into the text of the national treatment clause in future investment treaties: 1) include the requirement of "like circumstances" to reaffirm and thereby narrow the application of the clause to reasonable situations, and 2) insert objective criteria that determine what constitutes a comparator in "like circumstances." The objective criteria should take into account the economic, social, legal, and developmental impacts of the imposed measures on the foreign and domestic comparator to determine whether the comparator is in "like circumstances." This approach has been adopted in the COMESA Investment Agreement,³⁴⁶ and more recently, in the Morocco – Nigeria BIT.³⁴⁷ This approach ensures that the application of the national treatment obligation takes into account development and other policy goals, as well as investment policy considerations, when determining "like circumstances." The criteria adopted in the COMESA Agreement directs interpreters of the treaty to consider the effects of the state

³⁴⁶ Investment Agreement For the COMESA Common Investment Area (2007).

³⁴⁷ Morocco - Nigeria BIT (2016). Article 6(3).

measures on: (a) third persons and the local community; (b) the local regional or national environment, including the cumulative effects of all investments within a jurisdiction on the environment; (c) the sector the investor is in; (d) the purpose of the measure concerned; (e) the regulatory process generally applied in relation to the measure concerned; and (f) other factors directly relating to the investment or investor in relation to the measure concerned.³⁴⁸

- iii) A pre-establishment national treatment standard gives foreign investors a right of entry to the host state; thus, the host country loses its ability to screen incoming FDI. By committing to pre-establishment national treatment, the host state is in effect surrendering its sovereign powers to deny entry, or impose certain conditions, on foreign investments entering its territory. Thus harmful or unwanted FDI cannot be excluded. Although states usually insert exceptions to the pre-establishment model, which allows them to discriminate in certain sectors, the fact remains that it is difficult to precisely identify all sectors and industries where national treatment should not apply. Therefore, for developing countries seeking development, a pre-establishment clause may be too risky. However, if a developing country wishes to encourage FDI in a specific sector, then it can offer pre-establishment national treatment protection by specifying the sectors that exclusively enjoy national treatment in the pre-establishment stage, a method called the “positive list approach.”³⁴⁹

³⁴⁸ Investment Agreement For the COMESA Common Investment Area (2007). Article 17.

³⁴⁹ A positive list approach is the opposite of the “negative list approach” which requires a state to list the sectors where the national treatment clause does not apply. *See* UNCTAD, National Treatment § IV, at 1 (United Nations 1999).

Electing not to include a national treatment obligation in an investment treaty to avoid its negative effects is not a wise option. Foreign investors will be hesitant to enter a country that explicitly declares its willingness to discriminate against them. Hence, a better option is to include a national treatment clause that offers protection to foreign investors but also reserves the host state's right to regulate and discriminate in certain situations. To conclude on this issue, the following list of guidelines should help developing countries enact more effective national treatment clauses and thus enhance their development:

- i. Offer national treatment in the post-establishment stage of the foreign investment. However, the state may offer pre-establishment protection to certain industries and sectors that it wishes to liberalize and develop in accordance with its development plans by specifying these sectors using a positive list approach;
- ii. Require the foreign investment to be established and operate in accordance with the laws of the host country in order to enjoy national treatment protection;
- iii. Explicitly exclude the economic sectors and industries that do not qualify for national treatment in order to protect and enhance national infant entrepreneurs and natural resources;
- iv. Insert the requirement of "like circumstances" and a list of criteria (such as those adopted in the COMESA Agreement) that clarify and refine what a suitable comparator should be;³⁵⁰
- v. Insert explicit reservations in order to ensure the host state's right to impose legitimate non-discriminatory public purpose measures that have a connection to their purpose;³⁵¹

³⁵⁰ See Article 17 of the Investment Agreement For the COMESA Common Investment Area (2007).

- vi. Insert general reservations that preserve the host country's ability to take measures that may discriminate against foreign investors but will protect the essential interests of the host state in situations of emergency and crisis,
- vii. Qualify or limit the national treatment obligation by inserting a "development exception."³⁵² Under this exception, the host state is entitled to offer its domestic investors certain advantages and benefits that are designed to enhance its national development. Such a clause reflects the principle that developing countries, by virtue of their economic weakness, are entitled to special treatment by the more advanced states.³⁵³ The development clause allows the host state to have policy flexibility while maintaining the commitment to the basic principle of national treatment.³⁵⁴

IV. MOST-FAVORED-NATION TREATMENT (MFN)

When concluding investment agreements, the national treatment standard is the essential standard that a state grants to foreign investors to ensure non-discrimination and equality with

³⁵¹ This is the test adopted in *Pope & Talbot*. The Norwegian Model BIT adopts this test also. It states in footnote 1 "The Parties agree/ are of the understanding that a measure applied by a government in pursuance of legitimate policy objectives of public interest such as the protection of public health, human rights, labour rights, safety and the environment, although having a different effect on an investment or investor of another Party, is not inconsistent with national treatment and most favoured nation treatment when justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investment." Norway Model BIT n.1 (2015). UNCTAD, National Treatment § IV (United Nations 1999).

³⁵² This approach has been adopted in several investment treaties. e.g., the Morocco - Italy BIT (1990) at Article 3(3) states "Investors of the two Contracting Parties shall not be entitled to national treatment in terms of benefiting from aid, grants, loans, insurance and guarantees accorded by the Government of one of the Contracting Parties exclusively to its own nationals or enterprises within the framework of activities carried out under national development programs." See also the Netherlands – Jamaica BIT (1991) at Article 3(6).

³⁵³ UNCTAD, National Treatment § IV, at 47-48 (United Nations 1999).

³⁵⁴ *Id.* at 47.

domestic investors.³⁵⁵ However, countries also want the assurance and confidence that they have secured the “best deal” for their outbound investors; that is treatment as favorable as that offered by the host state to foreign investors from third states. Therefore, an additional guarantee of non-discrimination is added to the investment treaty, namely the Most-Favored-Nation (MFN) standard. Although most investment treaties combine the national treatment standard and the MFN standard together in the same article because of their shared objective of eliminating nationality based discrimination, they are two different standards.

A. DEFINITION AND EVOLUTION

The MFN standard shares with the national treatment standard the objective of eliminating nationality based discrimination. The difference between the two standards lies in the comparator. MFN treatment protects foreign investors from one state from less favorable treatment in comparison with foreign investors from other states (*i.e.*, third states). It is a commitment between state parties of an investment agreement not to provide foreign investors from third states with treatment more favorable than that offered to nationals of one party when investing in the territory of the other.³⁵⁶ Should the host state provide more favorable treatment

³⁵⁵ UNCTAD, Most-Favoured-Nation Treatment § II, at 1 (UNITED NATIONS 2010).

³⁵⁶ See Tony Cole, *The Boundaries of Most Favored Nation Treatment in International Investment Law*, 33 MICHIGAN JOURNAL OF INTERNATIONAL LAW 537, 539 (2012), “An MFN clause in an investment treaty is fundamentally a promise between the two states party to the treaty that neither state will give to investors from any third state more favorable treatment than that given to investors from the other state party to the treaty.”

to investors from third states, it is liable under the MFN clause and is obliged to provide equivalent treatment to home state investors benefiting from the MFN clause.³⁵⁷

The MFN standard has evolved in the context of trade rather than investment.³⁵⁸ It is a basic principle of international law that can be traced back to the Middle Ages, when Imperial grants of customs privileges were given to various cities within the Holy Roman Empire on the basis of favors obtained “by whatsoever other town.”³⁵⁹ The MFN standard, however, started to appear in mutual agreements between states in the twelfth century.³⁶⁰ In the agreement between King Henry V of England and Duke John of Burgundy in 1417 (Treaty for Mercantile Intercourse with Flanders), English vessels were granted the right to use “the harbors of Flanders ‘in the same way as French, Dutch, Sealanders and Scots.’”³⁶¹ MFN also appears in the 1490 treaty between England and Denmark.³⁶²

Although the MFN principle was used early in treaties, the term “MFN” was not coined until the seventeenth century.³⁶³ With the growth of trade and commerce in the eighteenth and nineteenth centuries, the MFN clause became standard in bilateral economic treaties.³⁶⁴

Despite the early and common use of MFN clauses in international economic relations between states, especially in the eighteenth and nineteenth centuries, MFN treatment did not

³⁵⁷ Id. at 539.

³⁵⁸ Id. at 544.

³⁵⁹ Georg Schwarzenberger, *The Most-Favoured-Nation Standard in British State Practice*, 22 BRITISH YEARBOOK OF INTERNATIONAL LAW 96, 97 (1945).

³⁶⁰ OECD, *Most-Favoured-Nation Treatment in International Investment Law* 3 (2004/02 OECD Working Papers on International Investment ed., OECD Publishing 2004).

³⁶¹ MOST-FAVORED-NATION TREATMENT § III, at 12 (UNCTAD ed., United Nations 1999).

³⁶² See Schwarzenberger, 22 BRITISH YEARBOOK OF INTERNATIONAL LAW 96, 97 (1945).

³⁶³ John Kline & Rodney Ludema, *Building a Multilateral Framework For Investment : Comparing the Development of Trade and Investment Accords*, 6 TRANSNATIONAL CORPORATIONS 1, 9 (1998), “The term ‘most favored nation’ appears to have originated with the 1692 treaty between Denmark and the Hanse cities.”

³⁶⁴ See UNCTAD, *Most-Favoured-Nation Treatment* § II, at 9 (UNITED NATIONS 2010). See also Andreas R. Ziegler, *Most-Favoured-Nation (MFN) Treatment*, in STANDARDS OF INVESTMENT TREATMENT 62-63 (August Reinisch ed. 2008).

form part of customary international law.³⁶⁵ To the contrary, it was seen as a higher standard than the international minimum standard required under customary international law.³⁶⁶ Thus, the MFN standard could only apply if the state parties of a bilateral agreement accepted it.³⁶⁷ Therefore, when BITs were concluded to protect investments in the mid-twentieth century, states were keen to include the MFN clause in their treaties.³⁶⁸

The purpose of the MFN clause in modern investment agreements is to create a level playing field among foreign investors from different nationalities in the host state. It ensures equality of treatment and conditions among different foreign investors, which establishes an atmosphere of competitive opportunity among all foreign investors.

The MFN standard shares many of the characteristics of the national treatment standard. This can be attributed to the common objective of these two standards, which is to eliminate nationality based discrimination. The MFN standard is also a relative standard, which requires comparison of the *de facto* or *de jure* treatment received by a foreign investor with the treatment received by another foreign investor of a different nationality in the host state.³⁶⁹ Also similar to national treatment, the comparator must be in “like circumstances,” even if the MFN clause does not explicitly require so.³⁷⁰ The standard does not require identical treatment of all different foreign investors in the host state; rather, it requires “not less favorable” treatment.³⁷¹

The MFN standard has drawn recent attention regarding its scope. While the purpose of the MFN standard is to protect foreign investors from less favorable treatment in comparison

³⁶⁵ Ziegler, *in* STANDARDS OF INVESTMENT TREATMENT 63 (Reinisch ed. 2008).

³⁶⁶ MOST-FAVOURED-NATION TREATMENT § III, at 2 (UNCTAD ed., United Nations 1999).

³⁶⁷ *See* Collins at page 109.

³⁶⁸ The first BIT was the Germany – Pakistan BIT (1959). It included a MFN clause in Article 3(3).

³⁶⁹ *See* SCHREUER, 206 (Oxford University Press 2 ed. 2012).

³⁷⁰ *Id.* at 207.

³⁷¹ COLLINS, 110 (Cambridge University Press. 2017).

with foreign investors from other states, it has been used as a tool to replace the articles of the basic treaty with more favorable treatment standards from other treaties.³⁷² Foreign investors have become able to access benefits granted to other investors in other treaties, often in a manner not intended by the state parties to the basic treaty.³⁷³ This process effectively rewrites the terms of the investment treaty by borrowing more favorable provisions from other investment treaties. The parties to the basic treaty may have intended not to offer foreign investors from certain countries certain benefits based on certain policy reasons. Thus, in this context, the MFN clause becomes a tool to alter the specifically negotiated basic treaty by importing a different protection regime from another treaty.³⁷⁴ This issue will be discussed in further detail below. First, however, the next sub-section will briefly survey the different types and scopes of MFN clauses in modern investment treaties.

B. MFN IN INVESTMENT TREATIES

The MFN standard is found under the treatment section of an investment treaty. It is usually combined with the national treatment article,³⁷⁵ but is sometimes found in a separate article.³⁷⁶

³⁷² The basic treaty is the BIT signed between the foreign investor's home country and the host country. The MFN clause contained in the basic treaty enables the foreign investor to import more favorable provisions from other BITs signed by the host state with other countries (the latter maybe referred to as "the other treaty").

³⁷³ See COLLINS, 110 (Cambridge University Press. 2017).

³⁷⁴ See SCHREUER, 206-07 (Oxford University Press 2 ed. 2012).

³⁷⁵ e.g., the Morocco - Nigeria BIT (2016). Article 6 titled (NATIONAL TREATMENT AND THE MOST FAVOURED NATION PROVISIONS).

³⁷⁶ e.g., the U.S. Model Bilateral Investment Treaty (2012). Article 4.

Some investment treaties offer both national treatment and MFN treatment, while others offer the treatment “more favorable to the investor” between the two treatments.³⁷⁷

The scope of the MFN standard depends on its exact wording in the BIT. Therefore, there is no unified interpretation of MFN clauses in investment treaties; rather, the MFN clause determines the beneficiaries, covered phases of the investment, conditions, exceptions, and any qualifications or clarifications.³⁷⁸ Despite variations among MFN clauses, a typical MFN clause in an investment treaty will read as follows:

Each Contracting Party shall accord to investors of the other Contracting Party and their investments treatment no less favorable than that it accords, in like circumstances, to investors and to investments of investors of any third State with respect to the management, maintenance, use, enjoyment or disposition of investments.³⁷⁹

A treaty may offer MFN protection to foreign investments and investors, or it may limit MFN protection to foreign investments, excluding foreign investors from the ambit of MFN protection. MFN protection may be offered in the pre-establishment and/or the post-establishment phases of investment. Only a few investment treaties provide for pre-establishment MFN treatment;³⁸⁰ the majority of treaties limit MFN treatment to the post-establishment phase. As with the national treatment standard, the reason for this relates to the possibility of

³⁷⁷ e.g., Japan - Iran BIT (2016). Article 4(1) stipulates “*Each Contracting Party shall in its Territory accord to investors of the other Contracting Party and to their investments treatment no less favourable than that it accords in like circumstances to its own investors and their investments or to investors of any non-Contracting party and their investments with respect to investment activities, **whichever is more favourable to the investor.***”

³⁷⁸ UNCTAD, Most-Favoured-Nation Treatment § II, at 38 (UNITED NATIONS 2010).

³⁷⁹ UAE - Mexico BIT (2016). Article 3(2).

³⁸⁰ Such as Article 4 of the U.S. Model Bilateral Investment Treaty (2012). And Article 4 of the Canada Model Foreign Investment Promotion and Protection Agreement (2004).

discriminating against foreign investors from different nationalities before entrance into the host country in accordance with host state's law, national policies, and development objectives.³⁸¹

Similar to the national treatment standard, the MFN standard requires comparison between foreign investors who are in "like circumstances." Some MFN clauses explicitly contain the "like circumstances" condition,³⁸² while others make no reference to it. Arbitral practice has shown that, whatever the wording of the MFN clause, being in "like circumstances" is required to support an MFN claim, even if the underlying treaty does not make reference to such a requirement.³⁸³

Investment treaties regularly subject the MFN clause to certain exceptions that limit its scope and application. These exceptions can be categorized as follows:

- i. Exceptions limiting the scope of MFN treatment in relation to other treaties. MFN cannot be used by the foreign investor to gain the benefits of other treaties, even if those other treaties with the host state provide better treatment for foreign investors from the other country. These exceptions allow the state parties of an investment treaty to preserve special arrangements they made with various countries that with which they have closer economic ties, such as: regional trade agreements, customs unions, and double taxation treaties.³⁸⁴

³⁸¹ The reasons for limiting MFN treatment to the post-establishment phase of the investment are very similar, if not identical, to those reasons of limiting national treatment to post-establishment mentioned above. Therefore, they will not be repeated here.

³⁸² *e.g.*, Article 3(2) of the German Model Treaty (2008). This treaty makes no reference to the 'like circumstances requirement.'

³⁸³ UNCTAD, Most-Favoured-Nation Treatment § II, at 54 (UNITED NATIONS 2010).

³⁸⁴ *e.g.*, Article 3(3) of the German Model Treaty (2008). "*Such treatment shall not relate to privileges which either Contracting State accords to investors of third States on account of its membership of, or association with, a customs or economic union, a common market or a free trade area.*"

- ii. Exceptions limiting the scope of MFN treatment in relation to the treaty itself. The scope of the MFN clause is thus narrowed to the matters and provisions that are not excluded. For example, a treaty may exclude dispute settlement provisions from the ambit of MFN.³⁸⁵ Accordingly, the foreign investor cannot claim MFN to gain the benefit of more favorable dispute settlement options granted to investors from third states. Other treaties designate the articles of the investment treaty where the MFN standard applies.³⁸⁶
- iii. Exceptions limiting the scope of MFN treatment in relation to public policy and security. This allows the host state to take measures related to its public security and order without breaching the MFN standard.³⁸⁷
- iv. Exceptions limiting the scope of MFN treatment in relation to the investment activity. Some treaties exclude certain investment activities from the protection of MFN, which allows the host state to discriminate or provide better treatment to foreign investors operating in those sectors. Some investment activities may be of major importance or touch upon the sovereignty and security of the host state; thus, the state reserves its right to take measures that preserve its vital interests. This can also have a developmental aspect, with the host state wanting to encourage foreign investors from certain countries to operate in the excluded

³⁸⁵ See for example Article 4(3) of the San Marino - Azerbaijan BIT (2015). “*For the avoidance of doubt, the present Article shall... not apply in respect of an investor's rights to submit disputes arising under this Agreement to any dispute settlement procedure.*”

³⁸⁶ e.g., Article 3(3) of the UK Model BIT (2008). “For the avoidance of doubt it is confirmed that the treatment provided for in paragraphs (1) and (2) above shall apply to the provisions of Articles 1 to 12 of this Agreement.”

³⁸⁷ e.g., Article 3(2) of the German Model Treaty (2008). “*Measures that have to be taken for reasons of public security and order shall not be deemed treatment less favourable within the meaning of this Article.*”

investment activities, and thus provide them with more favorable treatment. Such exceptions usually are annexed to the investment treaty and called reservations.³⁸⁸

Another matter related to the scope of investment activities is the right of the state parties of an investment treaty to designate certain measures that are excluded from MFN protection. This allows the host state to impose the designated discriminatory measures without breaching the MFN standard. For example, some treaties exclude restrictions on the procurement of raw or auxiliary materials, or energy and fuels, from MFN protection.³⁸⁹

Although the MFN standard seems, *prima facie*, to be a simple standard of protection, it has generated controversy among scholars and practitioners. The most significant controversy relates to whether the MFN standard extends to procedural rights (in particular dispute settlement procedures in other treaties), or whether it is only limited to substantive rights. The following sub-section considers the application of the MFN standard in arbitral practice, where this controversy originated.

³⁸⁸ *e.g.*, reservations made by the parties of NAFTA.

³⁸⁹ *e.g.*, Article 3(2) of the German Model Treaty (2008). “*The following shall, in particular, be deemed treatment less favourable within the meaning of this Article: 1) different treatment in the event of restrictions on the procurement of raw or auxiliary materials, of energy and fuels, and of all types of means of production and operation; 2) different treatment in the event of impediments to the sale of products at home and abroad; and 3) other measures of similar effect.*”

C. APPLICATION OF THE MFN STANDARD

The MFN standard does not operate to rewrite the terms of the basic treaty by incorporating more favorable terms from other treaties.³⁹⁰ In other words, if the host country provides more favorable treatment to other foreign investors via a treaty or national law, that better treatment is not automatically incorporated into the investment treaty containing the MFN standard. Rather, the MFN standard protects the “treatment” afforded by the host state to the foreign investor by entitling the latter to equivalent treatment.³⁹¹ If the host state fails to provide equivalent treatment to the affected foreign investor, then the foreign investor is entitled to invoke the MFN standard by asserting a claim against the host state. In its claim, the foreign investor may demand monetary compensation for the damages it sustained from the less favorable treatment it received.³⁹² The foreign investor does not (and cannot) demand the withdrawal of the measure affecting it or amendment of the protections and standards of the investment treaty containing the MFN standard.³⁹³

To succeed in an MFN claim, the tribunal must find that: i) the host state has granted foreign investors from other countries more favorable treatment, ii) the host state has failed to

³⁹⁰ Zachary Douglas, *The MFN Clause in Investment Arbitration: Treaty Interpretation Off the Rails*, 2 JOURNAL OF INTERNATIONAL DISPUTE SETTLEMENT 97, 105 (2011).

³⁹¹ “Each treaty defines what it considers a protected investment and who is entitled to that protection, and definitions can change from treaty to treaty. In this situation, resort to the specific text of the MFN Clause is unnecessary because it applies only to the treatment accorded to such defined investment, but not to the definition of ‘investment’ itself.” *Société Générale In respect of DR Energy Holdings Limited and Empresa Distribuidora de Electricidad del Este, S.A. v. The Dominican Republic* para. 41 (Award on Jurisdiction), (UNCITRAL, LCIA, 2008).

³⁹² UNCTAD, *Most-Favoured-Nation Treatment* § II, at 101 (UNITED NATIONS 2010).

³⁹³ See Cole, 33 MICHIGAN JOURNAL OF INTERNATIONAL LAW 537, 569-70 (2012).

provide equivalent treatment to the claimant,³⁹⁴ and, iii) the claimant is in “like circumstances” with the more-favorably treated foreign investors from third states.³⁹⁵ The requirement of “like circumstances” is similar to that under the national treatment standard and therefore will not be discussed here.

The discussion regarding the “more favorable treatment” under a MFN claim can be divided into two parts. The first deals with the application of the MFN clause to more favorable *substantive provisions* of other investment treaties. This part is not controversial.³⁹⁶ The second part of the discussion relates to the application of the MFN standard to the *procedural provisions* of other investment treaties. The second issue has gathered attention and created controversy among tribunals, as will be shown below.

1. Application of the MFN standard to substantive provisions:

The purpose of the MFN standard is to prevent nationality based favoritism by host states. Therefore, if the host state provides foreign investors from third countries with more favorable substantive treatment, then foreign investors, under the basic treaty, are entitled to receive equivalent treatment.³⁹⁷ This aligns with the objective of creating an environment of equal opportunities between different foreign investors in the host state.³⁹⁸

³⁹⁴ See Douglas, *The MFN Clause in Investment Arbitration: Treaty Interpretation Off the Rails*, 2 JOURNAL OF INTERNATIONAL DISPUTE SETTLEMENT 97, 104 (2011).

³⁹⁵ “The essential condition of the violation of a MFN clause is the existence of a different treatment accorded to another foreign investor in a similar situation. Therefore, a comparison is necessary with an investor in like circumstances.” *Parkerings-Compagniet AS v. Lithuania* para. 369 (Award), (ICSID, 2007). See also UNCTAD, *Most-Favoured-Nation Treatment § II*, at 63-66 (UNITED NATIONS 2010).

³⁹⁶ CHRISTOPHER DUGAN, 424 (Oxford University Press. 2008).

³⁹⁷ COLLINS, 110-11 (Cambridge University Press. 2017).

³⁹⁸ Cole, 33 MICHIGAN JOURNAL OF INTERNATIONAL LAW 537, 564 n.40, at 549 (2012).

The determination of whether the host state has, in fact, granted more favorable protection to other foreign investors requires comparison between the two treaties involved (*i.e.*, the basic treaty containing the MFN standard and the third party treaty that provides better treatment). The treaties being compared must deal with the same subject matter; that is, investments and investors. This principle, often referred to as the *Ejusdem Generis* principle,³⁹⁹ requires the third party treaty to regulate the same subject matter as the basic treaty; otherwise, the specific treatment will be taken out of context.⁴⁰⁰ Hence, in an investment claim, the MFN standard cannot be extended to benefits given by the host state to other countries outside the scope of foreign investments. Also, matters that are explicitly excluded from the application of the MFN standard in the basic investment treaty cannot be overridden via claiming breach of MFN if they were not excluded in third party treaties.⁴⁰¹

Some treaty provisions, although substantive in nature, are outside the scope of the MFN standard. Provisions regarding the scope of the treaty (*ratione temporis* and *ratione materiae*) are, generally, not within the domain of the MFN.⁴⁰² Hence, even if the host state offers more favorable treatment to investors from other countries (for example, a wider definition of investors or investments, or a longer temporal scope of the treaty), the MFN standard cannot be invoked in that regard. The tribunal in *Tecmed v. Mexico* stated the following:

Matters relating to the application over time of the Agreement, which involve more the time dimension of application of its substantive provisions rather than matters of procedure or jurisdiction, due to their significance and importance, go to the core of matters that must be deemed to be specifically negotiated by the Contracting Parties. These are determining factors for their acceptance of the

³⁹⁹ See Ziegler, in *STANDARDS OF INVESTMENT TREATMENT* 74-75 (Reinisch ed. 2008).

⁴⁰⁰ *Id.* at 74.

⁴⁰¹ *Id.* at 76.

⁴⁰² Also See *Société Générale In respect of DR Energy Holdings Limited and Empresa Distribuidora de Electricidad del Este, S.A. v. The Dominican Republic* para. 41 (Award on Jurisdiction), (UNCITRAL, LCIA, 2008).

Agreement, as they are directly linked to the identification of the substantive protection regime applicable to the foreign investor and, particularly, to the general (national or international) legal context within which such regime operates, as well as to the access of the foreign investor to the substantive provisions of such regime. Their application cannot therefore be impaired by the principle contained in the most favored nation clause.⁴⁰³

2. Application of the MFN standard to procedural provisions:

Whether the MFN standard extends to procedural provisions of an investment treaty is an issue of controversy -specifically, whether an investor may use MFN rights to claim the benefit of more favorable dispute settlement provisions found in other investment treaties. This controversy began with the 2000 arbitral decision in *Maffezini v. Spain*.⁴⁰⁴ The arbitral tribunal allowed Maffezini to bypass the requirement under the basic treaty,⁴⁰⁵ that investment disputes should be adjudicated in local courts for at least eighteen months before submitting the dispute to arbitration.⁴⁰⁶ Maffezini invoked the MFN clause under the basic treaty, relying on the more favorable dispute resolution clause found in the Chile – Spain BIT.⁴⁰⁷ In its analysis, the tribunal stated that “there are good reasons to conclude that today dispute settlement arrangements are inextricably related to the protection of foreign investors.”⁴⁰⁸ In the tribunal’s view, which was later adopted by other tribunals,⁴⁰⁹ international arbitration is essential to the protection of

⁴⁰³ *Técnicas Medioambientales Tecmed v. United Mexican States*, para. 69 (ICSID, 2003).

⁴⁰⁴ *Emilio Agustín Maffezini v The Kingdom of Spain* (Decision on Jurisdiction), (ICSID, 2000).

⁴⁰⁵ *Argentina - Spain BIT* (1991).

⁴⁰⁶ *Id.* at art. X(3).

⁴⁰⁷ Article 10(2) of the Chile – Spain BIT (1991).

⁴⁰⁸ *Emilio Agustín Maffezini v The Kingdom of Spain* para. 54 (Decision on Jurisdiction), (ICSID, 2000).

