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# The Role of the Domestic Law of the Host State in Determining the ratione materiae Jurisdiction of Investment Treaty Tribunals: The Partial Revival of the Localisation Theory

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# The Role of the Domestic Law of the Host State in Determining the *ratione materiae* Jurisdiction of Investment Treaty Tribunals: The Partial Revival of the Localisation Theory

Reza Eftekhar

# The Role of the Domestic Law of the Host State in Determining the *ratione materiae* Jurisdiction of Investment Treaty Tribunals: The Partial Revival of the Localisation Theory

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*To my wonderful wife: Mahnoush*

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## List of Abbreviations

### General

| | |
|---|---|
| ASEAN | Association of South East Asian Nations |
| BIT | Bilateral Investment Treaty |
| DSB | WTO Dispute Settlement Body |
| ECT | Energy Charter Treaty |
| ECtHR | European Court of Human Rights |
| EU | European Union |
| FCN | Friendship, Commerce and Navigation (treaties) |
| FDI | Foreign Direct Investment |
| FTA | Free Trade Agreement |
| ICC | International Chamber of Commerce |
| ICCA | International Council for Commercial Arbitration |
| ICJ | International Court of Justice |
| ICSID | International Centre for Settlement of Investment Disputes |
| IIA | International Investment Agreement |
| ILA | International Law Association |
| ILC | International Law Commission |
| LCIA | London Court of International Arbitration |
| MFN | Most-Favoured-Nation |
| NAFTA | North American Free Trade Agreement |
| OECD | Organisation for Economic Co-operation and Development |
| PCA | Permanent Court of Arbitration |
| PCIJ | Permanent Court of International Justice |
| SCC | Stockholm Chamber of Commerce |
| TTIP | Transatlantic Trade and Investment Partnership |
| UN | United Nations |
| UNCITRAL | United Nations Commission on International Trade Law |
| UNCTAD | United Nations Conference on Trade and Development |
| UNIDRIOT | International Institute for the Unification of Private Law |
| VCLT | Vienna Convention on the Law of Treaties |
| WTO | World Trade Organization |

### Journals, Publications, Reports, and Treaty Series

| | |
|---|---|
| AJIL | American Journal of International Law |
| Arb Int'l | Arbitration International |
| BYIL | British Yearbook of International Law |

| | |
|---|---|
| CMLJ | Capital Markets Law Journal |
| CUP | Cambridge University Press |
| Eur. J. Int'l L. | European Journal of International Law |
| ICLQ | International and Comparative Law Quarterly |
| ICSID Rep | ICSID Reports |
| ICSID Rev-FILJ | ICSID Review—Foreign Investment Law Journal |
| ILM | International Legal Materials |
| ILR | International Law Reports |
| Iran-USCTR | Iran-US Claims Tribunal Reports |
| J Int'l Arb | Journal of International Arbitration |
| Lloyd's Rep | Lloyd's Law Reports |
| OUP | Oxford University Press |
| RIAA | Reports of International Arbitral Awards |
| TDM | Transnational Dispute Management |
| YB ILC | Yearbook of the International Law Commission |

# Introduction

## I. The Relevance of the Host State Domestic Law in Investment Treaty Arbitrations: Revival of the Classical 'Localisation' Theory?

1. Beginning in the late 1950s and continuing well into the 1960s and the 1970s, Western European countries started concluding bilateral investment treaties with developing countries with the aim of legally protecting the overseas investments of their nationals in the latter countries.[1] This process of concluding bilateral investment treaties got a momentum when the United States and later Canada also joined the club by concluding many bilateral investment treaties in the 1980s and the 1990s.[2] Bilateral investment treaties were apparently invented by the North mostly in response to a trend of 'localisation' of foreign investment contracts and disputes in the developing world.[3] With the pervasive decolonisation in the world in the 1960s, and consequently, the emergence of many new developing countries, old and new Southern countries, now having a numerical majority in international organisations, in particular in the General Assembly of the United Nations ("UN"), went about updating the 'Calvo' doctrine[4] and attempted to create a legal framework pursuant to which the laws of the host state were considered as the applicable law to contractual disputes arising from foreign investment contracts. Furthermore, according to this 'localisation' theory, the national court of the host state, rather than courts of any other country or international arbitration, was the competent forum for deciding disputes arising out of foreign investment contracts. These efforts materialised in various forms and guises but were most notably reflected in the three Resolutions passed by the UN General Assembly in the 1960s and 1970s.[5] In the scholarly writings, this theory of leaving the destiny of foreign investment disputes in the hands of sovereign local elements (i.e., local laws and local courts) was known as the 'localisation' theory.[6]
2. The Western world understandably disliked this theory and did all it could to wipe out its effects on foreign investment contracts and disputes. In particular, through bilateral investment treaties, European and North American countries intended to insulate the investments of their subjects in developing countries from the interference of the laws and

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[1] R Dolzer and C Schreuer, *Principles of International Investment Law* (OUP 2012) 6-7; JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (1990) 24(3) The International Lawyer 656-657.

[2] R Dolzer and C Schreuer (n 1) 7; JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (n 1) 657-658.

[3] Sornarajah, *The International Law on Foreign Investment* (4th edn, CUP 2017) 206.

[4] For the genesis and specifications of the 'Calvo' doctrine, see Chapter 5, Section One.

[5] 'Permanent Sovereignty over Natural Resources' GA Res 1803, XVII, 14 December 1962; 'Declaration on the Establishment of a New International Economic Order' GA Res 3201, S-VI, 01 May 1974; 'Charter of Economic Rights and Duties of States' GA Res 3281, XXIX, 12 December 1974.

[6] The term 'localisation' was used, *inter alia*, by Sornarajah. See M Sornarajah (n 3) 116. Another commentator uses the term 'relocalisation' for the same theory put forward by developing countries in the 1960s-1980s. See VC Igbokwe, 'Developing Countries and the Law Applicable to International Arbitration of Oil Investment Disputes: Has the Last Word been Said?' (1997) 14(1) J Int'l Arb 99, 116-123.

the courts of the host state.[7] The 'treatification'[8] of international investment law sought to elevate the mere domestic public and private law relationship between states and foreign investors to an international level where international law was expected to overtake the domestic law of the host state and was supposed to have the last say on all matters. Furthermore, under the recently designed scheme of bilateral investment treaties, international law was believed to be uttered principally by international arbitral tribunals not the courts of the recipient state. Therefore, arbitration was opted for as the preferred method of dispute resolution under the regime of bilateral investment treaties. In comparison to national judges, arbitrators usually find it easier to apply international law to an international investment dispute.[9]

3. It could be argued that the wave of 'localisation' movements of developing countries represented by three Resolutions of the UN General Assembly was, *inter alia*, abated by the vast conclusion of bilateral – and later multilateral – investment treaties.[10] Under the new legal framework of the protection of foreign investments, even the most supportive scholars of 'localisation' theory admitted that the laws and the courts of the host state are not determinative of the fate of disputes arising out of the bilateral investment treaties.[11] As time went by, the 'localisation' theory was almost forgotten by all the stakeholders.

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[7] J Voss, 'The Protection and Promotion of European Private Investment in Developing Countries-An Approach Towards A Concept For A European Policy on Foreign Investment: A German Contribution' (1981) 18(3) Common Market Law Review 363, 369; K Kunzer, 'Developing a Model Bilateral Investment Treaty' (1983) 15 Law & Policy of International Business 273, 292-293; JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (n 1) 659-661.

[8] The term 'treatification' in this context has been devised by Salacuse. JW Salacuse, 'The Treatification of International Investment' (2007) 13(1) Law and Business Review of the Americas 155. See also JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (OUP 2013) 331-332.

[9] O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 94. See also HE Kjos, *Applicable Law in Investor-State Arbitration: The Interplay Between National and International Law* (OUP 2013) 24.

[10] In the words of Judge Brower and one of his former legal clerks, "the 'Southern' tsunami of NIEO [New International Economic Order] and the Charter [of Economic Rights and Duties of States] eventually abated. The subsequent conclusion of thousands of bilateral investment treaties, and, more recently, several multilateral investment treaties, in which States record their true, practical interests, have replaced the 'soapbox' Resolutions of the General Assembly…" CN Brower & S Melikian, ''We Have Met The Enemy And He Is US!' Is the Industrialized North 'Going South' on Investor–State Arbitration?' (2015) 31(1) Arb Int'l 22. In this respect, the *Antoine Goetz* tribunal considered that the emergence of bilateral investment treaties revived the role of international law in international investment disputes:

> It may be interesting to remark on this subject that choice of law clauses in investment protection treaties frequently refer to the provisions of the treaty itself, and, more broadly, to international law principles and rules. This leads to a remarkable comeback of international law, after a decline in practice and jurisprudence, in the legal relations between host States and foreign investors.

*Antoine Goetz et consorts v. République du Burundi*, ICSID Case No. ARB/95/3, Award, 10 February 1999 [20]. The English translation of the Award can be found in (2001) XXVI Yearbook Commercial Arbitration 24, 36.

[11] In consequence of these developments, even a commentator like Sornarajah, who is known to be always supportive of the localisation-related theories, concedes that when subject to bilateral investment treaties, international investment arrangements will slip out of the hands of domestic laws and national courts of the host state and will fall in the domain

4. Bearing these observations in mind, one would expect that international law is controlling in the resolution of disputes arising out of bilateral investment treaties. To be sure, it has been stated time and again by many investment treaty tribunals that in resolving disputes submitted to it, the investment treaty arbitral tribunal should apply the underlying investment treaty in tandem with rules and principles of international law.[12]
5. Generally speaking, this statement is correct. Indeed, in cases where the investor invokes the substantive rights conferred by an investment treaty (like national treatment or fair and equitable treatment), international law will be controlling since the question is whether the recipient state has violated the international standards of protection offered by the relevant international treaty. To be more accurate, however, the absolute statement that international law governs all aspects of disputes arising out of investment treaties should be more scrutinised. Two points are in order. Firstly, although not explicitly stated, the statement that international law governs investment treaties seems to concern the merits of the dispute rather than the jurisdiction of the arbitral tribunal.[13] In this regard, the ICSID Annulment

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of international law and international arbitration: "The proposition that a State contract falls within the domestic sovereignty of a host State may not hold valid where the investment made in pursuance of it is protected by a bilateral investment treaty or an international convention like the Convention on the Settlement of International Disputes [sic]." M Sornarajah, 'The Climate of International Arbitration' (1991) 8(2) J Int'l Arb 47, 66, 81-86.

[12] See, e.g., *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic*, ICSID Case No. ARB/97/3 (formerly *Compañía de Aguas del Aconquija, S.A. and Compagnie Générale des Eaux v. Argentine Republic*), Decision on Annulment, 03 July 2002 [102] (expressing that: "[…] the inquiry which the ICSID tribunal is required to undertake is one governed by the ICSID Convention, by the BIT and by applicable international law. Such an inquiry is neither in principle determined, nor precluded, by any issue of municipal law, including any municipal law agreement of the parties."); *Técnicas Medioambientales Tecmed, S.A. v. The United Mexican States*, ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003 [116] (observing that: "In addition to the provisions of the Agreement, the Arbitral Tribunal has to resolve any dispute submitted to it by applying international law provisions […] for which purpose the Arbitral Tribunal understands that disputes are to be resolved by resorting to the sources described in Article 38 of the Statute of the International Court of Justice […]"); *ADC Affiliate Limited and ADC & ADMC Management Limited v. The Republic of Hungary*, ICSID Case No. ARB/03/16, Award of the Tribunal, 02 October 2006 [290]-[292] (stating that: "In the Tribunal's view, by consenting to arbitration under Article 7 of the BIT […] the Parties also consented to the applicability of the provisions of the Treaty […] Those provisions are Treaty provisions pertaining to international law. […] The consent must also be deemed to comprise a choice for general international law, including customary international law, if and to the extent that it comes into play for interpreting and applying the provisions of the Treaty […] The sole exception to the foregoing is Article 4(3) of the BIT which provides: "The amount of this compensation may be estimated according to the laws and regulations of the country where the expropriation is made." In the present case, that law is Hungarian law. As the reference to domestic law is used for one isolated subject matter only, it must be presumed that all other matters are governed by the provisions of the Treaty itself which in turn is governed by international law.")

[13] A Newcombe & L Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International 2009) 77 (making a distinction between "the law applicable to the substance of the dispute" and "the law applicable to jurisdictional issues"). On the same point, it should be recalled that Article 42 of the ICSID Convention on applicable law is not helpful in determining the applicable law to jurisdiction. In *CMS v. Argentina*, the tribunal correctly said: "Article 42 is mainly designed for the resolution of disputes on the merits and, as such, it is in principle independent from the decisions on jurisdiction, governed solely by Article 25 of the Convention and those other provisions of the consent instrument which might be applicable, in the instant case the Treaty provisions…" The 'consent instrument' under examination in that case was an international investment agreement, which in turn has an express or implied *renvoi* to the national law of either of the contracting states in some respects including on matters affecting the jurisdiction of the tribunal. *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Decision on Objections to Jurisdiction, 17 July 2003 [88]. The tribunal in *Noble Energy v. Ecuador* also adhered to this viewpoint: "The Tribunal is of the opinion that Article 42(1) is irrelevant for purposes of jurisdiction. Article 42 of the ICSID Convention is a conflict rule which deals with the law governing the merits of the dispute […]

Committee in *Azurix v. Argentina* made it clear that it is to the allegations of the breach of the investment treaty that international law applies to the exclusion of domestic law:

> Each of Azurix's claims in this case was for an alleged breach of the BIT. The BIT is an international treaty between Argentina and the United States. By definition, a treaty is governed by international law […] and not by municipal law […] In any claim for breach of an investment treaty, the question whether or not there has been a breach of the treaty must therefore be determined, not through the application of the municipal law of any State, but through the application of the terms of the treaty to the facts of the case, in accordance with general principles of international law, including principles of the international law of treaties […][14]

6. It is very well conceivable, and, in fact, it happens not infrequently, that in respect to a matter concerning the jurisdiction of the investment treaty tribunal, the underlying investment treaty makes reference to domestic laws for the determination of a given issue. In such circumstances, the domestic law will have a significant role to play as 'law' in resolving the jurisdictional matter at stake.[15]
7. The second point is that many terms used in an investment treaty are generic and mostly not defined or otherwise directly regulated in the investment treaty itself (e.g., 'property', 'asset', 'investment', 'national' etc.). To be sure, an investment treaty is an agreement that regulates the relations between two or more states on the subject of mutual foreign

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Jurisdiction is a different matter. It is not subject to this conflict rule but is governed by Article 25 of the ICSID Convention." *Noble Energy, Inc. and Machalapower Cia. Ltda. v. The Republic of Ecuador and Consejo Nacional de Electricidad,* ICSID Case No. ARB/05/12 Decision on Jurisdiction, 05 March 2008 [57]. See also *Saipem S.p.A. v. The People's Republic of Bangladesh*, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007 [68]; C Schreuer *et al*, *The ICSID Convention: A Commentary* (CUP 2009) 550-552; E De Brabandere, *Investment Treaty Arbitration as Public International Law: Procedural Aspects and Implications* (CUP 2014) 123.

[14] *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Decision on the Application for Annulment of the Argentine Republic, 01 September 2009 [146]. See also *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No ARB/03/15, Award, 31 October 2011 [130] (stating that: "The Claimant relies on Argentina's responsibility for the violation of various provisions of the BIT [...] the primary governing law in this case is the BIT, supplemented by international law to which the BIT itself makes reference in various provisions.")

[15] In this regard, see *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia*, ICSID Case No. ARB/06/2, Decision on Jurisdiction, 27 September 2012 [47]-[52] (where the tribunal states that "[b]oth Parties agree, and rightly so, that the Tribunal's jurisdiction is governed by the ICSID Convention, by the Bolivia-Chile BIT […] and, to the extent the latter refers to it, by Bolivian law." Having noted that as per Article I(2) of the Bolivia-Chile BIT, 'investment' is defined as any kind of assets or rights related to an investment made in accordance with the laws and regulations of the host state, the tribunal concluded that: "… Bolivian law applies to determine (i) whether Quiborax and Allan Fosk were shareholders of NMM at the time the dispute arose in June 2004, and (ii) whether the Claimants' purported investment was made "in accordance with the laws and regulations" and the "legal provisions" of Bolivia […] Both Parties agree that these issues are governed by Bolivian law"; *Churchill Mining PLC v. Republic of Indonesia*, ICSID Case No. ARB/12/14 & *Planet Mining Pty Ltd v. Republic of Indonesia*, ICSID Case No. ARB12/40, Decisions on Jurisdiction for both Cases, 24 February 2014, both at [86] (stating that: "The Tribunal's jurisdiction is contingent upon the provisions of the ICSID Convention on the one hand, and of the […] BIT, […] on the other hand. In addition, where an international law instrument refers to jurisdictional requirements governed by the municipal law of a Contracting State, that municipal law shall also govern the jurisdiction of the Tribunal to the extent provided by the BIT."); M Sasson, *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer Law International 2017) 1-3.

investment. As such, the rights and duties of the state contracting parties, as well as the investors availing themselves of such treaties, are determined by these treaties. However, no investment treaty constitutes a self-standing regime. It is dependent on other sources of law to become operative. It is submitted that investment treaties are grounded on two legal pillars: international law and domestic law.[16] Therefore, in addition to the resources enumerated in Article 38(1) of the Statute of the International Court of Justice ("ICJ"),[17] either by expression or by implication, rules of domestic law may also be read into an investment treaty in order to supplement it and make it a complete legal system. Indeed, to avoid a situation of *non liquet*, an investment treaty tribunal should refer to an applicable body of law to define the open-textured terms and concepts in investment treaties exemplified above (e.g., asset) and apply the germane legal rules to the questions at issue. As such, an arbitral tribunal should first identify and describe the question at stake and then recognise the law applicable to it, which could be either international or municipal law.

8. The main task of an arbitral tribunal is to discern and to distinguish the areas of application of each legal system. In this way, no conflict will arise between the application of municipal law and international law. According to Fitzmaurice, when one makes a distinction between the international field and the domestic field, there will be no conflict between the two legal systems as each body of law will operate and will have supremacy within its own

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[16] *Asian Agricultural Products v. Democratic Republic of Sri Lanka*, ICSID Case No ARB/87/3, Final Award, 27 June 1990 [19]-[21] (stating: "[T]he Bilateral Investment Treaty is not a self-contained closed legal system limited to provide for substantive material rules of direct applicability, but it has to be envisaged within a wider juridical context in which rules from other sources are integrated through implied incorporation methods, or by direct reference to certain supplementary rules, whether of international law character or of domestic law nature …"; *Wena Hotels Ltd. v. Arab Republic of Egypt*, ICSID Case No. ARB/98/4, Award, 08 December 2000 [79] (noting that "… the IPPA is a fairly terse agreement of only seven pages containing thirteen articles. The parties in their arguments have not treated it as containing all the rules of law applicable to their dispute, and this is also the view of the Tribunal…"; *LG&E Energy Corp., LG&E Capital Corp., and LG&E International, Inc .v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability [97] (citing the above-mentioned statement from *Asian Agricultural Products v. Democratic Republic of Sri Lanka* Award with approval].

[17] Article 38(1) of the Statute of the ICJ reads:

> The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply:
>
> a. international conventions, whether general or particular, establishing rules expressly recognized by the contesting states;
>
> b. international custom, as evidence of a general practice accepted as law;
>
> c. the general principles of law recognized by civilized nations;
>
> d. subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law.

realm.[18] In this sense, "[n]ational law may be part of the 'applicable law' either governing the basis of a claim or more commonly governing a particular issue."[19]

9. With these points in mind, I argue that the applicable law to an investment treaty dispute, in its totality, is a combination of international and domestic law.[20] In other words, one can consider that domestic law can indeed play a role in the settlement of disputes arising out of international investment treaties, in particular, when matters concerning the jurisdiction of an investment treaty tribunal are at stake.
10. Indeed, through a proper review of the terms of bilateral investment treaties, as well as the more recent practice of investment treaty tribunals, one can readily recognise the role assigned to domestic laws in settling a number of jurisdictional issues in investment treaty arbitrations. To be more precise, it is axiomatic that the subject-matter jurisdiction of an investment treaty tribunal revolves around the concept of 'investment'. It is submitted that, in most cases, it is the domestic law of the host state which determines whether there are binding and enforceable rights underlying investments which are subject to an investment treaty claim.[21] Furthermore, it is the domestic law of the host state which determines whether the investment has been established legally and is thus capable of protection by

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[18] G Fitzmaurice, 'The General Principles of International Law Considered from the Standpoint of the Rule of Law' (1957) 92 Collected Courses of the Hague Academy of International Law 68. See also J Crawford (ed), *Brownlie's Principles of Public International Law* (8th Edition, OUP 2012) 110 (observing that each system of national and international law "is supreme *in its own field*; neither has hegemony over the other"); O Spiermann (n 9) 108 (stating that in investment treaty cases, "international and national law gain their own and exclusive fields of application"); *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Award, 14 July 2006 [66] (holding that "Article 42(1) has been the subject of controversy on the respective roles of municipal law and international law. It is clear from the second sentence of Article 42(1) that both legal orders have a role to play, which role will depend on the nature of the dispute and may vary depending on which element of the dispute is considered."); *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3 (also known as *Enron Creditors Recovery Corp. and Ponderosa Assets, L.P. v. The Argentine Republic*), Award, 22 May 2007 [207] (noting that: "While on occasions writers and decisions have tended to consider the application of domestic law or international law as a kind of dichotomy, this is far from being the case. In fact, both have a complementary role to perform and this has begun to be recognized …")

[19] J Crawford (n 18) 52.

[20] *Fedax N.V. v. The Republic of Venezuela*, ICSID Case No. ARB/96/3, Award, 09 March 1998 [30] (stating that "[i]t is of interest to note in this respect that the various sources of the applicable law [...] including the laws of the Contracting Party, the Agreement, other special agreements connected with the investment and the general principles of international law, have all had an important and supplementary role in the considerations of this case as well as in providing the basis for the decision on jurisdiction and the award on the merits [...]"); *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, 12 May 2005 [116]-[117] (observing that the "more pragmatic and less doctrinaire approach [is] allowing for the application of both domestic law and international law if the specific facts of the dispute so justifies." The tribunal further found that there is a 'close interaction' between the laws of Argentina, the underlying contract, and international law "as embodied both in the Treaty and in customary international law." It said that "all these rules are inseparable and will, to the extent justified, be applied by the Tribunal."); A Newcombe & L Paradell (n 13) 86; F Grisel, 'The Sources of Foreign Investment Law', in Z Douglas, J Pauwelyn, JE Viñuales (eds), *The Foundations of International Investment Law* (OUP 2014) 223.

[21] See, for instance, *Accession Mezzanine Capital L.P. and Danubius Kereskedöház Vagyonkezelö Zrt. v. Hungary*, ICSID Case No. ARB/12/3, Award, 17 April 2015; *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary*, ICSID Case No. ARB/12/2, Award, 16 April 2014; *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL *(formerly EnCana Corporation v. Government of the Republic of Ecuador),* Award, 03 February 2006; *Generation Ukraine, Inc. v. Ukraine,* ICSID Case No. ARB/00/9, Award, 16 September 2003; *William Nagel v. The Czech Republic,* SCC Case No. 049/2002, Final Award, 09 September 2003.

the investment treaty.[22] Questions like the existence of rights/interests underlying investments and the legality of the investment are significant questions of jurisdiction *ratione materiae* which should be answered by reference to domestic law. Such references to domestic law for the determination of these threshold issues arguably gives the laws of the host state a prime role in settling disputes arising out of investment treaties. To assimilate the importance of domestic laws of the host state in this regard, it is sufficient to bear in mind that the jurisdictional conditions of an investment treaty tribunal are cumulative. Therefore, if only one pre-condition is non-existent, the whole case may be dismissed. This by itself explains the all-importance of local laws of the host state in determining the outcome of an investment treaty case.

11. Furthermore, as the recent practice of investment treaty tribunals reveals, courts of the host state have now a more determinative role in the resolution of investor-state disputes. For instance, there are clauses in certain investment treaties that require investors to resort primarily to the courts of the host state for a defined period (like 18 months) before initiation of their arbitration case. This, on the surface, gives a chance to the courts of the host state to resolve the dispute before the investor could bring the case to international arbitration. Before the 2010s, these preconditions were effectively ignored by investment treaty arbitral tribunals and an investor who had failed to use local remedies for the defined period of time was absolved by the arbitral tribunal, either on the basis of the doctrine of 'futility' or by circumventing the requirement by resorting to the MFN clause of the underlying investment treaty.[23] Recent practice, however, demonstrates that such clauses are being more effectively interpreted nowadays. In point of fact, according to the more recent decisions on this matter, when the treaty so requires, before filing its case before an arbitral tribunal, an investor has to use local remedies for the defined period of time and non-compliance with such a precondition would have serious jurisdictional or admissibility consequences for the investor's case.[24] This development gives a more prominent role to

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[22] See, for example, *Alasdair Ross Anderson et al. v. Republic of Costa Rica*, ICSID Case No. ARB (AF)/07/3, Award, 19 May 2010; *Bear Creek Mining Corporation v. Republic of Peru*, ICSID Case No. ARB/14/21, Award, 30 November 2017; *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines,* ICSID Case No. ARB/03/25, Award, 16 August 2007; *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania*, ICSID Case No. ARB/11/24, Award, 30 March 2015; *Metal-Tech Ltd. v. Republic of Uzbekistan*, ICSID Case No. ARB/10/3, Award, 04 October 2013; *Plama Consortium Limited v. Bulgaria*, ICSID Case No. ARB/03/24, Award, 27 August 2008; *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 15); *Vladislav Kim and others v. Republic of Uzbekistan*, ICSID Case No. ARB/13/6, Decision on Jurisdiction, 08 March 2017; *Yukos Universal Limited (Isle of Man) v. Russian Federation*, PCA Case No. AA 227, Final Award, 18 July 2014.

[23] See Chapter 7, subsection A.

[24] See, for instance, *ICS Inspection and Control Services Limited v. The Argentine Republic*, PCA Case No. 2010-9, Award on Jurisdiction, 10 February 2012 (declining jurisdiction due to the claimant's failure to comply with the 18-month local courts requirement provided for by Article 8 of the Argentina-UK BIT and finding that the MFN clause did not extend to international dispute resolution issues); *Daimler Financial Services AG v. Argentine Republic*, ICSID Case No. ARB/05/1, Award, 22 August 2012 (finding by majority that the claimant does not have yet standing to assert its claims under the treaty because the investor had failed to observe the 18-month recourse to-local-courts requirement set forth in Article 10 of the Argentina-Germany BIT and finding that the MFN clause could not be used by the claimant to circumvent the conditions precedent to arbitration laid down in Article 10 of the BIT.) (The claimant's subsequent attempts to have this award annulled failed. *Daimler Financial Services AG v. Argentine Republic*, ICSID Case No. ARB/05/1, 07 January 2015, Decision on Annulment); *Kiliç İnşaat İthalat İhracat Sanayi Ve Ticaret Anonim Şirketi v. Turkmenistan*, ICSID Case No. ARB/10/1, Award, 02 July 2013 (finding that recourse

the courts of the host state as the first stop in the resolution of investment disputes. Moreover, the findings and the practice of the courts of the host state have in more recent years become the first reference book for arbitration tribunals when dealing with matters of municipal law in an investment treaty case.[25] For instance, if the question is whether the investor has committed a crime of bribery in the course of establishment of its investment, arbitral tribunals usually refer to the general practice of the courts of the host state in the application of municipal penal laws concerning bribery or to their specific rulings regarding the alleged bribery in question. These and other similar examples show that the courts of the host state which by the emergence of bilateral investment treaties were stripped of any function in the resolution of foreign investment disputes have now regained some of the lost roles in the field of investor-state arbitration.

12. The ever-increasing role of the laws and the courts of the host state in investor-state disputes is not limited to the practice of investment treaty tribunals. To be sure, when one reviews the text of the more recent investment treaties, one plainly sees that states are assigning more and more tasks to be discharged by the laws and the courts of the recipient state.
13. When one recalls that the two pillars of the 'localisation' theory were: (i) disputes arising out of foreign investment contracts should be resolved by reference to the host state law, and (ii) disputes arising out of foreign investment contracts should be resolved by the national courts of the host state and then considers this 'creeping' growth of the role of the municipal laws and municipal courts of the host state in the resolution of investment treaty arbitration disputes, one may pause to ponder the question of the overall impact of this 'remarkable comeback' of municipal laws and courts on the whole regime of investment treaty arbitration. Indeed, keeping these developments in law in mind – regarding the role of the laws and the courts of the host state in investment treaty arbitrations – it is not untenable to suggest that the forgotten doctrine of 'localisation' – which was once applied to foreign investment contracts – has been revived in the land of investment treaty arbitrations to some extent.

## II. Questions and Arguments

14. In light of the above, the main research question that this Thesis seeks to answer is (a) what is the role of domestic law in the jurisdiction *ratione materiae* of an investment treaty tribunal? and (b) to what extent has the 'localisation' theory been revived in light of the current role of the host state law in jurisdictional and other matters in investor-state arbitrations and the growing importance of the role of the courts of the host state in the resolution of investment treaty cases?

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to local courts in Article VII.2 of the Turkey-Turkmenistan BIT to be an impermissible requirement and precondition and eventually finding that it lacked jurisdiction over the dispute.)

[25] See, for instance, *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Award, 07 July 2004 [55]; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Decision of the *ad hoc* Committee on the Application for Annulment of Mr. Soufraki, 05 June 2007 [96]-[97]; *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide, 23 December 2010 [236]; *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 21) [175]; *Vigotop Limited v. Hungary*, ICSID Case No. ARB/11/22, Award, 1 October 2014 [509].

15. To find the answer to this main research question, the two Parts of this Thesis will try to ask and answer a number of sub-questions. In Part I, the Thesis enquires about the ensuing questions: (i) Does domestic law apply in investment treaty arbitrations? (ii) If domestic law is applied in investment treaty arbitrations, is it applied only as 'fact', as held by the PCIJ in *Certain German Interests in Polish Upper Silesia*,[26] or is it applied as 'law'? (iii) What is the role of domestic law, in particular, the domestic law of the host state, in determining the jurisdiction of an investment treaty tribunal? (iv) More specifically, what is the function of the domestic law of the host state in determining the jurisdiction *ratione materiae* of an investment treaty tribunal (which questions of jurisdiction *ratione materiae* are governed or impacted by host state law)? (v) What are the legal grounds for the application of domestic law of the host state to the questions of jurisdiction *ratione materiae* of an investment treaty tribunal? (vi) What are the legal consequences of the application of host state law to the jurisdiction *ratione materiae* of an investment treaty arbitral tribunal? (vii) How should an investment treaty tribunal ascertain the contents of the host state law? In Part II, the Thesis will look for answers for the following questions: (i) What were the roots, tenets, and pillars of the 'localisation' theory and what happened to this theory? (ii) What elements were responsible for the disappearance of the 'localisation' theory? (iii) More specifically, what was the role of bilateral investment treaties in wiping out the 'localisation' theory? (iv) Exploring the current state of jurisprudence and trends in investment treaty rulemaking, what can one say regarding the current role of the host state law in investment treaty arbitrations; (v) In the same vein, being mindful of the current state of jurisprudence and trends in investment treaty rulemaking, what can one say regarding the role of the host state courts in investment treaty arbitrations? (vi) Recalling answers to all previous questions in Part I and Part II of this Thesis, to what extent can one claim that the forgotten 'localisation' theory has been revived in the field of investment treaty arbitrations?
16. In short, this Thesis seeks to show in Part I that domestic law of the host state, and in certain instances, domestic law of the home state, applies in investment treaty arbitrations. In some cases, mostly matters of merits entailing an analysis as to whether the host state has complied with the treaty's substantive standards of protection as well as in issues of compensation, domestic law is applied principally in its 'factual' cloak. However, as will be shown, in a number of important jurisdictional matters, particularly matters concerning the jurisdiction *ratione materiae*, the laws of the host state are applicable as 'law', thus, directly determining the jurisdictional questions before an investment treaty tribunal. These areas of influence of the domestic law include, amongst other things, the legality of the investment and the creation/existence of property rights constituting investments. There are two principal grounds which warrant the application of domestic law of the host state as the 'law' applicable to these jurisdictional questions: first, the agreement of the contracting parties in the underlying investment treaty, and second, the nature of the issue which requires the application of the host state law. In the latter situations, although the parties to the treaty do not expressly refer to the application of domestic law to a given issue, they nevertheless use concepts like 'national', 'property', 'asset' etc. which, absent a definition in the treaty itself or through subsequent agreement or practice, could only be

[26] *Certain German Interests in Polish Upper Silesia* (*Germany v. Poland*), Judgment, P.C.I.J. Rep. Series A, No. 7, 1926 (25 May 1926) p 19.

determined pursuant to an analysis of domestic law.[27] Indeed, when these concepts have not otherwise been defined by the parties in the treaty or through subsequent agreement or practice, one would be left with a situation that customary international law has no answer to these issues. To avoid a situation of *non liquet*, the tribunal should refer to a body of law which has an answer to these questions. In such instances of a vacuum in international law, the application of general principles of law and conflict of laws rules leads to the application of local laws to the jurisdictional questions before the tribunal. It is further submitted that the application of the host state law to these subject-matter jurisdiction questions does entail important legal consequences for the tribunal's decisions on its competence, sometimes ending with dismissing jurisdiction to the whole case. As will also be established in Part I, there are reliable methods to ascertain the contents of the host state law in order to approach the above-mentioned threshold questions, chief amongst them being the case law and practice of the national courts of the host state.

17. Part II of the Thesis will show that the 'localisation' theory with its tendency to dominate the laws and the courts of the host state over foreign investment disputes was seriously defeated by a flood of commentaries and arbitral awards, but most importantly by the advent of bilateral investment treaties, equipping foreign investors with the unprecedented opportunity to avail themselves directly of international arbitration against the host state for seeking redress against violations of treaty standards governed principally by international law. However, as will be demonstrated, recent trends in investment treaty lawmaking and the jurisprudence of investment treaty tribunals now consider a much more influential role for the laws and courts of the host state, which in some respects is reminiscent of the then 'localisation' theory. Based on these developments, and the answers already provided to questions in Part I, it is my considered argument that the 'localisation' theory has been partially revived in the field of investment treaty arbitration.

## III. Structure

18. This Thesis is divided into two Parts. Part I concerns the role of domestic law in investment treaty arbitrations. In particular, the focus in Part I will be on the function of the domestic law of the host state in determining the jurisdiction *ratione materiae* of an investment treaty tribunal. This Part is broken into four Chapters (Chapters 1-4). Building on what has transpired in Part I, Part II of this Thesis entails an analysis of the 'localisation' theory and considers whether it has been revived in the field of investment treaty arbitration through the latest developments in the practice of investment treaty tribunals and trends in investment treaty rulemaking. Three Chapters comprise Part II (Chapters 5-7). The contents of each of these seven (7) Chapters are briefly described below.
19. **Chapter 1**: Following this Introduction, the first Chapter examines the role of domestic law (whether that of the host state or the home state) in matters of jurisdiction and merits in investment treaty arbitrations in general. This Chapter will pinpoint the situations that domestic law applies as 'law' and the situations that this body of law is taken into account as 'fact'. The function of Chapter 1 is, thus, outlining and flagging the role of the domestic law in investment treaty arbitrations in general.
20. Having set out the role of domestic law in investment treaty arbitrations in general, the following two Chapters will focus on the two particular subject-matter jurisdiction issues foreshadowed in Chapter 1, i.e., the legality requirement and the existence and creation of

[27] J Crawford (n 18) 54.

private law rights/interests underlying investments. These two Chapters will demonstrate the basis on which the internal laws of the host state apply to these questions in investment treaty arbitrations and will show what legal consequences would follow from the application of the local laws of the host state to these jurisdictional prongs. Furthermore, these twin Chapters will be followed by another Chapter which will examine the modality by which the contents of the host state domestic law should be ascertained by investment treaty tribunals. Thus, with the scene being set in Chapter 1 for more technical issues, **Chapter 2** of this work moves on to consider a particularised issue of subject-matter jurisdiction and the role that the laws of the host state play in the determination of the related question. The specific subject-matter jurisdiction question that Chapter 2 attends to is the legality requirement. **Chapter 3** looks into a distinct but subject-matter jurisdiction-related question of the creation and the existence of property rights underlying investments and the function that host state law carries out in resolving discrepancies in this connection. Unfortunately, many of the awards and literature which have found the laws of the host state applicable to the question of the creation and the existence of property rights have done so in a conclusory manner and without much reasoning. In particular, these conclusions have been, more often than not, totally divorced of the required conflict of laws analysis when such an analysis is required. This Chapter will, thus, demonstrate that in many occasions, a classic conflict of laws analysis attests to the application of the host state law to the question of the creation and the existence of property rights constituting investments. **Chapter 4** of this Thesis will then consider the question of the modality of ascertaining the contents of the laws of the host state. The discussions in Chapter 4 apply equally to both issues of subject-matter jurisdiction discussed in Chapters 2 and 3, i.e., the legality requirement and the creation and existence of rights/interests underlying investments.

21. In **Part II** of this Thesis, I turn to the question of whether, in light of the recent developments, the theory of 'localisation' has been revived in the context of investment treaty law. In order to do so, in **Chapter 5**, I go through a historical review of the theory of 'localisation'. In the course of this discussion, I will first move on to review the genesis and the historical background of this theory. In particular, the examination will demonstrate the considerable endeavour that developing countries went through on various fronts to strengthen this theory. The discussion will then be followed by exploring the contents of this legal theory in its heyday, especially in the period of the 1960s-1980s. As will be seen, the 'localisation' theory rested on two pillars: **First**, laws of the host state govern the foreign investment contract and the consequent contractual dispute. **Second**, the competent forum for resolving any contractual discrepancies between the host state and the foreign investor is a court and/or a tribunal of the host state. Finally, the consideration of the classic 'localisation' theory will come to an end by attending to the nadir of the theory, and, in particular, the role that bilateral investment treaties played in the fall of this theory. **Chapters 6 and 7** of this Thesis undertake to examine whether the 'localisation' theory has been revived in the context of investment treaty law in light of the recent developments of this body of international law. As was alluded to above, the classic 'localisation' theory was founded on two principles: **First**, laws of the host state govern the foreign investment contract and the consequent contractual dispute. **Second**, the competent forum for resolving any contractual discrepancies between the host state and the foreign investor is a court and/or a tribunal of the host state. As noted above, Chapters 1 to 4 of this Thesis deal

with the role of the host state law in the resolution of investment treaty disputes in general and the role of such law in the settling of matters of subject-matter jurisdiction in particular. **Chapter 6** will offer a contextualised distillate of Chapters 1 to 4, briefly recalling the role of host state law in the resolution of investment treaty disputes in general and the question of jurisdiction *ratione materiae* of an investment treaty tribunal in particular. This brief recollection will be followed by a brief comparison of investment treaty arbitration and rulemaking practice in the invocation of the laws of the host state in different periods in order to show the shift in the attention to the laws of the host state in the resolution of such issues. Having dealt with the role of the laws of the host state in Chapter 6, the main task of **Chapter 7** will then be to examine the role of the host state courts and tribunals in the resolution of investment treaty disputes. As will be seen in this Chapter, on some occasions, the courts of the host state have a direct role in the resolution of certain investment disputes. In addition, there are other occasions in which the courts and the tribunals of the recipient state have an indirect, but determinative, function in the settlement of some investment treaty disputes. Such municipal courts have a direct role in the resolution of investment disputes when they are one of, or the only, option(s) for a foreign investor to pursue investment treaty claims. These national judicial *fora* also have an indirect saying on jurisdictional or substantive issues when they should be referred to by the investor prior to the filing of the investment treaty dispute before investment treaty arbitration tribunals. This mostly occurs on two occasions: (i) when local remedies should be used for a defined timeframe as a precondition for the initiation of arbitral proceedings. (ii) when preliminary recourse should be had to the courts of the host state as a precondition to establishing the violation of the substantive treaty standards. Another indirect role of the national courts of recipient states in investor-state arbitrations is in matters which squarely fall within the jurisdiction of investment treaty tribunals but are better analysed and spelled out by the municipal courts of the host state. For instance, although it is for each investment treaty tribunal to rule upon its own subject-matter jurisdiction, the determinations of the courts of the host state in domestic law issues that an investment arbitration tribunal has to deal with as a preliminary matter, e.g., the existence of enforceable contractual rights underlying investment, are the best sources of inspiration for investment treaty tribunals. Chapter 7 will try to cover all these areas.

22. Since the role of the domestic laws of the host state in determining the jurisdiction *ratione materiae* of an investment treaty tribunal has not been previously explored in a comprehensive manner, I have devoted the lion share of Part I of this Thesis (consisting of Chapters 2 and 3) to dissecting the theoretical and practical function of the municipal laws of the host state in the subject-matter jurisdiction of investor-state arbitral tribunals. The novelty and originality of these two relatively longer Chapters is that they thoroughly analyse the legal bases for referring to the laws of the host state for the purpose of determining whether an underlying private right/interest exists and whether the investment in question stemming from the above-described right/interest has been made legally. These two Chapters produce new knowledge by discussing and analysing the actual application of the internal laws of the host state to subject-matter jurisdiction questions that may be posed to an investment treaty tribunal in practice. In contrast, matters concerning the role of the host state courts in investor-state arbitrations have already been discussed by

others.[28] As such, I have, as a consequence, allocated one Chapter (i.e., Chapter 7) directly to this discussion summarising the treaty practice, case law, and academic writings in this regard. Chapter 7, however, not only merely reproduces the treaty practice, case law, and academic writings on the subject; it portrays the recent trends in bolstering the role of the courts of the host state in international investor-state dispute settlement and thus constitutes an original contribution to existing knowledge on the subject-matter. Chapter 7 also identifies and synthesises all the four pertinent major recent developments regarding the promotion of the functioning of the national courts of the recipient state in the resolution of investment treaty disputes.

23. Finally, the Conclusion of this Thesis will undertake to make some concluding remarks regarding the two principal issues that this Thesis is entrusted to deal with: first, the role of the domestic laws of the host state in determining the jurisdiction *ratione materiae* of investment treaty tribunals, and, second, whether the classic 'localisation' theory has been revived in the course of the recent developments in investment treaty law. Indeed, the Conclusion will examine, first, the extent which the laws of the host state are relevant in settling matters of jurisdiction *ratione materiae* of investment treaty tribunals and, second, the extent that the growing importance of the role of the laws and the courts of the host state in investment treaty law tends to revive the 'localisation' theory in the context of investment treaty arbitrations.

## IV. Essential Concepts

24. In order to properly understand certain fundamental concepts not otherwise properly defined or described throughout this Thesis, in what follows, I have undertaken to address certain concepts and issues at the outset. The concepts under consideration here are 'applicable law' and 'domestic law'.

### A. Applicable Law

25. Every agreement has a governing law, which is called 'proper law' in common law, and 'applicable law' in continental law.[29] Indeed, a contract cannot exist in a vacuum.[30] The

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[28] See, for instance, B Demirkol, *Judicial Acts and Investment Treaty Arbitration* (CUP 2018); J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 103 *et seq*; C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (2005) 4(1) The Law & Practice of International Courts and Tribunals; C Schreuer, 'Interaction of International Tribunals and Domestic Courts in Investment Law' in Arthur W. Rovine (ed), *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (Martinus Nijhoff Publishers 2010).

[29] J Hill & MN Shuilleabhain (eds), *Clarkson & Hill's Conflict of Laws* (OUP 2016) 211; AFM Maniruzzaman, 'Choice of Law in International Contracts, Some Fundamental Conflict of Laws Issues' (1999) 16(4) J Int'l Arb 141. See also N Blackaby & C Partasides (eds), *Redfern and Hunter on International Arbitration* (OUP 2015) 157 (using the following various terms to describe the same concept: 'applicable law', 'governing law', 'the proper law of the contract', and 'the substantive law'.)

[30] As FA Mann has eloquently put it, "freedom of contract does not exist independently of the legal systems which grant it or confer any measure of sovereignty upon the contracting parties." See FA Mann, 'The Proper Law of Contracts Concluded by International Persons' (1959) 35 BYIL 56. See also *Saudi Arabia v. Arabian American Oil Company* (*Aramco*) (1963) 27 ILR (indicating that "[i]t is obvious that no contract can exist *in vacuo*, i.e. without being based on a legal system. The conclusion of a contract is not left to the unfettered discretion of the parties. It is necessarily related to some positive law which gives legal effect to the reciprocal and concordant manifestations of intent made by the parties. The contract cannot even be conceived without a system of law under which it is created.")

governing law with which we are concerned here deals with the substance of the dispute, i.e., the so-called "*lex cause*", rather than the law governing the arbitral procedure.[31] The applicable substantive law determines various questions regarding the rights, obligations, and liabilities of the parties.[32]

26. In case of bilateral investment treaties which accord both substantive and procedural rights to investors, the substantive applicable law, in its totality and comprising all of its components, also determines the Tribunal's jurisdiction. Jurisdiction is a well-known concept which has four aspects: *ratione materiae, ratione personae*, *ratione temporis*, and *ratione voluntatis*.[33] Jurisdiction *ratione materiae* (subject-matter jurisdiction) refers to a court or a tribunal's authority to decide a particular dispute. As noted above, in investment treaty arbitrations, the particular law applicable to the jurisdiction of the tribunal may be different from the particular law applicable to the merits.[34] Although as a principle, splitting the applicable law is not usually desirable,[35] when necessary, as Giuliano and Lagarde have put it, sometimes it is 'logically consistent' when the choice of another applicable law "relate[s] to elements in the contract which can be governed by different laws without giving rise to contradictions."[36] As such, this Thesis will mainly dissect the law applicable to the jurisdiction *ratione materiae* of an investment treaty tribunal which could be

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See also Lord McNair, 'The General Principle of Law Recognized by Civilized Nations' (1957) 33 BYIL 7; N Blackaby & C Partasides (n 29) 156-157.

[31] See N Blackaby & C Partasides (n 29) 157 (identifying various systems of law that have a bearing on an international arbitration, e.g., the law governing the arbitration agreement, the law governing the capacity of the parties, the law governing the procedure of arbitration, the law governing the recognition and enforcement of an arbitration agreement, and the applicable substantive law.) As noted, it is the latter body of law with which we are principally concerned in this Thesis.

[32] N Blackaby & C Partasides (n 29) 185-186.

[33] M Sornarajah, *The International Law on Foreign Investment* (n 3) 359-360. See also *Phoenix Action, Ltd. v. The Czech Republic*, ICSID Case No. ARB/06/5, Award, 15 April 2009 [54]. There is sometimes a suggestion of a further aspect of jurisdiction, i.e., *ratione loci*. The addition of this supposed extra component, however, seems to be mistaken as "international jurisdiction exists outside territorial jurisdiction so it is conceptually not a place—*locus*—but rather a space." See V Heiskanen, '*Menage a` trois*? Jurisdiction, Admissibility and Competence in Investment Treaty Arbitration' (2013) 29(1) ICSID Rev-FILJ 237.

[34] A Newcombe & L Paradell (n 13) 77 (making a distinction between "the law applicable to the substance of the dispute" and "the law applicable to jurisdictional issues"). On the same point, it should be recalled that Article 42 of the ICSID Convention on applicable law is not helpful in determining the applicable law to jurisdiction. In *CMS v. Argentina*, the tribunal correctly said: "Article 42 is mainly designed for the resolution of disputes on the merits and, as such, it is in principle independent from the decisions on jurisdiction, governed solely by Article 25 of the Convention and those other provisions of the consent instrument which might be applicable, in the instant case the Treaty provisions…" The 'consent instrument' under examination in this case was an international investment agreement, which in turn has express or implied references to the national law of either of the contracting states in some respects including on matters of jurisdiction. See *CMS Gas Transmission Company v. Argentine Republic* (n 13) [88]. The tribunal in *Noble Energy v. Ecuador* adhered to this viewpoint. It noted: "The Tribunal is of the opinion that Article 42(1) is irrelevant for purposes of jurisdiction. Article 42 of the ICSID Convention is a conflict rule which deals with the law governing the merits of the dispute […] Jurisdiction is a different matter. It is not subject to this conflict rule but is governed by Article 25 of the ICSID Convention." See *Noble Energy, Inc. and Machalapower Cia. Ltda. v. The Republic of Ecuador and Consejo Nacional de Electricidad* (n 13) [57]. See also *Saipem S.p.A. v. The People's Republic of Bangladesh* (n 13) [68].

[35] J Hill & MN Shuilleabhain (n 29) 225.

[36] M Giuliano & P Lagarde, 'Report on the Convention on the Law Applicable to Contractual Obligations' (1980) C 282 Official Journal 17.

different from the substantive law governing the issues of merits and reparation in an investor-state dispute.

27. The second point of prime significance under the rubric of 'applicable law' is recalling the importance of choosing the right applicable law to a given question. It is of vital importance to determine the applicable substantive law to legal questions arising in investment treaty arbitrations since "the outcome of the dispute may sometimes greatly depend on the rules determined to be applicable."[37] The failure by an investment treaty arbitral tribunal to select and apply the proper law may result in the annulment or non-enforcement of the investment treaty award. Pursuant to Article 52(1)(b) of the ICSID Convention,[38] failure to select and apply the proper law may be a valid ground for annulment of the arbitration award.[39] Such an approach is indeed warranted. The simple reason is that, as noted above, the applicable law determines the fate of the case and the correct selection of the proper law is the first

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[37] Y Banifatemi 'The Law Applicable in Investment Treaty Arbitration' in K Yannaca-Small (ed) *Arbitration under International Investment Agreements* (OUP 2010) 192. See also AFM Maniruzzaman, 'State Contracts in Contemporary International Law: Monist versus Dualist Controversies' (2001) 12(2) Eur. J. Int'l L. 309; E Gaillard & Y Banifatemi, 'The Meaning of "and" in Article 42(1), Second Sentence, of the Washington Convention: The Role of International Law in the ICSID Choice of Law Process' (2003) 18(2) ICSID Rev-FILJ 380-381.

[38] Article 52(1) of the ICSID Convention reads: "(1) Either party may request annulment of the award by an application in writing addressed to the Secretary-General on one or more of the following grounds: […] (b) that the Tribunal has manifestly exceeded its powers."

[39] See JF Armesto, 'Different Systems for the Annulment of Investment Awards' (2011) 26(1) ICSID Rev-FILJ 139 (stating that: "ICSID *ad hoc* committees have concluded that manifest excess of powers can occur if tribunals err by: • Totally disregarding the applicable law, or • Basing the award on a law that is not the applicable law under Article 42 of the ICSID Convention."). For the practice of ICSID on this matter, see e.g., *Klöckner Industrie-Anlagen GmbH and others v. United Republic of Cameroon and Société Camerounaise des Engrais*, ICSID Case No. ARB/81/2 (Klöckner I), Decision on Annulment, 03 May 1985 [3], [59]-[60], and [83]; *Amco Asia Corporation and Others v. Indonesia*, ICSID Case No. ARB/81/1, Decision on the Application for Annulment, 16 May 1986 [7.28]; *Maritime International Nominees Establishment v. Republic of Guinea*, ICSID Case No. ARB/84/4, Decision on Annulment, 22 December 1999 [4.04], [5.04]; *Wena Hotels Ltd. v. Arab Republic of Egypt*, ICSID Case No. ARB/98/4, Decision (Annulment Proceeding), 05 February 2002 [21 *et seq*]; *CDC Group plc v. Republic of Seychelles*, ICSID Case No. ARB/02/14, Decision on Annulment, 29 June 2005 [44 *et seq*]; *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile*, ICSID Case No. ARB/01/7, Decision on Annulment, 21 March 2007 [44]-[49], and [58 *et seq*]; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Decision of the *ad hoc* Committee on the Application for Annulment of Mr Soufraki (n 25) [83 *et seq*]; *Empresas Lucchetti, S.A. and Lucchetti Peru, S.A. v. The Republic of Peru*, ICSID Case No. ARB/03/4, Decision on Annulment, 05 September 2007 [97]-[98]; *CMS Gas Transmission Company v. The Republic of Argentina*, ICSID Case No. ARB/01/8, Decision of the *ad hoc* Committee on the Application for Annulment of the Argentine Republic, 25 September 2007 [48]-[51]; *Patrick Mitchell v. Democratic Republic of Congo*, ICSID Case No. ARB/99/7, Decision on Annulment, 01 November 2007; *Azurix Corp. v. The Argentine Republic* (n 14) [136]; *Helnan International Hotels A/S v. Arab Republic of Egypt*, ICSID Case No. ARB/05/19, Decision of the Ad hoc Committee on Annulment, 14 June 2010 [55]; *Sempra Energy Int'l v. Argentine Republic*, ICSID Case No. ARB/02/16, Decision on Annulment, 29 June 2010; *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Decision on the Application for Annulment of the Argentine Republic, 30 July 2010 [67], [377], [393], and [405]; *Mobil Cerro Negro Holding, Ltd., Mobil Cerro Negro, Ltd., Mobil Corporation and others v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/07/27, Decision on Annulment, 09 March 2017. For doctrinal authorities in this respect, see AK Bjorklund, 'Applicable Law in International Investment Disputes' in C Giorgetti (ed), *Litigating International Investment Disputes: A Practitioner's Guide* (Brill 2014) 262; E Gaillard, 'The Extent of Review of the Applicable Law in Investment Treaty Arbitration,' in E Gaillard & Y Banifatemi (eds) *Annulment of ICSID Awards, IAI International Arbitration Series No. 1* (Juris Publishing 2004) 223; C Schreuer *et al* (n 13) 191-270; A Broches, 'Observations on the Finality of ICSID Awards' (1991) 6(2) ICSID Rev-FILJ 92. In the context of *ad hoc* UNCITRAL investment arbitrations, see *The Czech Republic v. CME Czech Republic B.V.*, Challenge of Arbitral Award, Judgement of Svea Court of Appeal, 15 May 2003 (2003) 42 ILM 919, 963.

necessary substantive prerequisite of the correct settlement of the dispute. Indeed, in certain cases, the application of international law may result in finding a violation on the part of the host state whereas if one were to apply domestic law to the same factual scenario, the claim may be dismissed by the arbitral tribunal for lack of any breach. The same could happen the other way round. The ICJ observed in the *ELSI* case that "what is a breach of treaty may be lawful in the municipal law and what is unlawful in the municipal law may be wholly innocent of violation of a treaty provision."[40]

28. Finally, I should say a few words on the method to identify the applicable law to jurisdictional questions in investment treaty arbitrations. When faced with a legal question that it needs to resolve, a tribunal has to determine the applicable law to that question in the first place. This requires a conflict of laws analysis. However, in the investment treaty arbitration field, there does not seem to be so many commentators and/or arbitrators who have approached the question based on a proper conflict of laws analysis, which is the sound approach to identify the governing law to a particular issue. This is sometimes a problem of having too much expertise in one field of law without having an interest in the other. As Pierre Lalive has aptly observed, "too many distinguished public international lawyers seem to have little experience or understanding in problems in choice of law."[41] In his monograph on the "International Law of Investment Claims", Zachary Douglas describes the need to refer to conflict of laws rules to be more 'acute' in investment treaty arbitrations in comparison to public international disputes. He explains that in the absence of conflict of laws rules in investment treaties, the tribunals should articulate such rules by having recourse to general principles of private international law and principles derived from the particular architecture of investment treaties.[42] He then goes on to point out that:

> Some choice of law rules have attained such universal application that their transplant into the investment treaty regime cannot generate controversy. Such is the case with the *lex situs* rule for tangible property, which is universally applied by municipal courts […] and must be the appropriate choice of law rule for determining the existence or scope of property rights that comprise an investment. There is considerable authority for the proposition that the application of the *lex situs* rule is even required by general international law …[43]

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[40] *Elettronica Sicula S.p.A. (ELSI)* (*United States of America v. Italy*), Judgment, I.C.J. Rep. 1989 (20 July 1989) p 15, p 51 [73]. See also Article 3 of the Draft Articles on the Responsibility of States for Internationally Wrongful Acts ("Draft Articles") by the International Law Commission ("ILC") adopted in August 2001; *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic* (n 12) [95]-[96] (relying on Article 3 of the Draft Articles).

[41] P Lalive, 'Concluding Remarks', in E Gaillard and Y Banifatemi (eds), *Annulment of ICSID Awards* (Juris Publishing 2004) 313.

[42] On this point, see also C McLachlan, 'Investment Treaty Arbitration: The Legal Framework' in AJ van den Berg (ed), *50 Years of the New York Convention, ICCA International Arbitration Conference* (Kluwer Law International 2009) 143 (stating with regard to the appropriate choice of law approach in investment treaty arbitrations that: "… [T]his choice of law process may be distinguished from that undertaken in private international litigation or arbitration, since national and international law stand in a vertical, and not horizontal, relationship to each other.")

[43] Z Douglas, *The International Law of Investment Claims* (CUP 2009) 44-45.

29. Therefore, when required to identify the applicable law, an investment treaty tribunal should refer to the conflict of laws rules as they may be applicable in an investment treaty case. Some choice of law rules, like the *lex situs*, are so widely-accepted throughout the world that I can reasonably argue that the rule in question constitutes a 'general principle of law' which a tribunal needs to consider as a source of law under Article 38(1) of the Statute of the ICJ and as a tool of interpretation under Article 31 of the Vienna Convention on the Law of Treaties ("VCLT").

### B. Domestic Law

30. Throughout this Thesis, I refer directly or by reference to various terms synonymous with 'domestic law', such as 'municipal law', 'internal law', 'national law', and 'local law'.[44] As explained in Brownlie's Principles of Public International Law, although these terms might have 'slightly different connotations', in this Thesis, they are all used interchangeably to refer to the same concept which is 'the legal order of or within the state'.[45] Unless otherwise stated, the term domestic law in this Thesis refers to the domestic law of the host state.

## V. Thesis Approach and Sources

31. In the three subsections that will follow, I will outline my general approach and my interpretive approach in this Thesis regarding the questions that I seek to answer and will explain the sources that I have availed myself of in analysing the issues at stake.

### A. General Approach

32. Throughout this Thesis, I will undertake various academic exercises. Mostly I deal with the questions at issue in this Thesis in an analytical way. In certain limited points, the effort undertaken entails a descriptive exercise in that I have considered the past and/or current state of international law in general or international investment law in particular. The creativity in such exercises is actually identifying the practice, drawing the threads of such practice together, and distilling the applicable principles from the identified practice. Indeed, the novelty of this Thesis in such situations is gathering the bits and pieces scattered around and not picked up by others and trying to draw a meaningful picture of the investment treaty law as concerns the matters in question. In addition, in the course of this Thesis, I will come across issues as to which no practice exists or the existing practice is inconsistent or unpersuasive. In all such circumstances, the analysis will tend to enter into a problem-solving effort in order to provide guiding principles to the reader with regard to the unresolved matters at stake.
33. It should also be noted that I have tried to reflect the views expressed by others (including jurisprudence and scholarship) on any difficult issue as much as possible. However, as the present Thesis is an analytical piece of academic work, I have offered my own independent legal view on each subject in an effort to add a brick on the wall of legal knowledge.

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[44] See G Fitzmaurice (n 18) 68 (enumerating the various titles that refer to the same concept: "… State law, or domestic, municipal, national, or internal law, as it is variously called.")

[45] J Crawford (n 18) 48.

## B. Interpretive Approach

34. Bilateral investment treaties are treaties in the sense of Article 2(1)(a) of the VCLT. Therefore, in order to interpret them, one should employ rules of treaty interpretation. For various purposes in this Thesis, I will undertake a treaty interpretation exercise. Thus, it is important to clarify the approach to treaty interpretation at the outset.
35. My point of departure for treaty interpretation would be Articles 31 and 32 of the VCLT. By the end of May 2019, 116 countries have ratified the VCLT.[46] Therefore, it is widely applicable in the relations between various states in regulating their overseas international investment relations as set out in investment treaties. Moreover, these provisions of the Vienna Convention reflect customary international law rules of treaty interpretation.[47] Article 31 of the VCLT enumerates various tools of interpretation, including 'the ordinary meaning of the terms', 'object and purpose', 'context', etc. In my opinion, treaty interpretation is a combined exercise in which all the tools and elements of interpretation should be analysed and weighed together.[48] Therefore, together with the 'text' and 'the

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[46] See <https://treaties.un.org/pages/ViewDetailsIII.aspx?src=TREATY&mtdsg_no=XXIII1&chapter=23&Temp=mtdsg3&clang=_en> 'accessed 31 May 2019'.

[47] See, e.g., *Daimler Financial Services AG v. Argentine Republic* (n 24) [46] (stating that "This claim arises under the German-Argentine BIT, in conjunction with the ICSID Convention. As both the BIT and the ICSID Convention are international treaties concluded between sovereign States, both are subject to the usual customary law rules governing treaty interpretation under public international law, as reflected in Articles 31 and 32 of the Vienna Convention on the Law of Treaties ("Vienna Convention"). The Tribunal will apply these rules in discerning whether all of the jurisdictional requirements of the ICSID Convention and the BIT have been met."); *Jan Oostergetel and Theodora Laurentius v. The Slovak Republic*, UNCITRAL, Final Award, 23 April 2012 [140] (holding that "with respect to the interpretation of the BIT, the Tribunal will resort to the Vienna Convention on the Law of Treaties […] to which both States are parties, and which is in any event recognized as a codification of the customary international law governing treaty interpretation …"); *Salini Costruttori S.p.A. and Italstrade S.p.A. v. The Hashemite Kingdom of Jordan*, ICSID Case No. ARB/02/13, Decision on Jurisdiction, 15 November 2004 [75] (noting that "The Tribunal shall proceed to the interpretation of this Article in conformity with Articles 31 to 33 of the Vienna Convention on the Law of Treaties which reflect customary international law.")

[48] It should be borne in mind that Article 31 of the VCLT contains the 'rule' [in singular in contrast to 'rules' in plural] of interpretation of treaties. This implies that all the means of interpretation referred to in this provision, should be considered in totality, as the "process of interpretation is a unity". The relevant Report of the ILC is instructive in this respect: "Having regard to certain observations in the comments of Governments, the Commission considered it desirable to underline its concept of the relation between the various elements of interpretation in article 27 [now Article 31] and the relation between these elements and those in article 28 [now Article 32]. Those observations appeared to indicate a possible fear that the successive paragraphs of article 27 might be taken as laying down a hierarchical order for the application of the various elements of interpretation in the article. The Commission, by heading the article "General rule of interpretation" in the singular and by underlining the connexion between paragraphs 1 and 2 and again between paragraph 3 and the two previous paragraphs, intended to indicate that the application of the means of interpretation in the article would be a single combined operation. All the various elements, as they were present in any given case, would be thrown into the crucible, and their interaction would give the legally relevant interpretation. Thus, article 27 is entitled "General rule of interpretation" in the singular, not "General rules" in the plural, because the Commission desired to emphasize that the process of interpretation is a unity and that the provisions of the article form a single, closely integrated rule. In the same way the word "context" in the opening phrase of paragraph 2 is designed to link all the elements of interpretation mentioned in this paragraph to the word "context" in the first paragraph and thereby incorporate them in the provision contained in that paragraph. Equally, the opening phrase of paragraph 3 "There shall be taken into account together with the context" is designed to incorporate in paragraph 1 the elements of interpretation set out in paragraph 3. …" Report of the International Law Commission on the Work of Its Eighteenth Session, Geneva, 04 May-19 July 1966 (1966) (Vol. II) YB ILC 219-220. See also *Aguas del Tunari, S.A. v. Republic of Bolivia*, ICSID Case No. ARB/02/3, Decision on Respondent's Objections to Jurisdiction, 21 October 2005 [91] (aptly observing that: "Interpretation under Article 21 [sic] of the

ordinary meaning of the terms', one should also take into account the 'context' and the 'object and purpose' of the treaty. In addition, a treaty should always be interpreted in 'good faith'.

36. That being said, I should emphasise here that while in any interpretive exercise all the means of interpretation will be taken into account, given the particular status of bilateral investment treaties, it is the text of the treaty which is the first point of reference and the most concrete means for understanding the parties' intention. To be sure, unlike other treaties, the contracting parties to a bilateral investment treaty do not usually create materials recording their subsequent agreement after the conclusion of the treaty. They also do not usually go about forming subsequent practices indicating their agreement regarding the interpretation of the treaty. In many cases, the preparatory work of the conclusion of bilateral investment treaties is unavailable or non-existent. As such, although there are certain exceptions, in most cases, investment treaty arbitrators cannot usually avail themselves of the other useful materials for treaty interpretation that adjudicators of disputes arising out of other treaties may have access to. Despite what was just said, when interpreting bilateral investment treaties, the text of the treaty is in many cases useful and should be set as the starting point. This is how other adjudicators start their analysis. Indeed, in *Territorial Dispute between Libya and Chad* case, the ICJ indicated that "interpretation must be based above all upon the text of the treaty".[49] Furthermore, and by the same token, the ICJ had already pronounced on an earlier occasion that "if the relevant words in their natural and ordinary meaning make sense in their context, that is the end of the matter".[50] Therefore, for any interpretation purpose, like determining the substantive scope of the legality requirement, the text of the investment treaty will be the starting point in the "search for the real intention of the contracting parties in using the language employed by them."[51]
37. The last observation to make in this regard is that the interpretations offered here are neither pro-state nor pro-investor. Rather, all interpretations in this Thesis seek to adopt a 'balanced approach' to the questions at issue.[52]

### C. Sources

38. There are three main sources which have been relied upon in this Thesis to support the arguments put forward. These three sources will be briefly considered below. For the avoidance of doubt, I should mention that the order in which the sources are presented here does not reflect an opinion on the hierarchy of sources from a theoretical perspective, but

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Vienna Convention is a process of progressive encirclement where the interpreter starts under the general rule with (1) the ordinary meaning of the terms of the treaty, (2) in their context and (3) in light of the treaty's object and purpose, and by cycling through this three step inquiry iteratively closes in upon the proper interpretation.")

[49] *Territorial Dispute* (*Libyan Arab Jamahiriya v. Chad*), Judgment, I.C.J. Rep. 1994 (03 February 1994) p 6, pp 21-22 [41]. This statement was repeated in *Legality of Use of Force* (*Serbia and Montenegro v. Belgium*), Preliminary Objections, Judgment, I.C.J. Rep. 2004 (15 December 2004) p 279, p 318 [100]: ("Interpretation must be based above all upon the text of the treaty.")

[50] *Competence of the General Assembly for the Admission of a State to the United Nations*, Advisory Opinion, I.C.J. Rep. 1950 (03 March 1950) p 4, p 8.

[51] Lord McNair, *The Law of Treaties* (Clarendon Press 1961) 366.

[52] See *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15, Decision on Jurisdiction, 27 April 2006 [70]; *Saluka Investments B.V. v. The Czech Republic*, UNCITRAL, Partial Award, 17 May 2006 [300]. See also T Gazzini, *Interpretation of International Investment Treaties* (Hart Publishing 2016) 161, 163.

rather is based on the importance of these as material sources or sources *sensu lato* in the practice of international investment law. These sources are as follows: First, the practice of international courts and tribunals, especially that of investment treaty tribunals. Second, investment treaties or treaties with investment provisions. Third, doctrinal authorities and works and reports of international organisations like the United Nations Conference on Trade and Development ("UNCTAD").

39. Beginning with the first source, i.e., the jurisprudence of international courts and tribunals, it is clear that there is no doctrine of precedent or *stare decisis* in international investment law as it exists in common law. However, if one reviews the publicly-available investment treaty awards and decisions, one clearly sees that previous awards and decisions in the same field are vastly referred to by arbitrators. They rely on previous decisions and awards not because they are legally obliged to do so. Rather, there is some kind of a moral obligation to satisfy the vital needs of predictability and consistency – as the pillars of any legitimate dispute resolution system – in investment treaty arbitration and that is why investment tribunals follow previous cases. As such, investment treaty tribunals rely on past cases either to seek guidance from previous decisions and awards and/or to underpin the decision they have arrived on a point of law.[53] This has created 'a *de facto* doctrine of precedent'[54] or as others would have it 'a common law of investment protection'.[55] The current state of the law and practice in terms of relying on precedent is well summarised by the *El Paso* tribunal which held that: "ICSID arbitral tribunals are established *ad hoc*, … and the present Tribunal knows of no provision, … establishing an obligation of *stare decisis*. It is nonetheless a reasonable assumption that international arbitral tribunals, notably those established within the ICSID system, will generally take account of the precedents established by other arbitration organs, especially those set by other international tribunals."[56]
40. Furthermore, there is an additional practical reason for the importance of precedent in investment treaty arbitrations. Taking into account the fact that in an investment treaty dispute, the host state and the investor did not have an opportunity to determine the applicable law to their dispute beforehand, certain investment treaty tribunals have inferred an agreement of the disputants on the applicable law on the basis of the rules of law invoked in their submissions during the proceedings, i.e., mutual choice of the applicable law after the emergence of the dispute.[57] It is no secret that in investment treaty cases, both sides of the dispute rely on previous cases "either to conclude that the same solution should be adopted in the case [at hand] or in an effort to explain why [the] [t]tribunal should depart

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[53] See G Kaufmann-Kohler, 'Arbitral Precedent: Dream, Necessity or Excuse?: The 2006 Freshfields Lecture' (2007) 23(3) Arb Int'l; C Schreuer & M Weiniger, 'Conversations Across Cases - Is there a Doctrine of Precedent in Investment Arbitration?' (2008) 3 TDM; JP Commission, 'Precedent in Investment Treaty Arbitration—A Citation Analysis of a Developing Jurisprudence' (2007) 24(2) J Int'l Arb; G Guillaume, 'The Use of Precedent by International Judges and Arbitrators' (2011) 2(1) Journal of International Dispute Settlement.

[54] See G Kaufmann-Kohler (n 53) 357-358.

[55] C McLachlan, L Shore & Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (OUP 2017) 20.

[56] *El Paso Energy International Company v. The Argentine Republic* (n 52) [39]. See also *AES Corporation v. The Argentine Republic*, ICSID Case No. ARB/02/17, Decision on Jurisdiction, 26 April 2005 [30]-[31]; *Saipem S.p.A. v. The People's Republic of Bangladesh* (n 13) [67].

[57] See *Asian Agricultural Products v. Democratic Republic of Sri Lanka* (n 16) [18]-[24].

from that solution."[58] Consequently, as a matter of practice, in the course of the proceedings, the disputants lead the arbitral tribunal to consider previous cases as a source of applicable law.[59]

41. First and foremost, the decisions and awards cited in this Thesis come from the ICSID jurisprudence. According to recent research, the cumulative number of known investor-state arbitrations pursuant to investment treaties was 855 by the end of 2017.[60] As the "dedicated framework for the arbitration of investor-state dispute",[61] ICSID has been host to over sixty percent of known investor-state arbitration cases.[62] Case law produced under other arbitral rules (in particular, cases under the UNCITRAL Arbitration Rules)[63] and other forums have also been extensively relied upon in this Thesis. I have vastly used the electronic database of ITALAW in order to access the publicly-available awards and decisions referred to in this Thesis.[64]
42. The practice of these arbitral tribunals interpreting the same or similar provisions of interest in investment treaties, like the legality requirement, or on other topics in question in this Thesis, e.g., the existence and creation of rights/interests underlying investments, is very assistive in recognising the right approach to the questions posed by this Thesis when such an arbitral practice is consistent with regard to a given question.[65] Obviously, when the practice of arbitral tribunals on a specific matter is inconsistent, I have tried to adopt the most persuasive approach amongst the diverged practice. On the other hand, if no clear or

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[58] See, e.g., *Saipem S.p.A. v. The People's Republic of Bangladesh* (n 13) [66]; *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 15) [45].

[59] *El Paso Energy International Company v. The Argentine Republic* (n 52) [39].

[60] UNCTAD, 'Investor-State Dispute Settlement: Review of Developments in 2017' (United Nations 2018) 2.

[61] C McLachlan, L Shore & Matthew Weiniger (n 55) 4.

[62] According to a recent Report by UNCTAD, taking into account cases filed between 1987 and July 2017, 55% of the known investor-state arbitrations have been filed under the ICSID Convention and 6% of such disputes have been submitted under the ICSID Additional Facility Rules. UNCTAD, 'Special Update on Investor-State Dispute Settlement: Facts And Figures' (United Nations 2017) 5.

[63] According to the same report, of all the filed investor-state cases known in the above-mentioned period, 31% were filed under the UNCITRAL Arbitration Rules. See UNCTAD (n 62) 5.

[64] See <https://www.italaw.com/> 'accessed 31 May 2019'.

[65] In such circumstances, one can speak of some sort of *jurisprudence constante*: "a series of cases that resolve a particular issue in a certain way, which then acts as a guide in the future in resolving that same issue." See G Kaufmann-Kohler (n 53) 360. The late Thomas Wälde considered in his separate opinion in the *International Thunderbird Gaming* case that the consistent practice of investment treaty tribunals on a given issue may, after satisfaction of certain conditions, create rules of customary international law

> While individual arbitral awards by themselves do not as yet constitute a binding precedent […], a consistent line of reasoning developing a principle and a particular interpretation of specific treaty obligations should be respected; if an authoritative jurisprudence evolves, it will acquire the character of customary international law and must be respected […] An increasingly continuous, uncontested and consistent modern arbitral jurisprudence is part of the authoritative source of international law embodied in "judicial decisions" (Art. 38 (1) (d)) and will develop, with an even greater legally binding effect, into "international custom" (Art. 38 (1) (b)) […]

*International Thunderbird Gaming Corporation v. The United Mexican States*, UNCITRAL, Separate Opinion of Thomas Wälde, 01 December 2005 [16].

convincing answer is given in the investor-state case law to a particular question, I have tried to pinpoint the flaws of the practice or jurisprudence concerned and have sought to offer the solution that I see appropriate.

43. In addition to the jurisprudence of investment treaty tribunals, where appropriate, I have also drawn on the practice of other international courts and tribunals, particularly the jurisprudence of the ICJ and PCIJ. Furthermore, due to the close subject-matter-wise relationship between international investment law and international human rights law on the one hand, and international investment law and international trade law on the other, references have also been made to the practice of the European Court of Human Rights ("ECtHR") and WTO Dispute Settlement Body ("DSB"). In addition, mostly for the purpose of explaining issues of conflict of laws, frequent references have also been made to domestic case law in the relevant sections pertaining to choice of law matters.
44. Another significant source used in this Thesis is investment treaties, including both bilateral investment treaties and multilateral investment treaties. According to the latest statistics circulated by UNCTAD, by the end of 2017, 2,946 bilateral investment treaties have been concluded. In addition, by the end of that year, 376 treaties entailing investment provisions (like Free Trade Agreements and Economic Partnership Agreements) have been signed. These two types of treaties when added make a total of 3,322 international investment agreements.[66] This level of density in treaty rulemaking has assisted distilling state practice in some areas. Indeed, whereas each treaty is a prime source of law in its own right between the relevant contracting parties, it can in some areas evidence consistent state practice. To be sure, international investment agreements entail "a sweeping pattern of common features" and "a striking degree of commonality of languages" which create "a common lexicon of investment treaty law".[67] Of course, the growing preparation of national model BITs has helped the harmonisation and standardisation of the terms of bilateral investment treaties not only for the country which has formulated the draft but also, in certain cases, for other countries.[68] Another element that has fostered the

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[66] UNCTAD, 'IIA Issues Note: Recent Developments in the International Investment Regime' (United Nations 2018) 2.

[67] C McLachlan, L Shore & Matthew Weiniger (n 55) 5, 16. See also C McLachlan, 'The Principle of Systematic Integration and Article 31(3)(c) of the Vienna Convention' (2005) 54 ICLQ 279, 284 (describing this commonality as "akin to a continuous dialogue within an open-plan office.") In a different context, the *Mondev* tribunal referred to a concept of "a body of concordant practice" as a result of recurrence of certain terms in various investment treaties:

> the vast number of bilateral and regional investment treaties […] almost uniformly provide for fair and equitable treatment of foreign investments, and largely provide for full security and protection of investments. Investment treaties run between North and South, and East and West, and between States in these spheres *inter se*. On a remarkably widespread basis, States have repeatedly obliged themselves to accord foreign investment such treatment. In the Tribunal's view, such a body of concordant practice will necessarily have influenced the content of rules governing the treatment of foreign investment in current international law.

*Mondev International Ltd. v. United States of America*, ICSID Case No. ARB(AF)/99/2, Award, 11 October 2002 [117].

[68] Many countries in the world have drawn up draft bilateral investment treaties which, whenever possible, they use as a starting point in negotiating treaties with other countries, e.g., Austria Model BIT 2008, Brazil Model BIT 2015,

harmonisation of investment treaties is the existence of multilateral investment treaties.[69] This thriving conformity between the terms of investment treaties either in the form of recurrence of certain provisions, like repeated references to the legality requirement in various investment treaties, or the commonality in the language used for outlining certain requirements, like the language used to describe the temporal aspect of the legality requirement, has, in certain instances, been demonstrative of state practice, and, has, in any event, enlightened the path for finding generalised solutions to the topics under consideration. The Investment Policy Hub of UNCATD has been my first and foremost source for accessing investment treaties cited in this piece of work.[70]

45. Thirdly, doctrinal authorities, in particular, those from eminent practitioners and lecturers in the field, have also been a great source of inspiration in the formulation of my analyses in this Thesis.
46. Finally, I should mention that I have used Oxford University Standard for the Citation of Legal Authorities (OSCOLA) (2012) for the purpose of referring to the legal authorities and sources in the course of this Thesis.

Canada Model BIT 2004, France Model BIT 1999, Germany Model BIT 2008, India Model BIT 2015, Iran Model BIT 1994, Italy Model BIT 2003, Mexico Model BIT 2008, The Netherlands Model BIT 2018, Norway Model BIT 2015, Spain Model BIT 2008, Sweden Model BIT 2002, Switzerland Model BIT 1995, Thailand Model BIT 2002, Turkey Model BIT 2016, United Kingdom Model BIT 2008, and the United States Model BIT 2012.

[69] For instance, The Energy Charter Treaty ("ECT"), The North American Free Trade Agreement ("NAFTA") (Chapter 11), Agreement on Promotion, Protection and Guarantee of Investments among Member States of the Organization of the Islamic Conference, ASEAN Comprehensive Investment Agreement, Common Market for Eastern and Southern Africa ("COMESA") Treaty, etc.

[70] < https://investmentpolicyhub.unctad.org/> 'accessed 31 May 2019'.

## Part I: The Role of the Domestic Law of the Host State in Determining the *ratione materiae* Jurisdiction of An Investment Treaty Tribunal

## Chapter 1: The Role of Domestic Law in Investment Treaty Arbitrations in General

### Introduction

1. One of the nuances of understanding international law is discerning its relation and the modality of its co-existence with domestic law in seemingly overlapping and communal areas.[1] Such nicety is more outstanding in fields in which private entities and individuals, as well as private rights and interests, as creatures of domestic laws,[2] are at stake. One of such domains is the international law of investment.[3]
2. In international investment relations, states function, quite inevitably, in both public and private capacities. On the one hand, states offer international substantive standards of protection and procedural prerogatives to access international arbitration to investors under public international law treaties that they conclude with other sovereigns on the international plane. On the other hand, they enter into private law investment contracts with foreign private individuals or entities, or public entities acting in a private capacity.
3. The other side of the deal, i.e. the investors, as the direct beneficiaries of such treaties, are in most cases corporations that are the creations of municipal laws of their home state. Investors deal with recipient states mostly either based on a contract with a state entity or an investment authorisation issued by the host state,[4] both of which have their legal roots, principally, in the internal laws of the host state. Besides, the rights and interests arising from an investment contract or an investment authorisation are 'institutions' of domestic law. Thus, for an investment to be eligible for protection under international investment agreements, the investor needs to prove that the rights/interests in question are binding and enforceable under the domestic laws of the host state, and in some cases, are moreover vested in the investor. In addition, in order to be deemed lawful and deserve international protection under investment treaties, the investment of the investor should have been made in accordance with host state law.

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[1] M Dixon, *Textbook on International Law* (OUP 2013) 90; M Sasson, *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer Law International 2017) 102.

[2] See, for instance, *Barcelona Traction, Light and Power Company, Limited (New Application: 1962)* (*Belgium v. Spain*), Judgment, Merits, Second Phase, I.C.J. Rep. 1970 (05 February 1970) p 3, pp 33-34 [37]-[38] (stating that a 'corporate entity' is an 'institution of municipal law').

[3] In one of his earlier articles on investment treaty arbitration, Schreuer makes the point that it has proven very difficult to strike the right balance between the application of national law and international law in investment treaty arbitrations. See C Schreuer, 'Investment Arbitration - A Voyage of Discovery' (2005) 2(5) TDM 7 (stating that: "The applicable law in investment disputes has turned out to be a dangerous area. It takes great nautical skill to keep the proper balance between the Scylla and Charybdis of the two legal systems. A number of cases have actually foundered on the rocks of the proper or rather the improper law. Some awards have been annulled or set aside for failure to apply the proper law. Others were attacked but salvaged." See also *Antoine Goetz et consorts v. République du Burundi*, ICSID Case No. ARB/95/3, Award, 10 February 1999 [97] (explaining the unsettled issue of the relationship between national law and international law in the context of Article 42(1) of the ICSID Convention); VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (2006) 23(4) J Int'l Arb 285 (saying that: "foreign investment always implicates the national law of the host state, and the line between the private and public international law dimensions of [foreign investment treaty] arbitrations may be more difficult to draw in many instances.")

[4] For the various forms of foreign investors' legal engagements with host states, see *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Award, 16 August 2007 [343].

4. Accordingly, both bodies of law, i.e., international law and domestic law, have a role to play in the settlement of disputes arising out of or in connection with such 'hybrid' legal relationships.[5] Generally speaking, international law applies to the allegations of violation of the substantive standards of protection, international responsibility, and reparation,[6] whereas domestic law supplies the 'substantive aspects' of the rights underlying investments. The substantive aspects include the existence as well as the legality of a property right.[7]
5. To be sure, it is now increasingly being accepted that the proper question is how the two bodies of law should 'interact', rather than 'counteract'. From the viewpoint of public international law, as aptly noted by Fitzmaurice, when one makes a distinction between the international field and the domestic field, there will be no conflict between the two legal systems as each body of law will operate and will have supremacy within its own realm.[8] That is all the same in the field of international law of investment. As Monique Sasson puts it: "The key issue in

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[5] See Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (2003) 74 BYIL 151. In this respect, see also the ICSID tribunal's instructive statement in *El Paso v. Argentina*, which explains one facet of the interaction between the laws of the recipient state and international law in an investment treaty arbitration context:

> The fact that the BIT and international law govern the issue of Argentina's responsibility for violation of the treaty does not exclude that the domestic law of Argentina has a role to play too. The Tribunal agrees with the Claimant that this role is to inform the content of those commitments made by Argentina to Claimant that the latter alleges to have been violated. Thus, in order to establish which rights have been recognised by Argentina to the Claimant as a foreign investor, resort will have to be had to Argentina's law. However, whether a modification or cancellation of such rights, even if legally valid under Argentina's law, constitutes a violation of a protection guaranteed by the BIT is a matter to be decided solely on the basis of the BIT itself and the other applicable rules of international law.

*El Paso Energy International Company v. The Argentine Republic*, ICSID Case No ARB/03/15, Award, 31 October 2011 [135]. See also *Fedax N.V. v. The Republic of Venezuela*, ICSID Case No. ARB/96/3, Award, 09 March 1998 [30] (stating that "[i]t is of interest to note in this respect that the various sources of the applicable law [...] including the laws of the Contracting Party, the Agreement, other special agreements connected with the investment and the general principles of international law, have all had an important and supplementary role in the considerations of this case as well as in providing the basis for the decision on jurisdiction and the award on the merits [...]"); *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, 12 May 2005 [116]-[117] (observing that the "more pragmatic and less doctrinaire approach [is] allowing for the application of both domestic law and international law if the specific facts of the dispute so justifies." The tribunal further found that there is a "close interaction" between the laws of Argentina, the underlying contract, and international law "as embodied both in the Treaty and in customary international law." It said that "all these rules are inseparable and will, to the extent justified, be applied by the Tribunal."); E De Brabandere, *Investment Treaty Arbitration as Public International Law: Procedural Aspects and Implications* (CUP 2014) 122, 126-128; A Newcombe & L Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International 2009) 86.

[6] *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Decision on the Application for Annulment of the Argentine Republic, 01 September 2009 [146]; *El Paso Energy International Company v. The Argentine Republic* (n 5) [130] (stating that: "The Claimant relies on Argentina's responsibility for the violation of various provisions of the BIT [...] the primary governing law in this case is the BIT, supplemented by international law to which the BIT itself makes reference in various provisions.")

[7] M Sasson (n 1) 147.

[8] G Fitzmaurice, 'The General Principles of International Law Considered from the Standpoint of the Rule of Law' (1957) 92 Collected Courses of the Hague Academy of International Law 68. See also J Crawford (ed), *Brownlie's Principles of Public International Law* (8th Edition, OUP 2012) 110 (observing that each system of national and international law "is supreme *in its own field*; neither has hegemony over the other").

this context is not which law – municipal law or international – prevails, since there is normally no direct conflict. Rather, the issue is how these rules of law should interact."[9]

6. However, one should note that unlike disputes arising out of alleged breaches of international investment contracts which are principally governed by the municipal laws,[10] investment treaty arbitrations, which deal with alleged violations of international treaties, are, from a substantive point of view, governed by such investment treaties themselves in the first place, supplemented by applicable rules and principles of international law.[11] Nevertheless, as will be demonstrated in this Chapter and the ensuing Chapters, application of domestic law in investment treaty arbitrations is by no means negligible or incidental. If one runs through all the investment treaties concluded so far, one hardly comes across a treaty with no reference to domestic law. Similarly, if one considers the whole body of investment treaty arbitration practice, one is rarely faced with an award or decision in which no reference is made to domestic laws. It is

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[9] M Sasson (n 1) 9. See also in this respect, O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 108 (stating that in investment treaty cases, "international and national law gain their own and exclusive fields of application"); *CMS Gas Transmission Company v. Argentine Republic* (n 5) [115]-[122]; *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Award, 14 July 2006 [66] (holding that "Article 42(1) has been the subject of controversy on the respective roles of municipal law and international law. It is clear from the second sentence of Article 42(1) that both legal orders have a role to play, which role will depend on the nature of the dispute and may vary depending on which element of the dispute is considered.")

[10] See *Payment of Various Serbian Loans Issued in France* (*France v. Yugoslavia*), Judgment, P.C.I.J. Rep. Series A, No. 20, 1929 (12 July 1929) p 41 (stating: "Any contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of some country"); *Wintershall AG v. The Government of Qatar* (Ad hoc tribunal), Partial Award, 05 February 1988 (1989) 28(4) ILM 800, 802, 821-823; *Van Zyl and Others v. Government of Republic of South Africa and Others* (170/06), 20 September 2007, [2007] ZASCA 109 [64], available on the SAFLII website: <www.saflii.org/za/cases/ZASCA/2007/109.html.> 'accessed 31 December 2018'. (stating that: "Contracts concluded between states and aliens, are also governed by municipal law."); SKB Asante, 'The Stability of Contractual Relations in the Transnational Investment Process' (1979) 28(3) ICLQ 406 (opining that "an agreement between a host State and a private corporation … does not enjoy the status of an international agreement and on well settled principles of private international law, such an agreement should be governed by the law of the host state and not public international law.")

[11] *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic*, ICSID Case No. ARB/97/3 (formerly *Compañía de Aguas del Aconquija, S.A. and Compagnie Générale des Eaux v. Argentine Republic*), Decision on Annulment, 03 July 2002 [102] (expressing that: "[…] the inquiry which the ICSID tribunal is required to undertake is one governed by the ICSID Convention, by the BIT and by applicable international law. Such an inquiry is neither in principle determined, nor precluded, by any issue of municipal law, including any municipal law agreement of the parties."); *Técnicas Medioambientales Tecmed, S.A. v. The United Mexican States*, ICSID Case No. ARB (AF)/00/2, Award, 29 May 2003 [116] (observing that: "In addition to the provisions of the Agreement, the Arbitral Tribunal has to resolve any dispute submitted to it by applying international law provisions […] for which purpose the Arbitral Tribunal understands that disputes are to be resolved by resorting to the sources described in Article 38 of the Statute of the International Court of Justice […]"); *ADC Affiliate Limited and ADC & ADMC Management Limited v. The Republic of Hungary*, ICSID Case No. ARB/03/16, Award of the Tribunal, 02 October 2006 [290]-[292] (stating that: "In the Tribunal's view, by consenting to arbitration under Article 7 of the BIT […] the Parties also consented to the applicability of the provisions of the Treaty […] Those provisions are Treaty provisions pertaining to international law. […] The consent must also be deemed to comprise a choice for general international law, including customary international law, if and to the extent that it comes into play for interpreting and applying the provisions of the Treaty […] The sole exception to the foregoing is Article 4(3) of the BIT which provides: "The amount of this compensation may be estimated according to the laws and regulations of the country where the expropriation is made." In the present case, that law is Hungarian law. As the reference to domestic law is used for one isolated subject matter only, it must be presumed that all other matters are governed by the provisions of the Treaty itself which in turn is governed by international law."); *Siemens A.G. v. The Argentine Republic*, ICSID Case No. ARB/02/8, Award, 17 January 2007 [78].

submitted that with the passage of time, references to domestic law in investment treaties as well as in investment treaty decisions and awards have become much more frequent.

7. That being said, one needs to comprehend the nature of such reference to domestic law in each case. In fact, based on a proper characterisation of each single legal issue, it should be analysed whether internal laws are being referenced and/or applied as a source of governing 'law', or as 'facts' which need to be established prior to rendering an award on the basis of the governing international law. If applied as 'law', rather than as 'fact', another question which still hangs in the air is the legal ground pursuant to which domestic law applies: is it applied because the contracting state parties have expressly or impliedly referred to the application of domestic law in the relevant international investment agreement? or is it applied because the matter under consideration is in nature something related to the sovereignty of the host, or the home state for that matter, as to which international law has no legal rules to apply? Can one arrive at such a conclusion, i.e., application of domestic law as 'law', pursuant to a conflict of law analysis or, more generally, by virtue of general principles of law?
8. With this in mind, there are several legal matters in the distinct phases of jurisdiction, merits, and reparation in investment treaty arbitrations which behove the adjudicating forum to analyse the application of domestic law to related particular issues. Based on the questions dealt with in the previous paragraph, in so doing, an adjudicatory forum should necessarily examine: (i) the capacity and nature in which domestic laws apply in each jurisdictional and/or responsibility/remedy sphere (is it applied as 'law' or is it applied as 'fact'?). (ii) the reason or the legal ground for such an application.
9. On a related note, many international investment agreements do not contain specific provisions on applicable law.[12] Those investment agreements that do have governing law clauses often list both international law and domestic law as applicable laws, without determining which is pre-eminent or how they are to be combined.[13] It is submitted that such generic references to the application of domestic and international law in investment treaties do not help an arbitral tribunal in answering the above-mentioned questions. In addition, Article 42(1) of the ICSID Convention[14] in the context of investment treaty arbitrations under the aegis of ICISD is not also constructive for an investment treaty tribunal when trying to identify the law applicable to specific jurisdictional issues or matters concerning the merits of the case. As will be

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[12] See Y Banifatemi 'The Law Applicable in Investment Treaty Arbitration' in K Yannaca-Small (ed) *Arbitration under International Investment Agreements* (OUP 2010) 200, fn 27 (conducting research on bilateral investment treaties concluded by the United States, the United Kingdom, France, and Germany). See also C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (2014) 1(1) McGill Journal of Dispute Resolution 12 (saying that "the majority of BITs do not contain rules on applicable law"); A Parra, 'Applicable Law in Investor-State Arbitration' in M Rovine (ed), *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (Martinus Nijhoff Publishers 2007) 3, 7-8; UNCTAD, *Bilateral Investment Treaties 1995-2006: Trends in Investment Rulemaking* (United Nations 2007) 115-116.

[13] *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL, Final Award, 14 March 2003 [402]; *The Czech Republic v. CME Czech Republic B.V.*, Challenge of Arbitral Award, Judgement of Svea Court of Appeal, 15 May 2003 (2003) 42 ILM 919; JC Thomas & HK Dhillon, 'Applicable Law under International Investment Treaties' (2014) 26 SAcLJ, 975, 988; Z Douglas, *International Law of Investment Claims* (CUP 2009) 42, 44.

[14] Article 42(1) of the ICSID Convention provides:

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

illustrated later on in this Chapter, a typical provision on 'applicable law' in investment treaties and Article 42(1) of the ICSID Convention come close to 'redundancies' in investment treaty arbitrations when it comes to the actual application of these provisions by arbitrators. It is submitted that the answer to the above-referenced questions regarding the application of domestic law in investment treaty arbitrations is more appropriately found in other provisions of a given investment treaty – provisions other than the 'applicable law' provision – general principles of law (including general principles of conflict of laws), decisions of international judicial *fora* (particularly ICJ and PCIJ), and consistent and persuasive jurisprudence of investment treaty arbitrations. The idea is that proper cycling through these sources would lead one to robust answers regarding the application of domestic law in an investment treaty arbitration context.

10. In the following pages, I will embark upon offering proper responses to the foregoing questions. As a point of departure, in Section One, I will analyse the reasons for the significance of domestic laws in investment treaty arbitrations. Next, I will identify the guise under which such laws apply and will see whether they apply as 'laws' or as 'facts'. Thereafter, it will be demonstrated that when applied as law, domestic laws are applied on the basis of one of the following grounds: (i) the parties have expressly or impliedly chosen domestic law as applicable law to a particular issue; (ii) the issue concerns the sovereignty of the state and thus the nature of the issue necessitates the application of domestic law. As will be demonstrated, if the parties have not come to an agreement regarding these sovereignty-related issues in the pertinent investment treaty or through subsequent agreement or subsequent practice, customary international law does not usually fill the lacunae since it usually does not have a rule to solve such problems which fall within the province of domestic law.[15] In such circumstances, the application of general principles of law (including general principles of conflict of laws) usually leads to the application of domestic law to such sovereignty-related issues. Finally, in this context, I will also elucidate that the 'applicable law' clause of international investment agreements as well as Article 42(1) of the ICSID Convention offer no meaningful assistance to an arbitrator for the recognition of the role of domestic law in each specific and distinct domain of an investment treaty dispute.
11. In Section Two, the survey reviews specific areas in both jurisdictional and merits phases of an investment treaty arbitration where internal laws may be called upon to play a role. In analysing the jurisdictional stage, the inquiry will be made in both areas of personal and subject-matter jurisdiction. As to the merits, the main focus will be on discerning the 'nature' in which domestic law is applied in different substantive issues in general. As I will show, in principle, domestic law functions as 'fact' in the merits phase of an investment treaty arbitration. The discussion will be followed by identifying the limited and specific spheres in which domestic law is implemented as 'law' at the merits stage of an investment treaty case.
12. At the end of this Chapter, certain interim concluding remarks will be made, summarising the observations made herein.

## Section One: General Remarks with Regard to the Application of Domestic Law in Investment Treaty Arbitrations

13. As a point of departure, in this introductory Section, I will discuss the following general topics concerning the application of domestic law in investment treaty arbitrations in turn: (A) The Reason for Significance of Host State Law in Investment Treaty Arbitrations; (B) The Guise

[15] See subsection C.b *infra*.

in Which Domestic Law Applies in Investment Treaty Arbitrations; (C) The Legal Grounds for Application of Domestic Law as 'Law' in Investment Treaty Arbitrations; and (D) The Irrelevance of the Applicable Law Provision in Investment Treaties and the ICSID Convention.

### A. The Reason for the Importance of Host State Law in Investment Treaty Arbitrations

14. A proper consideration and analysis of the scheme, structure, and the content of international investment treaties and the legal relations arising therefrom makes clear that the idea that investment treaty arbitrations are solely governed by international law, with no role to be played by domestic law is too simplistic. There are three principal reasons for this proposition.

15. **Firstly**, in many parts of an investment treaty arbitration decision or award, there is a need to refer to the laws of the host or, less frequently, the home state. In most cases, such consideration is due to the citation of such laws in the underlying investment agreement. In order to demonstrate this, a proper case-study is warranted. As an example, I will recall certain provisions of the BIT between Germany and Philippines where reference to domestic law is explicit: Article 1(1) of the BIT defines the term 'investment' in the following way: "the term "investment" shall mean any kind of asset accepted in accordance with the respective laws and regulations of either Contracting State …". Article 1(2) of the same Agreement defines 'nationals' of Philippines as follows: "citizens of the Philippines within the meaning of its Constitution" and 'nationals' of Germany in this way: "Germans within the meaning of the Basic Law of the Federal Republic of Germany". Article 1 then determines the meaning of 'companies' in its paragraph 3, providing that: "with respect to the Republic of the Philippines: corporations, partnerships or other associations, incorporated or constituted and actually doing business under the laws in force in any part of the territory of that Contracting State wherein a place of effective management is situated …"[16] Article 1(4) then specifies the meaning of the term 'investor' by referral to paragraphs (2) and (3) of the same Article quoted above. Opening the substantive standards of protection of the BIT, Article 2(1) on 'Promotion and Acceptance' reads: "Each Contracting State shall promote as far as possible investments in its territory by investors of the other Contracting State and admit such investments in accordance with its Constitution, laws and regulations as referred to in Article 1 paragraph 1 …"[17] Article 9(4) of the BIT which deals with enforcement of awards of ICSID in case of an investor-state arbitration stipulates that: "… The award shall be enforced in accordance with domestic law." The Agreement also contains a Protocol in which at least 5 other references are made to domestic law. To give just one example, Article 2(a) of the Protocol provides: "As provided for in the Constitution of the Republic of the Philippines, foreign investors are not allowed to own land in the territory of the Republic of the Philippines…"[18] With this case-study in mind,

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[16] With respect to German "companies", the paragraph states: "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."

[17] Another substantive provision in the BIT which reemphasises the requirement for an investment to be made in accordance with host state law is Article 3(3) of the Agreement, which reads: "Each Contracting State shall apply in its territory to investments and to investors of the other Contracting State, with respect to their investments which are made in accordance with the legislation of that Contracting State and activities related to such investments, a treatment not less favorable than that granted to its own investments and investors, or the treatment granted to the investments and investors of the most favoured nation, if the latter is more favorable."

[18] See Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 18 April 1997, entered into force on 01 February 2000. This BIT was the basis for an eminent investment treaty case, namely, *Fraport AG Frankfurt Airport Services Worldwide v.*

it is fairly unsurprising to suggest that domestic law is an integral and indispensable element of governing law scheme of an investment treaty arbitration. Indeed, respecting the parties' choice of law in accordance with the principle of 'autonomy of the parties', an investment treaty arbitral tribunal has to apply domestic law as and when a legal question arises as to the matters regulated in the above-mentioned (or the like) provisions of the investment treaty.

16. **Secondly**, it is a widely accepted principle of international law that in an international investment relation, the investor has to take the host state law as he finds it, that it has a duty to diligently acquaint itself with the laws of the host state, that it has to respect the law of the recipient country, and that it has to comply with such laws when perfecting and operating its investment.[19]
17. **Thirdly**, as will be explained more fully below, rules and norms of international law are not capable of addressing all the legal questions that arise in the course of an investment treaty arbitration.[20] Indeed, the nature of the legal relations between the host state and the investor is such that, in many instances, the laws of the host state answer questions pertinent to the disputes arising out of such legal relationships. In this regard, McLachlan commendably depicts the modality of application, co-existence, and interaction of international law and domestic host state law in the context of international investment arbitration:

> International law does not purport to regulate numerous aspects of the ongoing relationship between the investor and the host state, which will probably be regulated by host state law. For ordinary working purposes, the investor's relationship with host state law will inevitably be primarily determined by host state law. The function of the international law standards enshrined in investment treaties is not to replace host state law. Rather it is to provide the fundamental protections of international law, in cases where the host state legal system has failed to secure such protection itself.[21]

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*The Republic of the Philippines*, ICSID Case No. ARB/03/25. The tribunal's award was later subject to an annulment proceeding. The Decision on the Application for Annulment was made on 23 December 2010.

[19] *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile*, ICSID Case No. ARB/01/7, Award, 25 May 2004 [197]-[206]; *Gami Investments, Inc. v. The Government of the United Mexican States*, UNCITRA, Final Award, 15 November 2004 [91]; *International Thunderbird Gaming Corporation v. The United Mexican States*, UNCITRAL, Arbitral Award, 26 January 2006 [164]; *Alasdair Ross Anderson et al v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010 [58] (observing that "prudent investment practice requires that any investor exercise due diligence before committing funds to any particular investment proposal. An important element of such due diligence is for investors to assure themselves that their investments comply with the law."); C McLachlan, L Shore & Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (OUP 2017) 309-310.

[20] *Barcelona Traction, Light and Power Company, Limited (New Application: 1962)* (*Belgium v. Spain*), Judgment, Merits, Second Phase, I.C.J. Rep. 1970 (05 February 1970) p 3, pp 33-34, 37 [38], [50]; *William Nagel v. The Czech Republic*, SCC Case No. 049/2002, Final Award, 09 September 2003 [316]; *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary*, ICSID Case No. ARB/12/2, Award, 16 April 2014 [162]; *Perenco Ecuador Ltd. v. The Republic of Ecuador and Empresa Estatal Petróleos del Ecuador* (*Petroecuador*), ICSID Case No. ARB/08/6, Decision on Remaining Issues of Jurisdiction and on Liability, 12 September 2014 [522] (stating that "[g]iven the absence of detailed general or conventional rules of international law governing the organisation, operation, management and control of an enterprise, a tribunal should in principle be guided by the more detailed prescriptions of the applicable municipal law…"); Z Douglas, *International Law of Investment Claims* (n 13) 52; M Sasson (n 1) 10.

[21] C McLachlan, 'Investment Treaty Arbitration: The Legal Framework' in AJ van den Berg (ed), *50 Years of the New York Convention, ICCA International Arbitration Conference* (Kluwer Law International 2009) 107.

18. Principally for these three cardinal reasons, domestic laws are of prime significance in investment treaty arbitrations. These three reasons will be further dissected in this present Chapter as well as in Chapters 2 and 3.

### B. The Guise in Which Domestic Law Applies in Investment Treaty Arbitrations: As 'Fact' or as 'Law'?

19. Domestic law appears in two distinct guises in investment treaty arbitrations: (i) as 'governing law'; and (ii) as 'facts' which should be established before responsibility is found on the part of the state. In fact, in the latter situation, domestic laws are referred to since they relate to 'factual' issues and pieces of evidence which should be decided upon by the adjudicating forum before ruling on state responsibility.[22]
20. It is argued by some jurists, commentators, and sometimes, prominent adjudicatory bodies, that in public international law disputes, tribunals usually apply domestic law merely as 'facts'. In *Certain German Interests in Polish Upper Silesia*, for instance, the PCIJ held that:

> [f]rom the standpoint of International Law and of the Court which is its organ, municipal laws are merely facts which express the will and constitute the activities of States, in the same manner as do legal decisions or administrative measures.[23]

21. Based on such a pronouncement, international tribunals take account of domestic laws only as 'facts'. Along the same lines, Judge Gros, in his Separate Opinion in *Barcelona Traction, Light and Power Company, Limited* (*Belgium v. Spain*) stated:

> In the present case, the rules of municipal law are nothing more than facts in evidence, and they deserve the same attention as the other facts, and the same rigour in their interpretation, but no more. The Court does not have to apply the rules of municipal law, as a municipal court of last instance would, to the relationships between the company and the shareholder; it takes account of them as being facts for the purpose of its appraisal of the legal situation laid before it by Parties and in order to see whether that situation as a whole is in conformity with the rules of international law or not. It is the latter rules which for an international tribunal go to constitute the reasons of its decision. It is therefore not enough to say that since a given municipal legal system creates a certain legal relationship, an international tribunal is obliged, on account of *renvoi* to municipal law, to accept that relationship as possessing the same legal cogency. The international tribunal takes this legal relationship as an established fact and tests it against the rules of international law…[24]

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[22] Dressed as 'facts', national laws can play multiple functions in international law such as evincing general or specific state practice in a particular subject, specifying the scope of a state's claim over maritime territory, and evidencing the compliance or non-compliance of the state with its international obligations. See M Dixon (n 1) 96. It is in this latter 'factual' guise that the municipal laws are being examined here.

[23] See *Certain German Interests in Polish Upper Silesia* (*Germany v. Poland*), Judgment, P.C.I.J. Rep. Series A, No. 7, 1926 (25 May 1926) p 19.

[24] *Barcelona Traction, Light and Power Company, Limited* (New Application: 1962) (*Belgium v. Spain*), Judgment, Merits, Second Phase, I.C.J. Rep. 1970 (05 February 1970) p 3, Separate Opinion of Judge Gros, pp 272-274. See also R Jennings & A Watts (eds), *Oppenheim's International Law* (Vol. 1, 9th edn, Longman 1992) 83 (stating that: "From

22. However, this opinion does not seem to withstand scrutiny even in a public international law context. In the *Serbians Loans Case*, the PCIJ considered itself as "having to decide as to the meaning and scope of a municipal law".[25] Furthermore, in the *Brazilian Loans Case*, the PCIJ considered itself as "bound to apply municipal law when circumstances so require."[26] To be sure, in certain situations, domestic laws have their own independent existence in public international law disputes as 'law' rather than as 'fact'.[27] As Judge Anzilotti opined in his Individual Opinion in *Consistency of Certain Danzig Legislative Decrees with the Constitution of the Free City*, domestic law can play two kinds of roles in international disputes: "[T]he Court, in performing its function as an organ of international law, may have to consider municipal laws from two entirely distinct standpoints. In the first place, it may have to examine municipal laws from the standpoint of their consistency with international law. (…) Secondly, the Court may find it necessary to interpret a municipal law, quite apart from any question of its consistency or inconsistency with international law, simply as a law which governs certain facts, the legal import of which the Court is called upon to appraise."[28]
23. Moreover, the fact that the PCIJ in *Certain German Interests in Polish Upper Silesia* seemingly confined the role of domestic law to establishing 'facts' needs more scrutiny. In his treatise on "The Prospects of International Adjudication", Wilfred Jenks made three observations regarding the PCIJ's statement in the *Certain German Interests in Polish Upper Silesia* case: (i) "There appears to be no later case in which the Court *per curiam* has reaffirmed this early view, which was expressed before the varied elements in the problem [i.e., the role of municipal laws in international adjudications] had been brought into proper focus." (ii) the PCIJ's statement is "not an exclusive indication of the manner in which the Court must regard municipal laws but merely an indication of the manner in which it should regard them in certain types of case which does not prejudice the possibility that it may be proper to regard them in a quite different manner in other types of case." (iii) "the use of the term 'facts' as a description of municipal laws [does not] necessarily affect materially the extent to which the Court may be called upon to interpret and apply such laws."[29]
24. In the context of investment treaty arbitrations, in principle, domestic law is applied as 'facts' "[w]hen the issue becomes the international validity of certain acts of the host state that have prejudiced the investor's legal entitlements under municipal law". In such circumstances, "international law is applied exclusively" as governing law.[30] To give one example, an investment treaty tribunal may consider, from a factual point of view, promises made to an investor in a domestic regulation at the time of undertaking his investment to find whether the

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the standpoint of international law, a national law is generally regarded as a fact with reference to which rules of international law have to be applied, rather than as a rule to be applied on the international plane as a rule of law; and insofar as the International Court of Justice is called upon to express an opinion as to the effect of a rule of national law it will do so by treating the matter as a question of fact to be established as such rather than as a question of law to be decided by the court").

[25] *Payment of Various Serbian Loans Issued in France* (n 10) p 46.

[26] *Payment in Gold of Brazilian Federal Loans Contracted in France* (*France v. Brazil*), Judgment, P.C.I.J. Rep. Series A, No. 21, 1929 (12 July 1929), p 124.

[27] See *Barcelona Traction, Light and Power Company, Limited* (n 2) p 3, pp 33-34, 37 [38], [50].

[28] *Consistency of Certain Danzig Legislative Decrees with Constitution of Free City*, Advisory Opinion, P.C.I.J. Rep. Series A/B, No. 65, 1935 (04 December 1935) p 63.

[29] CW Jenks, *The Prospects of International Adjudication* (Stevens & Sons 1964) 548-549.

[30] Z Douglas, *International Law of Investment Claims* (n 13) 70.

legitimate expectations of the investor in question have been frustrated by a subsequent change in the laws of the host state, and as such, whether the fair and equitable treatment standard of the investment treaty at issue has been violated.

25. That being said, there are, however, many occasions in investment treaty arbitrations in which investment treaty tribunals apply domestic law as 'law' rather than as 'fact'. In *National Grid v. Argentina*, it was held by the tribunal that both in its decision on jurisdiction and in its final award, which concerned the merits of the case, "the Tribunal dealt with the law of the host State as a matter of law, dispelling the notion that Argentine law may be considered a mere matter of fact."[31]
26. One prominent consequence of being applied as 'law' rather than as 'fact' in an investment treaty arbitration is that if the arbitral tribunal fails to apply the applicable domestic law, there could be a ground for the annulment of the award or decision, since the tribunal has failed to apply the proper law and as such exceeded its powers.[32]
27. It deserves mention that in investment treaty arbitrations, domestic laws are usually applied as 'law' when the issue in question concerns the 'legal entitlements' or the 'legal standing and status' of an investor.[33]

### C. The Legal Grounds for the Application of Domestic Law as 'Law' in Investment Treaty Arbitrations

28. In some cases, the application of domestic law in an investment treaty arbitration as 'law' is because such laws are applicable pursuant to the parties' express or implied agreement. In addition, in certain instances, the issue at stake concerns the sovereignty of a state and this issue, by nature, requires the application of the domestic – mostly mandatory – laws of the respective state. Usually, in such sovereignty-related areas, general international law has no rule to solve the legal problem when it arises.[34]
29. In the following pages, I will explain these two legal grounds for the application of domestic law in investment treaty arbitrations in turn.

#### a. The Parties Have Expressly or Impliedly Chosen Domestic Law to Govern a Particular Issue

30. There are usually specific provisions in international investment agreements, embodying the contracting parties' accord as to the application of municipal law of either of the contracting

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[31] *National Grid plc v. The Argentine Republic*, UNCITRAL, Award, 03 November 2008 [84]. See also *Total S.A. v. The Argentine Republic*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010 [39]; Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (n 5) 273. Cf. *Vladimir Berschader and Moïse Berschader v. The Russian Federation*, SCC Case No. 080/2004, Award, 21 April 2006 [96]: "The Vienna Convention provides no role for the domestic law of contracting states in the interpretation of international treaties. Therefore, in the instant case, it is clear that Russian national law is of no relevance in this regard. While Russian law may be relevant in establishing certain factual circumstances involved in the merits of the case, it has no role to play in determining the jurisdiction of the Tribunal."

[32] See Introduction *supra* [27].

[33] Z Douglas, *International Law of Investment Claims* (n 13) 70.

[34] It is needless to recall that there are situations in which the domestic law applies because of both legal grounds. In fact, there are certain issues in investment treaty arbitrations as to which a tribunal needs to apply domestic law both because the state contracting parties to an investment treaty have agreed as to the application of that body of law and also because the issue is something that is related to the sovereignty of the host or the home state to which general international law has no proper response.

parties to certain legal issues. As a result of such an agreement between the contracting parties in the investment treaty (which grants jurisdiction to the tribunal),[35] such matters are exclusively dealt with by domestic law.[36] For instance, Article I(g) of the BIT between Canada and Costa Rica defines 'investment' as "any kind of asset owned or controlled either directly, or indirectly through an enterprise or natural person of a third State, by an investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's laws . . . ."[37] Subsequently, in order to ascertain subject-matter jurisdiction, a tribunal deciding a case based on this BIT should in the first place verify that the alleged investment was made in accordance with the laws of the host state.[38]

31. Respecting the contracting parties' will is consistent with the principle of 'party autonomy' which is, almost always, recognised by rules of arbitration,[39] as well as national arbitration laws of the arbitration seat, where the seat of the arbitration matters, like in 'territorialised' non-ICSID arbitrations.[40]

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[35] It deserves mention here that the agreement between the contracting parties to an investment treaty is actually deemed as the agreement of the state party to the dispute with the investor who avails itself of the relevant treaty and files a claim against the state. In this regard, in *Antoine Goetz v. Burundi* , the arbitral tribunal held that:

> Undoubtedly, the applicable law has not been determined here, strictly speaking, by the parties to this arbitration (Burundi and the investors), but rather by the parties to the Bilateral Treaty (Burundi and Belgium). As was the case with the consent of the parties [to the arbitration], the Tribunal deems nevertheless that Burundi accepted the applicable law as determined in the above provision of the Bilateral Treaty by becoming a party to this Treaty, and that claimants did the same by filing their request for arbitration based on the Treaty.

*Antoine Goetz et consorts v. République du Burundi*, ICSID Case No. ARB/95/3, Award, 10 February 1999 [39]. The English translation of the Award can be found in (2001) XXVI Yearbook Commercial Arbitration 24, 36.

[36] See C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 4.

[37] See Article I(g) of the Agreement between the Government of Canada and the Government of the Republic of Costa Rica for the Promotion and Protection of Investments, signed on 18 March 1998, entered into force on 29 September 1999. This BIT was the basis for the dispute and the consequent arbitral award in *Alasdair Ross Anderson et al. v. Republic of Costa Rica* (n 19).

[38] This is what the tribunal in *Alasdair Ross Anderson et al. v. Republic of Costa Rica* actually did. See *Alasdair Ross Anderson et al. v. Republic of Costa Rica* (n 19) [53]-[59]. For a full discussion of this Award, see Chapter 2.

[39] According to recent research by UNCTAD, 55% of all known investment treaty cases have been filed under the ICSID Convention, 31% under UNCITRAL Arbitration Rules, 6% under ICSID Additional Facility Rules, and 5% under Stockholm Chamber of Commerce ("SCC") Rules. See UNCTAD, *Special Update on Investor-State Dispute Settlement: Facts and Figures* (United Nations 2017) 5. Since these are the arbitration rules that are mostly referred to in practice, throughout this whole Thesis, when analytical references need to be given to arbitral rules, I will mostly query the above-mentioned arbitration rules.

Article 42(1) of the ICSID Convention provides that "[t]he Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties." Article 35(1) of the UNCITRAL Arbitration Rules reads: "The arbitral tribunal shall apply the rules of law designated by the parties as applicable to the substance of the dispute." Article 54(1) of the ICSID Additional Facility Rules provides that: "The Tribunal shall apply the rules of law designated by the parties as applicable to the substance of the dispute." Finally, Article 22(1) of the Arbitration Rules of the SCC provides that: "The Arbitral Tribunal shall decide the merits of the dispute on the basis of the law(s) or rules of law agreed upon by the parties."

[40] See Y Banifatemi (n 12) 192 (saying that "[b]eing an arbitral process, investment treaty arbitration in no way differs from international commercial arbitration in that the principle of party autonomy is the primary rule governing the arbitration, including as regards the law applicable to the substance of the dispute. When the applicable law has been chosen by the parties, the arbitrators have a duty to apply such law and nothing but such law.")

32. Furthermore, when a treaty plainly refers to the application of the laws of the host state to a given question, an investment treaty tribunal should, as instructed by Article 31 of the VCLT, interpret the treaty in accordance with the 'ordinary meaning' of the terms of the treaty, thereby, giving effect to the *renvoi* contained therein. To be sure, in situations in which the parties refer to the domestic laws of either state, there is, in effect, a *renvoi* to the laws of the state parties. Referring to certain references to the laws of the host state in the underlying investment treaty, the tribunal in *Fraport v. Philippines* explained that:

> 335. Article 1(1) of the BIT provides that for the purpose of this Agreement "[t]he term 'investment' shall mean any kind of asset accepted in accordance with the respective laws and regulations of either Contracting State [...]". The qualification "accepted in accordance with the respective laws and regulations of either Contracting State" applies to every form of investment covered by the BIT. Article 2(1) provides: "Each Contracting State shall promote as far as possible investments in its territory by investors of the other Contracting State and admit such investments in accordance with its Constitution, laws and regulations as referred to Article 1, paragraph 1. [...]"
> [...]
> 394. The Tribunal cannot agree, as a matter of law, with the Claimant's contention that "[e]ven if there could be said to be an issue as to whether the Philippine laws were complied with [...], it could be of only municipal, not international legal significance". This interpretation, if accepted, would deprive a significant part of the ordinary words of a treaty of any meaning and effect. The BIT is, to be sure, an international instrument, but its Articles 1 and 2 and ad Article 2 of the Protocol effect a *renvoi* to national law, a mechanism which is hardly unusual in treaties and, indeed, occurs in the Washington Convention. A failure to comply with the national law to which a treaty refers will have an international legal effect.[41]

33. Therefore, when there is a *renvoi* to domestic law in an investment treaty, it is this body of law which conclusively determines the fate of the legal issue under consideration as a matter of law.[42]

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[41] *Fraport v. Republic of Philippines* (n 4) [335], [394].

[42] In this regard, see *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia*, ICSID Case No. ARB/06/2, Decision on Jurisdiction, 27 September 2012 [47]-[52] (where the tribunal states that "[b]oth Parties agree, and rightly so, that the Tribunal's jurisdiction is governed by the ICSID Convention, by the Bolivia-Chile BIT […] and, to the extent the latter refers to it, by Bolivian law." Having noted that as per Article I(2) of the Bolivia-Chile BIT, 'investment' is defined as any kind of assets or rights related to an investment made in accordance with the laws and regulations of the host state, the tribunal concluded that: "… Bolivian law applies to determine (i) whether Quiborax and Allan Fosk were shareholders of NMM at the time the dispute arose in June 2004, and (ii) whether the Claimants' purported investment was made "in accordance with the laws and regulations" and the "legal provisions" of Bolivia […] Both Parties agree that these issues are governed by Bolivian law"); *Metal-Tech Ltd. v. Republic of Uzbekistan*, ICSID Case No. ARB/10/3, Award, 04 October 2013 [121]; *Churchill Mining PLC v. Republic of Indonesia*, ICSID Case No. ARB/12/14 & *Planet Mining Pty Ltd v. Republic of Indonesia*, ICSID Case No. ARB12/40, Decisions on Jurisdiction for both Cases, 24 February 2014, both at [86] (stating that: "The Tribunal's jurisdiction is contingent upon the provisions of the ICSID Convention on the one hand, and of the […] BIT, […] on

### b. The Nature of the Legal Issue

34. In certain situations in investment treaty arbitrations, the application of domestic law is necessitated by considerations of sovereignty. Sovereignty means "the supreme and independent authority of the nation state within its own territory."[43] It follows from such authority that the state has exclusive jurisdiction to enact and enforce laws for its territory and the population living there.[44] For instance, in relation to international investment arrangements, it is well-settled in international law that the state has an exclusive right to control the movement of capital into its territory. Therefore, unless there is a specific treaty commitment to the contrary, the state may prohibit or set conditions on the movement of capital into its territory.[45]
35. This 'sovereignty' factor has found its way in the universally-applied choice of law rules. For instance, unless otherwise agreed by the state contracting parties, it is the law of the *situs* of a given tangible property comprising an investment that determines whether a property right has been created. The same law also specifies the nature and scope of such right and also identifies the person to whom the right in question vests.[46] It is usually the law of the host state, as the place of making and operating an investment, which determines the creation and existence of

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the other hand. In addition, where an international law instrument refers to jurisdictional requirements governed by the municipal law of a Contracting State, that municipal law shall also govern the jurisdiction of the Tribunal to the extent provided by the BIT."); M Sasson (n 1) 1-3; C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 2-3. Cf *Camuzzi International S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/2, Decision on Objection to Jurisdiction, 11 May 2005 [57] (stating that: "Even though particular aspects relating to the meaning and scope of the rights relating to the assets are governed by the law and regulations of the Argentine Republic, it must be borne in mind … that as regards jurisdiction the applicable law is that of the Convention and the Treaty …"); *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. The Argentine Republic*, ICSID Case No. ARB/09/1, Decision on Jurisdiction, 21 December 2012 [217]-[218] (where the tribunal holds that reference to domestic law in certain jurisdictional areas is for the purpose of determining 'a question of fact'.)

[43] TR van Dervort, *International Law and Organization* (Sage Publications 1998) 12. Brierly also explains the principle of 'sovereignty' in the following terms: "At the basis of international law lies the notion that a state occupies a definite part of this surface of the earth, within which it normally exercises, subject to the limitations imposed by international law, jurisdiction over persons and things to the exclusion of the jurisdiction of other states. When a state exercises an authority of this kind over a certain territory it is popularly said to have 'sovereignty' over the territory." JL Brierly, *The Law of Nations: An Introduction to the International Law of Peace* (Clarendon Press 1963) 162.

[44] JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Frameworks for Foreign Capital* (OUP 2013) 76.

[45] See ibid. Salacuse believes that a 'true open-door policy', which is a self-proclaimed label used by some countries, probably does not exist in reality. See ibid 87. In the same vein, in the context of international monetary regulations, by virtue of Article 6 of the IMF Articles of Agreement, IMF member states have the sovereign right to limit the inflow of capital. Article VI, Section 3 of IMF Articles of Agreement reads: "Members may exercise such controls as are necessary to regulate international capital movements, but no member may exercise these controls in a manner which will restrict payments for current transactions or which will unduly delay transfers of funds in settlement of commitments, except as provided in Article VII, Section 3(b) and in Article XIV, Section 2."

[46] Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (n 5) 282, 284; C Staker, 'Public International Law and the Lex Situs Rule in Property Conflicts and Foreign Expropriations' (1987) 58 BYBIL 151, 163-169; E Rabel, *The Conflict of Laws: A Comparative Study* (Vol. IV, University of Michigan Law School 1958) 30 (opining that: "It is at present the universal principle, manifested in abundant decisions and recognised by all writers, that the creation, modification, and termination of rights in individual tangible physical things are determined by the law of the place where the thing is physically situated").

property rights underlying investment, thereby giving the host state the 'sovereignty' privilege to regulate this crucial matter within its territory.[47]

36. That being said, if an issue concerns the 'sovereignty' of the host state, it does not matter whether the investment treaty expressly requires the application of domestic law or not. The ruling in *Encana v. Ecuador* with respect to the law applicable to the creation and existence of property rights underlying investment is worthwhile in this connection:

> 184. The second preliminary question concerns the applicable law. The relevant clause, Article XIII(7) of the BIT, provides only a tribunal exercising jurisdiction under the BIT "shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law". Unlike many BITs there is no express reference to the law of the host State. However for there to have been an expropriation of an investment or return (in a situation involving legal rights or claims as distinct from the seizure of physical assets) the rights affected must exist under the law which creates them, in this case, the law of Ecuador.[48]

37. With that in mind, it deserves mention that in matters related to the domestic jurisdiction of states general international law does not usually have rules to apply.[49] For instance, as alluded to above, customary international law does not have any rule regarding property law and

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[47] As alluded to above, this privilege emanates from the principle of 'territorial sovereignty' allowing each state to regulate property in its territory and under its effective control. See BA Wortley, 'Observations on the Public and Private International Law Relating to Expropriation' (1956) 5(4) The American Journal of Comparative Law 589 (quoting translations from Pufendorff's observations with respect to the rights of the sovereign: "The first right consists in this, that the rulers can prescribe laws for the citizens, with regard to the use of their property, in conformity with the interest of the state, or concerning the amount and quality of their possessions, as also the method of transfer to others, and other matters of the kind ...")

[48] *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL (formerly *EnCana Corporation v. Government of the Republic of Ecuador*), Award, 03 February 2006 [184].

[49] The most classic authority for this proposition is the ICJ Decision in the *Barcelona Traction Case*. The threshold question in *Barcelona Traction Case* concerned the right of Belgium to exercise diplomatic protection of Belgian shareholders in a company which was a juristic entity incorporated in Canada, the measures complained of having been taken in relation not to any Belgian nationals but to the company itself. See *Barcelona Traction, Light and Power Company, Limited* (n 2) [32]. Referring to the PCIJ Judgment in *Panevezys-Saldutiskis Railway*, the Court held that in the absence of a special agreement, this right is necessarily limited to intervention by a state on behalf of its own nationals. See *Barcelona Traction, Light and Power Company, Limited* (n 2) [36]. The Court then concluded that: "In this field international law is called upon to recognize institutions of municipal law that have an important and extensive role in the international field. This does not necessarily imply drawing any analogy between its own institutions and those of municipal law, nor does it amount to making rules of international law dependent upon categories of municipal law. All it means is that international law has had to recognize the corporate entity as an institution created by States in a domain essentially within their domestic jurisdiction. This in turn requires that, whenever legal issues arise concerning the rights of States with regard to the treatment of companies and shareholders, as to which rights international law has not established its own rules, it has to refer to the relevant rules of municipal law… " ibid [38]. With respect to the latter point, the Court explained that: "If the Court were to decide the case in disregard of the relevant institutions of municipal law it would, without justification, invite serious legal difficulties. It would lose touch with reality, for there are no corresponding institutions of international law to which the Court could resort. Thus the Court has, as indicated, not only to take cognizance of municipal law but also to refer to it…" ibid [50]. See also *Perenco Ecuador Ltd. v. The Republic of Ecuador and Empresa Estatal Petróleos del Ecuador* (n 20) [522] (stating that "[g]iven the absence of detailed general or conventional rules of international law governing the organisation, operation, management and control of an enterprise, a tribunal should in principle be guided by the more detailed prescriptions of the applicable municipal law…").

property rights.[50] Criticising the failure of the tribunal in *CME v. Czech Republic* to apply domestic Czech law to the question of property rights, Douglas provided the following interesting analogy:

> [t]o answer this question by reference to international law is tantamount to deciding *ex aequo et bono* for there are no principles or rules in the corpus of international law that could be of assistance. And just as the International Court of Justice might attract the opprobrium of international lawyers should it decide an international maritime boundary dispute by reference to Czech law, the failure of investment treaty tribunals to take notice of applicable municipal laws cannot escape criticism either.[51]

38. In fact, since customary international law contains no rules defining certain 'rights' and 'statuses', an adjudicating forum has no leeway to invent or devise definitions for certain concepts, which are exclusively defined and specified in national law. Unless the contracting parties to an international treaty have agreed to a definition, *inter alia*, by virtue of agreeing to a 'special meaning' in the sense of Article 31(4) of the VCLT or through subsequent agreement or subsequent practice, referring to international law to determine certain sovereignty-related matters would be unfounded under international law.[52]
39. In conclusion, in an investment treaty context, when an issue concerns the sovereignty of a state, it is usually the law of that state which applies to the issue.[53] This is because general international law does not have a corresponding rule with respect to the matter at stake to regulate the issue. Therefore, the issue has to be resolved by reference to domestic law. In such a case, conflict of laws rules determine the applicable domestic law to the matter at stake.

### D. Irrelevance of the Applicable Law Provision in Investment Treaties and the ICSID Convention

40. As was discussed above, in investment treaty arbitrations, courts and tribunals apply domestic law in companion with international law. The question that arises here is to what extent does an applicable law provision in an investment treaty or Article 42(1) of the ICSID Convention in ICSID arbitrations guide an arbitral tribunal in the actual application of these two bodies of law in different jurisdiction and merits phases of an investment treaty case.
41. To begin with, many investment treaties do not contain provisions on applicable law.[54] However, a good deal of such treaties includes 'applicable law' or 'governing law'

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[50] *William Nagel v. The Czech Republic* (n 20) [316]; *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 20) [162]; Z Douglas, *International Law of Investment Claims* (n 13) 52; M Sasson (n 1) 10.

[51] Z Douglas, *International Law of Investment Claims* (n 13) 67.

[52] M Sasson (n 1) 8.

[53] This is always subject to the caveat that the parties to the treaty have not already defined or determined the matter in the treaty itself or through subsequent agreement or subsequent practice.

[54] See Y Banifatemi (n 12) 200, fn 27 (conducting a research on bilateral investment treaties concluded by the United States, the United Kingdom, France, and Germany); C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 12 (saying that "the majority of BITs do not contain rules on applicable law"); A Parra (n 12) 3, 7-8; UNCTAD, *Bilateral Investment Treaties 1995-2006: Trends in Investment Rulemaking* (n 12) 115-116; O Spiermann, (n 9) 107; MN Kinnear, 'Treaties as Agreements to Arbitrate: International Law as the Governing Law' in AJ van den Berg (ed) *International Arbitration 2006: Back to Basics?* (Kluwer Law International 2007) 407

provisions.[55] Such provisions often direct the competent court or tribunal to apply the terms of the investment treaty at hand, international law, and domestic law of the host state to an investment treaty dispute.[56] For example, Article 30(1) of the BIT between China and Canada provides: "A Tribunal established under this Part shall decide the issues in dispute in accordance with this Agreement, and applicable rules of international law, and where relevant and as appropriate, take into consideration the law of the host Contracting Party."[57] Similarly, Article 9(7) of the BIT between Costa Rica and Switzerland provides: "The arbitral tribunal shall decide on the basis of the present Agreement and other relevant agreements between the Contracting Parties; the terms of any particular agreement that has been concluded with respect to the investment; the law of the Contracting Party which is a party to the dispute; including its rules on the conflict of laws; such principles and rules of international law as may be applicable."[58]

42. It is submitted that, in practice, such investment treaties which do have applicable law clauses do not differ from the former array of treaties which lack any governing law provisions in terms of giving proper guidance to an investment treaty tribunal regarding the choice of the applicable law to a given question. In fact, such 'applicable law' provisions do not necessarily

(indicating that: "Numerous treaties fail to state a governing law. Treaties in this category are often older treaties; those concluded more recently tend to state the governing law expressly." [references omitted])

[55] See A Newcombe & L Paradell (n 5) 79-83 (enumerating six (6) different approaches regarding items listed in an applicable law provision in investment treaties that do contain applicable law clauses).

[56] ibid 79. VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (n 3) 269 (characterising such applicable law clauses as ""multipolar" choice of law provisions", i.e., three or more sources of applicable law).

[57] See Article 30(1) of the Agreement between the Government of Canada and the Government of the People's Republic of China for the Promotion and Reciprocal Protection of Investments, signed on 09 September 2012, entered into force on 01 October 2014.

[58] See Article 9(7) of the Agreement between the Swiss Confederation and the Republic of Costa Rica on the Promotion and the Reciprocal Protection of Investments, signed on 01 August 2000, entered into force on 19 November 2002. See also Article 8(6) of the Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 1991, entered into force on 01 October 1992. This Agreement was the basis in the famous case of *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL.

offer any guidance as to the priority of one body of law over another.[59] In other words, they just "state the problem without resolving it."[60]

43. Additionally, Article 42(1) of the ICSID Convention,[61] which has similar prescriptions regarding the applicable bodies of law in an investment dispute, is more meaningful in investment contract disputes rather than investment treaty disputes. As McLachlan explains: "... when the Convention was prepared, the dominant paradigm for investment arbitration was the concession contract claim."[62] Similarly, the Annulment Committee in *Duke Energy v. Peru* stated that: "… [W]hen the ICSID Convention was formulated, the Convention's framers envisaged that the first basis for consent to the jurisdiction of the Centre would be by contract between the host state and the investor…"[63] In addition, Article 42(1) of the ICSID Convention suffers from the same undesired generality that do applicable law provisions in investment treaties. Douglas makes a plausible observation regarding the usefulness of applicable law provisions in investment treaties and Article 42 of the ICSID Convention:

> These provisions are open-textured and serve only to confirm that the tribunal is competent to apply the stipulated sources of law, rather than prescribe the connecting factors necessary to determine the applicable laws in any given case.[64]

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[59] Commenting on Article 8(6) of the Netherlands-Czech Republic BIT mentioned above, the tribunal in *CME v. Czech Republic* remarked that: "[T]he choice-of-law clause in the (Dutch) Treaty is broad and grants to the Tribunal a discretion, without giving precedence to the systems of law referred to. […] There is no ranking in the application of the national law of the host state, the Treaty provisions or the general principles of international law …" *CME Czech Republic B.V. v. The Czech Republic* (n 13) [402]. Expressing an opinion on the same provision pursuant to the Czech Republic's application for annulment, the Svea Court of Appeal opined that: "The four sources of law are not numbered, nor are they otherwise marked in such a manner that governing law in the relevant contracting state should primarily be applied and general principles of international law applied thereafter." See *The Czech Republic v. CME Czech Republic B.V.*, Challenge of Arbitral Award, Judgement of Svea Court of Appeal (n 13) 919. See also *National Grid plc v. The Argentine Republic* (n 31) 2008 [82] (stating that: "This provision points to the application of the Treaty itself, Argentine law (including its rules on conflict of laws), and "the applicable principles of international law." Although the Parties do not disagree that these are the relevant sources of law applicable to this dispute, they note the absence of specific guidelines under the Treaty as to which aspect of the dispute is governed by one source or the other and how those sources interact in case of conflict *inter se*"; JC Thomas & HK Dhillon (n 13) 988; VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (n 3) 287, 289.

[60] M Sasson (n 1) 10.

[61] Article 42(1) of the ICSID Convention reads: "The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable."

[62] C McLachlan, 'Investment Treaty Arbitration: The Legal Framework' (n 21) 109.

[63] *Duke Energy International Peru Investments No. 1 Ltd. v. Republic of Peru*, ICSID Case No. ARB/03/28, Decision on Annulment, 01 March 2011 [129]. See also N Blackaby & C Partasides (eds), *Redfern and Hunter on International Arbitration* (OUP 2015) 466-467; JC Thomas & HK Dhillon, (n 13) 985; O Spiermann (n 9) 107.

[64] Z Douglas (n 13) 42, 44. See also Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (n 5) 195. Moreover, one should bear in mind that, in the context of ICSID arbitrations, Article 42 of the ICSID Convention is not helpful in determining the applicable law to questions of jurisdiction. In *CMS v. Argentina*, the tribunal correctly said: "Article 42 is mainly designed for the resolution of disputes on the merits and, as such, it is in principle independent from the decisions on jurisdiction, governed solely by Article 25 of the Convention and those other provisions of the consent instrument which might be applicable, in the instant case the Treaty provisions…" The 'consent instrument' under examination in that case was an international investment agreement, which contained

44. If one takes into account the sources of law enumerated in Article 42 of the ICSID Convention and the sample applicable law clauses mentioned above,[65] one sees that the listing of these sources does not help a tribunal in the correct application of each body of law in its right place. For instance, the inclusion of the BIT itself in the list of applicable laws is stating the obvious and is not helpful in understanding the applicable legal regime to each specific question before the tribunal. In *AAPL v. Sri Lanka*, in the very the first award rendered in a BIT case, the ICSID Tribunal stated:

> [T]he Bilateral Investment Treaty is not a self-contained closed legal system limited to provide for substantive material rules of direct applicability, but it has to be envisaged within a wider juridical context in which rules from other sources are integrated through implied incorporation methods, or by direct reference to certain supplementary rules, whether of international law character or of domestic law nature ….[66]

45. With that in mind, it is equally true that the failure of the provision on 'applicable law' to refer to international law, domestic law or the BIT, does not preclude a tribunal to apply such bodies of law when the circumstances so require. For example, Article 1131 of the North American Free Trade Agreement ("NAFTA") on 'Governing Law'[67] and Article 26(6) of the Energy

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express or implied *renvoi* to the national law of either of the contracting states with regard to certain jurisdictional matters. See *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Decision on Objections to Jurisdiction, 17 July 2003 [88]. By the same token, the tribunal in *Noble Energy v. Ecuador* noted: "The Tribunal is of the opinion that Article 42(1) is irrelevant for purposes of jurisdiction. Article 42 of the ICSID Convention is a conflict rule which deals with the law governing the merits of the dispute […] Jurisdiction is a different matter. It is not subject to this conflict rule but is governed by Article 25 of the ICSID Convention." See *Noble Energy, Inc. and Machalapower Cia. Ltda. v. The Republic of Ecuador and Consejo Nacional de Electricidad*, ICSID Case No. ARB/05/12, Decision on Jurisdiction, 05 March 2008 [57]; *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/1, Decision on Jurisdiction, 08 December 2003 [48] (stating that: "As pointed out by both parties, the relevant provision for determining the law applicable to this dispute is Article 42(1) of the Convention. However, the rules applying to the dispute under Article 42(1) address the resolution of disputes on the merits, and so will not necessarily be those which apply to the Tribunal's determination of its jurisdiction under Article 41 at this stage of the proceedings.") See also *Camuzzi International S.A. v. The Argentine Republic* (n 42) [15]-[17]; *Saipem S.p.A. v. The People's Republic of Bangladesh*, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007 [68]; *Inmaris Perestroika Sailing Maritime Services GmbH and Others v. Ukraine*, Decision on Jurisdiction, 08 March 2010 [54]; *Alpha Projektholding GmbH v. Ukraine*, ICSID Case No. ARB/07/16; Award, 08 November 2010 [225]-[227]; *Ambiente Ufficio S.p.A. and others v. Argentine Republic*, ICSID Case No. ARB/08/9 (formerly *Giordano Alpi and others v. Argentine Republic*), Decision on Jurisdiction and Admissibility, 08 February 2013 [233]-[246]; *KT Asia Investment Group B.V. v. Republic of Kazakhstan*, ICSID Case No. ARB/09/8, Award, 17 October 2013 [85]; C Schreuer *et al*, *The ICSID Convention: A Commentary* (CUP 2009) 550-552; E De Brabandere (n 5) 123.

[65] See footnotes 57-58 *supra* with the accompanying texts.

[66] *Asian Agricultural Products v. Democratic Republic of Sri Lanka*, ICSID Case No ARB/87/3, Final Award, 27 June 1990 [19]-[21]. See also *Wena Hotels Ltd. v. Arab Republic of Egypt*, ICSID Case No. ARB/98/4, Award, 08 December 2000 [79]: (saying that: "… the IPPA is a fairly terse agreement of only seven pages containing thirteen articles. The parties in their arguments have not treated it as containing all the rules of law applicable to their dispute, and this is also the view of the Tribunal…".

[67] Article 1131(1) of NAFTA reads: "A Tribunal established under this Section shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law."

Charter Treaty "ECT"[68] do not include domestic law in their inventory of applicable sources of law. In spite of this absence, tribunals acting under these treaties apply domestic law to issues like the existence of property rights, the legality of investment, and nationality of investors.[69]

46. As results from this analysis, irrespective of the content of the provision on 'applicable law', a tribunal needs to go through the whole text of the investment treaty and see whether there is an agreement with respect to applicable law to the matter under consideration, and if not, then properly characterise the issue and discern its applicable law, *inter alia*, by reference to proper conflict of laws rules. The result of such an enquiry would either be applying international or domestic law.[70] In *EnCana v. Ecuador*, the tribunal noted that the applicable law clause of the underlying BIT (the Canada-Ecuador BIT) provided that the dispute should be decided in accordance with the BIT itself and applicable rules of international law. It stated that "[u]nlike many BITs there is no express reference to the law of the host State." This, however, did not dissuade the tribunal from applying domestic law. It held that "for there to have been an expropriation of an investment or return (in a situation involving legal rights or claims as distinct from the seizure of physical assets) the rights affected must exist under the law which creates them, in this case, the law of Ecuador." To buttress its reasoning regarding the applicable law to the question of the existence of property rights, the tribunal went on to invoke another provision of the BIT on 'Taxation Measures'.[71]
47. On the whole, the provision on 'applicable law' in an investment treaty and Article 42(1) of the ICSID Convention do not assist a tribunal in detecting the proper applicable law to a particular issue, especially, when the issue in question is that of jurisdiction. An arbitral tribunal should look for the applicable law to a given question elsewhere in the treaty and should in certain cases query general principles of law by conducting a 'case-by-case' analysis.[72]

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[68] Article 26(6) of the ECT provides: "A tribunal established under paragraph (4) shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law."

[69] For instance, in *Libananco v. Turkey*, the claimant had alleged a violation of the ECT. Although Article 26(6) of the Treaty does not refer to domestic law in the index of applicable sources of law, the tribunal had no doubt that it had to apply the host state's domestic law to the issue of whether the disputed property rights existed: "[I]t is common ground between the Parties that Turkish law applies to the issue of whether (and when) Libananco acquired the shares in question and thus had an "Investment"." See *Libananco Holdings Co. Limited v. Republic of Turkey*, ICSID Case No. ARB/06/8, Award, 02 September 2011 [385 *et seq*]. See C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 20. On a related note, Schreuer points out that a provision like the applicable law clause of NAFTA, which excludes any reference to the domestic laws of the host state, 'is not advisable' and is 'impractical' since there exist numerous contacts between the investment activity and 'various technical provisions of the host State's law'. See C Schreuer *et al*, *The ICSID Convention: A Commentary* (n 64) 562.

[70] In this connection see R Dolzer & C Schreuer, *Principles of International Investment Law* (OUP 2012) 293; A Parra (n 12) 8, 11.

[71] *EnCana Corporation v. Republic of Ecuador* (n 48) [184] (deciding a case under the Agreement between the Government of Canada and the Government of the Republic of Ecuador for the Promotion and Reciprocal Protection of Investments, signed on 29 April 1996, entered into force on 06 June 1997 (subsequently terminated)).

[72] As the Svea Court of Appeal indicated in its Judgment on the Czech Republic's annulment application as to the arbitral award in *CME v. Czech Republic*: "The un-numbered list [in Article 8(6) of the Netherlands-Czech BIT] almost gives the impression that the contracting states have left to the arbitrators the determination, on a case by case basis, as to which source or sources of law shall be applied." *The Czech Republic v. CME Czech Republic B.V.*, Challenge of Arbitral Award, Judgement of Svea Court of Appeal (n 13) 919. See also HE Kjos, *Applicable Law in Investor-State Arbitration: The Interplay Between National and International Law* (OUP 2013) 235; VC Igbokwe,

## Section Two: The Situations in Which an Investment Treaty Adjudicating Forum Needs to Refer to Domestic Laws

48. Having discussed the general role of domestic law in investment treaty arbitrations, in this Section, I am going to identify the specific areas in which domestic law is applicable in an investment treaty arbitration proceeding. For the purposes of the present Thesis, the discussion will be pursued in two specific areas: (i) applicability of domestic law to jurisdictional issues; (ii) applicability of domestic law to issues concerning the merits.[73] It should also be noted that this survey is not intended to be exhaustive. The idea is that the ensuing discussions (whether concerning jurisdiction or merits) cover the most important subjects in investment treaty arbitrations which are affected by the laws of the home or the host state.

### A. The Role of Domestic Law in Jurisdictional Issues

49. In a great majority of investment treaty cases, there are jurisdictional objections raised by respondents, compelling the tribunal to address the issue of jurisdiction, and, in so doing, inevitably, expressly or impliedly, to decide the issue of the applicable law of jurisdiction.[74]
50. As was discussed above, in order to ascertain jurisdiction, an arbitral tribunal has to refer to the laws of either the home or the host state in various situations. This reference is mainly because of the express *renvoi* in the investment treaty in question. For example, a majority of

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'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (n 3) 284.

[73] Of course, there are other particular areas in investment treaty arbitrations that are not addressed here, like attribution, remedies, and dispute settlement. In each of these topics, domestic law has certain functions. However, as the role of domestic law is relatively less extensive in these areas, and since the character of these issues is such that they have much less trace in the ensuing Chapters, these topics are not dealt with in this Chapter. For the role of domestic law in 'attribution', see M Sasson (n 1) 15-44; R Dolzer & C Schreuer (n 70) 216-227. As to the issue of 'dispute settlement', certain observations will be made as to the role of domestic law and national courts of the host state in Chapter 7 of this Thesis. As to issue of remedies and determination of damages, the role of domestic law is usually limited to a handful of issues. As Newcombe and Paradell observe, "the legal consequences of the IIA breach, such as reparation and compensation, [are] governed by international law. This is because the breach of an IIA standard by the host state creates a new obligation (a so-called secondary obligation) upon that state (i.e., essentially the obligation to provide reparation). That obligation arises in the international plane; it stems from the principle that a state's breach of an international obligation engages its international responsibility. Domestic law plays no part in any of these respects." See A Newcombe & L Paradell (n 5) 99. However, domestic law is relevant in a few issues regarding compensation, in particular, when the contracting parties have so provided in the relevant investment treaty. For instance, Article 4(3) of the BIT between Cyprus and Hungary, which by the way was the basis of the dispute in *ADC Affiliate Limited and ADC & ADMC Management Limited v. The Republic of Hungary* (n 10), provides that: "The amount of […] compensation may be estimated according to the laws and regulations of the country where the expropriation is made." See Agreement between the Government of the Republic of Cyprus and the Government of the Hungarian People's Republic on Mutual Promotion and Protection of Investments, signed on 25 May 1989, entered into force on 25 May 1990. Furthermore, there are certain BITs which determine the rate of interest by reference to the laws of the host state. For instance, Article 4(2) of the BIT between Thailand and Russia reads: "In case of delay the interest shall be paid from the date the payment was due until the date of actual payment at the following rate: a) in Thailand … (ii) in the case of movable property, as determined by the Civil and Commercial Code". See the Agreement between the Government of the Kingdom of Thailand and the Government of the Russian Federation on the Promotion and Reciprocal Protection of Investments, signed on 17 October 2002, not yet entered into force. In one case, the tribunal used the Czech statutory rate of interest without the investment treaty contracting parties specifically referring to the application of host state law to the determination of the rate of interest. See *Eastern Sugar B.V. (Netherlands) v. The Czech Republic*, SCC Case No. 088/2004, Partial Award, 27 March 2007 [373]-[374].

[74] C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 2; M Sornarajah, *the International Law on Foreign Investment* (4th edn, CUP 2017) 359-360.

BITs stipulate that they only protect 'investments' that are made 'in accordance with the laws of the host state.'[75] In fact, in resolving issues of jurisdiction, an investment treaty tribunal should in the first place refer to the relevant investment treaty, and when applicable, the ICSID Convention.[76] In certain respects, the investment treaty or the Convention will refer to the domestic laws of the contracting parties as applicable law (*renvoi*).[77] In such areas, the applicable law would be the domestic law, rather than the investment treaty itself, as it is the former which regulates the issue under consideration.

51. Moreover, even absent an explicit reference to internal laws, domestic law will be applied in specific areas where the jurisdictional issue concerns the 'sovereignty' of the state. For instance, it is widely-accepted in investment treaty arbitrations that nationality of an individual should be determined by reference to the law of the country whose nationality is being claimed, i.e. the home state of the investor.[78]
52. In the following pages, I will focus on the two cardinal and more debated spheres of jurisdiction, namely *ratione materiae* and *ratione personae*, and will see in which specific situations should an investment treaty arbitral tribunal apply domestic law.

**a. *Ratione Materiae***

53. When the issue under consideration is that of *ratione materiae*, most investment treaty tribunals, although with different approaches, have resorted to internal laws of host states, in one or several of the following situations: (i) determining the legality of an investment; (ii) verifying the creation and the existence of rights underlying an investment; and (iii) the

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[75] See, for instance, Article 1(2) of the Agreement between the Kingdom of Spain and the Republic of Albania on the Promotion and Reciprocal Protection of Investments, signed on 05 June 2003, entered into force on 14 January 2004: "The term "investment" means every kind of asset invested by investors of one Party in the territory of the other Party in accordance with the laws and regulations of the latter Party …".

[76] *Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Decision on Jurisdiction (Ancillary Claim), 02 August 2004 [38]; *CMS Gas Transmission Company v. Argentine Republic*, ICSID Case No. ARB/01/8, Decision on Objections to Jurisdiction (n 64) [88]; *Daimler Financial Services AG v. Argentine Republic*, ICSID Case No. ARB/05/1, Award, 22 August 2012 [50].

[77] In this regard, see *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 42) [47]-[52] (where the tribunal states that "[b]oth Parties agree, and rightly so, that the Tribunal's jurisdiction is governed by the ICSID Convention, by the Bolivia-Chile BIT […] and, to the extent the latter refers to it, by Bolivian law." Having noted that as per Article I(2) of the Bolivia-Chile BIT, 'investment' is defined as any kind of assets or rights related to an investment made in accordance with the laws and regulations of the host state, the tribunal concluded that: "… Bolivian law applies to determine (i) whether Quiborax and Allan Fosk were shareholders of NMM at the time the dispute arose in June 2004, and (ii) whether the Claimants' purported investment was made "in accordance with the laws and regulations" and the "legal provisions" of Bolivia […] Both Parties agree that these issues are governed by Bolivian law"; *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 42) [121]; *Churchill Mining PLC v. Republic of Indonesia* (n 42) & *Planet Mining Pty Ltd v. Republic of Indonesia* (n 42) both at [86] (stating that: "The Tribunal's jurisdiction is contingent upon the provisions of the ICSID Convention on the one hand, and of the […] BIT, […] on the other hand. In addition, where an international law instrument refers to jurisdictional requirements governed by the municipal law of a Contracting State, that municipal law shall also govern the jurisdiction of the Tribunal to the extent provided by the BIT."); M Sasson (n 1) 1-3; C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 2-3.

[78] See, for instance, the arbitral award in *Soufraki v. UAE*, where the tribunal held that: "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." *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Award, 07 July 2004 [55].

existence of the required approval for the investment. The role of the domestic law in these three areas will be subject to brief analysis in the following pages.

### i. The Legality Requirement

54. A majority of investment treaties expressly or impliedly indicate that 'investments' should be made 'in accordance' with the laws of the contracting party in whose territory the investment is made, i.e. the host state.[79] As an illustration, Article (1)1 of the BIT between Sweden and Kazakhstan provides: "The term "investment" shall mean any kind of asset owned or controlled directly or indirectly by an investor of one Contracting Party in the territory of the other Contracting Party, provided that the investment has been made in accordance with the laws and regulations of the other Contracting Party …"[80] This so-called 'legality requirement' is a prime 'gateway' for the application of domestic law as governing law in investment treaty arbitrations.[81] The above example epitomises a treaty expressly referring to the application of the host state law to the legality requirement. However, as will be explained in Chapter 2 of this Thesis, this requirement still counts, and so does the application of host state law, even if there is no such stipulation in the treaty.
55. Since in such a situation, domestic law is applied as 'law', rather than as 'fact', the outcome would be that if an investment is not made in accordance with the laws of the host state, it is not considered as an 'investment' protected by the investment treaty. That being so, the tribunal would have no jurisdiction *ratione materiae* to decide the case.[82]
56. To sum up this brief discussion, as a matter of legal determination, an arbitral tribunal which is charged with deciding an investment treaty case should analyse whether an investment is made legally in accordance with the laws and regulations of the host state. This application of host state law is mandatory, in most cases, because there is a *renvoi* to host state law in the investment treaty at issue. In addition, the legality requirement, and consequently, the application of the host state law, is still persistent even if the treaty does not expressly provide for it.

### ii. Creation and Existence of Rights Constituting Investments

57. As the tribunal in *Tidewater v. Venezuela* has indicated, reference to host state law in determining the existence of rights capable of protection under investment treaties is beyond

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[79] For instance, a comprehensive survey that I did on 60 of the bilateral investment treaties signed by Iran shows that a great majority of these treaties (more than 90%) contain express legality requirements. Furthermore, the rest of the Iranian BITs under consideration entail implicit references to the legality requirement. As such, there is no BIT, amongst the 60 agreements I could access, that does not contain an express or at least an implied reference to the legality requirement. Furthermore, another research that I did shows that all the bilateral investment treaties concluded by Australia, without one single exception, have express and/or implied legality requirements.

[80] Article 1(1) of the Agreement between the Government of the Kingdom of Sweden and the Government of the Republic of Kazakhstan on the Promotion and Reciprocal Protection of Investments, signed on 25 October 2004, entered into force on 01 August 2006. It is also noteworthy that certain BITs stipulate that a change in the form in which assets are invested does not affect their character as investments, provided such change is not contrary to the laws of the contracting party in whose territory the investment has been made. See, e.g., Article 1(2) of the Agreement between the Government of the Republic of Mauritius and the Government of the Republic of Ghana for the Promotion and Reciprocal Protection of Investments, signed on 18 May 2001, not yet entered into force.

[81] C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 5.

[82] See *Fraport v. Republic of Philippines*, ICSID Case No. ARB/03/25, Award (n 4) [396]-[404]; C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 4.

doubt.[83] In fact, it is the law of the host state which determines the creation, existence, scope, and nature of specific rights over a piece of property.[84] As has been put forward by the tribunal in *Emmis v. Hungary*, "the existence and nature of any such rights must be determined in the first instance by reference to Hungarian law, before the Tribunal proceeds to decide whether any such rights can constitute investments …"[85] Therefore, it is the law of the host state which determines whether, for example, title to an immovable property is perfected, whether the investor has acquired binding and enforceable contractual rights to a concession agreement, or more generally, whether the right alleged by the investor can be considered and recognised as 'property' protected by the treaty.[86]

58. In the absence of a definition of rights/interests and/or properties in the underlying investment treaty (either in the text of the treaty or through subsequent agreement or subsequent practice), there are two principal explanations for the application of the host state law to the issue of the existence of rights/interests over properties: (i) the application of the *lex situs* choice of law rule as a general principle of conflict of laws;[87] (ii) the need for a territorial nexus between the investment and the host state.[88] I will delve into these two reasons in a comprehensive way in Chapter 3 of this Thesis.
59. Keeping this in mind, it should be noted that although the fact that a property right or interest must exist under the law of host state in order to be protected under the investment treaty needs no stipulation in the relevant treaty itself, as this is a matter of host state sovereignty to which general international law has no rule to apply (unless the state contracting parties to the treaty agree otherwise in the treaty itself or through subsequent agreement or subsequent practice), still certain international investment agreements refer to the application of the host state law to the creation of property rights when enumerating different categories of 'investments' protected by the instrument. For example, Article 15.1(13) and 15-3 of the United States-Singapore Free Trade Agreement includes in its definition of 'investment' "licenses, authorizations, permits, and similar rights" with the important qualifier that they are "conferred pursuant to domestic law". The footnote to this provision notes that whether these rights hold the characteristics of an investment "depends upon such factors as the nature and extent of the rights that the holder has under the domestic law of the Party".[89] In addition, a small minority

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[83] *Tidewater Inc., Tidewater Investment SRL, Tidewater Caribe, C.A., et al. v. The Bolivarian Republic of Venezuela*, ICSID Case No. ARB/10/5, Award, 13 March 2015 [116].

[84] Z Douglas, *International Law of Investment Claims* (n 13) 52 *et seq*; E De Brabandere (n 5) 127. As will be seen in Chapter 3, the issue of the existence of rights over properties as a jurisdictional matter has a fellow traveller in expropriation cases, which is whether there exists a property right which is capable of expropriation.

[85] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 20) [149]. See also *William Nagel v. The Czech Republic* (n 20) [316] (stating that "the terms "investment" and "asset" in Article 1 of the Investment Treaty cannot be understood independently of the rights that may exist under Czech law.")

[86] *EnCana Corporation v. Republic of Ecuador* (n 48) [184], [188]; Z Douglas, *International Law of Investment Claims* (n 13) 52 *et seq*.

[87] Regarding the meaning and application of the rule see: E Rabel (n 46) 30; L Collins *et al* (eds), *Dicey, Morris and Collins on the Conflict of Laws* (14th edn, Sweet & Maxwell 2006) 1112–13. See also *George Rodney Burt (USA v. UK)* 6 RIAA 93; *Rio Grande Irrigation and Land Company (UK v. USA)* 6 RIAA 131; *Bank of New York and Trust Company et al. (USA v. Germany)* 8 RIAA 43.

[88] Z Douglas, *International Law of Investment Claims* (n 13) 52, 54-55.

[89] In this respect see JC Thomas & HK Dhillon (n 13) 976 (referring to United States – Singapore Free Trade Agreement, signed on 06 May 2003, entered into force 01 January 2004).

of BITs define intellectual properties covered by such instruments as those recognised by national laws of the host state.[90]

60. Therefore, for the reasons briefly discussed above, to constitute property rights protected by an investment treaty, such rights must exist under a domestic law, which law, in almost all cases, is the domestic law of the host state.

### iii. Approval of investments

61. In addition to the legality requirement, certain investment treaties require that an investment must be approved in accordance with the laws and regulations of the host state. For example, the Protocol of the BIT between Iran and Italy provides with reference to Article 1 of the Agreement that: "In the territory of the Islamic Republic of Iran[,] this Agreement shall apply to investments, reinvestments and any modification in the form of investments approved by the competent authority. ..."[91]

62. In the famous case of *Gruslin v. Malaysia*, the tribunal had before it Article 1(3)(i) of the BIT between Malaysia and Belgium-Luxembourg Union, providing that the agreement covers defined investments in Malaysia on the condition that such assets "… are invested in a project classified as an 'approved project' by the appropriate Ministry in Malaysia, in accordance with the legislation and the administrative practice, based thereon…"[92] Giving effect to this provision, the ICSID tribunal decided that no approval had been given by the competent authority in Malaysia for Gruslin's alleged investment and, consequently, held that it did not have jurisdiction to hear the case.[93]

63. Unlike the 'legality requirement' and the necessity of acquiring valid and enforceable property rights under the laws of the host state, the existence of the 'approval' condition and, subsequently, the application of the host state law to that requirement does need an expression in the relevant investment treaty. In other words, in the absence of a provision requiring the 'approval' of investments in accordance with the laws and regulations of the host state in the relevant investment treaty, the adjudicating forum has no reason and basis to check the investment approval mechanisms of the host state law in order to ascertain subject-matter jurisdiction.

## b. *Ratione Personae*

64. In addition to subject-matter jurisdiction, in order to ascertain jurisdiction to decide the case on its merits, an investment treaty tribunal needs to make sure that it has jurisdiction *ratione personae*. In this connection, it is for the tribunal to verify whether the claimant who has appeared before the tribunal falls within the definition of 'investor' in the relevant investment treaty vesting the tribunal with jurisdiction. To qualify as an 'investor', one needs to prove, to the satisfaction of the tribunal, that he/she is a 'national' of one of the contracting parties.

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[90] See, for instance, Article 1(2)(iv) of the Agreement between the Government of the Republic of India and the Government of the Republic of Ghana for the Reciprocal Promotion and Protection of Investments, signed on 05 August 2002, did not enter into force (terminated).

[91] Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Italian Republic and the Government of the Islamic Republic of Iran, signed on 10 March 1999, entered into force on 08 August 2003.

[92] Article 1(3)(i) of the Investment Guarantee Agreement between Malaysia and the Belgo-Luxemburg Union, signed on 22 November 1979, entered into force on 08 February 1982.

[93] *Philippe Gruslin v. Malaysia*, ICSID Case No. ARB/99/3, Award, 27 November 2000 [25.5]–[25.7].

65. To begin with, it is well-known that international law does not determine how nationality is acquired or lost. The Hague Convention on Certain Questions Relating to the Conflict of Nationality Law of 1930 provides in Article 1 that: "It is for each State to determine under its own law who are its nationals…"[94] In the same vein, the ICJ held in the *Nottebohm Case* that "it is for every sovereign state, to settle by its own legislation the rules relating to acquisition of nationality."[95] Similarly, in *Soufraki v. UAE*, the tribunal said that: "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."[96]
66. Accordingly, questions of nationality are answered by reference to domestic law. It is noteworthy that determining the nationality of an investor is one of the handful of instances where reference is made to the domestic laws of the home state, rather than the municipal laws of the host state.[97]
67. As was explained, a state has the sovereign right to set the benchmark for acquisition (or loss) of nationality. This goes without any stipulation in the relevant investment treaty. However, most investment treaties do express that nationality should be determined by reference to the laws of the home state. As to natural persons, there are two approaches in investment treaties: (i) a great majority of international investment agreements protect natural persons who are recognised as 'national' or 'citizen' by the home state's internal laws;[98] (ii) a small minority of investment treaties protect not only citizens but also individuals who qualify as permanent residents under domestic laws of the home state.[99] Almost the same observations made with respect to natural persons apply with regard to juridical persons. It is the law of the home state which determines whether a company, an incorporation, or more generally, an undertaking is a national of that country. This is again the result of the implementation of 'sovereignty' rights. However, investment agreements still express the role of home state law in the identification of the nationality of companies: A great majority of BITs use the place of 'incorporation',

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[94] See Convention on Certain Questions Relating to the Conflict of Nationality Law, signed on 13 April 1930, entered into force on 01 July 1937. See also Article 3 of the European Convention on Nationality, signed on 06 November 1997 in Strasbourg, entered into force on 01 March 2000.

[95] *Nottebohm* (*Liechtenstein v. Guatemala*), 2nd Phase Judgment, I.C.J. Rep. 1955 (06 April 1955) p 4, p 23.

[96] *Hussein Nuaman Soufraki v. The United Arab Emirates* (n 78) [55]. See also *Perenco Ecuador Ltd. v. The Republic of Ecuador and Empresa Estatal Petróleos del Ecuador* (n 20) [522] (stating that "[g]iven the absence of detailed general or conventional rules of international law governing the organisation, operation, management and control of an enterprise, a tribunal should in principle be guided by the more detailed prescriptions of the applicable municipal law…"); N Blackaby & C Partasides (n 63) 448.

[97] See *Iurii Bogdanov, Agurdino-Invest Ltd. and Agurdino-Chimia JSC v. Republic of Moldova*, SCC, Arbitral Award, 22 September 2005, Section 2.2.1 (ii) & (iii) (denying BIT protection to companies constituted under the laws of the host state, rather than the home state).

[98] As an example, the BIT between Iraq and Kuwait provides in Article 1(3) defining natural persons: "a) As regards the Republic of Iraq, Iraqis under the Iraqi Nationality and Naturalisation Law. b) As regards Kuwait, Kuwaitis under the Kuwaiti Nationality Law." See the Protocol between the Governments of the State of Kuwait and the Republic of Iraq on the Promotion of the Movement of Capital and Investments between the Two Countries, signed on 25 October 1964, entered into force on 07 June 1966.

[99] For instance, Article 1(e) of the BIT between Canada and Croatia defining the term 'investor', provides with regard to natural persons: "… in the case of The Republic of Croatia: (i) any natural person possessing the citizenship of or permanently residing in The Republic of Croatia in accordance with its laws … in the case of Canada: (i) any natural person possessing the citizenship of or permanently residing in Canada in accordance with its laws …" See Agreement between the Government of the Republic of Croatia and the Government of Canada for the Promotion and Protection of Investments, signed on 03 February 1997, entered into force on 30 January 2001.

'registration' or 'constitution' test, alone,[100] or in combination with other tests, such as 'seat' and/or 'control',[101] to ascribe nationality to a legal entity. The incorporation (registration) of a company is then determined by reference to the laws of the home state.[102] For example, the BIT between Belgium-Luxembourg Economic Union and Montenegro, defining the term 'companies', provides in Article 1(1)(b): "… [T]he "companies", i.e. any legal person constituted in accordance with the legislation of the Kingdom of Belgium, of the Grand Duchy of Luxembourg or of Montenegro and having its registered office in the territory of the Kingdom of Belgium of the Grand Duchy of Luxembourg or of Montenegro respectively."[103]

68. Having discussed the role of domestic law in the two cardinal jurisdictional thresholds described above, i.e., jurisdiction *ratione materiae* and jurisdiction *ratione personae*, I will now turn to the role of domestic law in issues concerning merits.

### B. The Role of Domestic Law in Issues Concerning Merits

69. Generally speaking, absent explicit treaty provisions, domestic laws have much less to say as 'law' in matters concerning the substantive rights of investors and obligations of the host states under international investment agreements. In this connection, it is a well-established prism of international law that a state "may not invoke the provisions of its internal law as justification for its failure to perform a treaty"[104] and that "[t]he characterization of an act of a State as internationally wrongful is governed by international law. Such characterization is not affected by the characterization of the same act as lawful by internal law."[105] As early as 1932, the PCIJ held in *Treatment of Polish Nationals in the Danzig Territory*,

> [a] state cannot adduce as against another State its own Constitution with a view to evading obligations incumbent upon it under international law or treaties in force. Applying these principles to the present case, it results that the question of the treatment of Polish nationals or other persons of Polish origin or speech must be settled exclusively on the basis of the rules

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[100] See, for instance, Article 1(1)(b) of the Agreement between the Government of the Lebanese Republic and the Government of the Republic of Belarus on the Promotion and Reciprocal Protection of Investments, signed on 19 June 2001, entered into force on 29 December 2002.

[101] See, for instance, Article 1(5)(b) of the Agreement between the Government of the Republic of Colombia and the Government of the Republic of Turkey Concerning the Reciprocal Promotion and Protection of Investments, signed on 28 July 2014, not yet entered into force.

[102] In addition, it should be noted that the law applicable to the capacity and standing of a company to bring and pursue an investment treaty claim is the *lex societatis*, which is usually the law of the place of incorporation. See Z Douglas, *International Law of Investment Claims* (n 13) 78-79.

[103] Agreement between The Belgium-Luxembourg Economic Union, on the one hand, and Montenegro, on the other hand, on the Reciprocal Promotion and Protection of Investments, signed on 16 February 2010, not yet in force.

[104] See Article 27 of the Vienna Convention on the Law of Treaties ("VCLT"), adopted and opened for signature on 23 May 1969, entered into force on 27 January 1980. Put differently, since domestic laws are not usually applied as 'law' in issues concerning the merits of the case on an international plane, a state cannot use provisions of its own law as a defence to a claim against it for alleged breaches of international law. See also Article 32 of the Draft Articles on the Responsibility of States for Internationally Wrongful Acts ("ILC Draft Articles") by the International Law Commission ("ILC") adopted in August 2001 (providing that: "The responsible State may not rely on the provisions of its internal law as justification for failure to comply with its obligations under this Part.")

[105] See Article 3 of the ILC Draft Articles. See also *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic* (n 11) [95]-[96] (relying on Article 3 of the ILC Draft Articles).

> of international law and the treaty provisions in force between Poland and Danzig.[106]

70. Similarly, the Annulment Committee in the *Vivendi* case held that:

> [I]n respect of a claim based upon a substantive provision of that BIT … the inquiry which the ICSID tribunal is required to undertake is one governed by the ICSID Convention, by the BIT and by applicable international law. Such an inquiry is neither in principle determined, nor precluded, by any issue of municipal law …[107]

71. In fact, substantive investment treaty standards have an independent operation as international law standards. To be sure, international law defines and circumscribes the substantive treaty standards and it is against this definition and circumscription that the legality of the conduct of the host state and its international responsibility is to be assessed.[108]
72. However, this is not to propose that national laws have no role to play with respect to substantive issues. This matter requires more in-depth scrutiny. In the words of McLachlan,

> [t]ribunals may owe their jurisdiction to the terms of a particular bilateral investment treaty. But that does not mean that the law applicable to the determination of the merits is so limited. Treaty rights are located within a matrix of applicable law, which includes a role for host state law, as well as a broader set of international law principles beyond the specific terms of the treaty. The question of the law applicable to the substance turns out, on examination, to require a more sophisticated legal reasoning approach, which combines choice of law analysis with techniques of interpretation.[109]

73. In my opinion, domestic law has two different principal functions in matters concerning the merits of the case: (i) as 'facts' or 'evidence', which should be analysed and/or considered before a determination is made as to compliance with a treaty standard in accordance with international law; (ii) as part of the 'applicable law', either governing the basis of a claim like

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[106] *Treatment of Polish Nationals and Other Persons of Polish Origin or Speech in Danzig Territory*, Advisory Opinion, P.C.I.J. Rep. Series B, No. 44, 1932 (04 February 1932) p 24. In the *Free Zones Case*, it was decided by the PCIJ that "France cannot rely on its own legislation to limit the scope of its international obligations". See *Free Zones of Upper Savoy and the District of Gex* (*France v. Switzerland*), Judgment, P.C.I.J. Rep. Series B, No. 46, 1932 (07 June 1932) p 167. Furthermore, in the Advisory Opinion in the *Greco-Bulgarian Communities Case*, it was stated that "it is a generally accepted principle of international law that in the relations between Powers who are contracting Parties to a treaty, the provisions of municipal law cannot prevail over those of the treaty". See *Greco-Bulgarian Communities*, Advisory Opinion, P.C.I.J. Rep. Series B, No. 17, 1930 (31 July 1930) p 32.

[107] *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic* (n 11) [102]. See also *SGS Société Générale de Surveillance S.A. v. The Republic of Paraguay*, ICSID Case No. ARB/07/29, Decision on Jurisdiction, 12 February 2010 [72]; Kjos (n 72) 77-78 (stating that: "Where the investor bases its claim on a provision of an investment treaty, it would […] be both legally impossible and contrary to the intentions of the states parties to the treaty for the tribunal to apply national law to establish an international wrongful act on the part of the host state. Indeed, an international claim requires the application of international law.")

[108] C McLachlan, 'Investment Treaty Arbitration: The Legal Framework' (n 21) 114; N Blackaby & C Partasides (n 63) 465, 467; E De Brabandere (n 5) 125-126. For the relevant case law, see, for example, *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Award (n 9) [67].

[109] C McLachlan, 'Investment Treaty Arbitration: The Legal Framework' (n 21) 103.

a contractual claim considered in the framework of an investment treaty dispute or governing a particular issue of substance when a treaty explicitly provides for its application. In the following pages, I will briefly touch upon these two functions.

**a. Domestic Law as 'Fact' in Issues Concerning Merits**

74. As was stated above, domestic law is usually applied as 'facts' in issues concerning merits in investor-state arbitrations. In such circumstances, domestic law is possible 'evidence' of a state's compliance or non-compliance with an international obligation.[110] A couple of examples of such application of domestic law (as 'facts' or 'evidence') in matters of substance is given by the tribunal in *Alps Finance v. Czech Republic*. The tribunal exemplifies certain situations in which an arbitral tribunal needs to factually analyse domestic laws to see whether the international obligation in question has been violated:

> This may for instance be the case of a miscarriage or denial of justice committed in patent disregard of the investor's procedural or substantive rights under domestic law, or of an intolerable abuse in the administration of a public contract between the investor and a State entity governed by municipal law, or of any other behaviour of State organs amounting to an intolerable impropriety in the way they apply internal law provisions against a foreign investor. In all above cases, reference to internal law is necessary to establish whether the host State is also liable for a violation of an international obligation under the applicable treaty or general international law.[111]

Zachary Douglas also provides us with another tangible example of domestic law being applied as 'fact' and/or 'evidence' in considering a matter of merits in an investment arbitration, this time from the perspective of a host state's defence:

> For instance, where the host state defends its alleged expropriatory conduct as 'non-discriminatory' and refers to other legislative enactments that treat different investors in the same way, these enactments are 'facts' for the investment treaty tribunal's judgment as to whether the test for expropriation has been satisfied in the particular instance.[112]

75. As noted above, one consequence of being applied as 'fact' in a substantive issue of merits is that compliance with domestic law does not necessarily translate to compliance with the international obligation in question. Equally, the tribunal deciding the investment treaty claim

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[110] *Gami Investments, Inc. v. The Government of the United Mexican States* (n 19) [91]; *Siemens A.G. v. The Argentine Republic*, ICSID Case No. ARB/02/8, Award, 17 January 2007 [78]. See also J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 13-40 (discussing and reviewing jurisprudence with respect to the possible application of domestic law as 'fact' when considering claims of fair and equitable treatment).

[111] *Alps Finance and Trade AG v. The Slovak Republic*, UNCITRAL, Award, 05 March 2011 [197].

[112] Z Douglas, *International Law of Investment Claims* (n 13) 70. There are further examples to be given: for instance, in order to examine whether the national treatment standard is breached or not, a tribunal might be asked to assess either an alleged discriminatory measure (*de facto discrimination*) or an alleged discriminatory law or regulation of the host state (*de iure discrimination*). In the latter case, the tribunal needs to take into account such laws as 'facts' for its comparative analysis, and then decide whether the standard of national treatment is breached according to the terms of the investment treaty and the principles of international investment law.

will not find the recipient state in breach of the investment treaty simply due to the violation of the latter's domestic law. In the *ELSI Case*, the ICJ pinpointed this rule, expressing that:

> Compliance with municipal law and compliance with the provisions of a treaty are different questions. What is a breach of treaty may be lawful in the municipal law and what is unlawful in the municipal law may be wholly innocent of violation of a treaty provision …

The Court further explained,

> [T]he fact that an act of a public authority may have been unlawful in municipal law does not necessarily mean that that act was unlawful in international law, as a breach of treaty or otherwise. A finding of the local courts that an act was unlawful may well be relevant to an argument that it was also arbitrary; but by itself, and without more, unlawfulness cannot be said to amount to arbitrariness… Nor does it follow from a finding by a municipal court that an act was unjustified, or unreasonable, or arbitrary, that that act is necessarily to be classed as arbitrary in international law, though the qualification given to the impugned act by a municipal authority may be a valuable indication.[113]

**b. Domestic Law as 'Law' in Issues Concerning Merits**

76. As was alluded to above, domestic law functions as "law" in issues concerning merits in either of the two following scenarios: (i) the treaty expressly refers to the application of the domestic law to the substantive matter at issue; (ii) the issue in question is in nature governed by a domestic law, like a contractual dispute. These two situations will be examined briefly in the ensuing pages.

**i. Express Treaty Reference to the Application of Domestic Law as 'Law'**

77. Commentary to Article 3 of the ILC Articles on Responsibility of States for Internationally Wrongful Acts considers that domestic laws can also form part of a treaty standard of protection in certain circumstances. In the words of the ILC:

> [I]n the fields of injury to aliens and their property and of human rights, the content and application of internal law will often be relevant to the question of international responsibility. In every case it will be seen on analysis that either the provisions of internal law are relevant as facts in applying the applicable international standard, or else that they are actually

[113] *Elettronica Sicula S.p.A. (ELSI)* (*United States of America v. Italy*), Judgment, I.C.J. Rep. 1989 (20 July 1989) p 15, p 51 [73] and p 74 [124]. By the same token, in *Alps Finance v. Slovak Republic*, it was held that: "… [M]unicipal law and the way it is enforced by State organs may well be relevant to the merits. Even in such a contest [sic] municipal law is not the "governing" law, but it constitutes a factual circumstance to be considered for ascertaining whether the host State committed a breach of its international duties in the enforcement of its own law… [A] possible breach by the state of its own law is not *per se* sufficient to constitute a breach of its international duties, which only occurs in the specific cases where the former gives inevitably rise to the latter …" *Alps Finance and Trade AG v. The Slovak Republic* (n 111) [197]-[198].

> incorporated in some form, conditionally or unconditionally, into that standard.[114]

78. Therefore, when the relevant investment treaty explicitly provides that in order to assess compliance with a treaty standard, the tribunal needs to refer to the laws of the host state, domestic law would act as 'law'. An example of this approach is Article IV of the Cooperation Agreement between the countries of the Caribbean Common Market ("CARICOM") and Cuba which provides: "Each Party shall ensure fair and equitable treatment of Investments of Investors of the other Party under and subject to national laws and regulations."[115] Another example is the BIT between India and Indonesia, which provides in Article 4(3): "Each Contracting Party shall, subject to its laws and regulations, accord to investment of investors of the other Contracting Party treatment no less favorable than that which is accorded to investments of its investors."[116]
79. Faced with such wording and formulation, an investment treaty tribunal should comply with the express treaty terms, respect the parties' choice, and apply the laws of the host state to the merits of the case. In such circumstances, the panel of arbitrators should decide whether the host state should be held internationally responsible by reference to the laws of the host state. The *Bogdanov v. Moldova* case is a good illustration in this respect: the claimants had argued that the respondent had violated Article 2(2) on 'full protection' and Article 3 on 'fair and equitable treatment' of the BIT between Russia and Moldova. Article 2(2) of the BIT contained the obligation of the host country to guarantee, in accordance with its own legislation, full and unconditional legal protection of the investments made by investors of the other contracting state. The question before the tribunal was whether this standard was violated by the introduction of a cap on the stock ownership by the Government of Moldova. Having noted that the language of Article 2(2) of the BIT was clear to the effect that the standard was not to be considered as 'corrective' of the host state's legislation, but had to be applied in accordance with Moldovan law, the tribunal found that as long as the restrictive measure adopted by the respondent did not contravene the law of Moldova, the full protection standard of the BIT had not been violated.[117] In contrast, Article 3 of the same BIT provided for the host state's commitment to grant investors of the other contracting party fair and equitable treatment. In the absence of any reference to host state law as the gauge for the application of the fair and equitable treatment standard in the pertinent treaty, the tribunal came to the conclusion that this time the standard "must be interpreted in accordance with the ordinary meaning of the terms, as well as the object and purpose of the BIT" and that the standard of treatment provided under Article 3 "must be interpreted to cover also any conduct that, even if it is in compliance with the national law of the host country … has unjust or unreasonable results …" As a corollary, the tribunal tested the same government measure (restriction on stock ownership)

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[114] Draft Articles on Responsibility of States for Internationally Wrongful Acts, with Commentaries (2001) UN Doc. A/56/10 [7].

[115] Article IV of the Trade and Economic Co-Operation Agreement between the Caribbean Community ("CARICOM") and the Government of the Republic of Cuba, signed on 05 July 2000, entered into force on 01 January 2001.

[116] Agreement between the Government of The Republic of Indonesia and the Government of the Republic of India for the Promotion and Protection of Investments, signed on 10 February 1999, entered into force on 22 January 2004.

[117] *Iurii Bogdanov, Agurdino-Invest Ltd. and Agurdino-Chimia JSC v. Republic of Moldova* (n 97) Section 4.2.3.

against fair and equitable treatment as an international standard of investment protection and found Moldova in breach of this standard.[118]

80. To give another example, in an expropriation context, some treaties expressly provide that the condition of 'due process', one of the frequently stated conditions for lawful expropriations in investment treaties, shall be examined by reference to the laws of the host state. Thus, in *Tenaris v. Venezuela*, the tribunal, *inter alia*, focused on the language of Article 4(a) of the Venezuela-Portugal BIT[119] which, for the tribunal, had "an explicit *renvoi* to Venezuelan domestic law". The tribunal found the expropriation by Venezuela in that case to be unlawful, amongst others, in the light of the fact that Venezuela had failed to observe the requirements of its own nationalisation legislation in carrying out the expropriation.[120]
81. To sum up, when a treaty expressly requires the application of domestic law as 'law' to a matter of merits and as the yardstick for finding 'international responsibility', an investment treaty tribunal should apply domestic law as 'law'. However, it should be noted that absent a clear legal definition or conclusive jurisprudence in host state law with respect to such international standards, like the fair and equitable treatment standard, when applying host state law to such matters, difficulties might arise in practice.[121]

### ii. Contractual Claims

82. An investment treaty tribunal would be competent to decide contractual claims in two instances: (i) when the treaty expressly provides for the jurisdiction of the tribunal to decide contractual disputes; and (ii) when the determination of whether a treaty obligation has been violated requires a primary analysis of whether the underlying investment contract has been breached. The latter analysis might be necessary in case the alleged treaty violation in question concerns the so-called 'umbrella clause'.[122]
83. It seems to be a settled issue that the law applicable to contractual claims is different from the law applicable to treaty claims. Generally speaking, whereas contractual claims are governed by the proper law of the contract, treaty claims are subject to international law.[123] The very well-known statement of the ICSID Annulment Committee in *Vivendi v. Argentina* explicates this point:

> [W]hether there has been a breach of the BIT and whether there has been a breach of contract are different questions. Each of these claims will be

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[118] ibid, Section 4.2.4.

[119] The BIT between the Portuguese Republic and the Government of the Republic of Venezuela, signed on 17 June 1994, entered into force on 07 October 1995. For a similar provision, see Article 4(1) of the Agreement between the Government of the Kingdom of Thailand and the Government of the Russian Federation on the Promotion and Reciprocal Protection of Investments (n 73).

[120] *Tenaris S.A. and Talta - Trading e Marketing Sociedade Unipessoal Lda. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/11/26, Award, 29 January 2016 [493]-[495].

[121] In this respect, see E De Brabandere (n 5) 5 (explaining the difference between the substantive standards of protection in investment treaty arbitrations and domestic law standards in public/administrative law disputes in the context of showing that the two fields of law, although have much in common, are not intrinsically the same.)

[122] ibid 127; PB Stephan, 'International Investment Law and Municipal Law: Substitutes or Complements?' (2014) 9(4) CMLJ 358-359.

[123] In *Mobil Oil Iran v. Iran*, the Iran-US Tribunal held that "allegations of breach [of contract] and allegations of expropriation raise different and distinct legal issues which thus must be considered separately". *Mobil Oil et al v. Iran et al*, IUSCT Case No. 74, 76, 81 & 150, Award No. 311-74/76/81/150-3, 14 July 1987, 16 Iran-USCTR, p 3, p 20 [58].

> determined by reference to its own proper or applicable law—in the case of the BIT, by international law; in the case of the Concession Contract, by the proper law of the contract, in other words, the law of Tucumán.[124]

Indeed, as is plain from the Annulment Committee's statement, generally speaking, it is the law of the host state which governs the merits of a contractual dispute.[125] In this connection, Article 9.25(2) of Trans-Pacific Partnership ("TPP"),[126] provides that in cases where the dispute is in relation to an alleged violation of an investment authorisation or an investment agreement [contract], the tribunal should apply:

> (a) the rules of law applicable to the pertinent investment authorisation or specified in the pertinent investment authorisation or investment agreement, or as the disputing parties may agree otherwise; or
>
> (b) if, in the pertinent investment agreement the rules of law have not been specified or otherwise agreed:
>
> (i) the law of the respondent, including its rules on the conflict of laws; and
>
> (ii) such rules of international law as may be applicable.[127] [footnotes omitted]

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[124] *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic* (n 11) [96]. See also *Payment of Various Serbian Loans Issued in France* (n 10) p 41 (stating: "Any contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of some country"); *Wintershall AG v. The Government of Qatar* (n 10) 821-823; *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Award (n 9) [67]; *Van Zyl and Others v. Government of Republic of South Africa and Others* (n 10) [64] (stating that: "Contracts concluded between states and aliens, are also governed by municipal law."); SKB Asante (n 10) 406 (opining that "an agreement between a host State and a private corporation … does not enjoy the status of an international agreement and on well settled principles of private international law, such an agreement should be governed by the law of the host state and not public international law.")

[125] Whereas, in most instances, the domestic law of the host state is applicable to the contractual dispute, there are still cases in which the parties' agreement or a conflict of laws analysis might lead to the application of another domestic law. See A Parra (n 12) 5-6. Parra exemplifies his opinion with 'commercial loan' arrangements as a sort of contract in which another domestic law (other than that of the host state) might apply to the contractual dispute in question.