⁴⁰⁹ The tribunal in *Gas Natural v Argentina* noted “We remain persuaded that assurance of independent international arbitration is an important – perhaps the most important – element in investor protection. Unless it appears clearly that the state parties to a BIT or the parties to a particular investment agreement settled on a different method for resolution of disputes that may arise, most-favored-nation provisions in BITs should be understood to be applicable to dispute settlement.” *Gas Natural SDG, S.A. v The Argentine Republic* para. 49 (Decision on Jurisdiction), (ICSID, 2005). See also *Siemens A.G. v The Argentine Republic* para. 102 (Decision on

investors' rights and is materially related to the treatment provided by the host state.⁴¹⁰ The *Maffezini* tribunal stated:

From the above considerations it can be concluded that if a third party treaty contains provisions for the settlement of disputes that are more favorable to the protection of the investor's rights and interests than those in the basic treaty, such provisions may be extended to the beneficiary of the most favored nation clause as they are fully compatible with the *ejusdem generis* principle. Of course, the third-party treaty has to relate to the same subject matter as the basic treaty, be it the protection of foreign investments or the promotion of trade, since the dispute settlement provisions will operate in the context of these matters; otherwise there would be a contravention of that principle.⁴¹¹

The MFN standard should not be extended to the procedural matters of an investment treaty for two main reasons. First, the dispute resolution provisions of the investment treaty have a different purpose than its substantive provisions. The substantive provisions are commitments made between the sovereign treaty parties of an investment agreement to provide certain treatment for investments and investors coming from one treaty party to the territory of the other.⁴¹² The dispute resolution provisions, on the other hand, are a mechanism for the beneficiaries of the treaty (*i.e.*, the foreign investors) to enforce those substantive treatment provisions in the event of their breach. Therefore, they cannot be considered as part of the treatment itself.⁴¹³ The second reason is that dispute resolution provisions of an investment treaty relate to the mandate of the adjudicating authority of the tribunal as agreed upon between the

Jurisdiction), (ICSID, 2004). “*the Tribunal finds that the Treaty itself, together with so many other treaties of investment protection, has as a distinctive feature special dispute settlement mechanisms not normally open to investors. Access to these mechanisms is part of the protection offered under the Treaty. It is part of the treatment of foreign investors and investments and of the advantages accessible through a MFN clause.*”

⁴¹⁰ Emilio Agustín Maffezini v The Kingdom of Spain para. 55 (Decision on Jurisdiction), (ICSID, 2000).

⁴¹¹ *Id.* at para. 56.

⁴¹² Douglas, *The MFN Clause in Investment Arbitration: Treaty Interpretation Off the Rails*, 2 JOURNAL OF INTERNATIONAL DISPUTE SETTLEMENT 97, 104 (2011).

⁴¹³ Plama Consortium Limited v Republic of Bulgaria para. 209 (Decision on Jurisdiction), (ICSID, 2005): “*It is one thing to add to the treatment provided in one treaty more favorable treatment provided elsewhere. It is quite another thing to replace a procedure specifically negotiated by parties with an entirely different mechanism.*”

state parties that gave their consent to arbitrate future investment disputes. The foreign investor, being a non-party to the treaty itself, cannot have the power to replace the terms to which the state parties had agreed in order to arbitrate future disputes with foreign investors. One of the fundamental principles of arbitration, whether it be commercial or investment arbitration, is consent. The parties to an investment treaty set the terms they see fit for their consent in the dispute resolution provisions of the investment treaty, and provide foreign investors with a standing offer to submit future disputes to arbitration based on those terms.⁴¹⁴ The investor cannot change those terms by invoking the MFN clause, as the host state has not given its consent to arbitrate disputes with investors from this state based on more favorable provisions imported from other investment treaties.⁴¹⁵

If the state parties of an investment treaty had explicitly, and without doubt, consented to treat the dispute resolution provisions as part of what the MFN standard in their treaty, then the MFN standard can be invoked to borrow more favorable procedural provisions from other treaties.⁴¹⁶ This is the position taken by the tribunal in *Plama v. Bulgaria*:⁴¹⁷

An MFN provision in a basic treaty does not incorporate by reference dispute settlement provisions in whole or in part set forth in another treaty, unless the

⁴¹⁴ *Wintershall Aktiengesellschaft v Argentine Republic* para. 160(3) (Award), (ICSID, 2008): “*In the ICSID system, ‘consent’ of the Host State to international arbitration is given – not generally, but inter alia under a particular investment treaty. The Host-State’s ‘consent’ is given when a bilateral investment treaty is concluded with another State.*”

⁴¹⁵ *Telenor Mobile Communications A.S. v The Republic of Hungary* para. 95 (Award), (ICSID, 2006): “*In the view of this Tribunal its is to interpret the BIT and for that purpose to apply ordinary canons of interpretation, not to displace, by reference to general policy considerations concerning investor protection, the dispute resolution mechanism specifically negotiated by the parties.*”

⁴¹⁶ *Vladimir Berschader and Morse Berschader v The Russian Federation* para. 181 (Award), (SCC, 2006): “*The present Tribunal will apply the principle that an MFN provision in a BIT will only incorporate by reference an arbitration clause from another BIT where the terms of the original BIT clearly and unambiguously so provide or where it can otherwise be clearly inferred that this was the intention of the contracting parties.*”

⁴¹⁷ *Plama Consortium Limited v Republic of Bulgaria* (Decision on Jurisdiction), (ICSID, 2005).

MFN provision in the basic treaty leaves no doubt that the Contracting Parties intended to incorporate them.⁴¹⁸

The extension of the MFN standard to procedural provisions of an investment treaty has serious public policy implications. With that extension, host states will become exposed to international arbitration in a manner that is likely to be wholly unexpected and against their will.⁴¹⁹ Also, foreign investors will get to “cherry pick” from other treaties the procedures that are most suitable to their interests. The tribunal in *Telenor v. Hungary* noted that an expansive reading of MFN clauses will cause uncertainty and unpredictability to the limitations contained in investment agreements,⁴²⁰ and explained the consequences of such expansive reading by stating:

The effect of the wide interpretation of the MFN clause is to expose the host State to treaty-shopping by the investor among an indeterminate number of treaties to find a dispute resolution clause wide enough to cover a dispute that would fall outside the dispute resolution clause in the base treaty, and even then there would be questions as to whether the investor could select those elements of the wider dispute resolution that were apt for its purpose and discard those that were not.⁴²¹

Investment agreements are concluded between sovereign states, where the state parties negotiate the terms and conditions of the treaty in view of their political, economic, and social interests. Consequently, a country may be party to many investment treaties, each of which contains a degree of variation from the others, due to that country’s different interests and objectives with different treaty partners. An interpretation of an MFN clauses as occurred in *Maffezini* disregards the fact that some treaties are concluded as a “package deal,”⁴²² where one of the state parties agrees to include more favorable dispute resolution provisions in the

⁴¹⁸ Id. at para. 223. See also KILIÇ İNŞAAT İTHALAT İHRACAT SANAYİ VE TİCARET ANONİM ŞİRKETİ v TURKMENISTAN para. 7.8.10 (Award), (ICSID, 2013).

⁴¹⁹ COLLINS, 120 (Cambridge University Press, 2017).

⁴²⁰ *Telenor Mobile Communications A.S. v The Republic of Hungary* para. 94 (Award), (ICSID, 2006).

⁴²¹ Id. at para. 93.

⁴²² In this regard See Ziegler, in STANDARDS OF INVESTMENT TREATMENT 83-84 (Reinisch ed. 2008).

investment treaty as a trade-off for other benefits not related to FDI.⁴²³ Hence, the foreign investor should not be entitled to receive the more favorable dispute resolution procedures of the “package deal” treaty.

D. POLICY GUIDELINES FOR MFN

The MFN standard eliminates nationality based discrimination and favoritism between different foreign investors in the host state. Hence, similar to national treatment, the MFN standard helps achieve an environment of equal opportunities between different foreign investors. Indeed, such an environment is essential to encouraging the inflow of foreign investors into the host country. With greater amounts of FDI flowing into the host country, the potential for development is greater too.

However, as illustrated above, the MFN standard can lead to negative consequences for the host state if wrongly applied and interpreted by foreign investors and arbitral tribunals. The MFN standard has various effects on the development agenda of the host state; which can be summarized as follows:

- i) The importation of more favorable dispute resolution procedures from other treaties –thus exposing the host state to international arbitration in an unanticipated manner, beyond what it has consented to in the basic investment treaty.

⁴²³ For example, to receive financial or military aid.

- ii) The possibility of importing treatment standards that do not exist in the basic treaty, or removing exclusions that do not exist in third party treaties - thus allowing foreign investors to benefit from protection standards that were not intended to be enjoyed by foreign investors from a certain country for political, economic, social, or developmental reasons of the host state.
- iii) The possibility of future tribunals to expand the temporal and jurisdictional scope of a treaty through the notion of “more favorable treatment.” Although tribunals have rejected such attempts from foreign investors, it remains a possibility that a future tribunal will erroneously alter the jurisdictional and temporal scopes of the basic treaty via the MFN standard.
- iv) The possibility of burdening the host state by taking account of all treatment offered to foreign investors in new investment treaties. As with the national treatment standard, the MFN is a relative standard that depends on the treatment provided to other foreign investors of different nationalities. Hence, the host state has to exercise caution when concluding other investment agreements and enacting national laws to not offer more favorable treatment to investors from other countries.
- v) The possibility of problems from the vague requirement of a comparator being in “like circumstances.”
- vi) The possibility that the pre-establishment MFN standard gives foreign investors from different nationalities a right of entry to the host state, with the host country losing its ability to screen incoming FDI to determine the nationalities it wishes to

attract in accordance with its development objectives and political and social stances towards other countries.

Given these effects, it is important that states seeking development from FDI carefully draft the MFN clause in their investment treaties. The following are suggested guidelines for drafting more effective, and less risky, MFN clauses in future investment treaties:

- i. For the same reasons mentioned in regard to national treatment, states should limit the scope of MFN protection to post-establishment activities. However, a host state that seeks sectorial development can offer pre-establishment MFN to investments operating in these designated sectors. In the latter scenario, the host state should explicitly state the sectors that benefit from the pre-establishment MFN protection, using a positive list approach.
- ii. States should include the requirement of “like circumstances” and list objective criteria that help identify a suitable comparator. The objective criteria used in the national treatment discussion, above, can also be used in the context of MFN with necessary modifications. The COMESA Agreement adopts this approach.⁴²⁴
- iii. States should explicitly exclude dispute resolution provisions of the investment treaty from MFN protection.⁴²⁵ It is more effective if the MFN clause enumerates the articles that it covers. These articles should be, exclusively, the articles dealing with substantive treatment standards.

⁴²⁴ Investment Agreement For the COMESA Common Investment Area (2007). Article 19(3)

⁴²⁵ *e.g.*, “For greater certainty, notwithstanding any other Bilateral Investment Agreement the Contracting Parties have signed with other States before or after the entry into force of this Agreement, the most favored national treatment shall not apply to procedural or judicial matters.” Article 3(3) of the UAE - Mexico BIT (2016).

- iv. States should explicitly exclude all previous investment treaties with third states from the coverage of the MFN protection to ensure that foreign investors will not try to benefit from more favorable treatment provisions the host state has concluded in the past.
- v. States should explicitly exclude all past and future taxation, regional integration, customs union, free trade area, and similar agreements from the operation of MFN protection.
- vi. States should insert general reservations that preserve the host country's ability to take measures that may discriminate between foreign investors but protect the essential interests of the host state in situations of emergency and crisis.
- vii. States should insert explicit reservations acknowledging the host state's right to impose legitimate non-discriminatory public purpose measures that have a connection with its public policy.⁴²⁶
- viii. States should explicitly exclude the sectors, industries, and non-conforming measures the host state wishes to maintain outside of MFN operation, and reserve a regulatory space to treat foreign investors differently (without discrimination) in accordance with its development objectives and needs.
- ix. States should define "treatment" or "measures" to give certainty and guidance to future tribunals as to what measures are subject to claims of breach under the MFN standard.⁴²⁷

⁴²⁶ The Norwegian Model BIT (2015) adopts this approach. *See* this point in national treatment above.

⁴²⁷ *e.g.*, "The following shall, in particular, be deemed 'treatment less favourable' within the meaning of this Article: unequal treatment in the case of restrictions on the purchase of raw or auxiliary materials, of energy or fuel or of means production or operation of any kind, unequal treatment in the case of impeding the marketing of products

V. FAIR AND EQUITABLE TREATMENT

Although foreign investors may be protected against nationality based discrimination under the national treatment and the MFN standards, this protection does not safeguard against other types of discriminatory and arbitrary measures by the host state. The host state may treat the foreign investor equally with its nationals; however, that treatment may not be internationally acceptable if its treatment of its own nationals falls below certain thresholds. Therefore, states agree to include a general standard of treatment that would ensure that foreign investors received treatment not less than that internationally accepted, *i.e.*, the international minimum standard.⁴²⁸ Including such a standard in an investment treaty ensures that there will be “a residual, but absolute minimum, degree of treaty protection to investments, regardless of possible vagaries in the host party’s national laws and their administration, or of a host party’s lapses with respect to treatment of its own nationals and companies.”⁴²⁹

When the BIT movement started in the 1950’s, this general -or minimum-standard was included. “It appears that the authors of the BITs considered that it was desirable to include a general standard, in addition to the specific rules, which would cover such issues and matters relevant for the desirable extent of protection which did not fall under the specific rules.”⁴³⁰ The language chosen by states to formulate this standard in their BITs was identical to the language

inside or outside the country, as well as any other measures having similar effects. Measures that have to be taken for reasons of public security and order, public health or morality shall not be deemed 'treatment less favourable' within the meaning of this Article.” Article 3(2) of the Egypt - Germany BIT (2005).

⁴²⁸ J.C. Thomas, *Reflections on Article 1105 of NAFTA: History, State Practice and the Influence of Commentators*, 17 ICSID REVIEW 21, 26 (2002).

⁴²⁹ Pamela Gann, *The U.S. Bilateral Investment Treaty Program*, 21 STANFORD JOURNAL OF INTERNATIONAL LAW 373, 373 (1985).

⁴³⁰ Rudolf Dolzer, *Fair and Equitable Treatment: A Key Standard in Investment Treaties*, 39 THE INTERNATIONAL LAWYER 87, 90 (2005).

adopted in the unsuccessful Havana Charter for an International Trade Organization:⁴³¹ fair and equitable treatment.⁴³²

The fair and equitable treatment (FET) standard is now one of the most important protection standards in international investment law.⁴³³ It exists, in different forms, in virtually all investment treaties.⁴³⁴ In essence, the FET standard is a general standard that fills the gaps left by other specific treatment standards in the BIT, such as national treatment or MFN.⁴³⁵ It ensures that foreign investors are not unjustly treated by the host state, and therefore it is a means to guarantee justice to foreign investors.⁴³⁶

The FET standard has drawn much attention and debate in regards to its scope and application.⁴³⁷ In particular, the debate is whether the FET standard is a reflection of the international minimum standard contained in customary international law for the treatment of aliens, or an autonomous standard additional to customary international law.⁴³⁸ Additionally, the undefined nature of what is “fair and equitable” has enabled foreign investors to bring a wide

⁴³¹ Havana Charter for an International Trade Organization (1948). *See also* Kenneth J. Vandeveld, *A Unified Theory of Fair and Equitable Treatment*, 43 INTERNATIONAL LAW AND POLITICS 43, 44 (2010).

⁴³² Article 11(2)(a)(i) of the Charter called for the negotiation of international agreements “to assure just and equitable treatment for the enterprise, skills, capital, arts and technology brought from one Member country to another.” Havana Charter for an International Trade Organization (1948).

⁴³³ The standard of fair and equitable treatment has acquired prominence in investment arbitration as a consequence of the fact that other standards traditionally provided by international law might not in the circumstances of each case be entirely appropriate. PSEG GLOBAL INC. AND KONYA ILGIN ELEKTRIK ÜRETİM VE TICARET LIMITED SIRKETI V Republic of Turkey para. 238 (Award), (ICSID, 2007). “[F]air and equitable treatment is emerging as one of the core concepts governing the relationship between foreign investors and host states in international investment law.” Stephan W. Schill, *Fair and Equitable Treatment under Investment Treaties as an Embodiment of the Rule of Law* Global Administrative Law Series IILJ WORKING PAPER 2006/6, at 2 (2006).

⁴³⁴ SCHREUER, 130 (Oxford University Press 2 ed. 2012).

⁴³⁵ *Id.* at 132.

⁴³⁶ SWISSLION DOO SKOPJE v The Former Yugoslav Republic of Macedonia para. 273 (Award), (ICSID, 2012).

⁴³⁷ “[T]he frequency with which it [FET] is invoked by foreign investors and applied as a basis for state responsibility by arbitral tribunals contrasts with an astonishingly fundamental lack of conceptual understanding about the principle’s normative content.” Schill, *Global Administrative Law Series IILJ WORKING PAPER 2006/6*, at 2 (2006).

⁴³⁸ SCHREUER, 134 (Oxford University Press 2 ed. 2012).

range of governmental measures to be scrutinized by investment arbitration tribunals.⁴³⁹ Therefore, it comes without surprise that the FET standard is now the most invoked standard by foreign investors in investment arbitration, with a high success rate.⁴⁴⁰ This raises the concern that the FET standard may have an overreaching effect on the host country's administrative and governmental action, "to a degree that threatens the policymaking autonomy of that country."⁴⁴¹ Arbitral tribunals have been inconsistent in their interpretation of the FET standard,⁴⁴² which has produced results which are the opposite of the desired certainty and stability for foreign investors.⁴⁴³

A. DEFINITION AND EVOLUTION

The FET standard, contrary to the NT and MFN standards, is an "absolute," "non-contingent" standard.⁴⁴⁴ This means that the treatment afforded to other investors(whether national or foreign) is irrelevant to the question of FET breach.⁴⁴⁵ Rather, the FET standard provides for

⁴³⁹ See Graham Mayeda, *Playing Fair: The Meaning of Fair and Equitable Treatment in Bilateral Investment Treaties*, 41 JOURNAL OF WORLD TRADE 273, 281 (2007).

⁴⁴⁰ UNCTAD, *Fair and Equitable Treatment § II*, at 1 (UNCTAD Series on Issues in International Investment Agreements ed., United Nations 2012).

⁴⁴¹ *Id.* at 1.

⁴⁴² "The contemporary meaning of the FET standard rests on interpretations by individual ad hoc arbitral tribunals with no effective appellate review. This opens the standard to inconsistent interpretations resulting in the uncertainty regarding its meaning." *See id.* at 6. *See also* Fiona Marshall, *Fair and Equitable Treatment in International Investment Agreements 2* (International Institute for Sustainable Development 2007).

⁴⁴³ Marcela Klien Bronfman, *Fair and Equitable Standard: An Evolving Standard*, 10 MAX PLANCK YEARBOOK OF UNITED NATIONS LAW 609, 612 (2006).

⁴⁴⁴ David Gaukrodger, *Addressing the Balance of Interests in Investment Treaties: The Limitation of Fair and Equitable Treatment Provisions to the Minimum Standard of Treatment under Customary International Law 8* (OECD Working Papers on International Investment 2017/03 ed., OECD Publishing 2017).

⁴⁴⁵ Bronfman, 10 MAX PLANCK YEARBOOK OF UNITED NATIONS LAW 609, 622 (2006).

“rulemaking in independent terms, without reference to the treatment of others.”⁴⁴⁶ A breach of other protection standards in the treaty does not automatically entail the breach of the FET standard, or *vice versa*.⁴⁴⁷

The FET standard appeared before the advent of the BIT movement. It can be traced back to multilateral documents, such as the Havana Charter for an International Trade Organization,⁴⁴⁸ and the Economic Agreement of Bogotá.⁴⁴⁹ Although the Havana Charter never came into force, it did influence the treaty practice of the United States, which began to include the FET standard in its FCN treaties.⁴⁵⁰ When the BIT movement started in the 1950s, the FET standard was transferred to BITs. “It appears that the authors of the BITs considered that it was desirable to include a general standard, in addition to the specific rules, which would cover such issues and matters relevant for the desirable extent of protection which did not fall under the specific rules.”⁴⁵¹ The inclusion of the FET standard in BITs has become general practice.

Although the FET standard is common and has existed for over a half century, it has only gained attention in recent years.⁴⁵² The vagueness of the standard, along with controversy regarding its origin and purpose, has not helped arbitral tribunals reach a unified interpretation regarding whether specific state conduct breaches the FET standard.⁴⁵³ This has resulted in

⁴⁴⁶ Herman Walker Jr, *Modern Treaties of Friendship, Commerce and Navigation*, 42 MINNESOTA LAW REVIEW 805, 811 (1958).

⁴⁴⁷ See Schreuer, 133 (Oxford University Press 2 ed. 2012).

⁴⁴⁸ Article 11(2)(i) of the Havana Charter for an International Trade Organization (1948).

⁴⁴⁹ Economic Agreement of Bogota (1948).

⁴⁵⁰ *e.g.*, Article I(1) of the Treaty of Friendship, Commerce, and Navigation between Germany and the United States (1954) reads: "Each Party shall at all times accord fair and equitable treatment to the nationals and companies of the other Party and to their property, enterprises and other interests." See also Article I(1) of the Treaty of Friendship, Commerce, and Navigation, U.S.-Netherlands (1956).

⁴⁵¹ Dolzer, 39 THE INTERNATIONAL LAWYER 87, 90 (2005).

⁴⁵² The first tribunal to apply the FET standard was *Emilio Agustín Maffezini v The Kingdom of Spain* (Award), (ICSID, 2000). Dolzer and Schreuer note that “It is only since 2000 that investment tribunals have started giving content to the meaning of the standard.” See SCHREUER, 130 (Oxford University Press 2 ed. 2012).

⁴⁵³ Schill, *Global Administrative Law Series IILJ WORKING PAPER 2006/6*, at 5 (2006).

“inconsistent decisions in the field of investment protection, possibly lessening the stability and predictability necessary for foreign investment and fostering the fragmentation of international investment law.”⁴⁵⁴

It is widely accepted among arbitral tribunals that the FET standard is an “autonomous” standard (*i.e.*, a standard that has its own meaning).⁴⁵⁵ However, the historical background of the FET standard reveals otherwise. The FET standard was originally introduced as a gap-filling device to protect foreign investors against the many types of situations in which “unfairness may manifest itself, such as, for example, an arbitrary cancellation of licences, harassment of an investor through unjustified fines and penalties or creating other hurdles with a view to disrupting a business.”⁴⁵⁶ It was intended to cover the situations of unfairness that are not covered by more specific treatment standards in the investment treaty, such as NT or MFN.⁴⁵⁷ Therefore, the FET standard was a reflection of the minimum standard of treatment for aliens under customary international law,⁴⁵⁸ which constitutes a “floor below which treatment cannot fall.”⁴⁵⁹ This intention is apparent in the comments added to the FET standard in the OECD Draft Convention on the Protection of Foreign Property in 1967.⁴⁶⁰ The OECD Draft Convention, which represented the position of OECD states at that time, explicitly notes that the

⁴⁵⁴ *Id.* at 9.

⁴⁵⁵ SCHREUER, 133 (Oxford University Press 2 ed. 2012).

⁴⁵⁶ UNCTAD, *Fair and Equitable Treatment* § II, at 6-7 (Agreements ed., United Nations 2012).

⁴⁵⁷ “[T]he FET standard serves to address such acts and occurrences which do not fall into the net of specific standards but nevertheless are deemed to be inconsistent with the object and purpose of the BIT, *i.e.*, to protect and promote foreign investment and thereby to contribute to the economic goals of the host state, as often recognized in BIT preambles.” Rudolf Dolzer, *Fair and Equitable Treatment: Today's Contours*, 12 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 7, 12 (2014).

⁴⁵⁸ See Katia Yannaca-Small, *Fair and Equitable Treatment Standard: Recent Developments*, in STANDARDS OF INVESTMENT PROTECTION 112 (August Reinisch ed. 2008). See also UNCTAD, *Fair and Equitable Treatment* § II, at 6 (Agreements ed., United Nations 2012).

⁴⁵⁹ Bjorklund, in STANDARDS OF INVESTMENT PROTECTION 31 (Reinisch ed. 2008).

⁴⁶⁰ OECD Draft Convention on the Protection of Foreign Property (1967).

FET standard “conforms to the ‘minimum standard’ which forms part of customary international law.”⁴⁶¹

In 1984, the Report of the OECD Committee on International Investment and Multinational Enterprises stated that, “[a]ccording to all Member countries which have commented on this point, fair and equitable treatment introduced a substantive legal standard referring to general principles of international law even if this is not explicitly stated.”⁴⁶²

One commentator, referring to the U.S. model BIT, notes:

Paragraph 4 first states that investments of nationals or companies of one party in the territory of the other party shall be accorded “fair and equitable” treatment. This standard serves as a guiding principle in cases where exact terms of the BIT do not furnish definitive guidance, and it establishes that where more than one interpretation may be given to a treaty provision or applicable statutes, it will be given the interpretation leading to the most fair and equitable result. Further, this standard is meant to supplement the nondiscrimination provisions in paragraphs 1 and 2 by providing a residual, but absolute minimum, degree of treaty protection to investments, regardless of possible vagaries in the host party’s national laws and their administration, or of a host party’s lapses with respect to treatment of its own nationals and companies. *The standard provides, in effect, a “minimum standard” which forms part of customary international law.*⁴⁶³

It is clear that the FET standard was intended to be an expression of the international minimum standard.⁴⁶⁴ It was not intended to be an autonomous standard, having a meaning of its own that is higher than what is required by the international minimum standard under customary international law.⁴⁶⁵ However, as will be discussed below, arbitral tribunals have interpreted this

⁴⁶¹ See notes and comments on paragraph (a) of Article (1) at para 4(a). Available at <https://www.oecd.org/%20investment/internationalinvestmentagreements/39286571.pdf>

⁴⁶² OECD, Committee on International Investment and Multinational Enterprises, Intergovernmental Agreements Relating to Investment in Developing Countries, Doc. No. 84/14, at 12, para. 36 (May 27, 1984).

⁴⁶³ Gann, 21 STANFORD JOURNAL OF INTERNATIONAL LAW 373, 389 (1985) [emphasis added].

⁴⁶⁴ Thomas, 17 ICSID REVIEW 21, 51 (2002).

⁴⁶⁵ “[i]f the historical background is to be taken seriously, then the FET standard when first used, could not have meant anything higher than the [international minimum standard of treatment].” SANTIAGO MONTT, STATE LIABILITY IN INVESTMENT TREATY ARBITRATION: GLOBAL CONSTITUTIONAL AND ADMINISTRATIVE LAW IN THE BIT GENERATION 69 (Hart Publishing, 2009).

standard inconsistently, without regard to its historical background, and have expanded its interpretation in a manner that favors investors.⁴⁶⁶ As a result, host states become restricted when enacting necessary domestic regulations or taking measures that they deem beneficial to their development and needs, fearing breach of FET. However, before discussing the interpretation of the FET standard in the context of investor-state arbitration, it is necessary to discuss the FET standard, and its different variations, in the contemporary BITs which have been the focus of that arbitral process.

B. FET STANDARD IN INVESTMENT TREATIES

The FET standard is included in almost all investment agreements and free trade agreements with investment chapters, in various formulations.⁴⁶⁷ However, in conceptual terms, the formulations of the FET standard in investment treaties can be placed into two main categories. The first is the simple “unqualified” formulation, which provides for no more than the host state’s obligation to provide foreign investors with fair and equitable treatment. This is the common formulation found in most BITs. For example, the Austria – Kyrgyzstan BIT provides an unqualified FET standard in the following terms:

⁴⁶⁶ “[M]any arbitral awards have interpreted the FET concept rather broadly, especially in cases relying on the legitimate expectations of the investor. The result may be an open-ended and unbalanced approach, which unduly favours investor interests and overrides legitimate regulation in the public interest.” UNCTAD, *Fair and Equitable Treatment* § II, at 11 (Agreements ed., United Nations 2012).

⁴⁶⁷ Yannaca-Small, *in* STANDARDS OF INVESTMENT PROTECTION 113 (Reinisch ed. 2008).