[126] The Trans-Pacific Partnership ("TPP") is a trade and investment agreement between Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam, and the United States which was signed on 04 February 2016 but was not ratified as required and did not come into force. Indeed, after the United States withdrew its signature, the agreement could not enter into force as structured and planned. All original TPP signatories, except the United States, agreed in May 2017 to revive the TPP and reached agreement in January 2018 to conclude the Comprehensive and Progressive Agreement for Trans-Pacific Partnership ("CPTPP" or TPP11 (with number 11 representing the number of the member states of the Partnership)). The formal signing ceremony was held on 08 March 2018 in Santiago, Chile. See J Hepburn, 'Revived Trans-Pacific Partnership (TPP) Treaty Text Is Released, With A Few Tweaks to The Previously-Negotiated Investment Chapter; Australia And New Zealand Continue to Disapply ISDS Between Them', 21 February 2018, See <https://proxy.ppl.nl:2094/articles/revived-trans-pacific-partnership-tpp-treaty-text-is-released-with-a-few-tweaks-to-the-previously-negotiated-investment-chapter-australia-and-new-zealand-continue-to-disapply-isds-between-them/> 'accessed 31 May 2018'.

[127] This provision is in contrast to paragraph 1 of the same Article, which concerns the 'governing law' of disputes based on alleged violations of the investment chapter of the Agreement itself, i.e., disputes arising out of the alleged treaty breaches. In such circumstances, the tribunal should apply the TPP and applicable rules of international law. A footnote to this latter provision notes: "For greater certainty, this provision is without prejudice to any consideration of the domestic law of the respondent when it is relevant to the claim as a matter of fact." ibid. See also C Schreuer,

84. According to this provision, absent an agreement by the contractual parties regarding the governing law, the dispute will be decided in accordance with the law of the host state and such rules of international law as may be applicable.
85. In this context, one may reasonably point to the possibility of a contract being subject to international law according to the explicit or implicit choice of the parties,[128] and, thus, deny the application of the host state law to an investment contract dispute. While it is theoretically possible for the parties to an investment contract to make such a choice, however, the choice would not be meaningfully helpful in deciding an actual investment contract claim since international law does not contain plenty of rules governing and regulating the specifics of contractual disputes.[129] Considering that a contract cannot exist in a vacuum,[130] even under such circumstances, the otherwise applicable domestic law will inevitably step in to fill the gaps in regulating the merits of an investment contractual relationship.[131]

**Conclusion**

86. It was shown in this Chapter that national law is sometimes 'relevant' and sometimes 'conclusive' in investment treaty arbitrations. Its application is 'relevant' when it is used in the form of a set of 'facts' which are necessary to deal with before deciding the issue on the basis of applicable international law. However, municipal law is also applied in the form and as a matter of 'law' in certain circumstances, and in this capacity it is 'conclusive' on the legal matters before an investment treaty tribunal. Bearing these discussions in mind, it is plainly wrong, or at least inaccurate, to argue, as some have,[132] that since investment treaty tribunals

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'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (n 12) 15-16 (analysing Article 24(1) of the US Model BIT (2012), which has a similar formulation).

[128] HE Kjos (n 72) 213 *et seq*.

[129] As an instance, see the ICSID tribunal's statement in *Adriano Gardella v. Ivory Coast* to the effect that public international law does not have plenty of rules governing specifics of contractual issues, except for the very generic rule of '*pacta sunt servanda*' and the principle of 'good faith'. See *Adriano Gardella S.p.A. v. Côte d'Ivoire*, ICSID Case No. ARB/74/1, Award, 29 August 1977, 1 ICSID Rep 283, 287 [4.3]. See also HE Kjos (n 72) 221.

[130] As FA Mann has eloquently put it, "freedom of contract does not exist independently of the legal systems which grant it or confer any measure of sovereignty upon the contracting parties." See FA Mann, 'The Proper Law of Contracts Concluded by International Persons' (1959) 35 BYIL 56. See also *Saudi Arabia v. Arabian American Oil Company* (*Aramco*) (1963) 27 ILR (indicating "[i]t is obvious that no contract can exist in vacuo, i.e. without being based on a legal system. The conclusion of a contract is not left to the unfettered discretion of the parties. It is necessarily related to some positive law which gives legal effect to the reciprocal and concordant manifestations of intent made by the parties. The contract cannot even be conceived without a system of law under which it is created.") See also Lord McNair, 'The General Principle of Law Recognized by Civilized Nations' (1957) 33 BYIL 7; N Blackaby & C Partasides (n 63) 156-157.

[131] See *Adriano Gardella S.p.A. v. Côte d'Ivoire* (n 129) 287 [4.3].

[132] See *EnCana Corporation v. Republic of Ecuador* (n 48) Partial Dissenting Opinion of Horacio A. Grigera Naon, 30 December 2005 [12] (disagreeing with the application of domestic law to the question of the existence of investment and stating that "[…] the local laws, administrative acts and practices and other conduct attributable to the host State at the moment they had the effect of operating the deprivation of property, are *facts* to be freely evaluated by the arbitrators to determine if the foreign investor's entitlement to protection under international law has been infringed at a specific moment in time or not."); *Vladimir Berschader and Moïse Berschader v. The Russian Federation* (n 31) [96] (stating that: "The Vienna Convention provides no role for the domestic law of contracting states in the interpretation of international treaties. Therefore, in the instant case, it is clear that Russian national law is of no relevance in this regard. While Russian law may be relevant in establishing certain factual circumstances involved in the merits of the case, it has no role to play in determining the jurisdiction of the Tribunal."); *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. The Argentine Republic* (n 42) [217]-[218]

are international tribunals applying rights under a treaty, international law must always prevail and municipal laws are merely 'facts' to be ascertained.

87. When applied as governing law, domestic law plays a role either because; (i) the parties have expressly referred to that body of law in the relevant investment treaty; or (ii) the question is in relation to the sovereignty of the state and has a national nature to which customary international law fails to provide a proper response.[133]
88. It was also submitted in this Chapter that in finding the applicable law to each question before an investment treaty tribunal, in particular, questions of jurisdiction, the possible applicable law provision of the pertinent investment treaty, and in case of ICSID arbitrations, Article 42(1) of the Convention, are of very little help, and in most situations border redundancy, as they do not guide the tribunal as to the sequence and priority of the possible applicable laws and their proper application in distinct jurisdictional and substantive issues.
89. According to the analysis done in this Chapter, domestic law is applied as 'law' in both jurisdiction *ratione materiae*, and jurisdiction *ratione personae* spheres. In both areas, domestic law of either the home or, more frequently, the host state has the last say on certain specific matters. In addition, it was shown that whereas domestic law is usually applied as 'fact' and 'evidence' in issues concerning merits, there are windows of opportunity for such laws to also cast as 'laws' in such circumstances, namely, (i) where the parties to the treaty have expressly provided so; and (ii) where the issue in question is governed by domestic law by its nature, like a contractual claim.
90. Having all these discussions in mind, a number of conclusions are in order: (1) in investment treaty arbitrations, domestic law can appear both as 'facts' and as 'laws' in matters of jurisdiction and merits. (2) In contrast to responsibility issues, domestic law is more frequently applied as 'law' in jurisdictional issues. This is partly because the applicable law regime of jurisdiction is different from and independent of the applicable law regime of merits. (3) In certain situations, the application of domestic law as 'law' is because of the stipulation in the treaty, like reference to domestic law with respect to 'approval' of investments. In other situations, such application is due to the nature of the issue, like the creation and existence of property rights underlying an investment. There are also communal areas in which domestic law is applied as 'law', both because the treaty has so provided and also because the nature of the issue necessitates the application of domestic law, like the 'legality requirement' or determining the nationality of a natural person.

(where the tribunal holds that reference to domestic law in certain jurisdictional areas is for the purpose of determining "a question of fact"). See also G Sacerdoti, 'Investment Arbitration under ICSID and UNCITRAL Rules: Prerequisites, Applicable Law, Review of Awards' (2004) 19(1) ICSID Rev-FILJ 25-26

[133] HE Kjos (n 72) 157.

## Introduction to Chapters 2 & 3: The Role of Domestic Law in Determining the Jurisdiction *Ratione Materiae* of Investment Treaty Tribunals

1. A great majority of investment treaties contain an introductory provision which purports to define the term 'investment'. Such a provision usually starts with a brief introduction, followed by a long list of assets which are usually samples of properties or property rights protected by the treaty.[1] What we are principally concerned with here in this Part is the brief introduction of the provision mentioned above. To open the discussion with an example, Article 1(1) of the BIT between Germany and Philippines provides:

> [T]he term "investment" shall mean any kind of asset accepted in accordance with the respective laws and regulations of either Contracting State …[2]

2. There are two elements in this brief sentence which this Thesis concerns itself with: first, the term 'asset' which has not been defined in the Treaty, and second, the phrase 'accepted in accordance with the respective laws and regulations of either Contracting State', or the so-called 'legality requirement'. These two issues have generated great debate in both practice and theory. Many pages of commentaries, scholarly writings, awards, decisions, and briefs have been devoted to discussing the meaning, scope, and legal consequences of such terms and phrases in the field of investment treaty law.

3. Since the determination of the meaning, scope, and legal consequences of these terms and phrases is central to the scope of application of investment treaties and, therefore, to the jurisdiction of an arbitral tribunal owing its competence to such treaties, where appropriate, when faced with an investment treaty claim, state respondents tend to formulate dispositive defences according to which the investor has acquired no rights and/or interests over assets or properties it alleges it owned or possessed, or that the investment it has allegedly made has been obtained through some sort of 'illegality'.[3] In more recent years, the 'illegality' defence

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[1] According to credible research carried out by UNCTAD, there are two major methods for the definition of the term 'investment' in investment treaties: a majority of investment treaties have used 'asset-based' definitions in investment protection agreements and a minority of investment agreements have opted for an 'enterprise-based' definition. See UNCTAD, *Scope and Definitions* (United Nations 2011) 21-22. While a great majority of investment treaties containing 'asset-based' definitions use open-ended and non-exhaustive listings of assets and properties, according to the same research conducted by UNCTAD, there are certain investment treaties which have used a closed-list approach. ibid 34-36.

[2] See Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 18 April 1997, entered into force on 01 February 2000.

[3] The following cases are some of the cases in which the issue of the legality requirement has been raised by respondent states: *Achmea B.V. (formerly Eureko B.V.) v. Slovak Republic* [I], PCA Case No. 2008-13; *Alasdair Ross Anderson et al. v. Republic of Costa Rica,* ICSID Case No. ARB (AF)/07/3; *Bear Creek Mining Corporation v. Republic of Peru*, ICSID Case No. ARB/14/21; *Convial Callao S.A. and CCI - Compañía de Concesiones de Infraestructura S.A. v. Republic of Peru*, ICSID Case No. ARB/10/2; *David Minnotte and Robert Lewis v. Republic of Poland*, ICSID Case No. ARB(AF)/10/1; *Flughafen Zürich A.G. et al. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/10/19; *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25; *Fraport AG Frankfurt Airport Services Worldwide v. Republic of the Philippines*, ICSID Case No. ARB/11/12; *Gustav F W Hamester GmbH & Co KG v. Republic of Ghana*, ICSID Case No. ARB/07/24; *Inceysa Vallisoletana S.L. v. Republic of El Salvador*, ICSID Case No. ARB/03/26; *Ioannis Kardassopolos v. Georgia*, ICSID Case No. ARB/05/18; *Khan Resources Inc., et al. v. Government of Mongolia*, UNCITRAL; *Liman Caspian Oil BV and NCL Dutch Investment BV v. Republic of Kazakhstan*, ICSID Case No. ARB/07/14; *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania*, ICSID Case No. ARB/11/24; *Metal-Tech Ltd. v. Republic of Uzbekistan*,

and the defence that no rights and/or interests over assets or properties exists are being more frequently raised in investment treaty arbitrations by respondent states in jurisdictional phases. One reason for such a defensive strategy is that, if successfully pleaded, as recent case-law has proven, the respondent would have the investor's entire case dismissed based on and due to the investor's unlawful conduct at the time of acquiring the investment and/or the inexistence of rights and/or interests over properties and assets. Another explanation for the prevalence of such defences in investor-state arbitrations, and this is particular to the legality requirement, is the growing frequency with which these clauses recur in international investment agreements. As a result, international arbitral panels have to deal with such defences over and over again for ascertaining or dismissing jurisdiction.

4. As was discussed in Chapter 1, such defences are based on the legal system of the host state. Through such jurisdictional defences, the recipient states argue before investment treaty adjudicating forums that the investor has acquired no rights and/or interests over properties or assets under its legal system, and/or that the investor, in acquiring its investment, has violated the laws of the host state.

5. For an investment treaty arbitral tribunal to decide such issues, it should answer three critical questions: **first**, why such matters should be resolved by reference to the laws of the host state? **second**, if the laws of the host state are applicable to such issues, how is the tribunal supposed to ascertain the contents of such law? and **third**, how to apply the verified host state law to the specific questions concerning the legality requirement or the defence of the inexistence of rights/interests in practice? [4]

6. In order to answer these questions, in Chapters 2 and 3 of this Thesis, the discussion will be followed in three parts: first, the legal basis for referring to the laws of the host state in resolving these jurisdictional matters; second, the actual function of the verified host state law in resolving specific questions regarding these jurisdiction *ratione materiae* issues. Chapter 2 addresses these two questions with regard to the legality requirement and Chapter 3 will endeavour to answer these same issues with respect to the question of the creation and

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ICSID Case No. ARB/10/3; *Phoenix Action, Ltd. v. Czech Republic*, ICSID Case No. ARB/06/5; *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24; *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia*, ICSID Case No. ARB/06/2; *SAUR International S.A. v. Argentine Republic*, ICSID Case No. ARB/04/4; *Veteran Petroleum Limited (Cyprus) v. Russian Federation*, PCA Case No. AA 228; *Vladislav Kim and others v. Republic of Uzbekistan*, ICSID Case No. ARB/13/6; *Yukos Universal Limited (Isle of Man) v. Russian Federation*, PCA Case No. AA 227.

The ensuing cases are some of the cases in which the issue of the non-existence of rights/interests over properties and assets has been raised by respondent states: *Accession Mezzanine Capital L.P. and Danubius Kereskedöház Vagyonkezelö Zrt. v. Hungary*, ICSID Case No. ARB/12/3; *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary*, ICSID Case No. ARB/12/2; *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL *(formerly EnCana Corporation v. Government of the Republic of Ecuador)*; *Generation Ukraine, Inc. v. Ukraine*, ICSID Case No. ARB/00/9; *William Nagel v. The Czech Republic*, SCC Case No. 049/2002.

[4] In this respect, see Y Banifatemi 'The Law Applicable in Investment Treaty Arbitration' in K Yannaca-Small (ed) *Arbitration under International Investment Agreements* (OUP 2010) 191-192 (distinguishing between (i) the identification of the applicable law; (ii) the subsequent investigation concerning the determination of the content of the applicable law; and (iii) the actual application of the applicable law).

existence of property rights and interests.[5] Thirdly, Chapter 4 will then consider the method(s) of ascertaining the contents of the host state law.

[5] As was seen in Chapter 1, there is a further jurisdictional requirement in certain investment treaties that requires an investor to acquire an investment approval from the official authorities of the host state as a precondition to establishing its investment. Obviously, and as is stated in many of the relatively few investment treaties that contain this condition, the process of the application for and granting of the investment approval should be carried out in accordance with host state law. Therefore, once again, laws of the host state are determinative in ascertaining subject-matter jurisdiction for investment treaty tribunals. However, this precondition will not be discussed in the following Chapters as the condition is neither a general principle of law nor so widespread in investment treaties. Consequently, bar a few cases, it has not surfaced in investment arbitration cases, and as such, does not warrant a separate discussion here.

## Chapter 2: Application of Domestic Law to the Legality Requirement

1. As framed, in this Chapter, I will deal with two questions regarding the application of the host state law to the legality requirement. In Section One, I will examine the legal bases for referring to the laws of the host state in determining issues concerning the legality requirement. In Section Two, I will consider the actual application of domestic law to particular questions regarding the legality requirement.

### Section One: The Legal Bases for Referring to the Laws of the Host State

2. When faced with an 'illegality' defence by the respondent state, the first question that should be answered by an arbitral tribunal seized of an investment treaty dispute is the basis and the legal footing for application of the laws of the host state in an international arbitration proceeding. Put differently, an international tribunal applying and interpreting an international investment treaty in an international dispute naturally expects to apply international law to the issues before it,[1] including to the matters regarding jurisdiction, unless there is a plausible reason, like a *renvoi*, which validates reference to and application of another body of law.[2]
3. To be sure, many investment treaties contain provisions expressly referring to the requirement that an investment should be made in accordance with the laws and regulations of the host state.[3] Other treaties do not have such express references, but nevertheless, contain provisions which implicitly require compliance with the laws of the host state at the time of establishing the investment.[4] However, there are treaties which do not contain even an implicit reference to

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[1] Generally speaking, an investment treaty is a 'treaty' within the meaning of Article 2(1)(a) of the of the Vienna Convention on the Law of Treaties ("VCLT") (adopted and opened for signature on 23 May 1969, entered into force on 27 January 1980) and is, in principle, and as per the above-mentioned provision as well as Article 31(3)(c) of the VCLT, governed and interpreted by rules of international law.

[2] *Fraport v. Republic of Philippines*, ICSID Case No. ARB/03/25, Award, 16 August 2007 [335], [394]; *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia*, ICSID Case No. ARB/06/2, Decision on Jurisdiction, 27 September 2012 [47]-[52]; *Metal-Tech Ltd. v. Republic of Uzbekistan*, ICSID Case No. ARB/10/3, Award, 04 October 2013 [121]; *Churchill Mining PLC v. Republic of Indonesia*, ICSID Case No. ARB/12/14 & *Planet Mining Pty Ltd v. Republic of Indonesia*, ICSID Case No. ARB12/40, Decisions on Jurisdiction for both Cases, 24 February 2014, both at [86]; M Sasson, *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer Law International 2017) 1-3; C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (2014) 1(1) McGill Journal of Dispute Resolution 2-3.

[3] E.g., Article 1(1) of the Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 18 April 1997, entered into force on 01 February 2000. As indicated in the previous Chapter, a comprehensive survey that I did on 60 of the bilateral investment treaties signed by Iran shows that a great majority of these treaties (more than 90%) contain express legality requirements. Furthermore, the rest of the Iranian BITs under consideration entail implicit references to the legality requirement. As such, there is no BIT, amongst the 60 agreements I could access, that does not contain an express or at least an implied reference to the legality requirement. Furthermore, another research that I did shows that all the bilateral investment treaties concluded by Australia, without one single exception, have express and/or implied legality requirements.

[4] An example is the BIT between Armenia and the United Kingdom. This BIT does not contain an express 'legality requirement'. It nevertheless provides in Article 2(1):

> Each Contracting Party shall encourage and create favourable conditions for nationals or companies of the other Contracting Party to invest capital in its territory, and, subject to its right to exercise powers conferred by its laws, shall admit such capital.

the requirement of compliance with the laws of the host state at the time of making an investment.[5] It is submitted that even if no such explicit or implicit reference is made to laws of the host state in the provisions of the relevant investment treaty, it could still be said that, under general principles of law, in order for the investor's case to proceed to the merits, the investment should have been made lawfully, in the sense that it should have been observant of the laws of the host state at the time of its establishment. Therefore, there are two main footings for reference to the laws of the host state to ascertain the legality of an investment at the time of its establishment: (i) reference by the contracting parties to the treaty to the laws of the host state, either explicitly or implicitly; and (ii) general principles of law which require that only lawful investments are eligible for being protected by investment treaties.

4. Both express reference to the laws of the host state and reference to such laws by implication will be scrutinised under the ensuing subsection **(A)**. The discussion will then be followed by an analysis of treaties which contain no reference at all to the requirement that the investment should be observant of the laws of host state at the time of its establishment **(B)**. This subsection would seek to pinpoint the role general principles of law play in requiring an investor to establish its investment in accordance with the laws of the host state. A final subsection will consider the possible role of international law rules in the determination of matters concerning the legality requirement **(C)**.

### A. Reference by the Contracting Parties in the Underlying Investment Treaty

5. As was alluded to above, most investment treaties provide that an investment should be made in accordance with the laws of the host state. This requirement clearly emanates from the concern of recipient states to safeguard the application of their laws and regulations while attracting foreign investment. Indeed, it has been argued that one of the disadvantages of foreign investment, particularly for developing countries, is the violation of the laws and fundamental legal principles of host states through corruptive or fraudulent practices of foreign investors, which in certain cases does more harm than the good of attracting foreign investment.[6] In fact, in cases where the investment has been made in violation of the laws of the host state, for instance, by forging or manipulating bidding documents, it is arguable that the public at large incurs a loss, and that loss is the difference between having a really competent investor with high qualifications and an investor with lower qualifications who has been ignorant of the laws of the state. In other words, in such a situation, the state, representing the public, is led to believe, through the bidding documents, that, for example, the investor has strategic partners assuring stable and high-quality supplies, that it owns or controls cutting-edge technology, and that it has ample financial resources. Had it been informed properly of the real and actual legal, financial, and technical qualifications of the investor, the state would, in a proper competitive bidding process, have awarded the bid to another bidder, which could

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The Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Armenia for the Promotion and Protection of Investments, signed on 27 May 1993, entered into force on 11 July 1996.

[5] The Energy Charter Treaty ("ECT") is an example in this respect. See the ECT, signed on 17 December 1994, entered into force on 16 April 1998.

[6] JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (OUP 2013) 19-21 (discussing the risks and costs of foreign investment for host states).

have had better actual capabilities and proficiency.[7] Put differently, the loss suffered by the public in this simple example is the benefits that they have been deprived of had they had a better service provider.[8]

6. Therefore, states keep including such requirements in their investment treaties to address their concern for the due observance of their laws by investors at the time of making their investments. In this respect, the tribunal in *Alasdair Ross Anderson v Republic of Costa Rica* specified that the incorporation of such a condition in the investment treaty between Canada and Costa Rica (the underlying treaty in that dispute which has a legality requirement in Article 1(g)) was a "clear indication of the importance that [the Contracting Parties] attached to the legality of investments made by investors of the other Party and their intention that their laws with respect to investments be strictly followed." It also added that "[t]he assurance of legality with respect to investment has important, indeed crucial, consequences for the public welfare and economic well-being of any country"[9] and that every country "has a fundamental interest in securing respect for its law."[10] Another obvious reason for the inclusion of the legality

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[7] The factual background of the *Inceysa* case is quite similar to the example given above. In that case, the tribunal found that in the bidding documents submitted by Inceysa, the investor did not disclose its real financial condition and that it provided false information regarding the identity and the experience of a strategic partner and its own experience. The tribunal considered these as 'fundamental elements' for adjudicating a bid, as to which the investor had presented untrue information and faulty documents. *Inceysa Vallisoletana S.L. v. Republic of El Salvador*, ICSID Case No. ARB/03/26, Award, 02 August 2006 [104], [111]-[118]. According to Carlevaris, "[t]he first arbitration in which an arbitral tribunal devoted a specific and in-depth analysis to the effects of an "in accordance with host State law clause" was *Inceysa*. This case is also the first one in which an ICSID tribunal decided that it lacked jurisdiction on the basis of such a clause." A Carlevaris, 'The Conformity of Investments with the Law of the Host State and the Jurisdiction of International Tribunals' (2008) 9(1) The Journal of World Investment & Trade 40. See also C Knahr, 'Investments "in accordance with the host state law"' (2007) 4(5) TDM 1.

[8] One eminent commentator on corruption in international investment arbitration has articulated the loss suffered by the public at large in a corruptive investment transaction very colourfully: "These hidden handshakes are all the more troubling when one considers that they usually occur within hotels quite literally walled away from the teeming poverty nearby, a visual contrast so evocative of what corruption yields throughout the developing world. For while those within the walls prosper, it is the poor that ultimately bear most of the corrosive effects of transnational corruption." He further brings up a delicate and rational point which is indicative of the loss effectively suffered by the public by stating that: "... payers of bribes will do one of two things to recoup this additional cost: either build the bribe into the price, or provide shortcuts to the quality of the project or product delivered. In either case, the immediate participants in corruption are enriched at the ultimate expense of the public." AP Llamzon, *Corruption in International Investment Arbitration* (OUP 2014) 2, 4. Referring to Rose-Ackerman's "Corruption and Governance", Llmazon further notes that: "… for the larger populace, investments and commercial transactions that are entered into with the aid of corruption are clearly inefficient once one looks at the distortive effect corruption has upon government's resources use prioritizations – whenever officials can influence the quantity and quality of services provided and the identity of beneficiaries, corruption will almost certainly lead to inefficiency." ibid 25-26. Rose-Ackerman, on whose two treatises Llamzon extensively relies in his book, states in this respect: "[t]he impact of high-level corruption goes beyond the mere scale of public investment and lost revenue for the public budget. Top officials select projects and make purchases with little or no economic rationale. For example, if kickbacks are easier to obtain on capital investments and input purchases than on labour, rulers will favour capital intensive projects irrespective of their economic justification [...] Corrupt rulers favour capital intensive projects over other types of public expenditures and will favour public investment over private investment. They will frequently support 'white elephant' projects with little value in promoting economic development." S Rose-Ackerman, 'The Challenge of Poor Governance and Corruption, in Global Crisis, Global Solutions' in B Lombord (ed), *Global Crises, Global Solutions: Costs and Benefits* (CUP 2004) 23.

[9] *Alasdair Ross Anderson et al. v. Republic of Costa Rica,* ICSID Case No. ARB (AF)/07/3, Award, 19 May 2010 [53].

[10] ibid [58].

requirement in investment treaties is recalling the power of the host state to control the entry of foreign investment to its country. In this connection, the tribunal in *Kardassopoulos v. Georgia* noted the obvious point that states retain the power to control investments made in their territory, which would allow them to exclude from protection activities not in accordance with their own legislation.[11]

7. Having queried the reasons for the inclusion of the legality requirement in investment treaties, in the following pages, I will examine the modality by which states have sought to include legality requirements in their investment treaties.

### a. Express Reference

8. As stated above, many international investment agreements contain express references to the requirement that an investor should comply with the laws and regulations of the host state at the time of making the investment. For instance, Article 1(1) of the BIT between Iran and Japan provides that:

> The term "investment" refers to every kind of asset, invested directly or indirectly by an investor of a Contracting Party in the Territory of the other Contracting Party in accordance with the laws and regulations of the other Contracting Party …[12]

9. As was mentioned in Chapter 1, in such circumstances, the BIT contains a *renvoi* to host state domestic law. Consequently, it is this body of law that governs the legality requirement. Thus, in *Metal-Tech v. Uzbekistan*, the tribunal noted that its jurisdiction "[…] is governed by the ICSID Convention and by the BIT. Where these treaties are silent on an issue that is relevant to determine jurisdiction, e.g. the manner in which consent is given, such issue is subject to customary international law unless the treaties refer to municipal law. This is in particular so when an investment treaty requires that an investment be made in accordance with host State law."[13]

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[11] *Ioannis Kardassopoulos v. The Republic of Georgia*, ICSID Case No. ARB/05/18, Decision on Jurisdiction, 06 July 2007 [182] (referring to M Sornarajah, *The International Law on Foreign Investments* (2nd edn, CUP 2004) 106: "no State has taken its fervour for foreign investments to the extent of removing any controls on the flow of foreign investments into the host State.") In this respect, a work done by UNCTAD focuses on the issue from a competition point of view. It says that: "Conditioning the coverage of an asset on compliance with local laws has several purposes. It confirms that both foreign and domestic investors have to observe the laws of the land, thereby establishing a "level playing field"..." UNCTAD, *Bilateral Investment Treaties 1995–2006: Trends in Investment Rulemaking* (United Nations 2007) 9. Another commentary by UNCTAD also focuses on this competition aspect of the legality requirement. It also adds that this provision seeks to ensure that the investment activities of the investor are in line with development policies of the host state: "[The legality requirement has the] effect of ensuring that both foreign and domestic investors are required to observe the laws of the land, thereby ensuring a "level playing field". Moreover, on the assumption that the host country's investment laws will be written and applied to further its development policy, this limitation also is intended to ensure that investment is covered only if it is consistent with the host country's development policy, and other policies, such as immigration or internal security, that impact on investment ..." See UNCTAD, *Scope and Definitions* (United Nations 2011) 38.

[12] Agreement between Japan and the Islamic Republic of Iran on Reciprocal Promotion and Protection of Investment, signed on 05 February 2016, entered into force on 26 April 2017.

[13] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [121]. This case was the first investment treaty case which was dismissed on grounds of corruption. It is to be noted that before *Metal-Tech*, the *World Duty Free* tribunal accepted the allegations of corruption put forward by Kenya and dismissed the claimant's case. That case, however, was brought pursuant to an arbitration clause in a contract, not an investment treaty. See CB Lamm, BK Greenwald & KM Young,

10. Having noted this, it should be added that there is no unified or harmonised practice regarding the location of this requirement in investment treaties nor is there any unique standard wording which formulates this condition. In other words, such requirement appears in various parts of different investment treaties with not necessarily identical language. The question then is how and where this requirement is expressed in different investment treaties, and how the location or the wording of the requirement would affect the interpretive assignment of the adjudicating forum if any? The following pages will address these questions.

### i. Varying Formulations and Its Impact

11. There are several different forms in which a legality requirement appears in investment treaties. For example, Article 1(g) of the BIT between Canada and Costa Rica, the underlying BIT in *Alasdair Ross Anderson et al v. Republic of Costa Rica*,[14] provides in Article 1(g) that:

> "investment" means any kind of asset owned or controlled either directly, or indirectly through an enterprise or natural person of a third State, by an investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's laws.[15]

As was mentioned above, Article 1(1) of the BIT between Germany and Philippines, the underlying Agreement in Fraport v. Philippines,[16] also refers to the legality requirement, however, using a different formulation:

> the term "investment" shall mean any kind of asset accepted in accordance with the respective laws and regulations of either Contracting State …[17]

12. It is submitted that as long as the concept and the message conveyed is the same, different wordings and formulations in the legality requirement usually do not matter in generally interpreting the clause. To be sure, this is not to argue that one should turn a blind eye on the ordinary meaning of the terms of the treaty, which is an express tool of treaty interpretation under Article 31 of the VCLT. Rather, what is being proposed here is to avoid engaging in a purely textual analysis which totally ignores the core intention of the contracting parties and the object and purpose of an investment treaty. In this regard, one commentator has noted that investment treaty arbitration tribunals have treated and interpreted legality clauses with different formulations in a similar fashion. Although he states in the first place, and quite correctly so, that "[t]he wording of clauses referring to host State law in the various treaties can [..] differ to a significant extent, and important interpretative consequences might flow

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'From World Duty Free to Metal-Tech: A Review of International Investment Treaty Arbitration Cases Involving Allegations of Corruption' (2014) 29(2) ICSID Rev-FILJ 328, 329.

[14] See *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9).

[15] See Agreement between the Government of Canada and the Government of the Republic of Costa Rica for the Promotion and Protection of Investments, signed on 18 March 1998, entered into force on 29 September 1999.

[16] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2). According to Knahr, *Fraport* was the second case – after *Inceysa* – to deal with an 'in accordance with host state law' requirement in detail and to deny jurisdiction due to a violation of domestic law by the investor. See C Knahr (n 7) 11.

[17] See Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments (n 3).

from this difference …" he goes on to note that: "these clauses presently appear to be interpreted uniformly in the arbitral practice irrespective of their context and wording."[18]

13. To give an example of such 'arbitral practice' offering a similar interpretation of clauses bearing the legality requirement with different wordings, one can refer to the award in *Fraport v. Philippines*.[19] In this case, the tribunal was faced with several provisions of Germany-Philippines BIT that contained references to the law of the host state: Article 1(1) of that BIT providing that for the purpose of this Agreement "[t]he term 'investment' shall mean any kind of asset accepted in accordance with the respective laws and regulations of either Contracting State [...]", Article 2(1) providing that: "Each Contracting State shall promote as far as possible investments in its territory by investors of the other Contracting State and admit such investments in accordance with its Constitution, laws and regulations as referred to Article 1, paragraph 1. [...]", and the Protocol to the Agreement, which was concluded on the same day as the BIT, stating at ad Article 2: "As provided for in the Constitution of the Republic of the Philippines, foreign investors are not allowed to own land in the territory of the Republic of the Philippines. However investors are allowed to own up to 40% of the equity of a company which can then acquire ownership of land." The tribunal recognised that there are some linguistic differences between these provisions, but went to consider that this linguistic difference did not appear to indicate an intentional nuance and hence to be legally significant.[20]

14. In short, unless the wording of a legality clause entails express limitations and/or qualifications, an investment treaty tribunal should adhere to the intention of the state contracting parties as reflected in a legality requirement and dismiss cases based on investments made in violation of the laws of the recipient state.

### ii. Varying Locations and Its Impact

15. A simple and quick review of different investment treaties shows that the legality requirement appears in various provisions of different investment treaties. Most frequently, this requirement is noticed in 'definitions' clauses.[21] In addition to that, the legality requirement is also observed in the 'scope of application' clauses as well as certain provisions regarding the substantive protection of investment. Below, I will review some of the most recurring locations in which the legality requirement materialises in investment treaties.

#### 1st. *In 'Definitions' Clauses*

16. A majority of investment treaties containing the legality requirement place this condition in the 'definitions' clause of the investment treaty. For example, paragraph (g) of the 'Definition' Article of the BIT between Canada and Costa Rica, which was the underlying BIT in *Alasdair Ross Anderson et al v. Republic of Costa Rica*,[22] reads:

> "investment" means any kind of asset owned or controlled either directly, or indirectly through an enterprise or natural person of a third State, by an

[18] A Carlevaris (n 7) 37. See also ibid 48.

[19] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2).

[20] ibid [334]-[342].

[21] See C Knahr (n 7) 1.

[22] *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9).

> investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's laws …[23]

17. In addition to this crystal-clear reference to the legality qualification in a 'definition' article, some investment agreements also stipulate that any change in the form of an investment would be covered by the agreement, provided that it is made in accordance with the laws and regulations of the host state. For instance, Article 1(a) of the BIT between Ghana and Guinea reads in the relevant part as follows:

> A change in the form in which assets are invested does not affect their character as investments, provided such change is not contrary to the laws of the Contracting Party in whose territory the investment has been made.[24]

2nd. *In 'Scope of Application' Clauses*

18. There are a smaller number of treaties which contain a legality requirement in the treaty's 'scope of application' provision. Article 11 of the BIT between Austria and the Philippines on 'Application of the Agreement' epitomises treaties in which the legality requirement appears in 'scope of application' clauses:

> This Agreement shall apply to investments made in the territory of one of the Contracting Parties in accordance with its legislation by investors of the other Contracting Party prior to as well as after the entry into force of this Agreement.[25]

19. Another sample of this group is the famous BIT between Spain and El Salvador which was the basis for the case *Inceysa Vallisoletana, SL v Republic of El Salvador*.[26] The clause in the Spain–El Salvador BIT defining 'investments' did not limit eligible investments to those made 'in accordance with law', but two other clauses in the BIT referred to the need for investments to have been made in accordance with the law of the host state. One such clause was Article 2(2) of that treaty concerning the scope of application of the treaty according to which the Agreement:

> "[…] will also apply to investments made before its entry into force by the investors of a Contracting Party in accordance with the laws of the other Contracting Party in the territory of the latter [ ... ]"[27]

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[23] Agreement between the Government of Canada and the Government of the Republic of Costa Rica for the Promotion and Protection of Investments (n 15).

[24] Article 1 of the Agreement between the Government of the Republic of Ghana and The Government the Republic of Guinea for the Promotion and Protection of Investments, signed on 18 May 2001, not yet entered into force.

[25] Article 11 of the Agreement between the Republic of Austria and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 11 April 2002, entered into force on 01 December 2003. See also Article 2 of the Agreement between the Government of the Kingdom of Thailand and The Government of the Republic of India for the Promotion and Protection of Investments, signed on 10 July 2000, entered into force on 13 July 2001.

[26] *Inceysa Vallisoletana, SL v Republic of El Salvador* (n 7).

[27] Agreement for the Reciprocal Promotion and Protection of Investments signed between the Republic of EI Salvador and the Kingdom of Spain, signed on 14 February 1995, entered into force on 20 February 1996. In this regard, see *Inceysa Vallisoletana, SL v Republic of El Salvador* (n 7) [196], [206].

3rd. *In Substantive Protection Clauses*

20. Some treaties refer to the legality requirement in substantive protection clauses of the investment treaty. For example, the BIT between Iran and the Bosnia and Herzegovina places the legality requirement in a provision which addresses protection of investments. Article 4(1) of that treaty says:

> Admitted Investments of investors of one Contracting Party effected within the territory of the other Contracting Party in accordance with the laws and regulations of the latter, shall receive in the other Contracting Party full legal protection and fair treatment not less favourable than that accorded to its own investors or to investors of any third state which are in a comparable situation.[28]

21. Another prominent sample, which was also mentioned above, is the BIT between Spain and El-Salvador, the underlying BIT in *Inceysa v. El Salvador*,[29] which contains another reference to the legality requirement in Article 3(1) concerning the protection of investments and abstention from adopting arbitrary and discriminatory measures. This Article provides in the relevant part: "Each Contracting Party shall protect in its territory the investments made, in accordance with its legislations ..."[30]

22. As was seen, the legality requirement emerges in several locations and various provisions of different investment treaties. Despite this fact, the analysis conducted by some of the above-mentioned adjudicatory bodies in the said investment treaty cases shows that the location of the requirement does not influence its interpretation, and this is so as long as the substance of the clause is largely the same. In this connection, the *Inceysa* tribunal correctly noted that:

> [T]he Claimant is not right to indicate that in order to determine whether its investment falls within the scope of the Agreement, it is necessary to examine only the definition of the term investment, contained in Article 1(2) of the Agreement, where there is no reference to the clause "in accordance with law," and that it is not possible to examine other clauses of the Agreement to determine the type of investments protected by it ... Indeed, if the Contracting States themselves agree that the limitation "in accordance with laws" could be included (as it actually was) in parts of the BIT other than the definition of investment, such as that referring to promotion and admission, it is obvious that the restrictive interpretation sustained by Inceysa is incorrect …[31]

23. This ruling simply means that whether the legality requirement materialises in the 'definitions' clause or elsewhere in the investment treaty, the legal consequences of the requirement remain the same.

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[28] Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Islamic Republic of Iran and the Government of Bosnia and Herzegovina, signed on 27 July 1996, entered into force on 02 June 2009.

[29] *Inceysa Vallisoletana, SL v Republic of El Salvador* (n 7).

[30] Agreement for the Reciprocal Promotion and Protection of Investments signed between the Republic of EI Salvador and the Kingdom of Spain (n 27).

[31] *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 7) [197]-[198].

### b. Implicit Reference

24. There are many investment treaties that do not expressly refer to the requirement of legality for an investment at the time of its establishment in the 'definitions' or 'scope of application' clauses. Instead, in the pertinent provision regarding 'admission, establishment, and promotion of investments', some treaties include a requirement that the state should admit and promote investments in accordance with its laws and regulations. An example is Article 2 of the BIT between the Netherlands and Cambodia which reads:

> Either Contracting Party shall, within the framework of its laws and regulations, promote economic cooperation through the protection in its territory of investments of nationals of the other Contracting Party. Subject to its right to exercise powers conferred by its laws or regulations, each Contracting Party shall admit such investments.[32]

25. Although provisions of this kind do not expressly circumscribe the scope of application of an investment treaty to investments made legally, however, by providing that promotion, protection, and admittance of investments must be made in accordance with the laws of the host state, by necessary implication, they mean that an investment must be made legally in order to be admitted and protected. In fact, it is inconceivable that the host state would admit, in accordance with its laws, an investment made in violation of the laws of the same state. It is axiomatic that the inclusion of the legality requirement in the admission clause does not limit the observance of legality merely to the admission of investments. It goes beyond that and spreads over the establishment. An admission that should be observant of host state laws presupposes a legally established investment.

26. The viewpoint expressed by Dolzer and Stevens with regard to admission clauses in bilateral investment treaties is that they "record the parties' undertaking to 'promote' investments under the treaty ... as long as they are made in accordance with the host country's legislation."[33] A similar understanding is shared by the tribunal in *Saluka v. Czech Republic*.[34] The underlying Netherlands-Czech Republic BIT contained in its Article 2 the requirement that "each Contracting Party…shall admit such investments in accordance with its provisions of law".[35] The tribunal took note of this provision and stated that:

> [I]t is necessarily implicit in Article 2 of the Treaty that an investment must have been made in accordance with the provisions of the host State's laws.[36]

Further, the tribunal concluded from this provision that:

> [T]he obligation upon the host State to admit an investment by a foreign investor (i.e. in the present context, to allow the purchase of shares in a

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[32] Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of Cambodia and the Kingdom of the Netherlands, signed on 23 June 2003, entered into force on 01 March 2006.

[33] R Dolzer & M Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff Publishers 1995) 51.

[34] *Saluka Investments B.V. v. The Czech Republic*, UNCITRAL.

[35] Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 1991, entered into force on 01 October 1992.

[36] *Saluka Investments B.V. v. The Czech Republic*, UNCITRAL, Partial Award, 17 March 2006 [204].

local company) only arises if the purchase is made in compliance with its laws.[37]

27. Therefore, in cases of implicit reference to the legality requirement too, an investment treaty tribunal should observe the agreement of the parties and dismiss cases based on investments made in violation of the laws and regulations of the host state.

### B. The Nature of the Legal Issue

28. There are investment treaties in which no legality requirement appears neither explicitly nor even by implicit terms. It is arguable that the legality requirement also applies to such treaties. In fact, as a general principle, it is the presumed intention of the contracting parties to an investment treaty that only investments made legally and in accordance with the laws of the host state would be protected by the treaty, and that investments made in violation of the laws and regulations of the recipient state would be denied protection. This understanding has been largely endorsed by several arbitral tribunals deciding investment treaty cases.

29. Firstly, in *Plama v. Bulgaria*, the tribunal, deciding a case under the ECT which does not contain a legality requirement, noted that: "Unlike a number of Bilateral Investment Treaties, the ECT does not contain a provision requiring the conformity of the Investment with a particular law. This does not mean, however, that the protections provided for by the ECT cover all kinds of investments, including those contrary to domestic or international law […] The Arbitral Tribunal concludes that the substantive protections of the ECT cannot apply to investments that are made contrary to law."[38]

30. In the same vein, the *Phoenix* tribunal observed that: "[…] States cannot be deemed to offer access to the ICSID dispute settlement mechanism to investments made in violation of their laws… These are illegal investments according to the national law of the host State and cannot be protected through an ICSID arbitral process. And it is the Tribunal's view that this condition – the conformity of the establishment of the investment with the national laws – is implicit even when not expressly stated in the relevant BIT…"[39] The tribunal further added that: "The purpose of the international mechanism of protection of investment through ICSID arbitration cannot be to protect investments made in violation of the laws of the host State or investments not made in good faith, obtained for example through misrepresentations, concealments or corruption, or amounting to an abuse of the international ICSID arbitration system. In other words, the purpose of international protection is to protect legal and *bona fide* investments."[40] (Citations omitted)

31. The tribunal in *Hamester v. Ghana* subscribed to the observations of the *Phoenix* tribunal with regard to the requirement of legality: "An investment will not be protected if it has been created in violation of national or international principles of good faith; by way of corruption, fraud, or deceitful conduct; or if its creation itself constitutes a misuse of the system of international investment protection under the ICSID Convention. It will also not be protected if it is made

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[37] ibid.

[38] *Plama Consortium Limited v. Bulgaria*, ICSID Case No. ARB/03/24, Award, 27 August 2008 [138]-[139].

[39] *Phoenix Action, Ltd. v. The Czech Republic*, ICSID Case No. ARB/06/5, Award, 15 April 2009 [101].

[40] ibid [100].

in violation of the host State's law (as elaborated, eg by the tribunal in *Phoenix*)."[41] The tribunal further emphasised that "[t]hese are general principles that exist independently of specific language to this effect in the Treaty."[42]

32. By the same token, in *SAUR International SA v. Republic of Argentina*, the tribunal noted that the requirement of not having committed a violation of the legal regime of the recipient state is a tacit condition inherent in every BIT. The tribunal reasoned that it cannot be understood under any circumstances that a state is offering the benefit of protection through investment arbitration when the investor, to obtain that protection, has committed an unlawful action.[43]

33. In short, as the practice of investment treaty tribunals plainly shows, investments made in violations of the laws of the host state will not be protected, irrespective of whether the underlying treaty contains a legality requirement or not. To be sure, "[r]espect for the integrity of the law of the host state is […] a critical part of development and a concern of international investment law."[44] As observed by the *Hamester* tribunal, the fact that illegal investments should not be protected by international investment law is a "general principle […] that exist[s] independently of the specific language to this effect in the Treaty."[45]

34. Having said that, one should bear in mind that when the terms of the treaty lack any explicit or tacit reference to the legality requirement, although, if made illegally, the investment would not be granted protection, however, as will be discussed later in this Chapter, in such a scenario, the denial of protection should be cloaked under a different guise than it would be under the explicit and implicit legality requirement scenarios. In fact, depending on the specific wording of the treaty in question, lack of legality, as required by the treaty containing an express or implied legality requirement, nullifies consent of the state, and therefore, the jurisdiction of the

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[41] *Gustav F W Hamester GmbH & Co KG v Republic of Ghana*, ICSID Case No ARB/07/24, Award, 18 June 2010 [123].

[42] ibid [124].

[43] *SAUR International SA v Republic of Argentina*, ICSID Case No ARB/04/4, Decision on Jurisdiction and Liability, 06 June 2012 [308] (further observing that the purpose of the investment arbitration system is to protect only lawful and *bona fide* investments and that the absence of an express legality requirement in a particular BIT is not a relevant factor). See also *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania*, ICSID Case No. ARB/11/24, Award, 30 March 2015 [494] (observing that "a State cannot be expected to have consented to an arbitral dispute settlement mechanism for investments made in violation of its legislation.") Cf *Bear Creek Mining Corporation v. Republic of Peru*, ICSID Case No. ARB/14/21, Award, 30 November 2017 [319]-[324] (noting, *inter alia*, that "the Tribunal may not import a requirement that limits its jurisdiction when such a limit is not specified by the parties.") However, it should be borne in mind that in this case, Article 816 of the Canada-Peru FTA was of particular relevance in the Tribunal's determination. This provision identifies the legality requirement as a 'special formality' that the host state is entitled to adopt if it so wishes. Thus, the tribunal concluded that: "Since nowhere in the FTA or otherwise in the record is there an express or implied provision of law to the effect that Peru made use of this option, it can only be concluded that there is no jurisdictional requirement that Claimant's investment was legally constituted under the laws of Peru." See ibid [319]. The tribunal also mentioned that: "The above conclusion does not exclude the possible relevance of illegality or lack of good faith with respect to the merits." See ibid [324].

[44] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [402].

[45] *Gustav F W Hamester GmbH & Co KG v Republic of Ghana* (n 41) [124]. See also R Moloo, 'A Comment on the Clean Hands Doctrine in International Law' (2011) 8(1) TDM.

tribunal. On the other hand, illegality in the absence of a specific requirement of legality in the treaty at issue culminates in 'unclean hands', which is a requirement of admissibility.[46]

35. In conclusion, as will be further explained later in this Chapter, for dismissing jurisdiction or admissibility,[47] as the case may be, it is sufficient for a tribunal to find non-compliance with the laws of the host state. That is so irrespective of whether the condition of legality is expressly or impliedly referred to by the underlying investment treaty or there is no such requirement in the investment treaty at all.

36. With these observations in mind, there is still an additional separate point that should be covered at this juncture and that is the reliance of certain investment treaty arbitration tribunals on the principles of international law alone or in combination with the laws of the host state in analysing whether a given investment is legal or not. In fact, the question is whether it is necessary and/or useful to rely on the rules of international law to examine the legality of the investment. This topic is addressed below.

### C. Relying on Principles of International Law for Dismissing Illegal Investments

37. It has been observed that in several investment treaty awards and decisions, arbitral tribunals reject the legality of the alleged investment in question by substantial recourse to some principles of international law, chief among them being the principles of good faith and international public policy. In fact, sometimes quite unnecessarily, and just for the sake of making the decision seem more cogent and in order to highlight their reasoning regarding the effect of illegality on the jurisdiction of the tribunal or the admissibility of the claim, some arbitral tribunals do not suffice themselves to an analysis of the laws of the host state, and go on to rely also on principles of international law to dismiss the case. For instance, having determined that Metal-Tech had made a series of corrupt payments to facilitate the establishment of its investment, the tribunal in *Metal-Tech v. Uzbekistan* found that those payments were made in violation of Uzbek law, whose "condemnation of corruption" was also "in conformity with international law and the laws of the vast majority of States".[48] Given what was said above about the requirement of legality of investments in accordance with the laws of the host state, even in treaties which do not include an express or implied legality requirement, the question here is: to what extent an extra reference to principles or doctrines

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[46] In this regard, see R Moloo (n 45). In the context of state responsibility, the ILC Special Rapporteur, James Crawford, explained that: "The so-called 'clean hands' Doctrine has been invoked principally in the context of the admissibility of claims before international courts and tribunals, though rarely applied". J Crawford, *The International Law Commission's Articles on State Responsibility: Introduction, Text and Commentaries* (CUP 2002) 162.

[47] On the distinction between jurisdiction and admissibility, see *Certain Questions of Mutual Assistance in Criminal Matters* (*Djibouti v. France*), Judgment, I.C.J. Rep. 2008 (04 June 2008) p 177, pp 200-201 [48] (indicating that "in determining the scope of the consent expressed by one of the parties, the Court pronounces on its jurisdiction, not on the admissibility of the application."); *Hochtief AG v. The Argentine Republic*, ICSID Case No. ARB/07/31, Decision on Jurisdiction, 24 October 2011 [90] (stating that: "Jurisdiction is an attribute of a tribunal and not of a claim, whereas admissibility is an attribute of a claim but not of a tribunal.") As eloquently put by one commentator, "while jurisdiction is about the scope of the State's consent to arbitrate, admissibility is about whether the claim, as presented, can or should be resolved by an international tribunal, which otherwise has found jurisdiction." See V Heiskanen, '*Menage a` trois*? Jurisdiction, Admissibility and Competence in Investment Treaty Arbitration' (2013) 29(1) ICSID Rev-FILJ 237.

[48] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [290].

of international law is necessary for investment treaty tribunals to deny jurisdiction for illegal investments or to declare claims based on such alleged investments inadmissible?

38. As a point of departure, it is appropriate to begin by considering briefly the relevant rules and principles of international law concerning investments made through abusive processes and bad faith and the rules and principles of international law against corruption. As was stated above, it happens that investments are obtained through fraudulent behaviour, misrepresentations, fabrication of documents, falsifying the facts, concealments, bribery or, more generally, through corruption, or are made in a way that amounts to an abuse of the international investment protection system. In this respect, the *obiter dictum* in *Phoenix v. Czech Republic* is instructive and reflects the position of international law in proscribing the protection of corrupt and abusive investments:

> 100. The purpose of the international mechanism of protection of investment through ICSID arbitration cannot be to protect investments made in violation of the laws of the host State or investments not made in good faith, obtained for example through misrepresentations, concealments or corruption, or amounting to an abuse of the international ICSID arbitration system. In other words, the purpose of international protection is to protect legal and *bona fide* investments.
>
> […]
>
> 106. In the Tribunal's view, States cannot be deemed to offer access to the ICSID dispute settlement mechanism to investments not made in good faith. The protection of international investment arbitration cannot be granted if such protection would run contrary to the general principles of international law, among which the principle of good faith is of utmost importance.[49]

39. In fact, there is substantial investment treaty jurisprudence suggesting that the protection of international investment arbitration cannot be granted if according such protection would run contrary to the principles of good faith and international public policy.[50] As has been put forward by Hersch Lauterpacht: "There is no right, however well established, which could not, in some circumstances, be refused recognition on the ground that it has been abused."[51] This understanding is reinforced when one refers to Article 31(1) of the VCLT which requires that treaties should be interpreted in good faith. Article 31(3)(c) of the same Convention also requires an adjudicating forum to take into account, together with the context, "any relevant rules of international law applicable in the relations between the parties." Good faith and international public policy could always be among such principles.

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[49] *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [100], [106].

[50] See, for instance, *Inceysa Vallisoletana, S.L. v. Republic of El Salvador* (n 7) [230]-[231]; *Plama Consortium Limited v. Bulgaria* (n 38) 2008 [143]-[144]; *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [106 *et seq*]; *Liman Caspian Oil BV and NCL Dutch Investment BV v. Republic of Kazakhstan*, ICSID Case No. ARB/07/14, Award (Excerpts), 22 June 2010 [194]. For a review of ICC Awards with respect to illegality, bribery, and corruption and the effects of such wrongdoing on jurisdiction, admissibility, and merits of contractual claims, see *World Duty Free Company v. Republic of Kenya*, ICSID Case No. ARB/00/7, Award, 04 October 2006 [148]-[155].

[51] H Lauterpacht, *Development of International Law by the International Court* (Stevens & Sons Limited 1958) 164.

40. In this respect, one also has to note that apart from myriads of national legislations and awards rendered by domestic courts as well as international courts and tribunals, there are several international instruments forbidding and combatting transnational corruption and bribery. Among such instruments are the following: The Inter-American Convention against Corruption of 1996,[52] Declaration of the General Assembly of the United Nations adopted on 16 December 1996 against Corruption and Bribery in International Commercial Transactions,[53] the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions of 21 November 1997,[54] two EU conventions on corruption—one relating to criminal law and one dealing with civil law— which were adopted by the Council of Europe on 27 January 1999[55] and 04 November 1999 respectively,[56] a Convention on Preventing and Combating Corruption approved by the Heads of States and Governments of the African Union on 11 July 2003,[57] and, lastly, and perhaps most importantly, the UN Convention on Corruption, approved by the General Assembly on 31 October 2003 (Resolution 58/4), which was opened for signature in Mérida, Yucatán, Mexico, from 9–11 December 2003 and thereafter at UN headquarters in New York City, and which was signed by 140 countries. As of August 2018, there are 186 parties to this Convention which include 181 UN member states, the Cook Islands, Niue, the Holy See, the State of Palestine, and the European Union. This latter Convention entered into force on 14 December 2005.[58] [59]

41. Having briefly reviewed the relevant international instruments, the position of investment treaty arbitration tribunals, and some commentators regarding the role and the rules of international law in combatting corrupt and abusive investments, I should now examine the

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[52] Inter-American Convention against Corruption, signed on 29 March 1996, entered into force on 06 March 1997 (1996) 35 ILM 724.

[53] 'United Nations Declaration against Corruption and Bribery in International Commercial Transactions' GA Res 51/191, 16 December 1996.

[54] OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, signed on 21 November 1997, entered into force on 17 December 1997 (1998) 37 ILM 1.

[55] Criminal Law Convention on Corruption, signed on 27 January 1999, entered into force on 01 July 2002, 2216 UNTS 225.

[56] Civil Law Convention on Corruption, signed on 04 November 1999, entered into force on 01 November 2003, 2246 UNTS 3.

[57] African Union Convention on Preventing and Combating Corruption, signed on 11 July 2003, entered into force on 05 August 2006 (2004) 43 ILM 1.

[58] United Nations Convention against Corruption, signed on 31 October 2003, entered into force on 14 December 2005, 2349 UNTS 41.

[59] As an aside, one problem with these instruments, as eloquently put forward by Llmazon, is that "[w]hile a number of recent treaties express well-meaning and appropriate condemnation, the consensus and rhetorical vitality of these instruments mask a central problem: international conventions have mostly been confined to the level of general principles and proscriptions, arrogating unto individual State sole responsibility for enacting and enforcing anti-bribery legislation." AP Llamzon (n 8) 2-3. An example of this attitude of dumping the responsibility of fighting corruption on individual states can be tracked at Article 1(1) of the OECD Convention (n 54). According to this provision,

> Each Party shall take such measures as may be necessary to establish that it is a criminal offence under its law for any person intentionally to offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a foreign public official, for that official or for a third party, in order that the official act or refrain from acting in relation to the performance of official duties, in order to obtain or retain business or other improper advantage in the conduct of international business.

relevance of such rules in the context of deciding upon legality requirement defences in investment treaty arbitration proceedings. In cases where the treaty explicitly provides for compliance with the laws of the host state at the time of making the investment, the focal point and the starting point for an investment treaty tribunal should, in principle, be the municipal laws of the host state. In this regard, Knahr says: "If a violation of national law is at issue, it should primarily be the national law itself to provide an answer to the question of legality or illegality of the action."[60] As a result, good faith, international public policy, and other relevant principles of international law could also be relied upon, not because there is a real requirement or duty to refer to international law, but just to make the decision seem more persuasive. In this respect, a comparison between the approach adopted in *Fraport* and *Inceysa* awards is noteworthy. There is an important difference between the two awards in the approach the two tribunals took in applying domestic law as a ground to evaluate the legality of the investment. Whereas in *Fraport*, the tribunal, in finding illegality on the part of the investor and rejecting its jurisdiction, quite correctly relied extensively on the laws of Philippines, the *Inceysa* tribunal found that the investment was illegal since it violated 'general principles of law'. Although the latter tribunal had generally attached significant importance to the host state law, it nevertheless discussed 'general principles of law' like good faith, *nemo auditur propriam turpitudinem allegans*, public policy, and the prohibition of unlawful enrichment in a comprehensive manner, based on their presumed congruency with the domestic law of El Salvador.[61]

42. Furthermore, it is the present author's opinion that in cases where reference to the legality requirement is implicit in the underlying treaty, applying good faith, international public policy, or other principles of international law for the purpose of dismissing jurisdiction in the case of illegal investments seems more justified as long as these principles are incorporated in the laws of the host state. Such reference could still be warranted if these principles do not form part of the law of the host state but the tribunal refers to them as additional reasons to justify the tribunal's decision.

43. Finally, in cases where the relevant treaty lacks any reference to assessing legality in accordance with domestic law, investment treaty tribunals have correctly dismissed investment claims grounded on corruption, fraud or other kinds of illegality based not only on the domestic laws of the host state but also on principles of international law, including good faith and public policy. In *Plama v. Bulgaria*, for example, the claimant had filed its claims pursuant to the ECT, which, as mentioned above, does not contain a provision requiring investments to be made in conformity with a particular law.[62] The ICSID tribunal observed that "[t]his does not mean, however, that the protections provided for by the ECT cover all kinds of investments, including those contrary to domestic or international law."[63] Finding that Plama's conduct in making its investment violated not only Bulgarian law, but also applicable rules and principles of international law, including the principle of good faith, the tribunal concluded that granting the claimant's investment the protections provided by the ECT would be contrary to the principle of *nemo auditur propriam turpitudinem allegans* and "contrary to the basic notion of

[60] C Knahr (n 7) 17, 28.

[61] *Inceysa Vallisoletana, S.L. v. Republic of El Salvador* (n 7) [243]. In this respect, see C Knahr (n 7) 8, 17, 28 (characterising the *Inceysa* tribunal's approach in this regard to be 'somewhat questionable').

[62] *Plama Consortium Limited v. Bulgaria* (n 38) [138].

[63] ibid [138].

international public policy—that a contract obtained by wrongful means (fraudulent misrepresentation) should not be enforced by a tribunal".[64] This understanding was also specifically confirmed in *World Duty Free*, where the tribunal, deciding an investment contract dispute, which usually does not contain a legality requirement or a similar clause, recognised that:

> In light of domestic laws and international conventions relating to corruption, and in light of the decisions taken in this matter by courts and arbitral tribunals, this Tribunal is convinced that bribery is contrary to the international public policy of most, if not all, States or, to use another formula, to transnational public policy. Thus, claims based on contracts of corruption or on contracts obtained by corruption cannot be upheld by this Arbitral Tribunal.[65]

44. Indeed, in such a situation, i.e. lack of any reference to the laws of the host state in the investment treaty or contract for assessing legality, there is a plausible justification for reliance on the principles of good faith, public policy, and *nemo auditur propriam turpitudinem allegans* in deciding the issue of legality in an investment arbitration case. As has been indicated by the WTO Appellate Body, although states are free to conclude treaties and exclude certain rules of international law in their relations, they cannot, however, contract out of the system of international law. In other words, they cannot be deemed to have ignored *jus cogens*.[66] Therefore, an investment treaty tribunal cannot ascribe an intention to the state parties that they could not have had, i.e. the contracting parties to an investment agreement, who have not included a legality requirement in their treaty, could not have agreed to protect investments which were made in violation of good faith and international public policy. Consequently, when an investment treaty lacks any provision regarding the legality requirement, in addition to checking the host state law, a tribunal is well-advised to verify whether the investment violates fundamental principles of international law, like good faith and public policy. To borrow some 'extreme examples' from the *Phoenix v. Czech* tribunal, "nobody would suggest that [international investment] protection [regime] should be granted to investments made in violation of the most fundamental rules of protection of human rights, like investments made in pursuance of torture or genocide or in support of slavery or trafficking of human organs."[67] In a nutshell, if an investment has been obtained violating international public policy or other fundamental principles of international law, it cannot benefit from the investment treaty system, even if the treaty lacks any reference to the legality requirement.

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[64] ibid [138]-[140], [143]-[145].

[65] *World Duty Free Company v Republic of Kenya* (n 50) [157]. In this respect, the tribunal had already quoted Judge Lagergren's observations in ICC Case No. 1110 of 1963 that "corruption is an international evil", which "is contrary to good morals and to an international public policy common to the community of nations". See ibid [148].

[66] *United States - Standards for Reformulated and Conventional Gasoline, Brazil and Venezuela v United States*, Report of the Appellate Body, WT/DS2/AB/R, WT/DS4/AB/R, Report No AB-1996-1, Doc No 96-1597, ITL 013 (WTO 1996), DSR 1996:I, 3, 29th April 1996, World Trade Organization [WTO], p 18. See also, J Pauwelyn, 'The Role of Public International Law in the WTO: How Far Can We Go?' (2001) 95(3) AJIL 539 (saying that: "States in their treaty relations, can contract out of one, more or in theory, all rules of general international law (other than those of *jus cogens*), but they cannot contract out of the system of international law. As soon as States contract with one another, they do so automatically and necessarily within the system of international law.")

[67] *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [78].

45. To sum up, in cases where the investment treaty stipulates the legality requirement, reference to good faith, public policy, and the principle of *nemo auditur propriam turpitudinem allegans* can make a decision seem more reasoned, but such reference is not necessary. When the treaty refers to the legality requirement in implied terms, the reference to such principles seems more justified but again not necessary. Finally, in case the treaty contains no express or implied term concerning the legality requirement, in addition to checking the relevant host state law, the tribunal can safely rely on the relevant general principles of international law as an independent basis to admit the case or to declare it inadmissible.[68]

## Section Two: The Actual Application of Domestic Law to Particular Questions Regarding the Legality Requirement

46. With the discussion of the legal basis for the application of domestic law to the legality requirement out of the way, I now turn to the application of domestic law to particular practical questions regarding the operation of the legality requirement. Generally speaking, there are two main questions concerning the legality requirement which should be addressed by reference to the laws of the host state: first, the scope of the legality requirement, and second, the consequence of violation of the laws of the host state and the impact of such violation on the operation of the legality requirement. These two questions will be addressed below in-depth.

### A. The Scope of the Legality Requirement

47. So far, I have delineated the meaning of the legality requirement in investment treaties and have discussed the legal basis for the application of host state law to this requirement. A significant question that still comes to mind in the context of the dimension of this requirement is the formal, substantive, and the temporal sphere of application of this so-called 'in accordance with host state law" condition.

48. An arbitral tribunal seized of the application of a legality requirement in an investment treaty has to determine the range of laws and regulations of the host state, in terms of the character of the lawmaker entity, that are relevant for its legality analysis. In so doing, the tribunal should answer whether only enactments of the Parliament of the host state are pertinent, or whether, in addition, regulations enacted by the cabinet of ministers, a commission of the ministers, or even resolutions of a single ministry or a state entity should also be taken into account. Furthermore, and more importantly, such a tribunal has to specify the kind of laws, in terms of the subject-matter of the law in question, the nature of the law, and the significance of the law, that are relevant for the legality analysis. To embark upon this task, the tribunal should find whether all the laws and regulations of the host state, irrespective of their subject-matter, hierarchy, significance or nature are relevant, or whether the survey should only be limited to the imperative laws of the recipient state or a specific group of such laws with a specified subject-matter.

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[68] One question that still arises in the last scenario, i.e., no reference to the legality requirement in the investment treaty, is when international law deems the investment illegal but host state law does not and *vice versa*. The task of the arbitral tribunal seems to be more complex in such episodes. In the author's opinion, in situations where international law does not extend its protection to an investment due to its illicitness despite host state laws' position to the contrary, the tribunal should give primacy to the international law. If, however, the investment is deemed illegal in host state law but legal under international law, the tribunal should respect host state laws' position and refrain from declaring the claim admissible.

49. To contextualise the discussion, in *Saba Fakes v. Turkey*,[69] the underlying BIT provided in its Article 2(2), embodying a legality requirement, that:

> The present Agreement shall apply to investments owned or controlled by investors of one Contracting Party in the territory of the other Contracting Party which are established in accordance with the laws and regulations in force in the latter Contracting Party's territory at the time the investment was made.[70]

The respondent in that case alleged that the claimant's investment transaction was made in breach of the Republic of Turkey's legislation relating to the promotion of foreign investment, a regulation of the telecommunication sector, as well as Turkish competition law.[71] Therefore, in that case, the tribunal was faced with two questions: (i) whether only legislations are relevant, in which case it only had to consider the violation of the law on encouragement of foreign investment and the competition law of Turkey, or whether other types of laws and regulations not enacted by the Turkish Parliament and laid down by other official governmental entities were also pertinent, in which case it should have also taken into account the regulation of the telecommunication sector. More importantly, the tribunal had to determine what legal subject-matters were relevant for its legality analysis: was it only the law on foreign investment that had to be analysed, or whether laws relating to telecommunication and competition should also have gone under scrutiny. Similarly, and on a related note, the tribunal should have also analysed the laws invoked in terms of their significance and hierarchy and indicated whether all the laws were applicable regardless of their fundamentality, or whether only the most imperative laws of the Republic of Turkey were germane.[72]

50. Despite the rendition of many investment treaty awards and decisions, and myriads of scholarly writings on the issue of the legality requirement in investment treaty arbitration, the precise 'formal' and 'substantive' scope of this requirement remains largely unknown.[73] With one notable exception,[74] most of the tribunals have formulated tests without much analysis and

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[69] *Saba Fakes v. Republic of Turkey*, ICSID Case No. ARB/07/20, Award, 14 July 2010.

[70] See Article 2(2) of the Agreement on Reciprocal Encouragement and Protection of Investments between the Kingdom of the Netherlands and the Republic of Turkey, signed on 27 March 1986, entered into force on 01 November 1989.

[71] *Saba Fakes v. Republic of Turkey* (n 69) [120].

[72] It is worth observing that this tribunal only briefly dealt with the second question, i.e. the relevance of the laws of the host state by their subject-matter. See ibid.

[73] See J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (2014) 5(3) Journal of International Dispute Settlement 532-533. See also A Carlevaris (n 7) 46-47 (observing that the interpretation of 'in accordance with host state law clauses' is not relatively clear and consistent with respect to the nature and the magnitude of the breach justifying the dismissal of jurisdiction).

[74] Recently, a decision on jurisdiction was issued in the dispute between 12 Kazakh nationals and the Government of Uzbekistan which deals with the 'formal' and 'substantive' scope of the legality requirement with an admirable thoroughness. See *Vladislav Kim and others v. Republic of Uzbekistan*, ICSID Case No. ARB/13/6, Decision on Jurisdiction, 08 March 2017. I should note here, however, that despite the comprehensive manner through which this tribunal handled these questions, I believe that the tribunal has gone too far in drawing up the benchmark for the 'substantive' scope of the requirement. Moreover, when applying the test it had constructed, the majority of the tribunal seems to have gone even further, in that it effectively excluded significant violations of the host state law from triggering the legality requirement on grounds which do not seem justified. It is my considered opinion that the

discussion,[75] and commentators have either favoured expansive or restrictive criteria for outlining the scope of this requirement unaccompanied by needed scrutiny.[76] This lack of transparency in the scope of the legality requirement and the absence of concrete yardsticks for outlining the frontiers of the relevant laws of the host state in undertaking a legality requirement analysis has given rise to a state of 'uncertainty', harming both the investors and host states.[77]

51. In this Section, I will try to reflect all the voices I have heard regarding the 'formal' and 'substantive' scope of the legality requirement and then put together what I believe is the most appropriate benchmark for setting out the 'formal' and 'substantive' boundaries of this requirement. To embark upon this task, I will begin with the less controversial 'formal' scope of the requirement and will try to frame an appropriate gauge for identifying the 'formal' contours of this requirement (**a**). Next, I will deal with the more challenging subject of the 'substantive scope' of the requirement. I will begin with reviewing the standpoints taken in the decisions of investment treaty arbitral tribunals and setting forth the various viewpoints of commentators. Where necessary, I will closely examine those views and decisions (**b**)(**i**). I will follow the discussion by setting out my own opinion about the 'substantive scope' of the legality requirement (**b**)(**ii**). In so doing, I will try to be observant and loyal to the 'rule of interpretation' as enshrined in Article 31 of the VCLT. Additionally, it is necessary to enquire into the 'temporal' aspect of the legality requirement and survey the various effects illegality might have depending on the timing of the occurrence of illegality, including illegality at the time of making the investment and illegality after the establishment of the investment. Relevant in this respect is considering the effect of the completion of the corrupt action, like payment of a bribe to the relevant public official, after the establishment of the investment and the jurisdictional and/or admissibility consequences of this act **(c)**.

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test devised by the tribunal in this case, as well as the consequent result achieved by the majority in applying the test are not based on a sound interpretive look to the legality requirement. This issue will be further dealt with below.

[75] See, for instance, *L.E.S.I. S.p.A. and ASTALDI S.p.A. v. République Algérienne Démocratique et Populaire*, ICSID Case No. ARB/05/3, Decision, 12 July 2006 [83] (stating that: "the mention in the text of conformity to laws and regulations in vigour does not constitute a formal acknowledgement of the notion of investment as understood in Algerian law in a restrictive fashion, but rather, adopting a classic and wholly justified formulation, the loss of protection suffered by any investments made in violation of fundamental governing principles.") (Translated from French); *Desert Line Projects LLC v. The Republic of Yemen*, ICSID Case No. ARB/05/17, Award, 06 February 2008 [104] (stating that the legality requirement in investment treaties is "intended to ensure the legality of the investment by excluding investments made in breach of fundamental principles of the host State's law, e.g. by fraudulent misrepresentations or the dissimulation of true ownership…"); *Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S. v. Republic of Kazakhstan*, ICSID Case No. ARB/05/16, Award, 29 July 2008 [319] (saying that: "as was determined by the arbitral tribunal in the *Lesi* case, investments in the host State will only be excluded from the protection of the treaty if they have been made in breach of fundamental legal principles of the host country.")

[76] As far as I am aware, a notable exception is the recent article by Jarrod Hepburn who specifically deals with this issue in-depth. See J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73). The contents of the article are mirrored in his recent book. See J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 139-155. See also U Kriebaum, 'Illegal Investments' in C Klausegger *et al* (eds), *Austrian Arbitration Yearbook 2010* (Beck, Sta¨mpfli & Manz 2010) 318-329.

[77] Indeed, achieving 'certainty' is one principal reason why certain tribunals have felt compelled to "contribute to the harmonious development of international investment law with a view to meeting the legitimate expectations of the community of States and investors". To cite just one example amongst many, see *Churchill Mining PLC* and *Planet Mining Pty Ltd v. Republic of Indonesia*, ICSID Case No. ARB/12/14 and 12/40, Award, 06 December 2016 [253].

### a. The Formal Scope of the Legality Requirement

52. When faced with an illegality objection by the host state, one of the questions for an investment treaty tribunal is the 'formal scope' of the legality requirement. In practice, this question mainly arises in cases where the law allegedly violated does not have the form of legislation enacted by the Legislative body of the recipient state,[78] but is a resolution or a regulation passed or laid down by the Executive or even the Judiciary of that state.[79]
53. Suppose that in a given case, the respondent objects that the investor violated the laws of the host state in making its investment since it covertly, and in breach of the foreign investment cap of the Constitution and foreign investment law of the host state, concluded agreements with its local partners of the bidding consortium, thereby controlling their shareholdings and votes.[80] In addition, assume that in the same case, the host state also contends that in the course of making its investment, the investor also failed to carry out an 'environmental impact assessment' ("EIA") in violation of the resolutions of the environmental organisation of the host state, an entity of the Executive branch of the government. Whereas the first two laws (i.e., the Constitution and the foreign investment law) are most probably captured by a typical legality requirement, it is not clear whether the environmental resolution is also caught by the 'formal scope' of the requirement.
54. In order to find the answer to such questions, the text of the legality requirement is the proper point of departure. Most investment treaties containing a legality requirement, stipulate that investments should be made in accordance with the 'laws' of the host state. Therefore, in order to understand the 'formal scope' of the legality requirement in such treaties, the meaning of the term 'law' as intended and understood by the contracting parties of the investment treaty in question is of critical importance. Certain investment treaties do define the term 'law' for the purposes of, *inter alia*, the legality requirement. For example, Article 1.7 of the BIT between India and Belarus reads:

> "law" includes:
>
> In respect of Belarus: normative legal acts of the Republic of Belarus.
>
> In respect of India:

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[78] The legislative power of a state may have different titles and/or structures in various jurisdictions. In the United Kingdom, the Parliament consists of the 'House of Commons' and the 'House of Lords'. In France, the Parliament consists of the '*Assemblée nationale*' and '*Sénat*'. In Germany, the two Houses of Parliament are the '*Bundestag*' and the '*Bundesrat*'. See R Youngs, *English, French & German Comparative Law* (Routledge 2014) 32-35. In Iran, the 'Islamic Consultative Assembly' and the 'Guardian Council' compose the Legislature. See Principles 62 to 99 of the Islamic Republic of Iran Constitution (1979, as amended in 1989).

[79] The author is aware of only one case in which the issue of the 'formal scope' of the legality requirement was considered separately by an investment treaty tribunal. See *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [378]-[380].

[80] The factual background in *Fraport v. Philippines* was similar to the hypothetical given above. In that case, through 'secret shareholder agreements', Fraport sought to exercise managerial control over Philippine International Air Terminals Co. ("PIATCO"), who on 12 July 1997 had concluded the concession contract for the construction and operation of an international passenger terminal at Ninoy Aquino International Airport in Manila ("Terminal 3") with the Philippine Department of Transportation and Communication ("DOTC"), and, thereby, knowingly orchestrated its investment in flagrant violation of the laws of Philippines, in particular, foreign ownership and control legislation known as the Anti-Dummy Law ("ADL").

(i) the Constitution, legislation, subordinate/delegated legislation, laws & bylaws, rules & regulations, ordinance, notifications, policies, guidelines, procedures, administrative measures/executive actions at all levels of government, as amended, interpreted or modified from time to time;
(ii) decisions, judgments, orders and decrees by Courts, regulatory authorities, judicial and administrative institutions having the force of law within the territory of a Party.[81]

55. As the above definition makes clear, when investing in India, an investor from Belarus has to comply with a broad array of laws extending to regulations laid down by the executive. However, the majority of investment treaties do not contain such definitions. In such circumstances, the wording of the legality requirement itself should guide the tribunal in ascertaining the 'formal scope' of the condition. Thus, if the above-mentioned dispute occurs between an Iranian investor and the Government of the Republic of Korea, the environmental resolution in question, would more likely than not, be captured by the legality requirement of the BIT between the two countries, which provides in the pertinent provision that "[t]he term "investment" refers to every kind of property or asset […] invested by the investors of one Contracting Party in the territory of the other Contracting Party in accordance with the *laws and regulations* of the other Contracting Party …"[82] [emphasis added] Generally speaking, the term 'law' mentioned in this provision is a comprehensive term which can potentially encompass an enforceable resolution by a single state department or a ministry.[83] Furthermore,

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[81] Treaty between The Republic of Belarus and The Republic of India on Investments, signed on 24 September 2018, not yet entered into force. Article 1.4 of this Treaty contains a legality requirement: ""investment" means an enterprise constituted, organised and operated in good faith by an investor in accordance with the law of the Party in whose territory the investment is made ..."

[82] Article 1(1) of the Agreement between the Government of the Republic of Korea and the Government of the Islamic Republic of Iran for the Promotion and Protection of Investments, signed on 31 October 1998, entered into force on 31 March 2006.

[83] 'Law' is a generic term which can appear in various different guises. Constitution, organic laws (as will be seen more fully below (see b.ii.2nd *infra*), the phenomenon of 'organic laws' exists in the constitutional law of certain legal regimes: "Organic laws fall between ordinary legislation and constitutional provisions on a scale of difficulty of adoption, amendment and repeal. In addition to their utility in dealing with important subjects whose implementation is rife with technical detail, creating the category can be a useful mechanism for getting over some obstacles in the constitution-writing process …" See M Tushnet, *Advanced Introduction to Comparative Constitutional Law* (Edward Edgar Publishing Limited 2014) 22), statutes, decrees, regulations, and orders issued and adopted by president, cabinet of ministers, a committee of ministers, individual ministries or state departments, as well as certain judicial decisions (depending, of course, on the jurisdiction in question) can all form 'laws'. In this regard, Black's Law Dictionary defines the term 'law' to correspond, *inter alia*, to the following various meanings: "That which is laid down, ordained, or established. A rule or method according to which phenomena or actions co-exist or follow each other. That which must be obeyed and followed by citizens, subject to sanctions or legal consequences, is a "law"… Act of the Legislature deposited in office of Secretary of State, properly authenticated by presiding officers of the two houses, and approved by Governor … body of principles, standards and rules promulgated by government … command which obliges a person or persons and obliges generally to acts or forbearances of a class … constitution or constitutional provision … governmental direction … judicial decisions, judgments or decrees … local rules of decision … municipal ordinance … proclamation of Governor … regulations … resolution passed by Legislature and approved by Governor … revised statutes … rule of civil conduct prescribed by the supreme power in a state … rule of conduct prescribed by lawmaking power of state … rules promulgated by government … statute or enactment of legislative body …" HC Black, *Black's Law Dictionary: Definitions of the Terms and Phrases of American and English Jurisprudence, Ancient and Modern* (West Publishing Co 1968) 1028.

the term 'regulation' appearing in the above-cited provision is usually used, in its 'specific' sense, to represent rules laid down by the Executive in implementing acts, statutes, and legislation passed by the Legislature.[84] In this sense, a resolution by the environmental organisation in question would also be captured by the term 'regulation'. The same finding could not have been readily made had the same dispute occurred under the BIT between Kazakhstan and Austria, in which the legality requirement reads: "This Agreement shall apply to investments made in the territory of either Party in accordance with its *legislation* by investors of the other Party prior to as well as after the entry into force of this Agreement."[85] [emphasis added] The reason for this wrinkle is the use of the apparently more restrictive term of 'legislation' rather than the more inclusive terms 'laws' and 'regulations'. From the viewpoint of a Romani-Germanic-educated lawyer, one may find the term 'legislation' to cover only the enactment of the Legislature, and not the resolutions or regulations laid down by the Executive.[86]

56. Bearing this in mind, it should be mentioned that in case doubt arises as to the characterisation of the law in question, – as to whether the law at issue is a 'legislation' (in its 'specific' sense) or a regulation (in its 'specific' sense) – one has to refer to the legal system of the host state and determine the status of the law at stake in accordance with the constitutional and public law regime of the of that state.[87]
57. Another point to make in this respect is that it is possible that the investment treaty in question sets out in the legality requirement a number of laws, legislation, and regulations which should be complied with in the process of making the investment. In such a situation, a tribunal can firmly hold that the stipulated laws should have been abided by in the process of establishment of the investment.[88] Whether other laws on top of those expressed laws should have been observed in the process of making the investment, would, of course, depend on the terms of the legality requirement in question.
58. The final point to make in this regard is that in case a domestic legal instrument does not have the force of law, it will not fall within the 'formal scope' of the legality requirement. Indeed,

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[84] According to Black's Law Dictionary, 'regulation' means: "The act of regulating; a rule or order prescribed for management or government; a regulating principle; a precept … Rule of order prescribed by superior or competent authority relating to action of those under its control…" See ibid 1451. These meanings seem to represent the term 'regulation' in its 'broad' rather than 'specific' sense.

[85] Article 26(1) of the Agreement for the Promotion and Reciprocal Protection of Investment between the Government of the Republic of Austria and the Government of the Republic of Kazakhstan, signed on 12 January 2010, entered into force on 21 December 2012.

[86] However, it seems that in 'Common Law', the term 'legislation' bears a more general meaning than what is understood by a 'Romani-Germanic' lawyer: "The act of giving or enacting laws; the power to make laws; the act of legislating; preparation and enactment of laws; the making of laws by express decree … Formulation of rule for the future … Municipal ordinances are legislation." HC Black (n 83) 1045.

[87] See *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [411] (stating that: "The term "legislation" in Article 12 [of the BIT] encompasses those normative actions regarded as "law" by the Host State's legal system which […] is defined by the normative-legal acts set out in Article 5 of the Uzbekistan Law on Normative-Legal Acts.")

[88] See, for instance, the Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments (n 3), which in its Protocol refers to a provision of Constitution of Philippines as a law that should be complied with by German investors. The Protocol to the Agreement, which was concluded on the same day as the BIT, states at ad Article 2: "As provided for in the Constitution of the Republic of the Philippines, foreign investors are not allowed to own land in the territory of the Republic of the Philippines. However investors are allowed to own up to 40% of the equity of a company which can then acquire ownership of land."

an essential prerequisite to fall within the 'formal' ambit of the legality requirement is that the instrument in question should have the force of law and should be binding. Thus, in *Vladislav Kim v. Uzbekistan*, the tribunal, *inter alia*, dismissed an alleged illegality objection by the respondent on the basis that the invoked instrument, i.e., Rules of Exchange Trade of Services in the Republican Stock Exchange, "Tashkent" ("TSE Rules"), did not constitute 'normative-legal acts'.[89]

### b. The Substantive Scope of the Legality Requirement

59. The 'substantive scope' of the legality requirement specifies the relevant group of host state's laws, in terms of their subject-matter, hierarchy, significance or nature, which an investment treaty tribunal should consider when assessing the legality of an investment.[90]
60. Disputants in investment treaty arbitrations usually disagree as to the 'substantive scope' of application of the legality requirement. Specifically, they are usually in contention as to whether the requirement extends to violations of all or only specified types of laws and regulations of the recipient state.[91] The case of respondent states is usually that the requirement encompasses any violation of its municipal laws irrespective of the law's subject-matter or significance.[92] On the other hand, claimants usually argue that the 'compliance with the host state law' requirement is triggered only when fundamental laws of the host state are violated.[93]
61. Assume that in an investment treaty case, the jurisdictional question before the tribunal is the illegality objection of the respondent, whereby the host state contends that in making its investment, the investor violated (a) mandatory provisions of development law of the host state regarding equity investment limitation of foreign investors in air transportation sector; (b) a provision of local content law for employing at least half of the board of directors' members of the joint venture from citizens of the host state; and (c) an implementing regulation of the foreign investment law requiring investors to state the full name of all of their major shareholders in investment application forms. In such a case, a preliminary task of the tribunal is to specify the 'substantive scope' of the legality requirement to see which one of these laws falls within the 'substantive' reach of the requirement in order to determine which violation is caught by the legality requirement.
62. According to certain investment treaty arbitral tribunals, only fundamental violations of the host state law count for triggering the legality requirement. Others believe that it is the subject-matter of the law that matters, not the severity of the violation. Finally, most recently a stringent test has been adopted by the tribunal in *Vladislav Kim v. Uzbekistan*. According to this tribunal, the twofold test devised by it "requires a case-by-case analysis examining both the seriousness of the investor's conduct and the significance of the obligation not complied with so as to

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[89] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [514].

[90] M Polkinghorne & SM Volkmer, 'The Legality Requirement in Investment Arbitration' (2017) 34(2) J Int'l Arb 149, 160.

[91] T Obersteiner, 'In Accordance with Domestic Law' Clauses: How International Investment Tribunals Deal with Allegations of Unlawful Conduct of Investors' (2014) 31(2) J Int'l Arb 265, 276.

[92] See, for instance, *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [239]-[240]; *Saba Fakes v. Republic of Turkey* (n 69) [119].

[93] For instance, in *Saba Fakes v. Turkey*, the claimant alleged that a 'certain level of violation' is required to trigger the legality requirement. According to the claimant, an investment should be considered 'illegal' only if made in violation of a fundamental legal principle. See *Saba Fakes v. Republic of Turkey* (n 69) [118]. See also *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania* (n 43) [300] (the claimant argued that to amount to illegality, there should be a 'serious violation of mandatory public order').

ensure that the harshness of the sanction of placing the investment outside of the protections of the BIT is a proportionate consequence for the violation examined."[94]

63. All these three views will be reviewed and analysed in the sub-section below (i). I submit that while each of the approaches considered below has some merits (some more than others), none of them entails a sound interpretive exercise as prescribed by Article 31 of the VCLT in construing the legality requirement. A watchful travel through the route of treaty interpretation, in accordance with Article 31 of the VCLT, can lead one to adopt a 'balanced interpretation' of the legality requirement using the available interpretive tools embedded in Article 31 of the VCLT (ii).

### i. Approaches Adopted in Investment Treaty Arbitrations

64. As was alluded to above, two main approaches can be discerned with regard to the 'substantive scope' of the legality requirement in the decisions of investment treaty tribunals: (i) 'subject-matter approach', according to which it is only the violation of certain types of laws that can trigger the legality requirement. (ii) 'significance-analysis approach', according to which the activation of the legality requirement depends on the significance of the law(s) violated. In this sub-section, I will firstly review and analyse the 'subject-matter approach' and then the 'significance-analysis approach'. As was briefly touched upon above, recently, a decision has been rendered in a dispute between 12 Kazakh nationals and the Government of Uzbekistan. In the decision on jurisdiction in that dispute, the tribunal devised, what it called 'principle-based reasoning'[95] which took into account not only the significance of the violation, but also the behaviour of the investor, and the collective impact that these two factors had on the interest of the host state.[96] This recent test will also be subject to thorough consideration below.

#### 1st. *Subject-Matter Approach (Compliance only with Laws Relating to Foreign Investment)*

65. According to this approach, in order to observe the legality requirement in the course of making the investment, the investor only needs to comply with foreign investment laws of the host state. This theory was put forward by the *Saba Fakes* tribunal[97] and is cited, at least, in two decisions of other investment treaty tribunals without being rejected or distinguished.[98]

66. In *Saba Fakes v. Turkey*, the respondent argued that the investor had established his investment in violation of Turkish law on foreign investment, a regulation of the telecommunications sector, and the competition law of Turkey. On the one hand, the tribunal said that the first alleged violation, i.e., violation of Turkish law on foreign investment, if found to exist, might trigger the legality requirement. On the other hand, it held that breaches of the telecommunications regulations and the competition law of Turkey exceed the 'substantive scope' of the legality requirement and are not covered by it.[99] Thus, the tribunal decided that the 'substantive scope' of the legality requirement was restricted to the laws and regulations 'governing the admission of investments in the host State'. The ICSID tribunal reasoned that

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[94] See *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [404].

[95] ibid [399].

[96] ibid [404]-[408].

[97] *Saba Fakes v. Republic of Turkey* (n 69).

[98] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [165]; *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [248].

[99] *Saba Fakes v. Republic of Turkey* (n 69) [120].

its finding was based on the 'plain language' of the underlying investment agreement,[100] which covered 'investments … established in accordance with the laws and regulations' of Turkey.[101] The tribunal also indicated that the object and purpose of the agreement in general also contributed to this view, restraining the above-stated 'laws and regulations' only to laws 'related to the very nature of investment regulation'.[102] Subsequently, according to this tribunal, in case the investor violated any other laws of Turkey, not related to investment laws, the respondent state could not rely on the legality requirement to deny BIT protection to the investor. Therefore, the tribunal found that the respondent could not rely on the investor's alleged violations of competition laws and telecommunications regulations of Turkey to generate the legal consequences of the application of the legality requirement.[103]

67. Unlike the viewpoint according to which investors need only to comply with 'fundamental laws' of the host state, which is based on the analysis of the significance of the laws within the legal scheme of the recipient state (see *infra*), under the present theory, the test is pertinence, i.e. abiding by laws which are, subject-matter-wise, pertinent to the type of the economic operation in question, i.e. laws relating to 'foreign investment'.
68. An investment law of a country may include in addition to its general law on foreign investment[104] – which is usually supplemented and elaborated by regulations and subordinate legislation – separate laws on foreign investment in specific economic sectors.[105] Thus, as it is implied from the *Saba Fakes* tribunal's findings, for satisfying the legality requirement, when establishing its investment, the investor needs only to comply with these laws of the host state.
69. The first obvious problem with this theory is that it is not backed by the 'ordinary meaning of the terms' of a typical legality requirement. While the *Saba Fakes* tribunal does mention that the interpretation it offers 'is made clear by the plain language of the BIT, which applies to 'investments . . . established in accordance with the laws and regulations …',[106] it fails to explain why the 'ordinary meaning' of the unqualified and generic terms of 'laws' and 'regulations' used in Article 2(2) of the underlying investment agreement should be restricted only to foreign investment laws of the host state.[107]
70. Moreover, the tribunal's statement that "it would run counter to the object and purpose of investment protection treaties to deny substantive protection to those investments that would violate domestic laws that are unrelated to the very nature of investment regulation" is not also well-reasoned. As set out in the Preamble of the underlying BIT, one purpose of the conclusion

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[100] Agreement on Reciprocal Encouragement and Protection of Investments between the Kingdom of the Netherlands and the Republic of Turkey (n 70).

[101] *Saba Fakes v. Republic of Turkey* (n 69) [119].

[102] ibid.

[103] ibid [120].

[104] JW Salacuse (n 6) 90 (explaining different titles used for describing such laws in various developing and developed countries).

[105] ibid 90-91.

[106] *Saba Fakes v. Republic of Turkey* (n 69) [120].

[107] R Dolzer and C Schreuer, *Principles of International Investment Law* (OUP 2012) 93 (saying that: "Whenever a clause 'in accordance with the laws of the host state' is contained in a treaty, it may be understood to imply that investments made in violation of national laws are not covered by the treaty. Therefore, the words 'in accordance with the laws' relate not just to the laws on admission and establishment but also to other rules of the domestic legal order, including those relating to corruption.") See also J Hepburn 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73) 547-548.

of the Agreement is stimulating 'economic development' in both states.[108] 'Economic development' would be achieved by preserving the 'public interest' of the host state.[109] It borders on inconceivable that investment contracts made in accordance with foreign investment laws, but in violation of, for example, criminal codes of the state in question (for instance, investment contracts brokered by payment of bribes to influential dignitaries of the host state) would serve the 'public interest' or contribute to the 'economic development' of the host state, and not surely to the 'sustainable development' of its economy. Indeed, it is very difficult to ascribe an intention to the contracting parties of international investment agreements, according to which, all of their laws (except those relating to foreign investment), irrespective of their significance and imperativeness, could be breached by investors in the course of making their investment, with the agreement still being applied and with no jurisdiction, admissibility, or substantive consequences for the defiant investors.

71. Furthermore, apart from its interpretive flaws, in practice, although not expressly rejected, this theory has not been supported by other tribunals deciding investment treaty cases.[110] For instance, in *Alasdair Ross Anderson v Republic of Costa Rica,* the tribunal found that the underlying economic operation did not comply with the requirements of the Organic Law of the Central Bank of Costa Rica and that, therefore, the claimants did not acquire their investment in accordance with the laws of Costa Rica.[111] The Organic Law of Costa Rica was not a law directly related to admission and establishment of foreign investments. In another leading case, the *Metal-Tech* tribunal concluded that the investor had made its investment in violation of the Uzbek Criminal Code. Therefore, the tribunal found that the legality requirement is engaged and that it lacked jurisdiction to hear the parties' claims and counterclaims brought under the relevant BIT even though the law violated did not concern laws of foreign investment.[112] Indeed, even those investment treaty tribunals which have cited and relied on *Saba Fakes* with regard to the 'substantive scope' of the legality requirement have not done so on an exclusive basis. Rather, they have considered a wide array of domestic laws to fit within the 'substantive' reach of the legality requirement, not confined to domestic laws on foreign investment. According to these awards, the 'substantive scope' of the legality requirement extends to the ensuing illegalities: (i) "nontrivial violations of the host State's legal order"; (ii) "violations of the host State's foreign investment regime"; and (iii) "fraud…to secure the investment …"[113] Finally, it is worth observing that this theory was not even applied by the *Saba Fakes* tribunal itself. In fact, the tribunal dismissed jurisdiction in this case on another ground.[114]

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[108] See the Preamble of the Agreement on Reciprocal Encouragement and Protection of Investments between the Kingdom of the Netherlands and the Republic of Turkey (n 70).

[109] *Joseph Charles Lemire v. Ukraine*, ICSID Case No. ARB/06/18, Decision on Jurisdiction and Liability, 14 January 2010 [272]-[273].

[110] J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73) 548-549.

[111] *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [57].

[112] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [372]-[373].

[113] *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [266]; *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [165].

[114] The tribunal concluded that the parties to the investment arrangement never intended to give effect to the alleged transfer of shares from Masoud to Mr. Fakes and, instead, agreed to implement an agreement which did not transfer even the legal ownership of the share certificates in Telsim to Mr. Fakes. As a result, the tribunal concluded that the

72. In sum, the standpoint according to which only compliance with the laws relating to the establishment of foreign investment matter for the satisfaction of the legality requirement is neither supported by a sound treaty interpretation exercise nor by the practice of investment treaty tribunals. Of course, as will be analysed *infra*, to meet the legality requirement, most laws relating to foreign investment should be complied with in the course of making the investment. However, as will be explained later, such laws are not the only category of laws of the host state that need compliance by virtue of the legality requirement.[115]

2nd. *Significance-Analysis Approach (Compliance only with Fundamental Laws of the Host State)*

73. The 'significance-analysis approach' seeks to establish that the legality requirement comes into play only when 'fundamental laws' of the host state have been infringed.[116] Interestingly, the main proponents of this approach are tribunals before which the legality requirement was not the main point of jurisdictional contention between the disputants. The opinion of the three investment treaty arbitral tribunals that have favoured this approach to the 'substantive scope' of the legality requirement will be reviewed briefly below.
74. In 2006, in *LESI and Astaldi v. Algeria*, the tribunal stated that investments would be excluded from treaty protection when made in violation of fundamental principles of law in force in the host state.[117] In 2008, the *Desert Line v. Yemen* tribunal opined that the legality requirement is "intended to ensure the legality of the investment by excluding investments made in breach of fundamental principles of the host State's law, e.g. by fraudulent misrepresentation or the dissimulation of true ownership".[118] Similarly, in 2009, in *Rumeli v. Kazakhstan*, the arbitral tribunal held that investments would be denied protection, only if they were made "in breach of the fundamental legal principles of the host country".[119] In short, the notion common in

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arrangement in question did not meet the requirement of a 'contribution', nor the requirements of 'duration' and 'risk' that an investment operation should necessarily have since no rights were actually transferred to the claimant through the underlying arrangement. Put differently, according to the tribunal, the investor had not made any investment in Telsim which would satisfy any of the three criteria for an 'investment' within the meaning of Article 25(1) of the ICSID Convention. *Saba Fakes v. Republic of Turkey* (n 69) [147]-[148].

[115] See J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73) 549. Hepburn also identifies another pitfall with this approach. According to him, almost all the laws that an investor deals with in the course of establishing its investment are related to foreign investment, and, therefore, there was no reason for the *Saba Fakes* tribunal to exclude competition and telecommunication regulations from the 'substantive scope' of the legality requirement. He says that: "…almost by definition, any host state law that an investment might breach is a law 'related to the very nature of investment regulation', as the *Fakes* tribunal itself put it. If a law does not regulate investment, it seems quite unlikely that an investment could breach it. The tribunal's proposed constraint may therefore not even serve its own stated purpose." ibid 547-548. In this regard, Salacuse properly remarks that foreign investment law is the "basic legal framework for undertaking and operating foreign investment projects." Nonetheless, he observes that such law is not the 'exclusive' law applicable to foreign investment. He opines, quite correctly, that "foreign investment projects also have to deal with and be subjected to a host of other laws, rules and regulations." According to Salacuse, a number of such foreign-investment-related laws are the ensuing: laws governing the acquisition of land, exchange controls, and labour laws. See JW Salacuse (n 6) 91.

[116] *Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S. v. Republic of Kazakhstan* (n 75) [319] (stating that: "investments in the host State will only be excluded from the protection of the treaty if they have been made in breach of fundamental legal principles of the host country.")

[117] *L.E.S.I. S.p.A. and ASTALDI S.p.A. v. République Algérienne Démocratique et Populaire* (n 75) [83].

[118] *Desert Line Projects LLC v Yemen* (n 75) [104].

[119] *Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S. v. Republic of Kazakhstan* (n 75) [319].

these decisions is that the legality requirement is set in motion only in cases where 'fundamental laws' of the host state are breached by the investor in the course of making its investment.

75. First and foremost, the obvious flaw of this approach is that it is not supported by the 'ordinary meaning of the terms' of a typical legality requirement.[120] A typical legality requirement reads: "This Agreement shall apply to investments in the State territory of one Contracting Party which were carried out in accordance with its legislation by investors from the State of the other Contracting Party …"[121] There is no limiting language in this provision confining the 'legislation' of a 'Contracting Party' which should be abided by investors to 'fundamental laws' of the host state. Probably, it was for this reason that in *Quiborax v. Bolivia*,[122] the tribunal dismissed the claimants' proposed limitation to the legality requirement. In that case, the claimants advocated a narrow reading of the legality requirement in the underlying investment treaty limited to breaches of fundamental legal principles or of the investment regime of the host state.[123] The tribunal considered such a reading of the legality requirement to be 'too narrow', which went 'beyond the terms of the BIT', and characterised it as "an attempt to further the investor's protection without due regard for the State's interests".[124]
76. Furthermore, this interpretive approach frustrates certain stated purposes of investment agreements, like 'economic development of the host state', which is frequently referred to as one of the objectives of these agreements.[125] It is hardly conceivable that 'economic development' of the host state could be achieved if only the observance of a fraction of the laws of the host state is sanctioned by the investment treaty in question. In other words, 'sustainable development' of the recipient state cannot be realised if the investor can violate a great majority of the laws of the host state at the time of establishing the investment without facing a sanction on an international plane.
77. Besides, another defect that this approach suffers from is that it gives no test or benchmark according to which one can recognise the 'fundamental laws' of the host state. If, for instance, the legality requirement question before the tribunal is whether the violation of taxation laws of the host state at the time of making the investment would activate the 'in accordance with the laws clause', this approach does not give the tribunal seized of deciding the dispute a yardstick to determine whether the relevant taxation legal provisions allegedly violated fall within the scope of 'fundamental laws' of the host state.

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[120] See J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73) 534-535.

[121] See Article 12 of the Agreement between the Government of the Republic of Kazakhstan and the Government of the Republic of Uzbekistan on the Promotion and Protection of Investments, signed on 02 June 1997, entered into force on 08 September 1997. This was the underlying BIT in *Vladislav Kim and others v. Republic of Uzbekistan* (n 73).

[122] *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2).

[123] ibid [263].

[124] ibid.

[125] See, for instance, the Preamble of the Agreement between the Slovak Republic and the Islamic Republic of Iran for the Promotion and Reciprocal Protection of Investments, signed on 19 January 2016, not yet entered into force (stating at the fourth recital that the parties seek to "promote investment that contributes to the sustainable development of the Contracting Parties …"); the Preamble of the Agreement Between the Government of Canada and the Government of the People's Republic of China for the Promotion and Reciprocal Protection of Investments, signed on 09 September 2012, entered into force on 01 October 2014 (providing in its second recital that the parties recognise "the need to promote investment based on the principles of sustainable development.")

78. In sum, like the previous approach, the 'significance-analysis approach' also does not withstand proper interpretive scrutiny. In addition, the very concept of 'fundamental laws', though having a restrictive feature, is not a clear term and does not effectively help an investment treaty tribunal when faced with specifics in an actual case.

3rd. *Combined-Effect Analysis (Double Analysis of the Significance of the Host State Law Violated Together with the Behaviour of the Investor)*

79. Having reviewed the first two approaches, I now turn to the third and the most recent view on the 'substantive scope' of the legality requirement. As was alluded to above, in *Vladislav Kim and others v. Uzbekistan*,[126] in comparison to the previous approach, i.e., the 'significance analysis approach', the tribunal took one step further in making the 'substantive scope' of the legality requirement even more limited.

80. To query the factual matrix of the case, in 2005, 12 Kazakh investors (claimants in this case) intended to obtain majority shares in two cement plants (namely BC and KC) in Uzbekistan. In so doing, they concluded a complex Share Purchase Agreement ("SPA"),[127] the legality of which was a central matter of dispute between the parties in the subsequent investment treaty case. In the course of the following years, those investors bought further shares in BC and KC from minority shareholders to support their already acquired majority stakes in the cement plants.[128] These transactions together led the investors to ultimately hold an 83% shareholding in BC and an 89% shareholding in KC. The claimants argued that as of 2010, the cement plants (BC & KC) encountered 'a campaign of harassment by Respondent' in the form of criminal and regulatory investigations.[129] This so-called 'campaign', according to the claimants, resulted in a criminal sentence being rendered against BC and four of its managers. The claimants contended that according to this penal judgment, 51% of the capital stock of BC should be transferred to the Uzbek Government.[130] The claimants also argued that in the meantime, previous minority shareholders of KC, represented and espoused by the Government of Uzbekistan, succeeded in a domestic litigation in Uzbekistan to retrieve their stakes, on the ground that they had been forced by the Kazakh investors to sell their shares to them (equivalent to approximately 12% of KC stakes).[131] Countering the claimants' statement of the factual background, Uzbekistan offered a narrative of legally defective transactions concluded by the claimants, illicit payments, and duress.[132] According to the respondent, it was the illegal conduct of the investors in acquiring the shares in BC and KC that gave rise to the domestic criminal proceedings.[133] Therefore, Uzbekistan, *inter alia*, objected that the claimants' investment was not made in compliance with Uzbek legislation and that, therefore, such investment does not attract the protection of the Kazakhstan-Uzbekistan BIT.[134]

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[126] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74).

[127] ibid [128]-[131].

[128] ibid [135].

[129] ibid [138].

[130] ibid [139].

[131] ibid [140].

[132] ibid [142].

[133] ibid [149].

[134] ibid [171].

81. By the defence of illegality of the investment being raised by the respondent, the parties had a dispute regarding the 'substantive scope' of the legality requirement. They disagreed as to how the tribunal was to identify those acts of noncompliance to which the legality requirement applies.[135]
82. Analysing the specifics of the dispute before it, the tribunal began by asserting that a prevailing tendency in investment treaty jurisprudence had been to confine the legality requirement to breaches of 'fundamental laws' of the host state, and noted that previous *fora* have used 'rule-like statements' to formulate the legality requirement's scope of application.[136] However, the tribunal expressed discontent with the trend of setting forth 'rule-like statements', which it considered to be sometimes too alienated from the terms of the underlying investment treaties. Although it acknowledged that these 'rule-like statements' 'provide the comfort of certainty', the tribunal went on to consider such statements as sometimes unjustifiably either under-inclusive or over-inclusive.[137] Therefore, instead of adhering to these so-called 'rule-like statements', the tribunal purported to concentrate its survey on the specific legality requirement in the underlying BIT.[138] According to the tribunal, the 'bare bones language' of this requirement as prescribed by the underlying treaty required the application of a 'principle', as opposed to 'rules'.[139]
83. On that premise, the tribunal went on to opine that for the legality requirement to be triggered, it does not suffice for the law violated to be 'fundamental'. For this panel, in addition to the fundamentality of the law in question, the act of violation should also be flagrant or egregious, thus, requiring an even higher threshold for the coming into play of the legality requirement. In view of this tribunal, what triggered the legality requirement was "noncompliance with a law that results in a compromise of a correspondingly significant interest of the Host State". In this respect, the tribunal specifically stated:

> The phrase "noncompliance with a law that results in a compromise of a correspondingly significant interest of the Host State" is chosen so as to focus more sharply the substantive scope of the legality requirement not on whether the law is fundamental but rather on the significance of the violation. The Tribunal believes that the gravity of the law itself is a central part of the examination but not the sole focal point. It is not only the law, but the act of noncompliance (or in some wordings, the violation) that is key. The seriousness of the act is a combination of both the importance of the requirements in the law and the flagrancy of the investor's noncompliance. The text or standing of the law – although central – does not in and of itself determine whether the legality requirement is triggered. Rather, the law must be considered in concert with the particulars of the investor's violation. An investor may violate a law of some import egregiously or it may violate a law of fundamental importance in only a

[135] ibid [381].

[136] ibid [384].

[137] ibid [399].

[138] Agreement between the Government of the Republic of Kazakhstan and the Government of the Republic of Uzbekistan on the Promotion and Protection of Investments (n 121).

[139] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [399].

> trivial or accidental way. Seriousness to the Host State is to be determined by the overall outcome, which will depend on the seriousness of the law viewed in concert with the seriousness of the violation.[140]

84. In short, the *Vladislav Kim* tribunal adopted a three-step analysis: **first**, reviewing the significance of the domestic law allegedly violated; **second**, the seriousness of the alleged violation; and **third** whether the combination of these two elements "results in a compromise of a significant interest of the Host State to such an extent that the harshness of the sanction of placing the investment outside of the protections of the BIT is a proportionate consequence for the violation examined".[141]
85. Applying the above-mentioned analytical steps, the tribunal went through various illegalities alleged by Uzbekistan in that case. Specifically, Uzbekistan had contended four different alleged violations of Uzbek law by the investors in making their investment: (i) Fraud in violation of Uzbek Securities Law (in particular, in violation of Order No. 04-103 on "Regulations on the Prevention of Manipulation of the Stock Market" dated 25 June 1999); (ii) failure to register the English SPAs (in particular, in violation of Article 22 of Law No. 218-I); (iii) false disclosure and concealment in registering the Tashkent SPA; and (iv) fraud causing significant harm to the state, BC and KC minority shareholders, the Tashkent Stock Exchange ("TSE"), and the brokers. To see how the tribunal applied its three-step test in practice, and to set the scene for analysing the tribunal's benchmark regarding the 'substantive scope' of the legality requirement, in the ensuing paragraphs, I will go through the first two illegalities alleged by the respondent and how the tribunal addressed them.
86. As to the first alleged violation, i.e. fraud in violation of Uzbek Securities Law, the respondent's defence was based on the alleged illegality in the complicated agreements through which the investors obtained majority shares in BC and KC. This complex setting of transactions involved the conclusion of SPAs under English law for a purchase price of approximately US$34 million. The transaction also involved certain other share purchase agreements registered with the TSE disclosing only a purchase price of US$2.2 million rather than the actual price of US$34 million mentioned above. Uzbekistan contended that through this fraudulent mechanism, the investors manipulated the stock market in violation of Order No. 04-103 which "[p]rohibits any market participants from [p]erform[ing] any act aimed at artificially inflating/underpricing of securities, the product of a false or misleading impression of active trading in order to induce third parties to buy/sell securities at a bargain price for the manipulators", and also provides that "[a] member (group members) of the securities market and/or their customers do not have the right to conclude a transaction of sale and purchase of a particular type of security on the basis of mutual agreement, with the intent to mislead other market participants".[142] According to the claimants, the structure they used was necessary because the legal framework of Uzbekistan was in a state of development at the time. They

[140] ibid [398]. See also ibid [404]. At paragraph 399 of the Decision, the tribunal specified its goal for setting up the above-mentioned principle by stating that it "does not so much seek to increase the scope of acts captured as a practical matter by existing rule-like statements but rather aims to identify the underlying principle that can provide a more nuanced definition of the limits of the acts of noncompliance that would trigger the legality requirement." See ibid, [399].

[141] ibid [405]-[408].

[142] ibid [426].

also noted that this structure was recommended to them by their broker and the seller of the shares.[143]

87. By a majority, the tribunal held that this alleged violation, i.e. the difference between the transaction's registered and actual price, was not "as egregious as Respondent alleges".[144] The most important factor for the tribunal in reaching its decision in this respect was that Uzbekistan could prove no intention to defraud on the claimants' part. In fact, although the majority admitted that the claimants registered an 'incorrect' price on the TSE,[145] to them, this "deliberate act of entering a false price on the exchange" was not equivalent to the existence of an intention to defraud or manipulate the market.[146] On the other hand, in an ensuing paragraph, the minority opined that the investors' conduct, falls within the definition of the term 'fraud' as understood in Uzbek law, and was a very serious violation, given the existence of a public reporting requirement integral to the operation of an exchange. The minority was also of the view that in order to secure the deal, the claimants intended the market to be given misleading information.[147]
88. The second alleged violation of the laws of the host state concerned the investors' alleged failure to register 'English law' SPAs. Uzbekistan argued that, in accordance with Article 22 of Law No. 218-I, the English SPAs should have been registered with the TSE.[148] On the contrary, the claimants asserted that the English SPAs were not subject to this registration obligation.[149] The tribunal, by majority, doubted whether such registration was necessary under Uzbek law.[150] In any event, it held that the alleged breach was not sufficiently significant to trigger the legality requirement. This holding was principally based on the severity of sanctions Uzbek law had determined for the failure to register. The parties disagreed as to the sanction specified in one of the laws (Order No. 2003-08) for failure to register. The majority, taking side with the claimants, held that the more appropriate translation of the Order provided for the 'invalidity' of the transaction, rather than rendering such transaction 'null and void'.[151] According to the majority, invalidity signified a milder sanction which represented the lower importance of the law.[152] Having concluded that the sanction of 'invalidity' does not herald a serious breach, the majority concluded that "such an act of noncompliance does not result in a

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[143] ibid [429]-[430].

[144] ibid [428]. The tribunal noted that the investment was made in a "highly uncertain legal environment, in which the applicable legal regime was unclear, difficult for any reasonable investor to ascertain, subject to change and still evolving", and that the investors acquired BC and KC in good faith to develop them. ibid [429], [432].

[145] ibid [437]. In this respect, the tribunal mentioned that it "accepts to an extent Claimants' argument that the English SPAs do more than the Tashkent SPAs in terms of gaining a "control Premium" and granting various rights such as a choice of law and choice of court agreement. But those additions in the Tribunal's opinion can't explain fully the difference between the price paid by Claimants in the English SPAs and the price recorded on the Tashkent SPAs." See ibid [483]. See also ibid [503].

[146] ibid [439].

[147] ibid [440].

[148] ibid [442].

[149] ibid [443].

[150] ibid [445].

[151] ibid [460]-[462].

[152] ibid [463]-[464]. In this connection, the majority also noted that the claimants' expert testifying on this point had a legal background whereas the respondent's expert had his background in economics. It also took into consideration the fact that the respondent did not call and cross-examine the claimants' expert.

compromise of an interest of sufficient significance so as to render proportionate the exclusion of the investment from the protections of the BIT."[153] On the other hand, the minority was of the view that the sanction of 'invalidity' for failure to register could not downgrade the seriousness of the investors' deliberate failure to observe Uzbek laws.[154]

89. Other alleged violations of Uzbek law were also dismissed by the majority for the reason that they could not trigger the legality requirement of the underlying investment agreement. Having applied its test to the various illegality allegations raised by the respondent, the majority of the tribunal concluded that Uzbekistan "either has failed to establish that claimants acted in noncompliance with various laws or that such acts of noncompliance do not result in a compromise of an interest that justifies, as a proportionate response, the harshness of denying application of the BIT."[155]
90. Having reviewed the test set out by the *Vladislav* tribunal and the way the test was applied by that tribunal, in the following paragraphs, I will analyse the appropriateness of this test as a benchmark for determining the 'substantive scope' of the legality requirement.
91. **First**, as with the two previous approaches, it seems that the test put forward by the *Vladislav* tribunal is by no means supported by 'the ordinary meaning of the terms' of the legality requirement, nor does the tribunal ultimately so contends. Nowhere does a typical legality requirement confine itself to violations of 'fundamental laws' of the host state. Furthermore, on its face, a typical legality requirement does not place emphasis on the seriousness of the violation on the part of the investor for the activation of the requirement. Therefore, this approach is not supported by 'the ordinary meaning of the terms' of a typical legality requirement.
92. **Second**, to be precise, the 'substantive scope' of the legality requirement has to do with *confining the laws that should be complied with* in the course of initiating the investment, not determining the boundaries of acts of non-compliance.[156] Put differently, the question, in fact, is the scope of the 'legality' requirement, i.e. the 'legal' provisions that should be complied with. Thus, in my opinion, it is not accurate to say that the 'substantive scope' of the requirement concerns determining the types of acts of non-compliance. Whereas, the former view (focus on laws rather than acts) concentrates on the laws of the host state that should be abided by, the latter standpoint (focus on acts rather than laws) pays particular attention to the behaviour of the investor, and, as a result, the 'intentions' of the investor.[157] Thus, inevitably,

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[153] ibid [464].

[154] ibid [465].

[155] ibid [541].

[156] In this respect, see M Polkinghorne & SM Volkmer (n 90) 149, 160 (saying that: "The legality requirement's subject-matter scope determines which of the host State's laws a tribunal should take into account when assessing the investment's legality.")

[157] At paragraph 403 of its Decision, the *Vladislav* tribunal admits to some extent that taking into account the investor's motives could be considered as a factor in the activation of the legality requirement:

> For this Tribunal, focusing on the seriousness of non-compliance, both in terms of the seriousness of the law and the action taken by the investor, *makes the good faith of the investor something that is considered as a factor in the overall assessment of the proportionality between the violation and the sanction*. An action in good faith possibly may render an act of noncompliance less serious, but – depending on the seriousness of the law violated – not necessarily. It may be that the law alleged to be violated has as an element of a violation that bad faith or a specific intent is required. Likewise, it may be

in most instances, a tribunal has to engage in ascertaining the investor's subjective 'motive' or 'intention' for committing the illegality and try to discover the possible *mens rea* of the investor which is really a criminal proceedings' assignment.[158] [159] The task of an investment treaty tribunal is not to establish the committing of a crime or imposing criminal punishments on the recalcitrant investor, but rather to establish whether host state law has, in fact, been breached.[160] Of course, in case a deliberate violation is found, the finding of illegality would be more robust

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> that the law alleged to be violated provides an exception if the act is undertaken in good faith when, for example, due diligence is exercised. [emphasis added]

See *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [403]. See also ibid [469]-[475]. Further, the tribunal includes the role the investor's intention can play in determining the significance of the violation by asking the following test questions:

> What does the investor's intent suggest as to the seriousness of the investor's conduct? Where a particular state of mind is not required for the violation, does the intentionality of the investor's conduct suggest a more egregious act? In contrast, does an act of noncompliance that is mere accident suggest a less egregious act? Whether intent as an aggravating factor, or lack of intent as an excuse, is to be considered may be indicated by the law itself.

See ibid [407], second bullet point.

[158] On this point, Carlevaris aptly points out that it "is in fact more difficult to determine the investor's good faith and knowledge of the causes of the illegality than the identity of the norms allegedly violated and the seriousness of the breach." See A Carlevaris (n 7) 47. In the same vein, Knahr commentates that a subjective assessment "seems problematic since it will probably be difficult in many instances to determine whether an investor had actually acted in good faith or whether he had knowingly committed a violation of a host state's domestic law. Hence, an objective assessment of the severity of the violation … seems preferable." See C Knahr (n 7) 17.

[159] Of course, in cases where the relevant legal provision of the law of the host state requires the existence of an 'intention' as a condition for the consummation of a crime or wrongdoing and as a requisite for the imposition of criminal or legal sanctions, the tribunal has to ascertain the required 'intention'. Nonetheless, as explained below, this should not transform an investment treaty tribunal into a national criminal court. In most, if not all cases, the investor is sophisticated enough not to commit a notable illegality unintentionally. Talking in the context of corruption, Llamzon quite correctly suggests that investors acting in this way always know the illegality of their actions yet decide to engage in corruption anyway, either overtly or tacitly. AP Llamzon (n 8) 5. In this connection, the minority in *Vladislav Kim* also observed that one reason showing that the actual purchase price of the shares was intentionally concealed from the Exchange was that the investors were "highly sophisticated international businessmen, with no doubt intimate knowledge of such matters." See *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [476]. In case doubt arises as to the intentional or unintentional nature of the actions or omissions of a sophisticated investor in cases where the presence of intention is a condition of the consummation of a wrongdoing, the more appropriate standard of proof to be applied by an arbitral tribunal is 'circumstantial evidence'. In this respect, in connection with the existence of corruption, a plainly significant criminal label, the tribunal in *Metal-Tech v. Uzbekistan*, relying on paragraph 303 of the *Oostergetel* Award, remarked that it would "determine on the basis of the evidence before it whether corruption has been established with reasonable certainty. In this context, it notes that corruption is by essence difficult to establish and that it is thus generally admitted that it can be shown through circumstantial evidence." *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [243]. The *Oostergetel* tribunal had earlier observed that "[f]or obvious reasons, it is generally difficult to bring positive proof of corruption. Yet, corruption can also be proven by circumstantial evidence." See *Jan Oostergetel and Theodora Laurentius v. The Slovak Republic*, UNCITRAL, Final Award, 23 April 2012 [303]. Consequently, if in such cases, an investment treaty tribunal can ascertain the intention of the investor to commit the illegality with 'reasonable certainty' by reference to 'circumstantial evidence', it has properly carried out its arbitration assignment.

[160] In this connection, Pierre Mayer points out that "[a]n arbitrator who declares an illegal contract to be null does not usurp the role of guardian of public order; he does not even *sanction* - in the sense of punishment – conduct he deems to be illicit. Rather, what he does is to recognise the illicitness as such, and likewise recognise the nullity which is its result; in sum, he only *states the law*, which is part of his normal duty." [emphases in the original text] See P Mayer, 'Mandatory Rules of Law in International Arbitration' (1986) 2 Arb Int'l 278.

from an equity perspective. However, as will be later explained in this Chapter, lack of intention of the investor in breach of the laws of the host state does not excuse the investor's illegality.[161]

93. A possible pitfall of the *Vladislav* tribunal's proposed test would be that, if proven to be unintentional, even significant violations of mandatory laws of the host state could be excluded from the capture of the legality requirement, a result that is very hard to be ascribed to the intention of state contracting parties to an investment treaty. For instance, if the foreign investment cap in infrastructural projects in country "A" is 50%, and the foreign investor, allegedly unaware of this mandatory legal limitation, acquires directly and indirectly 60% of the shares of the project company, under this test, it could be still absolved from this illegality because of its lack of bad faith.[162]
94. **Third**, the *Vladislav* tribunal considered the possibility that a significant law could be breached in a 'trivial' way. As a result, it concluded that not every violation of fundamental laws of the host state could trigger the legality requirement.[163] To me, it is hardly conceivable that a 'fundamental law' could be violated in a 'trivial' way. In fact, when a fundamental law is breached, the breach cannot be characterised as 'trivial': such a breach remains a 'breach' which cannot be classified severity-wise. To illustrate the point, two examples will be given below: **One**: suppose that according to foreign investment law of country "A", the foreign investment participation cap in the sanitation sector is 49.99%. It is clear that provisions regarding foreign investment cap are fundamental.[164] Now, suppose that investor "B", in violation of that law, acquires 50% of the shares of a joint venture project company in the

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[161] As the tribunal in *Alasdair Ross Anderson v Republic of Costa Rica* said, each investor "must meet [the legality] requirement, regardless of his or her knowledge of the law or his or her intention to follow the law". *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [52]. In other words, the intention of the investor and his/her knowledge of the laws and regulations of the host state at the time of making the investment have no role to play in the consideration of compliance with the legality requirement, unless the law allegedly violated stipulates the requirement of 'intention'. See also C Knahr (n 7) 17.

[162] In this respect, the very concept of 'mitigating factors' used by the tribunal (see *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [448]), referring to the obscurity and instability of the host state law and good faith of the investor is an inapposite use, not only because 'mitigation' as a term of art is not used for issues of responsibility, but is designed and intended to exonerate the non-performing party from 'liability for harm suffered by the aggrieved party to the extent that the harm could have been reduced by the latter party's taking reasonable steps' (For the definition of mitigation see UNIDROIT Principles Of International Commercial Contracts 2016, Article 7.4.8 (Mitigation of Harm)), but also since topics like 'good faith' or 'the obscurity of the laws of the host state' are only defences that could be raised against a committed illegality, not issues that should be analysed when considering whether the illegality itself has occurred. Cf *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) fn 405.

[163] ibid [398].

[164] Referring, *inter alia*, to the regulation of limiting equity investment to a specified maximum percentage of voting control in an enterprise in a given sector, Salacuse opines that the policy assumptions behind such regulation "is that government control of the entry by foreign investment in particular sectors is necessary to protect important national interests, such as national security or strategic economic industries." See JW Salacuse (n 6) 92. According to Salacuse, the prohibitions and limitations usually apply in sensitive industries, like armaments, telecommunications, power generation and distribution, transportation, and the exploitation of petroleum and natural resources. See ibid 93. On this point, in *Phoenix*, the tribunal found: "In the Tribunal's view, States cannot be deemed to offer access to the ICSID dispute settlement mechanism to investments made in violation of their laws. If a State, for example, restricts foreign investment in a sector of its economy and a foreign investor disregards such restriction, the investment concerned cannot be protected under the ICSID/BIT system. These are illegal investments according to the national law of the host State and cannot be protected through an ICSID arbitral process." See *Phoenix Action Ltd v. Czech Republic* (n 39) [101].

sanitation sector, and investor "C" acquires 70% of another project company in the same field. Although the level of non-compliance is different, both investors "B" and "C" have violated a fundamental law. Indeed, no one could say that by only acquiring %00.01 extra to the lawful cap, investor "B" has violated the law in a 'trivial' way. **Two:** assume that the tender regulations of the host state, in a mandatory provision, require foreign bidders not to: (a) have any existing project in the host state in the related economic field at the time of bidding; (b) have any active project in the countries with which the host state does not have normal political ties at the time of bidding; and (c) have shareholders or stakeholders who are nationals, citizens, or residents of countries with which at the time of bidding the host state does not have normal political and economic ties. Suppose that despite assuring that none of these conditions apply to them, the winner of the bid disregards only the first, and the runner-up, all the three legal conditions. Although the severity of non-compliance differs in the two cases, the violation by the 'winner' cannot be characterised as 'trivial' since it is still a violation of a fundamental requirement of a law of great importance to the host state.

95. **Fourth**, as frequently emphasised by the *Vladislav* tribunal,[165] the test of 'proportionality' was the most important gist behind the principle set by the tribunal for determining the 'substantive scope' of the legality requirement. After conducting a comparative study, Bucheler concludes that 'proportionality' may constitute a 'general principle of law' under Article 38(1)(c) of the ICJ Statute that may be relevant to the construction of investment treaties.[166] However, in the application of this principle, he warns against the risk of arbitrary outcomes due to uncertainty as to what interests matter in a proportionality analysis and what weight they carry in adjudicating an international dispute. In this respect, he makes a right comparison between domestic law and international law by noting that value orders provided by internal constitutions alleviate the concern on the domestic level, while international law might not have a unitary system comparable to that of a domestic situation to determine the importance and the weight of the interests at stake.[167] The admonished risk is very well present here. The *Vladislav* tribunal has given specific weight to the interests of the investor,[168] while not giving an equivalent weight to the interests of the host state. In addition, whereas the interests of the investor have been highlighted in this Decision, their duty to observe and respect the laws of the host state in the process of making the investment has been given short shrift. The tribunal states, "[t]he denial of the protections of the BIT is a harsh consequence ..."[169] That is definitely correct. One should, however, be mindful that benefiting from investment treaty protection is

[165] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [396]-[397], [400]-[404], [408], [413].

[166] G Bucheler, *Proportionality in Investor-State Arbitration* (OUP 2015) 82-83.

[167] ibid 66.

[168] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [393]-[396].

[169] ibid [396].

also a great advantage.[170] This amazing package of substantive and procedural protections should not be granted to any investor, but just to eligible investors with clean-hands.[171]

96. **Fifth**, the test offered by the *Vladislav* tribunal is very difficult to apply in certain circumstances involving serious violations of host state law, like criminal code provisions on the prohibition of fraud. For this very reason, when applying the test it devised in the general part to specific illegality allegations raised by Uzbekistan, the majority had to admit that the illegality of fraud was serious enough to trigger the legality requirement, and that the good faith of the investor and the uncertainty in the legal system of the host state "would not, of themselves, be exculpatory for a Claimant whose noncompliance with a Host State law inherently was of sufficient seriousness to render proportionate the loss of treaty protection."[172] Therefore, the *Vladislav* tribunal admitted that in certain situations the fundamentality of the law in question is the end of the matter, and that the adjudicating forum should not go further and inquire about the subjective motives of the investor in violating the legal provision(s) of the host state or examine the contemporaneous transparency of the law of the host state.
97. **Finally**, as admitted by the *Vladislav* tribunal,[173] the principle as suggested by it is very 'case-specific'. Such an intensively 'fact-based' test does not create sufficient clarity, certainty, stability, and predictability desired by both states and investors.[174] Such an intensively fact-based principle would not also facilitate decision-making for investment treaty tribunals.
98. Based on the foregoing, the test devised by the *Vladislav* tribunal is not the most appropriate test one can craft for drawing the 'substantive' borders of the legality requirement. That said, the tribunal's novelty and thoroughness in dealing with this matter should be greatly admired and appreciated.

### ii. The Proposed Solution

99. Having reviewed all the viewpoints on the 'substantive scope' of the legality requirement, in the following pages, I will offer my own point of view regarding the 'substantive' reach of this condition.

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[170] In this respect, Bucheler says that "[t]hrough a combination of substantive treaty protections, procedural tools, and robust enforcement mechanisms, the current system of investor-State arbitration constitutes one of the most effective means for the protection of non-State actors in international law." G Bucheler (n 166) 301. See also T Gazzini, *Interpretation of International Investment Treaties* (Hart Publishing 2016) 39, 49 (stating that: "[investment treaties] ensure foreign investors an increasingly sophisticated legal protection both in terms of normative standards and procedural remedies, without imposing on them any obligation … investment treaties amounted to a normative break-through as these treaties may pave the way to the direct access by the investor to international tribunals.") In this respect, referring to the dispute settlement clause of the ECT, the *Plama* tribunal mentions that: "By any standards, Article 26 is a very important feature of the ECT which is itself a very significant treaty for investors, marking another step in their transition from objects to subjects of international law…" and that: "…for a covered investor, Article 26 is a very important feature of the ECT; and as a remedy exercisable by an investor by itself and in its own right against the host state ... Under the ECT, the covered investor is more than an object of international law …" *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 08 February 2005 [141], [150].

[171] On this point, the *Mamidoil* tribunal correctly points to the fact that in "exchange for their acceptance to enter into investment treaties and giving their consent to the resolution of investment disputes by arbitral tribunals, States expect that such protection would extend only to investments that have been made lawfully." See *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania* (n 43) [291].

[172] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [435].

[173] ibid [400].

[174] See (n 77 *supra* and the accompanying text).

100. A typical legality requirement reads: ""investment" means any kind of asset owned or controlled either directly, or indirectly through an enterprise or natural person of a third State, by an investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's laws."[175] By a mere 'textual' or 'literal' approach to treaty interpretation,[176] by looking only at the 'ordinary meaning of the terms' of the legality requirement in the context in which they usually appear, one has to take sides with the argument of host states who frequently posit that legality requirement extends to any breach of any law of the recipient state.[177] Put differently, the position of host states is supported by the generic and unqualified use of the terms 'laws', 'legislation', and 'regulations' without any attributes, particularisation or specification of such 'laws', 'legislation' or 'regulations' in the legality requirement.

101. However, treaty interpretation is a combined exercise in which all the tools and elements of interpretation should be analysed and weighed together.[178] Therefore, together with the

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[175] See Article 1(g) of the Agreement between the Government of the Republic of Costa Rica and the Government of Canada for the Protection and Promotion of Investment (n 15). This was the underlying BIT in *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9).

[176] Fitzmaurice has distilled 6 principles of treaty interpretation from the practice of the International Court of Justice from 1951 to 1954. The first and the second of such principles are the 'principle of actuality (or textuality)' and 'natural meaning'. According to the first principle, "texts must be interpreted as they stand, and, *prima facie*, without reference to extraneous factors" and according to the second principle, "[p]articular words and phrases are to be given their normal, natural, and unstrained meaning, in the context in which they occur." See G Fitzmaurice, 'The Law and Procedure of the International Court of Justice 1951-1954: Treaty Interpretation and Other Treaty Points' (1957) 33 BYIL 203, 211-213.

[177] For instance, in *Saba Fakes v. Turkey*, the respondent contended that any violation of any of the host state's laws would result in the illegality of the investment within the meaning of the BIT, and would preclude such investment from benefiting from the substantive protection offered by the BIT. See *Saba Fakes v. Republic of Turkey* (n 69) [119]. In the same vein, in *Quiborax v. Bolivia*, the respondent asserted that the legality requirement in the underlying BIT covered all the laws and regulations of the recipient state. Specifically, Bolivia contended that the Bolivia-Chile BIT "does not draw a distinction between serious and non-serious breaches of the laws; it covers both alike". See *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [240]. See also T Obersteiner (n 91) 276.

[178] It should be borne in mind that Article 31 of the VCLT entails the 'rule' of interpretation of treaties: all the means of interpretation referred to in this provision should be considered in totality, as the "process of interpretation is a unity". The Report of the International Law Commission is instructive in this respect: "Having regard to certain observations in the comments of Governments, the Commission considered it desirable to underline its concept of the relation between the various elements of interpretation in article 27 [now Article 31] and the relation between these elements and those in article 28 [now Article 32]. Those observations appeared to indicate a possible fear that the successive paragraphs of article 27 might be taken as laying down a hierarchical order for the application of the various elements of interpretation in the article. The Commission, by heading the article "General rule of interpretation" in the singular and by underlining the connexion between paragraphs 1 and 2 and again between paragraph 3 and the two previous paragraphs, intended to indicate that the application of the means of interpretation in the article would be a single combined operation. All the various elements, as they were present in any given case, would be thrown into the crucible, and their interaction would give the legally relevant interpretation. Thus, article 27 is entitled "General rule of interpretation" in the singular, not "General rules" in the plural, because the Commission desired to emphasize that the process of interpretation is a unity and that the provisions of the article form a single, closely integrated rule. In the same way the word "context" in the opening phrase of paragraph 2 is designed to link all the elements of interpretation mentioned in this paragraph to the word "context" in the first paragraph and thereby incorporate them in the provision contained in that paragraph. Equally, the opening phrase of paragraph 3 "There shall be taken into account together with the context" is designed to incorporate in paragraph 1 the elements of interpretation set out in paragraph 3. …" Report of the International Law Commission on the Work of Its Eighteenth Session, Geneva, 4 May-19 July 1966 (1966) (Vol. II) YB ILC 219-220. See also *Aguas del Tunari, S.A. v. Republic of Bolivia*, ICSID Case

'text' and 'the ordinary meaning of the terms' in their 'context', one should also take into account the 'object and purpose' of the treaty. In addition, a treaty should always be interpreted in 'good faith'.[179]

102. With this important interpretive observation in mind, in determining the 'substantive scope' of the legality requirement, one has to appreciate the 'object' of the treaty, i.e., the economic operation as to which the legality requirement should be applied. This economic operation is international investment. International investment is a complex process.[180] In such a complicated process, involving numerous transactions, various formal and administrative procedures, and the necessity to deal with many public authorities over a good period of time, inadvertent mistakes could be made, thus violating certain laws and regulations of the host state which are not of vital importance or of mandatory nature.

103. Bearing this important point in mind, two of the most frequently stated 'purposes' of investment treaties are 'creating conditions which are favourable for investments' and 'stimulating private business initiatives'.[181] Such purposes would definitely be defeated if protection under the very same agreement were to be denied due to very small mistakes and mere technicalities that may understandably occur in such a complex process and are in most instances 'curable'.[182]

104. By now it has become clear that focusing merely on the text of the requirement does not lead one to safe waters. Indeed, paying heed to the 'object' and 'purpose' of investment treaties

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No. ARB/02/3, Decision on Respondent's Objections to Jurisdiction, 21 October 2005 [91] (aptly observing that: "Interpretation under Article 21 [sic] of the Vienna Convention is a process of progressive encirclement where the interpreter starts under the general rule with (1) the ordinary meaning of the terms of the treaty, (2) in their context and (3) in light of the treaty's object and purpose, and by cycling through this three step inquiry iteratively closes in upon the proper interpretation.")

[179] See *Abaclat and Others v. Argentine Republic*, ICSID Case No. ARB/07/5 (formerly *Giovanna a Beccara and Others v. The Argentine Republic*), Decision on Jurisdiction and Admissibility, 04 August 2011 [646] (stating that: "The principle of good faith is a fundamental principle of international law, as well as investment law.")

[180] See *Ceskoslovenska Obchodni Banka, A.S. v. The Slovak Republic*, ICSID Case No. ARB/97/4, Decision of the Tribunal on Objections to Jurisdiction, 24 May 1999 [72] (indicating that "An investment is frequently a rather complex operation, composed of various interrelated transactions, each element of which, standing alone, might not in all cases qualify as an investment"); *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3 (also known as: *Enron Creditors Recovery Corp. and Ponderosa Assets, L.P. v. The Argentine Republic)*, Decision on Jurisdiction, 14 January 2004 [72] (noting that "an investment is indeed a complex process including various arrangements, such as contracts, licences and other agreements leading to the materialization of such investment, a process in turn governed by the Treaty"); *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Dissenting Opinion of Mr. Bernardo M. Cremades, 19 July 2007 [36] (stating: "Foreign investment occurs within a sophisticated legal framework of foreign ownership, tax, antitrust, administrative, labour, environmental and other regulations as well as the law relating to obligations arising directly from contractual relations.") In this respect, two commentators have correctly observed that "[a]n investment is often a process rather than an instantaneous act." They also note that "a typical investment is not a simple event. An investment operation is often composed of a number of diverse transactions and activities, which must be treated as an integrated whole. Therefore, an investment is a complex process involving diverse transactions which have a separate legal existence but a common economic aim". See C Schreuer & U Kriebaum, 'At What Time Must Legitimate Expectations Exist?' in J Werner & A Heydar Ali, *A Liber Amicorum: Thomas Wälde: Law Beyond Conventional Thought* (CMP Publishing 2009) 269-270.

[181] See R Dolzer & M Stevens (n 33) 20-21 (referring to the Preamble of the Treaty between the Federal Republic of Germany and the Kingdom of Swaziland concerning the Encouragement and Reciprocal Protection of Investments, signed on 05 April 1990, entered into force on 07 August 1995.)

[182] For the 'curability' of an illegality and its effect on the activation of the legality requirement, see *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania* (n 43) [494].

shows that one should not be entangled in a mere 'textual' impasse in the interpretive exercise. To get rid of this 'textual' predicament, some have suggested that rather than 'the ordinary meaning of the terms', the boundaries of the requirement can be identified by reference to the 'object and purpose' of the treaty.[183] The 'object' and 'purpose' of investment treaties are usually recorded in their preambles.[184] Several objectives are referred to in the preambles of investment treaties, the most conventional of them being: "(a) the general desire of the parties to intensify and to develop their economic relations; (b) … the need to create conditions which are favorable for investments of nationals of either State in the territory of the other State; and (c) the conviction that the protection of such investments will lead to the stimulation of private initiative and to the promotion of the prosperity of both States concerned."[185] One investment treaty tribunal has indicated that one could get assistance from some of these objectives to distinguish the contours of the legality requirement. Thus, in the context of interpreting Article 12 of the BIT between Kazakhstan and Uzbekistan on "Application of the Agreement",[186] entailing a legality requirement, the *Vladislav* tribunal made reference to some of the goals mentioned in the Preamble of that BIT and noted:

> It is the combination of desiring to "promote greater economic cooperation" and the fact that an act not in compliance with legislation under Article 12 excludes an investment from the scope of application of the BIT generally, that indicates the necessary substantive limits on the legality requirement. Given the aim of encouraging investment through the provision of some measure of security, it is not plausible that the drafters of the BIT intended to include minor acts of noncompliance as a basis for denying jurisdiction.[187]

105. Of course, the purposes of a treaty as recorded in its preamble can be used to shed light on the scope of the legality requirement to some extent, i.e., to exclude from the legality requirement the violation of *de minimis* laws of the host state. Preambles, nonetheless, cannot serve a tribunal when specific and more difficult jurisdictional questions arise. Preambles in investment agreements are usually written in a much generalised pattern that one could hardly grasp any specific – in contrast to general – interpretation use for jurisdictional purposes from the recitals recorded therein. In *HICEE v. Slovak Republic*, in interpreting the phrase "invested

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[183] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [391]-[394].

[184] Several tribunals have considered the objectives of investment agreements to be recorded in their preambles. See, for example, *Siemens A.G. v. The Argentine Republic*, ICSID Case No. ARB/02/8, Decision on Jurisdiction, 03 August 2004 [81] (saying: "The Tribunal shall be guided by the purpose of the Treaty as expressed in its title and preamble"); *Continental Casualty Company v. The Argentine Republic*, ICSID Case No. ARB/03/9, Decision on Jurisdiction, 22 February 2006 [80] (saying that the interpretation it arrives at is supported "by the object and purpose of the BIT". For displaying the object and purpose of the BIT, the tribunal goes on to cite certain recitals of the BIT Preamble.)

This is, of course, not to suggest that the 'object and purpose' of investment agreements are exclusively recorded in their preambles. The title of the agreement, its opening articles, as well as other agreements or instruments forming the context of the treaty remain relevant. See T Gazzini (n 170) 157-158.

[185] See R Dolzer & M Stevens (n 33) 20-21. See also UNCTAD, *Bilateral Investment Treaties 1995–2006: Trends in Investment Rulemaking* (n 11) 3-4.

[186] Article 12 of the Agreement between the Government of the Republic of Kazakhstan and the Government of the Republic of Uzbekistan on the Promotion and Protection of Investments (n 121).

[187] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [394].

either directly or through an investor of a third State", the tribunal considered the investor's jurisdictional argument that the terms used in the Preamble of the BIT between the Netherlands and Slovak Republic[188] show that the Parties intended the scope of the Agreement to be broad and inclusive, rather than narrow:

> In the Tribunal's view, the wording chosen for the Preamble by the Parties is studiously neutral, and refers more to the goal of the stability of expectations than to any preconception as to the Agreement's coverage and scope. The Tribunal observes that, in general, the purpose of bilateral investment treaties can be taken to be the encouragement of investment, on a mutual and reciprocal basis, while balancing the interests of the investors and of the receiving State in that regard; in and of itself, however, that says nothing about where the balance has been drawn in the particular treaty in question […] The Tribunal does not therefore find anything in the object and purpose of the present Agreement that would help in any material way to determine the question of interpretation before it.[189]

106. In a similar vein, in *Plama v. Bulgaria*, the claimant had, *inter alia*, placed much reliance on the object and purpose of the Bulgaria-Cyprus BIT to broaden the scope of the MFN clause of the treaty,[190] which provides in its Preamble that one of the goals of the treaty is "the creation of favourable conditions for investments by investors of one Contracting Party in the territory of the other Contracting Party." The tribunal declined to grant this stated purpose as reflected in the Preamble of the BIT a high weight in interpreting the MFN clause. It observed that:

> Such statements are as such undeniable in their generality, but they are legally insufficient to conclude that the Contracting Parties to the Bulgaria-Cyprus BIT intended to cover by the MFN provision agreements to arbitrate in other treaties to which Bulgaria (and Cyprus for that matter) is a Contracting Party. Here, the Tribunal is mindful of Sir Ian Sinclair's warning of the "risk that the placing of undue emphasis on the 'object and purpose' of a treaty will encourage teleological methods of interpretation [which], in some of its more extreme forms, will even deny the relevance of the intentions of the parties".[191]

107. By the same token, more recently, in *Government of the Lao People's Democratic Republic v. Sanum Investments Ltd*, the High Court of Singapore, held that: "[i]t is a truism to say that the purpose of any BIT is to promote investments. But it does not follow from this general

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[188] See the Preamble of the Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic (n 35).

[189] *HICEE B.V. v. The Slovak Republic*, UNCITRAL, PCA Case No. 2009-11, Partial Award, 23 May 2011 [116].

[190] Agreement between The Government of the People's Republic of Bulgaria and The Government of the Republic of Cyprus on Mutual Encouragement and Protection of Investments, signed on 12 November 1987, entered into force on 18 May 1988.

[191] *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction (n 170) [193] (referring to I Sinclair, *The Vienna Convention on the Law of Treaties* (Manchester University Press 1984) 130.)

proposition that every ambiguity found in such treaties should invariably be resolved in favour of the investor."[192]

108. Finally, in *Saluka v. Czech Republic*, the tribunal had before it the preambular language in the Czech-Netherlands BIT. The Preamble set out the objectives of the Treaty in the following terms:

> Desiring to extend and intensify the economic relations between [the Contracting Parties] particularly with respect to investments by the investor of one Contracting Party in the territory of the other Contracting Party,
> Recognizing that agreement upon the treatment to be accorded to such investments will stimulate the flow of capital and technology and the economic development of the Contracting Parties and that fair and equitable treatment is desirable…[193]

109. In a famous comment, the tribunal noted that one cannot merely rely on these generally stated purposes to tilt towards the benefits of the investor to the detriment of the rights of the host state. Instead, the tribunal emphasised on the necessity of adopting a 'balanced approach' in interpreting the treaty:

> … 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 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.[194]

110. The necessity to have a 'balanced approach' to treaty interpretation is more nuanced when interpreting the legality requirement. Referring to the positions of the parties concerning the

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[192] *Government of the Lao People's Democratic Republic v. Sanum Investments Ltd*, Judgment of the Singapore High Court, 20 January 2015 [2015] SGHC 15 [124].

[193] Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic (n 35).

[194] *Saluka Investments B.V. v. The Czech Republic* (n 36) [300]. Similarly, Gazzini opines that: "International investment treaties pursue two main objectives. On the one hand, they aim to stimulate the flow of foreign investment and create a stable and predictable environment for their management; on the other hand, they promote the economic development of the host State and the co-operation between the States concerned." T Gazzini (n 170) 34. He also comments elsewhere that "when the treaty aims to pursue more than one objective, the interpreter must take them all into account to the extent they are relevant, in a balanced and unbiased manner." ibid 161. See also ibid 163. Additionally, see *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15, Decision on Jurisdiction, 27 April 2006 [70] (stating that: "This Tribunal considers that a balanced interpretation is needed, taking into account both State sovereignty and the State's responsibility to create an adapted and evolutionary framework for the development of economic activities, and the necessity to protect foreign investment and its continuing flow."); *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Award, 14 July 2006 [307].

'substantive scope' of the legality requirement which really represented the two ends of the spectrum: a very narrow interpretation by the investor and a very expansive interpretation by the state, the *Quiborax* tribunal gave its word to none and recalled the fundamentality of a 'balanced approach' in drawing the lines of the legality requirement:

> The Parties disagree about the scope of the legality requirement. The Claimants advocate a narrow reading of this requirement limited to breaches of fundamental legal principles or of the investment regime. The Respondent opposes an expansive construction encompassing any breach of its legal order irrespective of its seriousness or timing. The Tribunal is of the opinion that neither interpretation is entirely correct, the interpretation of the Claimants being too narrow and that of the Respondent too broad. The Claimants' interpretation goes beyond the terms of the BIT, in an attempt to further the investor's protection without due regard for the State's interests. By contrast, the Respondent's expansive view neglects the investor's interests with the result that an investment could be deprived of any treaty protection for any breach of the host State's legal order – however slight – committed at any time. This approach would create deleterious incentives, as host States would be in a position to strip investors of treaty protection by finding any minor breach at any time.
>
> Neither view is consistent with the objectives of the BIT, the Preamble of which states that the Parties "recogniz[e] the need to promote and protect foreign investments in order to support the economic prosperity of both States" and "wish[] to strengthen the economic cooperation to benefit both States." […] Accordingly, within the limits set by the applicable treaty interpretation rules, the Tribunal favours a balanced interpretation that takes account of the need to protect foreign investments, on the one hand, and of the State's other responsibilities, on the other.[195]

111. To draw the threads from these citations, one can distill two significant points from the above-cited authorities: (i) statements of purposes in preambles of investment treaties are too generalised to provide meaningful guidance when faced with particularised questions of jurisdiction. (ii) creating a favourable climate for investors is one but not the only purpose of international investment agreements. Such agreements should also serve state contracting parties in that they should set the scene for the economic development of the host states. Therefore, a tribunal charged with interpreting an investment treaty should seek to strike a balance between the interests of the investors and those of the host state by offering a 'balanced approach' to interpretation.

112. So far, I have established that neither 'the ordinary meaning of the terms' of a typical legality requirement nor 'the object and purpose' of investment treaties, when considered individually and in isolation, can pinpoint the boundaries of the 'substantive scope' of the legality requirement. Another element for interpretation as enshrined in Article 31 of the VCLT is 'good faith'. A 'good faith' interpretation would require a legality requirement to be

[195] *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [263]-[264].

interpreted effectively.[196] When applying a treaty which contains a legality requirement, an investment treaty tribunal should interpret the requirement effectively and should refrain from staying indifferent to the violation of the laws of the host state in the process of establishment of the investment. By including the legality requirement in an investment treaty, state parties to the agreement have indirectly entrusted the adjudicating forum with the task of safeguarding their laws from violation by the investor with the consequence that if an investor does not observe the laws of the host state, it cannot benefit from international protection under the agreement.[197]

113. Where do these observations leave me? Having noted these important interpretive points, one feels the need for a 'balanced' and 'effective' interpretation of the legality requirement while remaining loyal to the 'ordinary meaning of the terms' of the legality requirement. As will be explained in detail below, in my opinion, the lower end of the laws of the host states, i.e. *de minimis* laws, are excluded from the 'substantive scope' of the legality requirement. The higher end of such laws, i.e. fundamental laws of the host state, are included in the 'substantive scope' of the legality requirement. The median of the laws of the host state, i.e. ordinary laws, are also included in the substantive reach of the legality requirement, provided that they are violated by the investor in order to secure the investment or guarantee its success.

114. Having the above interpretive observations in mind, in the following three sub-sections, I will discuss each group of host state laws, setting out the specific reasons and supporting case law for inclusion or exclusion of such laws from the 'substantive scope' of the legality requirement.

1st. *Violation of de minimis Laws of the Host State*

115. As stated above, in my opinion, violation of mere technicalities and *de minimis* laws of the host state does not set the legality requirement in motion. It is, of course, correct that violation of any law is an illegal act under domestic law. It was stated by Lord Goff in *Tinsley v Milligan* that the common law rules on illegality do not distinguish 'between degrees of iniquity'.[198] Precisely for this reason, states, not infrequently, argue in investment treaty cases, where the legality requirement is at stake, that the requirement covers all the laws of the host state, and that a violation of each of these laws and regulations triggers the application of the requirement. To give two examples, in *Saba Fakes v. Turkey*, the respondent contended that any violation of any of the host state's laws would result in the illegality of the investment within the meaning of the BIT and would preclude such investment from benefiting from the substantive protection offered by the BIT.[199] In the same vein, in *Quiborax v. Bolivia*, the respondent asserted that the legality requirement in the underlying BIT covered all the laws and regulations

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[196] R Gardiner, *Treaty Interpretation* (2nd edn, OUP 2015) 179-181.

[197] As stated above, states insert legality requirements in their investment treaties to address their concern for the due observance of their laws by investors at the time of making their investments. In this respect, the tribunal in *Alasdair Ross Anderson v Republic of Costa Rica* specified that the incorporation of such a condition in the investment treaty between Canada and Costa Rica (the underlying treaty in that dispute which has a legality requirement in Article 1(g)) was a "clear indication of the importance that [the Contracting Parties] attached to the legality of investments made by investors of the other Party and their intention that their laws with respect to investments be strictly followed." It also added that "[t]he assurance of legality with respect to investment has important, indeed crucial, consequences for the public welfare and economic well-being of any country." *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [53].

[198] *Tinsley v Milligan* [1994] 1 AC 340, 362.

[199] *Saba Fakes v. Republic of Turkey* (n 69) [119].

of the recipient state. Specifically, Bolivia contended that the Bolivia-Chile BIT "does not draw a distinction between serious and non-serious breaches of the laws; it covers both alike".[200]

116. The viewpoint that supports the inclusion of all the laws and regulations of the host state in the 'substantive scope' of the requirement has certain proponents in the field of investment treaty arbitration. For instance, in *Mytilineos Holdings SA v Serbia and Montenegro*, the arbitrator appointed by Serbia wrote a dissenting opinion to the Partial Award on Jurisdiction, and opined that jurisdiction should have been denied, because the investor did various violations of domestic laws of the host state, such as the investor's failure to specify in the investment contracts the amount of money invested in the host state.[201] It is quite obvious that a requirement as per which an investor should cite the amount invested in the contract is not usually a critical requirement of law. On the contrary, it seems to be a *de minimis* legal provision, the failure to comply with which can easily be 'cured'.[202] Furthermore, in a recent article, Zachary Douglas comments that carving out 'technical' or '*de minimis*' violations of the host state law from the 'substantive scope' of the requirement is not logical.[203] Finally, a relatively recent work by UNCTAD also goes to the same direction by indicating that "[l]imiting the applicability of an investment agreement only to investments made in accordance with applicable laws and/or approval procedures is intended to induce foreign investors to ensure that *all local laws and regulations* are satisfied in the course of establishing an investment."[204] [emphasis added]

117. To be sure, as was touched upon above, by just looking at the text of a typical legality requirement or 'the ordinary meaning of terms' used therein, one cannot find a substantive limitation excluding from the scope of the requirement trivial or *de minimis* laws of the host state. That is because such clauses are usually written in an inclusive and general pattern using generic terms, like 'laws' and 'regulations' with no qualifier.[205]

118. However, it was explained above that through a sound interpretive exercise, one cannot solely focus on 'the ordinary meaning of the terms'. In addition to that, one has to pay heed to the 'object' and 'purpose' of the investment treaty in question, and as an underlying principle, always construe the treaty in 'good faith'.[206] The 'object' of an investment treaty is international investment the establishment of which is usually a lengthy and complicated process. In the process of establishment of an international investment, certain *de minimis* laws could unsurprisingly be breached. To hold that such violations trigger the exclusionary function of the legality requirement is neither in line with the 'purpose' of 'promoting

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[200] *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [240].

[201] *Mytilineos Holdings SA v. The State Union of Serbia & Montenegro and Republic of Serbia*, UNCITRAL, Dissenting Opinion from the Arbitral Award on Jurisdiction by Dobrosav Mitrović, 06 September 2006, pp 4-6.

[202] For the 'curability' of an illegality and its effect on the activation of the legality requirement, see *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania* (n 43) [494].

[203] Z Douglas, 'The Plea of Illegality in Investment Treaty Arbitration' (2014) 29(1) ICSID Rev-FILJ 155, 176.

[204] UNCTAD, *Scope and Definition* (n 11) 38.

[205] *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [389]; T Obersteiner (n 91) 276.

[206] (See paragraphs 196-199 *supra* and the accompanying texts). Indeed, the requirement that an investment treaty should be interpreted in 'good faith' is reinforced by considering that states might find it more convenient to take advantage of mere technicalities of their own laws to deprive investors of treaty protection by resorting to the legality requirement. In this regard, see A Carlevaris (n 7) 47; *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania* (n 43) [483].

investments' nor observant of the requirement of interpretation in 'good faith', in particular when the breach in question is 'curable'.

119. In this respect, many investment treaty tribunals have spelled out that the violation of *de minimis* laws of the host state does not trigger the legality requirement: As the most famous ruling in this respect, in *Tokios Tokeles v Ukraine*, faced with the respondent's allegation that the investment in question has not been made in accordance with the laws and regulations of Ukraine, the tribunal held that the investor's economic activity was not illegal, and the fact that the investor had made use of a wrong legal title in the registered name of its company and had omitted signatures on certain documents were so trivial to merit the dismissal of its claim based on the legality requirement. The tribunal stated that:

> [e]ven if [the tribunal] were able to confirm the Respondent's allegations, which would require a searching examination of minute details of administrative procedures in Ukrainian law, to exclude an investment on the basis of such minor errors *would be inconsistent with the object and purpose of the [BIT]*.[207] [emphasis added]

120. Likewise, in *Metalpar v. Argentina,* in the course of making the investment, the investor failed to register a company within the prescribed time in violation of the law of Argentina. The respondent asserted that this is an illegality which would preclude jurisdiction because the investment was not made in accordance with the laws of Argentina. The tribunal dismissed this argument, reasoning that "the lack of adequate registration could be sanctioned by refusing to register certain documents of the company, through a notice of warning, or by imposition of a fine on the company or its directors, but it would be disproportionate to punish this omission to register by denying the investor an essential protection such as access to ICSID tribunals."[208]

121. By the same token, in *Hamester v. Ghana*, the tribunal stated that the investor's submission of false invoices "might not be in line with what could be called "*l'e´thique des affaires*". However, according to the tribunal's viewpoint, such minor irregularities did not amount, in the circumstances of the case, to a fraud that would activate the legality requirement.[209] In the same vein, in *Alpha Projektholding v Ukraine*, the adjudicating forum concluded that a few minor defects in the paperwork submitted by the investor is not sufficiently critical to prevent ascertaining jurisdiction due to the application of the legality requirement.[210] Similarly, in *Quiborax v Bolivia*, the tribunal dismissed Bolivia's various illegality defences on the basis that the alleged illegalities were accidental and negligible errors and omissions in company records.[211] In a similar fashion, in *Hochtief v. Argentina*, the respondent asserted that Hochtief's loan transactions had not all been recorded as prescribed by Argentine financial legislation and that, therefore, the loans had not been made in accordance with the laws and regulations of Argentina as required by Article 2(2) of the Argentina-Germany BIT. The tribunal held that there is not "a sufficient basis for rejecting the claims concerning the loans

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[207] *Tokios Tokeles v. Ukraine*, ICSID Case No ARB/02/18, Decision on Jurisdiction, 29 April 2004 [86].

[208] *Metalpar S.A. and Buen Aire S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/5, Decision on Jurisdiction, 27 April 2006 [84]. (Translation adopted from paragraph 137 of *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [397]).

[209] *Gustav F W Hamester GmbH & Co KG v. Republic of Ghana* (n 41) [138].

[210] *Alpha Projektholding GmbH v. Ukraine*, ICSID Case No ARB/07/16, Award, 08 November 2010 [297].

[211] *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [280]-[281].

on the basis of their non-registration under Argentine regulations".[212] The tribunal drew on previous cases, and noted that other tribunals have focused on compliance with "fundamental principles of the host State's law".[213] According to *Hochtief* tribunal, "investments that are […] dependent upon government approvals that were not in fact obtained, or which were effected by fraud or corruption can be caught by a provision such as Article 2(2) of the Argentina-Germany BIT. But not every technical infraction of a State's regulations associated with an investment will operate so as to deprive that investment of the protection of a Treaty that contains such a provision."[214] Finally, in *Mamidoil v. Albania*, the tribunal focused its attention on the 'good faith' aspect of the interpretation of the legality requirement and said that "[s]tates must not be allowed to abuse the process by scrutinizing the investment *post festum* with the intention of rooting out minor or trivial illegalities as a pretext to free themselves of an obligation" or the "consequences of its standing agreement to arbitrate".[215]

122. In addition to the wealth of case law cited above, a prevailing opinion amongst commentators is that violations of *de minimis* laws of the host state should not be the trigger for the legality requirement.[216]

123. Therefore, an interpretation that takes into account the 'object' and 'purpose' of the treaty and is conducted in 'good faith' would exclude a violation of *de minimis* laws of the host state from the 'substantive scope' of the legality requirement. For this reason, violation of *de minimis* laws of the host state by the investor should not lead to a successful plea of illegality by the state.

124. Notwithstanding what has just been said, it might be problematic in certain cases to decide which laws are '*de minimis*' with the result that the investment violating them still qualifies as being 'in accordance with' the laws of the host state and which laws are not '*de minimis*' with the result that their violation constitutes an infringement of the national law of the host state and hence would prevent an investor or an investment from enjoying protection under an investment treaty.[217]

125. In order to discern the *de minimis* nature of any domestic law, an investment treaty tribunal could be assisted by legal expert testimony on issues of the host state law. In addition, certain

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[212] *Hochtief AG v. The Argentine Republic*, ICSID Case No. ARB/07/31, Decision on Liability, 29 December 2014 [200].

[213] ibid [199].

[214] ibid.

[215] *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania* (n 43) [483].

[216] See, e.g., J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73) 545-546 (looking at the issue from a 'textual' and 'good faith' point of view and remarking that: "The phrasing typically used does not require investments to be 'in substantial accordance with' host state law, but only to be 'in accordance with' host state law" and that "[i]nvestors ought not to be penalized to the extent of losing their ability to claim under investment treaties when they have breached only minor formalities in local laws. States may also be tempted to abuse very technical rules in their own laws to catch out investors unfairly"); A Carlevaris (n 7) 47 (approaching the issue from a teleological viewpoint and commenting that "[t]o exclude from protection under a BIT assets and activities which are covered by the definition of investment, but present minor irregularities under domestic law, would defeat the purpose of promoting investments, which is the main *raison d'etre* of both the Washington Convention and the numerous bilateral and multilateral investment instruments. Such an interpretation of the requirement would have a paradoxical effect in case of formal errors or other irregularities of minor importance. Furthermore, this interpretation may likely be abused by States that are obviously in a better position to take advantage of every minute detail of their legal system"); C Knahr (n 7) 24.

[217] See C Knahr (n 7) 24.

yardsticks could always be of service to the tribunal in recognising such laws, like whether the violation of the law is 'curable', whether the violation is sanctioned by the law at all, or whether it is simply sanctioned by an indeed nominal fine. Thus, if, for instance, the investor fails or forgets to fill in one blank area in a bidding document, for example, to announce the turn-over of the previous fiscal year of its company, this cannot be considered as a critical violation of the laws of the host state. After all, it is not a misrepresentation, and not surely an influential one. Furthermore, it is easily 'curable' by simply providing information when the defect is recognised. An actual example of such errors can be found in *Tokios Tokeles v. Ukraine* case.[218] In this case, Ukraine argued that the investments of *Tokios Tokeles* were not made in accordance with the laws of the host state since the claimant had not registered its subsidiary properly because only 'subsidiary enterprise' and not 'subsidiary private enterprise', as the claimant's subsidiary was called, was an accepted legal form under the laws of Ukraine.[219] It is clear, as the *Tokios Tokeles* tribunal correctly noted,[220] that the violation of such *de minimis* laws, which concern negligible formalities, does not trigger the legality requirement.

126. Having said that, I should note that another type of violation that could be characterised as a 'constructive' trivial breach is a violation of host state law which acts not in favour, but to the detriment of the investor itself. In *Inmaris Perestroika Sailing Maritime Services GmbH and Others v. Ukraine*,[221] one question before the tribunal was whether by failing to register the investment contract in accordance with Ukraine's Law on Foreign Investments Regime, the claimant has committed an illegality that should be remedied by denying jurisdiction. The tribunal reviewed Ukraine's Law and held that although registration of certain investment contracts is 'mandatory' under Ukrainian law, this is "in the sense that such registration is required if the parties to the contract wish to take advantage of legal protections for foreign investors, as well as certain tax and customs benefits that are conferred on foreign investments, under the laws of Ukraine." It further noted that while "the Law stipulates that contracts with foreign investors for "joint investment activity" should be registered, it also states the consequences of a failure to do so: "[u]unregistered foreign investments shall not provide privileges and guarantees stipulated by this Law."" Therefore, the tribunal concluded that the Law did not suggest that unregistered investments are illegal as such, and, thus, held that the claimants' investments was not contrary to Ukrainian law, and, therefore, outside the Treaty's protection by virtue of the fact that claimants did not avail themselves of the benefits of Ukraine's foreign investment law through registration of their contracts.[222]

127. All in all, two kinds of violations of host state law can be considered to be out of the 'substantive scope' of the legality requirement: (i) violation of mere curable legal formalities

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[218] *Tokios Tokeles v. Ukraine* (n 207).

[219] ibid [83].

[220] ibid [86].

[221] *Inmaris Perestroika Sailing Maritime Services GmbH and Others v. Ukraine*, ICSID Case No. ARB/08/8, Decision on Jurisdiction, 08 March 2010.

[222] ibid [144]-[145]. However, it should be noted that under certain international investment agreements, in order to gain BIT protection, the investor has to obtain a license from internal foreign investment authorities of the host state. For instance, Article 2 of the Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Republic of Turkey and the Government of the Islamic Republic of Iran, signed on 21 December 1996, entered into force on 13 April 2005, provides: "This Agreement shall only apply to investments approved by the competent authorities of the host Contracting Party." Under such circumstances, failure to get an investment license culminates in the inapplicability of the treaty to the recalcitrant investor due to its failure to fulfil a stipulated threshold condition of the subject-matter of the agreement, i.e. investment. See Chapter 1, p 49.

with no substantial or very light sanctions under the laws of the host state, i.e., *de minimis* laws of the host state; (ii) violation of laws which their infringement does not harm the state in any way and are solely aimed at protecting the interests of the investor itself.

2nd. *Violation of Fundamental Laws of the Host State*

128. It goes without saying that, according to 'the ordinary meaning of the terms' of a typical legality requirement, fundamental laws of the host state, at the highest end of the spectrum of importance, are admittedly within the 'substantive scope' of the legality requirement. Indeed, an 'effective interpretation' would dictate that without the inclusion of such laws in the 'substantive scope' of the legality requirement, the clause would be absolutely devoid of any meaning and effect. It is arguable that the significance of such laws for states is so high that, without the involvement of such laws in the legality requirement, the purpose of economic development would not be achieved.[223] In fact, it is very hard to ascribe an intention to a state contracting party to an investment agreement according to which the state would offer international substantive and procedural protection to an investment which has been made in violation of the 'fundamental laws' of the host state.

129. The fact that such laws are subsumed within the 'substantive' reach of the requirement is confirmed by several investment treaty tribunals: In 2006, in *LESI and Astaldi v. Algeria*, the tribunal stated that investments would be excluded from treaty protection when made in violation of fundamental principles of law in force in the host state.[224] In 2008, the *Desert Line v. Yemen* tribunal opined that the legality requirement is "intended to ensure the legality of the investment by excluding investments made in breach of fundamental principles of the host State's law, e.g. by fraudulent misrepresentation or the dissimulation of true ownership".[225] Similarly, in 2009, in *Rumeli v Kazakhstan*, the arbitral tribunal held that investments would be denied protection if they were made "in breach of the fundamental legal principles of the host country".[226] In addition to the ones just mentioned, almost all authorities cited so far are in agreement that fundamental laws of the host state are certainly subsumed under the 'substantive scope' of the legality requirement, though some believe that they are not the only laws that should be complied with when making the investment.

130. That being said, one should bear in mind that the difficult question is not whether 'fundamental laws of the host state' fall squarely within the 'substantive scope' of the legality requirement. This is absolutely settled. Rather, the real question in practice is how to discern such laws? Indeed the phrase 'fundamental laws of the host state' is vague itself and is not a 'judicially operational' term and, thus, needs clarification.[227]

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[223] U Kriebaum (n 76) 319.

[224] *L.E.S.I. S.p.A. and ASTALDI S.p.A. v. République Algérienne Démocratique et Populaire* (n 75) [83].

[225] *Desert Line Projects LLC v Yemen* (n 75) [104].

[226] *Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S. v. Republic of Kazakhstan* (n 75) [319].

[227] In the context of assessing the usefulness of the literal definitions offered for the standard of 'fair and equitable treatment', the *Suez* tribunal correctly observed that:

> What, then, is the meaning of "fair and equitable treatment" with respect to the investments undertaken by the Claimants? Philosophers and scholars have devoted tomes to the subject of fairness […] While their work is helpful in understanding the abstract concept and its implications, it does not answer a fundamental and practical question that every arbitral tribunal must answer: By what criteria, standard, or test is an arbitral tribunal to determine whether the specific treatment accorded to the investments of a

131. An articulation of the violations of 'fundamental laws' of the host state is offered by the tribunal in *Teinver v. Argentina*, which takes an inventory of the forms of illegal conduct which can set going the legality requirement:

> (a) lack of authorization to sign the agreement;
>
> (b) fraud or critical omission with regard to an investor's self-presentation during the bidding process;
>
> (c) engagement in any corruption; or
>
> (d) failure to comply with bidding or other procurement requirements.[228]

132. This seems a rather good but not very precise stocktaking of the relevant significant violations. Depending on the jurisdiction, the first type of violation (i.e. lack of authorisation to sign the agreement) renders a contract either invalid, incapable of being performed, unenforceable, null and void, or voidable. Therefore, it is a fundamental breach of host state law.[229] The second type of breach (i.e. fraud and misrepresentation) is undoubtedly a significant violation, the triggering effect of which has also been approved by other tribunals.[230] The third type of violation (i.e. corruption) is the prime example of a significant violation activating the exclusionary effect of the legality requirement. Other tribunals have endorsed this.[231] Finally, as to the fourth type of violation, i.e. failure to comply with bidding or other procurement requirements, it should be said that laws relating to bidding and procurement are usually of mandatory or otherwise important nature since they deal with 'public interests' and 'essential public needs'. However, as exemplified above, not every failure to abide by such laws is equivalent to a violation of fundamental laws of the recipient state. For instance, if just one box is left unfilled in a bidding application form concerning the name of one of the shareholders, it does not seem that such a violation would bend important

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> particular foreign investor in a given context is or is not "fair and equitable."? To say that "fair and equitable" means " just," "even-handed," "unbiased," or "legitimate," as some tribunals have done […] is quite frankly to state a tautology. Such formulations are not *judicially operational* in the sense that they lend themselves to being readily applied to complex, concrete investment fact situations, like those found in the present cases. [footnotes omitted] [emphasis added]

See *Suez, Sociedad General de Aguas de Barcelona, S.A.and Vivendi Universal, S.A. v. Argentine Republic*, ICSID Case No. ARB/03/19 (formerly *Aguas Argentinas, S.A., Suez, Sociedad General de Aguas de Barcelona, S.A.and Vivendi Universal, S.A. v. Argentine Republic*), Decision on Liability, 30 July 2010 [221]. Similarly, the phrase 'fundamental laws of the host state' used by certain tribunals and commentators is not very helpful and does not assist an investment treaty tribunal when faced with actual specific questions.

[228] *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. The Argentine Republic*, ICSID Case No. ARB/09/1, Decision on Jurisdiction, 21 December 2012 [327].

[229] The better approach, however, is to single out issues relating to the formation of the investment agreement and discuss them while dealing with the issue of creation and existence of property rights/interests. However, this would largely depend on the way the respondent has framed its defensive structure and whether it has raised the defence of the inexistence of the investment or has just brought and organised its defence under the single guise of illegality.

[230] See, e.g., *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 7); *Desert Line Projects LLC v Yemen* (n 75) [104]; *Plama Consortium Limited v. Republic of Bulgaria* (n 38) [136]-[137], [140]. In the context of the issue of legitimate expectations, see *International Thunderbird Gaming Corporation v. The United Mexican States*, UNCITRAL, Arbitral Award, 26 January 2006 [164] (noting that due to its misrepresentations vis-à-vis the Mexican authorities, the claimant could not reasonably rely on a representation made by a Mexican state entity).

[231] *World Duty Free Company v Republic of Kenya* (n 50); *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2).

provisions of bidding laws and regulations of the receiving country. This defect is perfectly 'curable'.

133. Another investment treaty tribunal also lists a number of violations that hit the 'fundamental laws of the host state'. According to the *Hochtief* tribunal, "investments that are […] dependent upon government approvals that were not in fact obtained, or which were effected by fraud or corruption can be caught by a provision such as Article 2(2) of the Argentina-Germany BIT…"[232] Although the violation of the laws relating to anti-bribery and prevention of corruption does seem to trigger the legality requirement, the tribunal fails to offer a more comprehensive list of fundamental laws of the host state.

134. In my opinion, the better and the more practical view would be to identify the 'fundamental laws' by reference to their character and their position within the hierarchy of the legal system of the host state. In this way, an investment treaty tribunal would have more useful and concrete tests at hand, rather than unclassified lists of certain limited number of laws addressed in a few cases decided before. In my viewpoint, three categories of laws compose such 'fundamental laws' for the purpose of the 'substantive scope' of the legality requirement: (i) constitutional laws; (ii) organic laws; and (iii) mandatory or compulsory laws.

135. As to the first category, i.e. constitutional laws, I note that on top of all the laws of a state stands the Constitution. A Constitution, in its broad sense, is a law which "attributes power to public authorities", "regulates the fundamental relations between public authorities" and "regulates the fundamental relations between the public authorities and the individual".[233] Constitutions usually contain provisions on "private property rights", "the ability of foreigners to secure legal rights in land", and "foreign investors' freedom to make and enforce contracts".[234] Be that as it may, it is possible that certain principles and/or articles in the Constitution would never meet foreign investments in practice like principles exclusively concerning the political rights of the nationals of the state concerned, like the right to vote. It is also possible that certain provisions of the Constitution do not set forth fundamental principles. Those non-economic and nonessential rules could be said to be excluded from the scope of the legality requirement as far as 'fundamental laws of the host state' are concerned.[235]

136. Turning now to the second category, in certain legal systems, a statutory layer exists between the Constitution and ordinary laws. These legal instruments are called 'organic statutes', or as per Article 46 of the French Constitution, '*lois organiques*'. Organic statutes are laws and rules which regulate and control significant political and economic matters which are not regulated by the Constitution.[236] Clearly, such laws are also of cardinal importance and should fit within the phrase 'fundamental laws of the host state'. In *Alasdair v. Canada*, the

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[232] *Hochtief AG v. The Argentine Republic* (n 212) [199].

[233] AW Heringa, *Constitutions Compared: An Introduction to Comparative Constitutional Law* (4th edn, Intersentia 2016) 3-4.

[234] See JW Salacuse (n 6) 89. For instance, Article XVI, Section 11(1) of the Constitution of the Philippines prohibits any foreign ownership in the mass media sector. Additionally, under Section 2 of Article XII of the Constitution of the Republic of Philippines, the only persons qualified to acquire or hold lands in the public domain are Filipino citizens and corporations 60 percent of whose capital is owned by Filipino citizens. See the 1987 Constitution of the Republic of the Philippines.

[235] J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73) 539.

[236] AW Heringa (n 233) 149-150.

tribunal found that the violation of the Organic Law of the Central Bank of Costa Rica triggers the legality requirement.[237]

137. The third category is 'mandatory' or 'compulsory' laws of the host state. In contrast to 'voluntary laws', the synonyms 'mandatory laws', 'obligatory laws', 'compulsory laws', or 'imperative laws' (*ius cogens* in Latin) are composed of rules which are applicable regardless of the wills of the persons who are influenced by those rules.[238] In my view, 'mandatory laws' of the host state are necessary ingredients of 'fundamental laws of the host state'. Such laws have been defined to include provisions of law designed to protect the political, social, and economic organisation of a country.[239] As such, mandatory laws are pertinent to the 'public interest' of the state concerned.[240] Having this general definition of mandatory laws in mind, below, I will try to introduce some of the usually salient relevant mandatory laws of the host state.

138. Criminal laws are usually amongst – and could be characterised as prime examples of – the mandatory laws of the host state. Crimes involving corruption, particularly bribery,[241] as well

[237] *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [55].

[238] R Youngs (n 78) 86. According to Articles 3(3), 3(4), 6(2) and 8(1) of the Rome I Regulation on the Law Applicable to Contractual Obligations, mandatory laws are provisions that cannot be derogated from by agreement. Furthermore, as per Article 9(2) of the same Regulations, mandatory laws "are provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract".

[239] *Joined Cases C-369/96 Jean-Claude Arblade, Arblade & Fils SARL and C-376/96 Bernard Leloup, Serge Leloup, Sofrage SARL* [1999] ECR I-8453 [30].

[240] According to Pierre Mayer, mandatory laws are the reinforced and elevated version of the rules of public policy. P Mayer (n 160) 278. See also M Blessing, 'Mandatory Rules of Law versus Party Autonomy in International Arbitration' (1997) 14(4) J Int'l Arb 23-24.

[241] *World Duty Free Company v Republic of Kenya* (n 50); *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2).

as crimes involving fraud[242] have been decided by investment treaty tribunals to trigger the legality requirement.[243] [244]

139. Mandatory laws of the host state are not limited to criminal laws. Certain laws relating to foreign investment are also of a mandatory nature. Thus, failure to obtain mandatory licenses prescribed by foreign investment law of the host state would also culminate in breach of fundamental and mandatory laws of the host state, which would, in turn, trigger the legality requirement.[245] For the same reason, more general economic laws relating to ownership and control of key public infrastructure (like airports, rail and road transport, energy grids, etc.) and key public entities, like anti-dummy, tender, and public procurement laws are also included within the framework of mandatory laws of the host state.[246] A specific practical example of such laws is the Anti-Dummy Law of Philippines at issue in *Fraport v Philippines*.[247] In that case, a breach by the investor, which deprived Philippines' nationals of the minimum

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[242] *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 7); *Desert Line Projects LLC v Yemen* (n 75) [104]. Particularly, in this connection, the *Vladislav* tribunal correctly held that:

> [T]he Tribunal may conclude, on the basis of an examination of the law of the Host State and the facts that pertain to an allegation, that there has been non-compliance with legislation sufficient to trigger the legality requirement. *In this regard, the commission of a criminal offence under Article 168 [on prohibition of fraud], if established, would constitute an illegality sufficient to cause the investment to fall outside the scope of Article 12 of the BIT as the loss of the protection of the BIT, and the vitiation of the Tribunal's jurisdiction, would be a proportionate response to an illegality of such significance.* [emphasis added]

See *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [522].

[243] On a related note, Douglas identifies another problem with asserting jurisdiction with respect to investments made in violation of the penal laws of the host state. He opines that to grant a civil remedy to a person who has violated the criminal law also results in undermining the deterrent effect of the criminal law. See Z Douglas (n 203) 167. This, indeed, would be another ill-effect of ignoring the violation of 'fundamental laws' of the host state for the purposes of the legality requirement.

[244] I should add here that in case the investment is illegal under domestic law '*per se*', to borrow examples from the *Phoenix* tribunal, like "investments made in pursuance of torture or genocide or in support of slavery or trafficking of human organs", one could, beyond the shadow of a doubt, hold that the investment is not protected by the investment treaty, *inter alia*, because it amounts to illegality under an 'in accordance with the host state law' requirement. See *Phoenix Action Ltd v. Czech Republic* (n 39) [78]. In *Mytilineos v. Serbia*, dismissing the respondent's objection to granting investment protection to the claimant on the basis of alleged non-compliance with the laws of the host state, the tribunal made note of the fact that the investment operation itself was not illegal *per se*. It cited and relied on *Tokios Tokeles*, paying regard to the fact that it was critical for the *Tokios Tokeles* tribunal that the investment activity as such was legal: "The [*Tokios Tokeles*] tribunal rejected this claim and found that Claimant's activity was covered by the definition of investment under the BIT since those investment activities in the publishing business were not illegal under the law of the host State. The tribunal further suggested that minor registration irregularities are harmless errors as long as the investment was not 'illegal *per se*'." *Mytilineos Holdings SA v. The State Union of Serbia & Montenegro and Republic of Serbia*, UNCITRAL, Partial Award on Jurisdiction, 08 September 2006 [151]. [Footnote omitted]; T Obersteiner (n 91) 276.

[245] *Hochtief AG v. The Argentine Republic* (n 212) [199].

[246] *Desert Line Projects LLC v Yemen* (n 75) [104]; U Kriebaum (n 76) 320; P Mayer (n 160) 288, fn. 29 and the accompanying text (saying that the most widely held opinion is that rules of public law are a subset of mandatory rules of law.); M Blessing (n 240) 23-24; R Youngs (n 78) 86.

[247] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2).

shareholding required under the above-mentioned law, culminated in a violation of a mandatory or a fundamental provision of the law of the recipient state, and consequently, set the legality requirement of the underlying investment treaty in motion.

140. In addition, laws of mandatory nature could also be of classical civil nature, like the conditions for the validity of a contract.[248] For instance, submitting false financial or technical information or misrepresenting financial or technical capabilities, in case such false information and misrepresentations induce the state to select a bidder as a winner of a bidding process[249] — which not only might involve the breach of criminal and tender laws of the host state but also may violate rules of classical civil nature regarding conditions for validity of contract — may activate the legality requirement.

141. A number of other laws which aim to protect the public interest and the public policy of the host state are also inside the realm of mandatory laws of the host state.[250] According to Pierre Mayer, the most frequently-encountered mandatory laws in international arbitration, all of which seek to safeguard the 'public interest' and the 'public policy' of the host state, are the following: competition laws, currency control laws,[251] environmental protection laws, measures of embargo, blockade, or boycott, and laws designed to protect parties presumed to be in an inferior bargaining position, such as wage-earners or commercial agents.[252]

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[248] *Plama Consortium Limited v. Republic of Bulgaria* (n 38) [136]-[137], [140] (finding that the claimant had violated Articles 27 and 29 of the Bulgaria's Obligations and Contracts Acts). See also AFM Maniruzzaman, 'International Arbitrator and Mandatory Public Law Rules in the Context of State Contracts: An Overview' (1990) 7(3) J Int'l Arb 53–64, 53 (saying that "[t]here are certain matters which fall within the exclusive jurisdiction of the host country's national law, as may be described the "reserved domain" of the national law. These matters relate to the validity of the contract in form and substance ..." He further goes on to elaborate on his proposition, indicating, in the context of 'concession contracts', that: "The laws relating to the form and conditions of the grant of concession, the power of the conceding authority, the necessity or otherwise of a ratification of the agreement and the observance of such other constitutional or administrative formalities which may be required in order to give effect to the concession, are all matters falling within the domain of the national law of the conceding State." ibid 58. See also R Youngs (n 78) 86 (exemplifying compulsory laws by formal legal conditions set forth for certain contracts, saying that: "One example of compulsory law is the requirement that certain types of contract shall conform to preconceived matters … [f]or instance, a contract to create a property right must usually create only one that is of a kind already recognised by law …")

[249] A similar situation occurred in *Inceysa Vallisoletana S.L. v. Republic of El Salvador*. However, in a blameworthy approach, the tribunal in that case did not determine which of the positive laws of El Salvador were breached by the investor.

[250] In the context of conflict of laws, Maniruzzaman indicates that "matters as the State may require to be performed in the public interest under its mandatory public law rules … fall within the exclusive jurisdiction of the host country's national law, as may be described the "reserved domain" of the national law". AFM Maniruzzaman (n 248) 53.

[251] With respect to the importance of exchange control regulations, one commentator notes that "violations of exchange controls normally constitute criminal offences in the foreign country concerned and often result in severe penalties including fines and imprisonment or both." See JW Salacuse (n 6) 84.

[252] P Mayer (n 160) 275. See also AFM Maniruzzaman (n 248) 57-58 (giving some examples of such laws: "…import-export rules; foreign exchange regulations; competition laws; taxation laws; measures of embargo, blockade or boycott; expropriation, nationalization and confiscations, etc.") In addition, a survey on some of the most recent model BITs and concluded investment treaties reveals certain areas of 'public interest' which the states have highlighted their preservation even in the preamble of these instruments. For instance, the sixth recital of the Preamble of the US Model BIT (2012) emphasises that the "protection of health, safety, and the environment, and the promotion of internationally recognized labor rights should not be sacrificed for achieving other investment treaty objectives." See also the preamble of the Agreement for the Promotion and Protection of Investment between the Government of the Republic of Austria and the Government of the Kyrgyz Republic, signed on 22 April 2016, not yet entered into force (stating, *inter alia*, that the Contracting Parties agree that the other objectives in the treaty "can be achieved without

142. Having identified a number of mandatory laws which stand as decent candidates to fit within the definition of the term 'fundamental laws' of the host state, one should admit that in certain instances it is difficult for an investment treaty arbitral tribunal to ascertain the mandatory nature of a given legal provision.[253] Nevertheless, there exist certain clues which could assist an arbitration tribunal in resolving this issue. The best tool to recognise the 'imperativeness' of a given rule of law is the legal provision itself, or the interpretive rules included in the legal Act or Code embodying the provision at stake.[254] Therefore, if the pertinent article stipulates that the rules contained therein cannot be derogated from by agreement, or more explicitly says that the rule in question is obligatory, mandatory, imperative, compulsory, etc. the tribunal can easily determine that the law at issue has a mandatory nature, the violation of which is equivalent to 'non-compliance' with the laws of the host state for the legality requirement's purpose.[255] However, not all the legal provisions are crystal-clear as to their nature. In many cases, the laws are silent as to whether they are

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relaxing health, safety and environmental measures of general applications", and that they recognise that: "the development of economic and business relations can promote respect for internationally recognised labour rights".) In the same vein, certain treaties include an apparently non-legally binding commitment by the contracting parties to abstain from relaxing the 'public interest' protection standards as a means of attracting or maintaining investment in their territories. See, for instance, Article 15 of the Agreement between Canada and Mongolia for the Promotion and Protection of Investments, signed on 08 August 2016, entered into force on 24 February 2017 (stating that: "The Parties recognize that it is inappropriate to encourage investment by relaxing domestic health, safety or environmental measures. Accordingly, a Party should not waive or otherwise derogate from, or offer to waive or otherwise derogate from, such measures as an encouragement for the establishment, acquisition, expansion or retention in its territory of an investment of an investor. If a Party considers that the other Party has offered such an encouragement, it may request consultations with the other Party and the two Parties shall consult with a view to avoiding any such encouragement.") The most comprehensive articulation of laws preserving public interests of the host state in an illustrative manner has been set out by Article 12(1) of the Indian Model BIT (2015).

> **Article 12: Compliance with Law of Host State**
>
> 12.1 Investors and their Investments shall be subject to and comply with the Law of the Host State. This includes, but is not limited to, the following:
>
> (i) Law concerning payment of wages and minimum wages, employment of contract labour, prohibition on child labour, special conditions of work, social security and benefit and insurance schemes applicable to employees;
>
> (ii) information sharing requirements of the Host State concerning the Investment in question and the corporate history and practices of the Investment or Investor, for purposes of decision making in relation to that Investment or for other purposes;
>
> (iii) environmental Law applicable to the Investment and its business operations;
>
> (iv) Law relating to conservation of natural resources;
>
> (v) Law relating to human rights;
>
> (vi) Law of consumer protection and fair competition; and
>
> (vii) relevant national and internationally accepted standards of corporate governance and accounting practices.

[253] As mentioned rightly by Pierre Mayer, the mere argument of the state that the law in question is mandatory does not suffice. See P Mayer (n 160) 292.

[254] R Youngs (n 78) 86.