Each Contracting Party shall accord to investments by investors of the other Contracting Party fair and equitable treatment and full and constant protection and security.⁴⁶⁸

The unqualified formulation provides minimal guidance to those interpreting the standard. In particular, it raises the question of whether such language can be interpreted in light of customary international law on the treatment of aliens, or whether it provides an autonomous standard that should be interpreted on a case-by-case basis by reference to general notions of fairness and equity.⁴⁶⁹ It must be remembered that the OECD Committee on International Investment and Multinational Enterprises reported that “[a]ccording to all Member countries ... fair and equitable treatment introduced a substantive legal standard referring to general principles of international law even if this is not explicitly stated.”⁴⁷⁰ However, arbitral tribunals interpreting the unqualified FET standard have “delinked [it] from customary international law and focused on the plain meaning of the terms ‘fair’ and ‘equitable.’”⁴⁷¹ The inherent vagueness of the unqualified FET standard opens the door for expansive interpretations, and provides a wide margin of discretion for arbitrators to review the state conduct in question subjectively according to their own understanding of fairness and equity.⁴⁷² It also allows foreign investors to

⁴⁶⁸ Article 3(1) of the Austria – Kyrgyzstan BIT (2016). *See also* Article 5(1) of the Japan – Kazakhstan BIT which states “*Each Contracting Party shall in its Area accord to investments of investors of the other Contracting Party fair and equitable treatment as well as full protection and security.*” Japan – Kazakhstan BIT (2014).

⁴⁶⁹ SCHREUER, 134-39 (Oxford University Press 2 ed. 2012).

⁴⁷⁰ OECD, Committee on International Investment and Multinational Enterprises, Intergovernmental Agreements Relating to Investment in Developing Countries, Doc. No. 84/14, at 12, para. 36 (May 27, 1984).

⁴⁷¹ UNCTAD, Fair and Equitable Treatment § II, at 22 (Agreements ed., United Nations 2012).

⁴⁷² One commentator describes the unqualified FET standard as an example of a “‘fundamental shift in power from States to arbitral tribunals’ whereby ‘substantial rule making power’ has, in effect, been transferred to tribunals whose ‘function is not restricted to applying pre-existing rules and principles to the facts of a case, but extends to developing the existing principles into more precise rules and standards of conduct.’” PATRICK DUMBERRY, THE FAIR AND EQUITABLE TREATMENT STANDARD: A GUIDE TO NAFTA CASE LAW ON ARTICLE 1105, at 128 (Kluwer Law International. 2013) (quoting S. Schill, *The Multilateralization of International Investment Law*, 275(2009)).

bring different state actions for review, even if the state action itself is not originally within the scope of the international minimum standard.⁴⁷³

The second category of formulations is the qualified FET standard. This formulation narrows the application of the FET standard by linking it to international law, or customary international law. A growing number of investment treaties use this formulation.⁴⁷⁴ For instance, the Qatar – Argentine BIT provides that the FET standard should be “interpreted and applied as the treatment provided to aliens in accordance with the principles of customary international law.”⁴⁷⁵ Other treaties provide for a qualified FET standard in the following terms:

Each Party shall accord to a covered investment treatment in accordance with the customary international law minimum standard of treatment of aliens, including fair and equitable treatment and full protection and security.⁴⁷⁶

This formulation provides for FET treatment as part of customary international law. It also reflects the historical background of the inclusion of the FET standard in investment treaties. The qualified FET standard should not be understood to require treatment above, or in addition to, what is required under the minimum standard of treatment for aliens under customary international law. This is the position taken by the NAFTA parties. Under the heading “International Minimum Standard,” NAFTA Article 1105 provides for FET treatment in the following terms:

Each 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.⁴⁷⁷

⁴⁷³ UNCTAD, Fair and Equitable Treatment § II, at 22 (Agreements ed., United Nations 2012).

⁴⁷⁴ *e.g.*, Canada - Mongolia BIT (2016); Morocco - Nigeria BIT (2016); Argentina - Qatar BIT (2016).

⁴⁷⁵ Article 3(4) Argentina - Qatar BIT (2016).

⁴⁷⁶ Article 6(1) Hong Kong - Chile BIT (2016).

⁴⁷⁷ Article 1105(1) of the North American Free Trade Agreement (NAFTA) (1992).

In 2001 the NAFTA parties, after the decision in *Pope and Talbot v. Canada* ruled that the FET standard was “additive” to the international minimum standard,⁴⁷⁸ issued an interpretive note for Article 1105.⁴⁷⁹ The purpose of the note was “to clarify and reaffirm the meaning” of Article 1105.⁴⁸⁰

Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.

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.

A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).⁴⁸¹

Hence, it is apparent that NAFTA parties wanted to reaffirm their understanding of the FET standard as treatment in accordance with customary international law.

The language of NAFTA’s interpretive note found its way into the model BITs of NAFTA parties and other investment agreements.⁴⁸² The U.S. Model BIT, for example, adopts a qualified FET standard similar to that of NAFTA.⁴⁸³ It explicitly states that the FET standard prescribes the customary international law minimum standard of treatment of aliens as the

⁴⁷⁸ *Pope & Talbot Inc v The Government Of Canada* para. 110 (Award on the Merits of Phase 2), (NAFTA, 2001).

⁴⁷⁹ Under Article 1131(2), an interpretation by the Free Trade Commission of a provision of the Agreement “shall be binding on a Tribunal” established under Chapter Eleven. It thus forms part of the governing law of a Chapter Eleven arbitration. *Id.*

⁴⁸⁰ North American Free Trade Agreement, Notes of Interpretation of Certain Chapter 11 Provisions, NAFTA Free Trade Commission, July 31, 2001. Available at http://www.sice.oas.org/tpd/nafta/Commission/CHI1understanding_e.asp

⁴⁸¹ Provision B, *Id.* [emphasis added].

⁴⁸² A growing number of recent investment agreements adopt the language of NAFTA’s interpretive note, such as: the Agreement Establishing the ASEAN-Australia-New Zealand Free Trade Area (2009), the Japan-Philippines FTA (2006), the China-Peru FTA (2009), the Malaysia-New Zealand FTA (2009), the India-Republic of Korea Comprehensive Economic Partnership Agreement (2009) and others.

⁴⁸³ “Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.” Article 5(1) of the U.S. Model Bilateral Investment Treaty (2012).

minimum standard of treatment to be afforded to covered investments.⁴⁸⁴ It adds that the concept of “fair and equitable treatment” does not require treatment in addition to or beyond that which is required by customary international law, and does not create additional substantive rights.⁴⁸⁵ To give further certainty to the substantive contents of the FET standard, the U.S. Model BIT provides that the obligation to provide FET treatment includes “the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world.”⁴⁸⁶

Similarly, and more recently, the (now stalled) Trans Pacific Partnership Agreement (TPPA) adopts a qualified FET standard identical to that of the U.S. Model BIT mentioned above.⁴⁸⁷ This is also the contemporary standard adopted by the European Union. In 2011 the European Parliament issued a resolution regarding the European Union’s investment policy.⁴⁸⁸ The resolution stated that future EU investment treaties should define FET by reference to the level of treatment established by customary international law.⁴⁸⁹

An explicit link between the FET standard and the international minimum standard provides guidance to arbitral tribunals interpreting the standard, and avoids expansive interpretations. By referring to examples of misconduct that infringe FET treatment (*e.g.*, denial of justice) interpreters are able to identify the acts and level of severity required to find a breach of the FET standard. In other words “treaties incorporating a reference to the minimum standard of treatment of aliens under customary law send out a message to arbitrators that the latter cannot

⁴⁸⁴ *Id.* at art. 5(2).

⁴⁸⁵ *Id.* at art. 5(2).

⁴⁸⁶ *Id.* at art. 5(2)(a).

⁴⁸⁷ Article 9.6(2) of the Trans Pacific Partnership Agreement (TPPA) (2016).

⁴⁸⁸ European Parliament resolution of 6 April 2011 on the future European International Investment Policy (2010/2203(INI)).

⁴⁸⁹ *Id.* at para 19.

go beyond what customary international law declares to be the content of the minimum standard of treatment.”⁴⁹⁰ Although the international minimum standard is not clearly defined,⁴⁹¹ nor is there a general consensus on its content,⁴⁹² a qualified FET formulation will nevertheless induce tribunals to apply a higher threshold to determine breach of the standard, as compared with the unqualified FET formulation.⁴⁹³

New trend in investment agreements is thus to use qualified FET provisions. This has come as a response to the expansive interpretations of the FET standard by tribunals in investor-state arbitrations. Linking the FET standard to customary international law is “an important element of governments’ efforts to address the balance between investor protection and the right to regulate.”⁴⁹⁴

⁴⁹⁰ UNCTAD, Fair and Equitable Treatment § II, at 28 (Agreements ed., United Nations 2012).

⁴⁹¹ One commentator defines the international minimum standard, without reference to its substantive content, as follows: “The international minimum standard is a norm of customary international law which governs the treatment of aliens, by providing for a minimum set of principles which States, regardless of their domestic legislation and practices, must respect when dealing with foreign nationals and their property. While the principle of national treatment foresees that aliens can only expect equality of treatment with nationals, the international minimum standard sets a number of basic rights established by international law that States must grant to aliens, independent of the treatment accorded to their own citizens. Violation of this norm engenders the international responsibility of the host State and may open the way for international action on behalf of the injured alien provided that the alien has exhausted local remedies.” Yannaca-Small, in STANDARDS OF INVESTMENT PROTECTION n.18 (Reinisch ed. 2008).

⁴⁹² e.g., The tribunal in *Sempra Energy v Argentina* explained that “[I]nternational law is itself not too clear or precise as concerns the treatment due to foreign citizens, traders and investors. This is the case because the pertinent standards have gradually evolved over the centuries. Customary international law, treaties of friendship, commerce and navigation, and more recently bilateral investment treaties, have all contributed to this development. Not even in the case of rules which appear to have coalesced, such as denial of justice, is there today much certainty.” *Sempra Energy International v Argentine Republic* para. 296 (Award), (ICSID, 2007).

⁴⁹³ UNCTAD, Fair and Equitable Treatment § II, at 29 (Agreements ed., United Nations 2012). See also Yannaca-Small, in STANDARDS OF INVESTMENT PROTECTION 113-14 (Reinisch ed. 2008).

⁴⁹⁴ Gaukrodger, 9 (2017/03 ed., OECD Publishing 2017).

C. THE APPLICATION OF THE FET STANDARD

The application of the FET standard is at the heart of investor-state arbitration issues resulting from BIT interpretation and application. This can be attributed to the vague and open-ended nature of the standard, which allows for the review of a wide range of state activities. Hence, “investment lawyers representing claimants naturally seek to tailor their cases and their arguments so that they will be subsumed under the FET standard.”⁴⁹⁵

Contemporary discussion of the application and interpretation of the FET standard in investment arbitration focuses on two main issues. The first relates to the appropriate threshold of liability for state misconduct. The liability threshold depends on whether the tribunal interprets the FET standard in light of customary international law, which provides for a higher liability threshold, or whether the tribunal interprets the FET standard as an autonomous standard, which provides a lower liability threshold. The second issue concerns the definition and content of the obligation to provide FET in arbitral practice. While arbitral tribunals have attempted to give some substantive content to the obligation to provide FET, they have not been consistent in doing so.⁴⁹⁶

1. Customary International Law and the Threshold of State Liability:

Considerable debate has surrounded the question of whether the FET standard merely reflects the international minimum standard or provides an autonomous standard that is additional to

⁴⁹⁵ Dolzer, *Fair and Equitable Treatment: Today's Contours*, 12 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 7, 10 (2014).

⁴⁹⁶ *Id.* at 10.

customary international law.⁴⁹⁷ The answer to this question is relevant to the appropriate threshold of liability to be applied by tribunals when reviewing state actions alleged to be in breach of the FET standard. This makes crucial the specific wording of the FET standard in the relevant investment treaty. A qualified FET standard, such as that found in NAFTA article 1105, requires interpreters to link FET with customary international law. On the other hand, an unqualified FET standard enables tribunals to apply a broader scope than that required by customary international law.⁴⁹⁸

Customary international law on the treatment of aliens prescribes a high threshold for state liability. It requires a grossly excessive and definite misconduct by the host state towards the foreign investor, in a manner that indicates “a clear injustice evident to any reasonable observer.”⁴⁹⁹ Hence, ordinary errors by the host state do not invoke the liability threshold under customary international law; rather, what is required is something more than mere error - something that is outrageous and invites condemnation.⁵⁰⁰

The threshold of liability for state misconduct under customary international law was laid down in the seminal *Neer* case in 1926.⁵⁰¹ An American citizen was killed by a group of armed men in Mexico. Mexican authorities had been unable to arrest the perpetrators. Thus, the United States lodged a claim with the Mexican–American Claims Commission on behalf of Mr. Neer’s family. The Commission found that the Mexican authorities had acted diligently and that the measures taken by the Mexican authorities in relation to the investigation of the crime did not

⁴⁹⁷ SORNARAJAH, 349 (Cambridge University Press 3 ed. 2012). *See also* SCHREUER, 134-39 (Oxford University Press 2 ed. 2012).

⁴⁹⁸ Yannaca-Small, *in* STANDARDS OF INVESTMENT PROTECTION 114 (Reinisch ed. 2008).

⁴⁹⁹ SORNARAJAH, 346 (Cambridge University Press 3 ed. 2012).

⁵⁰⁰ *Id.* at 346.

⁵⁰¹ *L. F. H. Neer and Pauline Neer (U.S.A.) v United Mexican States*, United Nations Reports of International Arbitral Awards IV 60, (General Claims Commission, 1926).

infringe the international minimum standard of treatment owed to aliens under customary international law.⁵⁰² The American–Mexican Claims Commission reviewing the case stated that a host government would violate the international minimum standard of treatment for aliens only when its actions amounted to “an outrage, to bad faith, to willful neglect of duty, or to an insufficiency of government action so far short of international standards that every reasonable and impartial man would recognize its insufficiency.”⁵⁰³

The *Neer* decision uses negative superlatives to describe the liability threshold for state misconduct. This illustrates the high bar for state liability under customary international law.⁵⁰⁴ Accordingly, if the FET standard is to be interpreted as a reflection of customary international law, a determination of breach of the FET standard would require a high degree of egregious state action. The tribunal in *S.D. Mayers v. Canada* held that a breach of article 1105 of NAFTA (international minimum standard) occurs:

[O]nly when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective. That determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders.⁵⁰⁵

Similarly, the tribunal in *Alex Genin et al. v. Estonia* stated that the FET standard found in the U.S. – Estonia BIT requires “an international minimum standard that is separate from domestic law, but that is, indeed, a minimum standard.”⁵⁰⁶ The tribunal adopted the *Neer* standard for state liability without explicitly referring to the *Neer* case by stating that “[a]cts that would violate this

⁵⁰² Id. at para. 5.

⁵⁰³ Id. at para. 3.

⁵⁰⁴ Kendra Leite, *The Fair And Equitable Treatment Standard: A Search for a Better Balance in International Investment Agreements*, 32 AMERICAN UNIVERSITY INTERNATIONAL LAW REVIEW 373 (2016).

⁵⁰⁵ *S.D. Myers Inc. v Government of Canada* para. 263 (Partial Award), (NAFTA, 2000).

⁵⁰⁶ *Alex Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. The Republic of Estonia* para. 367 (Award), (ICSID, 2006).

minimum standard would include acts showing a willful neglect of duty, an insufficiency of action falling far below international standards, or even subjective bad faith.”⁵⁰⁷

Arbitral tribunals have not been consistent on the appropriate threshold to be applied for state liability under qualified FET standards. While some have accepted the high liability threshold set in the *Neer* case,⁵⁰⁸ others have rejected it on a basis related to the narrow and particular group of situations to which the *Neer* case applies.⁵⁰⁹ Another group of tribunals has taken a middle approach; they have accepted the *Neer* case, but have emphasized the developing nature of customary international law, which requires some flexibility in applying the *Neer* standard depending on the circumstances of each case.⁵¹⁰

NAFTA tribunals are bound by the joint interpretation of Article 1105 of NAFTA issued by the NAFTA parties, which provides that the FET standard does not require anything more than customary international law.⁵¹¹ However, NAFTA tribunals have struggled with the question of what is customary international law today.⁵¹² For example, the tribunal in *ADF Group Inc. v. USA* questioned whether customary international law has evolved over time to go beyond the types of misconduct referred to in the *Neer* case.⁵¹³ It stated that:

What customary international law projects is not a static photograph of the minimum standard of treatment of aliens as it stood in 1927 when the Award in the *Neer* case was rendered. For both customary international law and the

⁵⁰⁷ Id. at para. 367.

⁵⁰⁸ *S.D. Myers Inc. v Government of Canada (Partial Award)*, (NAFTA, 2000). See also *Alex Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. The Republic of Estonia (Award)*, (ICSID, 2006).

⁵⁰⁹ *Mondev International Ltd v United States of America (Award)*, (ICSID Additional Facility, 2002).

⁵¹⁰ *International Thunderbird Gaming Corporation v The United Mexican States (Award)*, (NAFTA, 2006). See also *Glamis Gold, Ltd. v. United States of America (Award)*, (ICSID, 2009).

⁵¹¹ North American Free Trade Agreement, Notes of Interpretation of Certain Chapter 11 Provisions, NAFTA Free Trade Commission, July 31, 2001. Available at http://www.sice.oas.org/tpd/nafta/Commission/CH11understanding_e.asp

⁵¹² UNCTAD, Fair and Equitable Treatment § II, at 48 (Agreements ed., United Nations 2012).

⁵¹³ *Mondev International Ltd v United States of America para. 116 (Award)*, (ICSID Additional Facility, 2002).

minimum standard of treatment of aliens it incorporates, are constantly in a process of development.⁵¹⁴

Other tribunals have expressed the view that the standard laid down in the *Neer* case does not apply to foreign investments, as that case concerned “not the treatment of foreign investment as such but the physical security of the alien.”⁵¹⁵ The tribunal in *Mondev v. USA* was of the opinion that the *Neer* standard was both outdated and had a different purpose (*i.e.*, the physical protection of aliens):

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.⁵¹⁶

Other tribunals have held that the threshold for state liability under customary international law remains high; however, flexibility in application is required to reflect the development of customary international law. This is the stance taken by the tribunal in *Thunderbird v. Mexico*:

The content of the minimum standard should not be rigidly interpreted and it should reflect evolving international customary law. Notwithstanding the evolution of customary law since decisions such as *Neer Claim* in 1926, the threshold for finding a violation of the minimum standard of treatment still remains high, as illustrated by recent international jurisprudence. For the purposes of the present case, the Tribunal views acts that would give rise to a breach of the

⁵¹⁴ *ADF Group Inc. v. United States of America* para. 179 (Award), (ICSID, 2003).

⁵¹⁵ *Mondev International Ltd v United States of America* para. 115 (Award), (ICSID Additional Facility, 2002). The tribunal explained that: “there is insufficient cause for assuming that provisions of bilateral investment treaties, and of NAFTA, while incorporating the *Neer* principle in respect of the duty of protection against acts of private parties affecting the physical security of aliens present on the territory of the State, are confined to the *Neer* standard of outrageous treatment where the issue is the treatment of foreign investment by the State itself.” At para 115.

⁵¹⁶ *Id.* at para. 116.

minimum standard of treatment prescribed by the NAFTA and customary international law as those that, weighed against the given factual context, *amount to a gross denial of justice or manifest arbitrariness falling below acceptable international standards.*⁵¹⁷

In *Glamis Gold Ltd v. United States*, the tribunal maintained that the threshold of liability under customary international law is a high one; however, it noted that the *Neer* standard could be adapted to modern considerations of egregious misconduct that might cover a wider range of actions than would have been included under that standard in 1926:

This is evident in the abundant and continued use of adjective modifiers throughout arbitral awards, evidencing a strict standard. International Thunderbird used the terms “gross denial of justice” and “manifest arbitrariness” to describe the acts that it viewed would breach the minimum standard of treatment. S.D. Myers would find a breach of Article 1105 when an investor was treated “in such an unjust or arbitrary manner.” The Mondev tribunal held: “The test is not whether a particular result is surprising, but whether the shock or surprise occasioned to an impartial tribunal leads, on reflection, to justified concerns as to the judicial propriety of the outcome...”⁵¹⁸

It therefore appears that, although situations may be more varied and complicated today than in the 1920s, the level of scrutiny is the same. The fundamentals of the *Neer* standard thus still apply today: to violate the customary international law minimum standard of treatment codified in Article 1105 of the NAFTA, 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). The Tribunal notes that one aspect of evolution from *Neer* that is generally agreed upon is that bad faith is not required to find a violation of the fair and equitable treatment standard, but its presence is conclusive evidence of such. Thus, an act that is egregious or shocking may also evidence bad faith, but such bad faith is not necessary for the finding of a violation. *The standard for finding a breach of the customary international law minimum standard of treatment therefore remains as stringent as it was under Neer; it is entirely possible, however that, as an international community, we may be shocked by State actions now that did not offend us previously...*⁵¹⁹

⁵¹⁷ International Thunderbird Gaming Corporation v The United Mexican States para. 194 (Award), (NAFTA, 2006) [emphasis added].

⁵¹⁸ *Glamis Gold, Ltd. v. United States of America* para. 614 (Award), (ICSID, 2009).

⁵¹⁹ *Id.* at para. 696 [emphasis added].

Such a breach may be exhibited by a “gross denial of justice or manifest arbitrariness falling below acceptable international standards;” or the creation by the State of objective expectations in order to induce investment and the subsequent repudiation of those expectations.⁵²⁰

Notwithstanding the different interpretations of the qualified FET standard, a qualified FET standard typically establishes a more demanding threshold of liability for state actions. On the other hand, an unqualified FET clause attaches a broad scope to the standard, thus allowing interpreters to apply a low threshold of liability for state misconduct. Unqualified FET clauses have allowed a tribunal to consider the interpretation issued by the NAFTA parties regarding article 1105 and the recent trend in BITs to link the FET standard with customary international law to confirm that “those specific instruments aside, the standard is or might be a broader one,”⁵²¹ and that “the fair and equitable standard may be more precise than its customary international law forefathers.”⁵²² Thus, “the fair and equitable standard. . . can also require a treatment additional to, or beyond that of, customary law.”⁵²³

The tribunal in *Lemire v. Ukraine* noted that the drafting of the unqualified FET standard under the U.S. - Ukraine BIT allowed it to conclude that “actions or omissions of the Parties may qualify as unfair and inequitable, even if they do not amount to an outrage, to willful neglect of duty, egregious insufficiency of State actions, or even in subjective bad faith.”⁵²⁴ Similarly, the tribunal in *Vivendi Universal S.A. v. Argentina* stated that:

Dealing first with Respondent’s argument that the fair and equitable treatment is limited to and to be weighed against the so-called minimum standard of treatment

⁵²⁰ Id. at para. 627. The tribunal in *Merrill & Ring v. Canada* held a similar view, as it stated: “the Tribunal finds that the applicable minimum standard of treatment of investors is found in customary international law and that, except for cases of safety and due process, today’s minimum standard is broader than that defined in the Neer case and its progeny.” *Merrill & Ring Forestry L. P v. The Government of Canada* para. 213 (Award), (ICSID, 2010).

⁵²¹ *Enron Corporation & Ponderosa Assets, L.P v Argentine Republic* para. 258 (Award), (ICSID, 2007).

⁵²² Id. at para. 258.

⁵²³ Id. at para. 258.

⁵²⁴ *Joseph Charles Lemire v. Ukraine* para. 254 (Decision on Jurisdiction and Liability), (ICSID, 2010).

under international law, the Tribunal concludes that there is no basis for such a limitation and that such an interpretation runs counter to the ordinary meaning of the text of Article 3 [unqualified FET standard].⁵²⁵

The inconsistent applications of customary international law make it challenging for states to predict the threshold of liability that will apply to them. In order for states to have the confidence necessary to take measures that achieve their policy and development objectives, they should be allowed a high degree of deference. If a low liability threshold is applied, then any state action that is unfair or inequitable in the eyes of the tribunal may be determined as a breach of the FET standard. At the same time, applying the very high liability standard such as that in the *Neer* case might itself be unfair to foreign investors, as it is almost impossible for states to behave so egregiously. Thus, the most reasonable solution to this dilemma is that adopted in *Thunderbird v. Mexico*, which took into consideration the evolution of customary international law and called for a flexible interpretation in accordance with the facts and circumstances of the case – maintaining, however, that the threshold for state liability remain a high one.⁵²⁶

2. Contents of the FET Standard

Although the FET standard has garnered attention since 2000 as a result of the decision in *Maffezini* case,⁵²⁷ and has been extensively invoked in investor-state arbitrations,⁵²⁸ tribunals have not yet developed a unified understanding of the elements encompassed within the

⁵²⁵ *Compañía de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic* para. 7.4.5 (Award), (ICSID, 2007).

⁵²⁶ *International Thunderbird Gaming Corporation v The United Mexican States* para. 194 (Award), (NAFTA, 2006).

⁵²⁷ *Emilio Agustín Maffezini v The Kingdom of Spain* (Decision on Jurisdiction), (ICSID, 2000).

⁵²⁸ “*The standard of fair and equitable treatment has acquired prominence in investment arbitration as a consequence of the fact that other standards traditionally provided by international law might not in the circumstances of each case be entirely appropriate.*” *PSEG GLOBAL INC. AND KONYA ILGIN ELEKTRIK ÜRETİM VE TICARET LIMITED SIRKETİ V Republic of Turkey* para. 238 (Award), (ICSID, 2007).

obligation to provide FET.⁵²⁹ The Vienna Convention on the Law of Treaties (VCLT),⁵³⁰ requires interpretation “in good faith in accordance with the ordinary meaning to be given to the terms of the treaty.”⁵³¹ The ordinary meaning of the term “fair and equitable” has been determined variously to be “‘just,’ ‘even-handed,’ ‘unbiased,’ ‘legitimate.’”⁵³² The term “treatment” itself is also hard to define;⁵³³ it can encompass a wide range of state activities that include any “act, step or proceeding” taken by the host state.⁵³⁴ It is thus difficult to determine the types of infringements which are possible under the FET standard.⁵³⁵

The FET standard has no consolidated and conventional core meaning that can easily be applied by tribunals and host states.⁵³⁶ It should be interpreted with due regard to the surrounding circumstances of each case.⁵³⁷ It is similar to the principle of good faith found in the codes of civil law jurisdictions, which set out specific rules and then add the good faith principle as an overreaching principle that fills the gaps not covered by the specific rules.⁵³⁸ At its basic level, the FET standard should be understood as a gap filling device that protects foreign investors from unjust actions by the host state that do not fall within the domain of the more specific

⁵²⁹ Schill, Global Administrative Law Series IILJ WORKING PAPER 2006/6, at 5 (2006).

⁵³⁰ Vienna Convention on the Law of Treaties (1969).

⁵³¹ Id. at art. 31.

⁵³² MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile para. 113 (Award), (ICSID, 2004).

⁵³³ Schill, Global Administrative Law Series IILJ WORKING PAPER 2006/6, at 6 (2006).

⁵³⁴ The tribunal in *Saluka v. Czech Republic* stated that the term “measures” covers any action or omission of the host State. It referred to the ICJ’s decision in the *Fisheries Jurisdiction Case (Spain v. Canada)* where the ICJ found that the term is “wide enough to cover any act, step or proceeding.” See *Saluka Investments BV (The Netherlands) v The Czech Republic* para. 459 (Partial Award), (UNCITRAL, 2006).

⁵³⁵ “[I]t is difficult, if not impossible, ‘to anticipate in the abstract the range of possible types of infringements upon the investor’s legal position.’” *Total S.A. v. The Argentine Republic* para. 107 (Decision on Liability), (ICSID, 2010).

⁵³⁶ Schill, Global Administrative Law Series IILJ WORKING PAPER 2006/6, at 5 (2006).

⁵³⁷ *SWISSLION DOO SKOPJE v The Former Yugoslav Republic of Macedonia* para. 273 (Award), (ICSID, 2012).