[255] For instance, as per Articles 22 and 48 of Iran's Notarial Law (1932), sale of immovable properties in Iran should be notarised. Thus, if a sale contract is concluded without the formal requirement of notarisation, the buyer cannot prove and rely on the acquisition of ownership by virtue of the sale contract before government offices, administrative agencies or courts.

'permissible' or 'mandatory'.[256] In such situations, the tribunal could be handed with the guiding principles in the Constitution of the host state[257] and the decisions of judicial organs of the host state interpreting the nature of such laws (preferably if those decisions have been made by the highest judicial authorities of that state). Furthermore, and as always, the panel could be helped with an expert legal opinion on matters of host state law.[258]

143. A final point to make is that a 'good faith' interpretation necessitates the inclusion of only mandatory provisions of compulsory laws, not just any provision which pops up in laws with a general compulsory label. To elaborate on this point, it is widely known and accepted that penal codes are considered to be mandatory laws.[259] However, not all the provisions of such codes are so significant. The significance level of a provision can be recognised, *inter alia*, by reference to the sanction or punishment prescribed by the relevant provision of the code for the crime at stake. For certain offences, criminal punishment is a negligible fine. Thus, violation of such provisions could be said to fall outside the scope of the legality requirement. On the other hand, the sanction of imprisonment, compulsory dissolution of a company, and forfeiture of assets are heavy punishments which speak in favour of the significant nature of the violation.[260] Infringing such provisions of law would, in all likelihood, be caught by the legality requirement. The same observation can be made with respect to mandatory civil liability laws. Thus, in case the civil violation is sanctioned by the legal act being declared as void, invalid or voidable, the provision in question is most probably a fundamental provision. On the other hand, in case the violation is curable and not sanctioned by the legal act being declared as void or voidable, the provision in question is often not fundamental.[261]

144. In conclusion, if a violation on the part of the investor concerns fundamental provisions of the laws of the host state, including its Constitution, its organic laws, or its mandatory laws, then the violation triggers the operation of the legality requirement. Under this rule, if the violation concerns an insignificant provision within a law with a mandatory label, like a misdemeanour sanctioned by payment of a small fine, then the violation could not be said to activate the legality requirement.

3rd. *Violation of Ordinary Laws of the Host State*

145. So far, I have demonstrated that, first, the violation of *de minimis* laws of the host state does not trigger the legality requirement, and, second, the violation of fundamental laws of the

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[256] See A Sayed, *Corruption in International Trade and Commercial Arbitration* (Kluwer Law International 2004) 38 (saying that "[T]he imperative nature of any given law is normally established by reference to the letter of the particular enactment, which could contain … an explicit legislative intent signifying that such a legislation is imperative." However, he goes on to admit that in most cases, an explicit statement in the law to specify its mandatory and imperative nature is unavailable, and it is the task of the judge or the arbitrator to determine the nature of the law or legislation in question). See also R Youngs (n 78) 86.

[257] J Hepburn, 'In Accordance with Which Host State Laws? Restoring the 'Defence' of Investor Illegality in Investment Arbitration' (n 73) 538-539.

[258] See Chapter 4.

[259] See paragraph 138 *supra*.

[260] For instance, under Iranian law, the punishment for bribery is, *inter alia*, forfeiture of property and/or imprisonment from 6 months to 5 years. See Article 3 of the Aggravating the Punishment for the Crimes of Embezzlement, Bribery, and Fraud (1988).

[261] Cf *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [406], second bullet point. On this point, Knahr expresses the opinion that "actions either leading to civil liability or constituting criminal offences under domestic law would be illegal, consequently not being "in accordance with host state law". C Knahr (n 7) 24.

host state triggers the legality requirement. Having formed an opinion with respect to the two ends of the spectrum of the laws of the host state, I should now turn to the third group of such laws, i.e. ordinary laws. It goes without saying that by merely carving out the trivial violations of the host state from the 'substantive scope' of the 'in accordance with the law' clause, one cannot limit the scope of the legality requirement to only fundamental laws of the host state.[262] The simple reason is that there lies another body of laws between *de minimis* laws and fundamental laws, those laws being ordinary laws of the host state. Put differently, there is a gap between *de minimis* laws and fundamental laws of the host state which is filled by ordinary laws of that state. This gap has been noticed by some commentators. According to one commentator, there are different sorts of violations of host state law: from the violation of significant laws to the violation of trivial legal technicalities with a grey area sitting in between. Kriebaum notes in this respect that:

> It is clear that not every minor infraction will lead to a denial of investment protection. Only breaches of fundamental norms of a legal order will have such an effect. The significance of the contravention to host State law will be the most important factor in the decision whether the legitimacy of the investment as a whole is at stake. Sometimes the gravity of the contravention on its own will not provide an exact line between cases where investment protection should be denied and those where it should be upheld. *At the two ends of the spectrum – very important norm and minor formality – decisions will be easy to take*.[263] [emphasis added]

Thus, she takes cognizance of the fact that there are other violations of the laws of the host state as to which – in contrast to the cases of infringement of fundamental laws and *de minimis* laws of the host state – decision-making is not easy. With that said, she then goes on to pinpoint factors for decision-making in situations where the laws sitting in the middle of these two spectrums have been violated by the investor.[264]

146. Certain tribunals have voiced that the legality requirement can be activated by the violation of any of the 'prevailing laws' of the host state, and, thus, have effectively opined that the requirement is not just limited to fundamental laws. In *Anderson v. Costa Rica*, the tribunal held that in order to assess the legality of the establishment of the investment, "one must of necessity examine how the possession or ownership of that property was acquired and in particular whether the process by which that possession or ownership was acquired complied with *all of the prevailing laws"*.[265] [emphasis added] Therefore, according to this tribunal, the 'substantive scope' of the legality requirement is not merely confined to laws relating to

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[262] See *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [395].

[263] U Kriebaum (n 76) 319. On this matter, Carlevaris opines that the decisions rendered until 2008 "failed to enter into a detailed analysis of this question, and provide no guidance as to the distinguishing criteria - either by reference to the seriousness of the violation or to the nature of the provisions allegedly violated - between significant wrongful acts that entail exclusion from protection and minor irregularities which would not have this exclusionary effect. Although one can approve of the distinction to be drawn between insignificant administrative irregularities, such as those apparently invoked in *Tokios Tokeles*, and serious wrongful acts that might possibly amount to criminal offences, as in *Inceysa*, less extreme situations would be difficult to assess." A Carlevaris (n 7) 47.

[264] U Kriebaum (n 76) 320 *et seq*.

[265] *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [57].

foreign investment, or only to fundamental laws, but covers all the laws and regulations that are applicable to acquiring possession and/or ownership. Such laws could be of fundamental or ordinary nature.

147. Bearing these points in mind, one should consider situations in which the violation concerns normal and ordinary laws, which neither could be characterised as fundamental laws, nor as mere technicalities. It is the opinion of the present author that violation of ordinary laws of the host state would also trigger the legality requirement if the investment at stake could not have been made or could not have been successful but for the violation of the ordinary law(s) in question. I find support for this view in the ordinary meaning of the terms used for expressing a legality requirement. A typical legality requirement would provide: "The term "investment" refers to every kind of property or asset … invested by the investors of one Contracting Party in the territory of the other Contracting Party in accordance with the laws and regulations of the other Contracting Party …"[266] This provision plainly links the act of 'investing' to the observance of the laws of the host state. Thus, according to 'the ordinary meaning' of the terms of this provision, if an investment cannot be realised or established without the violation of the laws of the host state, that investment is caught by the exclusionary effect of the legality requirement.

148. Assume that an investment regulation of the host state requires foreign investors in the field of infrastructure to obtain, among other things, a construction authorisation before commencing the project. Suppose that the investor fails to obtain a construction permit, without which the investment operation could not have commenced. The investor nevertheless goes on and commences the project. In the wake of a dispute, upon consideration and analysis by an investment treaty tribunal, it becomes clear that under the circumstances and based on the available evidence, due to lack of the required technical standards, the construction permit would, more likely than not, have been denied by the pertinent authority had the investor applied for it. In this situation, the investor has apparently not violated a mandatory rule of host state law but has secured the investment by infringing an ordinary law of the host state. This is a situation which, according to my thesis, triggers the legality requirement. On the other hand, if according to the same regulation, the investor was required to acquire a license from the central bank of the recipient state not as a condition precedent for the commencement of the project, but only for the purpose of the legal channeling of investment revenues and proceeds, in case the investor fails to obtain such a permit, not because it could not get the license or the license would have been denied by the central bank, such violation cannot be considered as one activating the legality requirement. Indeed, whilst both violations of the investment regulation in question occurred in the process of the establishment of the investment, only the former, i.e., the failure to obtain the construction permit, was linked to the very establishment of the investment and allowed its commencement in violation of the law.

149. This view is supported by two prominent decisions which highlight that one should check the link between the acquisition or the success of the investment and compliance with the laws of the host state. I borrow the first support from the above-mentioned text in the *Anderson v. Costa Rica* award, where the tribunal expresses that: "one must of necessity examine how the possession or ownership of that property was acquired and in particular whether the process

[266] See Article 1(1) of the Agreement between the Government of the Lebanese Republic and the Government of the Islamic Republic of Iran on The Reciprocal Promotion and Protection of Investments, signed on 28 October 1997, entered into force on 14 May 2000.

by which that possession or ownership was acquired complied with all of the prevailing laws".[267] Thus, according to this tribunal, if possession or ownership of the investment is not acquired in accordance with the laws of the host state, the legality requirement acts to deprive the investor of investment treaty protection. A yet better support for this proposition can be found in the *Fraport* Award. In examining whether the making of the investment was tainted with illegality, the tribunal considered the effect of illegality on the profitability of the investment and its role in securing the investment. The Tribunal held:

> … Another indicator that should work in favour of an investor that had run afoul of a prohibition in local law would be that the offending arrangement was not central to the profitability of the investment, such that the investor might have made the investment in ways that accorded with local law without any loss of projected profitability.[268]

The tribunal had already dealt with the specific facts of the case and had found that Fraport considered that without the illegal arrangements the investment could not operate in a profitable way:

> … In the context of the internal Fraport documents, the secret shareholder agreements show that Fraport from the outset understood, with precision, the Philippine legal prohibition but believed that if it complied with it, the prospective investment could not be profitable.[269]

The tribunal further noted that:

> The record indicates that … local counsel explicitly warned that a particular structural arrangement would violate a serious provision of Philippine law. Moreover, the violation qua violation was explicitly discussed at the level of the Board of Directors. In view of the due diligence study prepared by financial experts (who had apparently not been briefed on the local law restrictions), the investor, Fraport, concluded that the only plausible way for its equity investment to prove profitable was to arrange secretly for management and control of the project in a way which the investor knew were not in accordance with the law of the Philippines. This was accomplished by Article 2.02 of the […] Shareholders' Agreement of 6 July 1999 which allowed Fraport […] to have a casting and controlling vote over matters which fell within its 'area of expertise and competence'. Thus the violation could not be deemed to be inadvertent and irrelevant to the investment. It was central to the success of the project. The awareness that the arrangements were not in accordance with

[267] *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [57]

[268] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [396].

[269] ibid [355].

> Philippine law was manifested by the decision to make the arrangements secretly and to try to make them effective under foreign law [...][270]

150. According to these two authorities, in particular, the second, in case the making or the success of the investment is hinged on the violation of the laws of the host state, the violation would trigger the legality requirement. In such situations, without committing the illegality, the investor would not have secured the investment or would not have made a successful investment. Hence, the illegality would taint the core of the investment. Thus, the critical question to be asked by the court or tribunal is whether the investor could have successfully made the investment or could have made an investment which was successful, but for the violation of host state law?

151. In terms of doctrinal support for this idea, Kriebaum considers 'the importance of the offending arrangement for the profitability of the investment' as a 'further element' in analysing the compliance with the host state law for the purpose of the legality requirement.[271] In contrast, the present Thesis suggests that 'the importance of the offending arrangement for the profitability of the investment' is not just a 'further element' in the analysis scheme, but could be a separate basis for dismissing a case on jurisdiction or admissibility, as the case may be, when the violation in question concerns, not necessarily a fundamental law of the host state, but also a normal or ordinary law of the recipient state, provided that such violation is an inevitable element for the making of an investment or its success.

152. Therefore, the second type of legality-triggering situation focuses both on the effect that the violation of a law has on the making or the success of the investment as well as the nature of the law violated. Subsequently, unlike in cases of violations of the fundamental laws of the host state, a situation in which ordinary laws have been violated entails a more fact-specific and a more case-by-case analysis.

153. Having said that, I should emphasise that not all violations of the ordinary laws of the host state would trigger the requirement. It could very well happen that ordinary laws of the host state are violated, nonetheless, there is no link between the very establishment or the success of the investment and the violation of the law. This absence of a link could be evidenced, *inter alia*, by the 'curability' of the breach. In *Mamidoil v. Albania*, the respondent argued that the claimant had not obtained a number of critical licenses (including construction, environmental, and exploitation permits). On the other hand, Mamidoil asserted that Albania had "consistently acknowledged the legality of the investment" over the last 12 years. The tribunal found that Mamidoil had failed to obtain the exploitation and construction permits and that these failures were more serious than 'minor administrative errors'. The tribunal dismissed Mamidoil's view that respondent's preliminary approval of the project created an obligation for Albanian authorities to issue the permits. Rather, according to the tribunal, such an obligation would have only arisen once the claimant properly applied for the permits. The tribunal also found that as of 2003, Albania had consistently insisted that the authorisations are lacking.[272] The tribunal also noted that Albania had, nevertheless, offered to cure the claimant's illegality. According to the tribunal, this proved that "in that State's own appreciation, the illegality of the investment was susceptible of being cured". Thus, the tribunal upheld jurisdiction and

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[270] ibid [398].

[271] U Kriebaum (n 76) 323.

[272] *Mamidoil Jetoil Greek Petroleum Products Societe S.A. v. Republic of Albania* (n 43) [468], [472].

decided to assess the legal importance of the absence of permits as a matter of merits.[273] As can be seen from this example, if an ordinary law of the host state is violated but the violation is not central to the making of the investment, the tribunal can assert jurisdiction since the legality requirement is not engaged.

154. In conclusion, the 'substantive scope' of the legality requirement includes fundamental laws of the host state (including its Constitution, its organic laws (if any), and mandatory provisions of law) as well as its ordinary laws, when the very establishment or the success of the investment depends on the compliance or non-compliance with such ordinary laws.

### c. Temporal Scope of the Legality Requirement

155. Another relevant question regarding the scope of the legality requirement that needs to be answered is whether it is only the illegality at the time of making the investment which is captured by the legality requirement and culminates in dismissing jurisdiction (or admissibility) or whether illegalities committed after the initiation of the investment are also caught by the requirement and are taken into account in dismissing jurisdiction (or admissibility).

156. Both the ordinary meaning of the terms of a typical legality requirement and the practice of investment treaty arbitration speak in favour of limiting the consideration of illegality for jurisdictional purposes to violations of the host state law at the time of the establishment of an investment and not extending its temporal reach to violation of the recipient state's laws after the establishment of the investment. In other words, non-compliance with host state law is relevant for jurisdictional purposes only when it occurs in the course of initiation of an investment. Therefore, if the investor commits a crime pursuant to the establishment of its investment, although this illegality might be raised by the host state as a defence to the merits of the case, such a defence cannot bar the tribunal's jurisdiction.[274] To explain the point, it is noteworthy to review some relevant jurisprudence.

157. In *Fraport v. Philippines*, the respondent had alleged that legality of investment is relevant for jurisdictional purposes, both at the initiation and during the operation of the investment.[275] The tribunal only accepted the first limb of Philippine's argument, that legality as a jurisdictional condition was relevant only at the time of making the investment.[276] In *Metal-Tech v. Uzbekistan*, the interpretive dispute between the parties revolved around the sentence "[t]he term 'investments' shall comprise any kind of assets, implemented in accordance with the laws and regulations of the Contracting Party in whose territory the investment is made …" in Article 1(1) of the underlying investment treaty. The claimant contended that the legality requirement in the underlying BIT must be interpreted as a bar to the jurisdiction only where the establishment of the investment was tainted by illegality.[277] Uzbekistan countered this argument by positing that the tribunal lacked jurisdiction over this dispute because the claimant's investment was 'implemented', i.e. made and operated, in violation of Uzbek law.[278]

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[273] ibid [494]-[495].

[274] It should, however, be noted that state parties to an investment treaty are free to formulate the clause in a way that it also covers illegalities occurred during the operation of the investment as a bar to jurisdiction.

[275] See *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [344].

[276] ibid [345].

[277] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [107(x)].

[278] ibid [110 (i)].

Taking a textual as well as a contextual interpretative approach, the tribunal found that the disputed term 'implemented' meant 'established' and 'made', rather than 'established and operated' as was suggested by the respondent. This led the tribunal to the conclusion that according to the BIT, illegality was a bar to jurisdiction only when the unlawful action occurred at the time of the establishment and making of the investment.[279] In the same vein, in *Quiborax v. Bolivia*, the respondent had alleged that the legality requirement of the Chile-Bolivia BIT covered any breach, regardless of when the breach is committed.[280] The tribunal decided that the 'temporal scope' of the legality requirement is limited to the establishment of the investment, and does not extend to its subsequent performance.[281] Based on this finding, the tribunal dismissed the relevance of two allegedly illegal conducts in its jurisdictional analysis on the basis of their occurring pursuant to the establishment of the investment.[282]

158. In summary, both the typical language of regular legality requirements in investment treaties as well as the prevailing practice of investment treaty arbitration speak in favour of limiting the consideration of illegality for jurisdictional purposes to violations of the host state law at the time of the establishment of investment.

159. Having said that, two technical points regarding the temporal scope of the legality requirement shall not be forgotten. First, in analysing whether a violation of the laws of the host state has occurred at the time of making the investment, as has been emphasised by one tribunal, the relevant analysis "has to be performed taking into account the laws [of the host state] in force at the moment of the establishment of the investment" rather than later modifications in legislation.[283] Second, it should be pointed out that in cases of bribery or conspiracy, the fact that illicit payments for securing an investment were made after the establishment of the investment should not influence the reality that investment itself was made illegally and it was only the compensation for the illegal interference of the official(s) concerned or third parties carrying clout that was paid thereafter. Thus, the ICISD panel in *Metal-Tech v. Uzbekistan* found that although payments to certain individuals post-dated the establishment of the claimant's investment, as the payments were intended to compensate the services they had rendered in securing the investment for Metal-Tech, the actual date of the payments could not influence the tribunal's temporal analysis of the legality requirement in the sense that the investment itself was made illegally.[284]

### d. Conclusion

160. In this subsection, I analysed the 'formal', the 'substantive', and the 'temporal' scope of the legality requirement. Whereas the 'formal' scope of the requirement has not caused so much controversy, the 'substantive' reach of this requirement has been subject to heated discussions.

161. As to the 'formal' scope, I noted that certain treaties do determine in detail the 'formal' ambit of the legality requirement. With regard to other treaties not having such level of detail,

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[279] ibid [185]-[193].

[280] *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 2) [239], [249].

[281] ibid [266].

[282] ibid [274], [277]. See also *Vladislav Kim and others v. Republic of Uzbekistan* (n 74) [410) (noting that "The legality requirement is limited to the time that the investment is made.")

[283] *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [103].

[284] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [267]-[273].

unless otherwise defined by the treaty in question, the use of the term 'legislation' in the legality requirement tends to signify a more specific concept in comparison to the term 'law'. Therefore, in many instances, the investment treaties that use the term 'legislation' tend to exclude other sources of law not enacted by the Legislature, for instance, regulations laid down by the Executive. At the same time, however, I mentioned that this depends on the pertinent jurisdiction. Thus, in case doubt arises as to the meaning and scope of the term 'legislation', refer must be had to the public law of the host state. Additionally, it was stated that the term 'law' has been defined to encompass, in addition to legislation enacted by the Legislature, other sources of regulation and decision-making. Therefore, unless otherwise provided by the treaty in question, if an investment treaty requires compliance with the 'laws' of the host state, in order to be protected under the investment treaty, the investor has to comply with the legislation laid down by the Legislature and the regulations enacted by the Executive which are in force at the moment of establishing its investment.

162. Turning to the 'substantive scope' of the requirement, it was submitted that the first point of reference for determining the 'substantive scope' of the legality requirement is the investment treaty itself. Contracting parties to investment agreements are naturally free to pinpoint the specific classes of the recipient state law that should be abided by in order to gain protection under investment treaties. A few investment treaties spell out certain laws compliance with which is required at the time of making the investment, though not in an exhaustive manner.[285] However, a great majority of investment treaties do not even benefit from such non-exhaustive illustrations. Vague and generic terms like 'laws of the host state', or 'legislation of the host state' frequently emerge in legality requirements.

163. Although generally formulated, there does not seem to be significant support for the idea that the legality requirement is without limitation. Almost all of the scholars and authorities tend to circumscribe the reach of the requirement by some sort of test. However, the tests offered for such circumscription by investment treaty tribunals and scholarship are not sound when looked at from the prism of a proper interpretive approach nor, in many instances, are such tests useful in practice. For example, to say that the 'substantive scope' of the legality requirement is limited to 'fundamental laws of the host state', although enlightening to a limited extent, does not effectively assist an investment treaty tribunal when faced with specificities of the case.

164. The solution should not detour from its path which is Article 31 of the VCLT. Thus, in proposing the solution, I have tried, to the extent possible, to remain loyal to 'the ordinary meaning' of a typical legality requirement, by simultaneously, endeavouring to offer an interpretation which is observant of the 'object' and 'purpose' of the treaty and done in 'good faith' in line with the principle of 'effective interpretation'. It is submitted that pursuant to an interpretive exercise on the basis of Article 31 of the VCLT: (i) an 'effective interpretation' watchful of the 'object' and 'purpose' of the treaty would require that *de minimis* laws of the host state be excluded from the 'substantive scope' of the legality requirement; (ii) an 'effective interpretation' based on the 'ordinary meaning of the terms' of a typical legality requirement

[285] For instance, the Protocol of the BIT between Germany and Philippines, which was concluded on the same day as the BIT, states at ad Article 2: "As provided for in the Constitution of the Republic of the Philippines, foreign investors are not allowed to own land in the territory of the Republic of the Philippines. However investors are allowed to own up to 40% of the equity of a company which can then acquire ownership of land." Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments (n 3).

which is considerate of the 'object' and 'purpose' of the treaty would reasonably lead one to accept that fundamental laws of the host state, including in particular the Constitution of the host state, its organic laws, and the mandatory laws of the host state, are squarely within the 'substantive scope' of the requirement; and (iii) an 'effective interpretation' based on the 'ordinary meaning of the terms' of a normal legality requirement – and, indeed, a 'balanced' approach to interpretation – results in confirming that ordinary laws of the host state are also inside the 'substantive' orbit of the requirement provided that their violation was made in order to acquire the investment or to guarantee the success of the investment.

165. This overall conclusion is to some extent supported by the two awards chaired by Gabrielle Kaufmann-Kohler.[286] According to these two awards, the 'substantive scope' of the legality requirement extends to the ensuing situations: (i) 'nontrivial violations of the host State's legal order'; (ii) 'violations of the host State's foreign investment regime'; and (iii) 'fraud…to secure the investment …'[287] Similarly, the solution adopted by this Thesis excludes trivial breaches from the scope of the legality requirement. It also includes, as these decisions implicitly do, violation of mandatory laws of the host state regarding foreign investment regime and criminal laws, though the decisions do not enumerate other laws of fundamental nature. Finally, both my solution and these two identical articulations of the 'substantive scope' of the legality requirement in the two mentioned awards tend to include ordinary laws of the host state within the reach of the requirement. The subtle difference is that according to my approach, ordinary laws are engaged provided that the violation is made to secure the investment or to guarantee its success. In contrast, the approach taken by these two decisions just includes 'nontrivial' breaches without further qualifying it. However, when talking about fraud, they do mention that fraud would be a trigger to the legality requirement if it is committed to secure the investment.

166. Finally, with regard to the 'temporal' reach of the legality requirement, both the 'ordinary meaning' of a typical legality requirement in investment treaties as well as the prevailing practice of investment treaty arbitrations support limiting the consideration of illegality for jurisdictional purposes to violations of the host state law at the time of the establishment of investment.

### B. The Consequences of the Legality Requirement

167. It goes without saying that the legality requirement has a limiting function. In other words, it limits the scope of application of the investment treaty in the sense that, if activated, it prevents an investor from availing itself of the protection of the investment treaty standards.[288] Indeed, an arbitral tribunal deriving its jurisdiction from an investment treaty is bound by the treaty's scope of application. Thus, illegality usually culminates in lack of jurisdiction.

168. However, the issue is not as simple as depicted above in both theory and practice. One has to deal with the general and specific consequences of illegality and consider whether illegality

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[286] *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2); *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2).

[287] *Quiborax S.A., Non-Metallic Minerals S.A. v. Plurinational State of Bolivia* (n 2) [266]; *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [165].

[288] *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 2) [255]. A study by UNCTAD also considers the inclusion of the 'in accordance with the law' clause as a 'narrowing technique' used in international investment agreements. UNCTAD, *Scope and Definitions* (n 11) 5, 28-29.

affects jurisdiction, admissibility, or as some have indicated, the merits of the claim. Should a jurisdictional analysis prevail, delving into an academic analysis, one should also consider the main reason for lack of jurisdiction in case of illegality: does, as the *Phoenix* tribunal has put it, illegality lead to the absence of one of the elements of the term 'investment', or is the lack of jurisdiction due to the fact that the host state has not extended its consent to illegal investments? If the latter is correct, is it a matter of lack of consent, lack of jurisdiction *ratione materiae*, or both?

169. In addition, illegality does not always occur in a very crystal-clear manner by the investor committing an obvious crime in the process of making the investment and by the tribunal merely dismissing the case. Special circumstances may arise in various cases, including cases where the public officials of the host state are actively engaged in the corrupt or otherwise illegal investment process, either by awareness or by direct or indirect involvement. In such situations, the investor, who might have had good faith, or had no option but to grease the unclean palms, might come up with a defence of *estoppel* or acquiescence and ask the tribunal to allow it to pass the jurisdictional barriers built by the respondent state.

170. This Section thus deals with these two issues in turn: first, the general and specific consequences of the legality requirement and second, the possible defences by an investor to an illegality defence raised by the host state.

### a. General and Specific Consequences of the Legality Requirement

171. As was stated above, defences of illegality, corruption, and fraud have become regular defences by host states in many international investment arbitration cases in recent years. The reason for raising such defences from a substantive point of view is, in the first place, that host states are rightly entitled to deny protection to investors who have occupied investment opportunities, most of the times to the exclusion of others, without complying with the laws and regulations of the host state. In addition, the litigation strategy reason for the respondent state's illegality defence is that, if pleaded successfully, the host state would, on most occasions, have the whole investor's case dismissed as a matter of lack of jurisdiction or inadmissibility.[289] The general and specific legal consequences of illegality will be explained below.

#### i. General Consequence of Illegality

172. As a matter of common sense, it is obvious that international protection through investment treaties cannot be granted to investments that are flagrantly made contrary to the laws of the host state. In this connection, the tribunal in *Teinver v. Argentina* observed that: "It is widely acknowledged in investment law that the protections of the ICSID dispute settlement mechanism should not extend to investments made illegally…"[290] Indeed, granting protection to such investments would undercut all the concerns for legality which are inherent in the very inclusion of the legality requirement in investment treaties. Although the violation in question

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[289] See C Knahr (n 7) 18 (anticipating in 2007 that the awards in *Fraport* and *Inceysa* could "open the gate" for states to make alleged violations of their domestic law by investors a regular objection to the jurisdiction of ICSID Tribunals.) See also *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [43] (stating that considering the all-encompassing nature of the respondent's defence, a finding of illegality by the tribunal "would constitute a complete bar to the entire case advanced" by the claimants.)

[290] *Teinver v. Argentina* (n 228) [317]. See also *Plama Consortium Limited v. Bulgaria* (n 39) [138]-[139]; *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [100]-[101]; *Gustav F W Hamester GmbH & Co KG v Republic of Ghana* (n 41) [123]-[124]; *SAUR International SA v Republic of Argentina* (n 43) [308].

is a violation of the laws of the host state, due to the express or implied *renvoi* to the laws of the host state in the underlying treaty, such violation takes an international effect, which effect would be the denial of international substantive and procedural protection to the illegal investment.[291] It has been asserted by some commentators that there is no known ICSID case in which the tribunal admitted the claims after finding that the claimant had made its investment in violation of the host state's laws through corruption, fraud, or other serious illegality.[292] Therefore, the general consequence of illegality is denial of international substantive and procedural protection to investments made illegally.

### ii. Specific Consequence of Illegality

173. It is submitted that in case the relevant legal provisions or principles of the host state law are not observed by the investor in the process of establishing its investment, then the express or implied legality requirement of the investment in the underlying investment treaty is not satisfied, and, therefore, the tribunal would lack jurisdiction to decide the case on its merits. The simple reason is that in such a scenario, the investment in question would not fit in the treaty's scope of application, and, thus, would be excluded from the jurisdictional realm of an investment treaty tribunal which derives its jurisdiction from that investment treaty.[293]

174. A very well-known example of dismissing jurisdiction due to illegality is the *Fraport* case.[294] In *Fraport v. Philippines*, the tribunal held that the claimant had made its investment in violation of the laws of Philippines, in particular, foreign ownership and control legislation known as the Anti-Dummy Law ("ADL"). The tribunal found that through 'secret shareholder agreements', Fraport sought to exercise managerial control over Philippine International Air Terminals Co. ("PIATCO"). PIATCO had concluded the concession contract for the construction and operation of an international passenger terminal at Ninoy Aquino International Airport in Manila ("Terminal 3") with the Philippine Department of Transportation and Communication ("DOTC") in 1997. The tribunal concluded that through these 'secret shareholder agreements', Fraport knowingly orchestrated its investment by circumventing the ADL and in flagrant violation of the ADL.[295] Rejecting Fraport's argument that the issue as to whether the Philippine laws were abided by would only be of municipal not international legal significance, the tribunal held that "[a] failure to comply with the national law to which a treaty refers will have an international legal effect."[296] The tribunal ended up deciding that because there was no 'investment in accordance with law', it lacked jurisdiction *ratione materiae* and, therefore, dismissed the case in its entirety.[297]

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[291] See *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [394].

[292] CB Lamm, BK Greenwald & KM Young (n 13) 349.

[293] See *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [372]. Of course, as has already been explained, depending on the terms of the treaty in question, in such a case, another course of action for an investment treaty tribunal is to rule that the claims presented to arbitration are inadmissible and to reject the case on this basis rather than to dismiss the case on jurisdiction. See Section One *supra*, Subsections B & C.

[294] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25.

[295] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [125], [309], [319]-[322], [354]-[355].

[296] ibid [394].

[297] ibid [401]. This decision was annulled by an ICSID Annulment Committee, consisting of Peter Tomka, Dominique Hascher, and Campbell McLachlan, on the ground that there was 'a serious departure from a fundamental rule of

175. In another leading case, decided 6 years later, the *Metal-Tech* tribunal found, as a factual matter, that the investor had paid certain individual consultants (including an Uzbek government official and the brother of the then Prime Minister of Uzbekistan) to use their position in the Uzbek Government and their family relationship to the Prime Minister, respectively, to facilitate the establishment of Metal-Tech's investment, in violation of the Uzbek Criminal Code and the legality requirement of the investment treaty. Therefore, the tribunal found that it lacked jurisdiction to hear the parties' claims and counterclaims brought under the relevant BIT.[298]

176. Another notable example in this respect is the award in *Alasdair Ross Anderson et al v. Republic of Costa Rica*[299] which concerned claims brought by 137 Canadian individual nationals against the Government of Costa Rica, alleging that the host state had failed to provide proper vigilance and regulatory supervision over its finance system, which negatively affected their investments, in violation of the BIT provisions regarding full protection and security, fair and equitable treatment, due process of law, and protection against expropriation.[300] The alleged investment made by the claimants was funds deposited with a scheme instituted by two Costa Rican individuals, Villalobos brothers, in exchange for a high interest rate on their deposit and repayment of the principal amount.[301] In deciding the dispute, the tribunal found, as a threshold matter, that it was "clear that the transaction by which the Claimants obtained ownership of their assets (i.e. their claim to be paid interest and principal by Enrique Villalobos) did not comply with the requirements of the Organic Law of the Central Bank of Costa Rica and that therefore the Claimants did not own their investment in accordance with the laws of Costa Rica."[302] The tribunal, thus, found that:

> The entire transaction between the Villalobos brothers and each Claimant was illegal because it violated the Organic Law of the Central Bank … If the transaction by which the Villalobos acquired the deposit was illegal, it follows that the acquisition by each Claimant of the asset resulting from that transaction was also not in accordance with the law of Costa Rica.[303]

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procedure'. The Committee found that substantial materials which were produced after the oral procedure formed the basis of the tribunal's ruling on illegality. The departure from a fundamental rule of procedure was that the tribunal did not permit submissions from the parties on these heavily relied upon evidence. In other words, the Committee held that since the right to be heard and the right to have adequate opportunity for rebuttal had not been observed by the tribunal, there was a serious departure from the principles of natural justice. See *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide, 23 December 2010 [177]-[178], [218], [227], [246]-[247].

[298] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [372]-[373].

[299] *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9).

[300] ibid [16].

[301] ibid [18].

[302] ibid [57]. Article 116 of the Organic Law of the Central Bank of Costa Rica provides that only entities expressly authorised by law may engage in financial intermediation in Costa Rica, and Article 157 of the same Law criminalises engaging in financial intermediation without authorisation. Ley Orga´nica del Banco Central de Costa Rica No 7558 (1995). See ibid [54].

[303] ibid [55].

The tribunal thus concluded that it lacked jurisdiction over the dispute because there was no investment made in accordance with the laws of Costa Rica, and, therefore, dismissed the whole case.[304]

177. Despite what was said above, it should be recalled that certain tribunals, arbitrators, and commentators have suggested that in the case of illegality, the issue should be considered as a question of merits rather than as a matter of jurisdiction (or admissibility). The prime examples for adoption of such a view are the awards in *Plama v. Bulgaria*[305] and *Malicorp v. Egypt*.[306] In *Plama*, for example, the tribunal decided to hear the allegation of the investor's fraudulent misrepresentation in the merits phase of the case. After a full hearing of all the relevant evidence and arguments, the tribunal was able to conclude that the respondent's case of fraudulent misrepresentation by the claimant had been proven. For the tribunal, the consequence of such a finding was not the vitiation of the tribunal's jurisdiction but the dismissal of the claimant's claims on the basis that its unlawful investment would not be protected by the substantive protections of the ECT.[307]

178. The first point to be noted in this respect is that in *Plama*, the case was brought under a treaty which did not contain a legality requirement, i.e., the ECT. Therefore, the abstention by the tribunal from rejecting the case on jurisdictional grounds is not strange since there is nothing in the ECT to directly and expressly confine the scope of the application of the Treaty, and, therefore, the tribunal's jurisdiction, to legal investments. Once again, everything goes back to the text of the pertinent treaty. In *Metal-Tech v. Uzbekistan*, the tribunal rightly mentioned that: "[T]he Contracting Parties to an investment treaty may limit the protections of the treaty to investments made in accordance with the laws and regulations of the host State. Depending on the wording of the investment treaty, this limitation may be a bar to jurisdiction, i.e. to the procedural protections under the BIT, or a defense on the merits, i.e. to the application of the substantive treaty guarantees."[308] Bearing this in mind, in cases of illegal investments with a treaty stipulation forbidding illegality, the claim should be dismissed on jurisdiction since legality is a jurisdictional condition provided by the treaty. One commentator has provided a cogent explanation for this jurisdictional consequence of illegality, explicating that, in such circumstances, the case should be dismissed on jurisdiction rather than on the merits:

> "In accordance with host State law clauses" are one of the available means by which States can limit their consent to arbitration by excluding investments made in breach of the host country law, and hence not worthy of protection. There seems to be no plausible ground for excluding illegal investments only from substantive protection under the BITS and not from

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[304] ibid [59]. See also *Inceysa Vallisoletana S.L. v. Republic of El Salvador*, ICSID Case No. ARB/03/26, Award, 02 August 2006 [209] (stating that "it is important to repeat that […] the legality of the investment is a premise for this Tribunal's jurisdiction.")

[305] *Plama Consortium v. Republic of Bulgaria* (n 38) [130].

[306] *Malicorp Ltd v. Arab Republic of Egypt*, ICSID Case No ARB/08/18, Award, 07 February 2011 [119]. Judge Bernardo M. Cremedas seems to be a believer of such a view too. He adopted this viewpoint in his Dissenting Opinion in *Fraport v. Phillipines*. See Dissenting Opinion of Mr. Bernardo M. Cremades in *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, 19 July 2007 [37]-[38], [40]-[41].

[307] *Plama Consortium v. Republic of Bulgaria* (n 38) [143].

[308] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [127].

> jurisdictional protection as well. The offer of arbitration (or of any other dispute settlement mechanism) is in fact an integral and extremely relevant part of the promotion and protection regime assured by BITS. The clauses in question are therefore proper limits to the jurisdiction of tribunals constituted pursuant to the international instruments in which the clauses are contained.[309]

179. In the same vein, in *Inceysa v. El Salvador*, the tribunal held that contracting parties signing investment treaties have broad discretion to limit their consent to arbitration, and hence, the jurisdiction of arbitral tribunals, to disputes that meet certain criteria determined by them. In view of the tribunal, it was "perfectly valid and common" for states to exclude from their consent and from the jurisdiction of the tribunal certain types of disputes or to limit their consent to disputes that are within the limits indicated in investment treaties.[310]

180. Moreover, and quite apart from the reasoning above, according to the *Phoenix* tribunal, in manifest cases of violation of host state law, the consideration of 'judicial economy' would militate against asserting jurisdiction by the tribunal.[311] Therefore, to promote 'judicial economy', in cases where the illegality is so manifest, the claim based on an illegal investment should be dismissed on jurisdiction.

181. To recap, in cases where the legality requirement is stipulated in the underlying investment treaty, or in instances where such requirement is implied from other terms and provisions of the treaty, non-compliance with the laws of the host state should culminate in the dismissal of jurisdiction. Conversely, if there is no trace of the legality requirement in the relevant international agreement, as explained earlier in this Chapter, the better course of action for the adjudicating forum is to dismiss the case, not on jurisdictional grounds, but either on the ground of inadmissibility or as a matter of merits. In the latter situation, to promote 'judicial economy' when the circumstances so require, the better course of action seems to be dismissing the case on admissibility grounds rather than on the merits.

### iii. The Missing Jurisdiction Limb

182. So far, I have concluded that a violation of the laws of the host state at the time of making the investment should move a tribunal to dismiss the case on jurisdictional (or admissibility) grounds. The question that remains is what leg or legs of the jurisdiction chair are missing when illegality occurs? Does the illegality break the subject-matter jurisdiction leg (or the so-called jurisdiction *ratione materiae*), or does it damage the *ratione voluntatis* leg of the jurisdiction chair? As a point of departure, it should be noted that for an investment treaty tribunal to be able to decide a case on its merits, it has to make sure that four jurisdictional requirements are met: *ratione personae*, *ratione temporis*, *ratione materiae*, and *ratione*

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[309] A Carlevaris (n 7) 49. For further commentary, see C Knahr (n 7) 17-18.

[310] *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 7) [184]. See also ibid [195].

[311] *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [104]. Similarly, deciding whether to consider the alleged illegalities as a matter of jurisdiction or merits, the *Minnotte* tribunal thought it imperative to analyse whether the alleged illegalities were "so manifest, and so closely connected to the facts (such as the making of an investment) which form the basis of a tribunal's jurisdiction as to warrant a dismissal of claims *in limine* for want of jurisdiction." See *David Minnotte and Robert Lewis v. Republic of Poland*, ICSID Case No. ARB(AF)/10/1, Award, 16 May 2014 [132].

*voluntatis*.[312] The first two jurisdiction legs are by their nature obviously out of the question for present purposes. Therefore, there remain two legs at the front of the jurisdiction chair: *ratione materiae* and *ratione voluntatis*.

183. There are two different approaches adopted by investment treaty tribunals with regard to the missing jurisdictional limb in the case of illegality: A very limited number of tribunals have considered legality to be an element of the objective definition of an 'investment'. On the other hand, a majority of investment treaty tribunals have opted for the view that, in case of an illegality, jurisdiction does not exist due to the non-existence of a stipulated legal condition for an 'investment', which is the core subject-matter of an investment treaty, and, thus, non-satisfaction of the *ratione materiae* condition. Interestingly, most of the tribunals of the second group have at the same time taken the position that illegality of investments nullifies consent and, thereby, negates *ratione voluntatis*.

184. Starting with the viewpoint adopted by the first group, according to which legality is an element in the objective definition of an 'investment', the *Phoenix* tribunal, which seems to be the biggest advocate of this approach, expressly included the legality requirement within the elements of the so-called '*Salini* test'.[313] Thus, according to this tribunal, the legality of an investment is an element of the objective definition of 'investment'.[314]

185. The other approach, i.e. lack of jurisdiction because of absence of a stipulated legal condition of an 'investment', opposes the inclusion of the legality element in the objective definition of 'investment' and believes, depending on the language of the treaty at stake, that the legality requirement is a component of consent or legal (rather than economic) element of an 'investment'. In *Metal-Tech v. Uzbekistan*, the tribunal said that:

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[312] See M Sornarajah, *The International Law on Foreign Investment* (n 3) 359-360. See also *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [54].

[313] *Phoenix Action, Ltd. v. The Czech Republic* (n 39) [114].

[314] This objective definition is most frequently referred to as the '*Salini* test' according to which the term 'investment' implies the presence of the following elements: (i) a contribution of money or other assets having economic value, (ii) a certain duration over which the economic activity is implemented, (iii) assumption of risk, and (iv) a contribution to the host state's development. *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco*, ICSID Case No. ARB/00/4, Decision on Jurisdiction, 23 July 2001 [52]. See also *Jan de Nul N.V. v. Arab Republic of Egypt*, ICSID Case No. ARB/04/13, Decision on Jurisdiction, 16 June 2006 [91]. It deserves mention that not all the subsequent investment treaty tribunals have followed all the requirements of the definition of 'investment' as identified by the '*Salini* test'. Indeed, some tribunals have simply ignored the test and some have applied the test less stringently. See, e.g., *Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania*, ICSID Case No. ARB/05/22, Award, 24 July 2008 [307-322]. That being said, a majority of tribunals have adopted the criteria almost verbatim or with some variations. As such, the '*Salini* test' remains the dominant theory for the objective definition of the term 'investment' though sometimes with certain amendments. For a recent decision on the applicability of the '*Salini* test' see *Cortec Mining Kenya Limited, Cortec (Pty) Limited and Stirling Capital Limited v. Republic of Kenya*, ICSID Case No. ARB/15/29, Award of the Tribunal, 22 October 2018 [291 *et seq*]. It is also worthy of note that this test has impacted investment treaty rulemaking. Indeed, several recent investment treaties list 'the commitment of capital or other resources', 'the expectation of profit', and 'the assumption of risk' (all elements of the '*Salini* test') in definitions of the term 'investment'. See, for instance, Article 8.1 of Comprehensive Economic and Trade Agreement (CETA) between Canada, of the One Part, and the European Union And Its Member States, signed on 30 October 2016, not yet entered into force, defining the term 'investment' in the following way: "investment means every kind of asset that an investor owns or controls, directly or indirectly, that has the characteristics of an investment, which includes a certain duration and other characteristics such as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk …".

> [T]he Contracting Parties to an investment treaty may limit the protections of the treaty to investments made in accordance with the laws and regulations of the host State. Depending on the wording of the investment treaty, this limitation may be a bar to jurisdiction, i.e. to the procedural protections under the BIT, or a defense on the merits, i.e. to the application of the substantive treaty guarantees.
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> […]
>
> Respondent submits that it "consented to arbitrate only those disputes concerning lawfully implemented investments. Where, as here, the investment at issue was made and implemented contrary to the laws and regulations of the Republic of Uzbekistan, Respondent has not granted its consent to arbitrate before ICSID a dispute concerning that investment." Whether the Respondent's consent covers the present dispute depends on the content of the BIT and in particular on Article 8(1) thereof. If the requirements set in Article 8(1) are not met, then the Respondent has not consented to submit the present dispute to ICSID arbitration and the *ratione voluntatis* condition required by Article 25(1) of the ICSID Convention is not satisfied.[315]

186. Apparently adopting an interpretive approach based on Article 31(1) of VCLT, the *Saba Fakes* tribunal indicated that the 'legality' of an investment cannot be incorporated into the definition of the term 'investment' in Article 25(1) of the ICSID Convention "without doing violence to the language of the ICSID Convention".[316] The tribunal then went on to conclude that the legality of investment is a matter of consent rather than the economic definition of the term 'investment':

> As far as the legality of investments is concerned, this question does not relate to the definition of "investment" provided in Article 25(1) the ICSID Convention and in Article 1(b) of the BIT. In the Tribunal's opinion, while the ICSID Convention remains neutral on this issue, bilateral investment treaties are at liberty to condition their application and the whole protection they afford, including consent to arbitration, to a legality requirement of one form or another. This is precisely the case of the Netherlands-Turkey BIT, which contains such a requirement in its Article 2(2) […]
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> […]
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> […] This provision plainly states that the BIT protection shall not apply to investments which have not been established in conformity with the

[315] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [127], [129]. See also ibid [372]-[373].

[316] *Saba Fakes v. Republic of Turkey* (n 69) [112]. In this case, jurisdiction was ultimately dismissed by the tribunal not due to the illegality of the investment but because the tribunal concluded that "Mr. Fakes has not made any investment in Telsim which would satisfy any of the three criteria for an investment to exist within the meaning of Article 25(1) of the ICSID Convention". The tribunal, accordingly, dismissed the claims for lack of jurisdiction and ordered Mr. Fakes to pay all of Turkey's fees and costs, finding that it did not need to determine "whether Mr. Fakes' transaction was conducted in accordance with the Respondent's laws and regulations relating to the admission of investments in Turkey and, thus, satisfied the requirement of legality set forth by the BIT to qualify as an investment protected by that instrument". ibid [147]-[149].

> Respondent's laws and regulations, the term "investment" having been defined in Article 1(b) of the BIT. If this condition is not satisfied, the BIT does not apply. As a result, the Contracting Party cannot be deemed to have given its consent to arbitrate the dispute under Article 8(3) of the BIT and there would therefore be no consent to the Centre's jurisdiction within the meaning of Article 25(1) of the ICSID Convention.[317]

187. Finally, in *Quiborax v. Bolivia*, the respondent had asserted that the legality requirement was an element of the '*Salini* test'.[318] The arbitral panel disagreed.[319] In its analysis, the tribunal opined:

> … [T]he Tribunal is of the view that neither conformity to the laws of the host State nor respect of good faith are elements of the definition of investment. The Contracting Parties to the BIT have limited the protections of the treaty to investments made in accordance with the law of the host State. This limitation may be a bar to jurisdiction, i.e. to the procedural protections under the Treaty, or to the application of the substantive treaty guarantees as a matter of merits … That does not mean that these elements are part of the definition of investment. *An illegal or bad faith investment remains an investment. It may not be a protected investment, i.e. deserve protection in the sense that access to treaty arbitration and/or substantive treaty guarantees may not be granted, but that is a different matter.*[320] (emphasis added)

188. These criticisms of the *Phoenix* approach seem to be well-placed. The whole idea behind the so-called '*Salini* test' is a definition of the term 'investment' from an economical point of view. If one reviews the elements enumerated for the test, one realises that these factors (contribution of economic resources, risk, duration, and regularity of profit and return) are all economic characteristics of an investment.[321] Having this in mind, it is hardly arguable that 'legality', as a legal attribute, is an economic feature of this type of economic operation. In fact, whereas the '*Salini* test' seeks to identify an 'investment' from an economic perspective, the legality requirement intends to examine the protectability of an 'investment' by the investment treaty from a legal point of view.

189. Another line of reasoning which reveals the inaccuracy of the *Phoenix* decision in including the legality requirement as an element of the '*Salini* test' is the array of awards and decisions which rule that the 'legality requirement' in an investment treaty has nothing to do with the

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[317] ibid [114]-[115].

[318] *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 2) [199].

[319] ibid [219].

[320] ibid [226]. The tribunal went on to consider the legality requirement as an element of jurisdiction *ratione materiae*: "… [I]n order for the Tribunal to conclusively ascertain whether or not it has *ratione materiae* jurisdiction over Quiborax and NMM, it must examine Bolivia's next objection." Bolivia's next objection was non-compliance with the laws of Bolivia in making the investment. ibid [237], [282].

[321] Sasson believes that the term 'investment' was originally a feature of economic analysis rather than an issue in international treaties protecting the rights and properties of aliens. See M Sasson (n 2) 101-102. Dolzer and Schreuer also opine that, in contrast to terms like 'rights', 'property', and 'interests', which have acquired legal meanings, the term 'investment' has its origin in economic terminology. See R Dolzer & C Schreuer (n 107) 60.

definition of investment according to the laws of the host state. To give only one example amongst many, in *Salini v. Morocco,* the state party to the dispute invoked Article 1(1) of the Italy-Morocco BIT, which entails a legality requirement and refers to the term 'investments' in the following way: "the categories of assets invested ... in conformity with that Party's laws and regulations". Morocco asserted that the underlying investment transaction relied upon by the claimant in this case did not fall within the scope of the notion of investment as defined under Moroccan law as required by Article 1(1) of the BIT, and, therefore, no investment existed under Article 25(1) of ICSID Convention. Put differently, the respondent state argued that the legality requirement of the BIT would mean that the notion of investment must be exclusively interpreted according to the domestic law of the host state. The tribunal rejected this argument by stating that 'in accordance with host State clauses' concern the validity of the investment and not its definition. It particularly said that this provision "… seeks to prevent the Bilateral Treaty from protecting investments that should not be protected, particularly because they would be illegal."[322]

190. Having said that, there remains a confusion as to the reasoning of the proponents of the second view, i.e. those who believe that illegality results in no jurisdiction due to the absence of a *legal* condition attributed to the term 'investment' by the contracting parties to the treaty: while some of the decisions and awards supporting this view correctly reject the inclusion of the legality requirement in the '*Salini* test', they go on to say, on the one hand, that there is no jurisdiction because there is no consent (no *ratione voluntatis*), and on the other hand, that there is no investment as a result of illegality, and thus no jurisdiction *ratione materiae*.

191. One can obviously say that non-compliance with the laws of the host state militates against jurisdiction *ratione materiae*. This issue could be considered from two different lenses: (i) the contracting parties to the treaty have expressly or impliedly limited the scope of the term 'investment' to 'legal' investments. Therefore, the subject-matter of the tribunal's jurisdiction is limited to legal investments.[323] (ii) since an investment procured by illegal acts (like fraudulent behaviour, misrepresentation, or bribery) does not comport with the condition of 'legality' which is, in many legal systems, a condition for the validity of a contract,[324] then there is no contract, and, therefore, no contractual or property rights to protect. Since there is no right, then there is no investment, and since there is no investment, there is no jurisdiction *ratione materiae* for the investment treaty tribunal.

192. On the other hand, one could say that the issue could exclusively be looked at from a 'consent' or *ratione voluntatis* angle. In this sense, one should merely focus on the scope of the consent given by the contracting parties in the relevant investment treaty. This has been clarified by very straightforward terms by the *Inceysa* tribunal. In *Inceysa*, the tribunal

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[322] *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco* (n 34) [46]. See also *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29, Decision on Jurisdiction, 14 November 2005 [109]-[110]; *L.E.S.I. S.p.A. and ASTALDI S.p.A. v. République Algérienne Démocratique et Populaire* (n 75) [83]; *Saipem S.p.A. v. The People's Republic of Bangladesh*, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007 [79] fn 11; and *Desert Line Projects LLC v. The Republic of Yemen* (n 75) [102]-[105].

[323] The *Fraport* tribunal considers the legality requirement as a "jurisdictional limitation *ratione materiae*". See *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [334].

[324] For instance, under Article 215 of the Iranian Civil Code, "the object of the contract should have financial value and embody reasonable and legitimate interest."

determined that the consent granted by El Salvador in the BIT "is limited to investments made in accordance with the laws of the host State of the investment", and that "disputes that arise from an investment made illegally are outside the consent granted by the parties and, consequently, are not subject to the jurisdiction of the Centre ..."[325] The tribunal found that Inceysa's investment was not made in accordance with Salvadoran law, because Inceysa had obtained its concession contract through misrepresentations during the public bidding process, including with respect to the identity of its strategic partner which was considered as "a deceit on one of the central aspects of the bid".[326] The tribunal, thus, concluded that, "because Inceysa's investment was made in a manner that was clearly illegal, it is not included within the scope of consent expressed by Spain and the Republic of El Salvador in the BIT and, consequently, the disputes arising from it are not subject to the jurisdiction of the Centre."[327]

193. In reconciling these two apparently overlapping views, one has to understand the meaning and effect of the term 'consent'. This term seems to have two meanings: (i) the first meaning of consent is equivalent to the term *ratione voluntatis*, which concerns the general expression of will regarding submission of disputes to arbitration. (ii) the second meaning is more specific, that is the submission of specific types of disputes to arbitration, like disputes concerning investments. In the second sense, if one bears in mind the general idea that when entering into investment treaties, states can limit the scope of their consent, one comes to the conclusion that when there is a legality clause inserted in the investment treaty by the parties, in case of an illegality, the logical consequence can only be the dismissal of a claim at the jurisdictional stage for lack of one of the requirements set out either in Article 25(1) of the ICSID Convention or other instruments governing the arbitration of the investment dispute, which requirement is consent to arbitration.[328] Therefore, the legality requirement circumscribes the types of the investments that the treaty applies to, i.e. legal investments, and, thereby, determines the types of disputes with respect to which the parties have consented to be referred to arbitration, i.e. disputes with respect to legal investments. In addition, by conditioning the term investment to 'legality', states would effectively limit the subject-matter scope of application of the treaty and, thus, the tribunal's jurisdiction. This twofold function of the legality requirement has been well-explained by the *Quiborax* tribunal: "… under the Bolivia-Chile BIT, the legality requirement is relevant to determine both the Treaty's scope of application and the scope of Bolivia's consent to arbitration."[329] In summation, it appears that lack of legality taints both 'consent', in its narrower sense, and subject-matter jurisdiction.

### b. Possible Defences by Investors

194. Faced with the defence of illegality by the host state, an investor might allege that dismissing the case on this ground would defeat the treaty's object and purpose. More frequently, however, are cases in which the investor tries to bring the host state in by making

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[325] *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 7) [207].

[326] ibid [123]. The tribunal found that Inceysa violated, among other things, the principle of good faith, the principle that no one should be permitted to profit from their own fraud, international public policy, and the prohibition against unlawful enrichment, all of which, according to the tribunal, were incorporated into Salvadoran law. See ibid [239], [242]–[243], [252]–[253].

[327] ibid [207], [257].

[328] A Carlevaris (n 7) 42.

[329] *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 2) [255].

accusations against the recipient state, triggering the so-called idiom of "misery loves company". The investor would do so under the following kinds of allegations: (i) the host state knew about the illegality but did not object at the time; (ii) the officials of the host state were involved in the corrupt process leading to the establishment of the investment. Furthermore, an investor might allege that it had no ill-intention when committing the illegality (iii). Whether these defences would take the investor anywhere will be subject to in-depth analysis in the following sequence in the upcoming pages: (i) object and purpose of the treaty; (ii) the involvement of the host state; and (iii) the good faith of the investor.

### i. Object and Purpose of the Underlying Investment Treaty

195. The general and overbroad statements in preamble of investment treaties regarding the protection of investments may tempt investors to use them in investment treaty arbitrations in various guises. In particular, faced with an illegality defence, an investor might seek to invoke the sweeping preambular investment protection language in the treaty. There seems to be little merit in invoking the vague and general sentences regarding the object and purpose of the treaty in countering the allegations of illegality when the explicit terms of the treaty or mandatory rules of international law call for dismissing the case. Thus, the *Fraport* tribunal articulated in its Award that:

> It is also clear that the parties were anxious to encourage investment, which was the *raison d'etre* of the treaty. But while a treaty should be interpreted in the light of its object and purposes, it would be a violation of all the canons of interpretation to pretend to use its objects and purposes, which are, by their nature, a deduction on the part of the interpreter, to nullify four explicit provisions.[330]

196. Moreover, when considering the preamble for the purpose of interpreting the legality requirement, the preambular paragraphs should be seen holistically. In *Quiborax v. Bolivia*, the tribunal recalled that the objectives of the BIT as set out in its preamble are twofold. While such objectives seek to preserve the investor's interests, at the same time, they also ensure the safeguarding of the interests of the state: "the Preamble of [the BIT] states that the Parties "recogniz[e] the need to promote and protect foreign investments in order to support the economic prosperity of both States" and "wish[] to strengthen the economic cooperation to benefit both States." Accordingly, within the limits set by the applicable treaty interpretation rules, the Tribunal favours a balanced interpretation that takes account of the need to protect foreign investments, on the one hand, and of the State's other responsibilities, on the other."[331]

197. Therefore, depending on the circumstances, a defence against the illegality argument, solely based on the object and purpose of an investment treaty as reflected in the preamble of the investment treaty in question would most probably be unavailing.

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[330] See *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [340]. By 'four explicit provisions', the tribunal was referring to Article 1(1), Article 2(1), Ad Article 2, and the Philippine Instrument of Ratification of the Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments (n 3). For the proposition that preambular languages in investment treaties are not particularly handy in resolving technical questions of jurisdiction, see Chapter 2, Section Two, A.b.ii *supra*.

[331] *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 2) [264].

### ii. The Involvement of the Host State

198. In certain circumstances, prominently in corruption and bribery cases, the host state, or persons representing it, contribute to illegality by, for instance, asking for and accepting bribes and inducements. In other situations, the illegal obtaining of the investment occurs despite the fact that the state is kept in the picture and is mindful of the illegal conduct. For example, assume that the investor procures the investment by violating a material provision of the foreign investment law of the host state. The host state takes cognizance of this fact but for some reasons does not contemporaneously object. Therefore, the question at issue here is whether one should take into account the knowledge and/or the contribution of the host state, or its representatives, in the equation of illegality. In other words, if the host state is aware of a breach of its laws in the period of making the investment or if it has contributed to the corruptive course of conduct, shall the illegality still act against the investor by simply denying jurisdiction? In effect, this question seeks to verify whether, as alleged by some, the only victim of the illegality should be the investor and whether the state, so involved in illegality, could benefit from its wrongdoing or negligence. These issues will be considered below.

1st. *Knowledge of the State*

199. Under this sub-heading, I am going to analyse a situation under which the recipient state is aware of a breach of its laws but nevertheless does not object to the disclosed illegality contemporaneously. It was suggested by the tribunal in *Fraport v. Philippines* that had Philippines known of the investor's illegal conduct, it might have been 'estopped' from invoking the illegality in arbitration. The tribunal explained, on the basis of the doctrine of *estoppel*, that the state could not have invoked breaches of the domestic law by the investor as a bar to jurisdiction if it had known them, or might have known them, and had knowingly overlooked them upon the admission of the investment.[332] In the same vein, other tribunals have stressed the need to protect the investor's reliance on the apparent validity of the investment transaction as practically acknowledged by the state.[333]

200. In a dissent to the Judgment in the *Case Concerning the Temple of Preah Vihear*, Judge Spender described the test for *estoppel* in international law in the following terms:

> [T]he principle [of estoppel] operates to prevent a State contesting before the Court a situation contrary to a clear and unequivocal representation previously made by it to another State, either expressly or impliedly, on which representation the other State was, in the circumstances, entitled to

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[332] See *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [346]-[347]. However, the arbitrators found no evidence of the state's awareness of the investor's unlawful behaviour, and, therefore, concluded by majority decision that they lacked jurisdiction.

[333] *Ioannis Kardassopoulos v. The Republic of Georgia* (n 11) [191]-[192]:

> The assurances given to Claimant regarding the validity of the JVA and the Concession were endorsed by the Government itself ... The Tribunal also notes that the Concession was signed and 'ratified' by the Ministry of Fuel and Energy, an organ of the Republic of Georgia. The Tribunal further observes that in the years following the execution of the Jvn and the Concession ... Georgia never protested nor claimed that these agreements were illegal under Georgian law. In light of all of the above circumstances, the Tribunal is of the view that Respondent created a legitimate expectation for Claimant that his investment was, indeed, made in accordance with Georgian law and, in the event of breach, would be entitled to treaty protection.

> rely and in fact did rely, and as a result the other State has been prejudiced or the State making it has secured some benefit or advantage for itself.[334]

201. Accordingly, the representation upon which the principle of *estoppel* is based has to be 'clear and unequivocal' and there must be actual and justified reliance by the other party.[335] It is clear from the adjectives 'clear' and 'unequivocal' that the satisfaction of *estoppel* requirements should be given a high evidentiary threshold. Therefore, a simple inaction on the part of the host state to prosecute a breach of its laws cannot discharge the investor's onus of establishing 'clear and unequivocal' representation by the state. Similarly, engaging in settlement negotiations with the investor does not mean that the state has acquiesced to the illegality.[336]

202. On the other hand, under the same principles discussed above, one could say that if pursuant to a formal inquiry from the investor, providing a correct state of the facts, the host state explicitly acknowledges the validity of the investment despite the non-compliance with the host state law, on the very same points which the state later objects to in the course of an investment treaty arbitration, the state cannot later claim the illegality of the investor's actions or inactions as a jurisdictional bar.

203. Be that as it may, one should still be mindful that the issue in question, i.e., the legality of investments, is one of jurisdiction. An arbitral tribunal has the duty to ensure that it has jurisdiction under the relevant treaty. The tribunal in *Eureko v. Slovakia* correctly indicated that:

> … jurisdiction is fixed by laws […] and that such jurisdiction cannot here be created, continued or extended by arguments based on the possible operation of doctrines of acquiescence, waiver or estoppel in respect of acts or omissions of Respondent (or Claimant)…[337]

204. In other words, the principle of *estoppel* or waiver cannot extend the scope of an investment treaty tribunal's jurisdiction. In effect, the only venue for the tribunal to ascertain jurisdiction under such circumstances, i.e., an admitted illegality on the part of the investor known to but actively ignored by the host state, seems to be making certain that the host state has indeed consented, under the applicable standards of the specific treaty, to extend the treaty protection to the specific investment at bar.

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[334] *Temple of Preah Vihear* (*Cambodia v. Thailand*) (Merits) Judgment, I.C.J. Rep. 1962 (15 June 1962) p 6, Dissenting Opinion of Judge Spender, pp 143-44.

[335] This formulation of the elements necessary for the application of *estoppel* have been reiterated in the subsequent jurisprudence of the ICJ: See *Land, Island and Maritime Frontier Dispute* (*El Salvador v. Honduras: Nicaragua intervening*) Application to Intervene, Judgment, I.C.J. Rep. (1990) (13 September 1990) p 92, p 118 ("essential elements required by estoppel: a statement or representation made by one party to another and reliance upon it by that other party to his detriment or to the advantage of the party making it."); *North Sea Continental Shelf* (*Federal Republic of Germany v. Denmark; Federal Republic of Germany v. Netherlands*), Judgment, I.C.J. Rep. 1969 (20 February 1969) p 3, p 26; accord *Delimitation of the Maritime Boundary in the Gulf of Maine Area* (*Canada v. United States of America*), Judgment, I.C.J. Rep. 1984 (12 October 1984) p 246, p 309.

[336] *Quiborax S.A., Non Metallic Minerals S.A. and Allan Fosk Kaplún v. Plurinational State of Bolivia* (n 2) [257].

[337] *Achmea B.V. v. The Slovak Republic*, UNCITRAL, PCA Case No. 2008-13 (formerly *Eureko B.V. v. The Slovak Republic*), Award on Jurisdiction, Arbitrability and Suspension, 26 October 2010 [219].

205. As it appears from these discussions, analysis of this nuanced issue is very fact-specific and should be decided on a case-by-case basis. In any event, in my opinion, for a tribunal to decide this issue, it needs to analyse, at least, the following factors: (i) the good faith of the investor and the amount of due diligence it had in familiarising itself and complying with the law of host state; (ii) the timespan in which the investor performed the relevant investment contract or acted under the investment authorisation from the time the state knew of the alleged illegality until it raised its objection to the alleged illegality (which mostly occurs in the wake of a dispute between the parties); (iii) the level of the state's knowledge of the illegality and the circumstances under which the state accepted the contract or issued the investment permit; (iv) the contemporaneous reaction of the two other organs of the state (usually the legislative and the judiciary) to the illegality of the investment (at the time of the establishment of the investment or immediately before or after the making of the investment); and (v) the contributions the state made to the investment despite the knowledge of illegality (like providing land, raw materials, etc.), and the benefits reaped by the host state during the operation of the illegal investment, if any.[338]

2nd. *Involvement of the Host State in the Corruption*

206. A state or persons representing the state could, in theory, contribute to the illegal acquisition of an investment by, for instance, accepting bribes. One important preliminary observation is that, technically speaking, in cases of bribery, it is not the host state *qua* the host state which benefits from the illicit payment. Rather, the individuals acting on behalf of the state reap such illegal benefits. In fact, if the recipient state is the beneficiary of the payment, it would not be a bribe anymore, rather, it would be better characterised as part of the consideration of the investment contract, irrespective of whether it is labelled as royalty fee, tax etc. Put differently, whereas, in the former situation, individuals take personal advantage of the payments, in the latter situation, the money remitted would go to the national fund and would constitute part of the budget of the state.[339]

207. It is also important to bear in mind that despite the involvement of certain representatives of the host state in the illegality, the interests of an investor with no clean hands shall not prevail over the public interests. The distinction between the public interests on the one hand and the interests of the respondent in an investment treaty arbitration on the other hand is important. The investor should be sanctioned not in order to benefit the respondent but rather to preserve the public interests. Furthermore, such an investor shall not be assisted by an arbitral tribunal in his/her illegal conduct by allowing him/her to use the apparatus of investment treaty arbitration. In this respect, the *World Duty Free* award refers to a statement from "Chitty on Contracts" which is illustrative of the above-mentioned point, although primarily from the perspective of English jurisprudence:

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[338] As support for some of these propositions, see *Ioannis Kardassopoulos v. The Republic of Georgia* (n 11) [191]-[192]; *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [346]; *Desert Line Projects LLC v. The Republic of Yemen* (n 75) [105]; *Inmaris Perestroika Sailing Maritime Services GmbH and Others v. Ukraine* (n 221) [140].

[339] *World Duty Free Company v Republic of Kenya* (n 50) [169], [178]. It should also be noted that those officials who are involved in taking bribes usually face civil, administrative, and criminal sanctions when the corruption issue is divulged. This is while, the foreign investor, because of his being foreign, usually escapes the adverse municipal legal consequences and sanctions of the host state.

> "Illegality may affect a contract in a number of ways but it is traditional to distinguish between (1) illegality as to formation and (2) illegality as to performance ..." "Where a contract is illegal as formed, ..., the courts will not enforce the contract, or provide any other remedies arising out of the contract. The benefit of the public, and not the advantage of the defendant, being the principle upon which a contract may be impeached on account of such illegality, the objection may be taken by either of the parties to the contract. 'The principle of public policy', said Lord Mansfield, 'is this: *ex dolo malo non oritur actio*. No court will lend its aid to a man who founds his cause of action upon an immoral or illegal act. If, from the plaintiff's own stating or otherwise, the cause of action appears to arise *ex turpi causa*, or the transgression of a positive law of this country, there the court says he has no right to be assisted. It is upon that ground the court goes; not for the sake of the defendant, but because they will not lend their aid to such a plaintiff. So if the plaintiff and the defendant were to change sides, and the defendant were to bring his action against the plaintiff, the latter would then have the advantage of it; for where both are equally at fault, *potior est conditio defendentis*.' The rules on illegality have been criticised as being unprincipled but a better way of viewing them, as the previous dictum from *Holman v. Johnson* illustrates [...], is as 'being indiscriminate in their effect and are capable therefore of producing injustice.' The 'effect of illegality is not substantive but procedural', it prevents the plaintiff from enforcing the illegal transaction. The '*ex turpi causa* defence', as was stated by Kerr L.J. in *EuroDiam Ltd v. Bathurst* [1990] QB 1, 'rests on a principle of public policy that the courts will not assist a plaintiff who has been guilty of illegal (or immoral) conduct of which the courts should take notice. It applies if in all the circumstances it would be an affront to public conscience to grant the plaintiff the relief which he seeks because the court would thereby appear to assist or encourage the plaintiff in his illegal conduct or to encourage others in similar acts'. ..... illegal contracts are not devoid of legal effect, but the *ex turpi causa* maxim entails that no action on the contract can be maintained."[340]

208. Having said that, the tribunal in *World Duty Free* indicated that "it would be "an affront to public conscience" to grant to the claimant the relief which it seeks because this tribunal "would thereby appear to assist and encourage the plaintiff in his illegal conduct."[341] Another relevant point put forward by *World Duty Free* tribunal is that "the law protects not the litigating parties but the public; or in this case, the mass of tax-payers and other citizens making up one of the poorest countries in the world."[342]

209. The tribunal in *Metal-Tech* also dealt with this issue. Although the tribunal was "sensitive to the ongoing debate that findings on corruption often come down heavily on claimants, while

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[340] ibid [161] (referring to HG Beale (ed), *Chitty on Contracts* (Vol. 1, 28th edition, Sweet & Maxwell 1999) [17-007]).

[341] ibid [178].

[342] ibid [181].

possibly exonerating defendants that may have themselves been involved in the corrupt acts", and noted that "the outcome in cases of corruption often appears unsatisfactory because, at first sight at least, it seems to give an unfair advantage to the defendant party", it explained that "the idea . . . is not to punish one party at the cost of the other, but rather to ensure the promotion of the rule of law, which entails that a court or tribunal cannot grant assistance to a party that has engaged in a corrupt act."[343]

210. All in all, the involvement of certain representatives of the government of the host state in the illegality is not a viable defence for an investor to sustain in order to protect itself against the illegality that it committed while establishing its investment.

3rd. *Investor's Good Faith*

211. As alluded to above, in certain situations, the investor may allege that although there is illegality, i.e. breach of the laws of the host state at the time of making the investment, it had no ill-intention to violate such laws. This could be due to two distinct reasons: (i) it did not know that it was breaching the laws of the host state; or (ii) it was forced into the corruption by the authorities of the host state.

212. To begin with the first reason, i.e., that the investor did not know that it was breaching the laws of the host state, it is noteworthy to recall an old maxim: "ignorance of the law is no defence". This same rule applies to an investor venturing its capital, equipment or technical knowledge abroad. In fact, an investor must take the host state law as he finds it and should familiarise himself with the law of the place where he is going to invest in, including at the time when he is establishing his/her investment.[344] According to the tribunal in *Alasdair Ross Anderson v Republic of Costa Rica*, each investor "must meet [the legality] requirement, regardless of his or her knowledge of the law or his or her intention to follow the law".[345] Pursuant to the above observation, the intention of the investor and his knowledge of the laws and regulations of the host state at the time of making the investment have no role to play in the compliance with the legality requirement equation.

213. As an aside, in most of the corruption situations (obviously not always), it is hard to consider genuine an investor saying that it did not know about the law of the host state. As quite correctly suggested by Llmazon, investors acting in this way always know the illegality of their actions yet decide to engage in corruption anyway, either overtly or tacitly.[346] In addition, as has been pointed out by one commentator, absolving investments violating the laws of the host state by an allegedly genuine investor from the jurisdictional scrutiny seems problematic since it will probably be difficult in many instances to determine, from a factual

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[343] *Metal-Tech Ltd. v. Republic of Uzbekistan* (n 2) [389].

[344] *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile*, ICSID Case No. ARB/01/7, Award, 25 May 2004 [197]-[206]; *Gami Investments, Inc. v. The Government of the United Mexican States*, UNCITRA, Final Award, 15 November 2004 [91]; *International Thunderbird Gaming Corporation v. The United Mexican States* (n 230) [164]; *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [58] (observing that "prudent investment practice requires that any investor exercise due diligence before committing funds to any particular investment proposal. An important element of such due diligence is for investors to assure themselves that their investments comply with the law."); C McLachlan, L Shore & Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (OUP 2017) 309-310.

[345] *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [52]. See also C Knahr (n 7) 17.

[346] AP Llamzon (n 8) 5.

point of view, whether an investor had actually acted in good faith or whether he had knowingly committed a violation of the host state's domestic law.[347]

214. Having said that, an exception could be made to this statement and that exception concerns the case of investing in countries whose laws are not clear or easily-accessible, and there is no chance to obtain access or clarity by a good faith effort via inquiring from the governmental authorities of the host state or by soliciting legal advice from a proper professional law firm or reputable freelance lawyers. In this connection, the *Fraport* tribunal said: "in some circumstances, the law in question of the host state may not be entirely clear and mistakes may be made in good faith …"[348] This situation of unclear laws was unsurprising in the early days of the real burgeoning of arbitration, which to me is the period after the end of World War II. At the time, and in the early 1960s, many countries had recently been decolonised and had premature and underdeveloped legal systems. Therefore, when engaged in international arbitrations, even when their law was chosen as the governing law to the contract by the parties themselves, the law was found to be inapplicable by the arbitral tribunal due to being vague and unsophisticated.[349] However, this trouble is not as prevalent around the world nowadays, although one cannot argue with certainty that it does not exist at all any longer. In fact, despite the numerous initiatives both at the national and international level to promote the transparency of investment legislation,[350] the investor is often not in a position to obtain sufficient knowledge of all relevant pieces of legislation. In my opinion, if in such circumstances, the badly advised investor, who means well and has done its best to acquaint itself with the laws of the host state,[351] acts timely in curing or rectifying a non-compliance, good faith

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[347] On this point, Carlevaris aptly points out that it "is in fact more difficult to determine the investor's good faith and knowledge of the causes of the illegality than the identity of the norms allegedly violated and the seriousness of the breach." See A Carlevaris (n 7) 47. In the same vein, Knahr commentates that a subjective assessment "seems problematic since it will probably be difficult in many instances to determine whether an investor had actually acted in good faith or whether he had knowingly committed a violation of a host state's domestic law. Hence, an objective assessment of the severity of the violation … seems preferable." See C Knahr (n 7) 17.

[348] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [396]-[398].

[349] For instance, in *Petroleum Development Ltd. v. Sheikh of Abu Dhabi*, Lord Asquith of Bishopstone, the umpire, stated that since no body of settled legal principles for the construction of modern commercial instruments existed in the Sheikhdom, and since justice was discretionary "in this very primitive" country, its laws could not be applied to the contract. *Petroleum Development Ltd v. Sheikh of Abu Dhabi* (*Abu Dhabi Case*) (1951) 18 ILR 144.

[350] See, for instance, the World Bank Guidelines:

> Each State is encouraged to publish, in the form of a handbook or other medium easily accessible to other States and their investors, adequate and regularly updated information about its legislation, regulations and procedures relevant to foreign investment and other information relating to its investment policies.

Guidelines on the Treatment of Foreign Direct Investment (1992) 7 ICSID Rev-FILJ 297. See also Articles 10 and 11 of the 2012 United States Model BIT, especially Article 10(1) which reads:

> Each Party shall ensure that its: (a) laws, regulations, procedures, and administrative rulings of general application; and (b) adjudicatory decisions respecting any matter covered by this Treaty are promptly published or otherwise made publicly available.

[351] *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile* (n 344) [197]-[206]; *Gami Investments, Inc. v. The Government of the United Mexican States* (n 344) [91]; *International Thunderbird Gaming Corporation v. The United Mexican States* (n 230) [164]; *Alasdair Ross Anderson et al v. Republic of Costa Rica* (n 9) [58] (observing that "prudent investment practice requires that any investor exercise due diligence before committing funds to any particular investment proposal. An important element of such due diligence is for investors to assure themselves that their investments comply with the law."); C McLachlan, L Shore & Matthew Weiniger (n 344) 309-310.

interpretation of the treaty requires that the investment be deemed lawful. Such rectifying action could be deemed as 'timely' when it occurs as soon as the investor becomes aware of the illegality, which should more preferably be before arising of a dispute, or, at the latest, the filing of a claim. Furthermore, the investor should present evidence that the advice it received misled it and confused its understanding of the host state law. It goes without saying that the investor must also show that it was reasonable for it at the time of making the investment to rely on the advice, which later proves to be wrong. Additionally, an investor cannot be heard to argue that it violated a mandatory rule of international law since it did not know whether the host state law included this norm or not. Therefore, these conditions must be satisfied cumulatively for an investor to be able to get away with the illegality: (i) the investor must show that it had good faith, for instance, by showing that it has not been condemned in the host state or any other state for commission of crimes or other sorts of illegalities of the kind at stake; (ii) it should show that it acted reasonably and did its best efforts to acquaint itself with the laws of the host state, for example, by hiring a reputable local lawyer or law firm; (iii) it should prove that the legal regime of the host state was nevertheless far away from transparent and clear; (iv) it should also establish that before a dispute arose, and upon being notified of the illegality it acted immediately to rectify the illegality to the extent possible; and (v) the investor cannot be heard to say that it violated a mandatory rule of international law, like prevention of bribery, under the impression that the laws of the host state did not entertain this rule.

215. As to the other reason for committing an illegality despite having good faith, i.e., having to pay bribes to get the investment project, one must observe that it is no legal excuse for the investor to avow that corruption is a common practice in the recipient country without which the award of a contract is difficult or even impossible.[352]

216. To conclude on this point, unless very special circumstances exist, the investor's good faith or lack of knowledge as to the laws of the host state do not nullify illegality or its consequences.[353]

217. That being said, it should be noted that jurisdiction would be dismissed if the illegality is the result of the investor's action or inaction. In other words, it is the investor's conduct which should be checked against the legal provisions of the host state. Therefore, if the alleged illegality is something which is the exclusive result of the violation of the host state law by the authorities of the host state in the course of the admission or establishment of the investment, then the legality requirement cannot be evoked to bar the tribunal from exercising jurisdiction. For instance, if according to the laws of country "A", investments in the public transportation

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[352] See *World Duty Free Company v Republic of Kenya* (n 50) [156] (reviewing ICC practice on this issue). That being said, in case the bribe is obtained by use of force, coercion, or oppression, then the scenario would probably be different. See ibid [181].

[353] On the other hand, a finding of bad faith or intentional violation of the host state law would buttress the tribunal's finding on illegality and, consequently, would lead to a decision of lack of jurisdiction. In *Fraport v. Philippines*, the investor had concluded certain secret and concealed shareholding agreements, which were in violation of Philippine's Anti-Dummy Laws. This action on the part of the investor had a twofold meaning to the arbitral panel: first that the host state had no way of knowing the illegality of the claimant's illegal arrangements; second, and more importantly, the investor did not act in good faith in non-compliance with the laws of the recipient state. *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines* (n 2) [323], [326]-[327], [332], [346]-[347], [355], [387], [398]. This latter finding arguably played an important role in the tribunal's persuasion for dismissing jurisdiction. ibid [323], [327], [398].

section should be procured through a bidding process, but the ministry of transportation of that country, with no legal justification, concludes a contract for urban track-building directly with an innocent and clean-handed foreign investor without holding a bidding process, then the host state cannot in later arbitration proceedings invoke the violation committed by itself to have the case dismissed. In fact, in such a situation, the illegality is beyond the investor's control. As stated in *Kardassopoulos v Georgia*, a state cannot avail itself of its own wrongdoing in order to deny protection of the investment under an investment treaty (*nemo auditur propriam turpitudinem allegans*):

> 183. […] the Tribunal observes that Respondent does not allege that Claimant committed any act in violation of Georgian law. Quite the contrary, it is the Respondent which argues that its State-owned enterprises violated Georgian law by exceeding their authority, thus rendering void *ab initio* the JVA and the Concession.
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> 184. Accordingly, Article 12 of the BIT cannot be invoked by Respondent to exclude Claimant's investment from protection under the BIT. It follows that notwithstanding the fact that the JVA and the Concession may be void *ab initio* under Georgian law, Claimant's investment nonetheless remains entitled to protection under the BIT and the Tribunal so finds.[354]

**Conclusion**

218. One of the prime areas in investment treaty arbitrations in which the municipal laws of the host state apply as 'law' is the jurisdictional issue of the legality requirement. Domestic laws of the host state determine whether the investment in question was established in a lawful manner or not. The application of the laws of the host state to the question of the determination of the legality of the investment is principally because of the express or implied agreement of the investment treaty contracting parties to the application of the laws of the host state to this matter. In any event, it was demonstrated in this Chapter that even if no reference has been made to the laws of the host state for the purpose of determining the legality of the investment, general principles of law require the application of the internal laws of the host state since unlawful investments, i.e., investments made in contravention of the host state law, do not deserve protection under international investment agreements. It was submitted that in this latter situation, i.e., lack of any legality requirement in the investment treaty at stake, the tribunal may dismiss the case on the ground of inadmissibility rather than lack of jurisdiction.

219. Like any other condition, the legality requirement has a limited scope. Although due to the use of open-textured terms of 'laws', 'regulations, and 'legislation' in the legality requirement, the 'formal' scope of the requirement is usually broad and mostly uncontroversial, the 'substantive' scope of the legality requirement is quite vague, which vagueness has created

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[354] *Ioannis Kardassopoulos v. The Republic of Georgia* (n 11) [183]-[184]. In that case, the tribunal found further support for its reasoning from the 'representations and warranties' given by the Georgian public authorities in the relevant instruments concerning the investment, in the frequent assurances and confirmations given by authorities of the host state as to the investment's legality, and in the lack of objections or complains during the period following the conclusion of the investment. ibid [185]-[194]. According to the tribunal, the overall conduct of the respondent had given rise to the investor's 'legitimate expectations' that the investment complied with the Georgian law. See ibid [192]-[194].

much controversy and ambiguity in practice and scholarship. It was submitted in this Chapter that a 'balanced' and 'holistic' interpretation of the legality requirement would include in the 'substantive' realm of the condition the fundamental laws of the host state (its constitution, its organic laws (if any), and its mandatory laws) as well as the ordinary laws of the host state, to the extent that the latter laws are violated at the time of the initiation of the investment in order to guarantee the establishment or the success of the investment. Finally, as the 'ordinary meaning of the terms' used in a typical legality requirement indicates, the 'temporal' scope of the legality requirement is confined to breaches of the internal laws of the host state at the time of making the investment not the subsequent violation of such laws.

220. As was shown in this Chapter, subject to the wording of the legality requirement in question, the violation of the laws of the host state at the time of the establishment of the investment leads to the negation of a legal attribute to the subject-matter of the dispute, i.e., investment. In this sense, the investment treaty would not apply to an investment which is not made in accordance with the laws of the host state. As a result, the investment treaty arbitral tribunal which derives its jurisdiction from the treaty in question will not have the competence to decide the case due to lack of jurisdiction *ratione materiae*.

221. Finally, unless absolutely manifest circumstances exist, the investor's good faith or its lack of knowledge would not absolve it from the legal consequences of non-compliance with host state law in the course of making its investment. Furthermore, the involvement of the host state authorities in a corruptive act leading to the establishment of the investment will not excuse the investor's illegal conduct at the time and will not bar the legal consequences of the legality requirement from being implemented in case of violation of the laws of the host state.

## Chapter 3: Application of Domestic Law to the Question Regarding the Creation/Existence of Rights/Interests Constituting Investments

### Introduction

1. As was indicated earlier, terms like 'property' and 'asset' frequently appear in introductory provisions of investment treaties which purport to define 'investment'. These core concepts ('property' and 'asset') are not usually defined in the text of the investment treaty itself. The determination of the meaning, scope, and legal consequences of these terms is central to the scope of application of investment treaties, and, therefore, to the jurisdiction of an arbitral tribunal owing its jurisdiction to such treaties. In other words, the very core object of protection in investment treaties is a property right or a bundle of property rights and/or interests. These property rights or interests, when coupled with necessary economic features, will form investments which are the subject-matter of investment treaties.[1] As a result, before inquiring about the legality of an investment, in order to ascertain jurisdiction *ratione materiae*, a tribunal should verify whether there exist property rights/interests capable of constituting investments.
2. Due to this obvious centrality of the concepts of 'property' and 'asset' for the investor's investment treaty case, respondent states are seen nowadays to object to the existence of property rights/interests constituting investments more frequently. Through such jurisdictional defences, the recipient states argue before the adjudicating forum that the investor has acquired no rights and/or interests over properties or assets under its legal system. One reason for deploying such a defence is that, if successfully pleaded, as recent case-law has proven, the respondent would have all of the investor's substantive claims dismissed based on and due to the inexistence of rights and/or interests over properties and assets allegedly constituting investment, and, as a result, for want of subject-matter jurisdiction.
3. For an arbitral tribunal to decide such an issue, it should answer three critical questions: first, why such matters should be resolved by reference to the laws of the host state? second, if the laws of the host state are applicable to such issues, how is the tribunal supposed to ascertain the contents of such law? and third, if it finds, based on a proper analysis of the host state law, that the state party to the dispute is right that there are no rights and/or interests recognised under the laws of the host state, how does that finding of law influence the jurisdiction of an investment treaty tribunal? Relevant in this respect is also the application of host state law to specific contract and property law questions in a jurisdictional equation. Whereas the second question will be addressed in Chapter 4 of this Thesis which focuses on the methods for ascertaining the contents of host state law, the other questions will be dealt with in the present Chapter.
4. In order to answer the questions subject to this Chapter, the discussion will be followed in two Sections: (**One**) the legal basis for referring to the laws of the host state; (**Two**) The actual application of the domestic law to particular questions regarding the creation and existence of rights/interests. Section Two will be divided into two subsections: **(A)** The general function of the host state law in determining the jurisdiction *ratione materiae* of an investment treaty tribunal; and **(B)** the application of domestic law of the host state to the specific relevant

[1] If one considers 'investment' as a tree sapling planted by a gardener to benefit from its fruits later, the root of the sapling would be the existence of valid and legal rights over properties and assets.

property and contract law questions before an investment treaty tribunal in a jurisdictional context.

## Section One: The Legal Bases for Referring to the Laws of the Host State

5. When faced with a defence according to which there are no rights and/or interests over properties or assets raised by a respondent state, the first question that should be answered by an arbitral tribunal called on to decide an investment treaty dispute is the basis and the legal footing for the application of the laws of the host state in an international arbitration proceeding. Indeed, an international tribunal applying and interpreting an international investment treaty in an international dispute naturally expects to apply international law to the issues before it, including to the matters regarding jurisdiction,[2] unless there is a plausible reason, like a *renvoi*, which validates reference to and application of another body of law.

6. It is submitted that customary international law has no rule to define 'property' and/or 'asset'. As a corollary, unless the contracting parties to the investment treaty have defined 'property' an/or 'asset' for the purpose of their investment treaty relations,[3] in most cases, it is the law of the host state that governs the issue of the existence of rights/interests over properties/assets underlying investment. This phenomenon of referring to the laws of the host state for ascertaining the existence of rights/interests underlying investments is so generally accepted that in one leading investment treaty case, both parties to the dispute practically affirmed the application of host state municipal law to the questions of existence and nature of the rights which were the essence of the alleged investment:

> [T]he existence and nature of any such rights must be determined in the first instance by reference to Hungarian law, before the Tribunal proceeds to decide whether any such rights can constitute investments capable of giving rise to a claim for expropriation for the purpose of its jurisdiction under the Treaties and the ICSID Convention. That is the basis upon which Claimants plead their case. Respondent submits the same. The Tribunal agrees.[4]

7. As will be discussed below, there are two legal grounds which warrant the application of the laws of the recipient state to the jurisdictional question of the existence of rights/interests over properties and/or assets. Considering the nature of the issue, it is submitted that it is exclusively

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[2] O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 94. See also VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (2006) 23(4) J Int'l Arb 268 (stating that the role of international law has arguably been put to rest in the foreign investment treaty regime of dispute resolution.)

[3] Indeed, although customary international law has no rules defining the concepts of 'rights' and 'property', the contracting parties to an investment treaty are free to define the content of property rights for the purpose of a particular treaty. See M Sasson, *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer Law International 2017) 104-110. See also C Lévesque, 'Investment and Water Resources: Limits to NAFTA' in MC Cordonier Segger, M Gehring, A Newcombe, R Buckley, A Zieglerstating (eds) *Sustainable Development in World Investment Law* (Kluwer Law International 2011) 425 (stating that: "Of course, if the Treaty itself or customary international law recognizes the existence of the alleged 'right' in international law, it is a different situation.")

[4] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary*, ICSID Case No. ARB/12/2, Award, 16 April 2014 [149].

the host state law which is determinative of the existence of rights over properties and assets **(A)**. Indeed, unless the parties have agreed otherwise in the treaty or through subsequent agreement or practice, since general international law does not, in principle, have rules to regulate this matter, this issue should be resolved by reference to host state law. By engaging in a conflict of law analysis in the context of finding the applicable law to the question of the existence of rights and interests over assets and properties, in most cases, one will end up with the outcome of the application of host state law to the question of creation and existence of properties. Finally, it has been observed that some investment treaties contain express or implicit language to the effect that these core private law issues are governed by the domestic law of the host state **(B)**. These two legal bases for referring to the laws of the host state for determining the existence and creation of rights over properties and assets will be analysed below in sequence.

### A. The Nature of the Legal Issue

8. Although it is possible for state parties to an investment treaty to define the terms 'rights', 'interests', 'properties' or 'assets' in the treaty itself, or to do so by way of subsequent agreement, or subsequent practice,[5] however, this is not usually the practice of investment treaties. In fact, an overwhelming majority of investment treaties do not define the terms 'rights', 'properties' or 'assets' and do not specify the legal regime governing the definition of these concepts. What they do instead is to refer to these terms in a general and unqualified manner.
9. According to Article 31 of the Vienna Convention on the Law of Treaties ("VCLT"), treaty terms should be given their 'ordinary meaning'. The question is which legal system defines such concepts and determines their 'ordinary meaning'? As the following discussion will show, it is, in most cases, the law of the host state which supplies the substantive content of the alleged 'right' and/or 'interest' in question.

#### a. Lack of a Response by General International Law in Principle

10. To be sure, several international instruments (mostly draft conventions) have tried to define the term 'property' of aliens for the purpose of international protection against unlawful measures of host states. They include very broad classifications of the term 'property'. Some of such instruments are as follows: the 1961 Harvard Draft Convention on International Responsibility of States for Injuries to Aliens (at Article 10(7))[6] and the 1967 OECD Draft Convention on Protection of Foreign Property (at Article 9(c)).[7] Indeed, these instruments set out the classification of rights protected by international law, like 'tangible' and 'intangible'

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[5] M Sasson (n 3) 104-110; C Lévesque (n 3) 425 (stating that: "Of course, if the Treaty itself or customary international law recognizes the existence of the alleged 'right' in international law, it is a different situation.")

[6] Article 10(7) of this Draft Convention reads:

> The term "property" as used in this Convention comprises all movable and immovable property, whether tangible or intangible, including industrial, literary, and artistic property, as well as rights and interests in any property.