⁵³⁸ See Dolzer, *Fair and Equitable Treatment: Today’s Contours*, 12 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 7, 12 (2014).

treatment standards.⁵³⁹ The tribunal in *PSEG v. Turkey* explained that “[b]ecause the rule of fair and equitable treatment changes from case to case, it is sometimes not as precise as would be desirable. Yet, it clearly does allow for justice to be done in the absence of more traditional breaches of international standards.”⁵⁴⁰

Arbitral tribunals have admitted that fleshing out the normative contents of the FET standard is a hard task given the vagueness and indeterminacy of the standard. The tribunal in *Total v. Argentina* noted that “this standard is inherently flexible, it is difficult, if not impossible, ‘to anticipate in the abstract the range of possible types of infringements upon the investor’s legal position.’ Its application in a given case must take into account relevant State practice and judicial or arbitral case law as well as the text of the BIT and other sources of customary or general international law.”⁵⁴¹

Arbitral tribunals have nonetheless endeavored to pinpoint “some typical obligations that may be included in the standard, as well as types of conduct that would breach the standard, in order to be guided in their analysis of the issue before them.”⁵⁴² Through a *de facto* doctrine of precedent,⁵⁴³ arbitral awards dealing with the FET standard have played a fundamental role in

⁵³⁹ SWISSLION DOO SKOPJE v The Former Yugoslav Republic of Macedonia para. 273 (Award), (ICSID, 2012).

⁵⁴⁰ PSEG GLOBAL INC. AND KONYA ILGIN ELEKTRIK ÜRETİM VE TICARET LIMITED SIRKETI V Republic of Turkey para. 239 (Award), (ICSID, 2007).

⁵⁴¹ Total S.A. v. The Argentine Republic para. 107 (Decision on Liability), (ICSID, 2010). One commentator notes that the “[f]air and equitable treatment does not have a consolidated and conventional core meaning as such nor is there a definition of the standard that can be applied easily. So far it is only settled that fair and equitable treatment constitutes a standard that is independent from national legal order and is not limited to restricting bad faith conduct of host States. Apart from this very minimal concept, however, its exact normative content is contested, hardly substantiated by State practice, and impossible to narrow down by traditional means of interpretative syllogism.” STEPHAN SCHILL, *THE MULTILATERALIZATION OF INTERNATIONAL INVESTMENT LAW* 263 (Cambridge University Press, 2009).

⁵⁴² Total S.A. v. The Argentine Republic para. 109 (Decision on Liability), (ICSID, 2010).

⁵⁴³ Mara Valenti, *The Protection of General Interests of Host States in the Application of the Fair and Equitable Treatment Standard*, in *CAMBRIDGE INTERNATIONAL TRADE AND ECONOMIC LAW : GENERAL INTERESTS OF HOST STATES IN INTERNATIONAL INVESTMENT LAW* 36 (Giorgio Sacerdoti ed. 2014).

shaping the “constitutive elements” of the standard.⁵⁴⁴ These elements are more specific obligations to which the FET standard is relevant and determinative.

At the outset, one may ask whether the use of two terms, namely “fair” and “equitable,” entail two independent meanings, or obligations, for FET. One of the corollaries of the “general rule of interpretation” in the VCLT is that “interpretation must give meaning and effect to *all the terms* of the treaty.”⁵⁴⁵ If one is to follow this rule, then the two terms “fair” and “equitable” should be given different meanings. If the essential purpose of the FET standard –to be a gap-filling provision that ensures justice-- is to be taken into consideration, then it can be said that “fair” means in accordance with the law, and “equitable” means to take into account the different interests involved, (*i.e.*, the investor’s and host state’s interests) when determining whether a certain state measure is “fair.”⁵⁴⁶ Arbitral tribunals seem not to follow this line of interpretation; rather, they consider “fair and equitable” to represent a single unified standard.⁵⁴⁷

Arbitral tribunals usually follow a “list approach” when articulating the contents of the FET standard, although these lists have not been identical.⁵⁴⁸ The most famous of these lists is from the tribunal in *Tecmed v. Mexico*:

The Arbitral Tribunal considers that this provision of the Agreement, in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations

⁵⁴⁴ COLLINS, 134 (Cambridge University Press. 2017).

⁵⁴⁵ United States - Standards for Reformulated and Conventional Gasoline, WT/DS2/9, at 23 (WTO, 1996). *See also* Article 31 of the Vienna Convention on the Law of Treaties (1969). [emphasis added].

⁵⁴⁶ *See in this regard* Valenti, *in* CAMBRIDGE INTERNATIONAL TRADE AND ECONOMIC LAW : GENERAL INTERESTS OF HOST STATES IN INTERNATIONAL INVESTMENT LAW 34-35 (Sacerdoti ed. 2014).

⁵⁴⁷ SCHREUER, 133 (Oxford University Press 2 ed. 2012).

⁵⁴⁸ Dolzer, *Fair and Equitable Treatment: Today's Contours*, 12 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 7, 14 (2014).

that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permit issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities. The investor also expects the State to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation.⁵⁴⁹

The *Tecmed* list of FET elements has been criticized for being pro-investor;⁵⁵⁰ but it contains all the elements that are now firmly rooted in the FET standard. At the risk of oversimplifying, at its basic level, the FET standard protects foreign investors from arbitrariness and discrimination, as well as from substantive and procedural denial of justice, and provides for a stable and transparent legal framework governing investment in the host state - in particular, the protection of the investor's legitimate expectations.⁵⁵¹ There is a common thread among arbitral tribunals not to include bad faith or malicious intent as a necessary element for the breach of FET.⁵⁵²

⁵⁴⁹ *Técnicas Medioambientales Tecmed v. United Mexican States*, para. 154 (ICSID, 2003).

⁵⁵⁰ Valenti, in *CAMBRIDGE INTERNATIONAL TRADE AND ECONOMIC LAW : GENERAL INTERESTS OF HOST STATES IN INTERNATIONAL INVESTMENT LAW* 39 (Sacerdoti ed. 2014).

⁵⁵¹ See generally Yannaca-Small, in *STANDARDS OF INVESTMENT PROTECTION* (Reinisch ed. 2008). See also UNCTAD, *Fair and Equitable Treatment § II*, at 1 (Agreements ed., United Nations 2012), "The standard protects investors against serious instances of arbitrary, discriminatory or abusive conduct by the host state."

Schill's account of FET content is: "(1) the requirement of stability, predictability and consistency of the legal framework, (2) the principle of legality, (3) the protection of investor confidence or legitimate expectations, (4) procedural due process and denial of justice, (5) substantive due process or protection against discrimination and arbitrariness, (6) the requirement of transparency and (7) the requirement of reasonableness and proportionality." Schill, *Global Administrative Law Series IILJ WORKING PAPER 2006/6*, at 11 (2006). See also Prof. Dolzer's list: "good faith in the conduct of a party, consistency of conduct, transparency of rules, recognition of the scope and purpose of laws, due process, prohibition of harassment, a reasonable degree of stability and predictability of the legal system, and, in particular, recognition of the legitimate expectation on the part of the investor . . . arbitrariness and discrimination also fall under the heading of FET." Dolzer, *Fair and Equitable Treatment: Today's Contours*, 12 *SANTA CLARA JOURNAL OF INTERNATIONAL LAW* 7, 15 (2014).

⁵⁵² "[T]here is a common thread in the recent awards under NAFTA and *Tecmed* which does not require bad faith or malicious intention of the recipient State as a necessary element in the failure to treat investment fairly and equitably. As recently stated in *CMS*, it is an objective standard 'unrelated to whether the Respondent has had any deliberate intention or bad faith in adopting the measures in question. Of course, such intention and bad faith can

The protection of investors' legitimate expectations is closely related, and considered part of, the obligation to provide a stable legal framework governing the foreign investment.⁵⁵³ Arbitral tribunals have noted that the protection of the legitimate expectations of the investor is "the most important function" of the FET standard.⁵⁵⁴ The justification is that the foreign investor relies on the regulatory, contractual, and/or informal representations offered by the host state when making its investment decision.⁵⁵⁵ A unilateral change by the host state in these interests may cause harm to the investment project. The tribunal in *Thunderbird v. Mexico* provided a definition of the concept of "legitimate expectations:"

[T]he concept of 'legitimate expectations' relates, ... 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 honour those expectations could cause the investor (or investment) to suffer damages.⁵⁵⁶

Arbitral tribunals have identified three main situations where an investor's legitimate expectations may arise, and consequently be protected, under the obligation to provide FET. These situations are i) expectations arising from contractual obligations between the foreign investor and the host country, ii) expectations arising from the regulatory framework of the host

aggravate the situation but are not an essential element of the standard." *Azurix Corp. v The Argentine Republic* para. 372 (Final Award), (ICSID, 2006). See also Yannaca-Small, in *STANDARDS OF INVESTMENT PROTECTION* 122 (Reinisch ed. 2008).

⁵⁵³ "The protection of the 'expectations that were taken into account by the foreign investor to make the investment' has likewise been identified as a facet of the standard." *Enron Corporation & Ponderosa Assets, L.P v Argentine Republic* para. 262 (Award), (ICSID, 2007).

⁵⁵⁴ *ELECTRABEL S.A. v. The Republic of Hungary* (Decision on Jurisdiction, Applicable Law and Liability), para. 7.75 (ICSID, 2012). Other tribunals have referred to the stability of the legal framework and the protection of legitimate expectation as "essential elements" of the FET standard. See *Occidental Exploration and Production Company v The Republic of Ecuador* para. 183 (Award), (LCIA, 2004).

⁵⁵⁵ Dolzer, *Fair and Equitable Treatment: Today's Contours*, 12 *SANTA CLARA JOURNAL OF INTERNATIONAL LAW* 7, 17 (2014).

⁵⁵⁶ *International Thunderbird Gaming Corporation v The United Mexican States* para. 147 (Award), (NAFTA, 2006).

state, and iii) expectations arising from informal representations made by host state officials to the foreign investor.

a. Contractual Obligations: The first relates to the unilateral modification of contractual undertakings by host governments.⁵⁵⁷ Contracts between the host state and the foreign investor generate “legal rights and therefore expectations of compliance.”⁵⁵⁸ However, arbitral tribunals have stressed that mere contractual obligations do not rise to the level of protection under the concept of legitimate expectations.⁵⁵⁹ Rather “[in] order that the alleged breach of contract may constitute a violation of the BIT, it must be the result of behaviour going beyond that which an ordinary contracting party could adopt. Only the state in the exercise of its sovereign authority (*‘puissance publique’*), and not as a contracting party, may breach the obligations assumed under the BIT.”⁵⁶⁰

b. Regulatory Framework The second situation relates to the change of the general regulatory framework governing the investment.⁵⁶¹ The legal framework governing the investment creates

⁵⁵⁷ “*Legitimate expectations may follow from explicit or implicit representations made by the host state, or from its contractual commitments.*” *Toto Costruzioni Generali S.P.A. v. Republic Of Lebanon* para. 159 (Award), (ICSID, 2012).

⁵⁵⁸ *Continental Casualty Company v. The Argentine Republic* para. 261 (Award), (ICSID, 2008).

⁵⁵⁹ “*It is evident that not every hope amounts to an expectation under international law. The expectation a party to an agreement may have of the regular fulfilment of the obligation by the other party is not necessarily an expectation protected by international law. In other words, contracts involve intrinsic expectations from each party that do not amount to expectations as understood in international law. Indeed, the party whose contractual expectations are frustrated should, under specific conditions, seek redress before a national tribunal.*” *Parkerings-Compagniet AS v. Lithuania* para. 344 (Award), (ICSID, 2007).

⁵⁶⁰ *Impregilo S.p.A. v. Islamic Republic of Pakistan* para. 260 (Decision on Jurisdiction), (ICSID, 2005).

⁵⁶¹ In *Bayindir v. Pakistan*, the tribunal held that FET treatment comprises “*the obligation to refrain ... from frustrating the investor’s reasonable expectations with respect to the legal framework affecting the investment.*” *Bayindir Insaat Turizm Ticaret Ve Sanayi A.Ş. v. Islamic Republic of Pakistan* para. 178 (Award), (ICSID, 2009).

an expectation of the foreign investor regarding its stability and predictability,⁵⁶² which affects the investment decision and the profitability of the investment project. As such, tribunals have acknowledged that “there is certainly an obligation not to alter the legal and business environment in which the investment has been made,”⁵⁶³ and therefore a host state should not “unreasonably modify the legal framework or modify it in contradiction with a specific commitment.”⁵⁶⁴

There is consensus among tribunals that the expectations of the foreign investor that can be relied upon are those that arise when the foreign investor enters the host state. In other words, the foreign investor must take the local law as it stands at the time of making the investment.⁵⁶⁵ Another requirement is that the foreign investor should have derived its expectations from the local laws and acted in reliance upon those laws and regulations.⁵⁶⁶ The expectations should be “reasonable” or “legitimate,” and therefore should not arise solely out of the investor’s subjective postulates.⁵⁶⁷ The protection of legitimate expectations cannot be assessed from the investor’s point of view, but rather must be balanced with the views of the host state. As explained by the tribunal in *Toto v. Lebanon*, “legitimate expectations are more than the investor’s subjective expectations. Their recognition is the result of a balancing operation of the different interests at

⁵⁶² “An investor’s decision to make an investment is based on an assessment of the state of the law and the totality of the business environment at the time of the investment as well as on the investor’s expectation that the conduct of the host State subsequent to the investment will be fair and equitable.” *Saluka Investments BV (The Netherlands) v The Czech Republic* para. 301 (Partial Award), (UNCITRAL, 2006).

⁵⁶³ *Occidental Exploration and Production Company v The Republic of Ecuador* para. 191 (Award), (LCIA, 2004).

⁵⁶⁴ *El Paso Energy International Company v. The Argentine Republic* para. 364 (Award), (ICSID, 2011).

⁵⁶⁵ Michele Potesta, *Legitimate Expectations in Investment Treaty Law: Understanding the Roots and the Limits of a Controversial Concept*, 28 ICSID REVIEW 88, 110 (2013).

⁵⁶⁶ *Suez, Sociedad General de Aguas de Barcelona S.A., and Vivendi Universal S.A. v The Argentine Republic* para. 226 (Decision on Liability), (ICSID, 2010).

⁵⁶⁷ Dolzer, *Fair and Equitable Treatment: Today’s Contours*, 12 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 7, 16 (2014).

stake, taking into account all circumstances, including the political and socioeconomic conditions prevailing in the host State.”⁵⁶⁸

The legitimate expectations of the foreign investor should be assessed in light of the host state’s circumstances and its sovereign right to regulate. Protection of an investor’s legitimate expectations should not imply that the legal framework governing the investment should be “frozen” as a result of this protection under the FET obligation. It is unreasonable to expect that the circumstances prevailing at the time the investment was made are to remain totally unchanged.⁵⁶⁹ In fact, a state has the obligation and responsibility to “amend their legislation in order to adapt it to change and the emerging needs and requests of their people in the normal exercise of their prerogatives and duties.”⁵⁷⁰ The issue regarding the host state’s right to regulate and the protection of investors’ expectations relating to the stability of the legal framework governing the investment is at the center of the debate surrounding the FET standard.⁵⁷¹ A recent OECD publication notes that “[the] FET provision, for example, is at the core of the right to regulate debate. A number of other provisions, such as those governing national treatment, most-favoured nation, indirect expropriation or capital flows are also important, but an initial focus on FET is warranted by its prominence.”⁵⁷²

⁵⁶⁸ *Toto Costruzioni Generali S.P.A. v. Republic Of Lebanon* para. 165 (Award), (ICSID, 2012). “*The assessment of the reasonableness or legitimacy must take into account all circumstances, including not only the facts surrounding the investment, but also the political, socioeconomic, cultural and historical conditions prevailing in the host State.*” *Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador* para. 340 (Award), (ICSID, 2008). Similarly, the tribunal in *Saluka* noted: “*In order to determine whether frustration of the foreign investor’s expectations was justified and reasonable, the host State’s legitimate right subsequently to regulate domestic matters in the public interest must be taken into consideration as well.*” *Saluka Investments BV (The Netherlands) v The Czech Republic* para. 305 (Partial Award), (UNCITRAL, 2006).

⁵⁶⁹ *Saluka Investments BV (The Netherlands) v The Czech Republic* para. 305 (Partial Award), (UNCITRAL, 2006).

⁵⁷⁰ *Total S.A. v. The Argentine Republic* para. 115 (Decision on Liability), (ICSID, 2010).

⁵⁷¹ David Gaukrodger, *The Balance Between Investor Protection and the Right to Regulate in Investment Treaties: A scoping paper 4* (OECD Working Papers on International Investment ed., 2017).

⁵⁷² *Id.* at 17.

Accordingly, some arbitral tribunals have been cautious with the scope of protection provided under the legitimate expectations elements of the FET standard. These tribunals have declared that unless the host state provides “specific commitments” to the foreign investor not to change its local laws (*e.g.*, through a stabilization clause), the host state shall have the right and privilege to exercise its sovereign regulatory powers freely.⁵⁷³ The tribunal in *Parkerings v.*

Lithuania stated:

A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a stabilisation clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment... In principle, an investor has a right to a certain stability and predictability of the legal environment of the investment. The investor will have a right of protection of its legitimate expectations provided it exercised due diligence and that its legitimate expectations were reasonable in light of the circumstances. Consequently, an investor must anticipate that the circumstances could change, and thus structure its investment in order to adapt it to the potential changes of legal environment.⁵⁷⁴

The obligation to provide a stable regulatory framework for the investment, and the protection of the investor’s legitimate expectations inherent in it, should not –unless a specific commitment in this regard has been made by the host country- preclude a host state from enacting and modifying its local laws in pursuit of its interests. What is protected, under this element of FET, is the *inequitable, unfair, arbitrary or discriminatory* modification of local laws that were relied upon by the investor to make the investment, causing him to suffer damages from this modification.⁵⁷⁵ The *Toto v. Lebanon* the tribunal explained that “[i]n the absence of a stabilisation clause or similar commitment, which were not granted in the present case, changes

⁵⁷³ Joseph Charles Lemire v. Ukraine para. 267 (Decision on Jurisdiction and Liability), (ICSID, 2010). See also Parkerings-Compagniet AS v. Lithuania para. 332 (Award), (ICSID, 2007).

⁵⁷⁴ Parkerings-Compagniet AS v. Lithuania paras. 332-33 (Award), (ICSID, 2007).

⁵⁷⁵ UNCTAD, Fair and Equitable Treatment § II, at 31 (Agreements ed., United Nations 2012).

in the regulatory framework would be considered as breaches of the duty to grant full protection and fair and equitable treatment *only in case of a drastic or discriminatory change* in the essential features of the transaction.”⁵⁷⁶ Similarly, in *Impregilo S.p.A. v. Argentina* the tribunal noted that “[t]he legitimate expectations of foreign investors cannot be that the State will never modify the legal framework, especially in times of crisis, but certainly investors must be protected from *unreasonable* modifications of that legal framework.”⁵⁷⁷

It appears that the FET standard, and in particular the protection of legitimate expectations, can be applied in a balanced manner that preserves the interests of the host state and the investor. However, a clear system of precedent does not exist in international investment law. Thus it is more than possible that other tribunals will not interpret the standard conservatively, as in the cases mentioned above. It would be safer for a state to modify the traditional language of the FET standard found in typical BITs, in order to avoid a broad interpretation. This issue will be addressed in the next section.

c. Informal Representations The third situation where legitimate expectations of investors may arise is when informal representations are made by host state authorities to the foreign investor. The host state may make certain unilateral promises or representations to the foreign investor, which the investor then relies on at the time of making its investment, expecting their fulfillment. The frustration of the expectation that the host state will fulfill its promises and representations may cause the investor to suffer damages.⁵⁷⁸ The tribunal in *Waste Management v. United Mexican States* stated that when applying the FET standard “it is relevant that the treatment is in

⁵⁷⁶ *Toto Costruzioni Generali S.P.A. v. Republic Of Lebanon* para. 244 (Award), (ICSID, 2012) [emphasis added].

⁵⁷⁷ *Impregilo S.p.A. v. Argentine Republic* para. 291 (Award), (ICSID, 2011) [emphasis added].

⁵⁷⁸ Potesta, 28 ICSID REVIEW 88, 103 (2013).

breach of representations made by the host State which were reasonably relied on by the claimant.”⁵⁷⁹

In order to create legitimate expectations protected under the FET standard, the host state’s informal representations should be both specific and relied upon by the investor when making the investment in the host state. The tribunal in *Glamis Gold v. United States of America* explained that “[a] State may be tied to the objective expectations that it creates in order to induce investment. Actionable reliance on such expectations thus require something greater than mere disappointment; it requires, as a threshold condition, the active inducement of a quasi-contractual expectation.”⁵⁸⁰ The tribunal in *PSEG v. Turkey* noted that “[l]egitimate expectations by definition require a promise of the administration on which the Claimants rely to assert a right that needs to be observed.”⁵⁸¹ As for the specificity of the representations, the tribunal in *Continental Casualty* stated:

[In] order to evaluate the relevance of [the ‘reasonable legitimate expectations’ concept] applied within Fair and Equitable Treatment standard and whether a breach has occurred, relevant factors include:

i) the specificity of the undertaking allegedly relied upon which is mostly absent here, considering moreover that political statements have the least legal value, regrettably but notoriously so.⁵⁸²

The three situations where legitimate expectations of the foreign investor may arise (contractual commitments, the legal framework governing the investment, and informal

⁵⁷⁹ *Waste Management, Inc. v. United Mexican States* para. 98 (“Number 2”) (Award), (ICSID, 2004).

⁵⁸⁰ *Glamis Gold, Ltd. v. United States of America* para. 799 (Award), (ICSID, 2009). The tribunal in *Parkerings v. Lithuania* similarly noted that “[An] expectation is legitimate if the investor received an explicit promise or guaranty from the host-State, or if implicitly, the host-State made assurances or representation that the investor took into account in making the investment.” *Parkerings-Compagniet AS v. Lithuania* para. 331 (Award), (ICSID, 2007).

⁵⁸¹ *PSEG GLOBAL INC. AND KONYA ILGIN ELEKTRIK ÜRETİM VE TICARET LIMITED SİRKETİ V Republic of Turkey* para. 241 (Award), (ICSID, 2007).

⁵⁸² *Continental Casualty Company v. The Argentine Republic* para. 261 (Award), (ICSID, 2008).

representations) are heavily discussed in literature and case law.⁵⁸³ However, the tribunal in *Electrabel v. Hungary* gave a good summary of the FET standard and the previous case law relating to its application.⁵⁸⁴ The tribunal asserted the obligation to protect the investor's legitimate expectations, but also emphasized the need to balance between the investors' interests and the host states' interests when reviewing alleged breaches of the FET standard:

7.74 The Tribunal shares the well-established scholarly opinions (e.g. Dolzer and Schreuer, pp. 133-147); and decisions cited by *Electrabel* (Bayindir, paragraph 178 and footnotes therein; *Waguih Elie George Siag and Clorinda Vecchi v Egypt*, paragraph 150) that *the obligation to provide fair and equitable treatment comprises several elements, including an obligation to act transparently and with due process; and to refrain from taking arbitrary or discriminatory measures or from frustrating the investor's reasonable expectations with respect to the legal framework adversely affecting its investment.*

7.75 *It is widely accepted that the most important function of the fair and equitable treatment standard is the protection of the investor's reasonable and legitimate expectations.* Hungary submits that this standard is not an absolute guarantee that shields investors from all regulatory change. *Electrabel*, for its part, does not contest Hungary's right to regulate *Dunamenti*, but maintains that investors may legitimately expect that any changes are made in a fair, equitable and transparent manner.

7.76 As regards *the relevant point in time for the assessment of legitimate and reasonable expectations, it is common ground in 'investment jurisprudence' and between the Parties that the assessment must refer to the time at which the investment is made, and that expectations must be based on more than subjective beliefs* (Reply, paragraph 116; Counter-Memorial, paragraphs 427-428). However, while Hungary asserts that legitimate expectations must be based on affirmative governmental representations, *Electrabel* argues that the investor's expectation that its contractual rights will not be affected by governmental

⁵⁸³ For further discussion regarding the content of FET in arbitral practice See Dolzer, *Fair and Equitable Treatment: Today's Contours*, 12 SANTA CLARA JOURNAL OF INTERNATIONAL LAW 7 (2014); Dolzer, *Fair and Equitable Treatment: A Key Standard in Investment Treaties*, 39 THE INTERNATIONAL LAWYER 87 (2005); Schill, *Global Administrative Law Series IILJ WORKING PAPER 2006/6* (2006); Yannaca-Small, in STANDARDS OF INVESTMENT PROTECTION (Reinisch ed. 2008); UNCTAD, *Fair and Equitable Treatment § II* (Agreements ed., United Nations 2012); Gaukrodger, *The Balance Between Investor Protection and the Right to Regulate in Investment Treaties: A scoping paper* (Investment ed., 2017).

⁵⁸⁴ *ELECTRABEL S.A. v. The Republic of Hungary* (Decision on Jurisdiction, Applicable Law and Liability), (ICSID, 2012).

measures without compensation is legitimate in and of itself, without further affirmative governmental representations or assurances.

7.77 While the investor is promised protection against unfair changes, it is well established that the host State is entitled to maintain a reasonable degree of regulatory flexibility to respond to changing circumstances in the public interest. Consequently, the requirement of fairness must not be understood as the immutability of the legal framework, but as implying that subsequent changes should be made fairly, consistently and predictably, taking into account the circumstances of the investment.

7.78 Fairness and consistency must be assessed against the background of information that the investor knew and should reasonably have known at the time of the investment and of the conduct of the host State. While specific assurances given by the host State may reinforce the investor's expectations, such an assurance is not always indispensable: MTD v Chile (ICSID Case No. ARB/01/7), Award, 25 May Part VII – Page 22 2004; GAMI Investments v Mexico. UNCITRAL, Final Award, 15 November 2004; and SD Myers v Canada, UNCITRAL, Second Partial Award, 21 October 2002. Specific assurances will simply make a difference in the assessment of the investor's knowledge and of the reasonability and legitimacy of its expectations.

7.79 Article 10(1) ECT not only speaks of fair and equitable treatment and equitable and stable conditions, it also refers to “favourable and transparent conditions.” The reference to transparency can be read to indicate an obligation to be forthcoming with information about intended changes in policy and regulations that may significantly affect investments, so that the investor can adequately plan its investment and, if needed, engage the host State in dialogue about protecting its legitimate expectations. Finally, the term “favourable” suggests the creation of an investor-friendly environment. Beyond that, it does not appear to add to the FET standard as it is generally understood.⁵⁸⁵

D. POLICY GUIDELINES FOR THE FET STANDARD

The FET standard ensures that foreign investors are protected from situations of unjust treatment by the host state that do not fall within the domain of other specific treatment standards, such as

⁵⁸⁵ Id. at paras. 7.74-7.79 [emphasis added].

national treatment or MFN. It is an important protection standard for foreign investors; however, its application in arbitral practice has been criticized as threatening a host state's right to regulate. The tribunal in *El Paso v. Argentina* explicitly pointed out that "some tribunals have ... extended the scope of the FET to a point where, according to this Tribunal, the sovereign power of the State to regulate its economy is negated."⁵⁸⁶ In particular, the protection of the investor's expectations regarding a stable legal framework may inhibit host states from regulating matters of public concern, to avoid liability of foreign investors. Hence, countries seeking development from FDI should consider revising the current formulation of FET treatment in a manner that grants them a greater margin of regulatory flexibility, along with a high threshold for state liability. In addition, the contents of the FET standard, and the elements protected under it, should be well defined and designated. In its current formulation, the FET standard raises the following issues:

- i.** The open-ended nature of the FET standard allows foreign investors to push the boundaries of the FET obligation to include legitimate state measures that serve a public or developmental goal.
- ii.** The vague and short formulation of the FET standard does not help arbitral tribunals to define the contents of the standard or draw boundaries on the host state's obligation to provide FET. The contents of the FET obligation are still evolving through arbitral practice, and hence, unless states narrow the FET standard in their future BITs, it is foreseeable that tribunals may adopt broader interpretations that favor foreign investors to the detriment of the host state's policy objectives.

⁵⁸⁶ *El Paso Energy International Company v. The Argentine Republic* para. 340 (Award), (ICSID, 2011).

- iii.** Customary international law on the treatment of aliens is broadly defined and its content has been subject to controversy among arbitral tribunals. Although qualifying the FET standard with customary international law helps in narrowing down the application of the standard, it still does not provide certainty to the threshold of liability that might be adopted by the tribunal. Thus states cannot be sure of the level of deference they will be given in the event of a dispute, nor will they be able to predict the outcome and consequences of their actions.
- iv.** The protection of investor's legitimate expectations relating to a transparent and stable legal framework governing the investment has a direct impact on the host state's ability to regulate. Any change in the legal framework in the host state may affect the foreign investor in various possible ways. Although arbitral tribunals have stressed the need to balance the interests of the investor with the interests of the host state, they have not developed a list of subjective criteria to achieve that balance. This, in return, may result in inconsistent and unpredictable arbitral decisions as to what infringes the investors' regulatory expectations.
- v.** It is settled in arbitral practice that the FET standard protects the expectations of the investor at the time the investment is made. However, as foreign investors come into the host state at different times, it is difficult for the host state to keep track of, and act in accordance with, the expectations each investor has at the time of entering. This is a complicated and taxing burden on the host state that may lead to difficult compliance, as each investor has different expectations depending on the time it enters the host state. All these different expectations cannot be

accommodated by the host state, as the latter's interests dictate regular revisions and amendments to its legal system.

BIT negotiators should develop a new perspective regarding the FET standard. States should formulate the FET standard in a way that provides guidance to tribunals regarding its interpretation and content. States should also explicitly reserve the right to regulate for the public good and in accordance with their development agendas. A better approach is not to include a broad FET standard similar to the typical formulation, but rather to breakdown the contents and elements of the standard and specify precisely which of these elements are protected under the BIT. This allows for a smaller margin of expansive interpretations by arbitral tribunals, and at the same time identifies the content and elements that are protected, leaving no room for investors and arbitral tribunals to expand the scope of protection. The following are policy guidelines and options for states regarding future FET clauses:

1. The host state should replace the typical FET clause with a list of specific obligations that mirror the obligations and elements under the FET standard settled under customary international law, without reference to FET or customary international law *per se*. By fleshing out the contents of the FET standard a host state can avoid the controversies and uncertainties arising from a typical qualified or unqualified FET provision. This approach allows the host state to broaden or narrow the protection as it wishes in accordance with its objectives and needs. Hence, states can include a list of prohibited acts and omissions that constitute a breach of the treaty. They can derive this list of prohibited actions from settled customary international law principles and investor-state arbitrations. UNCTAD

has suggested the following list of prohibited state actions that can be included under this option:⁵⁸⁷

- a. Denial of justice and flagrant violations of due process;
- b. Manifestly arbitrary treatment;
- c. Evident discrimination;
- d. Manifestly abusive treatment involving continuous, unjustified coercion or harassment;
- e. Infringement of legitimate expectations based on investment-inducing representations or measures, on which the investor has relied.

International customary law on the treatment of aliens will still be applicable to foreign investors, even if the BIT makes no reference to it. However, arbitral tribunals will not be able to hear an investor's claim regarding the host state's breach of customary international law, unless the dispute resolution clause of the BIT is wide enough to encompass such claims (for example, if the dispute resolution clause gives jurisdiction to arbitrators to hear "any dispute arising out of an investment").

2. BITs should be drafted to make clear that customary international law is a "ceiling," not a "floor," for the obligation to provide FET.⁵⁸⁸ By tying FET to

⁵⁸⁷ UNCTAD, Fair and Equitable Treatment § II, at 108-09 (Agreements ed., United Nations 2012).

⁵⁸⁸ This follows the approach adopted in the Canada Model Foreign Investment Promotion and Protection Agreement (2004); U.S. Model Bilateral Investment Treaty (2012).

customary international law the host state provides a qualified FET standard. It thus allows the host state to enjoy a higher threshold of liability than an unqualified FET standard. This means that the host state is not required to provide treatment that is beyond or additional to what customary international law prescribes. States must stress that customary international law is formed by the continuous practice of states that stem from their sense of compliance with a legal obligation. This informs interpreters that a claimant investor should provide enough evidence that a state action infringes customary international law. Finally, a state should ensure that the threshold of liability to be applied to them is high by incorporating the *Neer* standard. As such, a state can complement the qualified FET clause with an illustrative list of conduct that rises to the level of egregious conduct found in the *Neer* case,⁵⁸⁹ such as requiring that the conduct involves “gross denial of justice, manifest arbitrariness, a complete lack of due process, evident discrimination or a manifest lack of reasons.”⁵⁹⁰

3. Host states should include general exclusions and reservations as safeguards regarding the scope and application of the FET standard. In this regard four points are important:

- a. The host state’s right to regulate matters of public concern or take measures that pursue legitimate policy objectives should be clearly stated. The host state should insert an exception that allows it to change its regulations and take measures that it deems necessary for its development,

⁵⁸⁹ L. F. H. Neer and Pauline Neer (U.S.A.) v United Mexican States, United Nations Reports of International Arbitral Awards IV 60, (General Claims Commission, 1926).

⁵⁹⁰ UNCTAD, Fair and Equitable Treatment § II, at 106 (Agreements ed., United Nations 2012).

as long as the measures are not applied or enforced in an arbitrary or discriminatory fashion and are connected with a legitimate public purpose.

- b. To clarify that a breach of any treatment standard in the treaty does not automatically entail the breach of the FET standard, and that a breach of FET requires a separate examination.⁵⁹¹
- c. To expressly state that the assessment of investors' expectations should be weighed against the principles of business risk and due diligence, along with the right of the state to regulate in its best interest.
- d. The host state's level of development should be taken into consideration when claims of breach of FET arise.⁵⁹² The understanding of the obligation to provide fair and equitable treatment differs from country to country depending on its level of development. The regulatory, administrative and judicial organs of an underdeveloped state are not as advanced as those in developed countries. Hence, measuring the failure to provide FET with the same ruler for all countries is not fair. It is more than reasonable for an investor to expect a lower level of administrative and judicial due process and regulatory stability in underdeveloped and developing countries. Nonetheless, even underdeveloped and developing countries must adhere to, and comply with, the customary international

⁵⁹¹ This exception has been adopted in the U.S. Model Bilateral Investment Treaty (2012).

⁵⁹² This exception has been adopted in the Investment Agreement For the COMESA Common Investment Area (2007).

law standards for the treatment of aliens. The COMESA Agreement adopts this exclusion, by stating in Article 14.3 that:

For greater certainty, Member States understand that different Member States have different forms of administrative, legislative and judicial systems and that Member States at different levels of development may not achieve the same standards at the same time. Paragraphs 1 and 2 of this Article do not establish a single international standard in this context.⁵⁹³

4. It is important for states to balance the preamble of the BIT by not making the protection of investors its sole objective. Many BIT preambles provide that the objectives of the treaty are to create “a stable framework for investments” or “favorable conditions for investments.” Such emphasis on investor protection allows tribunals to resolve all interpretive uncertainties in favor of investors. Thus, it is important to include other objectives, such as sustainable development and the contracting parties’ right to regulate. Such language will help in achieving a more balanced interpretation not only to the FET standard, but also to all other treatment standards contained in the treaty. Such an approach is adopted in the Morocco – Nigeria BIT preamble which states:

RECOGNIZING the important contribution investment can make to the sustainable development of the state parties, including the reduction of poverty, increase of productive capacity, economic growth, the transfer of technology, and the furtherance of human rights and human development;

SEEKING to promote, encourage and increase investment opportunities that enhance sustainable development within the territories of the state parties;

UNDERSTANDING that sustainable development requires the fulfillment of the economic, social and environmental pillars that are embedded within the concept;

⁵⁹³ Id. at art. 14.3.

REAFFIRMING the right of the State Parties to regulate and to introduce new measures relating to investments in their territories in order to meet national policy objectives and taking into account any asymmetries with respect to the measures in place, the particular need of developing countries to exercise this right;

*SEEKING an overall balance of the rights and obligations among the State Parties, the investors, and the investments under this Agreement.*⁵⁹⁴

CONCLUSION

In this Chapter I have considered different BIT provisions, such as the definitions of “investments” and “investors,” along with the most-commonly invoked treatment standards (NT, MFN, and FET). As currently formulated in most BITs, these provisions are not adequately designed to promote development of host countries. Their vague and open-ended nature allows much room for innovative and expansive interpretations by foreign investors and tribunals, which then limits the host state’s ability to regulate and to pursue its development objectives.

Arbitral tribunals in investor-state arbitrations have interpreted these provisions with little regard to the interests of the host state, and with great bias to foreign investors. Hence, BITs are generally asymmetrical in their obligations, as they pose obligations on the host state to provide protection to foreign investments, without any corresponding obligations on the investor or the investment to contribute to the host state’s development agenda.

The vague BIT provisions and their expansive interpretations by investor-state tribunals jeopardize the entire BIT system which was built over many decades. In fact, there is a recent backlash in which countries are now refusing to enter into new BITs, or even withdrawing from

⁵⁹⁴ Morocco - Nigeria BIT (2016).

existing BITs.⁵⁹⁵ Therefore reviewing the current BIT template and equating the interests of all parties involved (host states and foreign investors) is vital.

Reforming the current BIT template requires rebalancing the equation between the two objectives sought from concluding BITs, namely investment protection and economic development. The rebalancing of foreign investor and host state interests should not occur by eliminating the investor-state dispute-settlement mechanism (ISDS), as called for by some organizations and scholars.⁵⁹⁶ Rather the solution rests in the wording and formulations of different treaty provisions. A recent report notes that “the outcome of many disputes hinged upon the wording of specific provisions in the applicable IIA [international investment agreement]. This underlines the importance of balanced and careful treaty drafting and the need to reduce uncertainty arising from (broadly worded) provisions.”⁵⁹⁷

A comprehensive review of all typical BIT provisions, and their interpretation and application by arbitral tribunals, is necessary. States should review BIT provisions with reflection on the issues and uncertainties that have appeared in investor-state arbitrations, and should draft balanced and up-to-date treaty provisions. This should include modifying the BIT template to increase the host state’s regulatory power, clarifying state party intent, precisely

⁵⁹⁵ Some States have terminated certain agreements or refrained from concluding (new) investment agreements. Most recently are the decrees signed by President Correa of Ecuador on 16 May 2017 to terminate “16 Bilateral Investment Treaties (BITs), including with the US, Canada, China and eight European countries.” See news article on TNI website <https://www.tni.org/en/article/ecuador-terminates-16-investment-treaties>. Other countries have previously terminated certain of their BITs; “Venezuela (e.g., with the Netherlands in 2008), South Africa (e.g., with Germany, Switzerland and the Netherlands in 2013), Ecuador (e.g., with Cuba, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, the Dominican Republic and Uruguay in 2008), or the announcement of Indonesia to terminate its investment treaties (e.g., with the Netherlands as of 2015).” See Andreas R. Ziegler, *Special Issue: Towards Better BITs? – Making International Investment Law Responsive to Sustainable Development Objectives*, 15 THE JOURNAL OF WORLD INVESTMENT & TRADE 803, 804 (2014).

⁵⁹⁶ See in general Gabrielle Kaufmann-Kohler & Michele Potesta, *Challenges on the Road Toward a Multilateral Investment Court* (Karl Sauvant ed., Columbia Center on Sustainable Investment 2017).

⁵⁹⁷ Investor–State Dispute Settlement: Review of Developments in 2016, at 29 (2017).

identifying the scope of the treaty, and adding reservations and exclusions to the BIT to give the host country more flexibility.

Some countries have started to react to concerns over interpretations of BITs by amending their model BITs in a manner that attempts to equalize the interests of foreign investors and host states. Some expansive interpretations of BIT provisions in investor-state arbitrations have influenced countries to insert clarifications and limitations to some treatment standards in order to avoid problematic interpretations in the future.

In the next chapter, I will provide a case study of a specific developing country that does not have a model BIT, using Jordan as an example of a country in need of FDI for its development. I will propose a model BIT for Jordan that accommodates the interests of both the foreign investor and the host state in light of recent developments in investor-state arbitrations and recent trends and best practices in investment treaty making.

CHAPTER FIVE

EQUATING THE INTERESTS IN FUTURE BITs: AN EXAMPLE

I. INTRODUCTION

Economic development has always been one of the main objectives behind the encouragement of FDI into capital-importing countries. Although there is no empirical evidence that signing BITs necessarily results in increased amounts of FDI,¹ it is certain that providing protection and treatment standards to home state investors constitutes a positive factor in the investment decision process.² Therefore, BITs play an important role in signaling that a capital-importing state is an investment-friendly destination. The increased inflow of FDI to such a capital-importing state will, presumably, result in economic growth and development.³

¹ For a full discussion on the impact of BITs on foreign investment inflows see Lisa E. Sachs & Karl P. Sauvant, *BITs, DTTs and FDI flows: an Overview*, in *THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT: BILATERAL INVESTMENT TREATIES, DOUBLE TAXATION TREATIES, AND INVESTMENT FLOWS* (Karl P. Sauvant & Lisa E. Sachs ed. 2009). See also Jeswald W. Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, 24 *THE INTERNATIONAL LAWYER* 655 (1990).

² To illustrate, MIGA requires the existence of an investment treaty between the investor's home state and the host state as a condition of their agreement to insure an investment. This requirement illustrates how BITs are seen as a tool that mitigates the risk of negative state behavior affecting the investment. See *The Convention Establishing the Multilateral Investment Guarantee Agency (MIGA)* (1985). Article 12(e)(iv).

³ “[C]ountries with emerging markets entered into BITs with industrialized states in order to attract capital and technology to advance their development, and did so at an accelerating pace.” JESWALD W. SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR*

The current FDI regime has not proved to support economic development, especially in developing countries.⁴ Bilateral investment treaties, and their interpretation by arbitral tribunals, have become a burden on developing countries.⁵ They have overprotected home state investors and investments, at the expense of the host state's development.⁶ This can be evidenced through the recent decisions by countries refusing to conclude new BITs or terminating existing ones.⁷ This is a result of the historical background and circumstances surrounding the formation of BITs in the 1950's.⁸ Recently, however, many countries and organizations have voiced the need to effectuate the reciprocal nature of investment treaties.⁹ BITs should serve as a tool for economic development, in addition to investment protection.

FOREIGN CAPITAL 345 (Oxford University Press. 2013). See also Karl P. Sauvant and Federico Ortino, *Improving the International Investment Law and Policy Regime: Options for the Future* 21 (2013).

⁴ See in general Aaron Cosby Nathalie Bernasconi -Osterwalder, Lise Johnson, Damon Vis -Dunbar, *Investment Treaties and Why They Matter to Sustainable Development*, (2012). Also see SORNARAJAH, *THE INTERNATIONAL LAW ON FOREIGN INVESTMENT* 48 (Cambridge University Press 3 ed. 2012).

⁵ Two particular issues can be highlighted to illustrate states' concerns about the application and interpretation of BITs: "(i) the failure of arbitral tribunals to apply treaties consistently, and (ii) tribunals' application of treaties in a manner that expands the treaties beyond their intended or anticipated scope." Ignacio Torterola and Ronan McHugh, *To Risk or Not to Risk? The State's Perspective of Investor-State Dispute Resolution at the 20th Anniversary of MIGA*, in *INVESTING WITH CONFIDENCE UNDERSTANDING POLITICAL RISK MANAGEMENT IN THE 21ST CENTURY* 177 (Gero Verheyen Kevin W. Lu, and Srilal M. Perera ed. 2009). Also, BITs have been criticized of "imposing constraints on the ability of the host country governments to adopt the policies needed to promote sustainable development." PENELOPE SIMONS J ANTHONY VANDUZER, GRAHAM MAYEDA, *INTEGRATING SUSTAINABLE DEVELOPMENT INTO INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE OF DEVELOPING COUNTRY NEGOTIATORS* 20 (Commonwealth Secretariat. 2013).

⁶ Kenneth J. Vandavelde, *A Brief History of International Investment Agreements*, 12 U.C.-DAVIS JOURNAL OF INTERNATIONAL LAW & POLICY 157, 179 (2005).

⁷ Some countries have terminated certain agreements or refrained from concluding (new) investment agreements. Most recently are the decrees signed by President Correa of Ecuador on 16 May 2017 to terminate "16 Bilateral Investment Treaties (BITs), including with the US, Canada, China and eight European countries." See news article on TNI website <https://www.tni.org/en/article/ecuador-terminates-16-investment-treaties>. Other countries have previously terminated certain of their BITs; "Venezuela (e.g., with the Netherlands in 2008), South Africa (e.g., with Germany, Switzerland and the Netherlands in 2013), Ecuador (e.g., with Cuba, El Salvador, Guatemala, Honduras, Nicaragua, Paraguay, the Dominican Republic and Uruguay in 2008), and the announcement of Indonesia to terminate its investment treaties (e.g., with the Netherlands in 2015)." Andreas R. Ziegler, *Special Issue: Towards Better BITs? – Making International Investment Law Responsive to Sustainable Development Objectives*, 15 THE JOURNAL OF WORLD INVESTMENT & TRADE 803, 804 (2014).

⁸ Salacuse, *BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries*, 24 THE INTERNATIONAL LAWYER 655, 665 (1990).

⁹ The United States and Canada, for example, drawing on their experience as respondents in NAFTA cases, have revised their model BITs to clarify the scope and meaning of different investment obligations. South Africa revised

The need to harness economic growth and development has reached a peak. Mobilizing investment and ensuring that it contributes to development objectives should be a priority for all countries, including, in particular, developing countries. This requires a review of the current BIT template used by most countries and a rebalancing of the approach, policies, and law-making of BITs, where both the economic development objectives of the host state and home state investor protection are addressed and equally preserved.

A. REBALANCING BITs

In light of the developments in investor-state arbitrations, many countries have started to redraft their model BITs to achieve a greater level of balance between investor protection and the host state's right to pursue its development objectives. For example, the United States and Canada, drawing on their experience as respondents in NAFTA cases, have revised their model BITs to clarify the scope and meaning of different investment obligations.¹⁰ South Africa revised its investment policy after it concluded that "BITs and international arbitration pose unacceptably high risks to the government's right to regulate in the public interest."¹¹ India's reconsideration of its BIT program addressed concerns about the imbalance between investment protection and the Indian state's regulatory power.¹² A new generation of investment treaties is emerging.

its investment policy after it concluded that "BITs and international arbitration pose unacceptably high risks to the government's right to regulate in the public interest." India's reconsideration of its BIT program was related to concerns about the imbalance between investment protection and the Indian state's regulatory power.

¹⁰ Reforming the International Investment Regime: An Action Menu. 124 (2015).

¹¹ David Gaukrodger, *The Balance Between Investor Protection and the Right to Regulate in Investment Treaties: A scoping paper* 9 (OECD Working Papers on International Investment ed., 2017).

¹² *Id.* at 9.

International organizations have presented working papers and studies on the importance of re-balancing the purposes of BITs to include economic development. The UNCTAD Secretariat recently published the “Investment Policy Framework for Sustainable Development (IPFSD)”¹³ in order to promote a new generation of investment agreements that contain a development agenda. The UNCTAD publication can also be used as a guide for policymakers when formulating their national and international investment policies. Other organizations, such as the OECD and IISD, have initiated similar studies and papers.¹⁴

Different countries have different economic, political, social, and development goals. The model BITs offered by different international organizations are offered on a “one size fits all” basis, as if all countries are equal in terms of their economic situation and development challenges. But investment treaties touch on critical matters that have different effects on different countries. Hence, no single model BIT can be expected to suffice on a global basis, given the range of states involved and their distinctive circumstances. This is evidenced by the failure of prior attempts for an international unified investment agreement.¹⁵ Therefore, the concept of a uniform model BIT on a global basis is obsolete. The solution to this problem rests

¹³ Investment Policy Framework for Sustainable Development (2015).

¹⁴ See Investment Treaty Law, Sustainable Development and Responsible Business Conduct: A Fact Finding Survey. (2014). See also Gaukrodger, (Investment ed., 2017). See also HOWARD MANN AARON COSBEY, LUKE ERIC PETERSON, KONRAD VON MOLTKE, IISD MODEL INTERNATIONAL AGREEMENT ON INVESTMENT FOR SUSTAINABLE DEVELOPMENT: NEGOTIATORS’ HANDBOOK (International Institute for Sustainable Development (IISD) 2nd ed. 2006).

¹⁵ For example, in 1995 OECD took the initiative to establish a Multilateral Agreement on Investment (MAI). The negotiators from capital-importing and capital exporting countries had different views on the proposed MAI. “All the principle negotiating states had substantial investments abroad and so had a common interest in seeing that those investments received maximum protection.” OECD capital-importing countries, on the other hand, were concerned about the types of foreign investment they will have to accept in their territories under the MAI and the high level of protection proposed by capital-exporting states. The negotiators seemed not to find a common ground, and therefore the negotiations for the MAI failed. See SALACUSE, THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL 353-54 (Oxford University Press. 2013). See also JESWALD W. SALACUSE, THE LAW OF INVESTMENT TREATIES 118-22 (Oxford University Press 2 ed. 2015).

on reforming the bilateral investment treaty itself, by drafting country-specific model BITs that are designed to accommodate the individual needs and objectives of each country.¹⁶

Country-specific model BITs must be designed and tailored to account for the particular needs and objectives of a host state. They are an important tool needed to attain the economic and development fruits of FDI. Unlike developed countries, most developing countries do not have model BITs that are specifically designed to foster their economic development.¹⁷ Nor do the BITs offered to them by other countries allow them the ability to act in their best interest and achieve development through FDI, as these BITs are designed to advance the interests of the capital-exporting state.¹⁸

By enacting “host state” model BITs, capital-importing countries would have increased control in negotiating and imposing the terms and conditions that are aligned with their own policies and development objectives.¹⁹ The host state model BIT, along with the home state model BIT, will serve as a mirror that reflects each party’s position and projection of the final BIT. From these two documents the parties can work together to reach a balanced final BIT that fits the specific relationship and accommodates the interests of both parties. The threat of moving investments offshore limits the ability of host countries to impose or introduce inefficient, or overly strict, provisions into the final BIT. At the same time, insisting on overly strict and vague treatment standards by the home state will run the risk of failing the BIT

¹⁶ A recent UNCTAD publication notes “A key challenge is promoting investment in areas that make the greatest contribution to sustainable development. This requires a new generation of investment promotion and facilitation strategies, tools, institutions and partnerships.” UNCTAD, at Executive summary page (UNCTAD 2015).

¹⁷ See list of public model BITs at <https://www.italaw.com/investment-treaties>. See also SALACUSE, *THE THREE LAWS OF INTERNATIONAL INVESTMENT : NATIONAL, CONTRACTUAL, AND INTERNATIONAL FRAMEWORKS FOR FOREIGN CAPITAL* 342 (Oxford University Press. 2013).

¹⁸ Andrew Newcombe, *Sustainable Development and Investment Treaty Law*, 8 *THE JOURNAL OF WORLD INVESTMENT & TRADE* 357, 363 (2007).

¹⁹ In other words, “the party who controls the draft [model BIT] usually controls the negotiation.”

negotiations, and losing a market for the home state's outbound investors. Hence, a balanced approach to protect the interests of both home state investors and the host state is vital for the success of any final BIT. If the final BIT strikes the right balance between economic development and investment protection, then development through FDI becomes projected.

In this chapter, I draw upon the analysis provided earlier in this thesis regarding the overly protective nature of BITs and their interpretation in order to provide recommendations and suggestions for policy makers in developing countries to draft host state model BITs that can be used when negotiating BITs with home countries. These host state BITs will balance the equation and preserve both parties' rights for development and investment protection in the final BIT between home and host states. To develop a tailored host state model BIT, I will use Jordan as an example of a developing state faced with many economic and development challenges, and which does not have a model BIT of its own that it can use when negotiating BITs with home countries.

B. EQUAL PRESERVATION OF INTERESTS

Rebalancing the interests in BITs does not mean removing or lowering investment protection standards. To the contrary, foreign investors look not only for good markets, but also for stable and low risk markets. Hence, they want to be sure that their invested capital will be neither discriminated against nor arbitrarily treated, and that it will be protected from governmental interference. A foreign investor also seeks guarantees that it will remain free to transfer its profits and capital to its home state. Finally, foreign investors want an efficient and neutral method to solve future disputes with the host state, preferably via international arbitration under the

auspices of the International Center for Settlement of Investment Disputes (ICSID).²⁰ Therefore, standards of protection are legitimate and reasonable demands of home state governments on behalf of their investors who invest large amounts of money and resources in host countries. Treatment standards not only provide assurance to home state investors, but they also discipline the host state, as they deter host governments from taking unjust, arbitrary, and discriminatory acts fearing paying large amounts of compensation to home state investors.

To rebalance BITs, this thesis suggests that host states draft model BITs that limit the broad and vague language of investment protection standards to specific and unambiguous commitments by the host state. By clarifying the ambiguities and specifying the commitments, two main advantages can be attained: i) host state investors and BIT interpreters will have a reduced margin for expansive and unintended interpretations, while maintaining internationally accepted standards of protection, and ii) host states will have greater predictability of interpretation and more regulatory flexibility to pursue their development objectives without the fear of liability to home state investors.

The host state model BIT should also rebalance investor rights *vis-a-vis* state obligations to become investor rights and obligations *vis-a-vis* host state rights and obligations. This is achieved by imposing obligations on the home state investor that ensure its contribution to host state development. Such obligations include requiring certain local employment quotas, conformity with corporate governance standards, social responsibility, and adherence to international conventions relating to the protection of human rights, the environment, and the like. The host state's right to regulate in the public good and pursue its legitimate public policy

²⁰ CONVENTION ON THE SETTLEMENT OF INVESTMENT DISPUTES BETWEEN STATES AND NATIONALS OF OTHER STATES (1965).

and development objectives must be explicitly preserved. Hence, a particular provision to that end must be inserted in the host state model BIT, and the treatment standards should be drafted in a manner that does not compromise this right. Finally, the host state model BIT should limit recourse to international arbitration if the home state investor fails to comply with its obligations under the treaty. Thus, arbitration would be limited or prohibited if the home state investor breaches the host state's local laws, is involved in corruption, or violates international conventions relating to human rights and the environment. The host state can reserve its right to raise these issues as defenses in investor-state arbitration, or to raise them as counter claims requesting compensation from, or set-off against the home state investor. Other improvements to future BITs that promote development through investment include the imposition of performance requirements that align with the host state's development agenda.²¹ These issues are discussed in further detail below.²²

C. THE NEED FOR INDIVIDUALIZED HOST STATE MODEL BITs

One host state model BIT cannot accommodate the different needs and objectives of all countries. Although there are many conceptual matters that can be transferred to individual model BITs, each state has its own policies, objectives, and goals; therefore, a single host country model BIT will not suffice. Each host state must have its own model BIT that is tailored

²¹ Performance requirements can be defined as "stipulations, imposed on investors, requiring them to meet certain specified goals with respect to their operations in the host country." UNCTAD, *Foreign Direct Investment and Performance Requirements: New Evidence From Selected Countries* § UNCTAD/ITE/IIA/2003/7, at 2 (UNCTAD ed., United Nations 2003).

²² See Table in Section II of this Chapter 5.

specifically to its needs. Thus, the recommendations and model clauses proposed in this chapter address a specific developing state in light of its development challenges. This thesis will use Jordan as an example of a developing country that is striving to attract FDI to enhance its economy and development.

Jordan is a good case study, since it is a developing country without a model BIT designed specifically to foster its development. Nonetheless, the recommendations and suggestions made in this chapter can be transferred and applied by policy makers in any country after studying the proposed clauses and adjusting them to their specific needs and goals. What is important for any developing host state when revising - or drafting - its model BIT is to maintain a balanced approach throughout its revision or drafting process by emphasising the rights and obligations of both the home state investor and the host state. Due to their resemblance with Jordan in economic situation, social fabric, development goals, and geographic location, countries in the MENA region should be able to benefit most directly from the recommendations set forth below.