[7] Article 9 (c) of this Draft Convention provides:

> "Property" means all property, rights and interests, whether held directly or indirectly, including the interest which a member of a company is deemed to have in the property of the company ...

properties. However, the problem is that they neither define such rights nor delineate their substantive regime and content. Put differently, these are, in effect, enumerations of rights rather than definitions. Indeed, there is no definition of 'property' or 'asset' in customary international law as these concepts are not created by this body of law.[8] Even assuming that customary international law has a principled definition of property or asset, which as explained above is not the case, customary international law has no rules to deal with the nuances of 'legal entitlements' alleged by investors in various investment treaty cases. For instance, "[t]here is no general international law on the privatisation of insurance companies […], nor is there an international law of television licensing agreements, nor is there an international law of zoning regulations."[9]

11. In addition, most investment treaties do not also define the terms 'property' and 'assets'. What they do instead is categorising different types of assets, which in no way is equivalent to defining the terms 'assets' and 'properties'. For instance, Article 1(1) of the BIT between Germany and Bosnia and Herzegovina provides with respect to the term 'investment' that:

> The term "investments" shall comprise every kind of asset, in particular:
> (a) Movable and immovable property as well as any other rights *in rem*, such as mortgages, liens and pledges;
> (b) Shares of companies and other kinds of interest;
> (c) Claims to money which has been used to create an economic value or claims to any performance having an economic value;
> (d) Copyrights, industrial property rights, technical processes, trade marks, trade names, know-how and goodwill;
> (e) Business concessions under public law, including concessions to search for, extract and exploit natural resources.[10]

12. This provision symptomises an open-ended listing of different arrays of properties and assets covered by investment treaties without defining the terms 'assets' or 'properties' themselves.
13. Being mindful of this, one scholar has opined that: "Investment treaties do not contain substantive rules of property law. There must be a *renvoi* to a municipal property law."[11] It is actually municipal law which has the required apparatuses for defining 'property' and/or 'asset'. This understanding of the applicable law to the questions of creation and existence of rights over properties and assets is shared by awards and decisions of international and national courts and tribunals. Below, I will review some examples from investment treaty arbitrations in this regard.
14. In *Nagel v. Czech Republic* case, the claimant had brought a claim against Czech Republic arising out of the respondent's failure to grant a public tender for mobile phone contracts to

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[8] See *William Nagel v. The Czech Republic*, SCC Case No. 049/2002, Final Award, 09 September 2003 [316]; *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [162]. See also Z Douglas, 'Nothing if Not Critical for Investment Treaty Arbitration: *Occidental*, *Eureko* and *Methanex'* (2006) 22(1) Arbitration International 43-46; Z Douglas, *International Law of Investment Claims* (CUP 2009) 52; M Sasson (n 3) 104-110.

[9] Z Douglas, 'Nothing if Not Critical for Investment Treaty Arbitration: *Occidental*, *Eureko* and *Methanex'* (n 8) 45.

[10] Treaty between the Federal Republic of Germany and Bosnia and Herzegovina Concerning the Encouragement and Reciprocal Protection of Investments, signed on 18 October 2001, entered into force on 11 November 2007.

[11] Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (2003) 74 BYIL 198.

the investor, despite the signature of a cooperation agreement with a state telecommunications company wholly owned by the respondent under which the parties would seek to obtain, through a consortium, the necessary licenses and permits to establish, own, and operate a GSM mobile telephone network in the Czech Republic. The case was submitted on the basis of the BIT between the United Kingdom and Czech Republic.[12] Article 8(3) of that BIT on governing law briefly provided that: "The arbitrator or arbitral tribunal to which the dispute is referred […] shall, in particular, base its decision on the provisions of this Agreement." The central question before the tribunal was whether the cooperation agreement mentioned above constituted an investment protected by the BIT. The claimant asserted that 'assets' are defined by the investment treaty and international law, and not by Czech law as the law of the host state.[13] This argument did not succeed. According to the tribunal, the requirement for the underlying 'right' or 'claim' to have financial value created a link with domestic law. It observed that:

> [W]hen read in their context, the terms "asset" and "investment" in Article 1 shall be considered to refer to rights and claims which have a financial value for the holder. This creates a link with domestic law, since it is to a large extent the rules of domestic law that determine whether or not there is a financial value. In other words, value is not a quality deriving from natural causes but the effect of legal rules which create rights and give protection to them.[14]

Shedding more light on the relation between host state law and rights forming the investment, the tribunal further noted that:

> [T]he basis of Mr Nagel's claims in this case is the Investment Treaty and that that Treaty should be interpreted in accordance with the rules of public international law. However, Czech domestic law will be of some relevance, since the terms "investment" and "asset" in Article 1 of the Investment Treaty cannot be understood independently of the rights that may exist under Czech law. It is therefore necessary to determine what is the legal significance of that Cooperation Agreement under Czech law.[15]

Having made these comments, the tribunal analysed Czech law and concluded that the cooperation agreement was only of a preparatory nature and, hence, the rights derived therefrom had no financial value.[16] The tribunal, thus, came to the conclusion that Mr. Nagel's rights under the cooperation agreement were not such as to constitute an 'asset', and,

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[12] Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Czech and Slovak Federal Republic for the Promotion and Protection of Investments with Protocol, signed on 10 July 1990, entered into force on 26 October 1992.

[13] *William Nagel v. The Czech Republic* (n 8) [82]. See also ibid [127].

[14] ibid [300].

[15] ibid [316].

[16] ibid [328].

subsequently, an 'investment' within the meaning of Article 1 of the United Kingdom-Czech Republic BIT.[17]

15. In *Emmis et al v. Hungary*, the claimants had brought claims against the respondent arising out of the alleged expropriation of claimants' investments in nationwide FM-frequency radio-broadcasting licenses in Hungary, through the Government's decision to award the radio-broadcasting frequencies formerly held by claimants to a third party. The tribunal considered, as a threshold issue, whether the investors had property rights capable of expropriation in 2009. For such determination, it turned to the law of the host state, Hungary. The tribunal evaluated the evidence presented by the parties, including the opinion of Hungarian law experts, and attached weight to the determinations of domestic courts on how Hungarian law should be understood and applied. As to the applicable law to the question of the existence of rights capable of being expropriated, the tribunal pointed out that:

> In order to determine whether an investor/claimant holds property or assets capable of constituting an investment it is necessary in the first place to refer to host State law. Public international law does not create property rights. Rather, it accords certain protections to property rights created according to municipal law.[18]

Based on such analysis of Hungarian municipal law, the tribunal considered that, after the expiration of the Hungarian broadcasting license they held from 1997 until 2009, the investors no longer had any valuable assets that Hungary could have taken.

16. This very concept, i.e. referring to the laws of the host state to ascertain the creation and existence of rights over properties and assets, was confirmed by the tribunal in *EnCana v. Ecuador* which stated that:

> [F]or there to have been an expropriation of an investment or return (in a situation involving legal rights or claims as distinct from the seizure of physical assets) the rights affected must exist under the law which creates them, in this case, the law of Ecuador.[19] [20]

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[17] ibid [329].

[18] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [162].

[19] *EnCana Corporation v. Republic of Ecuador,* LCIA Case No. UN3481, UNCITRAL *(formerly EnCana Corporation v. Government of the Republic of Ecuador),* Award, 03 February 2006 [184]. It is noteworthy that Article XIII(7) of the underlying BIT provided that a tribunal exercising jurisdiction under the BIT "shall decide the issues in dispute in accordance with this Agreement and applicable rules of international law". Agreement between the Government of Canada and the Government of the Republic of Ecuador for the Promotion and Reciprocal Protection of Investments, signed on 29 April 1996, entered into force on 06 June 1997 (subsequently terminated). Unlike many BITs that contain applicable law provisions, there was no express reference to the law of the host state in the applicable law provision. The tribunal nevertheless deemed it necessary to refer to such law for the above-mentioned purpose.

[20] In another case lodged against the Government of Ecuador, the investment treaty tribunal relied upon tax law regulations of Ecuador to decide that the claimant was entitled to VAT refunds under the laws of Ecuador. *Occidental*

17. By the same token, the tribunal in *Total v. Argentina* held that it is the law of the host state, in that case Argentina, that applied to the question of determining the content and the extent of Total's economic rights. It specifically indicated that: "… Argentine law has a broader role than that of just determining factual matters. The content and the scope of Total's economic rights (in Total's words, "Argentina's commitments to Total") [...] must be determined by the Tribunal in light of Argentina's legal principles and provisions."[21]
18. The principle of referring to domestic law for determining the private law entitlements has also been recognised by both PCIJ and ICJ. In one of its famous decisions, the PCIJ considered that: "In principle, the property rights and the contractual rights of individuals depend in every State on municipal law and fall therefore more particularly within the jurisdiction of municipal tribunals."[22] Furthermore, in 2007, in *Diallo* case, the ICJ stated that where an internationally wrongful act is represented by a violation of shareholders' rights, such rights are "defined by the domestic law of that State".[23]
19. In addition, certain decisions of some mixed claims commissions endorse the view that existence and creation of rights on a private plane are, naturally speaking, governed by domestic law. In *George W Cook (USA) v. United Mexican States*, Commissioner Nielsen noted that:

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*Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467, Final Award, 01 July 2004 [136]-[143].

[21] *Total S.A. v. The Argentine Republic*, ICSID Case No. ARB/04/01, Decision on Liability, 27 December 2010 [39]. The tribunal found further support for its holding by referring to the substantial reliance by Total on Argentina's acts of a legislative and administrative nature governing the gas, electricity, and hydrocarbons sectors, as well as the extensive discussion between the parties regarding the content and extent of Total's rights in respect of the operation of its investments, which it deemed to be a recognition that Argentina's domestic law plays a prominent role. ibid. Furthermore, in explicating its position, the tribunal went on to refer to two paragraphs of the Award in *Enron v. Argentina*. One of the paragraphs invoked by the tribunal was paragraph 206, which reconfirms that the role of the domestic law of the host state goes beyond settling factual issues. It also explains that such law governs the creation and existence of the rights underlying the investment:

> The Respondent is right in arguing that domestic law is not confined to the determination of factual questions. It has indeed a broader role, as it is evident in this very case from the pleadings and arguments of the parties that have relied heavily on the Gas Law and generally the regulatory framework of the gas industry, just as they have relied on many other rules of the Argentine legal system, including the Constitution, the Civil Code, specialized legislation and the decisions of courts. The License itself is governed by the legal order of the Argentine Republic and it must be interpreted in its light.

*Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3 (also known as *Enron Creditors Recovery Corp. and Ponderosa Assets, L.P. v. The Argentine Republic*), Award, 22 May 2007 [206].

[22] *Panevezys-Saldutiskis Railway Case* (*Estonia v. Lithuania*), Judgment, P.C.I.J. Rep. Series A/B, No. 76, 1939 (28 February 1939) p 18. Although the present author agrees with the first limb of this statement, however, the second limb (i.e. jurisdiction of the municipal courts to issues of property law) is subject to certain important reservations and discussions in investment treaty arbitrations which will be touched upon in Chapters 5 and 7 of this Thesis.

[23] *Ahmadou Sadio Diallo* (*Republic of Guinea v. Democratic Republic of the Congo*), Preliminary Objections, Judgment, I.C.J. Rep. 2007 (24 May 2007) p 582, p 606 [64].

> When questions are raised before an international tribunal, as they have been in the present case, with respect to the application of the proper law in the determination of rights grounded on contractual obligations, it is necessary to have clearly in mind the particular law applicable to the different aspects of the case. The nature of such contractual rights or rights with respect to tangible property, real or personal, which a claimant asserts have been invaded in a given case is determined by the local law that governs the legal effects of the contract or other form of instrument creating such rights. But the responsibility of a respondent Government is determined solely by international law.[24]

20. The same proposition is also accepted by certain municipal courts. To give one prominent example, in a famous judgment in the dispute between *Van Zyl and Others and Government of Republic of South Africa and Others*, the South African Supreme Court of Appeal considered it as a trite principle of international law that "[p]roperty rights are determined by municipal law. The questions whether any rights have been granted, exist or whether they have terminated are all questions that have to be determined according to local law." It further approved the reality that "[t]here is no universally acceptable concept of property rights".[25]
21. Therefore, as the practice of international courts and tribunals indicates, general international law has no rule to regulate questions of creation and existence of rights over properties and assets. As a review of the above-mentioned examples shows, it is the domestic law of the host state that settles the questions regarding proprietary and contractual rights/interests underlying investments.[26]

### b. Conflict of Laws Rules

22. Considering the fact that general international law does not have an answer to the question of creation and existence of rights/interests underlying investments, the matter should be resolved by domestic law. In such a case, the arbitrator should step into the conflict of laws realm to find the domestic law applicable to the question of creation and existence of rights constituting investments. A proper conflict of law analysis indicates that questions regarding creation and existence of rights underlying investments are governed by the municipal law of the host state, whether such rights are of proprietary or contractual nature or are other types of tangible and intangible rights.
23. It deserves mention at the outset that, whereas, as explained above, the scholarship and the jurisprudence of international courts and tribunals commendably point to the application of domestic law, rather than international law, to such questions, there does not seem to be so many commentators and/or arbitrators to have approached the question based on a proper analysis of conflict of laws, which is the sound approach to identify the governing law to a particular legal issue.
24. When faced with a legal question that it needs to resolve – in this case, the existence of rights and interests constituting investments – the tribunal has to determine the applicable law to that

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[24] *George W Cook (USA) v. United Mexican States* (1927) IV RIAA 213, 215 [7].

[25] *Van Zyl and Others v. Government of Republic of South Africa and Others* (170/06), 20 September 2007, [2007] ZASCA 109 [64], available on the SAFLII website: <www.saflii.org/za/cases/ZASCA/2007/109.html>.

[26] However, as was mentioned above, the parties to the treaty remain free to define 'property' and/or 'asset' in the treaty itself or through subsequent agreement or subsequent practice.

question in the first place. This requires a conflict of laws analysis. The starting point for a conflict of law analysis would be for the adjudicating forum to refer to its applicable rules regarding the determination of governing law. Thus, an ICSID tribunal has to refer to Article 42(1) of the ICSID Convention,[27] an ICC tribunal should refer to Article 21(1) of the ICC Arbitrations Rules of 2017,[28] Article 22(3) of LCIA Arbitration Rules (2014) would be applied by an LCIA arbitral panel,[29] an SCC tribunal should refer to Article 22(1) of the 2010 Rules,[30] finally, an *ad hoc* tribunal working under the 2010 UNCITRAL Arbitration Rules must begin its analysis with Article 35(1) of those Rules.[31]

25. The common feature of all these rules is respecting party autonomy, meaning that the arbitral panel should begin with the agreement of the parties as to the applicable law. Therefore, if the parties expressly refer to a particular law for determining the meaning of the terms 'asset' and 'property', that choice is usually conclusive for the tribunal.[32] However, if the parties have not made such a choice, which is usually the case in investment treaties, four out of five of the arbitration rules mentioned above indicate that the arbitral tribunal shall apply the law which it determines to be 'appropriate'.[33] Several commentators have opined that the effect of this

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[27] Article 42(1) of the ICSID Convention provides that:

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

[28] Article 21(1) of the 2017 ICC Arbitration Rules provides:

> The parties shall be free to agree upon the rules of law to be applied by the arbitral tribunal to the merits of the dispute. In the absence of any such agreement, the arbitral tribunal shall apply the rules of law which it determines to be appropriate.

[29] Article 22(3) of the 2014 LCIA Arbitration Rules provides that:

> The Arbitral Tribunal shall decide the parties' dispute in accordance with the law(s) or rules of law chosen by the parties as applicable to the merits of their dispute. If and to the extent that the Arbitral Tribunal decides that the parties have made no such choice, the Arbitral Tribunal shall apply the law(s) or rules of law which it considers appropriate.

[30] Article 22(1) of the 2010 SCC Arbitration Rules provides:

> The Arbitral Tribunal shall decide the merits of the dispute on the basis of the law(s) or rules of law agreed upon by the parties. In the absence of such agreement, the Arbitral Tribunal shall apply the law or rules of law which it considers to be most appropriate.

[31] Article 35(1) of the 2010 UNCITRAL Arbitration Rules reads:

> The arbitral tribunal shall apply the rules of law designated by the parties as applicable to the substance of the dispute. Failing such designation by the parties, the arbitral tribunal shall apply the law which it determines to be appropriate.

[32] As noted above, it goes without saying that if the parties define the terms 'assets' and/or 'properties' and/or set benchmarks for determining the scope of such terms for the purpose of their bilateral relations, the tribunal should respect their agreement.

[33] As to the ICSID Convention, it is recalled that Article 42(1) provides that in the absence of an agreement of the parties on the applicable rules of law, an ICISD Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable. A direct application of the law of the state party to the dispute by the tribunal plainly culminates in the application of the law of the host state to the question of the existence of rights and interests. In case the tribunal brings into the equation the conflict of laws of the host state, the result would probably be the same. Finally, with respect to this question, i.e. the existence of rights and interests, there are no 'applicable' 'rules of international law' to be considered by an ICSID tribunal.

rule is that arbitral tribunals are not obliged to determine the applicable law by engaging in an analysis of a set of national conflict of law rules of a specific country. Formulated differently, they have the authority to identify the applicable law directly, by choosing the law that they deem most appropriate (*voie directe*).[34] However, this direct selection of law cannot be done arbitrarily. As Heiskanen explains: "the *voie directe* approach remains a conflict-of-laws approach in the sense that it results in a choice of law and accordingly the arbitrators must provide reasons for their (contextual) choice of law." [35] The same observation is made by Derains and Schwartz: "[…] arbitrators may devise their own rule of conflict. However, whatever method is employed, the arbitrators must provide a reasoned explanation for their choice in accordance with the legitimate expectations of the parties."[36] For instance, under the 1998 ICC Arbitration Rules – which had a similar provision on applicable law, i.e., Article 17(1)[37] – the applicable law provision is reinforced by Article 25(2) of those Rules,[38] which requires an ICC tribunal to state the reasons for its award and which, therefore, prompts the tribunal to state why it found the rules of law it chose to be appropriate. Indeed, with respect to the authority of an arbitral tribunal to choose rules of law directly and without reference to any system of conflict of laws, or some particular conflict of law rule, the commentators note that although such authority is, indeed, granted to an arbitral tribunal, it will presumably seek to justify its choice of the applicable law by reference to some choice of law criteria in practice.[39]

26. In stating reasons for its choice of the most appropriate law, an arbitral tribunal acting under either of the foregoing arbitration rules might explain that it is only the domestic law that provides an answer to the question of the definition of 'property' and 'asset'. However, to identify the relevant domestic law, among all possible legal systems, the arbitral tribunal would issue a reasoned award only if it enters into a proper conflict of law analysis. In so doing, it should choose the proper set of choice of law rules. In this respect, several methods have been applied, some of which have proven to be much more sought-after.[40]

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[34] N Blackaby & C Partasides (eds), *Redfern and Hunter on International Arbitration* (OUP 2015) 224; GB Born, *International Arbitration: Law and Practice* (Wolters Kluwer 2012) 242; WL Craig, WW Park and J Paulsson, *Annotated Guide to the 1998 ICC Arbitration Rules with Commentary* (Ocean Publication Inc. 1998) 112; T Begic, *Applicable Law in International Investment Disputes* (Eleven International Publishing 2005) 8-9.

[35] V Heiskanen, 'And/Or: The Problem of Qualification in International Arbitration' (2010) 26(4) Arb Int'l 451, fn 27.

[36] Y Derains and EA Schwartz, *A Guide to the New ICC Rules of Arbitration* (Kluwer Law International 2005) 242.

[37] Article 17(1) of the 1998 ICC Arbitration Rules reads as follows:

> The parties shall be free to agree upon the rules of law to be applied by the Arbitral Tribunal to the merits of the dispute. In the absence of any such agreement, the Arbitral Tribunal shall apply the rules of law which it determines to be appropriate.

[38] This provision of the 1998 Rules reads: "The Award shall state the reasons upon which it is based."

[39] See M Blessing, 'Regulations in Arbitration Rules on Choice of Law' in AJ van den Berg (ed), *Planning Efficient Arbitration Proceedings: The Law Applicable in International Arbitration* (Kluwer Law International 1996) 413; B Wortmann, 'Choice of Law by Arbitrators: The Applicable Conflict of Laws System' (1998) 14(2) Arb Int'l 101.

[40] Gary Born refers to the most popular range of choice-of-law options to be the following: (1) "Choice-of-Law Rules of Arbitral Seat". (2) "Choice-of-Law Rules That Arbitral Tribunal Considers "Appropriate"". (3) ""Cumulative" Application of Choice-of-Law Rules". (4) "Choice-of-Law Rules of State With Closest Connection to Underlying Dispute". (5) ""International" Choice-of-Law Rules". GB Born, *International Arbitration: Law and Practice* (Wolters Kluwer 2016) 233-259. He also refers to two other choice of law methods, which appear to be the result of the application of choice of law rules, rather than the methods themselves. These two options are: (1) "Application of

27. If an investment treaty tribunal opts for the choice of law rules of the arbitration seat or international choice of law rules, the conflict of laws rules of almost all popular seats of arbitration for investment treaty disputes go for the application of the law of the *situs* of the property in matters of acquisition and transfer of property rights. As Rabel put it more than sixty years ago:

> It is at present the universal principle, manifested in abundant decisions and recognized by all writers, that the creation, modification, and termination of rights in individual tangible physical things are determined by the law of the place where the thing is physically situated.[41]

28. Another leading private international law authority has commented that rights over immovable properties are determined by the law of the *situs*.[42]
29. In fact, it has been accepted in numerous legal systems that acquisition of title and property rights in both moveable and immovable properties, the validity of such acquisition, the nature, content, and scope of the rights, their classification, and their termination (whether by way of transfer or extinction) is determined by the laws of a country in which the tangible asset in question is situated (*lex situs* or the law of the *situs*).[43] In other words, the *lex situs* conflicts rule enjoys universal support and application. Bearing in mind the universality of the rule, opting for other conflict of laws methods enumerated above would not, in all likelihood, generate a different result.
30. Given that in most cases, the foreign investment in question is situated in the soil of the host state, the *lex situs*, i.e., the law of the host state, governs the acquisition and termination of rights and interests constituting investments.
31. One should note, however, that investment treaties extend their protection not only to tangible properties (corporeal moveable and immovable assets) but also to intangible properties or incorporeal property. Thus, for instance, Article 1(a) of the 2008 UK Model BIT, expressly includes shares in and stocks and debentures of a company (at sub-section (ii)), claims to money (at sub-section (iii)), and intellectual property rights (at sub-section (iv)) within the safe protected zone of the investment treaty.[44]
32. Intangible property is something of individual value that cannot be touched, held, or pointed at. In other words, intangible property can include any item of worth that is not physical in

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Substantive Law of State With Closest Connection to Dispute". (2) "Application of Non-National Legal System in Absence of Parties' Choice-of-Law Agreement". ibid.

[41] E Rabel, *The Conflict of Laws: A Comparative Study* (Vol. IV, University of Michigan Law School 1958) 30.

[42] PM North & JJ Fawcett (eds), *Cheshire and North's Private International Law* (13th edn, Butterworths 1999) 924, 929-930. Some commentators believe that the determination of rights to immoveables according to the law of *situs* is because of the close control the authorities of the situation of the property have over such assets. See J Hill & MN Shuilleabhain (eds), *Clarkson & Hill's Conflict of Laws* (OUP 2016) 471, 473.

[43] In this respect, see Austrian's International Private Law Act (IPRG) of 1978, Articles 31-32; Belgian Code of Private International Law of 2004, Articles 87 and 94; Dutch Civil Code of 1838, Article 10:127; French Civil Code of 1803, Articles 3(2); German Introductory Act to the Civil Code of 1994, Article 43; Iranian Civil Code of 1928, Article 966; Italian Law on Private International Law of 1995, Article 51; Spanish Civil Code of 1889, Article 10; Swiss Federal Act on Private International Law of 1987, Articles 99-100; US Restatement (Second) on Conflict of Laws, Sections 244 & 246.

[44] The 2008 Model BIT of the Government of the United Kingdom of Great Britain and Northern Ireland.

nature. Therefore, such rights have no physical substance, and, thus, no actual location could be occupied by them. That being said, upon embarking upon a proper conflict of law analysis, in most instances, the same law, i.e. the law of the host state, would apply to the creation and existence of intangible properties. In fact, although intangible properties occupy no space, and, therefore, have no physical location, commentators have suggested that such properties should be artificially located by law.[45]

33. It is submitted that in most cases, the *situs* of intangible properties constituting investments is also the host state. In *Encana v. Ecuador*, the alleged entitlement at stake was the right to VAT refunds which is obviously an intangible right. In determining the applicable law to the question of the existence of legal rights, the majority of the tribunal had no doubt or difficulty to refer to the laws of the host state as the right point of reference. It said that "for there to have been an expropriation of an investment or return (in a situation involving legal rights or claims as distinct from the seizure of physical assets) the rights affected must exist under the law which creates them, in this case, the law of Ecuador."[46]
34. Indeed, with respect to some types of intangible properties protected by investment treaties, the *situs* of the properties is usually the country of the recipient state. In this regard, it is useful to study the relevant *situs* for three kinds of intangible properties frequently subject to investment treaty arbitrations: (i) shares and stocks of a company. (ii) intellectual property rights. (iii) debts and loans.
35. The *situs* of stocks of a company, as a type of intangible personal property, has been held to be at the domicile of the owner[47] or to be at the place where the certificate is found.[48] However, the more authoritative rule would seem to be that the domicile of the corporation is the basis of *situs*.[49] In *Macmillan Inc v. Bishopsgate Investment Trust plc (No 3),* the case involved competing claims to shares in a company which was incorporated in New York, although the transaction on which the parties' claims were based had been effected in London. The English Court of Appeal ruled that the matter as to the owner of the shares should be disposed of in accordance with *lex situs.*

> [T]here is authority and much to be said for treating issues of priority of ownership of shares in a corporation according to the *lex situs* of those shares. That will normally be the country where the register is kept, usually but not always the country of incorporation.[50]

The *situs* of a company whose shares and stocks have been purchased and is supposed to be protected by an investment treaty is in all likelihood the country of the recipient state. In the

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[45] See JG Collier, *Conflict of Laws* (CUP 2001) 251; St. John's Law Review, 'Situs of Intangible Property in Conflict of Laws' (2013) 30(2) St. John's Law Review 225. As Cheshire puts it, "[i]t is of course necessary for certain purposes, such as jurisdiction or probate, to assign a *situs* not only to good will, but to choses in action generally." PM North & JJ Fawcett (eds) (n 42) 927. See also J Hill & MN Shuilleabhain (eds) (n 42) 480.

[46] *EnCana Corporation v. Republic of Ecuador* (n 19) [184].

[47] See *Kilgour v. New Orleans Gas Light Co.*, 14 Fed. Cas. 468, No. 7764 (C.C.D. La. 1875); *Beverly Beach Properties, Inc. v. Nelson*, 68 So. 2d 604 (Fla. 1953) (dictum), cert. denied, 348 U.S. 816 (1954).

[48] See *Bowles v. R.G. Dun-Bradstreet Corp*., 25 Del. Ch. 32, 12 A.2d 392 (Ch. 1940).

[49] See, e.g., *Lockwood v. United States Steel Corp*., 209 N.Y. 375, 103 N.E. 697 (1913); *Doherty v. McDowell*, 276 Fed. 728 (D. Me. 1921); *Iron City Say. Bank v. Isaacsen*, 158 Va. 609, 164 S.E. 520 (1932).

[50] *Macmillan Inc v Bishopsgate Investment Trust plc (No 3)* [1996] 1 WLR 387 at 411.

same vein, in 2007, in *Diallo* case, the ICJ stated that where an internationally wrongful act is represented by a violation of shareholders' rights, such rights are "defined by the domestic law of that State".[51]

36. Similarly, the *situs* of intellectual property rights is the place where protection is sought, i.e. host state.[52] Finally, the *situs* of a debt is where the debtor resides. In cases of banking loans, for instance, the creditor is the bank, and the debtor is, more often than not, the host state. The residence of the host state is the host state with the result that the applicable law to the existence of such an intangible right is the law of the host state.[53]
37. Moreover, since the acquisition of contractual rights in international investment takes place through contracts, especially investment contracts, it should be noted that, in the absence of a choice of law by the parties, the universally-supported conflict of law rule is that the applicable law to such contracts is the law of the place which has the closest connection to the contract. This is pursuant to the application of the 'centre of gravity test' or the 'most significant connection test'.[54] It goes without saying that in most investment cases, it is the host state which has the closest connection to the investment contract. As such, the *lex contractus*, more often than not, coincides with the *lex situs*, i.e. the law of the host state.[55]
38. Having said that, it is worth observing that investment treaty tribunals do not usually enter into a conflict of law analysis in applying host state law to the definition of 'property', 'assets' or 'rights'. In fact, they tend to apply domestic law to this issue without going through a conflict of laws path. The same ignorance can also be traced in doctrinal authorities.

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[51] *Ahmadou Sadio Diallo* (n 23) p 582, p 606 [64].

[52] In this respect, see, for instance, Article 93 of Belgian Code of Private International Law of 2004 providing that "Intellectual property rights are governed by the law of the State for the territory of which the protection of the intellectual property is sought." See also St. John's Law Review (n 45) 228-229. With respect to goodwill, Cheshire touches upon an English Court of Appeal case which indicates that goodwill is deemed to be situated in a country in which the business to which it is attached is carried on. Thus, in the context of an investment treaty dispute, the *situs* of a goodwill would be the host country, where the investment operation was being carried out. See PM North & JJ Fawcett (n 42) 927 (citing *Reuter (RJ) Co Ltd v Mulhens* [1954] Ch 50 at 95, 96, [1953] 2 All ER 1160 at 1183).

[53] See J Hill & MN Shuilleabhain (eds) (n 42) 480, 483-484.

[54] In *Economy Forms Corp. v. Iran*, the Iran-United States Claims Tribunal identified the 'centre of gravity' as the prevailing test for the choice of applicable law to contractual relations under general principles of conflicts of law. *Economy Forms Corp. v. Iran et al*, IUSCT Case No. 165, Award No. 55-165-1, 13 June 1983, 3 Iran-USCTR p 42, pp 47-48. See also *Harnischfeger Corp. v. Ministry of Roads & Transportation*, IUSCT Case No. 180, Award No. 144-180-3, Partial Award, 13 July 1984, 7 Iran-USCTR p 90, p 99; *ICC Award No. 5717* (1990) ICC Bull. No. 2, at 22 *et seq* (stating that: "In complex international relationships such as that under review, a widely accepted choice of law principle in most jurisdictions, including England, Liechtenstein and France, is the center of gravity, or the connection, test. Under this test, the arbitrator selects the substantive law of the jurisdiction that has the greatest connection with the dispute.")

[55] See PM North & JJ Fawcett (eds) (n 42) 936. Article 4(c) of the Rome I Regulation on the applicable law in the absence of choice in contracts for the transfer of rights and interests in immovables reads:

> [A] contract relating to a right in rem in immovable property or to a tenancy of immovable property shall be governed by the law of the country where the property is situated.

See also *Bank of New York and Trust Company et al.* (*USA v. Germany*) 8 RIAA 42, at 43 (indicating that an investment contract of partnership was governed by the law of its *situs*, in that case, the law of Germany); *Rio Grande Irrigation and Land Company (UK v. USA)* 6 RIAA 131, 136 (stating that the applicable law to the validity of a lease agreement is the country of *situs*, in that case, the United States of America).

39. However, a handful of awards, as well as certain seminal academic works in the field of investment treaty arbitration, contain discussions on the relevance of a conflict of laws approach to the determination of the existence of private rights constituting investments. One such award was rendered in the *Nagel v. Czech Republic* case. In that case, the claimant, countering reference to host state law in order to define the term 'asset', asserted that "[t]he doctrine of *renvoi* is widely limited and excluded and cannot be used to refer matters from public international law to a domestic law system."[56] On the other hand, the respondent state posited that although the underlying transaction did not specify the controlling law, under the general conflict of law principles, Czech law was the only logical law to apply because that transaction was entered into and would have been performed primarily in the Czech Republic.[57] In deciding this dispute, the tribunal entered into a brief conflict of law analysis to determine the applicable law to the cooperation agreement in order to see whether this agreement created binding and enforceable rights for the investor vis-à-vis the state. It stated that:

> The Cooperation Agreement had strong links with the Government of the Czech Republic. One of the parties was a Czech State enterprise and the Agreement concerned cooperation in order to obtain rights to operate a GSM system in the Czech Republic. The Arbitral Tribunal therefore considers that Czech law should be regarded as the applicable law of the contract …[58]

40. In another case, the arbitral tribunal applied host state law to the whole case because it applied Article 24 of the SCC Arbitration Rules (the 1999 version) which authorised arbitral tribunals to "apply the law or rules of law which it considers to be most appropriate" in the absence of an agreement between the parties and because the law of the host state was mandatorily applicable to the questions of privatisation of state assets:

> [t]he law of the Republic of Moldova is applicable on the basis of the BIT, is pleaded by the Claimant and is considered applicable by the Arbitral Tribunal on the basis of the choice of law rule contained in article 24 of the Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce (it being the law of the host country of the investment and mandatorily applicable to questions regarding the privatization of state assets).[59]

41. Zachary Douglas describes the need to refer to conflict of laws rules to be more 'acute' in investment treaty arbitrations in comparison to public international disputes. He explains that in the absence of conflict of laws rules in investment treaties, the tribunals should articulate such rules and analysis by having recourse to general principles of private international law

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[56] *William Nagel v. The Czech Republic* (n 8) [127].

[57] ibid [152].

[58] ibid [303]. In fact, the tribunal's view was that in that specific case, it is *lex contractus* which determined the existence of rights under the contract.

[59] *Iurii Bogdanov, Agurdino-Invest Ltd. and Agurdino-Chimia JSC v. Republic of Moldova*, SCC, Arbitral Award, 22 September 2005 [3.2].

and principles derived from the particular architecture of investment treaties. He then goes on to point out that:

> Some choice of law rules have attained such universal application that their transplant into the investment treaty regime cannot generate controversy. Such is the case with the *lex situs* rule for tangible property, which is universally applied by municipal courts […] and must be the appropriate choice of law rule for determining the existence or scope of property rights that comprise an investment. There is considerable authority for the proposition that the application of the *lex situs* rule is even required by general international law …[60]

42. In short, the application of the universal choice of law rules of *lex situs* and *lex contractus* in most cases culminates in the application of the laws of the host state to the questions of existence of rights and interests over properties and assets. This approach to determining the applicable law to the questions of private rights comprising investments has not been duly noted by the scholarship and jurisprudence though some doctrinal authorities and arbitrators have touched upon the relevance and the importance of a conflict of laws analysis in this area.

### B. Reference by the Contracting Parties in the Underlying Investment Treaty

43. As was indicated above, due to the nature of the issue, and also pursuant to a proper conflict of laws analysis, the application of the host state law to issues regarding creation and existence of rights over properties and assets comprising investment is quite obvious. On top of these grounds for the application of host state local law, there are a limited number of investment treaties which explicitly provide that questions regarding creation and existence of rights over properties and assets are determined by reference to host state law. For instance, Article 1(a) of the BIT between the Netherlands and Argentina, after enumerating different categorisations of investments, stipulates that:

> [t]he meaning and scope of the different assets shall be determined by the laws and regulations of the Contracting Party in the territory of which the investment has been made.[61]

44. One of the other most explicit references to the application of host state law was made in the BIT between the United Kingdom and the Government of the Czech and Slovak Federal

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[60] Z Douglas, *The International Law of Investment Claims* (n 8) 44-45. On this point, see also C McLachlan, 'Investment Treaty Arbitration: The Legal Framework' in AJ van den Berg (ed), *50 Years of the New York Convention, ICCA International Arbitration Conference* (Kluwer Law International 2009) 143 (stating with regard to the appropriate choice of law approach in investment treaty arbitrations that: "… [T]his choice of law process may be distinguished from that undertaken in private international litigation or arbitration, since national and international law stand in a vertical, and not horizontal, relationship to each other.")

[61] Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Argentine Republic, signed on 20 October 1992, entered into force on 01 October 1994. See also Article 1(a) of the Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments, signed on 11 December 1990, entered into force on 19 February 1993.

Republic, which was the underlying BIT in the case *Nagel v. Czech Republic*.[62] Article 1(a) of that treaty provided:

> [T]he term "investment" means every kind of asset belonging to an investor of one Contracting Party in the territory of the other Contracting Party under the law in force of the latter Contracting Party in any sector of economic activity …[63]

45. This definition makes clear that in order to be characterised as an 'investment', an 'asset' should, in the first place, belong to the investor under the laws in force of the host state. In *Nagel v. Czech Republic*, the claimant had argued that "[i]nternational law, and not domestic law, is the residual source of governing law… The reference to the host State law in Article 1(a) is irrelevant here because it permits only the exclusion of categories of investment which the host State regards as illegal. It does not permit Czech law to define "asset" or "investment"..."[64] Conversely, Czech Republic relied on this provision to argue that it is the law of the host state which determines whether an investor has made an investment.[65] In applying the host state law to the question of the existence of rights, the tribunal did not specifically grapple with this provision. However, the wording of the provision gives more credit to the respondent's argument. In fact, the provision stipulates that the 'belonging' of an investment to an investor, i.e., the acquisition of the asset underlying the investment and the subsequent ownership rights, should be determined under and in accordance with the law of the host state. So, according to this provision, to determine the proprietary relation between the asset and the person, one has to refer to the law of the host state. Thus, this clause is not merely confined to saying that an investment should be made in accordance with the law of the host state. In other words, it is not merely a stipulation of the legality requirement, although this is also clearly inferred from this provision. This provision also clearly says that the acquisition of the asset underlying the investment should be in accordance with the enforceable laws of the recipient state.

46. Some other investment treaties have such a stipulation with respect to a limited array of assets mentioned in investment treaties. For instance, in certain BITs using an asset-based approach to the term 'investment', intellectual property rights are only accepted as investments if they are recognised by the laws of the host state (and, in some instances, also the home state). For instance, Article 1(iv) of the BIT between Ghana and Guinea solely covers the following array of intellectual property rights:

> Intellectual property rights, goodwill, technical processes and know-how and all similar rights *recognized by the national laws of both Contracting Parties* …[66] (emphasis added)

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[62] *William Nagel v. The Czech Republic*, SCC Case No. 049/2002.

[63] See Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Czech and Slovak Federal Republic for the Promotion and Protection of Investments with Protocol (n 12)

[64] *William Nagel v. The Czech Republic* (n 8) [77].

[65] ibid [180], [182], [185].

[66] Article 1(iv) of the Agreement between the Government of the Republic of Ghana and The Government the Republic of Guinea for the Promotion and Protection of Investments, signed on 18 May 2001, not yet entered into force.

47. Other investment treaties contain the same qualification, although with varying degrees of expression, with respect to business concessions. Such reference to the law of the host state can be found in myriads of investment treaties, including Article 1 of the BIT between Iran and China, which protects in its sub-section (e), "special rights *conferred by law* including rights to search for, extract and exploit natural resources …"[67] [emphasis added] One example of a more explicit nature is Article 1(a)(v) of the United Kingdom-Czech Slovakia BIT mentioned above, which includes as one type of investment: "[B]usiness concessions conferred by law or, *where appropriate under the law of the Contracting Party concerned*, under contract, including concessions to search for, cultivate, extract or exploit natural resources."[68] (emphasis added)

48. Although it is not strictly necessary, reliance on a provision in the treaty, containing the express or implied agreement of the parties regarding the applicable law to the question of existence and creation of rights and/or interests can give more comfort to an international arbitral tribunal, which otherwise needs to engage in a conflict of law analysis and delimit the contours of international law as far as the life and death of the creatures of private law is concerned.

### C. Conclusion

49. As was explained above, questions regarding the creation and existence of rights and/or interests over properties and assets are determined by the law of the host state. This is mainly because the nature of the issue necessitates the application of host state law. Indeed, customary international law does not, in principle, have rules to define the terms 'property' and 'asset. Therefore, unless the parties have defined these terms in the treaty itself or through subsequent agreement or subsequent practice, an investment treaty tribunal needs to refer to domestic law to resolve such matters. A proper conflict of law analysis usually leads us to the application of the law of the recipient state to these matters. This would be either because the contracting parties to the relevant investment treaty have made a choice (party autonomy), or because of choice of law rules like *lex situs* and 'centre of gravity' which call for the application of host state law. The issue is so clear that sometimes the parties to an investment treaty case even do not dispute it. For instance, in *Emmis v. Hungary*, the disputing parties had agreed that the nature of any rights that might form the basis of claimants' expropriation claim was to be determined under Hungarian law.[69]

## Section Two: The Actual Application of Domestic Law to Particular Questions Regarding the Creation and Existence of Rights/Interests underlying Investments

50. Having gone through the legal bases for the application of host state law to the question of the creation and existence of rights/interests underlying investments, I now turn to the application of domestic law to particular practical questions regarding matters of property and contract law that require determination in a jurisdictional analysis. Generally speaking, there are two main

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[67] Agreement on Reciprocal Promotion and Protection of Investment between the Government of the People's Republic of China and the Government of the Islamic Republic of Iran, signed on 22 June 2000, entered into force on 01 July 2005.

[68] Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Czech and Slovak Federal Republic for the Promotion and Protection of Investments with Protocol (n 12)

[69] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [48].

questions concerning the creation and existence of rights which should be addressed by reference to the laws of the host state: first, the general consequences of the application of host state law to this matter, and, second, the specific consequences of the application of host state law to the matters concerning the existence and creation of private rights and interests constituting investments. These two questions will be addressed below in-depth.

### A. The General Function of the Host State Law in Determining the Creation and Existence of Rights/Interests Underlying Investments

51. Having discussed the legal bases for relying on the internal laws of the host state for the purpose of determining the existence of rights underlying investments, at this juncture, I will turn to the critical role that this body of law plays in the jurisdiction *ratione materiae* of an investment treaty tribunal regarding the definition of 'property' and the determination of the scope of rights, assets, and properties which form the root of a tribunal's subject-matter jurisdiction. In this subsection, I will briefly touch upon the effect of existence or non-existence of rights over properties and assets on the jurisdiction *ratione materiae* of an investment treaty tribunal.
52. In case an arbitral tribunal finds that the investor had acquired rights under the laws of the host state at the relevant time, it has advanced one step in ascertaining jurisdiction *ratione materiae*.[70] Stated differently, the existence of rights under the laws of the host state is the core of an investment treaty tribunal's subject-matter jurisdiction. However, this should not be the end of the *ratione materiae* inquiry. The tribunal should then check the possible exclusions and limitations that might be placed by the contracting parties in the investment treaty on the subject-matter jurisdiction of an investment treaty tribunal, including but not limited to the legality requirement. Furthermore, some treaties expressly exclude certain categories of assets from the treaty's scope of application.[71] Upon fulfilling this task, the tribunal should proceed to verify that the right so acquired under the domestic law of the host state, and not otherwise limited or excluded by the investment treaty, satisfies the economic definition of 'investment',[72] and, thus, is an 'investment' protected by the relevant investment treaty.[73]

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[70] Strangely, the tribunal in *Nagel v. Czech Republic* noted that it treated the issue of whether Mr. Nagel made an investment as an issue of merits, rather than jurisdiction. The reason put forward by the tribunal was because the issue could not be "easily decided as a preliminary question of jurisdiction but one which requires a more detailed analysis both of the Treaty and of the facts of the case." See *William Nagel v. The Czech Republic* (n 8) [268].

[71] The inquiry into these subject-matter jurisdictional requirements was recognised by the tribunal in *Alasdair Ross Anderson et al v. Republic of Costa Rica*. In order to ascertain subject-matter jurisdiction in that case, the tribunal felt necessary for the claimants to make the following showings:

> 1) that the deposits constituted "assets" under the BIT; 2) that the Claimants owned or controlled those assets in the territory of Costa Rica in accordance with Costa Rica law; and 3) that if the deposits satisfied these two characteristics they did not fall within those categories of assets that the BIT expressly excludes from the definition of investment.

*Alasdair Ross Anderson et al v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010 [47].

[72] Sasson believes that the term 'investment' was originally a feature of economic analysis rather than an issue in international treaties protecting the rights and properties of aliens. See M Sasson (n 3) 101-102. Dolzer and Schreuer also opine that, in contrast to terms like 'rights', 'property', and 'interests', which have acquired legal meanings, the term 'investment' has its origin in economic terminology. See R Dolzer & C Schreuer, *Principles of International Investment Law* (OUP 2012) 60.

[73] Obviously, every asset acquired cannot be considered as an investment. For instance, if "A" buys a house in the Hague for the exclusive purpose of spending the summer holidays there, he cannot be deemed to have made an investment in the Netherlands. See UNCTAD, *Scope and Definitions* (United Nations 2011) 33.

Under some treaties, this is the end of the matter for subject-matter jurisdiction inquiry. However, some investment treaties go on to provide a further qualification for investments so acquired: obtaining an investment license or approval from official organs of the host state.[74] Therefore, under such treaties, there is a fourth level of inquiry that the tribunal should step in to finalise its subject-matter jurisdiction examination. Hence, depending on the terms and provisions of the treaty, the existence of rights under the laws of the host state is either one of the three or one of the four requirements that the tribunal should verify their presence before asserting jurisdiction *ratione materiae*. However, under both scenarios, the existence of rights or interests is always the first level and the root of the subject-matter inquiry.

53. On the other hand, and as the above discussion implies, if pursuant to an analysis of the host state law, the tribunal faces the situation of inexistence of rights over properties or assets at the relevant time, this would culminate in the absence of any basis for the alleged investment since there would be no ground to place the investment on it (i.e., no underlying right or property constituting the investment). Therefore, in such situations, the case should be dismissed on a jurisdictional basis as long as the contested right at stake is the only basis of the claimant's claim. Under such a scenario, the tribunal does not need to enquire about the legality of the investment, its objective definition or, as the case may be, approval of the investment by relevant authorities of the host state since the finding that there are no rights capable of forming an investment suffices to dismiss the case for lack of jurisdiction *ratione materiae*.
54. Having discussed the jurisdictional consequences of the existence or inexistence of rights over properties or assets, it is notable to mention that the issue of the existence of rights over properties and assets has a twin in the substantive law of expropriation which is closely connected and sometimes overlaps with the question of the existence of rights as a matter of jurisdiction *ratione materiae*. According to this twin rule, there cannot be an expropriation unless the complaint demonstrates the existence of proprietary rights, i.e., property rights susceptible to expropriation.[75] In *Generation Ukraine v. Ukraine*, the tribunal noted that since "expropriation concerns interference in rights in property, it is important to be meticulous in identifying the rights duly held by the Claimant at the particular moment when the alleged expropriation occurred."[76] Therefore, it pointed out that "[a] logical starting point would be to establish the investor's contribution of capital. One would then go on to examine the legal rights acquired by such capital Expenditure."[77] The tribunal also stated that in respect of a claimed right to use land, there "cannot be an expropriation of something to which the Claimant

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[74] See, for instance, Article 2 of the Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Republic of Turkey and the Government of the Republic of Iran, signed on 21 December 1996, entered into force on 13 April 2005; Article 1(3)(i) of the Agreement between the Republic of Austria and Malaysia for the Promotion and Protection of Investments, signed on 12 April 1985, entered into force on 01 January 1987. For more explanations on this treaty requirement see (Chapter 1, Section Two (A)(a)(iii)).

[75] I this regard, the tribunal in *Bayindir v. Pakistan* noted that: "The first step in assessing the existence of an expropriation is to identify the assets allegedly expropriated." *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29, Award, 27 August 2009 [442]. In the same vein, the tribunal in *Chemtura v. Canada* remarked that "in assessing an expropriation claim, the practice of NAFTA tribunals has been to follow a three-step approach focusing on (i) whether there is an investment capable of being expropriated, (ii) whether that investment has in fact been expropriated, and (iii) whether the conditions set in Article 1110(1 )(a)-(d) have been satisfied." *Chemtura Corporation v. Government of Canada*, UNCITRAL (formerly *Crompton Corporation v. Government of Canada*), Award, 02 August 2010 [242]. See also R Dolzer and C Schreuer (n 72) 99.

[76] *Generation Ukraine, Inc. v. Ukraine*, ICSID Case No. ARB/00/9, Award, 16 September 2003 [6.2].

[77] ibid [18.4].

never had a legitimate claim."[78] Therefore, it is not only for the purpose of verifying the existence of an investment, and, as a result, for establishing subject-matter jurisdiction, that an investment treaty tribunal needs to ascertain the existence of rights underlying investments. In expropriation cases also, an investment treaty tribunal should verify the existence of private rights capable of being expropriated. It is submitted that in both situations, it is the law of the host state that determines the existence of rights underlying investments or rights capable of being expropriated.

55. Under certain investment treaties, the jurisdiction of the tribunal is limited to deciding expropriation cases.[79] In such cases, the non-existence of property rights capable of being expropriated could culminate in the dismissal of the case on a jurisdictional basis, both because the root of jurisdiction ratione materiae of the tribunal is missing and because the tribunal was not chosen to decide non-expropriation claims. In such cases, it is also possible for the tribunal to skip the jurisdictional discussion and directly enter into an expropriation analysis, beginning with the question of the existence of expropriable property.

56. These twins are not, however, totally identical. In the case of expropriation, the right should always be vested in the claimant so that the property in question be capable of expropriation. In this respect, the tribunal in *Emmis v. Hungary*, whose jurisdiction was limited to deciding expropriation claims, noted that in order to decide a fair and equitable treatment claim, in contrast to an expropriation claim, "[i]t would not be so crucial for the Claimants to prove the existence of a proprietary right pertaining to the 2009 tender under Hungarian law".[80] Observing, however, that its jurisdiction is limited to expropriation claims, the tribunal indicated that: "…the only way that the expropriation claim can be held to be within the Tribunal's jurisdiction is if Sláger had a proprietary right that survived the expiry of its broadcasting right under that Agreement."[81] Therefore, even if the claimant had proven that he had rights below the level of ownership, the tribunal could not have had ascertained jurisdiction, since its jurisdiction was limited to expropriation claims, and expropriation, as a preliminary point requires rights vested in the claimant capable of being expropriated. Consequently, whereas in expropriation claims, the right in question should be vested in the claimant in accordance with the host state law, in case of the verification of rights underlying investment for jurisdictional purposes, the cardinal point is establishing the existence of the right, and not necessarily its proprietary nature.

### B. The Specific Function of the Host State Law in Determining the Creation and Existence of Rights/Interests Underlying Investments

57. By now, it is quite clear that it is the law of the host state that on most occasions determines the creation and existence of rights and/or interests over assets or properties and contractual

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[78] ibid [22.1].

[79] See, for instance, Article 10 of the Agreement between the Kingdom of the Netherlands and the Hungarian People's Republic for the Encouragement and Reciprocal Protection of Investments, signed on 02 September 1987, entered into force on 01 June 1988. The Albanian Law on Foreign Investment also limits Albania's consent to ICSID arbitration to the following types of disputes: "… expropriation, compensation for expropriation, or discrimination and also … the transfers in accordance with Article 7 …" See *Tradex Hellas S.A. v. Republic of Albania*, ICSID Case No. ARB/94/2, Decision on Jurisdiction, 24 December 1996 (1999) 14(1) ICSID Rev-FILJ 174.

[80] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [144].

[81] ibid.

rights. I showed that the applicability of the laws of the host state to the creation and existence of property and contractual rights and/or interests is principally because of the nature of the issue that requires determination by the local law that creates such legal rights. In fact, international law has no substantive rules regarding the creation and existence of rights on a private plane. In addition, I pointed out above that a proper conflict of law analysis, in most cases, culminates in the application of the laws of the host state to the question of the creation and existence of property rights. Furthermore, as was reviewed above, certain investment treaties stipulate that the laws of the recipient state determine the creation and existence of rights.

58. However, specifying the applicable law to the question of creation and existence of rights is the first step that an arbitral tribunal seized of an investment treaty case has to take. The second phase of the enquiry is the actual application of that body of law to the specific questions before a court or tribunal. One such aspect was discussed above. As was discussed in the previous subsection, the consequence of the application of the host state local law to the questions regarding the existence of rights underlying investments culminates in two possible results: one, that there is a right under the laws of the host state, in which case the tribunal can proceed and check the existence of other conditions of *ratione materiae* jurisdiction, and, two, that the laws of the host state do not recognise the alleged right, meaning that the case should be dismissed to the extent that the claimant's case solely rests upon the existence of such a right.

59. This is not the end of the inquiry. In a real case, one should also deal with the specific function of the host state law in determining the jurisdiction *ratione materiae* of an investment treaty tribunal. Indeed, when called on to decide an investment treaty case, an investment treaty tribunal may quite easily come to the conclusion that the host state law is applicable to the specification of private rights underlying investments. The consequence of the application of the host state law may also be readily known to the tribunal in general. The predicament for a tribunal may, in such circumstances, be the actual application of the host state law to the specific property and contractual law questions. For instance, assume that the threshold question before an investment treaty tribunal is whether the claimant, a road-building company, acquired title to a set of second-hand asphalt mixing plants previously owned by the host state and sold to the investor pursuant to a sale agreement that is a side agreement to the main BOT contract. These plants were seriously damaged and effectively demolished before the commencement of the work by local people who claimed that the road that the investor had contracted to build would destroy the grasslands they used as pastures for their livestock. With the machinery destroyed, the investor files a BIT case against the host state claiming that the respondent has failed to accord its investment full physical protection and security. The host state, on the other hand, claims that the investor had no rights in the equipment because it failed to abide by a local law requiring the registration of heavy machinery in the public register for transfer of title to be consummated. Now, in order to ascertain subject-matter jurisdiction, after determining the applicable law in general terms, the investment treaty tribunal needs in the first place to identify the legal entitlement of the investor to the asphalt mixing plants and determine the scope of such entitlement. In so doing, the tribunal should grapple with the details of the law of the host state and ascertain whether title to the machinery had been transferred to the investor at the time the alleged breach occurred or, if title has not been transferred, whether the investor has any other interest in the property in question. This is, of course, a more difficult task to embark upon than determining the applicable law to the question of the existence of rights/interests in general.

60. It is submitted that many different legal facets and specifications of contractual and property rights and/or interests underlying investments are governed and determined by the laws of the host state. In most cases, the domestic law of the host state contains detailed legal norms and rules regulating the creation and existence of rights to properties and contractual rights. This view is confirmed both by a proper conflict of laws analysis and by a review of the relevant investment treaty jurisprudence.
61. As was discussed above, rights and interests are the core of the subject-matter jurisdiction of an investment treaty tribunal. The question, however, is whether the acquisition of any right or interest satisfies this test, or whether such right should have certain specifications under the law of the host state in order to be protected. As will be shown below, not every right in general, and not even every right to a property or every contractual right passes the test of protectability under an investment treaty. Rather, depending on the nature of the claim or the investment at issue, the right should have certain specifications under the laws of the host state. An analysis of these requirements pinpoints the specific property and contractual issues that should be determined by reference to the laws of the recipient state in an investment treaty arbitration context. The analysis in this part of the discussion will be largely based on the practice of investment treaty tribunals and conflict of laws analysis. The question is how and to what extent the host state law would help a tribunal in very specific property or contract law questions that arise in practice when trying to determine the creation and/or existence of rights underlying investments.
62. There are plenty of issues regarding the creation and existence of rights underlying investment that should be addressed by reference to the laws of the host state. To begin with, it is the law of the host state which determines what property is, i.e., the conditions for a right to be characterised as a property right. Secondly, the laws of the host state set forth the conditions for the transfer of title in property. Thirdly, since in modern international law, contractual rights are also protected, it is the task of the laws of the host state to dictate the conditions for the protection of such rights. These conditions may encompass conditions for the validity and enforceability of contracts. In the following pages, I will begin with analysing the role of the laws of the host state in the definition of property and property rights (a). Next, I will turn to the function of the internal laws of the capital-importing country in setting the legal requirements for the transfer of title (b). Finally, the analysis will turn its attention to the task of the recipient state's laws in regulating the conditions for the protection of contractual rights (c).

**a. Definition of Property**

63. In order to gain protection under an investment treaty, there is no question that the investor must prove that he/she has a legal right or interest in the first place.[82] In fact, when no legal right/interest exists, there could be no investment, with the result that there will be no case for the investor. It is important to note that only legal rights and/or entitlements are protected by

[82] *Marvin Roy Feldman Karpa v. United Mexican States*, ICSID Case No. ARB(AF)/99/1 (also known as *Marvin Feldman v. Mexico*), Award, 16 December 2002 [118]. The tribunal had already found that no expropriation had occurred in that case, *inter alia*, because "at no relevant time has the IEPS law, as written, afforded Mexican cigarette resellers such as CEMSA a "right" to export cigarettes." See ibid [111] See also *Generation Ukraine, Inc. v. Ukraine* (n 76) [22.1] (where after concluding that the claimant had no contractual right to the relevant property, the tribunal stated that "there cannot be an expropriation of something to which the Claimant never had a legitimate claim.")

investment treaties and mere economic interests or expectations which have no root in the legal system of the host state are not protected by investment treaties.[83] In this regard, one commentator has opined that:

> To equate property rights with any interest with an economic value would render property a subjective concept and attribute relevance to interests that fall short of being legally protected interests.[84]

64. Having said that, it should be pointed out, however, that a review of investment treaty jurisprudence would indicate that in order to be protected by the investment treaty, the legal right in question should concern a property, and therefore, have economic value. Thus, to gain protection, the legal right in question should still have an economic connection. Indeed, under the laws of many countries, one indispensable characteristic of property is having economic value. In other words, not every legal right recognised under the laws of the host state is protected by investment treaties. For instance, the right to free speech or to freedom of religion do not constitute assets protected by investment treaties since they do not have financial or economic value, i.e. they cannot be sold and purchased. The fact that a right should have economic value in order to be protected by an investment treaty was confirmed in *Emmis v. Hungary* where the tribunal said that: "[T]he loss of a right conferred by contract may be capable of giving rise to a claim of expropriation but only if it gives rise to an asset owned by the claimant to which a monetary value may be ascribed […]"[85] A right has economic value when it can be the subject of a commercial contract i.e. that could be sold, bought, transferred in any way, and rented for monetary value. The Iran-US Claims Tribunal held in *Amoco*:

> Expropriation, which can be defined as a compulsory transfer of property rights, may extend to any right which can be the object of a commercial transaction, i.e., freely sold and bought, and thus has a monetary value. [...] It is because Amoco's interests under the Khemco Agreement have such an economic value that the nullification of those interests by the Single Article Act can be considered as a nationalization.[86]

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[83] M Sasson (n 3) 113-114 (criticising the *Pope & Talbot* tribunal for blurring "the distinction between legal interest and commercial interest and [elevating] the latter to a property right that can be expropriated." She also takes issue with the fact that in this Award, the "definition of property right is remitted to the "true interest at stake" without attributing any relevance to whether the interest is a legal one governed by a municipal law." Furthermore, she also takes issue with Mr. Horacio Grigera Naon' dissenting opinion in *EnCana Corporation v. Republic of Ecuador* for his disagreement with the application of domestic law to the question of whether intangible rights to VAT refund were acquired by the investor and for his broad-brush approach to the existence of interests capable of protection under an investment treaty.) ibid 114-115.

[84] M Sasson (n 3) 115. See also *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL, Separate Opinion on the issues at the quantum phases of *CME v. Czech Republic* by Ian Brownlie, C.B.E., Q.C., 14 March 2003 [20] (referring to the list of assets mentioned in the relevant BIT and stating that: "These provisions relate exclusively to assets 'invested' and, whilst the list of types of asset is extensive, the concept has certain limitations. In the first place, the genus consists of legal entitlements and does not extend to mere expectations …")

[85] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [169].

[86] *Amoco International Finance Corporation v. The Government of the Islamic Republic of Iran, National Iranian Oil Company, National Petrochemical Company and Kharg Chemical Company Limited*, IUSCT Case No. 56, Award No. 310-56-3, 14 July 1987, 15 Iran-USCTR, p 189, p 220 [108].

65. To be sure, it is submitted that the reason why many investment treaty tribunals indicate that for a right to be characterised as property it should have economic value is because the law of the host state provides for such a requirement. Indeed, as was brilliantly put by Schreuer, for verifying the very existence of legal property rights, the laws of the municipal state have to be queried:

> […] in cases where jurisdiction is limited to claims alleging the violation of a treaty's substantive standards an incidental application of domestic law is often called for. The most obvious situation of this kind arises where there is a dispute about the existence of rights that the investor seeks to protect. Whether these rights are property rights, rights arising from contracts or other intangible rights, they typically exist by virtue of a domestic legal system. Therefore, the preliminary question of the existence of the rights in dispute cannot be answered without resort to a domestic system of law, most often the host state's law. Therefore, even if a claim is based on the violation of a BIT or other treaty, domestic law is likely to be relevant.[87]

66. Furthermore, an investment treaty tribunal has to refer to the laws of the host state in order to see whether the right in question has economic value. The tribunal in *Nagel v. Czech Republic* made a reasoned and significant observation in connection with the relation between the domestic law of the host State and having economic value:

> It follows that, when read in their context, the terms "asset" and "investment" in Article 1 shall be considered to refer to rights and claims which have a financial value for the holder. This creates a link with domestic law, since it is to a large extent the rules of domestic law that determine whether or not there is a financial value. In other words, value is not a quality deriving from natural causes but the effect of legal rules which create rights and give protection to them.[88]

67. In short, in order to be protected by the investment treaty, an investor has to prove that it has a legal right protected by the laws of the host state. That legal right should be attributed to a tangible or intangible property which has economic value. The very requirement that a legal right has to have economic value in order to be characterised as a 'property' and the assessment as to whether any given right has the attribute of 'monetary value' are issues to be determined by the laws of the host state.

**b. Conditions for Transfer of Title**

68. In certain situations, investors seek to establish that the host state is liable for the expropriation of their property. In such circumstances, the threshold goes higher for the investor who must prove that the alleged right to property was vested in the investor. In other words, in order to

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[87] C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (2014) 1(1) McGill Journal of Dispute Resolution 17-18.

[88] *William Nagel v. The Czech Republic* (n 8) [300].

make a viable expropriation claim, the investor must, as a preliminary step, establish that he has a proprietary right or interest. Being called upon to decide an expropriation claim, the tribunal in *Emmis v. Hungary* considered whether the nature of the alleged rights held by the claimants as to the new license was proprietary or not.[89] It concluded that rights capable of being expropriated should stand one step higher than other legal rights having economic value:

> [T]he existence of such rights is not sufficient to answer the question whether this Tribunal had jurisdiction to vindicate such rights on the international plane. For that purpose, it is necessary to determine whether the rights constitute valuable proprietary assets of the Claimants.[90]

69. A right is proprietary and is vested in an investor if it is special to it, and belongs to him/her to the exclusion of the others. In other words, the investor should exclusively own the asset or property in question. Thus, the investor's rights should be proprietary, in the sense that it could be owned, transferred, and inherited. Therefore, procedural rights in a tender cannot be vested in an investor since such rights are usually claimable by all participants. In this connection, the *Emmis* tribunal pointed out that:

> [T]he loss of a right conferred by contract may be capable of giving rise to a claim of expropriation but only if it gives rise to an asset owned by the claimant to which a monetary value may be ascribed. The claimant must own the asset at the date of the alleged breach. It is the asset itself - the property interest or chose in action - and not its contractual source that is the subject of the expropriation claim. Contractual or other rights accorded to the investor under host state law that do not meet this test will not give rise to a claim of expropriation.
>
> […]
>
> [A] property right is something quite different. It constitutes a right held by its owner to the exclusion of others. It is no answer to say that the rights acquired by bidders in the 2009 Tender were acquired for valuable consideration. That may have created a contractual relationship between each bidder and the ORTT. But each bidder did not thereby acquire a valuable asset, capable of being alienated. If that were so, it would mean that each bidder had, by virtue of its participation in the bid, acquired the same asset. But this makes no sense in the context of a tender, the very purpose of which is to determine which of a number of bidders is to acquire the asset in question, namely the 2009 Broadcasting Right… In the second place, none of the rights alleged to arise directly from participation in the 2009 Tender could be said to be assets or property owned or controlled by Claimants. On the contrary, Sláger's rights in the 2009 Tender were rights

[89] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [144], [165].

[90] ibid [252]. See also ibid [168].

concerning participation in a process that would determine whether it could acquire ownership of an asset.[91]

70. In addition, in order to be considered owned by the investor, the rights concerned should not be potential but rather definitive rights that are vested in the Claimant. The *Merrill & Ring* tribunal held in this regard that: "The right concerned would have to be an actual and demonstrable entitlement of the investor to a certain benefit under an existing contract or other legal instrument. This reasoning underlies the Feldman tribunal's conclusion that an investor cannot recover damages for the expropriation of a right it never had … Expropriation cannot affect potential interests."[92]
71. In short, when raising a claim of expropriation, the investor must prove that the alleged property was capable of being expropriated. A property can be expropriated when it is substantively and definitively owned by somebody to the exclusion of others.
72. To answer the question of whether the allegedly expropriated rights were vested in the investor at the time of expropriation is a task which should be performed by the law of the host state as the law of the *situs* of the property. Thus, in order to see whether any expropriation has occurred, the *Emmis* tribunal, as a preliminary matter, analysed and then relied upon the evidence presented to it on Hungarian law to verify whether the rights in question were proprietary in nature or not.[93] Similarly, in *Bayview v. Mexico*, the claimants contended that they had an investment in Mexico in the form of their rights to water located in Mexico which was allegedly wrongfully seized by the respondent.[94] The tribunal considered three pieces of Mexican legislation (namely, the Mexican Constitution, the Mexican Law of National Waters, and Mexico's General Law of National Assets) to find that the claimants could have no such property rights in water in Mexican rivers.[95]
73. Indeed, embarking upon a conflict of laws analysis, it is the law of the *situs* that determines whether the buyer has acquired title to the goods subject to the contract, and determines the nature and scope of the title.[96] In other words, it is the law of the place where the properties are situated at the time of transfer which determines whether proprietary rights in the assets were transferred. This rule applies to both moveable[97] and immoveable properties.[98] *Lex situs* remains the applicable law to the questions regarding transfer of title even if title is intended to be transferred via a contract. In fact, in such situations, it is the *lex situs*, rather than the

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[91] ibid [169], [253]-[254].

[92] *Merrill and Ring Forestry L.P. v. Canada*, ICSID Case No. UNCT/07/1, Award, 31 March 2010 [142].

[93] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [178].

[94] *Bayview Irrigation District et al. v. United Mexican States*, ICSID Case No. ARB(AF)/05/1, Award, 19 June 2007 [109].

[95] ibid [118].

[96] J Hill & MN Shuilleabhain (eds) (n 42) 473; E Rabel (n 41) 49-50.

[97] See *Glencore International AG v Metro Trading International Inc* [2001] 1 Lloyd's Rep 284 (holding that under English conflicts of laws rules, the transfer of title to movable property is governed by the law of the place where the property is situated); *Bonhams 1793 Ltd v. Lawson et al* [2015] EWHC (Comm) [40] (stating that "[a]t the time when that agreement transferred title, the chassis was in Belgium. On normal conflicts of laws principles, Belgian law as the *lex situs* governs whether good title to the chassis was transferred to Mr Swaters …"); *Air Foyle Ltd v Center Capital Ltd* [2003] 2 Lloyd's Rep 753.

[98] *Bank of Africa Ltd v Cohen* [1909] 2 Ch 129.

governing law of the contract which determines whether proprietary interests in a moveable or immoveable property are transferred.[99] The same is true with respect to intangible properties. Indeed, as Auld J expressed in *Macmillan Inc v Bishopsgate Investment Trust plc (No 3)*, "[i]n general, disputes about the ownership of land and of tangible and intangible movables are governed by *lex situs*".[100] In addition, it is the law of the host state as the law of *situs* which determines whether certain formal steps should be exhausted after the exchange of offer and acceptance for the transfer of title to be finalised pursuant to a contract, for instance, execution of a deed or registration of the transfer in a public register.[101]

74. In summary, when a tribunal needs to ascertain whether title of the property had been transferred to the investor at the time of the alleged expropriation or that contractual rights allegedly confiscated were vested in the investor, it has to refer to the laws of the host state. This applies to both the substantive and the formal validity of the transfer of title to the allegedly expropriated property.

### c. Conditions for Protection of Contractual Rights

75. It is generally accepted in international law that intangible rights including contractual rights may amount to investments for the purpose of protection under investment treaties.[102] The *SPP* tribunal spells out the position of international law with respect to the protection of contractual rights: "… there is considerable authority for the proposition that contract rights are entitled to the protection of international law and that the taking of such rights involves an obligation to make compensation therefore."[103] Indeed, it has been acknowledged by myriads of international arbitral tribunals that taking of intangible rights including contractual rights could, potentially, constitute an expropriation or a measure having an equivalent effect.[104] Additionally and as pointed out by the *White Industries* tribunal, many investment treaties

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[99] J Hill & MN Shuilleabhain (eds) (n 42) 476. See in this respect, *The WD Fairway* (No 3) [2009] 2 Lloyd's Rep 420.

[100] *Macmillan Inc v Bishopsgate Investment Trust plc* (No 3) [1996] 1 WLR 387 at 410.

[101] J Hill & MN Shuilleabhain (eds) (n 42) 473; E Rabel (n 41) 46-48. It is precisely because of the relevance of the law of the *situs* in determining the formal validity of transfer of title that Article 11(5) of the Rome I Regulation prescribes that overriding mandatory provisions of the *situs* regarding formal validity cannot be condoned by the applicable law to the substance of the contract or the law governing the formal validity of the contract:

> Notwithstanding paragraphs 1 to 4, a contract the subject matter of which is a right *in rem* in immovable property or a tenancy of immovable property shall be subject to the requirements of form of the law of the country where the property is situated if by that law: (a) those requirements are imposed irrespective of the country where the contract is concluded and irrespective of the law governing the contract; and (b) those requirements cannot be derogated from by agreement.

In this respect, see J Hill & MN Shuilleabhain (eds) (n 42) 258.

[102] C Schreuer, L Malintoppi, A Reinisch & A Sinclair, *The ICSID Convention: A Commentary* (CUP 2009) 126.

[103] *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*, ICSID Case No. ARB/84/3, Award, 20 May 1992 [164].

[104] See *Norwegian Shipowner's Claims* (*Norway v. USA*), (1922) RIAA 307; *SeaCo Inc. v. The Islamic Republic of Iran, The Iranian Meat Organization and others*, IUSCT Case No. 260, Award No. 531-260-2, 25 June 1992, 28 Iran-USCTR, p 198 [45]; *Impregilo S.p.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/3, Decision on Jurisdiction [274]; *Eureko B.V. v. Republic of Poland*, UNCITRAL, Partial Award, 19 August 2005 [241]; *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29, Decision on Jurisdiction, 14 November 2005 [255]; *White Industries Australia Limited v. The Republic of India*, UNCITRAL, Final Award, 30 November 2011 [12.3.1]-[12.3.3].

expressly include in their definition of 'investment' what can only be *in personam* or intangible rights, namely: the "right to money or to any performance under a contract having a financial value".[105]

76. That being said, not every right arising from a contract gives rise to rights protected by investment treaties. Indeed, if the investment in question is formed by contractual rights, in order to be protected by the investment treaty, the underlying contract should be both binding and enforceable. In fact, there would no substantive right to protect before a contract is formed and becomes effective.[106]

77. It is submitted that the binding nature of a given contract and its enforceability should be determined by reference to the laws of the host state. It was discussed earlier in this Chapter that, in most cases, the law of the host state is the *lex contractus*. It will be shown below that different questions regarding the creation and existence of contractual rights are determined by the *lex contractus* (which in most cases is host state law).

78. Indeed**,** a first question that an arbitral tribunal has to deal with when faced with an investment which has a contractual right nature is ascertaining the validity and existence of the contract in question. According to Article 10(1) of the Rome I Regulation, "[t]he existence and validity of a contract, or of any term of a contract, shall be determined by the law which would govern it under this Regulation if the contract or term were valid." In addition, according to Articles 11(1), 11(2), and 11(3) of the same Regulations, the law that governs the substance of the contract also would govern the formal validity of the contract[107] as well as the formal validity of an act having legal effect to an existing contract (like a termination notice) or a contemplated contract (like formal conditions for a contractual offer in certain instances), whether the parties were in the same country at the time of the conclusion of the contract or not.[108] The same rule is followed by English jurisprudence. In a quite recent case before the English Court of Appeal, it was stated that it is now a "well established principle of English private international law that questions relating to the existence and terms of a contract are governed by the putative proper law."[109]

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[105] *White Industries Australia Limited v. The Republic of India* (n 104) [7.3.8].

[106] As expressed by Spiermann, "[a] contract would not be a contract if not binding". See O Spiermann (n 2) 94.

[107] The concept of formal validity of a contract has been defined by the famous Giuliano-Lagarde Report: "every external manifestation required on the part of a person expressing the will to be legally bound, and in the absence of which such expression of will would not be regarded as fully effective." M Giuliano & P Lagarde, 'Report on the Convention on the Law Applicable to Contractual Obligations' (1980) No. C 282/1 Official Journal 29. McParland defines formal validity in the following way: "'Formal validity' is concerned with rules which require certain attributes as a matter of form for contracts or documents of that particular type, whether it be that they be in writing, signed, executed as a deed, or that they must comply with some requirement of form or procedure in execution." See M McParland, *The Rome I Regulation on the Law Applicable to Contractual Obligations* (OUP 2015) 724. In contrast, material validity has been defined to concern "matters which are intrinsic to the contract …" See ibid. See also J Hill & MN Shuilleabhain (eds) (n 42) 257-258.

[108] According to the Giuliano-Lagarde Report, this same solution was adopted in Germany, Italy, France, and under the Benelux Treaty. See M Giuliano & P Lagarde (n 107) 30.

[109] *Midgulf International Ltd v. Groupe Chimique Tunisien* [2010] EWCA Civ 66, [2010] 2 Lloyd's Rep 543 (CA), [56]. For a classic case example in this respect see, *In Re Bonacina* [1912] 2 Ch 394 (CA), 402 (declaring a contract valid under the applicable law, in that case, the law of Italy, which was otherwise invalid under English law as the *lex fori*.)

79. It was analysed earlier in this Chapter that the law governing the contract, or more appropriately in this context, 'the putative proper law',[110] would, in most instances, be the law of the host state. Therefore, the law of the recipient state would determine whether the contract in question is formally and materially valid and exists. In other words, such law determines many questions regarding the formation of the contract, including offer and acceptance, the validity of the consent (including matters vitiating consent, like mistake, duress, misrepresentation, non-disclosure and undue influence), legality, and consideration.[111]
80. Considering the issue in an investment treaty arbitration context, in order to ascertain whether a contract is binding, the tribunal should verify whether the contract in question is validly formed according to the laws of the host state. In other words, whether the conditions for the validity of the contract under the laws of the host state have been satisfied. Therefore, if an EPC contract is signed with no intention to create legal relations or the contract is signed with a person on the government's side having no capacity to contract, the contract in question is not binding, and, thus, no contractual rights could be said to exist. This is what the tribunal in *Nagel v. Czech Republic* did when analysing the validity of the Cooperation Agreement at issue in that case. The tribunal considered the laws of the Czech Republic, as the host state, to verify the validity of the Cooperation Agreement and found that the agreement was binding and was validly concluded.[112]
81. That being said, it goes without saying that the contract underlying the alleged investment should continue to be binding up until the time of the alleged breach. In fact, in certain cases, the central question is whether the contractual rights allegedly forming the investment existed at the time of the alleged breach. To give an example, assume that investor "A" concludes a contract with the Ministry of Agriculture of state "B" to perform supervisory functions over the production and processing of pesticides in Province "C" for a period of five years. Assume further that approximately after five (5) years from the commencement of the contract, the Ministry of Agriculture unilaterally terminates the contract on the basis that: (i) the term of the contract had expired; and (ii) the investor has failed to observe the environmental standards in carrying out its contractual obligations. The starting question for such a case would be whether

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[110] M McParland (n 107) 717-718.

[111] ibid 719-720. J Hill & MN Shuilleabhain (eds) (n 42) 255, 262. An exception to this rule is the capacity to contract which, in the case of a company, is determined by the law of its place of incorporation. See ibid 259 (referring to *Integral Petroleum SA v. SCU-Finanz AG* [2015] ILPr 50). In *George W Cook (USA) v. United Mexican States*, Commissioner Nielsen noted that: "When questions are raised before an international tribunal, as they have been in the present case, with respect to the application of the proper law in the determination of rights grounded on contractual obligations, it is necessary to have clearly in mind the particular law applicable to the different aspects of the case. The nature of such contractual rights or rights with respect to tangible property, real or personal, which a claimant asserts have been invaded in a given case is determined by the local law that governs the legal effects of the contract or other form of instrument creating such rights…" See *George W Cook (USA) v. United Mexican States* (n 24) 213, 215 [7]. Similarly, Schreuer has opined that: "The protection of property through an investment treaty or general international law is contingent upon the existence and extent of property rights as determined by the applicable domestic law. Similarly, if an investor claims that its rights, arising from a contract, have been expropriated or have been subjected to treatment that is contrary to a treaty's fair and equitable standards, domestic law will also be relevant. It will be necessary to look at the existence of the contract and the rights arising under it in terms of the applicable domestic law. Only after clarifying these preliminary issues under domestic law is it possible to determine whether a breach of the international standards has actually occurred." [footnotes omitted] C Schreuer, 'The Relevance of Public International Law in International Commercial Arbitration: Investment Disputes' 21 online: <www.univie.ac.at/intlaw/pdf/csunpublpaper_1.pdf>.

[112] *William Nagel v. The Czech Republic* (n 8) [317]-[320].

the investor had contractual rights at the time of the alleged breach, in this case, at the time of the alleged unlawful termination. In other words, it should be considered whether the contractual rights still existed and not lapsed and extinguished at the time of the alleged breach. Once again it is the law of the host state which determines whether such rights were extinguished at the time of the alleged breach. According to Article 12(1)(d) of the Rome Regulations I, the law applicable to the contract shall also govern "the various ways of extinguishing obligations …". Thus, it is the law of the recipient state which determines whether an act of the state (like national legislation or an executive decree), a mutual or unilateral termination, lapse of time or a novation would extinguish contractual rights.[113] In *Emmis v. Hungary*, the tribunal was seized, *inter alia*, of the task to determine whether the claimants' alleged contractual rights at the time of the breach were enforceable. In so doing, it referred to the Civil Code of Hungary and the position of Hungarian courts in related litigation proceedings.[114] The tribunal eventually dismissed the claims because, according to the laws of Hungary, the rights acquired by the claimants were not binding any more at the time when the alleged wrongdoing took place. In fact, the claimants had a fixed-term contract that had already expired when Hungary took the alleged expropriatory measure. In *Azinian et al v. The United Mexican States*, the tribunal was considering whether the annulment of a concession contract constituted an expropriation under Article 1110 of NAFTA. In finding whether an expropriation had occurred, the tribunal noted that the concession contract was subject to the Mexican law governing public service concessions. It then found that the concession contract had been declared invalid under the above-mentioned law. This conclusion had been affirmed by three levels of Mexican courts, whose decisions were not challenged in the arbitration.[115] Therefore, the tribunal came to the conclusion that since no binding contractual rights existed any longer under host state law, thus, no expropriation had occurred. In contrast, if at the time the alleged breach occurs, the rights and/or interests relied upon by the investor still exist under the laws of the host state, like in case of open-ended businesses, such rights would pass the 'continuing binding force' test.[116]

82. In addition to being binding, a contract must be enforceable under the laws of the host state for the investor to be able to claim a protected investment. Since many of the investment contracts, in particular, infrastructure contracts, are public contracts, they cannot be characterised as freely negotiated contracts and mere offer and acceptance do not suffice. Therefore, usually, certain formalities and conditions precedent should be observed and satisfied for the contract to be deemed enforceable. The exhaustion of such formalities should be checked against the laws of the host state. The test for enforceability is usually protectability before the courts of the host state. In other words, the rights in question should be claimable before the national courts of the recipient state. Therefore, if what is acquired by the investor after the exchange of offer and acceptance in an administrative contract is speculative, a mere

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[113] See M McParland (n 107) 763-764; J Hill & MN Shuilleabhain (eds) (n 42) 262.

[114] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary* (n 4) [185]-[190].

[115] *Robert Azinian, Kenneth Davitian, & Ellen Baca v. The United Mexican States*, ICSID Case No. ARB (AF)/97/2, Award, 01 November 1999 [96], [105]. This seems to be the first case in the history of NAFTA in which an award was rendered. Similarly, the case seems to be the first one under the aegis of the ICSID Additional Facility Rules in which a final award was rendered

[116] See FN Pagani, JIG Cueto, 'Tidewater v. Venezuela: Property Rights Capable of Expropriation in a Company Operating under Short-Term Contracts' (2015) 32(4) J Int'l Arb 449.

hope, a contingent expectation subject to satisfaction of a condition or occurrence of an event, a simple permission to proceed to fulfil further remaining steps or a mere procedural entitlement to complete a process, the alleged acquired right usually does not constitute an 'asset' under the domestic laws of the host state, and, thus, does not fall within the scope of application of investment treaties. In *PSEG v. Turkey*, the tribunal rejected Professor Dolzer's Rejoinder Opinion to the effect that the treaty definition of investment refers to any right, even one that can be exercised at any time in the future, for being unpersuasive. In contrast, it considered the respondent's argument that the definition of investment does not include an option "persuasive as a general approach".[117] In the same vein, the *Merrill & Ring* tribunal held that "a potential interest that may or not materialize under contracts the [i]nvestor might enter into with its foreign customers" is not protected by NAFTA.[118] The tribunal also said that "the right concerned would have to be an actual and demonstrable entitlement of the investor to a certain benefit under an existing contract or other legal instrument."[119]

83. Following the same logic, a bidder in a tender before being announced as the bid winner has no concrete right to constitute an asset protected by an investment treaty. Even when announced as the bid winner, depending on the laws and regulations in place in the host country, the investor may still need to fulfil certain conditions before being awarded the pertinent license, authorisation, permit, or concession. Put differently, it is only when all the formalities are satisfied, or the conditions precedent fulfilled, that the contract in question is enforceable and effective.[120] In *Apotex v. the United States*, the claimant had asserted that but for the respondent's alleged breach of its legal obligations, Apotex would have been granted final, not tentative, approval because no other impediments to approval existed at that time. The tribunal remarked that is was "unpersuaded by this submission. Whether or not each of Apotex's ANDAs[[121]] would have been granted final approval is by no means certain on the evidence. But in any event, the critical enquiry must be as to the nature of the alleged "property" as at the date of the alleged breach – not at some future point."[122] Similarly, it was for this reason that the tribunal in *Nagel v. Czech Republic* held that in order to have financial value, the intangible rights in question should be more than mere hopes to acquire the license. The tribunal noted that "a claim can normally have a financial value only if it appears to be well-founded or at the very least creates a legitimate expectation of performance in the future."[123] It also stated that a mere prospect to acquire a license does not equate with a right having financial value:

> [T]he basic undertaking in the Cooperation Agreement was that the parties should work together for the purpose of obtaining a GSM licence. There

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[117] *PSEG Global, Inc., The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Limited Sirketi v. Republic of Turkey*, ICSID Case No. ARB/02/5, Award, 19 January 2007 [189]-[190].

[118] *Merrill and Ring Forestry L.P. v. Canada* (n 92) [140].

[119] ibid [142].

[120] The same is true with regard to a licensee's claim to the renewal of its license. It can only claim for the renewal when all the required conditions are fulfilled. See *CMS Gas Transmission Company v. The Republic of Argentina*, ICSID Case No. ARB/01/8, Award, 12 May 2005 [199].

[121] Abbreviated New Drug Application.

[122] *Apotex Inc. v. The Government of the United States of America*, ICSID Case No. UNCT/10/2, Award on Jurisdiction and Admissibility, 14 June 2013 [215].

[123] *William Nagel v. The Czech Republic* (n 8) [301].

> was not, and could not be, a guarantee that a licence would in fact be obtained. That would depend on the Government, and the Government had made no undertaking in this regard. Mr Nagel could do no more than hope that his cooperation with the State-owned Czech company SRa would increase his chances to become involved in the operation of GSM in the Czech Republic, but he could not be certain of getting a licence. Although he may have been encouraged by various remarks from Ministers or Government officials or by the general interest they demonstrated in his plans, this was not sufficient, in the Arbitral Tribunal's view, to raise his prospects based on the Cooperation Agreement to the level of a "legitimate expectation" with a financial value.[124]

84. Therefore, although the tribunal recognised that Mr. Nagel had certain rights under the Cooperation Agreement, in view of the members of the panel, such rights were not sufficient to constitute an 'asset' under the treaty.[125] In addition, in the same case, the tribunal reasoned that for the Cooperation Agreement to be enforceable against the state, the tribunal took into account the legal requirement under Czech law that there should have been an approval or some other binding commitment by the state made in a form to make the Czech Government responsible for the implementation of the Agreement. Upon examining the file and the evidence before it, the arbitral panel did not find such formal commitments on the part of the Government.[126]
85. In summary, it is the law of the host state that determines whether the contract underlying the alleged contractual rights is binding and enforceable.

**Conclusion**

86. It was shown in this Chapter that domestic law of the host state has a determinative role in another significant *ratione materiae* issue in investment treaty arbitrations. As I demonstrated in this Chapter, it is in most cases, the law of the host state that determines whether a right/interest exists over a piece of property/asset which is said to constitute the alleged investment.
87. As framed, there are two grounds for the application of the laws of the host state to the question of the existence of rights/interests underlying investments. **Firstly**, I established that the nature of the issue requires, in principle, the application of domestic law. In fact, although it is always open to the contracting parties to an investment treaty to define the terms 'property', 'asset', 'property interest', etc. for the purposes of their overseas investment relations by way of express or implied agreements or by way of subsequent agreement or subsequent practice, they do not usually do so in investment treaties. Furthermore, customary international law does not have a set of default rules for determining the substantive contents of rights/interests underlying investments. It is actually domestic law that does have the apparatus for defining 'property' constituting investment. As stated by one commentator: "Investments disputes are about investments, investments are about property, and property is about specific rights over

[124] ibid [326].

[125] ibid [329].

[126] ibid [321]-[325].

things cognisable by the municipal law of the host state."[127] Having come to the conclusion that it is domestic law that can answer questions concerning private law aspects of property and contract, it was shown in this Chapter that the application of conflict of laws rules of *lex situs* and *lex contractus*, in most occasions, leads to the application of the laws of the host state to the question of the creation and existence of rights/interests forming the investment. **Secondly**, certain investment treaties expressly mention that the creation and existence of rights/interests with regard to all or a number of assets enumerated by the investment treaty is governed by the laws of the receiving state.

88. For these two reasons, it is the law of the host state that governs the questions regarding the creation and existence of rights/interests underlying investments, and as such, it is the municipal law of the recipient state that furnishes a core component of the tribunal's *ratione materiae* jurisdiction. In fact, as was pointed out above, the consequence of the application of the host state local law to the questions regarding the existence of rights underlying investments culminates in two possible results: one, that there is a right under the laws of the host state, in which case the tribunal can proceed and check the existence of other conditions of *ratione materiae* jurisdiction, and, two, that the laws of the host state do not recognise the alleged right, meaning that the case should be dismissed to the extent that the claimant's case solely rests upon the existence of such an alleged right.
89. Furthermore, when considered in more depth, laws of the host state regulate and determine very detailed practical questions concerning the creation and existence of rights underlying investments, including but not limited to matters concerning the definition of 'property', legal conditions of transfer of title in tangible and intangible property, and the binding force and enforceability of alleged contractual rights underlying investments.

[127] Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (n 11) 197.

## Chapter 4: Ascertaining the Contents of the Host State Law

1. Having dealt with the question of the legal basis for referring to the laws of the host state, an arbitrator deciding upon the legality requirement issue and/or the question of the creation and existence of rights/interests underlying investments in an investment treaty case should answer a second question which is the modality of establishing the contents of the host state law that the arbitrator is not familiar with.[1] No arbitrator could be expected to know the domestic laws of all individual states. Even very eminent arbitrators who might have decided myriads of cases lodged against or initiated by different states might have only dealt with a very small bit of the colossal legal systems of those countries to the extent that the issues related to the cases before them required the application of those small fractions of municipal laws.[2] Indeed, as one commentator has opined, the "very nature of international arbitration entails that the arbitrators are not necessarily trained in *lex causae*… The arbitrators may … come from different legal cultures and may not have any background in, or knowledge of, the *lex causae*."[3] In this regard, the PCIJ admitted in the *Brazilian Loans* case that the Court should not be expected to know the law of all individual states:

> Though bound to apply municipal law when circumstances so require, the Court, which is a tribunal of international law, and which, in this capacity, is deemed itself to know what this law is, is not obliged also to know the municipal law of the various countries.[4]

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[1] In this respect, see Y Banifatemi 'The Law Applicable in Investment Treaty Arbitration' in K Yannaca-Small (ed) *Arbitration under International Investment Agreements* (OUP 2010) 191-192 (distinguishing between various stages of (i) the identification of the applicable law; (ii) the subsequent investigation concerning the determination of the content of the applicable law; and (iii) the actual application of the applicable law).

[2] In a seminal article published by Arbitration International, Prof. Gabrielle Kaufmann-Kohler, an obviously eminent and reputable figure in contemporary international arbitration, quite candidly admitted that she had decided myriads of cases based on domestic laws of various countries spread in the five continents of the world while she did not know those laws at the time the proceedings in each case had commenced. She also said that even after deciding these cases she did not master these laws. She indicated that:

> Reflecting back on the cases in which I have been involved as an arbitrator, and certainly forgetting some of them, I realized that I have resolved disputes under German, French, English, Polish, Hungarian, Portuguese, Greek, Turkish, Lebanese, Egyptian, Tunisian, Moroccan, Sudanese, Liberian, Korean, Thai, Argentinean, Colombian, Venezuelan, Illinois, New York ... and Swiss law. Do I know these laws? Except for New York law, which I learned many years ago and would not pretend to now know, and Swiss law which I practice, although not that often as you see, the answer is clearly no.

G Kaufmann-Kohler, 'The Arbitrator and the Law: Does He/She Know it? Apply It? How? And a Few More Questions' (2005) 21(4) Arb Int'l 631. See also P Landolt, 'Arbitrators' Initiatives to Obtain Factual and Legal Evidence' (2012) 28(2) Arb Int'l 173.

[3] G Knuts, 'Jura Novit Curia and the Right to Be Heard – An Analysis of Recent Case Law' (2012) 28(4) Arb Int'l 671.

[4] *Payment in Gold of Brazilian Federal Loans Contracted in France* (*France v. Brazil*), Judgment, P.C.I.J. Rep. Series A, No. 21, 1929 (12 July 1929), p 124.

2. In other words, in a case before an international adjudicatory forum, "the principle of *iura novit curia* applies to international law, it does not apply to matters of national law."[5] In the *Fisheries Jurisdiction* case, the ICJ approved that the Court knows international law and has the duty to apply it even if the parties have not pleaded it before the World Court. Thus, in the circumstances that the Government of Iceland had failed to appear in order to plead its objections or to make its observations on the United Kingdom's arguments and contentions in law, the Court held that:

> The Court […] as an international judicial organ, is deemed to take judicial notice of international law, and is therefore required in a case falling under Article 53 of the Statute, as in any other case, to consider on its own initiative al1 rules of international law which may be relevant to the settlement of the dispute. It being the duty of the Court itself to ascertain and apply the relevant law in the given circumstances of the case, the burden of establishing or proving rules of international law cannot be imposed upon any of the parties, for the law lies within the judicial knowledge of the Court.[6]

3. Despite the fact that international adjudicators master international law, as mentioned above, arbitrators appointed in investment treaty arbitrations are, in most instances, unfamiliar with the laws of the host state.[7] Such an understandable lack of knowledge regarding the internal laws of many different individual states in individual investment treaty cases warrants obtaining reliable information about the laws of the host state in question and how they are applied in practice. This information should be acquired by a method that is observant of the 'right of the parties to be heard'.[8] Therefore, the role of the evidence presented by the disputants

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[5] J Crawford (ed), *Brownlie's Principles of Public International Law* (8th Edition, OUP 2012) 52.