The proposed model clauses and policy guidelines for Jordan will incorporate the development challenges faced by Jordan, thereby aiming to effectively overcome these challenges through future FDI. The proposed BIT will shift the focus found in most BITs from pure investment protection to balanced protection tied with economic development. The legal issues that have hindered the development of other countries, such as the overly protective treatment standards and their innovative interpretations by arbitral tribunals, will be addressed to avoid similar situations in the future. This is not to say that other institutional and regulatory reforms within the country are not required. No model BIT will substitute for a sound and transparent administrative and legal system in the host state. However, BITs can play a role in

achieving the developmental goals of a country, if they are synchronized with a broader reform policy in all government levels and sectors.

D. A FOCUS ON JORDAN AND ITS DEVELOPMENT CHALLENGES

As a small, developing country, Jordan has many of the economic problems associated with developing economies, including high external debt, a small export base, a small manufacturing sector, high unemployment (15.25% officially,²³ but the unofficial rate is approximately 30%), high poverty (14.2%), and inflation (2.4%).²⁴ The government is heavily reliant on foreign assistance due to insufficient supplies of water, oil, and other natural resources. Moreover, the country faces a host of regional problems, such as refugees and regional instability,²⁵ which resulted in a debt-to-GDP ratio of 95% at the end of 2016.²⁶

The purpose of this section is not to go into the details of the Jordanian economy and its many challenges.²⁷ Rather, this section identifies the most critical development challenges in the country that are considered a priority for the Jordanian government, so that those issues might be considered in the subsequent discussion of how best to address Jordan's needs in a model host state BIT.

²³ Jordan Economic Growth Plan 2018-2022, at 6 (The Economic Policy Council ed., 2017).

²⁴ Information found on the World Fact Book <https://www.cia.gov/library/publications/the-world-factbook/geos/jo.html>

²⁵ Information found on the World Bank IBRD- IDA Data Website, Jordan. Available at <http://data.worldbank.org/country/jordan>, visited on July 17, 2015.

²⁶ Jordan Economic Growth Plan 2018-2022, at 5 (Council ed., 2017).

²⁷ A comprehensive discussion of Jordan's economic challenges and the Government's plan to overcome them can be found in the recently published "Jordan Economic Growth Plan 2018 – 2022", available at <https://rhc.jo/sites/default/files/JEPGReportEn.pdf>.

Jordan's first developmental challenge is securing its energy sources. Jordan lacks any vast quantities of natural resources and is dependent on importing conventional energy sources.²⁸ Recent regional instability, along with the worldwide long term increase in oil prices, have put a heavy burden on the government. Thus, the Jordanian government is actively promoting FDI in the energy sector. This includes investments in the fields of nuclear energy, oil shale, and natural gas.²⁹ In addition to conventional energy sources, Jordan is actively encouraging investments in the renewable energy sector.³⁰ The National Energy Strategy (2007-2020) sets a target to increase the share of renewable energy sources in the country's energy mix to 10% by 2020.³¹ To that effect, a law was enacted in 2010 that promotes and incentivizes renewable energy related investments.³²

The second major development challenge is Jordan's scarce water resources. Jordan is the second poorest country in the world in water resources.³³ In addition to the scarcity of water resources, Jordan has an out-dated water transmission and distribution network. It is reported that almost 57% of potable water is leaked in the distribution process before reaching consumers.³⁴ The 2016-2025 National Water Strategy seeks to attract FDI in the areas of waste-water

²⁸ OECD Investment Policy Reviews: Jordan 2013, at 197 (2013).

²⁹ Id. at 204-06.

³⁰ "Jordan has tremendous wind, solar and biomass energy potential which can only be realized by large-scale investments. In 2007, the Government of Jordan developed an integrated and comprehensive Energy Master Plan. Renewable energy accounted for only 1% of the energy consumption in Jordan in 2007." Salman Zafar, *Renewable Energy Investment in Jordan*, ECOMENA: ECHOING SUSTAINABILITY, 2017. Available at <http://www.ecomena.org/cleantech-investment-in-jordan/>

³¹ Jordan's National Energy Strategy. (2007).

³² Law on Renewable Energies and Energy Efficiency (2010).

³³ <http://www.jordantimes.com/news/local/jordan-world%E2%80%99s-second-water-poorest-country>

³⁴ "At present, an estimated 57 percent of the potable water supply in Jordan's Zarqa Governorate is lost through leaks in the water transmission and distribution network, with additional losses attributed to management weaknesses." MCC and Jordan: A Partnership Toward Sustainable Solutions 1 (Fact Sheet) (Millennium Challenge Corporation ed., 2010).

collection and treatment, rehabilitating and upgrading water distribution systems and infrastructure, and protecting water resources and its management.³⁵

Other economic challenges exist, although they may not be as urgent as the ones mentioned above. These include issues in the tourism and hospitality, public transport, and telecommunication sectors. These sectors contribute greatly to the country's GDP, provide employment opportunities, provide hard currency, and increase Jordan's exports.³⁶ Thus future BITs in Jordan require incorporating these challenges in the BIT, by focusing on attracting FDI in these sectors.

E. DEVELOPMENT CHALLENGES AND A MODEL BIT FOR JORDAN

By targeting specific sectors in its model BIT, which should also be integrated in an overall development policy, Jordan can attract FDI that is vital for its development. The sectoral approach of attracting FDI enables host states to maintain a diversified FDI portfolio, while also building a base for other industries.³⁷ Therefore, for a country that lacks natural resources and is faced with a variety of economic challenges, the model BIT should adopt an approach of attracting quality FDI, instead of distorting its efforts by attempting to attract any type of FDI, which might not contribute to the country's economy.³⁸

³⁵ See National Water Strategy 2016 - 2025 (Ministry of Water and Irrigation - Jordan ed., 2016).

³⁶ Jordan Economic Growth Plan 2018-2022, at 7 (Council ed., 2017).

³⁷ Ana Arias Urones & Ashraf Ali Mahate, FDI Sectorial Diversification: The Trade-Transport-Tourism Nexus (Karl P. Sauvant & Matthew Schroth ed., Columbia FDI Perspectives 2017).

³⁸ Mann notes that developing countries should shift their focus from "looking at the quantity of investment as the only issue, to the quality of that investment as the key issue." See Howard Mann, *Reconceptualizing International Investment Law: Its Role in Sustainable Development*, 17 LEWIS & CLARK LAW REVIEW 521, 534 (2013).

Drafting a balanced and focused BIT for Jordan will not waive the need for further reforms on the state level to encourage FDI into the country. The Jordanian government realizes that attracting FDI requires “enhancing [Jordan’s] doing business eco-system, cutting the red-tape and bureaucracy, upgrading its economic legislation framework, and streamlining its economic judicial transactions.”³⁹

F. A MODEL BIT FOR JORDAN

The model BIT for Jordan proposed here is inspired by the recent practices in various bilateral and multilateral investment treaties. It also builds upon the recent efforts of other countries that have amended their model BITs, attempting to balance their interests with the interests of home state investors. The model BITs proposed by international organizations (such as UNCTAD and IISD) will also be consulted and referenced.⁴⁰ The model BIT proposed for Jordan takes into account the country’s economic challenges mentioned above, in addition to the preservation of the government’s regulatory flexibility to pursue its development objectives. The proposed BIT will also take into account the application and interpretation of different treaty provisions in investor-state arbitrations, with the goal of limiting the possibility of overreaching and unintended interpretations. Finally, the proposed BIT will introduce some provisions and obligations that are not usually found in typical BITs. These provisions impose obligations on

³⁹ Jordan Economic Growth Plan 2018-2022, at 11 (Council ed., 2017).

⁴⁰ See UNCTAD, Investment Policy Framework for Sustainable Development (UNCTAD 2015). Also see A Model International Investment Agreement for the Promotion of Sustainable Development (Konrad von Moltke ed., International Institute for Sustainable Development 2004).

host state investors that change the standard nature of BITs, as they typically only provide rights to host state investors with no corresponding obligations on those investors.

The following section contains a table that is divided into six sections each addressing a specific part of the proposed BIT for Jordan, as follows: i) preamble and objectives, ii) definitions and admission (investments and investors), iii) treatment standards (NT, MFN, and FET), iv) dispute resolution, v) investor obligations, and vi) host state reservations and exceptions. The chart will summarize the current issues pertaining to these points, and propose the solution by illustrating examples from recent BITs and Model treaties. Table 2 will then propose a model BIT for Jordan based in the discussion and examples provided in the chart.

II. TABLES

Table (1): Current Issues in BITs and the Way Forward

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
<p align="center">Preamble</p>	<p>The starting point to draft any international treaty is to determine the objectives sought from it.</p> <p>Investment treaties are no different. The objectives of a BIT are usually stated in its preamble, which typically emphasizes the protection of foreign investors as the treaty's main goal.⁴¹</p> <p>Preambles are not a source of legal obligation. However, preambles play a determining role when it comes to the interpretation of treaty terms.⁴²</p> <p>The emphasis on investment protection in the treaty preamble has led arbitral tribunals to resolve any interpretive delinquencies with bias to investment protection.⁴³</p>	<p>Jordan's model BIT should have a balanced preamble that explicitly states - in addition to investment protection - that the broader objective of the BIT is the development of the host state. The preamble should also give reference to the host state's right to regulate matters of public concern and pursue its development policies. Such an approach acknowledges that the host state has rights under the treaty similar to the rights of foreign investors.</p> <p>Additionally, as Jordan is a developing country, it may not be able to provide the same level of transparency and protection as the developed treaty partner. Developing countries, by virtue of their economic weakness, should be allowed a margin of special treatment by the more advanced treaty party.⁴⁴ Therefore, it is beneficial for Jordan to mention in the preamble</p>	<p>The preamble of the Trans-Pacific Partnership Agreement (TPPA),⁴⁵ emphasizes that the broader goal of the TPPA is to “bring economic growth and social benefits, create new opportunities for workers and businesses, contribute to raising living standards, benefit consumers, reduce poverty and promote sustainable growth.”⁴⁶</p> <p>Additionally, the TPPA preamble affirms the state parties’ “inherent right to regulate and resolve to preserve the flexibility of the Parties to set legislative and regulatory priorities, safeguard public welfare, and protect legitimate public welfare objectives, such as public health, safety, the environment, the conservation of living or non-living exhaustible natural resources, the integrity and stability of the financial system and public morals.”⁴⁷</p>

⁴¹ Many BIT preambles provide that the objectives of the treaty are to create “a stable framework for investments” or “favorable conditions for investments.”

⁴² See Article (31)(1) of the Vienna Convention on the Law of Treaties (1969).

⁴³ “Interpretations giving significant weight to the object and purpose of investment treaties have been criticized as favouring investors to the detriment of host States.” J. ROMESH WEERAMANTRY, TREATY INTERPRETATION IN INVESTMENT ARBITRATION 191 (Oxford University Press. 2012).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
		<p>that differences between the parties in their level of development exist. This approach will inform interpreters that the developing host state should be given a larger margin of deference in investor-state arbitrations.</p>	<p>The TTPA recognizes that not all of its 12 treaty partners are on equal footing in terms of development, and therefore its preamble acknowledges “<i>the differences in their levels of development and diversity of economies.</i>”⁴⁴</p> <p>The TTPA’s preamble may form a new norm in investment treaty making. Its preamble equalizes the two main objectives of investment treaties, mainly investment protection and host state development. Similarly, the preamble of the recent Slovak – Iran BIT seeks “<i>to promote investment that contributes to the sustainable development of the Contracting Parties,</i>” and aims to “<i>secure an overall balance of rights and obligations between investors and the Host State.</i>”⁴⁹</p> <p>Developing countries like Jordan should adopt – in their model BIT - preambular language similar in content to that of the TTPA and/or the Slovak – Iran BIT.⁵⁰</p>

⁴⁴ UNCTAD, National Treatment § IV, at 47-48 (United Nations 1999).

⁴⁵ Trans Pacific Partnership Agreement (TPPA) (2016).

⁴⁶ Id. at Preamble.

⁴⁷ Id. at Preamble.

⁴⁸ Id. at Preamble.

⁴⁹ Slovak – Iran BIT (2016).

⁵⁰ See also the preamble of the Morocco - Nigeria BIT (2016).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
Objectives	<p>The preamble of a BIT plays an important role in the interpretation of the treaty. However, the preamble itself is not a source of legal obligations on the parties, and is seen as a mere statement of the motives that induced the parties to enter into the treaty. Hence, their use in interpretation is supplementary and may not be given significant weight by interpreters. Therefore, inserting a treaty provision that states the treaty's objectives will make these objectives obligatory on interpreters, in accordance with the rules of interpretation found in the Vienna Convention on the Law of Treaties (VCLT).⁵¹</p>	<p>To safeguard against a tribunal's neglect of the preamble, the parties can add an "objectives clause" at the beginning of the BIT. This provision will outline the objectives of the BIT and the intention of the parties. Such a provision, being part of the treaty terms and thus compulsory when interpreting the treaty, "gives added weight to the objective as an interpretational guide, beyond that which is normally attributed to the preamble."⁵²</p>	<p>The following text is suggested for the objectives clause:⁵³ <i>The objective of this Agreement is to stimulate, encourage, and increase the flow of Investments that contribute to and support the development of each Party, in particular the Host State where the Investment is located.</i> The text of the objective clause should be short and uncomplicated. Efforts to reflect all intentions and objectives of the parties may render it ineffective and may cause confusion to interpreters.⁵⁴</p>

⁵¹ Article 31(1) of the VCLT requires interpreters to interpret a treaty "in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose." Vienna Convention on the Law of Treaties (1969).

⁵² SADC Model Bilateral Investment Treaty Template with Commentary 8 (Southern African Development Community ed., 2012).

⁵³ Compare this text with the one in HOWARD MANN AARON COSBEY, LUKE ERIC PETERSON, KONRAD VON MOLTKE, IISD MODEL INTERNATIONAL AGREEMENT ON INVESTMENT FOR SUSTAINABLE DEVELOPMENT: NEGOTIATORS' HANDBOOK 4 (International Institute for Sustainable Development (IISD) 2nd ed. 2006).

⁵⁴ See in general id. at 4.

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
<p style="text-align: center;">Definition of Investment</p>	<p>The definition of investment determines the types of economic projects covered under the BIT. The definition is also important to determine ICSID jurisdiction when disputes arise.⁵⁵</p> <p>Most BITs adopt an open asset-based definition of investment that covers a wide range of economic activities. However, the ICSID case law in this regard shows that this type of definition has enabled arbitrators to include transactions that were not originally envisaged by the state parties as covered investments (for example portfolio investments and government debt securities).⁵⁶</p> <p>In addition, the typical definition of investment in most BITs does not require the investment activity to</p>	<p>1) Before drafting the definition of “investment,” any country will have to designate its development challenges and the goals it seeks to achieve from protecting FDI. Upon that determination it will be better situated to draft the most suitable definition for covered investment under its BITs.</p> <p>2) The developmental challenges in Jordan are mainly those related to its energy and water sectors. However, the country needs FDI in other sectors as well to stimulate the overall growth of its economy.</p> <p>Therefore, the Jordanian model BIT should adopt a definition that allows all kinds of investment (open asset-based definition), with emphasis on energy and water related FDI. The emphasis on water and energy projects can be achieved via granting pre-establishment rights to FDI in these sectors exclusively.</p> <p>3) An open asset-based definition is not recommended by international institutions.⁵⁷</p>	<p>The definition of investment adopted in the Colombia – Turkey BIT is a good example of what Jordan should adopt in its model BIT.⁵⁸ The definition is detailed and long, hence it is not included in this table. However, it is an open-asset-based definition that explicitly excludes portfolio investments, public debt operations, claims to money arising out of a commercial transaction, and credit given in commercial transactions. The definition in the said BIT does not exclude IP rights not protected under domestic law - a recommended exclusion by UNCTAD.⁵⁹</p> <p>Other investment treaties (e.g. the COMESA Agreement)⁶⁰ also exclude goodwill market share, which - according to NAFTA jurisprudence - constitute an investment.⁶¹</p> <p>The Colombia – Turkey BIT requires the characteristics of an investment to be present in any economic project to have treaty protection.⁶² However, the required</p>

⁵⁵ Article 25 of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965).

⁵⁶ Investment Policy Framework for Sustainable Development 81 (2015).

⁵⁷ The SADC Model BIT, for example, discourages the use of open-asset based definitions. See SADC Model Bilateral Investment Treaty Template with Commentary 12-13 (Community ed., 2012).

⁵⁸ Colombia - Turkey BIT (2014).

⁵⁹ UNCTAD, Investment Policy Framework for Sustainable Development 92 (UNCTAD 2015).

⁶⁰ Investment Agreement For the COMESA Common Investment Area (2007).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
	<p>contribute to the host state's development in order to be covered under treaty protection.</p>	<p>However, for a country like Jordan, which needs FDI in virtually all sectors, the asset-based definition becomes the best option due to the wide range of investments such a definition covers. However, the asset-based definition can be narrowed by incorporating the requirement that economic activities covered under the BIT must have the “characteristics of an investment.” These characteristics are i) a substantial commitment (of capital and other resources), ii) the assumption of risk, iii) a lasting interest in the host state, iv) the expectation of profit, and v) condition that only the assets and resources used in the operation of the investment project are given protection (this eliminates vacation assets and other assets not used in the operation of the investment project from the ambit of treaty protection).</p> <p>4) Jordan can also narrow the open asset-based definition by including a legality requirement (i.e. that the investment must be made in accordance with the host country's laws). This requirement ensures that only those investments that comply with Jordan's local laws will be given treaty protection.</p>	<p>characteristics in the Colombia – Turkey BIT do not include the “contribution to the development of the host state” requirement. The inclusion of such a characteristic is important to signal the host country's desire to give protection to beneficial investments. “This would have the advantage of making clear that the policy of the treaty is not just investor and investment protection, but also the protection of the legitimate expectation of the host country that the investment will make a contribution to economic development.”⁶³ This approach has been adopted in the new Indian Model BIT, which requires “<i>significance [of the investment] for the development of the country where the investment is made.</i>”⁶⁴</p>

⁶¹ Lahra Liberti, Intellectual Property Rights in International Investment Agreements: An Overview 10 (2010/01 OECD Working Papers on International Investment ed., OECD Publishing 2010).

⁶² Colombia - Turkey BIT (2014).

⁶³ SCOPE AND DEFINITION - UNCTAD Series on Issues in International Investment Agreements II, at 120 (2011).

⁶⁴ India Model BIT (2016).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
		<p>5) Finally, Jordan can exclude some investment projects that may fall under the open-asset based definition, but are not FDI, such as portfolio investments (and other forms of indirect investment). The risks imposed by portfolio investments and other financial papers (being highly volatile and short-term) and the possibility of having the host state engage in investor-state arbitrations with indirect investors pose greater risks than the advantages these sorts of indirect investments may bring. Therefore, in Jordan's situation, it is advisable to explicitly exclude portfolio investments and other financial papers from the ambit of covered investments in its model BIT.</p> <p>6) Finally, Jordan is encouraged to adopt a development-based definition of investment. This is a supplementary requirement that necessitates that a foreign investment must contribute to the development of the host state to be given protection.</p>	

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
<p>Definition of Investor</p>	<p>The definition of Investor determines the natural and juridical persons that are entitled for treaty protection. The definition also plays an important role in ICSID jurisdiction.</p> <p>Typically, BITs use the nationality test for natural persons, and the place-of-incorporation test for juridical persons. The place-of-incorporation test for juridical investors may give protection to mailbox companies that have no real economic ties with the country of incorporation. These shell companies can be established in the home state for the sole purpose of benefiting from the BIT. Hence, the place-of-incorporation test creates room for treaty shopping by host state nationals or investors from third countries, who - in regular circumstances - are not entitled to benefit from the BIT.</p>	<p>1) The approach taken when defining “investor” should be tied with the approach taken when defining “investment.” If Jordan is to adopt an open asset-based definition for investments because of its policy of attracting a wide range of FDI, then it should adopt the place-of-incorporation definition for “investors.” This definition is easy to satisfy, giving a wide range of investors the ability to take advantage of the treaty; thus, it complements the approach followed in the definition of “investment.” Although the place-of-incorporation definition may create the opportunity for treaty shopping, a country like Jordan, which is striving for FDI, might not consider this an issue, as long as it receives the investment that complies with the definition set of “investments.”</p> <p>2) To overcome the possibility of treaty shopping, Jordan may also require foreign investors to have substantial business activities in the home country to benefit from treaty protection. It can require so in the definition itself or by including a “denial of benefits” clause in the investment treaty. This will prevent treaty shopping and consequently manage its exposure to investment claims.</p>	<p>The new Indian Model BIT adopts a similar approach to the one recommended here for Jordan.⁶⁵ The Model BIT defines an investor as: “A legal entity constituted, organized and operated in compliance with the Law of the Home State, owned or controlled by a Natural Person or a legal entity of the Home State and conducting real and substantial business operations in the Home State.” Thus, the Indian Model BIT adopts a place-of-incorporation definition that requires i) ownership or control by nationals of the home state, and ii) substantial business activities in the home state.</p> <p>The COMESA Agreement adopts a set of criteria to determine whether an investor has “substantial business activity” in the home state. These criteria are: i) <i>the amount of investment brought into the country</i>; ii) <i>the number of jobs created</i>; iii) <i>its effect on the local community</i>; and iv) <i>the length of time the business has been in operation</i>.⁶⁶</p> <p>The Indian Model BIT defines “control” as the investor’s right to “appoint a majority of the directors or senior management officials or to control the management or policy</p>

⁶⁵ Id. at “Investor.”

⁶⁶ Article 1(4)(ii) of the Investment Agreement For the COMESA Common Investment Area (2007).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
		<p>3) Another limitation can be added to the definition to reduce the possibility of treaty shopping under the place-of-incorporation definition: the requirement of “control.” Under this requirement, the foreign investor must be controlled by nationals of the home country to benefit from the BIT. Thus, a juridical investor not controlled by nationals of the home country, although incorporated in the home country, will not qualify for treaty protection.</p>	<p><i>decisions of such Enterprise.” It also defines ownership as the investor’s ownership of “more than 50% of the capital or funds or contribution in the Enterprise.”</i></p> <p>In regards to natural investors, the Japan - Uruguay BIT adopts a flexible definition.⁶⁷ It prohibits dual nationals from benefiting from the treaty; however, a caveat is included that allows natural persons who are nationals of both contracting parties to benefit from the BIT if “<i>such natural persons have at the time of the investment and ever since been domiciled outside the Area of the Contracting Party in which they made such investments.</i>” This caveat allows dual nationals who have no real economic ties with the host state to benefit from the treaty, even though they hold the nationality of the host state.</p> <p>The denial of benefits clause in the Indian Model BIT allows the host state to deny treaty benefits -even after the constitution of arbitral proceedings - to investors or investments that are i) “<i>owned or controlled, directly or indirectly, by persons of a non-Party or of the Host State, or ii) been established or restructured with the primary purpose of</i></p>

⁶⁷ Japan - Uruguay BIT (2015).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
Treatment Standards: National Treatment (NT)	<p>The purpose of the NT standard is to provide a level playing field to foreign investors by ensuring that the host state will not make any negative differentiation between foreign and national investors through its laws or administrative actions.⁶⁹</p> <p>However, the NT standard - being of a relative nature - requires comparison with the treatment received by local investors in “like circumstances.” Thus, host governments will have to regularly study the effects of any measures they wish to introduce on foreign and domestic investors to determine</p>	<p>1) The Jordanian Model BIT should offer NT in the post-establishment stage of the foreign investment to preserve its ability to screen incoming FDI. However, an exception to that should be made to FDI in the energy and water sectors. This exception will emphasize the importance of projects in these sectors to the country and encourage their inflow. The exceptions to post-establishment NT (energy and water related FDI) should be made through a positive list approach, where these sectors are explicitly and exclusively given pre-establishment NT rights.</p> <p>2) Jordan can also require that the foreign investments be established and operated in accordance with the laws of the host country to</p>	<p><i>gaining access to the dispute resolution mechanisms”</i> provided for in the BIT.⁶⁸ Adopting a similar denial of benefits clause in the Jordan model BIT is recommended to eliminate the possibility of giving treaty protection to foreign investors who are not entitled to it.</p>
			<p>The COMESA Agreement provides for post-establishment NT, which promises “<i>investors and their investments treatment no less favourable than the treatment it accords, in like circumstance, to its own investors and to their investments.</i>”⁷⁰ The second paragraph of this article lists the criteria that must be considered when determining the “like circumstances” requirement. These are the effects of the measures on: “<i>i) third persons and the local community; ii) on the local regional or national environment, including the cumulative effects of all investments within a jurisdiction on the environment; iii) the sector the investor is in; iv) the aim of the measure concerned; v) the regulatory process generally applied in relation to the measure</i></p>

⁶⁸ Article 20.1 of the India Model BIT (2016).

⁶⁹ See RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 198 (Oxford University Press 2 ed. 2012).

⁷⁰ See Article 17 of the Investment Agreement For the COMESA Common Investment Area (2007).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
	<p>if the proposed measures result in differential treatment. What adds to this problem is the fact that the “like circumstances requirement” is not defined, and hence is applied subjectively by different tribunals.</p> <p>Additionally, the NT standard can impede host countries from pursuing legitimate public policy objectives that discriminate against foreign investors, such as the protection of infant industries in the host state, or taking discriminatory measures in times of emergency and crises to preserve national interests.</p> <p>Finally, some treaties offer NT at the pre-establishment stage of the investment. By giving foreign investments a right of entry to the host state, the host country loses its ability to screen incoming FDI.</p>	<p>enjoy national treatment protection.</p> <p>3) Jordan should also make exclusions and reservations to some economic sectors and industries that do not qualify for NT. This approach is usually taken to protect and enhance national infant entrepreneurs and natural resources by giving them governmental loans and subsidies that are not given to foreign investors.</p> <p>4) Inserting a requirement that comparison for NT purposes should be made with national investors who are in “like circumstances” with the foreign investor. This requirement should be coupled with a list of subjective criteria that clarify and refine what a suitable comparator (national investors in “like circumstances”) should be.</p> <p>5) Insert explicit reservations to the host state’s right to impose legitimate non-discriminatory public purpose measures.</p>	<p><i>concerned; and vi) other factors directly relating to the investment or investor in relation to the measure concerned.”</i></p> <p>The Morocco – Nigeria BIT also adopts these criteria.⁷¹</p> <p>Some recent treaties exclude certain sectors from the ambit of the NT obligation; for example, the Japan – Kenya BIT provides that NT shall not apply “to measures adopted or maintained by a Contracting Party with respect to incentives only for the purpose of promoting small and medium sized enterprises in its Area.”⁷² Jordan may want to add some sectors where it may not want to extend NT, such as agriculture projects that are subsidized by the Jordanian government.</p> <p>Some recent treaties have started to include exceptions relating to the right of the BIT parties to take “any actions that it considers necessary for the protection of its essential security interests,” and other measures “taken in time of war or other emergency in international relations.”⁷³ Such exceptions</p>

⁷¹ Morocco - Nigeria BIT (2016).

⁷² Article 3(3) of the Japan – Kenya BIT (2016). This approach has been also adopted in the Morocco - Italy BIT (1990) which states in Article 3(3) “Investors of the two Contracting Parties shall not be entitled to national treatment in terms of benefiting from aid, grants, loans, insurance and guarantees accorded by the Government of one of the Contracting Parties exclusively to its own nationals or enterprises within the framework of activities carried out under national development programs.” See also the Netherlands – Jamaica BIT (1991) at Article 3(6).