[6] *Fisheries Jurisdiction* (*United Kingdom of Great Britain and Northern Ireland v. Iceland*) Merits, Judgment of 25 July 1974, p 10 [17]. See also J Paulsson, 'International Arbitration and the Generation of Legal Norms: Treaty Arbitration and International Law' (2006) 3(5) TDM 14; E De Brabandere, *Investment Treaty Arbitration as Public International Law: Procedural Aspects and Implications* (CUP 2014) 109-110.

[7] Party-appointed arbitrators appointed by host states are sometimes nationals of the host state. However, even in such cases, the party-appointed arbitrator is sometimes appointed because of his fluency in international law and arbitration rather than the domestic law of the host state. Bearing this point in mind, in many cases where a national of the host state is appointed as an arbitrator by the respondent state, the nominated person should not be expected to master the nuances of the internal law of the host state. Besides, even if the appointed person is fluent in the law of the host state, the fact that one member of the tribunal is knowledgeable about the domestic law does not make the whole tribunal an expert of the municipal law.

In practice also, the requirement that the arbitrators should have knowledge of the applicable host state law substantially narrows down the parties' range of choices for the appointment of competent arbitrators. J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 113.

[8] The principle that disputing parties must be heard on all the relevant issues (including legal matters) is one of the most fundamental rules of procedure. C Schreuer, L Malintoppi, A Reinisch & A Sinclair, *The ICSID Convention: A Commentary* (CUP 2009) 987-991. As was noted in Chapter 2, the *Fraport* award was annulled by the ICSID Annulment Committee, on the basis that there was "a serious departure from a fundamental rule of procedure". The departure from a fundamental rule of procedure in that case was that the tribunal did not permit submissions from the parties on heavily relied upon evidence. As such, the Committee held that since the right to be heard and the right to have adequate opportunity for rebuttal had not been observed by the tribunal, there was a serious departure from the

to introduce the law of the host state is of critical significance. Indeed, there are two principal ways by which an arbitral panel can obtain information about the laws of a given state: (i) submissions and evidence presented by the parties; and (ii) independent research conducted by the tribunal itself.[9] The PCIJ properly identifies the two ways by which the contents of the applicable law could be ascertained. It said in the *Brazilian Loans Case* that:

> Al1 that can be said in this respect is that the Court may possibly be obliged to obtain knowledge regarding the municipal law which has to be applied. And this it must do, either by means of evidence furnished [to] it by the Parties or by means of any researches which the Court may think fit to undertake or to cause to be undertaken.[10]

4. It must be noted that to respect the right of the parties to be heard, whereas an investment treaty tribunal has the right to conduct its own independent research and analysis – in particular, in jurisdictional matters that require a 'proactive' role to be carried out by the tribunal[11] – its conclusion should primarily be informed by the submissions of the parties to the dispute, or the comments that the parties provide on the arbitral tribunal's independent research and inquiry. This proposition is confirmed by the tribunal in *Emmis v. Hungary* which pinpointed that the submissions of the parties regarding the contents of the applicable municipal law and how it is applied in practice are of fundamental significance in framing the tribunal's mind with regard to local law issues at stake:

> Where the Tribunal is presented with a question of municipal law essential to the issues raised by the Parties for its decision, the Tribunal, whilst retaining its independent powers of assessment and decision, must seek to determine the content of the applicable law in accordance with evidence presented to it as to the content of the law and the manner in which the law would be understood and applied by the municipal courts.[12]

5. This is precisely why the International Law Association ("ILA") in its famous Recommendations on Ascertaining the Contents of the Applicable Law in International Commercial Arbitration provides that "[a]rbitrators should primarily receive information about the contents of the applicable law from the parties."[13] This is all the more so in cases where the application of that body of law is outcome-determining:

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principles of natural justice. See *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide, 23 December 2010 [177]-[178], [218], [227], [246]-[247].

[9] For different approaches to determining the contents of the applicable law, see JDM Lew, LA Mistelis & S Kroll, *Comparative International Commercial Arbitration* (Kluwer Law International 2003) 440-444; G Knuts (n 3) 672.

[10] *Payment in Gold of Brazilian Federal Loans Contracted in France* (*France v. Brazil*) (n 4) p 124.

[11] J Hepburn (n 7) 165.

[12] *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary*, ICSID Case No. ARB/12/2, Award, 16 April 2014 [175].

[13] International Law Association Rio De Janeiro Conference (2008) International Commercial Arbitration, Final Report Ascertaining the Contents of the Applicable Law in International Commercial Arbitration, Clause 5.

> When it appears to the arbitrators that the contents of applicable law might significantly affect the outcome of the case, arbitrators should promptly raise that topic with the parties and establish appropriate procedures as to how the contents of the law will be ascertained (in submissions with materials attached, through experts, witnesses or otherwise).[14]

6. Furthermore, the research undertaken by a court or tribunal should be checked with the parties to the dispute. In this respect, two specific clauses of ILA's above-mentioned Recommendations should be taken into consideration, which are based on the concern to assure 'due process' and tend to prevent 'taking the parties by surprise':

> Before reaching their conclusions and rendering a decision or an award, arbitrators should give parties a reasonable opportunity to be heard on legal issues that may be relevant to the disposition of the case. They should not give decisions that might reasonably be expected to surprise the parties, or any of them, or that are based on legal issues not raised by or with the parties
>
> […]
>
> If arbitrators intend to rely on sources not invoked by the parties, they should bring those sources to the attention of the parties and invite their comments, at least if those sources go meaningfully beyond the sources the parties have already invoked and might significantly affect the outcome of the case. Arbitrators may rely on such additional sources without further notice to the parties if those sources merely corroborate or reinforce other sources already addressed by the parties.[15]

7. Therefore, in threshold jurisdictional issues like the legality requirement and the existence and creation of rights/interests underlying an investment, in which the issues are outcome-determinative, reliance on the information and comments provided by the parties becomes much more important and necessary.
8. Having dealt with the methods to ascertain the contents of the host state law, the next question is the means through which one can identify and grasp the rules of local law. Undoubtedly, such information should be obtained by the submission and consideration of certain materials. Some of such materials are listed by the WTO Appellate Dispute Settlement Body in *US — Carbon Steel*: "Such evidence will typically be produced in the form of the text of the relevant legislation or legal instruments, which may be supported, as appropriate, by evidence of the consistent application of such laws, the pronouncements of domestic courts on the meaning of such laws, the opinions of legal experts and the writings of recognized scholars. The nature and extent of the evidence required to satisfy the burden of proof will vary from case to case."[16]

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[14] ibid, Clause 3.

[15] ibid, Clauses 8 and 10.

[16] *United States — Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany*, Report of the Appellate Body, WT/DS213/AB/R, Report No AB-2002-4, Doc No 02-6520, 28th November 2002, World Trade Organization [WTO] [157].

9. In practice, most disputants do their best to persuade the tribunal that their interpretation of domestic law is more to the point. In so doing, they usually file one, two, or sometimes, several of the materials mentioned above. They undertake to translate the relevant provisions of host state law (if necessary) in the way they see right, file relevant academic texts, and submit and translate (if necessary) decisions by municipal courts of the host state with regard to the issue in question. Moreover, if they are so lucky to find them, the parties would invoke the decisions of other international *fora* concerning the same legal issue of the relevant domestic law. Another significant way to assist the tribunal in understanding the host state law is through the submission of legal expert opinions on the pertinent issues of domestic law.[17] As pointed out by one commentator, "[w]hile the meaning of a statute or the interpretation of a case may not be apparent at a glance by the arbitrators, expert testimony might clarify the meaning and propose an interpretation of domestic law that is consistent with other sources before the tribunal."[18]
10. It is clear that the starting point for any investment treaty tribunal is the text of the domestic law or regulation in question. However, not all statutory texts are unambiguous. Furthermore, in certain instances, although the legal text is clear, it does not cover the whole picture which is the domestic legal system of the host state in its totality. A law translated and presented to the tribunal may have been repealed, amended, or superseded by another law.[19] Another possibility is that the law at issue may be construed and implemented totally differently in the host state in practice in a way that does not conform to the understanding and education of the arbitrators deciding the investment treaty case. Consequently, as one scholar has commendably suggested, it is a necessity to look beyond the text of the domestic regulation or statute.[20] As noted above, there are several ways to look behind the legal texts themselves.
11. As will be delineated in Chapter 7, of vital importance amongst the pieces of evidence proffered for establishing the contents of host state law are documents showing the application of the law of the host state in practice. In this regard, decisions of municipal courts (in particular, the highest of such courts) are of critical significance. In this connection, in the PCIJ case of the *Serbian Loans*, the Court noted that:

> For the Court itself to undertake its own construction of municipal law, leaving on one side existing judicial decisions, with the ensuing danger of contradicting the construction which has been placed on such law by the highest national tribunal and which, in its results, seems to the Court reasonable, would not be in conformity with the task for which the Court

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[17] For instance, in *Nagel v. Czech Republic*, the claimant had provided the tribunal with three legal expert opinions with respect to Czech law. The respondent had also relied upon an opinion of a legal expert for the explication of its laws. *William Nagel v. The Czech Republic*, SCC Case No. 049/2002, Final Award, 09 September 2003 [71], [306]-[307]. In certain cases, the tribunal relies upon the legal expert testimony submitted by the parties to reach a conclusion. See, for instance, *Plama Consortium Limited v. Bulgaria,* ICSID Case No. ARB/03/24, Award, 27 August 2008 [136]-[137].

[18] J Hepburn (n 7) 134.

[19] Along the same lines, see PB Stephan, 'International Investment Law and Municipal Law: Substitutes or Complements?' (2014) 9(4) CMLJ 357 (stating that: "the observer may fail to anticipate secondary rules that call off the primary rules that appear to apply to the transaction at hand, or the government may simply ignore its announced rules.")

[20] J Hepburn (n 7) 169-177.

> has been established and would not be compatible with the principles governing the selection of its members.[21]

12. Similarly, in this respect, the Annulment Committee in *Fraport v. Philippines* stated that an arbitral tribunal should give particular consideration to decisions of municipal courts as to the construction of the internal laws in question in order to determine how it would be applied within the overall domestic legal system. The Committee went on to note that "[t]his was particularly important in the present case as it is recognised that the Tribunal had not been chosen for its knowledge of Philippine law."[22] Therefore, legal findings of municipal courts of the host state are treated as 'evidence' of municipal law in investment treaty arbitrations and serve the purpose of establishing the contents of the local law of the recipient state.[23]

**Conclusion**

13. It is obvious that members of an arbitral tribunal seized of deciding an investment treaty case do not possess vast knowledge regarding sophisticated issues of municipal laws of all the individual states that happen to be respondents in investment treaty cases. For instance, in a dispute where the central question is whether an investor acquired enforceable contractual rights upon being announced as the winner of a bidding process in country A, no foreign arbitrator can be expected to know all the laws and regulations and administrative and/or judicial jurisprudence regarding bidding processes in that state. In this respect, to sail in safe waters, members of the tribunal should be oriented by the parties and become acquainted with the laws, regulations, and jurisprudence of the host state through the submissions and evidence presented by the disputants. Of course, the tribunal remains free to conduct its own independent research. However, if the issue the tribunal has independently surveyed is crucial to the outcome of the case, the tribunal should invite comments by the parties.
14. While several materials can assist an investment treaty tribunal in understanding the contents of the host state law (including the text of the laws and regulations in question (when necessary, a translation of such texts), legal expert testimony, doctrinal authorities on host state law as well as the practice of the courts of the host state on legal matters at issue, etc.), the most helpful and trustworthy tool for obtaining information regarding the meaning of the law in question seems to be through the jurisprudence of the courts of the host state (in particular, those of a higher rank) which determine how municipal law is implemented and interpreted in practice. As a matter of fact, courts of the host state are specialists and practitioners of host state law and they apply that body of law on a daily basis. Subsequently, unless negative circumstances exist that eliminate trust in specific court findings in question or the judicial system of the host state as a whole, investment treaty tribunals shall give due consideration and particular weight to the pertinent decisions of host state courts as the prime means for ascertaining the contents of host state law.

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[21] *Payment of Various Serbian Loans Issued in France* (*France v. Yugoslavia*), Judgment, P.C.I.J. Rep. Series A, No. 20, 1929 (12 July 1929) p 46.

[22] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide, 23 December 2010 [236].

[23] *Vigotop Limited v. Hungary*, ICSID Case No. ARB/11/22, Award, 1 October 2014 [509].

## Part II: The Revival of the Localisation Theory in Light of the Developments in Investment Treaty Law

1. So far, I have reviewed the role played by the internal laws of the host state in the determination of certain jurisdictional and substantive issues in investment treaty arbitrations. In Chapter 1, it was shown that host state law functions as 'law', rather than as 'fact', in a paramount way in deciding specific issues of subject-matter jurisdiction. It was also said in that Chapter that the municipal laws of the host state have a voice in matters of liability and merits, but this time primarily as 'facts' rather than as 'laws' unless the treaty in question provides otherwise. Chapters 2 and 3 concerned two specific and essential questions of *ratione materiae*, namely the legality of investment and the existence of rights/interests underlying investments and the application of municipal laws of recipient states to these jurisdictional matters. These two Chapters delineated the legal bases of the application of domestic laws of recipient states to these jurisdictional prongs. The discussion then followed in these Chapters by an analysis of the impact that the application of this body of law could have on the outcome of the jurisdiction *ratione materiae* analysis of an investment treaty tribunal. In addition, in these two Chapters (i.e. Chapters 2 &3), I dealt with a series of practical and significant subject-matter jurisdictional-related legal questions that had to be answered by reference to the laws of the host state. Additionally, Chapter 4 of the Thesis addressed the related question of ascertaining the contents of the host state law in an investment treaty arbitration.
2. Having pinpointed the general role of the national law of the host state in investment treaty arbitrations and its specific function in the determination of issues of subject-matter jurisdiction and bearing the outcome of these analytical steps in mind, in Part II of this Thesis, I will consider the overall effect and the level of control that the laws and the national courts of the host state have on the fate of an investment treaty case.
3. All those interested in international law of investment and the so-called 'international development law'[1] are familiar with concepts like the 'Calvo Doctrine' and the 'Localisation Theory'. As will be explained below in more detail, these were theories which dominated a great bulk of the developing world for long periods of time by resorting to which the governments and theorists of the underdeveloped nations attempted to leave the destiny of disputes arising out of foreign investment contracts in the hands of the laws and domestic courts and tribunals of the host state. In other words, the 'localisation theory' had two main pillars: First, any dispute arising from a foreign investment contract should be decided in accordance with the local laws of the recipient state. Second, local courts of the host state would have sole jurisdiction to decide foreign investment disputes. Due to significant resistance by the developed states which materialised itself in many different guises like arbitral awards unfavourable to localisation-related theories, and, in particular,

[1] The term 'international development law' has been used by a number of commentators: see, for instance, O Schachter, 'The Evolving International Law of Development' (1976) 15 Columbia Journal of Transnational Law 1; M Bulajic, *Principles of International Development Law: Progressive Development of the Principles of International Law Relating to the New International Economic Order* (Vol. 38, Series: Nijhoff Law Specials 1986); E Kwakwa, 'Emerging International Development Law and Traditional International Law - Congruence or Cleavage?' (1987) 17 The Georgia Journal of International and Comparative Law 431; M Sornarajah, 'The Climate of International Arbitration' (1991) 8(2) J Int'l Arb 47, 72-73; AF Maniruzzaman, 'International Development Law as Applicable Law to Economic Development Agreements: A Prognostic View' (2001) 20 Wisconsin International Law Journal 1.

with the advent of the bilateral investment treaties, nowadays, we treat these theories as stories of historical interest that one could tell his/her law students at a leisure time. The life and death of the 'localisation theory' will be reviewed in Chapter 5 of this Thesis.

4. That being said, although such kind of historical treatment does not seem to be far from the truth, a careful analysis of investment treaty law as it stands today would show that nowadays, the laws of the host state have a controlling role in the end result of investment treaty cases at least to some extent. This was very much shown in Chapters 1 to 3 and will be very briefly discussed here again with a focus on the shift of the approach of bilateral investment treaties and investment treaty arbitrations towards the issue. This topic will be covered in Chapter 6 of this Thesis. Additionally, Chapter 7 will demonstrate that, particularly as a result of recent developments in investment treaty law, the courts and tribunals of the host state have now a stronger foothold to make more outcome-determining interventions, observations, and decisions with respect to investment treaty cases not only on matters regarding jurisdiction but also on matters concerning admissibility and merits. When recalling the two pillars of the 'localisation theory' as it was formulated in the 1960s and 1970s, i.e., (1) foreign investment disputes should be decided in accordance with host state laws, and (2) foreign investment disputes should solely be decided by the host state courts, these developments in the role of the laws and the courts of the host state in modern investment treaty law, when seen and coupled together, might strike any reasonable bystander as giving rise to 'relocalisation of foreign investment disputes to some extent'. Indeed, one could say that although the 'localisation theory' in the context of foreign investment contracts has been purged long ago, a trend which has gradually got momentum in investment treaty law is considered to be reflective of several features of the old 'localisation theory'.
5. In order to examine the current level of the importance of the laws and the judicial systems of host states in investment treaty cases, I will open this Part Two by a historical analysis of the 'Calvo Doctrine' and the 'localisation theory' (Chapter 5). In this Chapter, I will also look into the historical roots, premises, and the contents of these theories and doctrines followed by an enquiry regarding the fate of these ideas. Chapter 5 will then continue by considering the emergence of investment treaties – in particular, bilateral investment treaties – and the function they were intended to carry out in eliminating the effects of the host state law and the interference and influence of the judiciary of the recipient state on the outcome of foreign investment disputes. Chapter 6 will then come in to distil the in-depth discussions of Chapters 1 to 3 of this Thesis (in particular, on the role of the laws of the host state on issues of subject-matter jurisdiction), followed by a brief consideration of the shift in the approach of investment treaty-making and investment treaty arbitration towards the role of the laws of the host state, thereby, outlining the overall impact of the laws of the host state on the outcome of investment treaty cases in light of the recent developments in investment treaty arbitration practice. However, the 'localisation theory' had two pillars as far as matters regarding dispute settlement were concerned. One pillar was that the laws of the host state governed the substance of the dispute and the other was that courts of the host state had sole jurisdiction to decide these investment contract cases. Therefore, in order to appraise the current level of 'localisation' of investment treaty law, it is imperative to analyse not only the current role of host state laws but also the current role of host state courts in investment treaty arbitrations. Put differently, both of the prime materialisations of the local state power, i.e., laws which are the products of the lawmaking

body of the state and courts which are emanations of the law-enforcing body of the state, should be analysed to see whether investment treaty arbitrations have been 'localised', and if so, to what extent. Furthermore, the true role of host state law in investment treaty arbitration will not be fully discovered without analysing the relevance of the courts of the host state and their findings in an investment treaty arbitration since laws are literally spelt out by the courts in practice. Therefore, Chapter 6 will be followed by another Chapter entailing a critical and thorough appraisal of the contribution that the national courts and tribunals of the capital-importing countries make to a given investment treaty arbitration proceeding (Chapter 7). The discussion considers the latest approaches and trends in investment treaty-making and investment treaty arbitration jurisprudence as to the role that is assigned to the courts of the host state in the resolution of investment treaty disputes.

6. As will be discussed in the ensuing Chapters, these developments in investment treaty law show that laws and courts of the host state have gained such significant and outcome-determining roles in current investment treaty law which could be reminiscent of the old 'localisation theory' to some extent.

## Chapter 5: The Localisation Theory: Roots, Contents, and Its Legal Destiny

### Introduction

1. I will open this Chapter by reviewing the roots, contents, and the fate of the domestic-centric theories of 'Calvo Doctrine' and the 'Localisation Theory' (**Section One**), followed by a consideration of the advent of bilateral investment treaties and the impact of such treaties on the theories put forward by developing states in the 1960s-1970s to safeguard the position of their laws and courts in resolving foreign investment disputes (**Section Two**).

### Section One: Classical Domestic-Centric Theories: The Calvo Doctrine and the Localisation Theory

2. Approximately two hundred years ago, almost the whole world was reigned by a few European countries which either colonised other countries and areas or had substantial economic, political, and military dominance over them. The first wave of decolonisation took place in Latin America.[1] Unsurprisingly, the historical distrust of international arbitration, as an apparatus devised by West European countries to protect their interests, seems to have stemmed from South America.[2] In fact, before the vast decolonisation of the 1955-1965 period which culminated in the formation of another powerful group of developing countries, the Latin American countries were the vanguards of what more than a century later would be called the 'localisation theory'.
3. Dissatisfied with the outcome of foreign investment arbitration and diplomatic protection cases, these countries were urged by Carlos Calvo, an Argentinian national, to localise foreign investment contracts by making them subject to the jurisdiction of the courts and the laws of the host state.[3] Besides, in accordance with this theory – which was later called the 'Calvo Doctrine' – foreign investors were required to waive the right to call for diplomatic protection by their government at the time of the conclusion of the investment

[1] The dates of independence and the then world powers from which these Latin American countries became independent are as follows: Argentina (1816, from Spain); Bolivia (1825, from Spain); Brazil (1822, from Portugal); Chile (1810, from Spain); Colombia (1810, from Spain); Costa Rica (1821, from Spain); Cuba (1898, from Spain and 1902 from the US); Dominican Republic (1844, from Haiti); El Salvador (1821, from Spain); Guatemala (1821, from Spain); Haiti (1803, from France); Honduras (1821, from Spain); Mexico (1810, from Spain); Nicaragua (1821, from Spain); Panama (1821, from Spain and later from Colombia); Paraguay (1811, from Spain); Peru (1821, from Spain); Uruguay (1825, from Brazil); Venezuela (1811, from Spain). As can be seen, most of these countries went through decolonisation in the 1810s-1820s and became independent from Spain, with the eminent exception of Brazil which became independent from Portugal and Haiti which became independent from France.

[2] L Atsegbua, 'International Arbitration of Oil Investment Disputes: The Severability Doctrine and Applicable Law Issues Revisited' (1993) 5 African Journal of International & Comparative Law 634, 638.

[3] On some scholars' accounts, there was another eminent jurist from the Latin American region, namely Mr. Andres Bello from Venezuela, who was actually the first person to advance the Latin American version of 'localisation'. See FG Dawson, 'The Influence of Andres Bello on Latin-American Perceptions of Non-Intervention and State Responsibility' (1987) 57 BYIL 253, 273; S Montt, *State Liability in Investment Treaty Arbitration: Global Constitutional and Administrative Law in the BIT Generation* (Hart Publishers 2009) 42.

contract.[4] [5] The aim of the formulation of the Calvo doctrine was to assert the Latin American countries' right to economic self-determination and territorial jurisdiction.[6]

4. Although it did not sell globally, the doctrine received a very warm welcome in Latin American countries. They sought to implement the essential ideas inherent in the Doctrine by inserting coherent provisions in their treaties, constitutions, municipal laws, and in the contracts they concluded with western investors.[7] Indeed, the most obvious manifestation of this doctrine can be tracked down to the inclusion of certain contractual clauses in a number of foreign investment contracts concluded between the governments of Latin American countries and foreign investors pursuant to which foreign investors agreed to waive their right to seek diplomatic protection from their national government in connection with disputes arising out of the investment contract. This type of provision became famous as 'Calvo Clause'.[8] This so-called Calvo Clause was inserted, to simply give one single example, in a contract for completion of the most important railroad line in Chile in 1861.[9]
5. Going approximately one century forwards in the history, with the vast extinguishment of colonialism across Asia and Africa in the second half of the 20th century, like the Latin American countries, the new independent states as well as other older independent – but previously ill-influenced by colonial powers – countries also began to design and implement laws, policies, and strategies to gain legal control over foreign investment contracts and disputes.[10] These localisation efforts were either made individually or collectively.

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[4] J Paulsson, 'Third World Participation in International Investment Arbitration' (1987) 2(1) ICSID Rev-FILJ 19-20.

[5] The conditions prescribed by the Calvo Doctrine have been usefully distilled by certain commentators: "… the inference drawn from the whole text, read together with the general principle that foreigners are subject to the local law and must submit their disputes to local courts, has given the Spanish-American countries a basis to assert the doctrine that in his private litigation the alien must exhaust his local remedies before invoking diplomatic interposition and that in his claims against the state he must make the local courts his final forum." See EM Borchard, *The Diplomatic Protection of Citizens Abroad or the Law of International Claims* (The Banks Law Publishing Company 1915) 793. Another commentator has also usefully extracted the main pillars of the Doctrine: "Calvo, basing his theories on the generally accepted rules of national sovereignty, equality of states, and territorial jurisdiction, set forth two cardinal principles which constitute the core ideas of his doctrine: First, that sovereign states, being free and independent, enjoy the right, on the basis of equality, to freedom from "interference of any sort" […] by other states, whether it be by force or diplomacy, and second, that aliens are not entitled to rights and privileges not accorded to nationals, and that therefore they may seek redress for grievances only before the local authorities. These two concepts of nonintervention and absolute equality of foreigners with nationals are the essence of the Calvo Doctrine." See DR Shea, *The Calvo Clause: A Problem of Inter-American and International Law and Diplomacy* (University of Minnesota Press 1955) 19-20.

[6] M Sornarajah, 'The Climate of International Arbitration' (1991) 8(2) J Int'l Arb 47, 71; DR Shea (n 5) 19-20.

[7] DR Shea (n 5) 20-21.

[8] See RP Lazo, 'The No of Tokyo Revisited: Or How Developed Countries Learned to Start Worrying and Love the Calvo Doctrine' (2015) 30(1) ICSID Rev-FILJ 176.

[9] See RP Lazo (n 8) 176; S Montt (n 3) 46.

[10] See M Sornarajah, 'Power and Justice in Foreign Investment Arbitration' (1997) 14(3) J Int'l Arb 103, 111-112. For an economic analysis of such strategies and policies in a legal context, see JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Frameworks for Foreign Capital* (OUP 2013) 59 *et seq*; T Wälde, 'A Requiem for the 'New International Economic Order': The Rise and Fall of Paradigms in International Economic Law' in G Hafner, G Loibl, A Rest, L Sucharipa-Behrmann & K Zemanek (eds) *Liber Amicorum Professor Ignaz Seidl-Hohenveldern in Honour of his 80th Birthday* (Kluwer Law International 1998) 778 *et seq*.

6. On an individual level, certain countries revised their laws and regulations to stipulate that the applicable law to investment contracts is the law of the state contracting party to such contracts. For instance, Article 23 of the Petroleum Act of Iran (1974) provided that: "[t]he validity, interpretation and implementation of the [petroleum] contracts shall be subject to the laws of Iran." Another example that comes to mind in this regard is Article 74 of Decree No. 222 (1987) of Colombia which provided that contracts to which the state or a state entity is a party are governed by the laws of Colombia and subject to the jurisdiction of Colombian courts.[11]
7. In addition to amendments of their laws, many of the developing countries with rich natural resources moved to explicitly mention in their investment contracts with aliens that their laws, and not any other law, govern the substance of their foreign investment contractual relationships. In particular, in a series of petroleum investment contracts concluded by certain Members of the Organization of the Petroleum Exporting Countries ("OPEC") with foreign investors, the laws of the host state were chosen as the applicable law of the contract.[12]
8. On a collective level, the efforts of the developing countries in localising foreign investment contracts were principally manifested in a series of resolutions adopted by the UN General Assembly where the developing countries had a numerical majority. The most salient of these resolutions are the following: General Assembly Resolution No. 1803

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[11] See HAG Naon, 'Arbitration in Latin America: Overcoming Traditional Hostility' (1989) 5(2) Arb Int'l 164, fn 39.

[12] See L Atsegbua (n 2) 655-656; VC Igbokwe, 'Developing Countries and the Law Applicable to International Arbitration of Oil Investment Disputes: Has the Last Word been Said?' (1997) 14(1) J Int'l Arb 99, 116-118 (referring to the Production Sharing Contract between the Nigerian National Petroleum Corporation ("NNPC") and Ashland Oil Nigeria Limited ("AON") dated 12 June 1973, the Service Contract dated 07 August 1978 between the National Iranian Company ("NIOC") and Ultramar Company and, the contract between Saudi Arabia and ENI). See also AS El-Kosheri and TF Riad, 'The Law Governing A New Generation of Petroleum Agreements: Changes in the Arbitration Process' (1986) 2 ICSID Rev-FILJ 270-271 (referring to the 1971 Joint Structure Agreement concluded between the "NIOC" and Amerada Hess Corp; 1974 Service Contract concluded between the "NIOC" and Ultramar Co. Ltd., and the 1980 contract between Indonesia and P.T. Anggi Chemallay).

More broadly, in a comprehensive survey conducted by Martin Bartels, 29 investment contracts concluded by developing countries with foreign investors in the mining sector from the 1950s-1980s have been identified which expressly provide for the application of the laws of the host state to the contract: (1) the contract between Indonesia and Anggi Chemallay (1980); (2) the contract between Bukit Asam and Indonesia (1973); (3) the contract between Sulawesi and Indonesia (1977); (4) the contract between Rennell Island and Solomon Islands (1972); (5) the contract between Sierra Rutile and Sierra Leone (1972); (6) the contract between Gove and Australia (1968); (7) the contract between Petaquilla and Panama (1971); (8) the contract between Cuajone and Peru (1969); (9) the contract between Alcan Queensland and Australia (1965); (10) the contract between Wittennom and Australia (1972); (11) the contract between Selebi Phikwe and Botswana (1959); (12) the contract between Amalgamated Diamond and Ghana (1976); (13) the contract between Metalsazmeh and Iran (1970); (14) the contract between Cerro Matoso and Colombia (1970); (15) the contract between Las Brisas and Colombia (1975); (16) the contract between IAN/TOTAL and Colombia (1980); (17) the contract between Vaupes Y Guyana and Colombia (1978); (18) the contract between O'OKIEP Copper and Lesotho (1970); (19) the contract between Lesteng-La-Trai and Lesotho (1974); (20) the contract between Cerro Colorado and Panama (1980); (21) the contract between OK Tedi and Papua New Guinea (year not identified); (22) the contract between Moyamba & Bonthe and Sierra Leone (1961); (23) the contract between Brokopondo and Surinam (1958); (24) the contract between Quebrada Blanca and Chile (1977); (25) the contract between Finan and Jordan (1974); (26) the contract between JPCM and Jordan (1975); (27) the contract between Aquaba and Jordan (1978); (28) the contract between Kerio Valley and Kenya (1971); (29) the contract between Kinangoni and Kenya (1971). See M Bartels, *Contractual Adaptation and Conflict Resolution* (Kluwer Law and Taxation Publishers 1985) 106-107.

(XVII) of 14 December 1962 on "Permanent Sovereignty over Natural Resources",[13] the General Assembly Resolution No. 3201 (S-VI) on 01 May 1974 on "Declaration on the Establishment of a New International Economic Order",[14] and the General Assembly Resolution No. 3281 (XXIX) on 12 December 1974 on "Charter of Economic Rights and Duties of States".[15]

9. Article 2(2)(C) of the "Declaration on the Establishment of a New International Economic Order" is the most notable resemblance of the efforts of developing countries to localise foreign investment contracts.[16] This provision, *inter alia*, confirms the right of each sovereign state to:

> … 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. In any case where the question of compensation gives rise to a controversy, it shall be settled under the domestic law of the nationalizing State and by its tribunals, unless it is freely and mutually agreed by all States concerned that other peaceful means be sought on the basis of the sovereign equality of States and in accordance with the principle of free choice of means.[17]

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[13] 'Permanent Sovereignty over Natural Resources' GA Res 1803, XVII, 14 December 1962.

[14] 'Declaration on the Establishment of a New International Economic Order' GA Res 3201, S-VI, 01 May 1974. This Resolution entailed a number of broad economic goals for developing states: "national sovereignty over a State's resources, sovereign equality of States, discretion of States as to the admission of foreign investment, better conditions for the economic and social development of poorer countries in international trade and investment, equal share of profits between the host states and investors, and lowering the standard of compensation for expropriated foreign companies." See M Herdegen, *Principles of International Economic Law* (OUP 2013) 16. See also J Voss, 'The Protection and Promotion of European Private Investment in Developing Countries-An Approach Towards A Concept For A European Policy on Foreign Investment: A German Contribution' (1981) 18(3) Common Market Law Review 363, 371.

[15] 'Charter of Economic Rights and Duties of States' GA Res 3281, XXIX, 12 December 1974.

[16] Thomas Wälde characterises the two cited 1974 Resolutions of the General Assembly, i.e., the "Declaration on the Establishment of a New International Economic Order" and the "Charter of Economic Rights and Duties of States", as the most 'important', 'comprehensive', 'far-reaching', and 'controversial' resolutions of the General Assembly in economic matters. T Wälde (n 10) 772.

[17] To have a better picture of developing countries' achievements in this Resolution, it is worthwhile to cite Article 2 of this Resolution in full:

> 1. Every State has and shall freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities.
>
> 2. Each State has the right:
>
> (a). To regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities. No State shall be compelled to grant preferential treatment to foreign investment;

10. As one can see, the precious and remarkable achievement of developing countries as enshrined in this provision is a default rule pursuant to which the laws of the host state apply to the critical question of determining compensation in case of a taking which question should be decided by the courts or tribunals of the host state unless otherwise agreed.[18] These two accomplishments in this very important international instrument precisely represent the two anchors of the 'localisation theory': foreign investment disputes should be resolved by reference to the local law of the host state, and, in principle, such disputes should be settled by the national courts and tribunal of the recipient state.
11. Another noticeable particular example that comes to mind in terms of collaborative endeavours of developing countries in the post-colonisation era is the marked opposition of the Latin American countries (supported by Iraq and Philippines) in 1964 to the resolution of finalising the draft text of the envisaged ICSID Convention. In the related meeting, Latin American countries, represented by Chile, voiced vehement opposition to the idea of resolution of foreign investment disputes by international arbitration rather than by the national courts of the host state.[19]
12. Additionally, as an allied sectoral move, in 1968, at the XVIth Conference of OPEC, the Members of the Organisation put forward a unified position concerning the competent forum for the resolution of foreign investment disputes in the petroleum sector by adopting Resolution XVI.90. The Member States declared that:

> Except as otherwise provided in the legal system of a Member Country, all disputes arising between the Government and operators shall fall

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> (b). To regulate and supervise the activities of transnational corporations within its national jurisdiction and take measures to ensure that such activities comply with its laws, rules and regulations and conform with its economic and social policies. Transnational corporations shall not intervene in the internal affairs of a host State. Every State should, with full regard for its sovereign rights, cooperate with other States in the exercise of the right set forth in this subparagraph;
>
> (c). To 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. In any case where the question of compensation gives rise to a controversy, it shall be settled under the domestic law of the nationalizing State and by its tribunals, unless it is freely and mutually agreed by all States concerned that other peaceful means be sought on the basis of the sovereign equality of States and in accordance with the principle of free choice of means.

Given the contents of this provision and other rules contained in this Resolution, it is unsurprising that a number of developed countries voted against this Resolution (namely, Belgium, Denmark, Germany, Luxembourg, the United Kingdom, and the United States) or abstained (e.g. Austria, Canada, France, Ireland, Italy, Japan, the Netherlands, Norway, and Spain).

[18] Another collective UN-oriented attempt by developing countries at this juncture was the "Code of Conduct on Transnational Corporations", which aimed at regulating the conduct of transnational corporations. See Draft United Nations Code of Conduct on Transnational Corporations (1984) 23(3) ILM 626-640. This Code was drafted by the United Nation's Commission on Transnational Corporations, a subcommittee of the Economic and Social Council of the United Nations. Due to substantial disagreement over the contents of the Draft Code, the negotiations were suspended in 1992. See P Muchlinski, *Multinational Enterprises and the Law* (OUP 2007) 660-662.

[19] International Centre for Settlement of Investment Disputes (ICSID), *History of the ICSID Convention* (Vol. 2, ICSID 1968) 606; RP Lazo (n 8) 181-182.

exclusively within the jurisdiction of the competent national courts or the specialized regional courts, as and when established.[20]

13. As can be clearly observed, a common denominator of all these collaborative and individual efforts by developing countries is that they try to determine the local courts of the recipient state as competent forums to decide foreign investment cases and/or to designate the law of the host state as the governing law to investor-state controversies.
14. Pursuant to the above-mentioned unilateral measures and collaborative endeavours by developing countries, some scholars, particularly from the so-called Third World countries, contended that, even absent any stipulation, the internal law of the host state is the law applicable to the substance of investment contract disputes and that the court of the host state is the competent forum for adjudicating disputes arising out of such contractual relationships.[21] Indeed, from the lens of these commentators, all these measures, resolutions, and doctrines purported to 'localise' investment contracts with foreign investors, thereby subjecting them to the control and the jurisdiction of host state law and host state judicial system.[22]
15. However, these efforts received strong reactions from the countries of the North, i.e. capital-exporting countries. The mindset was that subjecting the foreign investment contract to the national law and national courts of the host state would leave the investor at the whim of its co-contractor.[23] These reactions were represented either in the guise of legal doctrines or in the form of arbitral awards rendered in favour of western investors by ignoring the laws of the host state. These western responses are frequently referred to as the 'internationalisation'[24] of foreign investment contracts. In Sornarajah's view, pursuant to the so-called theory of internationalisation, investment contracts concluded between foreign investors and host states are "by nature international contracts subject to some supranational system".[25]
16. In terms of doctrinal support, according to Sornarajah, several theoretical solutions were offered by publicists of capital-exporting countries to internationalise state contracts with foreign investors. In his view, these theories are: (i) 'the assimilation of international contracts to international treaties'; (ii) insertion of 'stabilisation' clauses immunising contracts from future legislative changes; (iii) choosing 'general principles of law',

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[20] Declaratory Statement of Petroleum Policy in Member Countries, Resolution No. xvr.90, 1968 OPEC Conference, Vienna: Austria, reprinted in OPEC Official Resolutions and Press Releases, 1960-1990, at p 63.

[21] See, for example, AS El-Kosheri and TF Riad (n 12) 257-258; M Sornarajah, 'The Climate of International Arbitration' (n 6) 47; L Atsegbua (n 2) 634, 636-637 (referring the above-cited UN Resolutions and stating that they "have given a strong impetus to developing countries and these countries now claim that foreign investment contracts are governed by the domestic law of the nationalising State." [footnote omitted]).

[22] The term 'localisation' was used, *inter alia*, by Sornarajah. See Sornarajah, *The International Law on Foreign Investment* (4th edn, CUP 2017) 116. Another commentator uses the term "relocalisation" for the same theory put forward by developing countries in the 1970s-1980s. See VC Igbokwe, 'Developing Countries and the Law Applicable to International Arbitration of Oil Investment Disputes: Has the Last Word been Said?' (n 12) 116-123.

[23] O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 94; C Leben, 'La Théorie Du Contrat d'Etat Et L'évolution Du Droit International Des Investissements' (2004) 302 Collected Courses of the Hague Academy of International Law 221-222.

[24] M Sornarajah, *The International Law on Foreign Investment* (n 22) 339 *et seq*. El-Kosheri and Riad alternatively term this concept as 'delocalization' or 'transnationalization'. See AS El-Kosheri and TF Riad (n 12) 257-258.

[25] M Sornarajah, 'Power and Justice in Foreign Investment Arbitration' (n 10) 103, 107.

'transnational law' or 'public international law' as the substantive law applicable to disputes arising from the investor-state contract; (iv) including arbitration clauses in investment contracts pursuant to which disputes arising from investment contracts must be settled by an arbitral tribunal rather than by the state party's courts.[26]

17. In Sornarajah's opinion, these theories were bolstered by a series of international arbitral awards rendered in favour of foreign investors, which for him were 'charades'.[27] Indeed, in a series of arbitral awards rendered in the period of the 1950s-1980s, several arbitral tribunals refused the application of domestic law of the host state to the so-called 'economic development agreements'[28] and went on to apply international law or general principles of law to the substance of the investment contract disputes.[29] These arbitral tribunals disregarded the laws of the host state either because they considered the law of the host state to be insufficient and/or inchoate to resolve complicated issues of

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[26] M Sornarajah, 'The Climate of International Arbitration' (n 6) 47, 50-69. See also HE Kjos, *Applicable Law in Investor-State Arbitration: The Interplay Between National and International Law* (OUP 2013) 215 *et seq*. For a review of the theoretical underpinnings of the 'internationalisation' theory, see FA Mann, 'The Law Governing State Contracts' (1944) 21 BYIL 11; P Jessup, *Transnational Law* (Yale University Press 1956); A Verdross, 'The Status of Foreign Private Interests Stemming from Economic-Development Agreements with Arbitration Clauses' in M Bender (ed) *Selected Readings on Protection by Law of Private Foreign Investment* (The Southwestern Legal Foundation, International and Comparative Law Center 1964); FA Mann, 'State Contracts and State Responsibility' (1960) 54 AJIL 572; A Verdross, 'Quasi-International Agreements and International Commercial Transactions' (1964) 18 Yearbook of World Affairs 230; J Paulsson, 'Third World Participation in International Investment Arbitration' (n 4) 46; SM Schwebel, 'International Arbitration: Three Salient Problems' (1987) 3(3) Arb Int'l 1-60; P Weil, 'The State, the Foreign Investor, and International Law: The No Longer Stormy Relationship of a *Ménage à Trois*' in S Schlemmer-Schulte and KY Tung (eds) *Liber Amicorum Ibrahim F.I. Shihata* (Kluwer Law International 2001).

[27] M Sornarajah, 'The Climate of International Arbitration' (n 6) 47, 50-69. See also L Atsegbua (n 2) 634, 647 *et seq*; M Sornarajah, 'Power and Justice in Foreign Investment Arbitration' (n 10) 103, 107.

[28] This term has been used by several commentators. See, for instance, JN Hyde, 'Economic Development Agreements' (1962) 105 Collected Courses of the Hague Academy of International Law; A Verdross, 'The Status of Foreign Private Interests Stemming from Economic-Development Agreements with Arbitration Clauses' (n 26); SI Pogany, 'Economic Development Agreements' (1992) 7(1) ICSID Rev-FILJ; RB Lillich, 'The Law Governing Disputes under Economic Development Agreements: Re-Examining the Concept of Internationalisation' in RB Lillich & CN Brower (eds), *International Arbitration in the Twenty-First Century, Towards Judicialization and Uniformity* (Transnational Publishers 1994).

[29] See, for instance, *Petroleum Development Ltd. v. The Sheikh of Abu Dhabi* (1951) 18 ILR 144; *Ruler of Qatar v. International Maritime Oil Company* (1953) 20 ILR 534; *Saudi Arabia v. Arabian American Oil Company (Aramco)* (1963) 27 ILR 117 *et seq*; *Sapphire International Petroleum Ltd. v. National Iranian Oil Company (NIOC)* (1964) 13 International & Comparative Law Quarterly 1011 *et seq*; *BP Exploration Company (Libya) Limited v. Government of the Libyan Arab Republic*, 10 October 1973 and 01 August 1974 (1979) 53 ILR 297 *et seq*; *Texaco Overseas Petroleum Company and California Asiatic Oil Company v. The Government of the Libyan Arab Republic*, Award on Merits, 19 January 1977 (1979) 53 ILR 389; *LIAMCO v. The Government of the Libyan Arab Republic*, Award of 12 April 1977 (1981) Yearbook of Commercial Arbitration 89 *et seq*; *Revere Copper and Brass, Inc v. Overseas Private Investment Corporation*, Award, 24 August 1978, AAA Case No. 16/10/0137/76, 17 ILM 1321.

For commentary and description of these awards, see, VC Igbokwe, 'Developing Countries and the Law Applicable to International Arbitration of Oil Investment Disputes: Has the Last Word been Said?' (n 12) 111-114; M Sornarajah, 'The Climate of International Arbitration' (n 6) 47, 58-64; L Atsegbua (n 2) 634, 650-655; M Sornarajah, 'Power and Justice in Foreign Investment Arbitration' (n 10) 103, 107 *et seq*; KM Al-Jumah, 'Arab State Contract Disputes: Lessons from the Past' (2002) 17(3) Arab Law Quarterly 215, 217-223; MB Ayad, 'Harmonization of Custom, General Principles of Law, and Islamic Law in Oil Concessions' (2012) 29(5) J Int'l Arb 477, 499-513.

international investment law[30] or because of the fact that the transnational nature of such contracts and the great economic interests at stake necessitated the application of international law rather than domestic law. In the latter group of awards, some of the arbitral tribunals reasoned that application of the host state law would be inappropriate in the context of those investment contractual disputes because the investor has assumed a substantial risk when investing in the host state and subjecting him/her to the laws of the host state would dissuade foreign investments to flow to developing countries.[31]

18. These influential doctrines and arbitral awards, backed by the significant element of political power, seriously curtailed the efforts of the capital-receiving countries to localise foreign investment contracts. Even the legal value and the law-creating effect of the biggest achievements of developing countries, i.e., the Resolutions of the General Assembly of the United Nations, were also seriously called into question by some of these arbitral awards.[32]
19. The force behind these efforts to negate the control of the laws and the courts of the host state over the destiny of international investment contracts even imposed itself on the more long-standing and more persistent countries of Latin America. In an article published in 1989, a commentator from Latin America narrated an end to the 'Latin American hostility' vis-a-vis international arbitration beginning from 1975 or thereabouts.[33] According to Salacuse, the fact that in the 1990s, many of the Latin American countries acceded and/or ratified the ICSID Convention is an indicator of their approach to the internationalisation of foreign investment contracts and their departure from localisation theories including the Calvo Doctrine.[34]
20. Apart from these sturdy legal encounters on the part of the developed countries' scholars and practitioners, the economic element also simultaneously betrayed the governments of the developing countries leaving them almost empty-handed vis-à-vis their nations with no substantial attainment to justify the workability of their much-vaunted domestic-based legal and economic theories. Put differently, these domestic-based legal and economic theories had not brought wealth and prosperity to the developing nations. Therefore, the

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[30] See, for instance, *Petroleum Development Ltd. v. The Sheikh of Abu Dhabi* (n 29) 144; *Ruler of Qatar v. International Maritime Oil Company* (n 29) 534; *Saudi Arabia v. Arabian American Oil Company* (n 29) 117 *et seq*.

[31] See, for instance, *Sapphire International Petroleum Ltd. v. National Iranian Oil Company (NIOC)* (n 29) 1011 *et seq*; *BP Exploration Company (Libya) Limited v. Government of the Libyan Arab Republic* (n 29) 297 *et seq*; *Texaco Overseas Petroleum Company and California Asiatic Oil Company v. The Government of the Libyan Arab Republic* (n 29) 389; *LIAMCO v. The Government of the Libyan Arab Republic* (n 29) 89 *et seq*; *Revere Copper and Brass, Inc v. Overseas Private Investment Corporation* (n 29) 1321.

[32] See, for instance, *Texaco Overseas Petroleum Company, California Asiatic Oil Company v. The Government of the Libyan Arab Republic* (n 29) 389 [83].

[33] HAG Naon (n 11) 137-138, 156-157. See also VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (2006) 23(4) J Int'l Arb 274.

[34] JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (n 10) 72. Most Latin American countries signed and ratified the ICSID Convention in the 1990s: Argentina (signature 1991, ratification 1994); Bolivia (signature 1991, ratification 1995); Chile (signature 1991, ratification 1991); Colombia (signature 1993, ratification 1997); Costa Rica (signature 1981, ratification 1993); Ecuador (signature 1986, ratification 1986); Guatemala (Signature 1995, ratification 2003); Nicaragua (signature 1994, ratification 1995); Panama (signature 1995, ratification 1996); Peru (signature 1991, ratification 1993); Uruguay (signature 1992, ratification 2000), and Venezuela (signature 1993, ratification 1995). See <https://icsid.worldbank.org/en/Pages/about/Database-of-Member-States.aspx> 'accessed 31 May 2018'. However, three of these countries, namely Bolivia, Ecuador, and Venezuela denounced the ICSID Convention respectively in 2007, 2009, and 2012.

governments of these countries did not have a good reason to persist in the pursuit of such theories any further.[35]

21. As a result of the western legal theorising and legal actions as well as the new economic realities, it was not difficult to hear the drums of the funeral ceremony of the 'localisation theory' and the new international economic order. Indeed, one commentator observed that by 1990, the new international economic order project was 'basically dead'.[36]
22. From a legal angle, the last element that came to the scene to totally defeat the 'localisation theory' and the purported legal achievements of the UN Resolutions (including the 'New International Economic Order' and the 'Charter of Economic Rights and Duties of States') was the vast and ever-increasing conclusion of bilateral – and in certain instances multilateral – investment treaties which were intended to actually – and this time not artificially – internationalise foreign investment contracts, thus, effectively dispossessing the laws and the courts of the host state of any meaningful effect on the fate of these transnational investment arrangements. This significant development in the history of international investment law and its consequences will be studied briefly below.

**Section Two: The Emergence of Bilateral Investment Treaties**

23. While the theory of 'localisation' was fading away by the enormous attacks of arbitral awards, doctrinal authorities, and the new realities of the liberal economic world, a new player, full of vim and vigour, stepped into the battleground and put an end to the already doomed 'localisation theory'.

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[35] Analysing the historical developments from an economic point of view, Salacuse describes two general development models adopted by developing countries since the 1950s. For Salacuse, the first development model, i.e. Development Model I, which was very popular in the 1950s-1960s, had four basic elements: (i) public ordering and state planning; (ii) reliance on public sector enterprises; (iii) restriction and regulation of the private sector; and (iv) restrictions on foreign investment and influence of the economy. Salacuse considers that Development Model II stood in sharp contrast to Development Model I with the following chief features: (i) reliance on markets and private ordering; (ii) privatization; (iii) deregulation; and (iv) opening economies. According to Salacuse, the 1980s was the period for shifting of developing countries from Development Model I to Development Model II with plenty of consequences for the legal and regulatory policy-making of developing countries. It is the opinion of the said commentator that the main reasons for the switch from Development Model I to Development Model II were the following: (i) "Development Model I had quite simply failed to bring about development. By the 1980s, the economies of most developing countries were stagnant, burdened with enormous debt, and saddled with inefficient public enterprises requiring constant government subsidies"; (ii) "powerful external forces were insisting upon fundamental changes in Third World economic policies, often as a condition to financial and developmental assistance"; (iii) "the end of the communism in Eastern Europe and the Soviet Union in 1989 deprived many developing countries of sources of moral and material support for Development Model I"; (iv) "the successful example of certain high-growth Asian states which had avoided many of the elements of Model I, particularly its restrictions on foreign capital and private enterprise, also promoted a search for a new approach." See JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (n 10) 59-74. In this respect, see also T Wälde (n 10) 778-796. According to Herdegen, the following three were the principal reasons for the abandonment of the 'new international economic order' project by developing countries: (a) the quest for foreign investment as a vital factor for economic and social development; (b) collapse of most communist systems; (c) an ever-increasing number of bi- and multilateral investment treaties providing comprehensive protection of foreign investments. M Herdegen (n 14) 18. See also R Dolzer and C Schreuer, *Principles of International Investment Law* (OUP 2012) 5.

[36] JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (n 10) 58. See also T Wälde (n 11) 771. Already in 1997, even Sornarajah, one of the most determined supporters of the 'localisation theory', had felt the fading away of the efforts of the developing countries to localise foreign investment contracts. M Sornarajah, 'Power and Justice in Foreign Investment Arbitration' (n 10) 103, 139.

24. At the time when developing countries – formerly fond of the localisation theory – were desperately seeking to obtain foreign investment to restructure, and indeed rescue, their economies, these treaties were deemed as the holy grail for the attraction of foreign capital and technology.[37] The conclusion of such treaties by developing countries was also considered as a signal that the developing country concerned does not follow the classical 'Calvo' or 'localisation' theories any longer, and surely not strictly. Other external forces also prompted the conclusion of such treaties, including, *inter alia*, the requirement by export credit guarantee agencies of developed states and international financial institutions that, for insurance, for coverage to be granted to investments abroad or for loans to be granted, there should be or there should better be a bilateral investment treaty in place between the home and the host country.[38]
25. Whereas most of the developing countries welcomed the conclusion of such treaties for the reasons outlined above, it was the western capital-exporting world which invented and was the initiator and the driving force behind the conclusion of bilateral investment treaties.[39] In the eyes of the developed countries of West Europe and North America, these treaties were considered to safeguard foreign private investments on the basis of international law and to remove disputes arising from such investments from national courts' jurisdiction and the perceived yoke of local laws of the host state.[40] Indeed, in view of the developed countries, the greatest deficiency of rules of customary international law in the realm of foreign investment protection was that they did not accord western investors with an

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[37] Even the most resistant South American countries which were obsessed with the Calvo Doctrine started to conclude such agreements in the 1990s. For instance, Argentina concluded its first bilateral investment treaty on 22 May 1990 with Italy; Venezuela also concluded its first bilateral investment treaty with Italy one month later in June 1990; Peru concluded its first bilateral investment treaty with Thailand on 15 November 1991; Brazil concluded its first bilateral investment treaty with Portugal on 09 February 1994, and Colombia signed its first bilateral investment treaty with the United Kingdom on 09 March 1994.

[38] M Sornarajah, *The International Law on Foreign Investment* (n 22) 204-206; J Voss (n 14) 363, 372; JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (1990) 24(3) The International Lawyer 661; R Dolzer and M Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff Publishers 1995) 11-13 (saying that Germany and France link the availability of insurance from national investment guarantee schemes to the existence of a bilateral investment treaty); R Dolzer and C Schreuer (n 35) 5-6. In this respect, see also LS Poulsen, 'Political Risk Insurance and Bilateral Investment Treaties: A View from Below' (02 August 2010) Columbia FDI Perspectives. See <http://www.vcc.columbia.edu/content/political-risk-insurance-and-bilateral-investment-treaties-view-below.> 'accessed 31 May 2018'.

Dolzer and Stevens also explain that one reason for the emergence of bilateral investment treaties was that FCNs were not any longer appropriate to regulate the investor-state relations in the new decolonised world. See R Dolzer and M Stevens, *Bilateral Investment Treaties* (Martinus Nijhoff Publishers 1995) 10-11. See also, JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (n 10) 340, 344.

[39] See R Dolzer and M Stevens (n 38) 1-3; JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (n 38) 657-658; JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (n 10) 342 (all explaining the practice of the West European countries and the United States in concluding bilateral investment treaties in the post-World War II period). Sornarajah considers that the move for investment treaties was set off by developed countries in response to the calls for a 'New International Economic Order' made by developing states. Sornarajah, *The International Law on Foreign Investment* (n 22) 206.

[40] See J Voss (n 14) 363, 369; K Kunzer, 'Developing a Model Bilateral Investment Treaty' (1983) 15 Law & Policy of International Business 273, 292-293; JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (n 38) 659-661.

effective and binding mechanism for settlement of investment disputes. Thus, they tried to remedy and address this perceived defect by concluding bilateral investment treaties which after a while provided prospective state consent for a mechanism of the settlement of investment disputes between states and investors through international arbitration,[41] thus giving investors a direct right to bring claims against host states without needing an awkward diplomatic protection piggyback from their home government and, additionally, stripping local courts of the host state – which always tended to apply their own laws to investment disputes – of their jurisdiction to decide investment disputes,[42] thereby entangling developing countries in a self-induced 'internationalisation' situation.[43] In fact, this investor-state arbitration mechanism granted investors a privilege of direct recourse to

[41] In fact, in the early years of the conclusion of bilateral investment treaties, such agreements did not contain investor-state dispute settlement procedures. See R Dolzer and C Schreuer (n 35) 6-7 (referring to Article 11 of the 1959 BIT between Germany and Pakistan, and stating that at the time investment agreements did not contain investor-state dispute settlement clauses.) In fact, the very next bilateral investment agreement concluded by Germany with Malaysia did not also contain an investor-state dispute settlement mechanism. See Agreement between the Federal Republic of Germany and the Federation of Malaya Concerning the Promotion and Reciprocal Protection of Investments, signed on 22 December 1960, entered into force on 06 July 1963. Dolzer and Schreuer explain that it was with the treaty between Chad and Italy of 1969 that BITs began offering arbitration between host states and foreign investors. ibid 7.

[42] JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (n 38) 672-673; R Dolzer and C Schreuer (n 35) 235.

[43] Of course, this is not to suggest that such agreements did not provide for the jurisdiction of the national courts of the host state. To be sure, many of these agreements did contemplate the jurisdiction of the national courts of the host state as an option. For instance, Article 9(2) of the bilateral investment treaty between Egypt and Finland has given an investor as many as four (4) choices to select from for the settlement of its disputes with the host state, including opting for the courts of the host state. See Agreement between The Government of The Republic of Finland and The Government of The Arab Republic of Egypt on The Promotion and Protection of Investments, signed on 03 March 2004, entered into force on 05 February 2005. Investor's freedom to choose, however, signifies a natural preference for arbitration. As Dolzer and Schreuer explain:

> From the investor's perspective, this is not an attractive solution. Rightly or wrongly, the investor will fear a lack of impartiality from the courts of the state against which it wishes to pursue its claim. In many countries, an independent judiciary cannot be taken for granted and executive interventions in court proceedings or a sense of judicial loyalty to the forum state are likely to influence the outcome. This is particularly so where large amounts of money are involved. Not infrequently, legislation is the cause of complaints by investors. Domestic courts will often be bound to apply the local law even if it is at odds with international legal rules protecting the rights of investors. In fact, in some countries the relevant treaties may not even be part of the domestic legal order. At times, domestic courts may be the perpetrators of the alleged violation of investor rights […] Even where courts decide in the investor's favour, the executive may ignore their decisions.[…] In all these situations domestic courts cannot offer an effective remedy to foreign investors. [footnotes omitted]

See R Dolzer and C Schreuer (n 35) 235. See also C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (2005) 4(1) The Law & Practice of International Courts and Tribunals 1; C Schreuer, 'Interaction of International Tribunals and Domestic Courts in Investment Law' in Arthur W. Rovine (ed), *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (Martinus Nijhoff Publishers 2010) 71. Regarding some of the same points, namely, the alleged corruption of the courts of the host state and their alleged dependability, see CN Brower & S Blanchard, 'What's in a Meme? The Truth about Investor-State Arbitration: Why It Need Not, and Must Not, Be Repossessed by States' (2014) 52 Columbia Journal of Transnational Law 757.

arbitration without first having a contractually-agreed arbitration clause in place.[44] This granting of a procedural right to private persons to have direct recourse to international arbitration with respect to a wide range of investment protection issues was seen as a "dramatic extension of arbitral jurisdiction in the international realm".[45] In view of the late Thomas Wälde, from the lens of the investor, the advantage of accessing international arbitration which was supposed to unchain the investor from the yoke of the host state courts even trumps the application of international law to the investment dispute:

> It is the ability to access a tribunal outside the sway of the host State which is the principal advantage of a modem investment treaty. This advantage is much more significant than the applicability to the dispute of substantive international law rules. The remedy trumps in terms of practical effectiveness the definition of the right.[46]

26. Besides, to the best satisfaction of foreign investors, as will be discussed below, under the new regime of protection by bilateral investment treaties, the investors did not need to exhaust local remedies anymore in order to obtain international protection for their investments as the condition was removed under the new system of international investment protection.[47]
27. Bearing all these considerations in mind, even a commentator like Sornarajah, who is known to be always supportive of the localisation-related theories, concedes that when subject to bilateral investment treaties, international investment arrangements will slip out of the hands of domestic laws and will fall in the domain of international law:

> The proposition that a State contract falls within the domestic sovereignty of a host State may not hold valid where the investment made in pursuance of it is protected by a bilateral investment treaty or an international convention like the Convention on the Settlement of International Disputes [sic]. [48]

28. Thus, as a result of this significant development, it was presumed that the more these treaties were concluded, the more the role of the laws and the courts of the host state was diminished. Whereas by 1989, approximately only 300 bilateral investment treaties had

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[44] See J Paulsson, 'Arbitration without Privity' (1995) 10(2) ICSID Rev-FILJ 232; JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (n 10) 343.

[45] J Paulsson (n 44) 232-233.

[46] TW Wälde, 'The "Umbrella" Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases' (2005) 6(2) Journal of World Investment & Trade 183, 190. See also PB Stephan, 'International Investment Law and Municipal Law: Substitutes or Complements?' (2014) 9(4) CMLJ 355 (saying that: "What investors do not trust is not so much the governing law, but rather the institutions that will apply the law. Investors demand a more reliable dispute resolution process than the host state normally can provide.")

[47] In this Regard, see Chapter 7, Section One.

[48] M Sornarajah, 'The Climate of International Arbitration' (n 6) 47, 66, 81-86; VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (n 33) 275.

been concluded,[49] by September 1994 they more than doubled reaching the approximate number of 700,[50] at the end of 2008 the number of bilateral investment treaties amounted to 2608,[51] and reached the figure of 2,957 by the end of 2016.[52] This dense network of bilateral investment treaties connecting all the four corners of the world formed a very strong front of 'internationalisation', practically wiping out any possible remaining actual materialisation of the 'localisation' theory.

**Conclusion**

29. In short, the 'treatification'[53] of international investment law tended to elevate the mere domestic public and private law relationship between states and foreign investors to an international level where international law was expected to overtake the domestic law of the host state and was supposed to have the last say on all matters. Furthermore, under the recently designed scheme of bilateral investment treaties, international law was believed to be uttered principally by international arbitral tribunals not the courts of the recipient state.
30. Judge Brower, an arbitrator most frequently appointed by investors in the history of investment treaty arbitrations,[54] describes these developments as follows:

> Fortunately, the 'Southern' tsunami of NIEO and the Charter eventually abated. The subsequent conclusion of thousands of bilateral investment treaties, and, more recently, several multilateral investment treaties, in which States record their true, practical interests, have replaced the 'soapbox' Resolutions of the General Assembly. The landmark arbitral award of Professor Rene-Jean Dupuy in the case of Texaco Overseas Petroleum Company and California Asiatic Petroleum Company v Libya issued 19 January 1977 soon established definitively that neither the NIEO nor the succeeding Charter constituted international law, in part precisely because of the aforementioned votes against the Charter and abstentions by industrialized States […] In due course the late Professor Thomas Waelde declared 'A Requiem for the "New International Economic Order": The Rise and Fall of Paradigms in International Economic Law'… Thus was 'the South' defeated and both international law and peaceful

[49] JW Salacuse, 'BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries' (n 38) 655.

[50] R Dolzer and M Stevens (n 38) 1.

[51] UNCTAD, *World Investment Report 2008: Transnational Corporations and the Infrastructure Challenge*, U.N. Doc. UNCTADIWIR/2008 (United Nations 2008) 14.

[52] UNCTAD, *World Investment Report 2017: Investment and the Digital Economy*, U.N. Doc. UNCTAD/WIR/2017 (United Nations 2017) 111.

[53] The term 'treatification' in this context has been devised by Salacuse. JW Salacuse, 'The Treatification of International Investment' (2007) Law and Business Review of the Americas 155. See also JW Salacuse, *The Three Laws of International Investment: National, Contractual, and International Framework for Foreign Capital* (n 10) 331-332.

[54] See <http://investmentpolicyhub.unctad.org/ISDS/FilterByArbitrators> 'accessed 31 May 2018'.

> investor–State dispute settlement through international arbitration restored, indeed enhanced.[55] [Footnotes omitted]

31. With what is said so far, it might strike any reasonable bystander that the 'localisation' theory was totally wiped out and its story finishes here. However, as was already foreshadowed in Chapters 1-4, considering the current status of investment treaty law, domestic law of the host state plays a prominent role in determining the threshold question of jurisdiction *ratione materiae* of an investment treaty tribunal. In addition, as will be seen more fully in Chapters 6 and 7, the developments in investment treaty law manifest a broader role for domestic laws and national courts of the host state in investment treaty arbitrations. When one considers the discussions in Chapters 1-4 regarding the role of host state law in subject-matter jurisdiction and then bears in mind the recent developments in investment treaty law concerning the broader role of domestic law and national courts in investor-state arbitrations (discussed in Chapters 6 and 7), one may not be blamed for thinking that the 'localisation' theory has been revived to some extent. In fact, it is pursuant to the analysis conducted in Chapters 6 and 7 that I argue that the 'localisation' theory has resurfaced in the field of investment treaty arbitration to some extent.

[55] CN Brower & S Melikian, ''We Have Met The Enemy And He Is US!' Is the Industrialized North 'Going South' on Investor–State Arbitration?' (2015) 31(1) Arb Int'l 22. In the words of the *Antoine Goetz* tribunal, the emergence of bilateral investment treaties revived the role of international law in international investment disputes:

> It may be interesting to remark on this subject that choice of law clauses in investment protection treaties frequently refer to the provisions of the treaty itself, and, more broadly, to international law principles and rules. This leads to a remarkable comeback of international law, after a decline in practice and jurisprudence, in the legal relations between host States and foreign investors.

*Antoine Goetz et consorts v. République du Burundi*, ICSID Case No. ARB/95/3, Award, 10 February 1999 [20].

## Chapter 6: Partial Revival of the Localisation Theory in the Field of Investment Treaty Arbitration: The Current Role of Host State Law

### Introduction

1. As it was shown in the previous Chapter, the 'localisation' theory rested on two pillars: first, the laws of the host state govern the substance of foreign investment dispute, and, second, only the courts of the host state are competent to decide cases filed pursuant to foreign investment contracts. Chapter 5 also recalled the destiny of the 'localisation' theory and reviewed what befell this theory, in particular, in the wake of the conclusion of a tremendous number of investment treaties containing arbitration clauses giving investors direct access to international arbitration against the receiving state. It was discussed in Chapter 5 that, as a result of the developments in international investment law, it was common ground in the 1990s that the 'localisation' theory had ceased to exist and did not have any practical effect.
2. Be that as it may, I demonstrated in Chapters 1-4 that the domestic law of the host state does have a significant role in determining a number of critical issues in an investment treaty arbitration, notably matters concerning the jurisdiction *ratione materiae* of an investment treaty tribunal. What I have not shown yet is the trend towards the inclination to the local law in investment treaty law in the course of time. I do not say that the laws of the host state had a determinative role in investment treaty cases from the very beginning of investment treaty case law. Rather, the argument is that this role was gradually attained by the municipal law through developments in treaty rulemaking and investment treaty arbitration jurisprudence.
3. Chapter 6 is entrusted with the task of distilling the in-depth discussions of Chapters 1 to 4 of this Thesis, followed by a brief consideration of the shift in the approach of investment treaty rulemaking and investment treaty arbitration practice towards the role of the laws of the host state in the field of investment treaty arbitration, thereby, outlining the overall impact of the laws of the host state on the outcome of investment treaty cases in light of the recent developments in investment treaty law. Thus, this Chapter will briefly show that the laws of the host state have obtained such a prominent role in investment treaty arbitrations in the course of time that one can consider the rematerialisation of the effects of the 'localisation' theory in the arena of investment treaty arbitration.

### Section One: A Distillation of Chapters 1-3 Regarding the Role of the Domestic Law of the Host State in Determining the Jurisdiction *ratione materiae* of An Investment Treaty Tribunal

4. As was discussed in Chapter 1, there are several jurisdictional and substantive situations in an investment treaty arbitration in which the laws of the host state are determinative as 'law'. In particular, as delineated in Chapters 2 and 3, as far as the all-important issue of *ratione materiae* jurisdiction is concerned, the domestic laws of the host state have a significant role in several respects: (i) a majority of investment treaties provide that investments should be made in accordance with the laws of the host state.[1] The inclusion of the legality requirement in investment treaties got momentum gradually. In earlier BITs,

[1] See, for instance, Article 1(1) of the Agreement between the Government of the Kingdom of Sweden and the Government of the Republic of Kazakhstan on the Promotion and Reciprocal Protection of Investments, signed on 25 October 2004, entered into force on 01 August 2006.

the requirement that investments should be made in accordance with the laws of the host state was not expressly stated.[2] However, as time went by, more BITs began to include the legality requirement within their provisions.[3] Relying on these provisions, investment treaty tribunals have dismissed jurisdiction with regard to illegal investments. (ii) in most instances, the creation and existence of property rights underlying investment should be determined by reference to the laws of the host state.[4] [5]

5. This brief distillation of the discussions in Chapters 1-4 of this Thesis clearly manifests the reality that the local laws of the host state have regained some control in the arena of international investment law and have done so step by step. This progressive reassertion of the role of the internal laws of the receiving states is owed to two factors: first, in more recent years, states have started to leave more areas (jurisdictional or otherwise) in the hands of domestic law when they conclude investment treaties (investment treaty rulemaking), and, second, investment treaty tribunals have been granting a more prominent role to the laws of the host state in the resolution of investment treaty disputes (investment treaty arbitration practice). Coupled together, these two factors have given a firmer stance to the laws of the host state in the resolution of investment treaty disputes.

**Section Two: Developments in Investment Treaty Law Regarding the Role of Host State Law in the Resolution of Investment Treaty Arbitration Cases**

6. To begin with the new trends in investment treaty rulemaking, in order to really see the difference between previous practice and current practice, it is useful to make a comparison between states' older and newer model BITs. Although some states have not updated their model BITs, many have done so. The difference between the two model BITs manifests the difference in the approach to the role of host state law in a crystal-clear manner. To have a better picture, in the following paragraphs, I am going to raise the example of one

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[2] See, for instance, the Treaty between the Federal Republic of Germany and Pakistan for the Promotion and Protection of Investments, signed on 25 November 1959, entered into force on 28 April 1962; the Protocol between the Governments of the State of Kuwait and the Republic of Iraq on the Promotion of the Movement of Capital and Investments between the Two Countries, signed on 25 October 1964, entered into force on 07 June 1966; the Netherlands and Indonesia: Agreement on Economic Cooperation, signed on 07 July 1968, entered into force on 17 July 1971.

[3] See, for instance, Article 1(1) of the Agreement between the Republic of Austria and the State of Kuwait for the Encouragement and Reciprocal Protection of Investments, signed on 16 November 1996, entered into force on 22 September 1998; Article 1(1)(a) of the Agreement between Australia and the Islamic Republic of Pakistan on the Promotion and Protection of Investments, signed on 07 February 1998, entered into force on 14 October 1998; The Agreement between the Government of the Republic of Croatia and the Government of the Republic of Indonesia on the Promotion and Protection of Investments, signed on 10 September 2002, not yet entered into force.

[4] See Chapter 3, Section One.

[5] Furthermore, according to certain investment treaties, only investments will be protected which are approved by the competent authorities of the host state in accordance with their laws and regulations. See, for instance, Article 3(2) of the Agreement between Japan and the Islamic Republic of Iran on Reciprocal Promotion and Protection of Investment between Iran and Japan, signed on 05 February 2016, entered into force on 26 April 2017. Although the approval requirement did not usually show up in earlier investment treaties, in more recent years, one can see that this requirement is more frequently referred to by certain countries. See, for example, Article 2 of the Agreement between the Government of the Kingdom of Thailand and the Belgo-Luxemburg Economic Union on the Reciprocal Promotion and Protection of Investments, signed on 12 June 2002, entered into force on 19 September 2004; Article 10 of the Agreement on the Promotion and Reciprocal Protection of Investments between the Kingdom of Spain and the Islamic Republic of Iran, signed on 29 October 2002, entered into force on 13 July 2004.

developing country, namely India, and one developed country, namely, the Netherlands, and compare the contents of their older Model BITs with their latest Model BITs from the prism of the role of the municipal law of the host state in investment treaty law.

7. Beginning with the first example, i.e., India, the comparison is between the 2003 and 2015 Model BITs adopted by India. It should be borne in mind that the 2003 Indian Model BIT already had many references to host state law, e.g. with respect to the legality requirement. However, when one reads the 2015 version, one sees far more references to domestic law. Whereas the preamble of the 2003 Indian Model BIT makes no reference to domestic law, the preamble of the 2015 model reaffirms "the right of Parties to regulate investments in their territory in accordance with their law and policy objectives." Furthermore, it is notable that unlike the 2003 version, the 2015 Model BIT of India includes a comprehensive definition of the term 'law' in Article 1.6: ""law" includes: (i) the Constitution, legislation, subordinate/delegated legislation, laws & bylaws, rules & regulations, ordinance, notifications, policies, guidelines, procedures, administrative measures/executive actions at all levels of government, as amended, interpreted or modified from time to time; (ii) decisions, judgments, orders and decrees by Courts, regulatory authorities, judicial and administrative institutions having the force of law within the territory of a Party." There is also a definition of the term 'measure' in Article 1.8 which includes: "a law, regulation, rule, procedure, decision, administrative action, requirement or practice." Furthermore, Article 1.11 of the 2015 Model BIT also defines the term 'Pre-investment activity' and stipulates that such activity must be carried out in accordance with host state law.[6] Further expanding the trespassing role of the domestic laws of the host state, Article 2.4 of the 2015 Model BIT indicates that the Treaty does not apply to, *inter alia*: "any law or measure regarding taxation, including measures taken to enforce taxation obligations." Unlike, this broad limitation in the 2015 Model BIT, this limitation is confined to national treatment and most-favoured-nation treatment in the 2003 Model BIT (Article 3(3)(b)). In addition, the footnote to Article 5.1 of the 2015 Model BIT (enumerating the conditions for a lawful expropriation, including the condition of 'public purpose'), indicates that when India is the expropriating party, and the subject of expropriation is land, "any measure of expropriation relating to land shall be for the purposes as set out in its Law relating to land acquisition and any questions as to "public purpose" and compensation shall be determined in accordance with the procedure specified in such Law." Besides, Article 6(1) of the 2015 Model subjects the obligation to allow transfers of funds to the laws of the host state. On the same point, Article 6.3 enumerates various exceptions to the obligation of allowing the transfer of funds based on the legal and regulatory measures and policies of the host state. Another notable development in the 2015 Model is that although the draft treaty contains various express and implicit legality requirements, Article 11, entitled "Compliance with laws", records the agreement of the Contracting Parties that: "(i) Investors and their investments shall comply with all laws, regulations, administrative guidelines and policies of a Party concerning the establishment, acquisition, management, operation and disposition of investments … (iii) Investors and their investments shall comply with the

[6] "The term "Pre-investment activity" includes any activities undertaken by the investor or its enterprise prior to the establishment of the investment in accordance with the law of the Party where the investment is made. Any activity undertaken by the investor or its investment pursuant to compliance with sectoral limitations on foreign equity, and other limits and conditions applicable under any law relating to the admission of investments in the Party where the investment is made in specific sectors falls within the meaning of "Preinvestment activity"."

provisions of law of the Parties concerning taxation, including timely payment of their tax liabilities." A final notable insertion of domestic law in the latest version is the exclusion in Article 32.1(iii) of the adoption or enforcement by a Party of measures of general applicability applied on a nondiscriminatory basis that are necessary to ensure compliance with law and regulations that are not inconsistent with the provisions of the Agreement from the scope of the BIT. As one can see, when comparing the two Model BITs, the law of the host state has been given a much more expansive role in the more recent Model BIT, i.e., Indian Model BIT 2015.

8. Another noteworthy comparison could be made between the 2004 Netherlands Model BIT and the 2018 Netherlands Model BIT. Whereas the former Model did not contain an express legality requirement, Article 2(1) of the 2018 Model reads: "This Agreement shall apply to an investment, made in accordance with the applicable law of the host Contracting Party at the time the investment is made …" Along the same lines, and as another outstanding development, Article 7(1) of the 2018 Model BIT reads: "Investors and their investments shall comply with domestic laws and regulations of the host state, including laws and regulations on human rights, environmental protection and labor laws." Furthermore, as per Article 10(2) of the 2018 version, the recipient state has been given a margin of discretion to ensure compliance with its tax laws: "Nothing in this Agreement shall be construed to prevent a Party from adopting or maintaining any taxation measure aimed at preventing the avoidance or evasion of taxes pursuant to its tax laws or its agreements for the avoidance of double taxation." In addition, Article 11(3) of the 2018 Model BIT on the duty to allow the free transfer of funds, allows the host state to adopt certain measures for safeguarding its laws with respect to certain public purpose matters without taking such measures to be considered as violating the BIT. In short, as one can see, there are many more references to host state law in the newer model in contrast to the references to host state law in the previous Dutch Model BIT. When compared to the Indian Model BIT of 2015, although references to domestic law are understandably less in the 2018 Model BIT of the Netherlands, the fact that even the Netherlands, as a country which has never been a respondent in an investment treaty case so far, has felt the need to give host state law more relevance in its bilateral investment treaties is telling as to the overall approach of state practice regarding the role of host state law in the field of investment treaty law.
9. What these two case-studies simply show is that with the passing of time, states include more references to host state law in investment treaties with regard to both jurisdictional and liability matters. In fact, as these developments show, not only laws of the host state are more expressly mentioned to be determinative with respect to jurisdictional questions (like the legality requirement) but also state contracting parties to international investment agreements have shown a tendency to give some role to host state law in matters of liability by envisaging certain actions taken in accordance with host state laws as exceptions to treaty violations under certain peculiar circumstances.
10. Turning to the second factor, i.e., the shift in the investment treaty arbitration practice towards the role of host state law in investment treaty arbitrations, as was noted in Chapters 1 to 3, in recent years, many investment treaty arbitration tribunals have effectively and actually applied the laws of the host state to certain threshold jurisdictional matters like the creation and existence of rights or the legality requirement. This was not the practice in earlier investment treaty cases. In *Pope & Talbot Inc. v. Canada*, the tribunal had to decide

whether the alleged right of access to the US market was an investment protected by NAFTA and whether such an alleged investment was expropriated by Canada. Although the tribunal ultimately rejected the claimant's expropriation case on its merits, it had, as a preliminary point, accepted that the alleged right asserted by the claimant constituted an investment for the purposes of Article 1110 of NAFTA. Without engaging the domestic law of the host state, the tribunal found in general terms that: "true interests at stake are the Investment's asset base, the value of which is largely dependent on its export business".[7] As is plain from the foregoing quotation, the tribunal did not examine the alleged interest at issue from a legal prism and, as such, did not get itself into analysing the applicable municipal law of the host state. Rather, by alluding to the term 'true interests at stake', it approached the issue from a commercial perspective which does not seem to be the right way of dealing with this legal matter. This Interim Award dates back to 2000. Similarly, in a Partial Award rendered in 2005 in *Eureko v. Poland*, the majority of the investment treaty tribunal failed to appreciate the role of the host state law (laws of Poland) in determining the alleged contractual rights at stake and, instead, affirmed the existence of such alleged entitlements in an abstract manner divorced from any analysis of any internal law.[8]

11. In comparison, starting from 2003, beginning with the decision of the *Nagel* tribunal, investment treaty tribunals have gradually become more vocal regarding the role of domestic law of the host state in its 'law' cloak in the determination of the underlying legal rights and interests in investment treaty arbitrations.[9] In addition, other investment treaty tribunals have paid due regard to the laws of the host state in determining matters concerning the legality requirements and have made decisions and dismissed investment treaty cases based on those very laws.[10] That is while in the beginning, reference to host state law for dismissing an investment treaty case on the ground of illegality was done half-heartedly and without explicit reference to the specific laws of the host state.[11] Bearing in mind this shift in the jurisprudence, one can plainly consider the existence of an 'established trend' regarding the application of domestic law in the defined matters of *ratione materiae* jurisdiction.

**Conclusion**

12. As can be seen, although BITs came to wipe out all the traces of the 'localisation' theory, as time went by, states began to customise bilateral investment treaties in a way that would

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[7] *Pope & Talbot Inc. v. The Government of Canada*, UNCITRAL, Interim Award, 26 June 2000 [98].

[8] *Eureko B.V. v. Republic of Poland*, UNCITRAL, Partial Award, 19 August 2005 [240]-[243].

[9] See, for instance, *William Nagel v. The Czech Republic*, SCC Case No. 049/2002, Final Award, 09 September 2003; *Generation Ukraine, Inc. v. Ukraine*, ICSID Case No. ARB/00/9, Award, 16 September 2003; *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL *(formerly EnCana Corporation v. Government of the Republic of Ecuador)*, Award, 03 February 2006; *Emmis International Holding, B.V., Emmis Radio Operating, B.V., MEM Magyar Electronic Media Kereskedelmi és Szolgáltató Kft. v. The Republic of Hungary*, ICSID Case No. ARB/12/2, Award, 16 April 2014; *Accession Mezzanine Capital L.P. and Danubius Kereskedöház Vagyonkezelö Zrt. v. Hungary*, ICSID Case No. ARB/12/3, Award, 17 April 2015.

[10] See, for instance, *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Award, 16 August 2007; *Alasdair Ross Anderson et al. v. Republic of Costa Rica*, ICSID Case No. ARB (AF)/07/3, Award, 19 May 2010; *Metal-Tech Ltd. v. Republic of Uzbekistan*, ICSID Case No. ARB/10/3, Award, 04 October 2013.

[11] See, e.g., *Inceysa Vallisoletana S.L. v. Republic of El Salvador*, ICSID Case No. ARB/03/26, Award, 02 August 2006.

revive the ‘localisation’ theory to a certain extent and with respect to certain outcome-determinative matters. As can be seen from the analysis conducted in this Chapter and in Part I of this Thesis, states, in particular, in more recent years, have hinged certain threshold jurisdictional matters to the determinations of host state law. In addition, state contracting parties to international investment agreements have shown a tendency to give some role to host state law in matters of liability by envisaging certain actions taken in accordance with host state laws as exceptions to treaty violations under certain peculiar circumstances. Furthermore, in the course of time, investment treaty tribunals also started appreciating the role of host state law in determining issues concerning subject-matter jurisdiction, thereby, reviving the function of these laws in the resolution of investment treaty cases to a certain extent.

13. However, as was alluded to above, this is only one side of the coin. The other pillar of the ‘localisation’ theory was that the court of the host state was the only competent forum for the settlement of investment disputes. This role was overtaken by the advent of bilateral investment treaties and was given away to international arbitration. It seems, however, that, like the laws of the host state, courts of the host state are also reoccupying some of their lost posts.

## Chapter 7: Partial Revival of the Localisation Theory in the Field of Investment Treaty Arbitration: The Current Role of Host State Courts

### Introduction

1. A complete appraisal of the revival of the 'localisation' theory will not be possible without analysing the relevance of the courts of the host state and their findings in investment treaty arbitrations. Therefore, it is necessary to go through a critical and thorough appraisal of the contributions that the national courts and tribunals of capital-importing countries currently make to a given investment treaty arbitration proceeding. The discussion considers the latest approaches and trends in investment treaty rulemaking and investment treaty arbitration jurisprudence as to the role that is assigned to the courts of the host state in the resolution of investment treaty disputes. Specifically, this Chapter seeks to track the most recent developments in the apparently endless competition between arbitration and national courts in the arena of deciding international investment disputes.

2. As was explained above, one significant *raison d'être* for devising bilateral investment treaties was the avoidance of the intervention of the local courts of the host state in the settlement of investment disputes between investors and the host state and its emanations.[1] Therefore, apart from the inclusion of investor-state arbitration dispute-settlement apparatus in almost all of the modern bilateral investment treaties,[2] which is naturally the preferred option for foreign investors for the resolution of their investment treaty disputes with recipient states,[3] mechanisms were devised in investment treaties as well as in the ICSID Convention to militate against the interference by the national courts of the recipient state in the investment treaty dispute-settlement procedure, including the elimination of the

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[1] C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (2005) 4(1) The Law & Practice of International Courts and Tribunals 1; TW Wälde, 'The "Umbrella" Clause in Investment Arbitration: A Comment on Original Intentions and Recent Cases' (2005) 6(2) Journal of World Investment & Trade 183, 190.

[2] Of course, as mentioned above, earlier bilateral investment treaties lacked the possibility of referring investment disputes to international arbitrations. However, the mood changed towards the late 1960s and early 1970s. See Chapter 5, fn 41 and the accompanying text.

[3] Dolzer and Schreuer believe that, for various reasons, the courts of the host state do not usually serve as a viable option for investors for the settlement of their disputes with host states:

> From the investor's perspective, this is not an attractive solution. Rightly or wrongly, the investor will fear a lack of impartiality from the courts of the state against which it wishes to pursue its claim. In many countries, an independent judiciary cannot be taken for granted and executive interventions in court proceedings or a sense of judicial loyalty to the forum state are likely to influence the outcome. This is particularly so where large amounts of money are involved.
>
> Not infrequently, legislation is the cause of complaints by investors. Domestic courts will often be bound to apply the local law even if it is at odds with international legal rules protecting the rights of investors. In fact, in some countries the relevant treaties may not even be part of the domestic legal order. At times, domestic courts may be the perpetrators of the alleged violation of investor rights. […] Even where courts decide in the investor's favour, the executive may ignore their decisions. […] In all these situations domestic courts cannot offer an effective remedy to foreign investors.

Dolzer and Schreuer, *Principles of International Investment Law* (OUP 2012) 235.

requirement of the exhaustion of local remedies[4] which is a pre-condition of Diplomatic Protection[5] and bringing disputes before the ECtHR.[6] In this respect, Article 26 of the ICSID Convention provides that: "Consent of the parties to arbitration under this Convention shall, unless otherwise stated, be deemed consent to such arbitration to the exclusion of any other remedy. A Contracting State may require the exhaustion of local administrative or judicial remedies as a condition of its consent to arbitration under this Convention." Pursuant to this provision, unless otherwise agreed between the parties, local remedies do not need to be exhausted before referring the case to arbitration. Consequently, when a bilateral investment treaty lacks any reference to the requirement of the exhaustion of the local remedies as a prerequisite to consent to arbitration – which is the case in most instances[7] – the investor does not need to exhaust local remedies before filing its request

[4] Dolzer and Schreuer (n 3) 264-267.

[5] See Article 14 of the ILC Draft Articles on Diplomatic Protection (2006) with the heading of "Exhaustion of local remedies" which provides:

> 1. A State may not present an international claim in respect of an injury to a national or other person referred to in draft article 8 before the injured person has, subject to draft article 15, exhausted all local remedies.
>
> 2. "Local remedies" means legal remedies which are open to an injured person before the judicial or administrative courts or bodies, whether ordinary or special, of the State alleged to be responsible for causing the injury.
>
> 3. Local remedies shall be exhausted where an international claim, or request for a declaratory judgement related to the claim, is brought preponderantly on the basis of an injury to a national or other person referred to in draft article 8.

[6] Article 35(1) of the European Convention on Human Rights entitled "Admissibility criteria" reads: "The Court may only deal with the matter after all domestic remedies have been exhausted, according to the generally recognised rules of international law, and within a period of six months from the date on which the final decision was taken."

[7] Only a scant number of bilateral investment treaties expressly provide for the requirement of the exhaustion of local remedies before submitting the dispute to arbitration. See, for instance, Article 9 of the Agreement between the Government of the People's Republic of China and the Government of the Republic of Cote D'Ivoire on the Promotion and Protection of Investments, signed on 30 September 2002, not yet entered into force. According to Schreuer, only a few, mostly older bilateral investment treaties, refer to the requirement of exhaustion of local remedies. See C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (n 1) 2. See also C Schreuer, 'Interaction of International Tribunals and Domestic Courts in Investment Law' in Arthur W. Rovine (ed), *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (Martinus Nijhoff Publishers 2010) 73 (referring to Article 7 of the Agreement on the Mutual Promotion and Guarantee of Investments between Romania and Sri Lanka, signed on 09 February 1981, entered into force on 03 June 1982).

On the other hand, a thorough study carried out by UNCTAD also enumerates some of the more recent bilateral investment treaties which expressly *exclude* the exhaustion of local remedies rule. See UNCTAD, *Bilateral Investment Treaties 1995-2006: Trends in Investment Rulemaking* (United Nations 2007) 107-108 (referring to Article 10 of the Agreement between the Republic of Austria and the United Arab Emirates for the Promotion and Protection of Investments, signed on 17 June 2001, entered into force on 01 December 2003; Article 10 of the Agreement between the Government of the Republic of Croatia and the Government of the Kingdom of Cambodia on the Promotion and Reciprocal Protection of Investments, signed on 18 May 2001, entered into force on 15 June 2002).

for arbitration.[8] Investment treaty practice in ICSID arbitrations confirms this proposition.[9] The situation is no different in non-ICSID arbitrations (e.g. *ad hoc* arbitration under UNCITRAL Rules, arbitration under ICSID Additional Facility Rules, or arbitration administered by the ICC or the Stockholm Chamber of Commerce).[10] Indeed, as the SCC tribunal in *Rosinvest v. Russian Federation* has observed, "[s]o far as it is necessary to do so[,] the consent to investor-state arbitration, as explained, amounts to a waiver of the principle of exhaustion of local remedies. By choosing international arbitration to settle third party investment arbitration disputes[,] the principle of exhaustion of national legal remedies is excluded."[11]

3. However, this is not the end of the story. In fact, although the courts of the host state are not the prime venues for the resolution of investment treaty disputes, and although the early intervention of such courts through the exhaustion of local remedies rule has been thwarted by the advent of bilateral investment treaties, the ICSID Convention, and the practice of investment treaty tribunals, the courts of the host state, nevertheless, remain critical actors in the process of investment treaty dispute settlement in certain instances. With the more recent developments in investment treaty law, it is arguable that the role and the function of such courts in the process of investment treaty dispute settlement has become even more outstanding. Indeed, the courts and tribunals of the host state interfere with or even have an outcome-determining role in investment treaty arbitrations in matters of jurisdiction, admissibility, and merits. This is either as a result of express provisions in the relevant bilateral or multilateral investment treaty or the jurisprudence of international courts and/or tribunals (including investment treaty arbitrations), or a combination of the two factors mentioned here. The functions of the courts of the host state in investment treaty arbitrations will be analysed below.
4. Apart from the normal host state court interventions in international arbitrations, the courts of the host state can also influence the process of investment treaty arbitration in a number of distinct ways. There are four (4) types of such interventions by the courts of the host

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[8] For the interpretation of Article 26 of the ICSID Convention, see C Schreuer, L Malintoppi, A Reinisch & A Sinclair, *The ICSID Convention: A Commentary* (CUP 2009) 348-413. See also C McLachlan, L Shore & Matthew Weiniger, *International Investment Arbitration: Substantive Principles* (OUP 2017) 105, 152-153.

[9] See, e.g., *Amco Asia Corporation and others v. Republic of Indonesia*, ICSID Case No. ARB/81/1, *Ad hoc* Committee Decision on the Application for Annulment, 16 May 1986 [63]; *Lanco International Inc. v. The Argentine Republic*, ICSID Case No. ARB/97/6, Preliminary Decision: Jurisdiction of the Arbitral Tribunal, 08 December 1998 [39]-[40]; *Generation Ukraine, Inc. v. Ukraine*, ICSID Case No. ARB/00/9, Award, 16 September 2003 [13.1]-[13.6]; *IBM World Trade Corporation v. República del Ecuador*, ICSID Case No. ARB/02/10, Decision on Jurisdiction and Competence, 22 December 2003 [80]; *AES Corporation v. The Argentine Republic*, ICSID Case No. ARB/02/17, Decision on Jurisdiction, 26 April 2005 [69]-[70]; *Saipem S.p.A. v. The Peoples Republic of Bangladesh*, ICSID Case No. ARB/05/07, Award, 30 June 2009 [174]-[184]; *Helnan International Hotels A/S v. Arab Republic of Egypt*, ICSID Case No. ARB/05/19, Decision of the *Ad hoc* Committee on Annulment, 14 June 2010 [9], [28]-[57].