⁷³ E.g. Article 5(2) of the Rwanda - Turkey BIT (2016).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
		<p>6) Insert general reservations that preserve the host country's ability to take measures that may discriminate against foreign investors but will protect the essential interests of the host state in situations of emergency and crisis.</p> <p>7) Finally, Jordan can qualify or limit the NT obligation by inserting a "development exception." Under this exception, the host state is entitled to offer its domestic investors certain advantages and benefits that are designed to enhance its national development.</p>	<p>disable the NT obligation on the host state. Hence, Jordan is advised to adopt similar exceptions to its NT obligation.</p> <p>The Norwegian Model BIT adopts a development exception, which allows Norway to take discriminatory measures that preserve its national interests and development objectives even if these measures breach the NT obligation. It states "<i>The Parties agree/ are of the understanding that a measure applied by a government in pursuance of legitimate policy objectives of public health, human rights, labour rights, safety and the environment, although having a different effect on an investment or investor of another Party, is not inconsistent with national treatment and most favoured nation treatment when justified by showing that it bears a reasonable relationship to rational policies not motivated by preference of domestic over foreign owned investment.</i>"⁷⁴ It is worth mentioning that this test was adopted in the <i>Pope & Talbot v. Canada</i> case,⁷⁵ before its inclusion in the Norway Model BIT.</p>

⁷⁴ Norway Model BIT n.1 (2015).

⁷⁵ *Pope & Talbot Inc v The Government Of Canada* para. 79 (Award on the Merits of Phase 2), (NAFTA, 2001).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
<p>Treatment Standards: Most-Favored-Nation (MFN)</p>	<p>The MFN standard eliminates nationality based discrimination and favoritism between different foreign investors in the host state.</p> <p>However, the vague and loose ended MFN clauses typically included in BITs has allowed foreign investors to import more favorable dispute resolution procedures from other treaties – thus exposing the host state</p>	<p>1) Jordan should limit the scope of MFN protection to post-establishment activities. However, it can grant energy and water related FDI pre-establishment MFN treatment to encourage such investments. However, as with the NT, these exclusions should be made via a positive list approach.</p> <p>2) Explicitly exclude the dispute resolution articles of the investment treaty from MFN protection.⁷⁷ It would be more effective if the</p>	<p>Finally Jordan may want to define “treatment” and/or “measures” that will (or will not) breach the NT standard. This gives certainty and guidance to future tribunals as to what measures breach the NT standard. Such definitions have been adopted in the TPPA.⁷⁶</p> <p>The TPPA grants post-establishment MFN treatment that requires comparison with national investors in “like circumstances,”⁷⁹ although the TPPA does not provide the criteria required to determine a similar comparator as the COMESA agreement.⁸⁰</p> <p>Nonetheless, the TPPA explicitly excludes procedural provisions from the protection of the MFN clause. Article 9.5 reads “<i>For greater certainty, the treatment referred to in</i></p>

⁷⁶ E.g. “The following shall, in particular, be deemed ‘treatment less favourable’ within the meaning of this Article: unequal treatment in the case of restrictions on the purchase of raw or auxiliary materials, of energy or fuel or of means production or operation of any kind, unequal treatment in the case of impeding the marketing of products inside or outside the country, as well as any other measures having similar effects. Measures that have to be taken for reasons of public security and order, public health or morality shall not be deemed ‘treatment less favourable’ within the meaning of this Article.” Article 3(2) of the Egypt - Germany BIT (2005).

⁷⁷ E.g. “For greater certainty, notwithstanding any other Bilateral Investment Agreement the Contracting Parties have signed with other States before or after the entry into force of this Agreement, the most favored national treatment shall not apply to procedural or judicial matters.” Article 3(3) of the UAE - Mexico BIT (2016).

⁷⁹ See Article 9.5 of the Trans Pacific Partnership Agreement (TPPA) (2016).

⁸⁰ See Article 17(2) of the Investment Agreement For the COMESA Common Investment Area (2007).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
	<p>to international arbitration in an unanticipated manner. This has also allowed foreign investors to “cherry-pick” the dispute resolution provisions that are most suitable to their situation.</p> <p>The typical MFN clause may also allow the importation of treatment standards that do not exist in the basic treaty. Also, foreign investors may be able to remove exclusions and limitations in the basic treaty, by referring to third party treaties that do not contain such limitations.</p>	<p>MFN clause enumerates the articles that it covers.</p> <p>3) Explicitly exclude all previous investment treaties from the coverage of the MFN protection to ensure that foreign investors will not try to benefit from more favorable treatment provisions the host state has concluded in the past.</p> <p>4) Explicitly exclude all past and future taxation, regional integration, customs unions, free trade agreements, and the like from the coverage of MFN protection.</p> <p>5) Similar to NT, Jordan should insert general reservations that preserve the host country’s ability to take measures that may discriminate between foreign investors but protect the essential interests of the host state in situations of emergency and crisis. In addition, it should insert explicit reservations to the host state’s right to impose legitimate non-discriminatory public purpose measures.⁷⁸</p>	<p><i>this Article does not encompass international dispute resolution procedures or mechanisms, such as those included in Section B (Investor-State Dispute Settlement).</i>⁸¹</p> <p>The COMESA Agreement excludes “i) any customs union, free trade area, common market or monetary union, or any similar international conventional or other forms of regional preferential arrangements, present or future, of which any of the Member States is or may become a party; or ii) any matter, including international agreements, pertaining wholly or mainly to taxation,”⁸² from the ambit of MFN protection.</p> <p>The Commonwealth Secretariat recommends the exclusion of all pre-existing BITs and other agreements from MFN coverage.⁸³ It also suggests limiting MFN to <i>de jure</i> discrimination,⁸⁴ although no investment treaty to date has adopted this approach.</p>

⁷⁸ The Norwegian Model BIT (2015) adopts this approach. See this point in national treatment above.

⁸¹ Article 9.5(3) of the Trans Pacific Partnership Agreement (TPPA) (2016).

⁸² See Article 19 of the Investment Agreement For the COMESA Common Investment Area (2007).

⁸³ PENELOPE SIMONS J ANTHONY VANDUZER, GRAHAM MAYEDA, INTEGRATING SUSTAINABLE DEVELOPMENT INTO INTERNATIONAL INVESTMENT AGREEMENTS: A GUIDE OF DEVELOPING COUNTRY NEGOTIATORS 135 (Commonwealth Secretariat. 2013).

⁸⁴ Id. at 134.

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
		<p>6) Explicitly exclude the sectors, industries, and non-conforming measures the host state wishes to maintain, and reserve a regulatory space to treat foreign investors differently (without discrimination) in accordance with its development objectives and needs.</p>	
<p>Treatment Standards: Fair and Equitable Treatment (FET)</p>	<p>The FET standard ensures that foreign investors are protected from situations of unjust treatment by the host state that do not fall within the domain of other specific treatment standards, such as NT or MFN. It is an important protection standard for foreign investors; however, its application in arbitral practice has been criticized of imposing a threat to the host state's right to regulate.</p> <p>The short, vague, and unqualified formation of the FET standard currently adopted in a vast number of BITs raises the following issues:</p>	<p>The FET standard is the most relevant standard to the host state's right to regulate and pursue its development objectives without being hindered by investment protection standards. Hence, the drafting of this standard in the Jordanian BIT should be given extra care and time.</p> <p>This thesis suggests a straightforward elimination of the FET standard. Basically, the Jordan model BIT should not refer to, or use the terms, "fair and equitable." Rather, it is proposed here that Jordan break down the contents and elements of the FET standard and specify precisely which of these elements are protected in its model BIT. This allows for a smaller margin of expansive interpretations by arbitral tribunals, and at the same time, identifies the content and elements that are</p>	<p>In its publication regarding the FET standard, UNCTAD suggests different options for host countries regarding the FET standard.⁸⁶ The recommended options are a qualified FET standard, or no FET standard <i>per se</i>. In the latter option it suggests a list of prohibited state actions that breach the FET standard, although not explicitly mentioning "fair and equitable" in its suggested clause. The prohibited state actions include: i) <i>denial of justice and flagrant violations of due process</i>; ii) <i>manifestly arbitrary treatment</i>; iii) <i>evident discrimination</i>; iv) <i>manifestly abusive treatment involving continuous, unjustified coercion or harassment</i>; and v) <i>Infringement of legitimate expectations based on investment-inducing representations or measures, on which the investor has relied</i>.⁸⁷</p>

⁸⁶ UNCTAD, Fair and Equitable Treatment § II (UNCTAD Series on Issues in International Investment Agreements ed., United Nations 2012).

⁸⁷ Id. at 108-09.

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
	<p>1) Host governments cannot be sure of the level of deference they will be given in the event of a dispute (i.e. liability threshold). Hence, the outcomes of FET breach claims in investor-state arbitrations are unpredictable.</p> <p>2) The typical FET formulation gives a wide margin for foreign investors and tribunals to extend the standard over legitimate state measures that serve a public or developmental goal.</p> <p>3) There is no clear definition of content and elements protected under the FET standard. Hence, it is difficult for host governments and interpreters to draw the boundaries of the obligation to provide FET treatment and to develop a consistent interpretation.</p> <p>4) Protecting the expectations of the</p>	<p>protected, leaving no room for investors and arbitral tribunals to widen the scope of protection. Although such an approach may require a long and detailed FET provision, it will, however, qualify, clarify, and narrow the standard, making its application easier and more predictable:</p> <p>1) The FET provision in the model BIT should flesh out the elements that Jordan is willing to protect. It would more effectively, in the view of this thesis, to describe and list the prohibited state actions that breach the FET standard. The description of prohibited state actions should be drafted in a way that gives a degree of deference and severity to state actions that breach the FET obligation. A modified version of the <i>Neer</i> standard is recommended in this regard.⁸⁵</p> <p>2) In addition, it should be clear within the drafting of the clause that legitimate expectations of the investor are protected. However, these expectations should be weighed against the principles of business risk and due</p>	<p>Alternatively, the Iran – Slovak BIT uses the terms “fair and equitable,” although it conditions the breach of the FET standard on a set of prohibited state actions similar to those suggested by UNCTAD.⁸⁸ Article 3(2) of the Iran – Slovak BIT provides that “a breach of the obligation of fair treatment referenced in paragraph 1 may be found only where a measure or series of measures constitutes,” and proceeds to list the prohibited state actions.⁸⁹</p> <p>UNCATD suggests a substitute formulation that makes no reference to the terms “fair and equitable” and provides clear language that ties the protection of investors’ legitimate expectations with business risk and the host country’s policy objective. The suggested clause reads: <i>Each Party shall abstain from treating investors and their investments in a manner that is manifestly arbitrary, discriminatory or abusive. It shall not deny justice in any legal or administrative proceedings or otherwise flagrantly violate</i></p>

⁸⁵ The tribunal in the *Neer* case required government actions that breach the international minimum standard to amount to “an outrage, to bad faith, to willful neglect of duty, or to an insufficiency of government action so far short of international standards that every reasonable and impartial man would recognize its insufficiency.” See L. F. H. Neer and Pauline Neer (U.S.A.) v United Mexican States, United Nations Reports of International Arbitral Awards IV 60, para. 3 (General Claims Commission, 1926).

⁸⁸ Slovak – Iran BIT (2016).

⁸⁹ Id. at art. 3(2).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
	<p>foreign investor is a burdensome task on the host state in light of its need to constantly review and amend its national legislation in accordance with its evolving policies and objectives. However, it is also unfair to not protect the presumptions that the foreign investor relied upon when making the investment. Hence, there needs to be a balance of both interests involved.</p>	<p>diligence, along with the right of the state to regulate in its best interest.</p> <p>3) Finally, three important exceptions are suggested to further limit and clarify the FET obligation:</p> <p>i) preserve Jordan’s ability to regulate and take measures that serve a legitimate public / developmental goal, provided that such measures are not taken in a discriminatory or arbitrary fashion,</p> <p>ii) acknowledge that Jordan is a developing country and that its level of development should be taken into consideration when claims of breach of FET treatment arise, and</p> <p>iii) that a breach of any treatment standard in the BIT does not entail an automatic breach of the FET standard.</p>	<p><i>due process.</i></p> <p><i>[Neither Party shall infringe legitimate expectations based on investment-inducing representations or measures, on which the investor has relied when making an investment. In this respect, the investor’s conduct and accepted business risk in the territory of the Party concerned should be taken into account when determining the legitimate expectations of the investor].⁹⁰</i></p> <p>The Nigeria – Singapore BIT includes an exception regarding the level of development of each party and its relation in the assessment of FET breaches. The exception reads “<i>In applying this article, Parties understand that they have different forms of administrative, legislative, and judicial systems and are at different levels of development and may not achieve the same standard at the same time.</i>”⁹¹ The COMESA agreement adopts a similar exception, but also adds that due to the different development levels of its parties, the FET obligation does “<i>not establish a single international standard in this context.</i>”⁹² This makes the severity level in state actions</p>

⁹⁰ UNCTAD, Fair and Equitable Treatment § II, at 109 (Agreements ed., United Nations 2012). See also Article 8.10 of the Comprehensive Trade and Economic Agreement between Canada and the European Union.

⁹¹ Article 3(4) of the Nigeria – Singapore BIT (2016).

⁹² Article 14(3) of the Investment Agreement For the COMESA Common Investment Area (2007).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
			<p>required for a breach of the FET standard to be found dependent on the host state's level of development.</p> <p>In regards to the protection of investor's expectations, the TPPA gives leverage to its parties by stipulating that <i>"the mere fact that a Party takes or fails to take an action that may be inconsistent with an investor's expectations does not constitute a breach of this Article, even if there is loss or damage to the covered investment as a result."</i>⁹³</p> <p>The right of the host state to take measures in pursuit of its public policy and development objectives can either be added in the FET standard as an exception, or can be added as a standalone provision in Jordan's model BIT as a general exception that applies to all treatment standards. This thesis is of the view that a standalone provision is more efficient than including this exception with each treatment standard. Such a provision is discussed below.</p>

⁹³ Article 9.6(4) of the Trans Pacific Partnership Agreement (TPPA) (2016).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
Dispute Resolution	<p>The dispute resolution provision governing investor-state disputes is one of the most important provisions in any BIT. Usually, BITs provide for arbitration as a method for dispute resolution under the auspices of the ICSID Convention.⁹⁴</p> <p>However, the increased use of investor-state dispute settlement (ISDS) by foreign investors, coupled with the inconsistent and sometimes contradictory decisions of tribunals have raised concerns for host states. Australia, Germany, and South Africa, for example, have announced their intention to not include ISDS clauses in their future BITs.⁹⁵</p> <p>The overuse of ISDS by foreign investors can contribute to the creation of a “regulatory chill” effect in the host state. Additionally, the ISDS is a costly and time-consuming</p>	<p>The ISDS provision in the model BIT for Jordan should be both limited and precise. This can happen by adding the following to the ISDS provision:</p> <ol style="list-style-type: none"> 1) Insert “cool-off” periods where the foreign investor must engage in amicable settlement efforts with the government for a certain period to attempt to resolve the issue amicably before resorting to ISDS. 2) Require the exhaustion of local remedies in the host state before allowing recourse to ISDS. This allows the host state, through its local administrative and judicial branches, to rectify any breach to the BIT at an early stage, avoiding ISDS. 3) Limit the jurisdiction of ISDS tribunals to review disputes arising solely from the substantive provisions of the BIT (i.e. treatment standards). Such a limitation will exclude disputes arising from other legal documents (i.e. investment contracts, however this also requires 	<p>The Canada – Hong Kong BIT includes a detailed and precise ISDS clause.⁹⁶ The clause requires the parties to “<i>hold consultations and attempt to settle a claim amicably before an investor may submit a claim to arbitration.</i>”⁹⁷ The ISDS clause in the said BIT stipulates that the consultations shall be held within 60 days, unless the disputing parties agree to a longer period.⁹⁸</p> <p>The Norwegian Model BIT explicitly requires foreign investors to seek local remedies before submitting a claim to ISDS.⁹⁹ It provides in Article 15(3) that an investor is entitled to submit a claim to arbitration when “<i>agreement cannot be reached between the parties to this dispute within 36 months from its submission to a local court for the purpose of pursuing local remedies, after having exhausted any administrative remedies.</i>” Similarly, the SADC Model BIT recommends adopting a provision that requires the exhaustion of local remedies as a precondition to initiating ISDS proceedings. The suggested</p>

⁹⁴ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965).

⁹⁵ Lise Johnson & Lisa Sachs, *International Investment Agreements, 2013: A Review of Trends and New Approaches*, in YEARBOOK OF INTERNATIONAL INVESTMENT LAW AND POLICY, 2013-2014, at 29 (Andrea K. Bjorklund ed. 2014).

⁹⁶ Canada - Hong Kong BIT (2016).

⁹⁷ Id. at art. 21(1).

⁹⁸ Id. at art. 21(1).

⁹⁹ Norway Model BIT (2015).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
	<p>process on the host state that imposes an extra burden on the host state's administrative resources.</p> <p>One the other hand, ISDS has been a successful tool in protecting investor rights. Hence eliminating ISDS provisions from BITs can severely impact the global flow of capital, especially to developing countries, and the withdrawal of current FDI from developing host countries. In addition, the ISDS clause makes the host state more diligent in its dealings with foreign investors and induces it to make reforms in its administrative and judicial branches to avoid disputes and liability to foreign investors. Thus, not including an ISDS clause may have a negative consequence on the overall development of the host state.</p>	<p>not including an umbrella clause in the BIT). This limitation also serves to confine the jurisdiction of the ISDS tribunal to breaches of treatment standards and not any other provision in the BIT. Hence, language such as “any dispute relating to an investment” or “any matter relating to an investment” should be avoided in the ISDS provision.</p> <p>4) Limit the jurisdiction of ISDS tribunals to review disputes arising from investments that are established and operated in conformity with host state's local laws. Such a limitation will exclude investments that are not respectful of Jordan's laws, or investments that are involved in corruption and/or in breach of international conventions relating to the protection of human rights, environment, labor and the like.</p> <p>5) Insert time limitations where, once passed, the foreign investor shall lose its right to submit the dispute to ISDS (i.e. statute of limitations).</p> <p>6) Explicitly prohibit access to ISDS where an investment authorization or a contract includes a choice of forum clause for the resolution of disputes pertaining to that investment, authorization, or contract (this point applies if</p>	<p>text requires an investor to submit “a claim before the domestic courts of the Host State for the purpose of pursuing local remedies, after the exhaustion of any administrative remedies, relating to the measure underlying the claim under this Agreement, and a resolution has not been reached within a reasonable period of time from its submission to a local court of the Host State.”¹⁰⁰</p> <p>On the other hand, The ASEAN Agreement allows the foreign investor to proceed directly to initiate ISDS proceedings in any fora provided in the treaty (ICSID, UNCITRAL, or local courts,) albeit conditioning that recourse to one forum precludes the investor from using any of the other fora provided in the treaty (i.e. no U-turn model).¹⁰¹</p> <p>As to the issues that can be submitted to ISDS, the ASEAN Agreement adopts an approach of specifying (and enumerating) those treaty provisions that can be claimed as breached in ISDS proceedings. Article 20(1) of the ASEAN Agreement reads: “<i>This Article shall apply to investment disputes between a Party and an investor of another Party concerning an alleged breach of an obligation</i></p>

¹⁰⁰ See Article 29.4(b)(i) of the SADC Model Bilateral Investment Treaty Template with Commentary (Community ed., 2012).

¹⁰¹ Article 20(3) of the Agreement on Investment under the Framework Agreement on Comprehensive Economic Cooperation between the Association of Southeast Asian Nations and the Republic of India (2014).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
		<p>an umbrella clause is included in the model BIT).</p> <p>7) Finally, it is recommended that Jordan adds a provision to the ISDS clause that allows the disputing parties to agree to resort to other dispute resolution methods (such as mediation) at any time, even after the initiation of ISDS proceedings.</p>	<p><i>of the former Party under Article 3 (National Treatment), Article 7 (Treatment of Investment), Article 8 (Expropriation and Compensation), Article 9 (Compensation for Losses) and Article 11 (Transfers), which causes loss or damage to the investor in relation to its investment as referred to in subparagraph 1 (b) of Article 1 (Scope) with respect to the management, conduct, operation, or sale or other disposition of such investment.”</i>¹⁰²</p> <p>The same article continues to prohibit claims relating to disputes existing before the entry of the BIT, or those that have been previously settled.</p> <p>The SADC Model BIT recommends adding a provision that excludes any “investment authorization or a contract [which] includes a choice of forum clause for the resolution of disputes pertaining to that investment or the authorization or contract” from arbitration under the BIT, if “the underlying measure in the arbitration would be covered by such a choice of forum clause.”¹⁰³</p> <p>Finally, the recently concluded Canada – EU CETA denies ISDS proceedings to any</p>

¹⁰² Article 20(1) of the id. at.

¹⁰³ Article 29.9(b) of the SADC Model Bilateral Investment Treaty Template with Commentary (Community ed., 2012).

Article	Discussion of existing issues	Notes for the Model BIT for Jordan	Examples and Recommendations
			<p>investor “if the investment has been made through fraudulent misrepresentation, concealment, corruption, or conduct amounting to an abuse of process.”¹⁰⁴ This prohibition allows only those investments that conform to the host state’s local laws to submit claims in ISDS proceedings. Also, the CETA allows the disputing parties “to have recourse to mediation” at any time, even if the ISDS proceedings have been initiated.¹⁰⁵</p>

¹⁰⁴ Article 8.18(3) of the Comprehensive Trade and Economic Agreement between Canada and the European Union (2016).

¹⁰⁵ Article 8.20(1) of the id. at.

Suggested Reservations and Exclusions in the Jordan Model BIT

Article	Discussion	Recommendations
Investor's Obligations	<p>Most BITs set out obligations for the host state with no corresponding obligations on the foreign investor. However, the BIT is a tool designed to protect foreign investment and enhance the development of the host state.</p> <p>To achieve the latter goal, foreign investors and their investments should be subject to certain obligations and responsibilities that assist the host country in reaching its desired level of development. These obligations include adopting the best practices in the investment's respective industry by using the latest and environmentally safe technologies, adhering to international polices, conventions, and compliance with international standards that ensure transparency, social responsibility, and other similar obligations.</p> <p>Another issue is adding a requirement that the investment contributes to the host state's development. This addition will signal the host state's main objective of attracting FDI, and dictates a development-oriented interpretation of the treaty's treatment standards. The issue is, however, how such a contribution will be assessed and measured. Different investments contribute</p>	<p>Jordan should insert obligations on foreign investors to help its development. The following recommendations and examples can help policy makers and negotiators in drafting these obligations and requirements:</p> <ol style="list-style-type: none"> 1) Require that investors comply with Jordan's local laws at both the pre-entry and the post-entry stage of an investment. Foreign investors and investments that do not comply with this requirement can be sanctioned by: <ol style="list-style-type: none"> i) denying them treaty protection, ii) requiring tribunals to consider investor conduct when interpreting treatment standards, and iii) provide for Jordan's right to bring counterclaims in ISDS arising from investors' violations of its local law. 2) Require investors to adopt best practices and corporate governance principles, and endeavor to contribute to the development of the host state (Jordan).¹⁰⁶ The Iran – Slovak BIT adopts a provision to this effect. It reads “<i>Investors and investments should apply national, and internationally accepted, standards of corporate governance for the sector involved, in particular for transparency and accounting practices. Investors and their investments should strive to make the maximum feasible contributions to the sustainable development of the Host State and</i>

¹⁰⁶ Slovak – Iran BIT (2016).

Article	Discussion	Recommendations
	<p>in different ways to the host state's economy. For this reason, some recent treaties use a "best efforts" obligation on investors to contribute to the host state development. It is recommended to include clear language that stipulates the host state's requirement of contribution to its development, whether it is a compulsory or best efforts obligation.</p>	<p><i>local community through appropriate levels of socially responsible practices.</i>"¹⁰⁷ Similarly the Canada – Burkina Faso BIT requires the contracting parties to encourage foreign investors to adopt internationally recognized principles of corporate governance and other principles related to human rights, labor, and anti-corruption. Article 16 of the said BIT reads: "Each Party should encourage enterprises operating within its territory or subject to its jurisdiction to incorporate internationally recognized standards of corporate social responsibility in their practices and internal policies, such as statements of principle that have been endorsed or are supported by the Parties. These principles address issues such as labour, the environment, human rights, community relations and anti-corruption."¹⁰⁸</p>
<p>Host State Exceptions</p>	<p>Jordan is advised to make explicate reservations that preserve its rights to regulate and apply measures that pursue a legitimate public policy or development goal. Of course, these reservations should not be used as a disguise to discriminate against foreign investors or cause harm to their investments through arbitrary and unjustified measures. Rather, the reservations preserve Jordan's right to maintain its political, economic, and social security and interests. They should also preserve Jordan's right to take measures in times of emergency and crises. Hence, it is important that these reservations be purpose-restricted to assure foreign investors that such reservations are only used for a legitimate public</p>	<p>The Iran – Slovak BIT contains a reservation that allows the contracting parties to take measures that preserve their interests. It states "Subject to the requirement that such measures are not applied in a manner that would constitute arbitrary or unjustifiable discrimination between investments or between investors, nothing in this Agreement shall be construed to prevent the Contracting Party from adopting or enforcing measures necessary: a) to protect public security or public morals or to maintain public order; b) to protect human, animal or plant life or health; c) to ensure compliance with laws and regulations; or d) for the conservation of living or non-living exhaustible natural resources."¹⁰⁹</p>

¹⁰⁷ Id. at art. 10(3).

¹⁰⁸ Article 16 of the Canada – Burkina Faso BIT (2016).

¹⁰⁹ Slovak – Iran BIT (2016). Article 11.1

Article	Discussion	Recommendations
	<p>purpose and will not be used as a tool to infringe treatment standards without liability to investors. The process of enacting and applying public policy related regulations and measures should be both legitimate and transparent. This requires Jordan to adopt a broader reform policy on all levels and branches of the government.</p> <p>In addition, Jordan should insert exceptions to non-conforming measures that breach the BIT. Usually states reserve their right to maintain some measures that breach the BIT but are necessary for the host state. BITs usually express these exceptions in an annex attached to the BIT.</p>	<p>Similarly, the Hong Kong – Chili BIT provides that “<i>Nothing in this Agreement shall be construed to prevent a Party from adopting, maintaining, or enforcing any measure otherwise consistent with this Agreement that it considers appropriate to ensure that investment activity in its area is undertaken in a manner sensitive to environmental, health or other regulatory objectives.</i>”¹¹⁰ Additionally, the same BIT allows a contracting party to take any action “<i>that it considers necessary to protect its essential security interests,</i>” including measures taken “<i>in time of war or other emergency in international relations.</i>”¹¹¹</p> <p>Some treaties, after the Argentinean Peso crisis, started to include an exception that allows the host country to adopt necessary measures that preserve its financial and monetary systems without liability to foreign investors. For example, one treaty provides: “<i>This Agreement does not apply to non-discriminatory measures of general application taken by a public entity in pursuit of monetary and related credit or exchange rate policies.</i>”¹¹²</p> <p>Finally, non-conforming measures that the host state wishes to keep in effect after the conclusion of the BIT should be excluded. The language of the exclusion should identify: i) the non-conforming measure(s), and ii) what treatment standard(s) they are excluded from. For example: “<i>Articles 4 (National Treatment), 5 (Most-Favoured-Nation Treatment), 8 (Senior Management, Board of Directors and Entry of Personnel) and 9 (Performance Requirements) shall not apply to any measure that a Party adopts or</i></p>

¹¹⁰ Article 15 of the Hong Kong – Chili BIT (2016).

¹¹¹ Id. at art. 6(6) and 6(b)(iii).

¹¹² Article 18(3) of the Canada – Burkina Faso BIT (2016).

Article	Discussion	Recommendations
		<p><i>maintains with respect to sectors, subsectors or activities, as set out in its schedule to Annex II (Reservations for Future Measures).¹¹³</i></p>
<p>Performance Requirements</p>	<p>Within the framework of its development objectives, Jordan may decide to impose “performance requirements” on foreign investors. Performance requirements are “stipulations, imposed on investors, requiring them to meet certain specified goals with respect to their operations in the host country.”¹¹⁴</p> <p>As a member of the WTO, Jordan is prohibited from imposing performance requirements relating to export quotas.¹¹⁵ However, Jordan may insert performance requirements relating to other matters, such as the use of local labor, the performance of certain services for local communities, or the use of local input materials.¹¹⁶ These performance requirements align with the development challenges in Jordan, such as its high unemployment rate and need for the transfer of skills and know-how, especially in the energy and water sectors.</p>	<p>The Canada – EU CTEA provides that a contracting party may impose certain performance requirements that have development purposes. Article 8.5 reads: “Paragraph 2 does not prevent a Party from conditioning the receipt or continued receipt of an advantage, in connection with an investment in its territory, on compliance with a requirement to locate production, provide a service, train or employ workers, construct or expand particular facilities, or carry out research and development in its territory.”¹¹⁷</p> <p>Other model treaties go further to allow the host country to impose employment quotas for its nationals in FDI projects. The SADC Model BIT, for example, provides that “a State Party may require an Investor of the other Party or its Investment, in keeping with its size and nature, to have progressive increases in the number of senior management, executive or specialized knowledge positions that nationals of the Host State occupy; institute training programs for the purposes of achieving the increases set out in the preceding paragraph and to Board of Director positions; and to establish mentoring programs for this purpose.”¹¹⁸</p>

¹¹³ Id. at art. 17(2).

¹¹⁴ UNCTAD, Foreign Direct Investment and Performance Requirements: New Evidence From Selected Countries § UNCTAD/ITE/IIA/2003/7, at 2 (UNCTAD ed., United Nations 2003).

¹¹⁵ See Articles III and XI of the General Agreement on Tariffs and Trade (GATT) (1947).

¹¹⁶ A Model International Investment Agreement for the Promotion of Sustainable Development 2 (Konrad von Moltke ed., International Institute for Sustainable Development 2004).

¹¹⁷ Article 8.5(3) of the Comprehensive Trade and Economic Agreement between Canada and the European Union (2016).

¹¹⁸ Article 7.4 of the SADC Model Bilateral Investment Treaty Template with Commentary (Community ed., 2012).

Table (2): Proposed Model BIT for Jordan

Article	Suggested Draft for the Jordan Model BIT
<p>Treaty Preamble</p>	<p>Desiring to strengthen the bonds of friendship and cooperation between the State Parties;</p> <p>Acknowledging the importance of Investments and their contribution to the economic development of the Parties, including the reduction of poverty, increase of productive capacity, economic growth, the transfer of technology, and the furtherance of human rights and human development;</p> <p>Seeking to promote, encourage and increase investment opportunities that enhance economic development and growth within the territories of the Parties;</p> <p>Recognizing that the promotion of Investment requires co-operative efforts by Investors and both Contracting Parties, whether the Host Party to investments or the Home Party of Investors;</p> <p>Understanding that sustainable development requires the fulfillment of the economic, social and environmental pillars that are embedded within the concept;</p> <p>Reaffirming the inherent right of the State Parties to regulate and to introduce new measures relating to investments in their territories in accordance with their laws and in order to meet national policy goals, development objectives, and face emergencies, including the right to change the conditions applicable to such Investments;</p> <p>Recognizing the differences in the levels of development between the Parties, and hence the asymmetries with respect to any measures currently in place;</p> <p>Seeking an overall balance of the rights and obligations among the Parties, the Investors, and the Investments under this Treaty;</p> <p>Agreeing that these objectives can be achieved without relaxing health, safety and environmental measures of general application;</p> <p>Determined to prevent and combat corruption, and promote corporate social responsibility and accountability;</p>

	The Parties of this Treaty have agreed to the following:
Treaty Objectives	The objective of this Treaty is to stimulate, encourage, and increase the flow of Investments that contribute to, and support, the economic development of each Party, in particular the Host Party where the Investment is located.
Treaty Scope	<ol style="list-style-type: none"> 1. This Treaty applies to measures adopted or maintained by the Parties relating to: <ol style="list-style-type: none"> i. Investors, as defined in this Treaty; and ii. Investments, as defined this Treaty. 2. Regarding the application of this Treaty to investments, this Treaty applies to Investments that are made and maintained in good faith and in accordance with Host Party laws and regulations, whether these Investments were made before or after signature date of this Treaty. 3. This Treaty does not bind either Party in relation to any act or fact that took place or any situation that ceased to exist before the date of signature of this Treaty. 4. For greater certainty, this Treaty provides only post establishment protection and does not cover the pre-establishment phase or matters of market access unless where explicitly provided otherwise in this Treaty and its attached Annexes. 5. This Treaty shall apply to Investments approved by the competent authority of the Host Party, if so required by its laws and regulations, and made prior to or after the signature date of this Treaty.
Definition of Investment	<p>The term “Investment” means: any kind of asset owned or controlled in good faith by an Investor in the Territory of the other Party in accordance with the latter’s applicable laws, and which is used by the Investor in the activities and operations of the business project, and has the following characteristics:</p> <ol style="list-style-type: none"> a) the commitment of capital and other resources; and b) the expectation of gain or profit; and c) the assumption of risk for the Investor; and d) a reasonable duration; and

	<p>e) has significance to the development of the Party where it is located.</p> <p>1. For purposes of this Treaty, and provided that it satisfies the above, an Investment includes:</p> <ul style="list-style-type: none"> i. shares, stock and other forms of equity participation in an enterprise; ii. bonds, debentures, loans and other forms of debt instruments that have a maturity date of three years or more; iii. tangible property, including real property; and intangible property, including rights, such as leases, mortgages, liens and pledges on real property; iv. rights conferred pursuant to law, such as licenses and permits; v. intellectual property rights; <p>2. However, an Investment does not include:</p> <ul style="list-style-type: none"> i. any interest in debt securities issued by a government or government- owned or controlled enterprise, or loans to a government or government owned or controlled enterprise; ii. any pre-operational expenditure relating to admission, establishment, acquisition or expansion of the Investment that is incurred before the commencement of substantial and real business operations of the Investment in the Host Party, except in the designated economic sectors in Annex I (Incentivized Sectors) of this Treaty;¹¹⁹ iii. portfolio investments: which are in the nature of acquisition of shares or voting power amounting to, or representing less, than (10%) ten percent of a company through stock exchanges; iv. claims to money that arise solely from commercial contracts for the sale of goods or services;
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¹¹⁹ The Annex should stipulate that Investments in the energy and water sectors (in Jordan) enjoy pre-establishment rights and protection.

	<p>v. Goodwill, brand value, market share or similar intangible rights;</p> <p>vi. claims to money that arise solely from the extension of credit in connection with any commercial transaction referred to in (v) above;</p> <p>vii. any intellectual property rights belonging to an Investor that are not used in the Investment;</p> <p>viii. an order or judgment sought or entered in any judicial, regulatory, administrative, or arbitral proceeding;</p> <p>ix. any other claims to money that do not involve the kind of interests or operations set out in the definition of Investment in this Treaty.</p> <p>3. The term “investment” shall include reinvestment (investment of the proceeds of the initial investment) and change in the form of investment (alteration of the form in which assets are invested), provided that the new investment meets the above criteria and is done in accordance with the laws of the Host Party.</p>
<p>Definition of Investor</p>	<p>The term “Investor” means: any natural or legal person from one Party that has made an Investment in the Territory of the other Party, on the date when any breach of this Treaty is alleged and on the date when the claim was submitted to Arbitration.</p> <p>1. a natural person means: a person holding the nationality of the Home Party, in accordance with the latter’s domestic laws in this regard. Natural persons who hold dual nationalities shall be deemed nationals of their dominant and effective nationality, but a dual national who holds the nationality of the Host Party shall not, in any case, be deemed an Investor for purposes of this Treaty.</p> <p>2. a legal person: is an entity duly constituted or organized in accordance with the laws of the Home Party, and:</p> <ul style="list-style-type: none"> i. has its registered office, central administration or principal place of business in the territory of the Home Party; and ii. is owned or controlled by a Natural Person or a legal entity of the Home Party; and iii. conducts real and substantial business operations in the Home Party. For this purpose, substantial business operations are determined based on:

	<p>a. the amount of investments in the Home Party; b. the number of jobs created in the Home Party; c. the length of time the legal person has been in operation in the Home Party.</p> <p>3. sovereign wealth funds, government owned companies, and not-for-profit entities of one Party investing in the other Party's Territory are deemed Investors for purposes of this Treaty, provided that they obtain the prior written approval of the Host Party before conducting any Investment activities.</p> <p>4. a legal person is deemed to be "controlled" by an Investor if the latter has the right to appoint a majority of the directors or senior management officials or to control the management or policy decisions of such legal person, including by virtue of their shareholding, management, partnership or other legal rights or by virtue of shareholders agreements or voting agreements or partnership agreements or any other agreements of similar nature.</p> <p>5. a legal person is deemed to be "owned" by an Investor if the latter owns more than (50%) fifty percent of the capital or funds or contribution in the legal person, or by other companies or entities which are ultimately owned and controlled by the Investor.</p> <p>1. Each Party shall accord Investors, and their Investments, treatment that is not less favorable than that accorded, in like circumstances, to investments of its own investors in accordance with its laws and regulations in relation to the expansion, management, conduct, operation and sale or other disposition of an Investment by an Investor in its Territory. For greater certainty, the term "expansion" in this Article shall not include the establishment or acquisition of an investment.</p> <p>2. Investments in the sectors designated in Annex 1 of this Treaty shall enjoy national treatment in the pre-establishment, establishment, and acquisition stages.</p> <p>3. For greater certainty, references to "like circumstances" in paragraph 1 of this Article requires an overall examination on a case-by-case basis of all the circumstances of an Investment including, but not limited to:</p> <ul style="list-style-type: none"> i. its effects on third person and the local community; ii. its effects on the local, regional or national environment, including the cumulative effects of all investments within a jurisdiction on the environment; iii. the sector in which the Investor is in;
<p>National Treatment (NT)</p>	

<p>iv. the aim of the measure concerned;</p> <p>v. the regulatory process generally applied in relation to the measure concerned;</p> <p>vi. other factors directly relating to the investment or investor in relation to the measure concerned;</p> <p>The examination referred to in this paragraph shall not be limited to or be biased toward any one factor.</p> <p>4. The treatment provided for in this Article shall not oblige the either Party to accord Investments of Investors of the other Party the same treatment that it accords to investments of its own investors with regard to:</p> <ul style="list-style-type: none"> i. any Investor or Investment that is not in compliance with the terms of this Treaty, or the applicable laws and regulations of the Host Party; or ii. any subsidies, privileges, incentives, rights, or preferential treatment given to investments of investors in the agriculture sector and the sectors provided in Annex I of this Treaty; or iii. any measures adopted or maintained with respect to incentives only for the purpose of promoting, encouraging, and safeguarding small and medium sized enterprises and infant industries in its Territory; or iv. any existing non-conforming measure stipulated in Annex II (Non-Conforming Measures) of this Treaty;¹²⁰ or v. any actual or future advantages accorded by either Party by virtue of its current or future membership of, or association with a customs, economic or monetary union, a common market or a free trade area; to investments or investors of its own; or vi. any matter relating wholly or partially to taxation; or vii. any measures taken in pursuit of a legitimate public policy goal, development objective, or to face a national or international emergency, provided that such measures are not taken in an arbitrary and/or 	
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¹²⁰ Annex II should stipulate the measures that breach the NT obligation under the Treaty, however Jordan wishes to maintain for any reason.

	<p>discriminatory manner and are justified by showing that they bear a reasonable relationship to rational policies and objectives.</p>
<p>Most-Favored-Nation (MFN)</p>	<ol style="list-style-type: none"> 1. Each Party shall accord Investors, and their Investments, treatment that is not less favorable than that accorded, in like circumstances, to investments of third state investors in accordance with its laws and regulations in relation to the expansion, management, conduct, operation and sale or other disposition of an Investment by an Investor in its Territory. For greater certainty, the term “expansion” in this Article shall not include the establishment or acquisition of an investment. 2. Investments in the sectors designated in Annex 1 of this Treaty shall enjoy most-favored-nation treatment in the pre-establishment, establishment, and acquisition stages. 3. For greater certainty, references to “like circumstances” in paragraph 1 of this Article requires an overall examination on a case-by-case basis of all the circumstances of an Investment including, but not limited to the criteria stipulated in Article (National Treatment)(3) above. 4. The treatment provided for in this Article shall not oblige the either Party to accord Investments of Investors of the other Party the same treatment that it accords to third state investors and their investments with regard to: <ol style="list-style-type: none"> i. any bilateral or multilateral agreement or treaty that provides better treatment to third state investors and their investments if such agreement or treaty is entered into by either Party before the signature date of this Treaty; ii. any Investor or Investment that is not in compliance with the terms of this Treaty, or the applicable laws and regulations of the Host Party; or iii. any subsidies, privileges, incentives, rights, or preferential treatment given to third state investors and their investments in the agriculture sector and the sectors provided in Annex I of this Treaty; or iv. any existing non-conforming measure stipulated in Annex II (Non-Conforming Measures) of this Treaty; or v. any actual or future advantages accorded by either Party by virtue of its current or future membership of, or association with a customs, economic or monetary union, a common market or a free trade area; to third state investments or investors; or

	<p>vi. any matter relating wholly or partially to taxation; or</p> <p>vii. any measures taken in pursuit of a legitimate public policy goal, development objective, or to face a national or international emergency, provided that such measures are not taken in an arbitrary and/or discriminatory manner and are justified by showing that they bear a reasonable relationship to rational policies and are not driven by preference to investments or investors from a particular third state.</p> <p>5. For greater certainty, the treatment referred to in this Article applies exclusively to the substantive provisions of this Treaty, in particular Articles (A, B, C, & D). The treatment referred to herein does not apply to, or encompass, international dispute resolution procedures or mechanisms, such as those included in Article X (Investor-State Dispute Settlement).</p> <p>1. Each Party shall abstain from treating Investors of the other Party and their Investments in a manner that is:</p> <ul style="list-style-type: none"> i. manifestly arbitrary; or ii. discriminatory on manifestly wrongful grounds, such as the Investor's gender, race or religious belief; or iii. abusive, such as coercion, duress and harassment of Investors; or iv. fundamentally in breach of the principle of due process embodied in the principle legal systems of the world, such as denying justice in any civil, criminal, or administrative proceedings; or v. in fundamental breach of the concept of transparency in judicial and administrative proceedings. <p>2. Neither Party shall infringe legitimate expectations based on investment-inducing representations or measures, which the Investor has relied on substantially when making an Investment. In this respect, the Investor's conduct and accepted business risk in the Territory of the Party concerned should be taken into account when determining the legitimate expectations of the Investor. However, the mere fact that a Party takes, or fails to take, an action that may be inconsistent with an Investor's expectations does not constitute a breach of this Article, even if there is loss or damage to the covered Investment as a result.</p> <p>3. In applying this Article, the Parties understand that they have different forms of administrative, legislative, and judicial systems, and are at different levels of development; hence they may not achieve the same standard at the same time.</p>
<p style="text-align: center;">Fair and Equitable Treatment (FET)</p>	

	<p>4. A determination that there has been a breach of another provision of this Treaty, or of a separate international treaty or agreement, does not establish that there has been a breach of this Article.</p> <p>5. Nothing in this Article shall be construed to prevent a Party from taking any measure(s) it deems necessary to achieve public policy and development goals, maintain the stability and integrity of its financial system, respond to a national or international emergency, maintain security and order within its Territory, regulate any matter that it deems legitimate and beneficial to its people, preserve its national resources and/or public health and/or the environment, or to comply with any international obligation or undertaking, even if such measure(s) cause harm or damage to a covered Investor or Investment under this Treaty, provided however that such measure(s) are taken in good faith and are not applied in an arbitrary or discriminatory fashion.</p>
<p style="text-align: center;">Denial of Benefits</p>	<p>The Host Party may at any time, including after the institution of arbitration proceedings, deny the benefits of this Treaty to:</p> <ul style="list-style-type: none"> i. an Investment or Investor owned or controlled, directly or indirectly, by persons of a non-Party or of the Host Party, or ii. an Investor that does not have substantial business activities in the Home Party where it is constituted or organized; or iii. an Investment or Investor that has been established or restructured in bad faith, or with the primary purpose of gaining access to the dispute resolution mechanisms provided in this Treaty, or iv. an Investment or Investor that is not in compliance with the terms of this Treaty, or the applicable laws and regulations in effect at the Host Party, or any international convention that the Host Party is a contracting member to.
<p style="text-align: center;">Investor-State Dispute Settlement (ISDS)</p>	<ul style="list-style-type: none"> 1. Disputes between a Host Party and an Investor in relation to an Investment shall be resolved via amicable consultations between the Host Party and the Investor. When such dispute(s) arises, the Investor shall submit within (90) ninety days from the date of that event giving rise to the dispute (or (90) ninety days from the date when the Investor becomes aware of such event), a written request to the Host Party to hold amicable consultations for purposes of resolving the dispute. The Host Party shall respond to the Investor and initiate amicable consultations within (30) thirty days from the date of its receipt of the Investor's written request. 2. If the Host Party and the Investor fail to resolve the dispute within (180) one hundred and eighty days from the date when the amicable consultations were initiated, or a settlement cannot be reached within this period for any reason, then the Investor shall exhaust all local remedies, including any judicial or administrative remedies, available under the

laws and regulations of the Host Party.

3. If the Investor fails, for any reason, to resolve the dispute via local remedies within (36) thirty six months from the date of initiation of any judicial and/or local remedies available under the laws and regulations of the Host Party, then the Investor may, within (12) twelve months from the date when the exhaustion of local remedies period has lapsed, resort to arbitration to finally resolve the dispute. Arbitration shall be under, and in accordance with, the Convention on the Settlement of Investment Disputes between States and Nationals of other States (hereinafter “ICSID”) and the then in force ICSID arbitration rules and regulations.
4. The ICSID tribunal shall have jurisdiction to review claims, and for that purpose issue awards, submitted by Investors or Investments in relation to alleged breach(s) by the Host Party of the substantive provisions of this Treaty exclusively, namely Articles A (NT), B (MFN), C (FET), and (D), and :
 - i. the alleged breach of the substantive provisions of this Treaty is claimed to have caused the Investor and/or its Investment harm or damage; and
 - ii. the claim is submitted by an Investor or Investment that is in compliance with terms of this Treaty, and the applicable laws and regulations of the Host Party; and
 - iii. the claim is submitted by an Investor or Investment that has followed the dispute resolution procedure set in paragraphs 1 and 2 of this Article in the sequence of their numbering in this Article, and within the given timeframes and limitations stipulated in each paragraph; and
 - iv. the claim is not submitted by an Investor or Investment regarding a dispute that has arisen, or has been settled, before the date of signature of this Treaty, and
 - v. the claim is not submitted by an Investor or Investment that is established in the Host Party through fraud, fraudulent misrepresentation, concealment, corruption, or conduct amounting to an abuse of process.
5. The Host Party in a dispute with an Investor shall have the right to raise an objection, at any stage of the arbitration proceedings that the Investor, which is the other party to the dispute, has –in fact- received an indemnity covering wholly or partially his losses under an insurance policy.
6. Where an investment authorization or a contract includes a choice of forum clause for the resolution of disputes

	<p>pertaining to that Investment or the authorization or contract, no arbitration under this Treaty may be initiated by the Investor when the underlying measure in the arbitration would be covered by such a choice of forum clause.</p> <p>7. Nothing in this Article shall preclude an Investor or Investment from seeking interim relief before a judicial or authority in the Host Party, for the sole purpose of preserving the Investor's rights and interests during the timeframes stipulated in paragraphs 1, 2, and 3 of this Article, or during the pendency of the arbitration, provided that the sought interim relief does not involve the payment of monetary damages.</p> <p>8. Nothing in this Article shall be understood to preclude the Host Party and the Investor from having recourse to mediation to solve their dispute(s), even after the institution of any legal, administrative, or arbitral proceedings. Recourse to mediation is without prejudice to the legal position or rights of both the Host State and the Investor under this Treaty and shall be governed by the rules agreed to by the disputing parties. The disputing parties shall endeavor to solve their dispute(s) via mediation within (60) sixty days from the date of initiation of mediation proceedings, and during this period any legal, administrative, or arbitral proceedings shall be put on hold pending the outcome of the mediation process.</p>
<p>Investor's Obligations</p>	<p>1. Investors and Investments should apply national, and internationally accepted, standards of corporate governance for the sector involved, in particular for transparency and accounting practices. Investors and their Investments should strive to make the maximum feasible contributions to the sustainable development of the Host Party and local community through appropriate levels of socially responsible practices.</p> <p>2. Investors and their Investments should comply with and abide to the terms of this Treaty, the applicable laws and regulations of the Host Party, and all international conventions and treaties relating to the protection of human rights, labor, and the environment, at all times and stages of the investment project. An investor or Investment that fails to comply with the any of the above shall be denied the protections and benefits of this Treaty.</p> <p>3. The Investor's or Investment's conduct in the Host Party shall be considered and weighed against any claims of breach of this Treaty in any judicial, administrative, or arbitral proceedings. The Host Party shall have the right to assert as a defense or counterclaim right of set off or other similar claim that the Investor has not fulfilled its obligations under this Treaty to comply with the Host State laws and regulations or that it has not taken all reasonable steps to mitigate possible damages. Any adjudicating authority constituted by virtue of the dispute settlement procedure under this Treaty, may set-off any amount(s) from any compensation(s) owed to the Investor or Investment in the event that such adjudicating authority finds the Investor's or Investment's conduct in the Host Party to be inappropriate, harmful to the Host Party, or not compliant with the terms of this Treaty and/or the applicable laws and regulations of the Host Party and/or any international convention or treaty relating to the protection of human rights, labor, and the environment.</p>

	<p>Nothing in this Treaty shall be construed to prevent a Party from taking any measure(s), actions, omissions, or enforce any laws or regulations that are necessary:</p> <ul style="list-style-type: none"> i. to achieve public policy and development objectives; or ii. to maintain the stability and integrity of its financial system; or iii. to respond to a national or international emergency or crises; or iv. to maintain security and order within its Territory; or v. to preserve its national resources and/or public health and/or safety and/or labor standards and/or the environment; or vi. to comply with any international obligation or undertaking; or vii. to support, encourage, and safeguard its small and medium sized enterprises and infant industries; or viii. to regulate matters of public concern and benefit; or ix. to combat corruption, money laundry, terrorism, and promote the rule of law within its Territory; or x. to protect any other essential economic, social, environmental, and security interests. <p>even if such measure(s), actions, omissions, or laws cause harm or damage to a covered Investor or Investment under this Treaty, provided however that such measure(s) actions, omissions, or laws are taken in good faith and are not applied in an arbitrary or discriminatory fashion.</p>
<p>Host Party Exceptions</p>	
	<ul style="list-style-type: none"> 1. The Parties are entitled to condition the receipt or continued receipt of an advantage, in connection with an Investment in its Territory, on compliance with a requirement to locate production, provide a service, train or employ workers, construct or expand particular facilities, or carry out research and development in its Territory. 2. Nothing in this Treaty shall preclude a Party from conditioning the procurement of any governmental or public good or
<p>Performance Requirements</p>	

	<p>service on the:</p> <ul style="list-style-type: none">i. level or percentage of domestic content in such goods or services; orii. give preference to goods or services produced in its Territory or to purchase goods or services from persons in its Territory; oriii. to transfer a particular technology, a production process or other proprietary knowledge to a person in its Territory; oriv. to use a particular technology or a production process in its Territory.
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III. CONCLUSION

Balancing investment treaties and preserving the two competing and inextricable objectives (investment protection and host state development) is not an easy task for any country. To strike the right balance between the two interests involved, the host state (i.e. capital-importing state) must design and draft a model BIT that is meticulously drafted to accommodate its need and objectives. The host state will use its tailored model BIT as an indication of its position, and a projection of the level of protection it is willing to afford to home state investors and its development goals that it wishes to achieve. The host state, along with the home state, will use their model BITs to reach a truly negotiated and balanced final BIT that preserves both parties' objectives and interests. Over protecting host state's interests will render the model BIT ineffective at protecting the rights and property of home state investors. At the same time, over protecting home state investors will affect that host state's right to regulate and pursue its development objectives.

The table provided in the previous section provides how to approach the issue of balancing BITs. At the beginning, each country has to determine its development objectives that it seeks to achieve from protecting FDI. It then has to incorporate these development challenges into its model BIT by incentivizing FDI in these sectors (for example, providing FDI in these sectors with pre-establishment rights exclusively). The objectives of the treaty and assurance that all interests of the involved parties are preserved should be explicitly mentioned in the treaty preamble and included in the BIT terms.

The definition of investment is of extreme importance; it should be defined in a fashion that requires incoming FDI to comply with the host state's law and contribute to its development in order to gain treaty protection. Similarly, the definition of investor must ensure that incoming investors have real ties with their home countries to avoid treaty shopping by investors, who otherwise are not entitled to treaty protection.

The treatment standards are of vital importance to the success of any model BIT. Balancing these standards requires avoidance of open-ended phrases and loosely drafted provisions that have the potential of expansive interpretation. Rather, these treatment standards should be clearly defined, and their scope of protection should be precisely outlined. Host states are encouraged to insert limitations and exceptions that help in narrowing and clarifying the scope of these treatment standards, which will shrink the possibilities of their breach by the host state. Special attention should be given to the national treatment, most-favored-nation, and fair and equitable treatment standards, as they are the most invoked in investor-state dispute settlement (ISDS).

Similarly, the ISDS clause should require the home state investor to exhaust local remedies and attempt to settle the dispute amicably as a pre-condition to ISDS. It should also restrict access to ISDS to those investments and investors who are in compliance with host state laws and have fulfilled their obligations under the treaty. The jurisdiction of the ISDS tribunal should be confined to the substantive provisions of the BIT (i.e. treatment standards) as to not allow claims based on other procedural provisions of the BIT. Also, ISDS tribunals should be obliged to take the home state investor's conduct in the host state into account when reviewing any claims of treaty breach, by inserting a requirement to that end in the BIT.

Finally, home state investors should be obligated to comply with international standards and principles that ensure their integrity and beneficial input to the host state development, such as compliance with corporate governance principles, human rights and labor conventions, and protection of the environment. The host state may also want to impose performance requirements that do not contradict the prohibited restrictions under the GATT and TRIMS agreements. These can be in the form of requiring the home state investor to employ a certain number or percentage of nationals in managerial and technical positions, or to train local labor on how to use new technologies and industrial processes, as well as other similar requirements that provide a positive asset to the host state.

By tracing the evolution of international investment law since its early beginnings in the BC era until modern times, this thesis finds that economic development was, and remains, the primary purpose behind the conclusion of BITs and other investment agreements. Most international agreements and conventions pertaining to international investment, such as ICSID and MIGA, put the development of host countries as their chief objective and purpose.

The current formulation and drafting of BITs has overprotected home state investors and negated the development of host states and their right to regulate and pursue their interests. It has also shown, through ICSID case law, how the broad and loosely drafted clauses and treatment standards in BITs have enabled interpreters to expand the protection of investors on the account of host states.

The solution to the current state-of-affairs is not one related to the ISDS process itself, but rather is related to the broad and unqualified provisions of BITs. In particular, the definitions and treatment standards found in typical BITs need to be clearly defined and limited in scope. No model BIT can suffice on a universal level, due to the difference in development levels and

objectives of different countries. Hence, the solution rests in drafting balanced model BITs for each country in accordance with its objects and goals. This approach allows for country-specific issues to be addressed in a balanced investment treaty, which will result in a greater impact and role of FDI in the development of the host state.

A model BIT for Jordan should incorporate the country's development objectives, in addition to balancing and qualifying the BIT terms to avoid the issues and interpretations that have appeared previously in ISDS cases. The model BIT for Jordan uses the best practices and recent trends in other model BITs, recently concluded BITs, and multilateral investment agreements. The recommendations and suggestions made for the Jordan BIT can be conceptually transferred to other model BITs for other countries, provided that they are amended in alignment with the host state's needs, objectives, and policies.

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