[10] See, for instance, *CME Czech Republic B.V. v. The Czech Republic*, UNCITRAL, Final Award, 14 March 2003 [412]; *Yaung Chi Oo Trading Pte. Ltd. v. Government of the Union of Myanmar*, ASEAN I.D. Case No. ARB/01/1, Award, 31 March 2003 [40]; *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Award, 26 June 2003 [142 *et seq*]; *Nykomb Synergetics Technology Holding AB v. The Republic of Latvia*, SCC, Arbitral Award, 16 December 2003, Section 2.4; *Mytilineos Holdings SA v. The State Union of Serbia & Montenegro and Republic of Serbia*, UNCITRAL, Partial Award on Jurisdiction, 08 September 2006 [197]-[225]; *RosInvestCo UK Ltd. v. The Russian Federation*, SCC Case No. V079/2005, Award on Jurisdiction, October 2007 [153]. See also Z Douglas, *The International Law of Investment Claims* (CUP 2009) 98-99.

[11] *RosInvestCo UK Ltd. v. The Russian Federation* (n 10) [153].

state in the process of investment treaty dispute settlement: (A) the requirement to use local remedies for a defined period of time as a precondition of filing the case before international arbitration; (B) the requirement to refer to the local remedies as a condition precedent of the establishment of a breach of the investment treaty substantive standards; (C) the requirement to refer to the holdings of domestic courts as a means of clarifying the meaning, interpretation, and application of disputed points of host state law; and (D) the requirement to refer to the courts of the host state as a competent forum to resolve matters in dispute in an investment treaty case. These four (4) types of functions by the courts of the host state in investment treaty disputes will be considered in turn below.

## A. The Requirement of Using Local Remedies for A Defined Period of Time As A Precondition of Filing the Case before International Investment Arbitration

5. Courts of the host state impact upon the process of international investment arbitration pursuant to a clause in certain investment treaties which generally looks like an exhaustion of local remedies requirement but is actually different. This requirement is the precondition to use domestic remedies for a certain period of time before the initiation of international investment arbitration.[12] The difference between the two requirements is that in the exhaustion of local remedies requirement scenario, unless circumstances prescribe otherwise, the investor has to go through all the stages of the court system of the host state before filing its dispute in arbitration, whereas in the scenario of the requirement to use domestic remedies for a certain period of time, the investor is free to resort to arbitration once the prescribed time has elapsed. Indeed, by virtue of such a requirement, the investor does not need to wait for a final or non-appealable decision of the courts of the host state.[13] Furthermore, unlike customary international law rule of exhaustion of local remedies, this requirement is applicable in an investment treaty arbitration only when expressly provided by the underlying investment treaty.[14]
6. As mentioned above, pursuant to such a requirement, an investor can bring a dispute before an international arbitral tribunal only once it has sought resolution of its disputes before the domestic courts of the host state for a determined period of time. The aggrieved investor may bring its case before an international arbitral panel if the internal proceedings before the national courts of the host state do not result in the settlement of disputes in the defined period of time or if despite the rendition of a decision by the courts of the host state the

[12] This requirement is ironically labelled by one eminent commentator and practitioner as one of the 'grandchildren' of the Calvo Doctrine. C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (n 1). For a similar labelling of akin requirements, see M Sornarajah, 'Power and Justice in Foreign Investment Arbitration' (1997) 14(3) J Int'l Arb 103, 137-138.

[13] See *Emilio Agustín Maffezini v. The Kingdom of Spain*, ICSID Case No. ARB/97/7, Decision of the Tribunal on Objections to Jurisdiction, 25 January 2000 [28]; *Siemens A.G. v. The Argentine Republic*, ICSID Case No. ARB/02/8, Decision on Jurisdiction, 03 August 2004 [104]; *Gas Natural SDG, S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/10, Decision of the Tribunal on Preliminary Questions on Jurisdiction, 17 June 2005 [30]; C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (n 1) 3; U Kriebaum, 'Local Remedies and the Standards for the Protection of Foreign Investment' in C Binder, U Kriebaum, A Reinisch & S Wittich, *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer* (OUP 2009) 420.

[14] B Demirkol, *Judicial Acts and Investment Treaty Arbitration* (CUP 2018) 80.

dispute persists.[15] For instance, Article 8 of the bilateral investment treaty between Argentina and the United Kingdom provides:

> (1) Disputes with regard to an investment which arise within the terms of this Agreement between an investor of one Contracting Party and the other Contracting Party, which have not been amicably settled shall be submitted, at the request of one of the Parties to the dispute, to the decision of the competent tribunal of the Contracting Party in whose territory the investment was made.
> (2) The aforementioned disputes shall be submitted to international arbitration in the following cases:
> (a) if one of the Parties so requests, in any of the following circumstances:
> (i) where, after a period of eighteen months has elapsed from the moment when the dispute was submitted to the competent tribunal of the Contracting Party in whose territory the investment was made, the said tribunal has not given its final decision;
> (ii) where the final decision of the aforementioned tribunal has been made but the Parties are still in dispute;
> (b) where the Contracting Party and the investor of the other Contracting Party have so agreed.
> […][16]

7. A plain reading of this provision would lead one to conclude that, unless the parties have agreed otherwise, initial recourse must be made to the local remedies for a period of eighteen (18) months before the investor can submit its case to international arbitration. If this process is not followed, the arbitration panel would either not have jurisdiction to hear the case or the case would be declared inadmissible due to a procedural shortcoming.[17]
8. That said, one should bear in mind that in earlier investment treaty arbitrations, where a treaty did refer to such requirements, investment treaty arbitration tribunals did not seem to pay heed to such stipulations.[18] In cases where this requirement was expressly included

[15] C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (n 1) 5; C Schreuer, 'Interaction of International Tribunals and Domestic Courts in Investment Law' (n 7) 73.

[16] Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments, signed on 11 December 1990, entered into force on 19 February 1993.

[17] Of course, different investment treaties use different timespans for the preliminary recourse to the courts of the host state. For instance, the agreement between Botswana and Belgium-Luxembourg determines the recourse to the local remedies to be for a timeframe of six (6) months. See Article 12 of the Agreement between the Belgium-Luxembourg Economic Union, on the One Hand and the Republic Of Botswana, on the Other Hand, on the Reciprocal Promotion and Protection of Investments, signed on 07 June 2006, not yet entered into force. As per Article VII of the Agreement between the Republic of Turkey and Turkmenistan Concerning the Reciprocal Promotion and Protection of Investments, signed on 02 May 1992, entered into force on 13 March 1997, the local remedies shall be used for a period of one (1) year before commencing arbitration.

[18] As will be seen below, however, the situation in investment treaty arbitrations seems to have changed in more recent years with investment treaty arbitral tribunals giving effect to such stipulated requirements.

in the underlying investment treaty,[19] the application of this provision was either avoided by investment treaty tribunals by reference to the MFN Clause of the relevant investment treaty[20] or done away by invoking the principle of 'futility' or other similar grounds.[21]

9. Indeed, as one commentator has opined, this 'half-hearted of local remedies rule' is neither realistic nor useful since (i) the time periods foreseen for the settlement of disputes by national courts and tribunals are too short for resolution of investment disputes of large scale, in particular, where the courts of the host state are of ill repute in prolonged resolution of cases; and (ii) the investor ultimately retains the right to resort to international arbitration once the time has lapsed and, considering that it usually conceives the courts of the host state as unreliable, he/she might deem this requirement as a time and money consuming ceremony which must be inevitably carried out before referring the case to investment treaty arbitration and, as a result, not try seriously to have its case heard and decided by the courts and the tribunals of the recipient state.[22]
10. Be that as it may, the table seems to have turned in recent years by more tribunals enforcing and effectively interpreting the local remedies requirement stipulated in investment treaties by, in some occasions, rejecting the application of the 'futility' principle to this requirement, and in others, by dismissing attempts to circumvent the requirement by drawing on MFN clauses.[23]
11. To give one example of this recent practice, the ICSID tribunal in *İçkale İnşaat Limited Şirketi v. Turkmenistan* found that Article VII(2) of the Turkey-Turkmenistan bilateral

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[19] See, for example, Article 8 of the Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina (n 16).

[20] See, for instance, *Emilio Agustín Maffezini v. The Kingdom of Spain* (n 13) [54]-[64]; *Siemens A.G. v. The Argentine Republic* (n 13) [32]-[110]; *Gas Natural SDG, S.A. v. The Argentine Republic* (n 13) [24]-[49]; *Suez, Sociedad General de Aguas de Barcelona S.A., and InterAguas Servicios Integrales del Agua S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/17, Decision on Jurisdiction, 16 May 2006 [52]-[66]; *National Grid plc v. The Argentine Republic*, UNCITRAL, Decision on Jurisdiction, 20 June 2006 [79]-[93]; *Suez, Sociedad General de Aguas de Barcelona, S.A.and Vivendi Universal, S.A. v. Argentine Republic*, ICSID Case No. ARB/03/19, Decision on Jurisdiction, 03 August 2006 [52]-[68].

[21] See, for instance, *Abaclat and Others v. Argentine Republic*, ICSID Case No. ARB/07/5 (formerly *Giovanna a Beccara and Others v. The Argentine Republic*), Decision on Jurisdiction and Admissibility, 04 August 2011 [579]-[584].

On both grounds, see C Schreuer, 'Investment Arbitration - A Voyage of Discovery' (2005) 2(5) TDM 3.

[22] C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (n 1) 4-5. On this point, see also *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Decision on Jurisdiction, 08 February 2005 [224] (characterising such provisions as "nonsensical from a practical point of view").

[23] See, for instance, *ICS Inspection and Control Services Limited v. The Argentine Republic*, (PCA Case No. 2010-9), Award on Jurisdiction, 10 February 2012 (declining jurisdiction due to the claimant's failure to comply with the 18-month local courts requirement provided for by Article 8 of the Argentina-UK BIT and finding that the MFN clause did not extend to international dispute resolution issues); *Daimler Financial Services AG v. Argentine Republic*, ICSID Case No. ARB/05/1, Award, 22 August 2012 (finding by majority that the claimant does not have yet standing to assert its claims under the treaty because the investor had failed to observe the 18-month recourse to-local-courts requirement set forth in Article 10 of the Argentina-Germany BIT and finding that the MFN clause could not be used by the claimant to circumvent the conditions precedent to arbitration laid down in Article 10 of the BIT.) (The claimant's subsequent attempts to have this award annulled failed. *Daimler Financial Services AG v. Argentine Republic*, ICSID Case No. ARB/05/1, 07 January 2015, Decision on Annulment); *Kiliç İnşaat İthalat İhracat Sanayi Ve Ticaret Anonim Şirketi v. Turkmenistan*, ICSID Case No. ARB/10/1, Award, 02 July 2013 (finding that recourse to local courts in Article VII.2 of the Turkey-Turkmenistan BIT to be an impermissible requirement and precondition and eventually finding that it lacked jurisdiction over the dispute).

investment treaty[24] constitutes a mandatory preliminary recourse to the local remedies, and a procedural bar to arbitration, which cannot be circumvented by a defence of 'futility'.[25]

12. This recent trend in investment treaty arbitration seems to be a significant turn of events. Indeed, to the extent that an investment treaty does refer to the requirement of exhaustion of local remedies for a given period of time, if the precondition of preliminary recourse to the courts of the host state is ignored by the investor, then the investment treaty tribunal would be unable to hear or decide the case on its merits due either to lack of jurisdiction or inadmissibility of the claim. It goes without saying that this development in investment treaty practice tends to give the courts of the host state a better place than they used to occupy in the overall framework of the resolution of investment treaty disputes.

### B. Reference to Domestic Courts of the Host State As A Prerequisite of the Violation of Investment Treaty Standards

13. In certain recent investment treaty arbitrations, the arbitral tribunals adjudicating a case pursuant to international investment agreements which lack any procedural requirement of the use of the domestic courts for a certain period of time or exhaustion of local remedies have held that a violation of treaty standards, like expropriation and fair and equitable treatment, occurs, or is likely to occur, when some recourse has been made to the domestic courts of the host state in the first place and the redress has been denied by those courts.[26]

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[24] See Agreement between the Republic of Turkey and Turkmenistan Concerning the Reciprocal Promotion and Protection of Investments (n 17). As per Article VII of this Agreement:

> 1. Disputes between one of the Parties and one investor of the other Party, in connection with his investment, shall be notified in writing, including a detailed information, by the investor to the recipient Party of the investment. As far as possible, the investor and the concerned Party shall endeavour to settle these disputes by consultations and negotiations in good faith.
>
> 2. If these disputes cannot be settled in this way within six months following the date of the written notification mentioned in paragraph 1, the dispute can be submitted, as the investor may choose to:
>
> (a) The International Center for Settlement of Investment Disputes (ICSID) set up by the "Convention on Settlement of Investment Disputes Between States and Nationals of other States". (in case both Parties become signatories of this Convention.)
>
> (b) an ad hoc court of arbitration laid down under the Arbitration Rules of Procedure of the United Nations Commission for International Trade Law (UNCITRAL). (in case both parties are members of U.N.)
>
> (c) the Court of Arbitration of the Paris International Chamber of Commerce.
>
> provided that, if the investor concerned has brought the dispute before the courts of justice of the Party that is a party to the dispute and a final award has not been rendered with one year. [sic]
>
> […]

[25] *İçkale İnşaat Limited Şirketi v. Turkmenistan*, ICSID Case No. ARB/10/24, Award, 08 March 2012 [167 *et seq*].

[26] See, for instance, *Ronald S. Lauder v. The Czech Republic*, UNCITRAL, Final Award, 03 September 2001 [204]; *Marvin Roy Feldman Karpa v. United Mexican States*, ICSID Case No. ARB (AF)/99/1, Award, 16 December 2002 [114], [134]; *Loewen Group, Inc. and Raymond L. Loewen v. United States of America* (n 10) [153]; *Generation Ukraine, Inc. v. Ukraine* (n 9) [20-30]-[20-33]; *Waste Management, Inc. v. United Mexican States*, ICSID Case No. ARB (AF)/00/3, Award, 30 April 2004 [97], [116]; *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL (formerly *EnCana Corporation v. Government of the Republic of Ecuador*), Award, 03 February 2006 [196]; *Jan de Nul N.V. and Dredging International N.V. v. Arab Republic of Egypt*, ICSID Case No.

14. To give an example, in *Helnan v. Egypt*, the claimant argued that the respondent had indirectly taken Helnan's contractual rights when one of its ministries degraded the claimant's hotel from five to four stars. Whereas the claimant tried to change the ministerial decision by communicating several times with the relevant ministry, it never filed a complaint before the courts of Egypt. The tribunal held that absent recourse to the Egyptian courts, the respondent's degrading decision could not be seen as a treaty breach; "it needs more to become an international delict."[27]
15. To set a more recent example, in *Cervin and Rhone v. Costa Rica*, the claimants argued that, by levying tariffs for Liquid Petroleum Gas without paying heed to the economic equilibrium of the market participants, Costa Rica had breached the fair and equitable treatment standard in the BIT between Costa Rica and Switzerland BIT. Quoting with approval from the award in *Generation Ukraine v. Ukraine*, the tribunal considered that it is significant that the claimants had not tried to obtain clarification regarding the alleged breach in the courts of Costa Rica. Although the tribunal noted that the Costa Rica–Switzerland BIT did not oblige investors to exhaust local remedies in the first place, it nevertheless took note of the fact that remedies were available for the claimants in the national courts of Costa Rica and a recourse by the claimants to such courts could have resolved the dispute in question.[28]
16. Making the violation of investment treaty standards contingent upon a preliminary recourse to the local remedies of the recipient state effectively results in incorporating such recourse to the courts of the host state into the substantive standards of treaty protection,[29] and can serve as a partial revival of the 'localisation' theory which was advanced by developing countries in the 1960-s and 1970-s.[30]
17. This requirement seems also to be finding its way in more recent investment treaties. The BIT between India and Belarus signed in 2018 provides at Article 3.4 that: "While considering an alleged breach of this article, a Tribunal shall take account of whether the investor or, as appropriate, the locally-established enterprise, pursued action for remedies before domestic courts or tribunals prior to initiating a claim under this Treaty." Similarly, the same treaty requires in Article 5.6 that in considering whether an expropriation has occurred, the "[t]ribunal shall take account of whether the investor or, as appropriate, the

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ARB/04/13, Decision on Jurisdiction, 16 June 2006 [121]; *Saipem S.p.A. v. The People's Republic of Bangladesh*, ICSID Case No. ARB/05/07, Decision on Jurisdiction and Recommendation on Provisional Measures, 21 March 2007 [150]-[153]; *Parkerings-Compagniet AS v. Republic of Lithuania*, ICSID Case No. ARB/05/8, Award, 11 September 2007 [316]-[320], [344], [360]-[361], [449], [453], [454]; *Metalpar S.A. and Buen Aire S.A. v. The Argentine Republic*, ICSID Case No. ARB/03/5, Award on the Merits, 06 June 2008 [144]-[146], [181], [214]-[217].

[27] *Helnan International Hotels A/S v. The Arab Republic of Egypt*, ICSID Case No. ARB/05/19, Award, 03 July 2008 [148].

[28] *Cervin Investissements S.A. and Rhone Investissements S.A. v. Republic of Costa Rica*, ICSID Case No. ARB/13/2, Award, 07 March 2017 [505]-[506].

[29] However, it should be pointed out that some of the investment treaty cases in which this ruling was rendered entailed the issue of whether a denial of justice had occurred. See, for instance, *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic*, ICSID Case No. ARB/97/3, Award, 21 November 2000 [80]; *The Rompetrol Group N.V. v. Romania*, ICSID Case No. ARB/06/3, Decision on Respondent's Preliminary Objections on Jurisdiction and Admissibility, 18 April 2008 [111], [114]; *Chevron Corporation (USA) and Texaco Petroleum Company (USA) v. The Republic of Ecuador*, UNCITRAL, PCA Case No. 34877, Interim Award, 01 December 2008 [80], [90], [214]-[238]. See also J Paulsson, *Denial of Justice in International Law* (CUP 2005) 107 *et seq*.

[30] See C Schreuer, 'Calvo's Grandchildren: The Return of Local Remedies in Investment Arbitration' (n 1) 16-17; C Schreuer, 'Interaction of International Tribunals and Domestic Courts in Investment Law' (n 7) 75-76.

locally-established enterprise, pursued action for remedies before domestic courts or tribunals prior to initiating a claim under this Treaty."[31]

## C. Recourse to the Courts of the Host State As A Point of Reference for Clarifying Preliminary Points of the Domestic Law

18. It is trite knowledge that decisions of domestic courts are not binding on international arbitrations deciding the same or closely-related disputes.[32] More specifically, it is also true that an international arbitral tribunal is the judge of its own jurisdiction.[33] This proposition clearly arises from the kompetenz-kompetenz legal doctrine.[34] Therefore, an investment treaty tribunal is not in principle bound by the findings of the courts of the host state in matters concerning its jurisdiction. Rather, it is the sole arbiter of its competence.
19. Nevertheless, as was indicated by the arbitral panel in *Occidental v. Ecuador*, domestic and international procedures "may both have cumulative effects and interact reciprocally".[35] Indeed, in the area of investment treaty arbitration, in certain matters, the arbitral tribunal directly or indirectly leaves decision-making regarding certain points in the hands of the national courts of the host state.

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[31] Treaty between The Republic of Belarus and The Republic of India on Investments, signed on 24 September 2018, not yet entered into force.

[32] In *Amco v. Indonesia*, the ICSID tribunal held that any judgment by a domestic court would not be binding on an international arbitral tribunal. The Tribunal stated: ". . . an international tribunal is not bound to follow the result of a national court. One of the reasons for instituting an international arbitration procedure is precisely that parties—rightly or wrongly—feel often more confident with a legal institution which is not entirely related to one of the parties. If a national judgment was binding on an international tribunal such a procedure could be rendered meaningless." *Amco Asia Corporation and others v. Republic of Indonesia*, ICSID Case No. ARB/81/1, Award, 20 November 1984 [177]. See also *Ceskoslovenska Obchodni Banka, A.S. v. The Slovak Republic*, ICSID Case No. ARB/97/4, Decision of the Tribunal on Respondent's Further and Partial Objection to Jurisdiction, 1 December 2000 [35].

[33] See, for instance, Article 41(1) of the ICSID Convention: "The Tribunal shall be the judge of its own competence"; Article 45(1) of the ICSID Additional Facility Rules: "The Tribunal shall have the power to rule on its competence. For the purposes of this Article, an agreement providing for arbitration under the Additional Facility shall be separable from the other terms of the contract in which it may have been included"; Article 23(1) of the UNCITRAL Arbitration Rules as revised in 2010: "The arbitral tribunal shall have the power to rule on its own jurisdiction, including any objections with respect to the existence or validity of the arbitration agreement."

For investment treaty practice in this respect, see *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*, ICSID Case No. ARB/84/3, Decision on Jurisdiction, 14 April 1988 [38]; *Petrobart Limited v. The Kyrgyz Republic*, SCC Case No. 126/2003, Award, 13 February 2003, Section 5.3.2; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Award, 07 July 2004 [55]; *Inceysa Vallisoletana S.L. v. Republic of El Salvador*, ICSID Case No. ARB/03/26, Award, 02 August 2006 [209]-[213]; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Decision of the ad hoc Committee on the Application for Annulment of Mr Soufraki, 05 June 2007 [59], [78]; *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Award, 16 August 2007 [391]; *Empresas Lucchetti, S.A. and Lucchetti Peru, S.A. v. The Republic of Peru*, ICSID Case No. ARB/03/4, Decision on Annulment, 05 September 2007 [81]-[87]. See also in this respect, the jurisprudence of the PCIJ and ICJ in *The Electricity Company of Sofia and Bulgaria* (*Belgium v. Bulgaria*) Judgment, (Preliminary Objection) P.C.I.J. Rep. Series A/B, No. 77, 1939 (04 April 1939) p 64; *Aegean Sea Continental Shelf* (*Greece v. Turkey*), Judgment, I.C.J. Rep. 1978 (19 December 1978) p 3.

[34] The principle of competence/competence recognises the jurisdiction of an arbitral tribunal to decide matters regarding its own jurisdiction when and as such jurisdiction is contested. See JF Poudret & S Besson, translated by SV Berti & A Ponti, *Comparative Law of International Arbitration* (Sweet & Maxwell 2007) 385.

[35] *Occidental Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467, Final Award, 01 July 2004 [58].

20. It is prevalent practice in investment treaty arbitrations to refer to, and rely on, the holdings of the courts of the host state in matters concerning the law of the host state. For instance, in *Azinian v. Mexico*, the tribunal considered and relied on the decisions rendered by the three levels of Mexican courts regarding the validity of the underlying concession agreement which was governed by Mexican law. Although the tribunal noted that preliminary recourse to Mexican courts did not foreclose submission of the dispute to arbitration, it nevertheless held that the annulment of the concession had been found by Mexican courts to be in conformity with applicable Mexican laws and that the standards contained in such laws were not being challenged by the claimants. Therefore, for the tribunal, the decisions of the courts of Mexico were not expropriatory and truly represented the position of the Mexican law on this critical threshold issue.[36] In a similar vein, another NAFTA tribunal, again deciding a case in which Mexico was the respondent, observed that: "It was for the Mexican courts to rule on the licitness of the expropriation as a matter of Mexican law. The present Tribunal defers to the Sentencia as an authoritative expression of national law. The present Tribunal will moreover give respectful consideration to the Sentencia insofar as it applies norms congruent with those of NAFTA."[37]
21. As can be seen from the two examples cited above, generally speaking, investment treaty tribunals give deference to the judicial determinations of the courts of the host state regarding matters of host state law. To be sure, the task of an investment treaty tribunal is to check actions and/or inactions of the host state (including its judicial organs) against international law standards.[38] This international law guardian task of investment treaty arbitral tribunals is not incompatible with giving deference to the findings by the courts and tribunals of the recipient state on matters of domestic law in dispute. Indeed, the municipal court's decision(s), actions, and inactions could be targeted by the investment treaty arbitration tribunal only if the alleged breach of the investment treaty is attributed to the judicial organs of the host state. If, however, the particular dispute in question concerns an alleged violation of the investment treaty which has not been committed by the judiciary of the state but as to which the interpretation proffered by the national court regarding a point of host state law remains pertinent, the arbitral panel should consider, and if circumstances so require, give deference to the verdict of the state court. More specifically speaking, investment treaty tribunals should refer and give deference to the findings of the courts of the host state in jurisdictional matters which are governed by the laws of the host state. Two prime examples of such matters, as was seen in Chapters 2 and 3, are the legality of investment and the existence of property rights underlying investment both of which issues are usually governed by the laws of the host state.[39]

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[36] *Robert Azinian, Kenneth Davitian, & Ellen Baca v. The United Mexican States*, ICSID Case No. ARB (AF)/97/2, Award, 01 November 1999 [96]-[99].

[37] *Gami Investments, Inc. v. The Government of the United Mexican States*, UNCITRAL, Final Award, 15 November 2004 [41].

[38] *Amco Asia Corporation and others v. Republic of Indonesia* (n 32) [150]; *Robert Azinian, Kenneth Davitian, & Ellen Baca v. The United Mexican States* (n 36) [97]-[103]; *Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, ICSID Case No. ARB(AF)/98/3, Decision on Jurisdiction, 09 January 2001 [47]-[60]; *Saipem S.p.A. v. The Peoples Republic of Bangladesh* (n 9) [188]-[190]; *RosInvestCo UK Ltd. v. The Russian Federation*, SCC Case No. V079/2005, Final Award, 12 September 2010 [602]-[603].

[39] See Chapter 2, Section One & Chapter 3, Section One.

22. Having said that, the question remains as to why international tribunals give such a deference to the findings of the courts of the host state whereas there is usually nothing in the underlying treaty or the arbitration rules to stop them from giving their own independent opinion about the disputed matter without regard to the holdings of the courts of the host state?
23. As was delineated in Chapter 4, on an international plane, judges and/or arbitrators who are supposed to settle disputes arising out of treaties are deemed to know international law. This is presumably why they occupy the distinguished chairs of international adjudicators. That knowledge of international law, however, does not make arbitrators and judges of international stature experts in domestic law. In short, as stated by the PCIJ in the *Brazilian Loans Case*, "[t]hough bound to apply municipal law when circumstances so require, the Court, which is a tribunal of international law, and which, in this capacity, is deemed itself to know what this law is, is not obliged also to know the municipal law of the various countries."[40]
24. Bearing this in mind, whether the findings of the courts of the host state are submitted by the parties to the dispute or are referred to pursuant to the tribunal's own investigations or a combination of both, a sensible approach by a given investment treaty arbitral tribunal in matters where the laws of one of the state parties are applicable to a particular question would be giving proper weight to the practice of the domestic courts of that state (the contracting state's case law) in determining the meaning, scope or the effect of the internal legal provision at issue. In other words, an investment treaty tribunal "must step into the shoes and mindset" of a domestic judge and must determine what a national court applying national law would have done in these cases, "rather than directly apply its own interpretation" of domestic law.[41]
25. Attributing a great weight to the findings of the courts of the host state in matters concerning domestic law is widely accepted in the practice of investment treaty tribunals. While noting that it is the ultimate power to be the final arbiter of its own jurisdiction, the *Soufraki* tribunal mentioned that in deciding the jurisdictional question at stake, in that case, the issue of nationality, "[the international tribunal] 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."[42] [emphasis added] In the same vein, the ICSID Annulment Committee in the *Soufraki* case held that in interpreting and applying domestic law, a tribunal should accord a distinguished treatment to the case law of the relevant state:

> An international tribunal's duty to apply Italian law is a duty to endeavour to apply that law in good faith and in conformity with national jurisprudence and the prevailing interpretations given by the State's

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[40] *Payment in Gold of Brazilian Federal Loans Contracted in France* (*France v. Brazil*), Judgment, P.C.I.J. Rep. Series A, No. 21, 1929 (12 July 1929), p 124. See also *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide, 23 December 2010 [236] (noting that "the Tribunal had not been chosen for its knowledge of Philippine law."

[41] *Chevron Corporation and Texaco Petroleum Company v. The Republic of Ecuador* (I) (PCA Case No. 34877), Partial Award on the Merits, 30 March 2010 [375]. See also *Payment in Gold of Brazilian Federal Loans Contracted in France* (n 40), p 124.

[42] *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Award (n 33) [55].

> judicial authorities. A State's nationality law consists of its legislative and administrative provisions as well as the binding interpretations of those provisions by its highest court. Mr. Soufraki argues that a State's law also includes its interpretative case law, official government circulars, and the consensus of leading scholars that illuminate its application and meaning. The ad hoc Committee agrees that, when applying national law, an international tribunal must strive to apply the legal provisions as interpreted by the competent judicial authorities and as informed by the State's "interpretative authorities."
>
> It is the view of the Committee that the Tribunal had to strive to apply the law as interpreted by the State's highest court, and in harmony with its interpretative (that is, its executive and administrative) authorities…[43]

A similar line of reasoning was pursued by the ICSID Annulment Committee in the *Fraport* case, which involved questions of the illegality of investment and as such called for the application and interpretation of the laws of the host state law:

> So far as Philippine law was concerned, the Tribunal identified ADL as the specific law in question. To the extent of its applicability, the Tribunal (whilst retaining its independent powers of assessment of the evidence and decision) should give particular consideration to municipal decisions as to the construction of the ADL in determining how it would be applied within the municipal legal system. […] This was particularly important in the present case as it is recognised that the Tribunal had not been chosen for its knowledge of Philippine law. It follows that the right of the parties to be heard importantly includes an opportunity to be heard on the meaning and effect of any such relevant municipal decisions.[44]

26. There are two common denominators in these three decisions: **first**, an investment treaty tribunal retains the ultimate power to ascertain or to dismiss its jurisdiction; **second**, nevertheless, when faced with jurisdictional matters the governing law of which is the laws of one of the contracting states, the tribunals should give particular weight or "due consideration"[45] to the way the disputed matters of law have been decided and interpreted by the national courts of that state and treat those decisions with high deference, in particular, when those decisions have been rendered by the highest courts of the state in question[46] or where the decisions at issue represent the prevailing practice of the courts of

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[43] *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Decision of the *ad hoc* Committee on the Application for Annulment of Mr. Soufraki (n 33) [96]-[97].

[44] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide (n 40) [236].

[45] *Vigotop Limited v. Hungary*, ICSID Case No. ARB/11/22, Award, 1 October 2014 [509].

[46] See *Payment of Various Serbian Loans Issued in France* (*France v. Yugoslavia*), Judgment, P.C.I.J. Rep. Series A, No. 20, 1929 (12 July 1929) p 36; *Ahmadou Sadio Diallo* (*Republic of Guinea v. Democratic Republic of the Congo*), Judgment, I.C.J. Rep. 2010 (30 November 2010) p 639, p 665 [70]; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Decision of the ad hoc Committee on the Application for Annulment of Mr. Soufraki (n 33) [97] (stating that: "It is the view of the Committee that the Tribunal had to strive to apply the law as

the pertinent state.[47] The reason for giving such particular weight to the decisions of the courts of the host state is that, unlike investment treaty tribunals, courts of the host state are knowledgeable about and master the relevant domestic law and apply it on a daily basis. Therefore, they are well-placed to determine with accuracy how the law of the recipient state should be interpreted and, as such, their decisions are "informative for understanding the domestic law provisions and their meaning and application to the circumstances."[48] By valuing the credible jurisprudence of host state courts, an arbitral tribunal avoids divorcing "domestic law from its domestic context".[49] Thus, unless circumstances exist that nullify the weight of the relevant ruling or practice, the decisions of municipal courts of the host state should be given particular weight by investment treaty tribunals in appropriate situations.

27. The approach adopted by investment treaty tribunals vis-à-vis the determinations of the courts of the contracting parties has its root in the earlier findings of the PCIJ and ICJ. Indeed, in the *Serbian Loans case*, the Permanent Court acknowledged that it is not appropriate for it to ignore the findings of the relevant national courts on matters of domestic law and replace them with its own opinion:

> For the Court itself to undertake its own construction of municipal law, leaving on one side existing judicial decisions, with the ensuing danger of contradicting the construction which has been placed on such law by the highest national Tribunal ... would not be in conformity with the task for which the Court has been established and would not be compatible with the principles governing the selection of its members.[50]

The Court then further went on to add that: "It is French law, as applied in France, which really constitutes French law."[51]

28. By the same token, in the companion case of the *Brazilian Loans*, the PCIJ made the following observations which seek to pinpoint the propositions made above and merit quoting *in extenso*:

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interpreted by the State's highest court."); J Crawford (ed), *Brownlie's Principles of Public International Law* (8th Edition, OUP 2012) 53.

[47] It is also notable that Article 8.31(2) of the CETA requires the Tribunal to "follow the prevailing interpretation given to the domestic law by the courts and the authorities" of the host state when applying the domestic law of the recipient state. See Comprehensive Economic and Trade Agreement (CETA) between Canada, of the One Part, and the European Union And Its Member States, signed on 30 October 2016, not yet entered into force. See also Article 20(12) of the 2018 Netherlands Model BIT: "In determining the consistency of a measure with this Agreement, the Tribunal may consider, as appropriate, the domestic law of the disputing Party as a matter of fact. In doing so, the Tribunal shall follow the prevailing interpretation given to the domestic law by the court or authorities of that Contracting Party and any meaning given to domestic law by the Tribunal shall not be binding upon the courts or the authorities of that Contracting Party."

[48] *Luigiterzo Bosca v. Lithuania*, UNCITRAL, Award, 17 May 2013 [163].

[49] J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 109. See also O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 114.

[50] *Payment of Various Serbian Loans Issued in France* (n 46) p 36.

[51] ibid 46-47.

> [79] Though bound to apply municipal law when circumstances so require, the Court, which is a tribunal of international law, and which, in this capacity, is deemed itself to know what this law is, is not obliged also to know the municipal law of the various countries. All that can be said in this respect is that the Court may possibly be obliged to obtain knowledge regarding the municipal law which has to be applied. And this it must do, either by means of evidence furnished [to] it by the Parties or by means of any researches which the Court may think fit to undertake or to cause to be undertaken.
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> [80] Once the Court has arrived at the conclusion that it is necessary to apply the municipal law of a particular country, there seems no doubt that it must seek to apply it as it would be applied in that country. It would not be applying the municipal law of a country if it were to apply it in a manner different from that in which that law would be applied in the country in which it is in force.
>
> [81] It follows that the Court must pay the utmost regard to the decisions of the municipal courts of a country, for it is with the aid of their jurisprudence that it will be enabled to decide what are the rules which, in actual fact, are applied in the country the law of which is recognized as applicable in a given case. If the Court were obliged to disregard the decisions of municipal courts, the result would be that it might in certain circumstances apply rules other than those actually applied; this would seem to be contrary to the whole theory on which the application of municipal law is based.
>
> [82] Of course, the Court will endeavour to make a just appreciation of the jurisprudence of municipal courts. If this is uncertain or divided, it will rest with the Court to select the interpretation which it considers most in conformity with the law. But to compel the Court to disregard that jurisprudence would not be in conformity with its function when applying municipal law…[52]

29. Similarly, in the *Diallo* case, the ICJ made clear-cut pronouncements regarding the weight and the importance of the decisions of domestic courts regarding matters of domestic law:

> The Court recalls that it is for each State, in the first instance, to interpret its own domestic law. The Court does not, in principle, have the power to substitute its own interpretation for that of the national authorities, especially when that interpretation is given by the highest national courts.[53]

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[52] *Payment in Gold of Brazilian Federal Loans Contracted in France* (*France v. Brazil*), Judgment, P.C.I.J. Rep. Series A, No. 21, 1929 (12 July 1929), pp 124-125.

[53] *Ahmadou Sadio Diallo* (n 46) p 639, p 665 [70]. For further jurisprudence from the Court, see also *Elettronica Sicula S.p.A. (ELSI) (United States of America v. Italy)*, Judgment, I.C.J. Rep. 1989 (20 July 1989) p 15, p 36 [62] (noting that "Where the determination of a question of municipal law is essential to the Court's decision in a case, the Court will have to weigh the jurisprudence of the municipal courts …").

30. What one can extrapolate from the above is further support for the propositions mentioned above: international adjudicators master international law and not domestic law; the best source to find the correct interpretation of the relevant domestic law is the case law produced by the courts of the relevant state; as a result, international courts and tribunals should treat the judgments of domestic courts in matters of domestic law, in particular, judgments of the pertinent higher courts, with high deference.[54]
31. That being said, there remains a legitimate concern that the state party to the dispute might abuse its position and tend to manipulate the veritable interpretation of its laws in a pending case by resorting to its courts and obtaining a favourable judgment which would serve as a deadly weapon in the jurisdictional or the merits phase of the investment treaty case. To guard against such an inappropriateness when evidently occurred, an investment treaty tribunal should move to block such abusive attempts by substituting its own interpretation for the interpretation by the national courts of the host state. As the World Court has recently held "[e]xceptionally, where a State puts forward a manifestly incorrect interpretation of its domestic law, particularly for the purpose of gaining an advantage in a pending case, it is for the Court to adopt what it finds to be the proper interpretation."[55] Indeed, in such a scenario, the problematic ruling of the court of the host state does not uphold the weight that it should have otherwise deserved. Such a tainted domestic judgment does not and cannot be representative of how the law of the host state is applied in practice. Therefore, the tribunal should ignore the respective judgment and replace its own interpretation. The whole idea behind valuing the credible jurisprudence of host state courts is informing the investment treaty tribunal's analysis of respective matters of domestic law not making the investment treaty arbitral tribunal a passive subordinate of domestic courts' rulings.[56] The PCIJ had prescribed a similar approach when the jurisprudence of the courts of the state was 'uncertain' or 'divided'.[57] However, this proposition, i.e., replacing the host state courts' judgment with the tribunal's opinion, remains limited to cases of manifest arbitrary determinations by the courts of the host state or, as the PCIJ noted in the *Brazilian Loans case*, in cases where the jurisprudence of the domestic courts is 'uncertain' or 'divided'.
32. The concern that the respondent state may get its courts to render a decision in its favour which could be misused in the investment treaty arbitration proceedings is put forward by the arbitral tribunal in *Inceysa v. El Salvador* which offered its solution to the problem in the ensuing manner:

> 209. Before deciding whether the investment made by Inceysa is protected by the BIT, considering that it was made in accordance with the laws of EI Salvador, it is important to repeat that, as the legality of the investment is

[54] An additional practical benefit that one can derive from this approach (i.e., relying on the interpretation of domestic law by municipal courts of the host state) is making the eventual arbitral award or decision more acceptable in the host state and enhancing the legitimacy of the process and outcome of the investment treaty arbitration in question.

[55] *Ahmadou Sadio Diallo* (n 46) p 639, p 665 [70].

[56] O Spiermann (n 49) 114.

[57] *Payment in Gold of Brazilian Federal Loans Contracted in France* (n 52), p 125 (indicating that: "the Court will endeavour to make a just appreciation of the jurisprudence of municipal courts. If this is uncertain or divided, it will rest with the Court to select the interpretation which it considers most in conformity with the law.") See also *Elettronica Sicula S.p.A. (ELSI) (United States of America v. Italy)* (n 53) p 36 [62].

> a premise for this Tribunal's jurisdiction, the determination of such legality can only be made by the tribunal hearing the case, i.e. by this Arbitral Tribunal.
>
> 210. Consequently, any resolutions or decisions made by the State parties to the Agreement concerning the legality or illegality of the investment are not valid or important for the determination of whether they meet the requirements of Article 25 of the Convention and of the BIT, in order to decide whether or not the Arbitral Tribunal is competent to hear the dispute brought before it.
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> 211. Sustaining an opinion different than the one described above would imply giving signatory States of agreements for reciprocal protection of investments that include the "in accordance with law" clause the power to withdraw their consent unilaterally (because they would have the power to determine whether an investment was made in accordance with their legislation), once a dispute arises in connection with an investment.[58]

33. Analysing the citation above, to the extent that the *Inceysa* tribunal affirmed that it had the duty to independently investigate the matter and make its own determinations regarding this jurisdictional issue, its holding seems to be correct. To be sure, an investment treaty tribunal does have an independent duty to ascertain jurisdiction irrespective of the parties' submissions.[59] Furthermore, rulings of municipal courts are not binding on and have no *res judicata* effect for the proceedings before investment treaty tribunals. In this latter respect, the *Fraport* tribunal cited *Inceysa* with approving terms and observed that: "holdings of municipal legal institutions cannot be binding with respect to matters properly within the jurisdiction of this Tribunal."[60] Nevertheless, the *Inceysa* tribunal's generalised statement, which tends to strip local courts' determinations of any value in investment treaty arbitrations, does not seem to be accurate. According to the tribunal's opinion, the rulings of the courts of the host state remain completely irrelevant to the determination of the issues regarding the jurisdiction of the investment treaty tribunal.[61] To be sure, if sound judgment

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[58] *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 33) [209]-[211].

[59] See, for instance, *Ioan Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania*, ICSID Case No. ARB/05/20, Decision on Jurisdiction and Admissibility, 24 September 2008 [65] (saying that: "The Tribunal understands its duty to determine its jurisdiction, including through examination of the jurisdictional requirements, *sua sponte*, if necessary, as it has an obligation to reject a claim if the record shows that jurisdiction is lacking. Or, put differently, a tribunal can rule on and decline its jurisdiction even where no objection to jurisdiction is raised if there are sufficient grounds to do so on the basis of the record.")

[60] *Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Award (n 33) [391]. See also *Southern Pacific Properties* (*Middle East*) *Limited v. Arab Republic of Egypt* (n 33) [38]; *Petrobart Limited v. The Kyrgyz Republic* (n 33) Section 5.3.2; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Award (n 33) [55]; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Decision of the *ad hoc* Committee on the Application for Annulment of Mr Soufraki (n 33) [59], [78]; *Empresas Lucchetti, S.A. and Lucchetti Peru, S.A. v. The Republic of Peru* (n 33) [81]-[87].

[61] See *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 33) [210]:

> [A]ny resolutions or decisions made by the State parties to the Agreement concerning the legality or illegality of the investment are not valid or important for the determination of whether they meet the requirements of Article 25 of the Convention and of the BIT, in

is handed down by the highest courts of the host state with respect to the issues in dispute, one wonders why the investment treaty tribunal should turn a blind eye to such a decision. Of course, this is not to suggest that the investment treaty arbitral tribunal should grant *res judicata* effect to the decision of the host state court. This is not and cannot be the case.[62] The proposition that is being made here is that a decision by the local courts of the respondent state should be given due consideration by the arbitral tribunal unless it is 'arbitrary', 'discriminatory' or otherwise 'shocking to the conscience'. In this respect, the *Unglaube* tribunal noted: "[T]he Tribunal would, without hesitation, have found that, under the Constitution and laws of Costa Rica, it is the Attorney General and the Supreme Court who are empowered to give authoritative and final interpretation of the law […] The construction of the 1995 National Park Law is a matter of Costa Rican law, and it is not appropriate for this Tribunal to substitute an opinion of its own or make any finding of liability unless the Attorney General and the Court are found to have acted in a manner which is arbitrary, discriminatory or otherwise shocking to the conscience."[63]

34. To particularise the proposition made above, i.e., giving proper weight to the verdicts of national courts unless circumstances require otherwise, one has to pay attention to the circumstances surrounding each national court decision and conduct a case-by-case analysis. In this connection, the *Petrobart* tribunal recalled that it was "mindful of the fact that a judgment rendered by a foreign court of law may well become relevant as evidence in the arbitration in question. The weight, if any, to be attributed to such evidence will depend on the facts and the legal issues involved in the individual case."[64]
35. In this respect, one would consider it useful to draw a distinction between decisions of the courts of the host state which address the abstract legal issue in question without involving the matters and the discrete dispute before the investment treaty tribunal and those decisions of the courts and tribunals of the host state which deal with the very dispute in question and the same parties and/or their affiliates in the investment treaty case or the same factual matters directly related to such a dispute. For instance, suppose that two years before the wake of a dispute between the parties in the investment treaty arbitration at issue,

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order to decide whether or not the Arbitral Tribunal is competent to hear the dispute brought before it.

[62] As noted above "an international tribunal is not bound to follow the result of a national court. One of the reasons for instituting an international arbitration procedure is precisely that parties—rightly or wrongly—feel often more confident with a legal institution which is not entirely related to one of the parties. If a national judgment was binding on an international tribunal such a procedure could be rendered meaningless." See *Amco Asia Corporation and others v. Republic of Indonesia*, ICSID Case No. ARB/81/1, Award (n 32) [177]. See also J Crawford (ed) (n 46) 59 (stating that "… there is no effect of *res judicata* from the decision of a national court so far as an international jurisdiction is concerned. Even if the subject-matter may be substantially the same, the parties may well not be …"

[63] *Marion Unglaube v. Republic of Costa Rica*, ICSID Case No. ARB/08/1, Award, 16 May 2012 [253]. In the same vein, Zachary Douglas comments that: "The general rule should be that there is a rebuttable presumption that a prior judicial decision will be upheld by the treaty tribunal absent any serious procedural irregularities or a manifest error of law." Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (2003) 74 BYIL 284. Similarly, another notable commentator has observed that: "It will be only in exceptional circumstances that an international tribunal will depart from the construction adopted by a national authority of its own law, such as where a manifestly incorrect interpretation is put forward in the context of a pending case." J Crawford (ed), *Brownlie's Principles of Public International Law* (8th Edition, OUP 2012) 53. See also *Kopecky v Slovakia*, App. No. 44912/98 (ECHR, Judgment of 28 September 2004) [56].

[64] *Petrobart Limited v. The Kyrgyz Republic* (n 33) Section 5.3.2.

in an unrelated case, the supreme court of country A (the host country) renders a final and binding judgment on the legal preconditions of the finalisation of a BOT contract in the waste management economic sector of country A (Scenario 1). Now, assume that the judgment rendered by the supreme court of the host state involves the disputing parties (or their affiliates) and the same legal question before the investment treaty tribunal (Scenario 2). Bearing in mind the points made above, an investment treaty tribunal should, in general, and unless the negative circumstances described above exist,[65] pay due heed to the judgment in Scenario 1 since there is very little or no doubt tainting the judicial integrity of such a domestic award. On the other hand, as to the second scenario, the tribunal should still respect the finding by the supreme court but seek to scrutinise it more carefully, as in this scenario, the conditions surrounding the rendition of the judgment might give rise to justifiable doubts as to the undue intervention by the state party in the conduct of the domestic proceedings and the outcome of the case.[66] The investment treaty tribunal's scrutiny is more warranted in scenario 2 when the case before the local courts of the host state is filed by the host state after the request for arbitration by the investor has been filed or after the actual commencement of arbitration proceedings. In such a situation, the integrity of the judgment rendered by the court is called into question by the circumstances of the pending arbitration case and one may think that the local proceeding has been commenced by the respondent state for the sole purpose of obtaining a favourable judgment in the courts of the host state to be assistive in the parallel investment treaty arbitration proceedings.[67]

36. That being said, even in the second scenario, i.e., judgment by the court of the host state involving the same or similar dispute and/or the same disputants or their affiliates, the

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[65] See fn 63 *supra* and the accompanying text.

[66] This is the concern that was shared by the ICJ in the *Diallo* case mentioned above. In that case, the ICJ took note of the fact that when the specific matters in dispute before the Court are or were also before national courts, there is a concern that the domestic proceedings might be interfered with: "[e]xceptionally, where a State puts forward a manifestly incorrect interpretation of its domestic law, particularly for the purpose of gaining an advantage in a pending case, it is for the Court to adopt what it finds to be the proper interpretation." See *Ahmadou Sadio Diallo* (n 46) p 639, p 665 [70]. See also J Crawford (ed) (n 46) 53 (observing that: "It will be only in exceptional circumstances that an international tribunal will depart from the construction adopted by a national authority of its own law, such as where a manifestly incorrect interpretation is put forward in the context of a pending case.") This also seems to be the underlying concern in the *Inceysa* tribunal's pronouncements, i.e., abusing the local proceedings to nullify consent in the specific case at hand. *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (n 33) [211]. While this concern is valid in certain cases, its generalisation to the weight of all domestic judgments seems to be out of proportion.

[67] The ICSID Annulment Committee in *Fraport v. Philippines* observed in this regard:

> This is not to say that the Prosecutor's Resolution was necessarily dispositive of the point for the purpose of the Tribunal's determination of its jurisdiction. On the contrary, the decisions of municipal authorities seized of cases against an alien which arise directly out of the same set of facts may need to be scrutinised very carefully by an international tribunal. The tribunal would need to satisfy itself, *inter alia*, as to the impartiality of the relevant decision-maker, in view of the pendency of proceedings against the state of which that decision-maker is an organ. The tribunal retains the ultimate power to judge the probative value of evidence placed before it.

*Fraport AG Frankfurt Airport Services Worldwide v. The Republic of the Philippines*, ICSID Case No. ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide (n 40) [242]

tribunal has to be heedful of the judgment if it finds no 'arbitrary' or 'discriminatory' element in the verdict, no unusual speed in the resolution of the case, and no evidence of otherwise improper interference by the state party to the dispute in the orderly conduct of the domestic proceedings. Even in cases where the local proceedings commence pursuant to the submission of the request for arbitration or the commencement of the investment treaty arbitration, the judgment of the national court of the host state should still be given weight if the above-mentioned red flags do not exist.[68] This is *a fortiori* so if it is through the arbitration process that certain irregularities are divulged. For example, if in the course of the exchange of briefs, oral submissions in the hearings, testimony of witnesses, or pursuant to inquiries by the arbitral tribunal, a reasonable doubt arises that the investor has committed a crime in the process of making the investment which gives rise to criminal prosecutions in the courts of the host state, no one could justifiably blame or downgrade the subsequent judgment of the legal authorities of the host state on the sole basis that the local litigation prosecution only started after the filing of the case before the investment treaty tribunal.[69] Indeed, arguing otherwise would be to show great disrespect to the judicial system of the host state which, absent strong proof of corruption and inefficiency in general or in the specific case at hand, would be totally inappropriate for an investment treaty tribunal to express or even to imply.[70]

37. On a related note, and as alluded to above, the higher the local judicial authority that renders the judgment, the more valuable and trustworthy would be the decision made by the courts of the host state. For example, in case the decision in question has been made by the supreme court of the host state, the arbitral tribunal should consider giving it more weight in comparison to a judgment handed down by a court of first instance.[71] The reason for such a distinction is obvious: a final decision by the highest judicial authority of the host state, say by the supreme court or a court of appeal, ought to involve a number of checks and balances. Furthermore, although it is not always true, it is usually the case that judges sitting in higher benches have more experience, knowledge, talent, and a greater sense of responsibility for preserving the integrity of the legal system of the host state, thereby, making their judgment a more reliable source for ascertaining the contents of the host state

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[68] See fn 63 *supra* and the accompanying text.

[69] For instance, in *Metal-Tech v. Uzbekistan*, much of the evidence of the corruption was divulged pursuant to the tribunal's *sua sponte* investigations. *Metal-Tech Ltd. v. Republic of Uzbekistan*, ICSID Case No. ARB/10/3, Award, 04 October 2013 [244]-[266]. Although the internal court proceeding in that case was not triggered pursuant to the tribunal's investigations, it is really conceivable that the fact of the commitment of an illegality could occur to the respondent after the commencement of the arbitration proceedings and upon the tribunal's investigation prompting the respondent to launch internal court proceedings against the investor, its representatives, its employees, or even the governmental authorities engaged in the alleged illegality.

[70] Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (n 63) 273-274.

[71] *Payment of Various Serbian Loans Issued in France* (n 46) p 36; *Ahmadou Sadio Diallo* (n 46) p 639, p 665 [70]; *Hussein Nuaman Soufraki v. The United Arab Emirates*, ICSID Case No. ARB/02/7, Decision of the ad hoc Committee on the Application for Annulment of Mr. Soufraki (n 33) [97] (stating that: "It is the view of the Committee that the Tribunal had to strive to apply the law as interpreted by the State's highest court."); WTO, *United States: Anti-Dumping Act of 1916 – Report of the Panel* (31 March 2000) WT/DS136R [6.53]—[6.59] (noting that "Interpretations by the Supreme Court of the United States […] prevail over interpretations made by the courts of appeals of the various circuits. Interpretations by courts of appeals, in turn, prevail over interpretations by district courts, but only within the same circuit … We shall respect the formal hierarchy of court decisions in the US federal system to the extent that it is applicable.")

law.[72] This presumption, however, could be rebutted if one finds that the judgment is stained by one or a number of improprieties listed above.[73]

### D. Recourse to the Courts of the Host State As Equal Dispute Settlement Venues

38. A classical situation in which courts of the host state may be considered to have the last say on all the allowable investment treaty disputes is a 'fork-in-the-road' situation. Pursuant to a so-called 'fork-in-the-road' clause, investors are given a choice between international arbitration and national courts of the host state. Once the investor opts for one forum, the choice is final. For example, Article 8(2) of the BIT between Argentina and France, entailing a so-called 'fork-in-the-road' clause, provides: "[o]nce an investor has submitted the dispute to the courts of the Contracting Party concerned or to international arbitration, the choice of one or the other of those procedures is final."[74] As a result, if the investor chooses to have its case heard by the national courts of the host state, it loses the right to resort to arbitration.[75] However, it should be mentioned that arbitral tribunals have interpreted such provisions restrictively, in that they have held that recourse to national courts of the recipient state would foreclose access to arbitration only if the same parties have filed the same dispute with the same cause of action before the courts of the host state.[76]

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[72] This is for this check and balance reason that a single judgment by the court of the first instance cannot usually amount to international responsibility for the national state of the court. Indeed, the aggrieved party should not stop at the first level of the judicial hierarchy and should step up and appeal the objected decision in higher courts of the host state before he/she can claim the international responsibility of the host state. Crawford notes in this regard: "There are also cases where the obligation is to have a *system* of a certain kind, e.g. the obligation to provide a fair and efficient system of justice. There, systematic considerations enter into the question of breach, and an aberrant decision by an official lower in the hierarchy, which is capable of being reconsidered, does not of itself amount to an unlawful act." ILC (J Crawford), 'Second Report on State Responsibility' (UN Doc. A/CN.4/498 1999) [75] (emphasis in original). See also B Demirkol (n 14) 78-79, fn 14 (listing authorities for the necessity to give the state an opportunity to rectify an incorrect judgment or problematic judicial act through the totality of its judicial system.)

[73] See fn 63 *supra* and the accompanying text.

[74] Agreement between the Government of the Argentine Republic and the Government of the Republic of France for Reciprocal Protection and Promotion of Investments, signed on 03 July 1991, entered into force on 03 March 1993.

[75] Z Douglas, *The International Law of Investment Claims* (n 10) 152-157; R Dolzer and C Schreuer (n 3) 267-268; C Schreuer 'Travelling the BIT Route—Of Waiting Periods, Umbrella Clauses and Forks in the Road' (2004) 5(2) J World Investment and Trade 231.

[76] See, for instance, *Eudoro Armando Olguín v. Republic of Paraguay*, ICSID Case No. ARB/98/5, Decision on Jurisdiction, 08 August 2000 [20]-[23], [30]; *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic* (n 29) [40], [42], [53]-[55], [81]; *Alex Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. The Republic of Estonia*, ICSID Case No. ARB/99/2, Award, 25 June 2001 [47], [58], [321], [333]; *Middle East Cement Shipping and Handling Co. S.A. v. Arab Republic of Egypt*, ICSID Case No. ARB/99/6, Award, 12 April 2002 [71]; *Compañiá de Aguas del Aconquija S.A. and Vivendi Universal S.A. v. Argentine Republic*, ICSID Case No. ARB/97/3, Decision on Annulment, 03 July 2002 [36], [38], [42], [55], [113]; *CMS Gas Transmission Company v. The Republic of Argentina*, ICSID Case No. ARB/01/8, Decision of the Tribunal on Objections to Jurisdiction, 17 July 2003 [77]-[82]; *Champion Trading Company, Ameritrade International, Inc. v. Arab Republic of Egypt*, ICSID Case No. ARB/02/9, Decision on Jurisdiction, 21 October 2003, Section 3.4.3; *Azurix Corp. v. The Argentine Republic*, ICSID Case No. ARB/01/12, Decision on Jurisdiction, 08 December 2003 [37]-[41], [86]-[92]; *IBM World Trade Corporation v. República del Ecuador* (n 9) [58]-[71], [82]-[84]; *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Decision on Jurisdiction, 14 January 2004 [95]-[98]*; LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Jurisdiction, 30 April 2004 [75]-[76]; *Occidental Exploration and Production Company v. The Republic of Ecuador*

39. Apart from the so-called 'fork-in-the-road' situation, some investment treaties have considered host state courts as a possible venue, along with others, to which the aggrieved investor can refer to in the wake of a dispute. In such cases, on equal footing with arbitration mechanism(s) contemplated in the relevant investment treaty, if chosen by the investor, the courts of the host state are competent to resolve all the allowable disputes arising out of the investment treaty in question. For instance, Article 12(3) of the BIT between Switzerland and Egypt provides that if disputes cannot be resolved through consultation, negotiation or mediation and/or if the investor is not satisfied with the outcome of the domestic administrative procedure, which in the case of this BIT, should be tried for a period of six months, then the investor is offered a range of options to pursue its investment claim. The first on the list in this dispute settlement menu is "the courts of the Contracting Party in whose territory the investment has been made."[77] Similarly, Article 18(2) of the BIT between Iran and Japan records the state contracting parties' agreement that one available procedural choice for an aggrieved investor is to submit its disputes before "the competent court of the other Contracting Party in the Territory of which the investment has been made" once the cooling-off period has expired or in the interim.[78]
40. A review of more recent investment treaties would show that the courts of the host state are more frequently referred to in investment treaties as a possible avenue for the investors to drive their investment disputes through. In particular, certain countries tend to give exclusive jurisdiction to settle investment treaty disputes to the courts of the host state. To give one example, in investment treaties it concludes with developed countries, Australia tends to exclude resolution of investment treaty disputes by international arbitration on the basis that "both countries have robust, developed legal systems for resolving disputes between foreign investors and government".[79] For instance, in its 2004 trade agreement with the United States, Australia managed to exclude the possibility of investor-state arbitration as a venue of redress for foreign investors.[80] More recently, the 2014 Australia–

(n 35) [37(a)], [38]-[63]; *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16, Decision on Objections to Jurisdiction, 11 May 2005 [116], [127]; *Pan American Energy LLC and BP Argentina Exploration Company v. The Argentine Republic*, ICSID Case No. ARB/03/13, Decision on Preliminary Objections, 27 July 2006 [155]-[157]; *M.C.I. Power Group L.C. and New Turbine, Inc. v. Republic of Ecuador*, ICSID Case No. ARB/03/6, Award, 31 July 2007 [36]-[38], [171]-[191]; *Desert Line Projects LLC v. The Republic of Yemen*, ICSID Case No. ARB/05/17, Award, 06 February 2008 [124]-[138]; *Chevron Corporation (USA) and Texaco Petroleum Company (USA) v. The Republic of Ecuador* (n 29) [198], [200], [207]; *Toto Costruzioni Generali S.p.A. v. The Republic of Lebanon*, ICSID Case No. ARB/07/12, Decision on Jurisdiction, 11 September 2009 [203]-[217]; *Charanne B.V. and Construction Investments S.a.r.l. v. Spain*, SCC Case No. 062/2012, Final Award, 21 January 2016 [408]-[409]. Cf *Pantechniki S.A. Contractors & Engineers (Greece) v. The Republic of Albania*, ICSID Case No. ARB/07/21, Award, 30 July 2009 [53]-[67]; *H&H Enterprises Investments, Inc. v. Arab Republic of Egypt*, ICSID Case No. ARB/09/15, Award, 06 May 2014 [356]-[387].

[77] Agreement between The Swiss Confederation and The Arab Republic of Egypt on the Promotion and Reciprocal Protection of Investments, signed on 07 June 2010, entered into force on 15 May 2012.

[78] Agreement between Japan and the Islamic Republic of Iran on Reciprocal Promotion and Protection of Investment, signed on 05 February 2016, entered into force on 26 April 2017.

[79] See E Fabry & G Garbasso, '"ISDS" in the TTIP: The Devil is in the Details' (Notre Europe, Jacques Delors Institute 2015) 15.

[80] Australia-United States Free Trade Agreement (2004), signed on 18 May 2004, entered into force on 01 January 2005. The exclusion of arbitration in investment dispute settlement was done on the basis of both parties' invocation to "the mutual credibility of their respective legal systems". See CN Brower & S Blanchard, 'What's in a Meme? The

Japan Economic Partnership Agreement does not include any provisions on investor-state arbitration.[81] [82] That being said, to what extent this dispute settlement method is used by investors in practice is another question and remains to be seen.

41. Apart from the two instances mentioned above, i.e., the 'fork-in-the-road' situation and the contemplation of the court of the host state as an equal or an exclusive option for dispute settlement in investment treaties, a review of more recent bilateral investment treaties shows that certain investment disputes have effectively been earmarked for the courts of the host state to decide to the exclusion of the jurisdiction of arbitral tribunals. Indeed, in such situations, unlike the two instances explained above, the role and the function of the courts of the host state is more tangible, realistic, and influential, leaving the investor with no choice but to have the relevant dispute solved by such judicial authorities.
42. A chief and prevalent example of the investment disputes that could only be resolved by the courts of the host state in certain recent bilateral investment treaties is disputes regarding taxation measures of the host state. There are two approaches to such disputes: (i) the first approach is observed in the 2012 Model BIT of the United States. Article 21(2) of the US Model BIT provides that "Article 6 [which concerns Expropriation] applies to all taxation measures". However, an aggrieved investor who claims that a given taxation measure by the host state has the effect of expropriating its property is prevented from submitting its claim to investor-state arbitration unless it, in the first place, has submitted its dispute to the Contracting Parties' respective 'competent authorities' and those authorities fail within one hundred and eighty (180) days from the date of the submission of the dispute to "agree that the taxation measure is not an expropriation". [83] The adverse implication of this provision is that if the competent authorities of the two Contracting Parties accord within the prescribed time period that the property of the investor has not

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Truth about Investor-State Arbitration: Why It Need Not, and Must Not, Be Repossessed by States' (2014) 52 Columbia Journal of Transnational Law 764.

[81] Agreement between Australia and Japan for an Economic Partnership, signed on 08 July 2014, entered into force on 15 January 2015.

Australia's insistence that investment disputes should be decided by its own courts does not seem to be unprecedented. In an article published in 1991, Sornarajah refers to one instance in which Australia broke an agreement to mine sand on Fraser Island made with an American company and insisted that the dispute should be settled by Australian courts rather than international arbitration. M Sornarajah, 'The Climate of International Arbitration' (1991) 8(2) J Int'l Arb 49, fn 13.

[82] The most recent approach adopted by Canada, Australia, the United States, as well as the European Union in taking certain measures against international arbitration as a method for the resolution of investment treaty disputes could be explained from an economic point of view. Indeed, as noted by one commentator, some of the developed countries have recently adopted a more protectionist and nationalistic approach towards issues pertinent to the inflow of foreign investment which has resulted in attempts to reassert control over previously privatised economic sectors and activities. See KP Sauvant, 'Driving and Countervailing Forces: A Rebalancing of National FDI Policies' (2009) Yearbook on International Investment Law And Policy 2008-2009, 215, 242, 254-257.

[83] Article 21.2 of the 2012 US Model BIT reads:

> 2. Article 6 [Expropriation] shall apply to all taxation measures, except that a claimant that asserts that a taxation measure involves an expropriation may submit a claim to arbitration under Section B only if:
>
> (a) the claimant has first referred to the competent tax authorities of both Parties in writing the issue of whether that taxation measure involves an expropriation; and
>
> (b) within 180 days after the date of such referral, the competent tax authorities of both Parties fail to agree that the taxation measure is not an expropriation.

been expropriated by virtue of the disputed tax measure(s), that is the end of the matter for the investor's expropriation claim on the basis of the challenged tax measure, meaning that the road for him to drive towards international arbitration for redress is blocked. In such a situation, the investor's only procedural remedy would be the courts and administrative tribunals of the host state. (ii) Another more recent approach can be observed in the new Indian Model BIT. One of the several matters excluded from the treaty's scope of application by virtue of Article 2.4 of the Model is "any law or measure regarding taxation, including measures taken to enforce taxation obligations". The Model Treaty then goes on to provide in the same provision that: "For greater certainty, it is clarified that where the State in which investment is made decides that conduct alleged to be a breach of its obligations under this Treaty is a subject matter of taxation, such decision of that State, whether before or after the commencement of arbitral proceedings, shall be nonjusticiable and it shall not be open to any arbitration tribunal to review such decision."[84]Although this provision does not specify the body making the decision regarding the nature of the disputed measure, one could arguably consider that such a decision comes from the courts or administrative tribunals of the host state. In any event, when excluded from the treaty's ambit of application due to the internal determination of the nature of the disputed measure, disputes regarding controversial taxation measures cannot be submitted to investment treaty arbitration any longer. Therefore, the only viable forum which remains for filing such disputes is, in all likelihood, the national court of the host state.

**Conclusion**

43. As was seen in Chapter 6, domestic law of the host state has a determinative role, *inter alia*, in resolving critical matters of subject-matter jurisdiction of investment treaty tribunals. This is a gradual achievement attained by host state law in the field of investment treaty arbitration. This more outstanding function of the laws of the host state in investor-state arbitrations is principally owed to more frequent references to the laws of the host state in investment treaties on the one hand, and the due attention paid by investment treaty tribunals to the capacities of the laws of the host state in the resolution of investment treaty cases on the other hand.

44. It was demonstrated in the present Chapter that against the background of a significant refusal of the courts of the host state as a forum for resolution of foreign investment disputes when the system of international investment agreements was initially put in place, it is obvious nowadays that recent developments in treaty rulemaking and investment treaty arbitration practice have created a more decisive role for the local courts of the recipient state in the settlement of investment treaty cases. Through these developments, recourse to the courts of the host state has, on certain occasions, become a precondition of consent to arbitration, admissibility of investment treaty claims or finding a breach of the investment treaty's substantive standards by the host state. Furthermore, from the lens of international adjudicators, courts of the recipient state are the primary points of reference for the interpretation of issues of host state law at stake in an investor-state arbitration case. Besides, the local courts of the respondent state are now more assertive as a sole forum for

[84] Article 2.4(ii) of the Model Text for the Indian Bilateral Investment Treaty (2015). In this respect, see G Hanessian & K Duggal, 'The 2015 Indian Model BIT: Is This Change the World Wishes to See?' (2015) 30(3) ICSID Rev-FILJ 734-735.

the resolution of all the allowable investment treaty disputes or as the only available competent forum for resolving certain discrepancies like disputed tax measures of the host state.

45. To what extent these developments in investment treaty law regarding the role of the laws and the courts of the host state (as the two arms of the classic 'localisation theory') have acted to revive the 'localisation theory', if any, will be subject to the Final Conclusion of this Thesis.

## Final Conclusion

1. It is the task of this 'Final Conclusion' to share some thoughts on the essential question of whether the theory of 'localisation' has been revived in the course of the recent developments of investment treaty arbitrations in the light of the studies and findings of Chapters 1-7, and if so, to what extent.
2. It was submitted and shown in this Thesis that, in addition to the provisions of investment treaties themselves, the applicable law to bilateral and multilateral investment treaties is a combination of domestic law and international law with each having its own specific field of application. This Thesis analysed the eventualities in which domestic law is applied in investment treaty arbitrations as 'fact' and as 'law'. It was submitted that whereas domestic law mostly applies as 'fact' in the merits phase of an investment treaty case, when it comes to matters of jurisdiction, in particular, subject-matter jurisdiction, the municipal law of the host state functions as 'law'. With a particular focus on the application of domestic law to issues of subject-matter jurisdiction, this Thesis examined various situations in which domestic law might be applied as 'law', the basis of such application, the modality of the ascertaining the contents of domestic law, and the consequences of the application of domestic law in an investment treaty arbitration proceeding. Furthermore, the more recent roles occupied by the courts of the host state in the resolution of investor-state disputes were also examined in light of the new developments in investment arbitration jurisprudence and the terms of more recent investment treaties. Being mindful of the analyses conducted herein, it has now become clear that through the gradual insertion of local elements (i.e., laws and courts of the host state) into investment treaties and through the developments in investment treaty arbitration practice, nowadays, one can see that investment treaty arbitrations are 'localised' to some extent, meaning that host states have managed to effectively 'relocalise' their legal relationship with foreign investors at least to some degrees. In other words, the host states, in particular through recent developments, have reasserted the control they had lost when their cherished 'localisation' theory was struck by the flood of 'internationalisation' and the fatal hurricane of bilateral investment treaties.
3. Through the analysis carried out in Chapters 1-4 of this Thesis, I was able to draw certain general conclusions. **Firstly**, it was shown in Chapter 1 that, irrespective of the broad formulation of the applicable law clause of the underlying investment treaty, the role of the domestic law of the host state in determining the all-important subject-matter jurisdiction of an investment treaty tribunal is pervasive. Indeed, many of the issues concerning jurisdiction *ratione materiae* have a direct or an indirect link with the laws of the host state.[1] Such matters include the definition and determination of rights comprising investments, the legality of investments, and, in certain cases, the approval for the investment. To elaborate on this point, one leg of the jurisdiction chair is the subject-matter or jurisdiction *ratione materiae*. In order to ascertain jurisdiction *ratione materiae*, an arbitral tribunal, seized of deciding an investment treaty case should have before it a check-list, enlisting at least three items: (1) whether there are rights over assets and properties recognised by the domestic laws of the host state; (2) whether such rights have been validly and legally obtained; and (3) whether such recognised and valid rights under the laws of the host state meet the economic definition of an investment, or

[1] A Newcombe & L Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International 2009) 95-96 (stating that: "Domestic law questions often arise at the jurisdictional phase of IIA arbitration proceedings, as they are relevant to establishing the existence of the protected investment or the specific disputed contractual or proprietary right, and thus a tribunal's jurisdiction *ratione materiae*.")

the so-called '*Salini* test'.[2] If all the boxes of the check-list are ticked, then the tribunal can make sure that one leg of the chair works properly well. The first two items of the above-mentioned list were subject to detailed discussion in this Thesis. In fact, while the issue of the existence of 'investment' requires an autonomous interpretation and an analysis of economic features, and, as such, warrants a general economic examination, the rest of jurisdiction *ratione materiae* analysis is legal discussions of existence and validity of rights, in which host state law plays the principal role.

I argue that there are two main legal grounds to justify the application of the internal laws of the recipient state for the purpose of identifying rights over properties and specifying the legality or illegality of an investment. It was demonstrated in Chapters 2 & 3 that the domestic law of the host state applies to the above-mentioned topics of subject-matter jurisdiction either because the contracting parties to the investment treaty have expressly or implicitly agreed so or because the nature of the issue requires the application of host state law. In the latter situation, domestic law applies because the matter in question is one which is related to the sovereignty of the host state as to which international law usually, and unless the contracting parties to the investment treaty have agreed otherwise, does not have a rule to apply. In such situations, general principles of law call for the application of domestic law to the matters concerned. In this relation, it was also established in Chapters 2 & 3 that a proper conflict of laws analysis indicates that it is the law of the host state which has the last say on these matters of subject-matter jurisdiction. Besides, it was indicated that due to its significance in settling these two issues, i.e., the creation and existence of rights/interests over properties and assets and the legality of investment, domestic law of the host state plays a prominent role in determining the jurisdiction *ratione materiae* of a tribunal, leaving very little playing field for international law in this respect.[3] Indeed, whilst it is the domestic law of the host state that determines whether valid and enforceable rights exist, the role of international law would be to determine whether such rights are protected by the treaty.[4] Being mindful of these observations, although much will depend on how the case is pleaded in each individual dispute, generally speaking, it is now arguable that domestic law has indeed "frequent centrality to the outcome of the case".[5] In this light, it cannot be argued that, in international disputes, municipal laws function merely as 'facts'.[6]

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[2] As framed, there are other possible criteria set by some investment treaties like obtaining approval for investments, which is not subject to our close examination in this Thesis.

[3] One possible role for international law could be providing lists of limitations, exclusions, and exceptions in the 'definitions' clause of an investment treaty or defining the terms 'property' or 'asset' directly by an agreement in the treaty or through subsequent agreement and/or subsequent practice.

[4] M Sasson, *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer Law International 2017) 103.

[5] In 2017, Jarrod Hepburn concluded with dismay that "the place of domestic law in [investment treaty] arbitrations has received somewhat less attention, notwithstanding its frequent centrality to the outcome of the case …" J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 3-4. Additionally, already in 2003, Douglas had observed that: "With disturbing frequency, questions of municipal law relating to aspects of the investment are brushed aside as peripheral or dealt with superficially by tribunals …" Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (2003) 74 BYIL 273. See also VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (2006) 23(4) J Int'l Arb 287 (characterising the role of the national law of the host state in foreign investment treaty arbitrations as 'vital' and 'enduring'.)

[6] In *Certain German Interests in Polish Upper Silesia*, for instance, the PCIJ held that:

> [f]rom the standpoint of International Law and of the Court which is its organ, municipal laws are merely facts which express the will and constitute the activities of States, in the same manner as do legal decisions or administrative measures.

Surely, one can fairly criticise an opinion that treats local laws as mere 'facts' in investment treaty arbitrations.[7] Furthermore, it is not even accurate to argue that, when applied as law, domestic law "will be confined to certain incidental and preliminary questions".[8] In point of fact, one could firmly say that domestic law applies to a number of preliminary but fundamental questions in an investment treaty arbitration.

4. **Secondly**, Chapters 2 & 3 went through the legal consequences that the application of the host state law can have on the specific *ratione materiae* issues before an investment treaty tribunal and the upshot of such application for the outcome of the whole case. In particular, through these discussions, it was shown that municipal laws of the host state supply the 'substantive aspects' of the rights underlying investments. The substantive aspects include the existence as well as the legality of a property right.[9] Chapters 2 & 3 of the Thesis also dealt thoroughly with the specific *ratione materiae* questions that may turn up in an investment treaty arbitration case and the assistance that can be provided by the domestic law of the host state to resolving such matters. Through this discussion, it was readily apparent that domestic law of the host state has the role and the capability of answering various questions posed by nuanced *ratione materiae* issues.
5. **Finally**, Part I was concluded by outlining the methods of ascertaining the contents of the host state law. As it was set out in Chapter 4, the rulings of the courts of the host state are the prime means for ascertaining the contents of the host state law.
6. Part II of this work commenced its mission by narrating the history, contents, and the fate of the classical 'localisation' theory. This task was carried out by Chapter 5 of the Thesis. There it was discussed that the backbone idea of the 'localisation' theory was that the fate of an investment contract dispute should be decided by the laws and the courts of the host state. Put differently, those who supported the 'localisation' theory

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See *Certain German Interests in Polish Upper Silesia* (*Germany v. Poland*), Judgment, P.C.I.J. Rep. Series A, No. 7, 1926 (25 May 1926) p 19. See also *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL *(formerly EnCana Corporation v. Government of the Republic of Ecuador)*, Partial Dissenting Opinion of Horacio A. Grigera Naon, 30 December 2005 [12] (disagreeing with the application of domestic law to the question of the existence of investment and stating that "[…] the local laws, administrative acts and practices and other conduct attributable to the host State at the moment they had the effect of operating the deprivation of property, are *facts* to be freely evaluated by the arbitrators to determine if the foreign investor's entitlement to protection under international law has been infringed at a specific moment in time or not.") *Vladimir Berschader and Moïse Berschader v. The Russian Federation*, SCC Case No. 080/2004, Award, 21 April 2006 [96] (stating that: "The Vienna Convention provides no role for the domestic law of contracting states in the interpretation of international treaties. Therefore, in the instant case, it is clear that Russian national law is of no relevance in this regard. While Russian law may be relevant in establishing certain factual circumstances involved in the merits of the case, it has no role to play in determining the jurisdiction of the Tribunal."); *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. The Argentine Republic*, ICSID Case No. ARB/09/1, Decision on Jurisdiction, 21 December 2012 [217]-[218] (where the tribunal holds that reference to domestic law in certain jurisdictional areas is for the purpose of determining "a question of fact"); R Jennings & A Watts (eds), *Oppenheim's International Law* (Vol. 1, 9th edn, Longman 1992) 83 (stating that: "From the standpoint of international law, a national law is generally regarded as a fact with reference to which rules of international law have to be applied, rather than as a rule to be applied on the international plane as a rule of law; and insofar as the International Court of Justice is called upon to express an opinion as to the effect of a rule of national law it will do so by treating the matter as a question of fact to be established as such rather than as a question of law to be decided by the court"); G Sacerdoti, 'Investment Arbitration under ICSID and UNCITRAL Rules: Prerequisites, Applicable Law, Review of Awards' (2004) 19(1) ICSID Rev-FILJ 25-26.

[7] M Sasson (n 4) 1-3.

[8] O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 108; C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (2014) 1(1) McGill Journal of Dispute Resolution 17 (where he states that in such situations domestic law is "incidentally applied").

[9] M Sasson (n 4) 147.

put forward the viewpoint that the applicable law of foreign investment contracts should be the municipal laws of the host state and that any dispute arising from such contracts should be decided by the courts of the host state. Chapter 5 addressed this theory and described how it was wiped out by the developed countries. This Chapter was concluded by looking into the phenomenon of bilateral investment treaties which were effectively the last terminating effort for the annihilation of the 'localisation' theory.

7. Thereafter, in Chapter 6, it was shown that both the more recent investment treaty arbitration practice, and to some extent, the trends in investment treaty-making attest to the fact that the role of domestic law in investment treaty arbitrations, in particular, in matters concerning jurisdiction *ratione materiae* is nowadays more outstanding and clear. For instance, if one were to consider previous case law which touched upon such matters, one would have most probably faced silence on the role of the host state law by the arbitral tribunal or would have witnessed that the tribunal would have merely alluded to such a role without being elaborative on the point. One reason that could explain the previous approach could be the unfamiliarity of arbitrators with domestic law or their hesitance to vocally apply domestic law in an international dispute. However, if one considers the current practice, one realises that the investment treaty arbitral tribunals are usually more express on this reality and deal with the role of the host state law in a more comprehensive manner. Furthermore, it was argued in Chapter 7 that the more recent practice of investment treaty arbitration as well as the trends in treaty rulemaking attest to the fact that the courts of the host state have nowadays a much more prominent role through interventions and determinations on various matters related directly or indirectly to matters in dispute in investment treaty arbitrations.
8. These developments, taken overall, leave any reasonable bystander with one plain conclusion: The 'localisation' theory has to some extent resurfaced. This is not to suggest that these developments have fully revived the 'localisation' theory. To be sure, one could only strongly argue for a 'partial' revival of the 'localisation' theory. I use the phrase 'revival of the localisation theory' because the new developments have brought back to life the determinative roles of the host state law and host state courts, the two pillars of the 'localisation' theory, in international investment disputes. Furthermore, these determinations by the laws and the courts of the host state are indeed effective and important since, in certain cases, the determination by the laws of the host state, or the courts of the host state for that matter, is the end of the story for a significant part or all of the case. In one of his earlier articles on investment treaty arbitration, Schreuer describes investment arbitration as a 'voyage' by the sea. He warns that before "embarkation, the passengers need to have their passports checked", otherwise, there will be no journey.[10] The arbitral tribunal sets a passport check for investors to ascertain jurisdiction. If the passport is not valid or there is no visa, there will be no journey at all. Assume that the preliminary point in dispute in an investor-state arbitration is whether the contract constituting alleged contractual rights has been validly entered into under the municipal law of the host state. If the answer to this question is in negative, then, as far as the alleged contractual rights in question are concerned, no claim can be upheld. Indeed, even if a given claim is very strong on the merits, for instance, a viable expropriation claim, but the case suffers from the lack of a subject-matter jurisdiction element, like illegality pursuant to the host state law or the non-recognition of the alleged right/interest by the host state law, the claimant's case would still fail. In *Accession Mezzanine v. Hungary*, in spite of the fact that the tribunal had noted and recognised the wrongfulness of the respondent's conduct in the tender process, it

[10] C Schreuer, 'Investment Arbitration - A Voyage of Discovery' (2005) 2(5) TDM 4.

nevertheless dismissed the claimant's case for lack of jurisdiction.[11] For the same reason, in *Alasdair Ross Anderson et al v. Republic of Costa Rica*, the tribunal stated that considering the all-encompassing nature of the respondent's defence, a finding of illegality by the tribunal "would constitute a complete bar to the entire case advanced" by the claimants.[12] Furthermore, it is arguable, and it was shown in this Thesis, that the more the courts of the host state are engaged directly or indirectly in an investment treaty arbitration, the more is the law of the host state engaged (*qui elegit judicem elegit jus*) since courts of the host state are obliged and/or tend to apply their own municipal law. Similarly, the more the laws of the host state are engaged in such arbitrations, the more significant becomes the role of the domestic courts of the host state since the best place to find the actual application and interpretation of host state law is the jurisprudence of host state courts. This mutual effect can be properly named as the synergetic interaction between host state law and host state courts in investment treaty arbitrations. In this sense, the role and the function of the laws and the courts of the host state cannot be under-appreciated any longer.

9. I though use the term 'partial revival' of the 'localisation' theory since the laws and the courts of the host state do not necessarily have a say in every investment treaty arbitration case. As to the role of the courts of the host state, it should be mentioned that some investment treaties include the courts of the host state as an available option for the investor to opt for in the case of an investment treaty dispute. Even certain recent treaties have selected the courts of the host state as the only forum the aggrieved investor can refer to in case of an investment treaty claim. In the first situation, i.e., the availability of the courts of the host state amongst other venues, the investor does not usually opt for the courts of the host state when it has the option of international arbitration available unless the arbitration proceedings are deemed much more expensive, the dispute is not of a massive or sensitive nature, or the courts of the host state are well-equipped to justly and fairly deal with investment treaty disputes. As to the second situation, i.e., the courts of the host state being the only available forum to resolve the dispute, two observations come to mind: firstly, despite the recent developments, such approach in investment treaties is not yet widespread and even remains, arguably, even rare. Secondly, if the investor has an arbitration clause in its contract with the host state, it might try to circumvent the bilateral investment treaty's dispute settlement provision by invoking the arbitration clause of the pertinent contract. Bearing this in mind, the answer to the question of whether the second limb of the 'localisation' theory has been completely revived in the context of investment treaty arbitration is in the negative. On the other hand, the relevant matters in which the laws of the host state have a say should firstly arise in a case so that the laws of the host state could play their role. One could very well imagine a case, and there are many out there, in which there is no question of jurisdiction *ratione materiae* at all. Furthermore, when such matters do arise in a case, there could be other matters within the same case which are governed by international law rather than municipal law.[13] Therefore, because the

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[11] *Accession Mezzanine Capital L.P. and Danubius Kereskedöház Vagyonkezelö Zrt. v. Hungary*, ICSID Case No. ARB/12/3, Award, 17 April 2015 [190], [200].

[12] *Alasdair Ross Anderson et al v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010 [43]. See also VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (n 5) 268 (stating that "… jurisdictional questions … may bring foreign investment arbitration to *an abrupt end*…") [emphasis added].

[13] See A Newcombe & L Paradell (n 1) 97 (stating that: "Domestic law has a different role depending on the investment allegedly adversely affected and the treaty standard invoked by the claimant. Thus, the scope of the tribunal's duty to apply domestic law varies from case to case.")

matters regulated or affected by the determinations and/or interventions of the laws and courts of the host state are limited and such matters do not necessarily arise in every single case, the more reasonable characterisation of these new developments would be to label them as 'the partial revival of the localisation theory'. All in all, it is reasonably defendable to say that the 'localisation' theory has been partially revived in the field of investment treaty arbitration with the laws and the courts of the host state occupying more decisive areas in the land of investor-state dispute settlement.

10. Although it is always difficult to predict the future, one can only guess that given the recent trends observed in concluding bilateral and multilateral investment treaties by Western and developing countries, the practice of investment treaty arbitrations, as well as the growing importance to respect the sovereignty of states, the role of the domestic laws and national courts of the host state will be more meaningful and more outstanding as time goes by. This is all happening at a time when Western countries are having their second thoughts on the effectiveness and legitimacy of international arbitration as a means for resolving investment treaty disputes. This has apparently concerned some so far as to label these developments as the 'emergence of a 'NEO-NIEO''[14] or "re-statification" of investment dispute settlement.[15] Therefore, the current movement seems to be towards the 'localisation' rather than 'internationalisation'.
11. The strong trend towards 'localisation' when coupled with the current backlash against the legitimacy of investment treaty arbitration could eventually culminate in the total collapse of the investment treaty arbitration system. This, in turn, among other things, may hamper the rule of law in the international economy sphere.
12. To avoid such an outcome, the path forward is to clearly recognise the role of the laws and the courts of the host state in the resolution of investment treaty disputes. This will give substantial comfort to host states. In this way, they would sense that the resolution of investment treaty cases takes place by paying due heed to their laws and judicial systems. In such a scenario, host states would not feel alienated from the system and would appreciate investment treaty arbitral awards more than they do currently.
13. At the same time, it is imperative to regulate the role of these local elements and circumscribe their function in the resolution of investment treaty cases. If this latter exercise is not carried out properly, the local elements will progressively encroach on arbitration and governance of international law on issues of merits and responsibility which may lead either to the total annihilation of the system or its significant alteration.

[14] CN Brower & S Melikian 'We Have Met The Enemy And He Is US!' Is the Industrialized North 'Going South' on Investor–State Arbitration?' (2015) 31(1) Arb Int'l 19–26.

[15] CN Brower & S Blanchard, 'From "Dealing in Virtue" to "Profiting from Injustice": The Case Against "Re-Statification" of Investment Dispute Settlement' (2014) 55 Harvard International Law Journal Online.

## Summary

It was submitted and shown in this Thesis that, in addition to the provisions of investment treaties themselves, the applicable law to bilateral and multilateral investment treaties is a combination of domestic law and international law. This piece of work analysed the eventualities in which domestic law is applied in investment treaty arbitrations as 'fact' and as 'law'. With a particular focus on the application of the domestic law in the all-important and threshold issues of subject-matter jurisdiction, this Thesis examined various situations in which domestic law might be applied as 'law' when determining matters concerning jurisdiction *ratione materiae*, the basis of such application, the modality of the ascertaining the contents of domestic law, and the consequences of the application of domestic law to the subject-matter jurisdiction equation of an investment treaty arbitration proceeding. Furthermore, in addition to the focus on the role of domestic law in subject-matter jurisdiction, the more recent significant roles occupied by the courts of the host state in the resolution of investor-state disputes were also examined in this Thesis in light of the new developments in investment arbitration jurisprudence and the terms of more recent investment treaties. Being mindful of the analyses conducted herein, it has now become clear that through the gradual insertion of local elements into investment treaties (i.e., domestic laws and domestic courts) and through the developments in investment treaty arbitration practice, nowadays, one can see that investment treaty arbitrations are 'localised' to some extent, meaning that host states have managed to effectively 'relocalise' their legal relationship with foreign investors at least to some degrees. In other words, the host states, in particular through recent developments, have reasserted the control they had lost when their cherished 'localisation' theory was struck by the flood of 'internationalisation' and the fatal hurricane of bilateral investment treaties.

Through the analysis carried out in Chapters 1-4 of this Thesis, I was able to draw certain general conclusions.

Firstly, it was shown in Chapter 1 that, irrespective of the broad formulation of the applicable law clause of the underlying investment treaty, the role of domestic law of the host state in determining many jurisdictional and substantive issues is pervasive. It was also shown that whereas domestic law acts mostly as 'fact' in the determination of matters concerning merits, it usually wears its 'applicable law' cloak when dealing with matters of jurisdiction, in particular, when addressing the all-important subject-matter jurisdiction of an investment treaty tribunal. Indeed, many of the issues concerning jurisdiction *ratione materiae* have a direct or an indirect link with the laws of the host state. Such matters include the definition and determination of rights comprising investments, the legality of investments, and, in certain cases, the approval of the investment. I also discussed in Chapter 1 that there are two main legal grounds to justify the application of the internal laws of the recipient state for the purpose of identifying rights over properties and specifying the legality or illegality of an investment. It was demonstrated in Chapter 1 of this Thesis that domestic law of the host state applies to the above-mentioned topics of subject-matter jurisdiction either because the contracting parties to the investment treaty have expressly or implicitly agreed so or because the nature of the issue requires the application of host state law. In the latter situation, domestic law applies because the matter in question is one which is related to the sovereignty of the host state as to which general international law usually does not have a rule to apply. In such situations, absent an agreement by the state contracting parties in the treaty itself or through subsequent agreement or subsequent practice regarding the definition and/or determination of the pertinent matter, general principles of law call for the application of domestic law to the matters concerned. It was also established in

Chapter 1 of this Thesis that a proper conflict of laws analysis indicates that it is usually the law of the host state which has the last say on these matters of subject-matter jurisdiction.

In Chapter 2 of this Thesis, dealing specifically with the question of determining the legality of the investment in accordance with the host state law, I demonstrated that the municipal laws of the host state apply to this question principally because a majority of investment treaties make express or implicit references to the host state laws when determining whether an investment has been made lawfully or not. In addition, I also showed that when the purpose is protecting an investment by international law, general principles of law also require the application of host state laws to the question of the lawfulness of an investment. In this sense, as per general principles of law, investments made in contravention of host state laws are not protected by international law. Therefore, it was said in Chapter 2 that even in circumstances where the underlying investment treaty has no reference to the application of the local laws of the recipient country, the latter laws should determine whether an investment has been made legally. Next, I dealt with the 'temporal', 'formal', and 'substantive' scope of the legality requirement. As to the less controversial 'temporal' and 'formal' aspects of the legality requirement, I concluded that depending on the formulation of the legality requirement, all the binding and enforceable laws and regulations of the host state in force at the time of establishing the investment shall be considered in the analysis that an investment treaty tribunal should undertake when deciding whether an investment has been made lawfully in accordance with host state laws. Turning to the more challenging question of the 'substantive' ambit of the legality requirement, I devoted a lengthy discussion to reviewing relevant investment treaty arbitration practice – which proved to be inconsistent – doctrinal authorities, and treaty interpretation principles, ultimately coming to the conclusion that the 'substantive' reach of the legality requirement extends to the fundamental laws of the host state (including its Constitution, its organic laws, and its mandatory laws) as well as its ordinary laws. As to the second group, i.e., ordinary laws, I concluded that the violation of such laws triggers the legality requirement only when these laws are infringed for the purpose of securing the investment or assuring the profitability of the investment. Finally, I addressed the consequences of the application of host state law to the legality requirement, concluding that a finding by an investment treaty tribunal to the effect that an investment has been made in violation of host state laws culminates in dismissing the case for lack of jurisdiction *ratione materiae*.

Next, in Chapter 3, this time analysing another aspect of subject-matter jurisdiction, I dealt with the question of the role of the laws of the host state in determining the creation and existence of rights/interests constituting investments. At the outset, I showed that, unless otherwise agreed in the treaty itself, customary international law has no rules to regulate issues concerning property law. Such issues are, thus, exclusively answered by reference to domestic laws. General principles of law and conflict of laws analyses corroborate this understanding. Indeed, in most cases, a conflict of laws survey ends up in the application of host state law either pursuant to a *lex situs* or a *lex contractus* analysis. In Section One of this Chapter, reference was also made to certain investment treaties which make this point clear, i.e., that the creation and existence of rights/interests underlying investments should be determined by referring to the local laws of the host state. Furthermore, it was shown in that Chapter that if an analysis pursuant to domestic law comes to the conclusion that there did not exist a legally binding and enforceable right/interest at the time of the alleged investment, the investment treaty tribunal should reject the case for want of subject-matter jurisdiction.

Finally, I also examined the various aspects of specific property and contractual law issues that an investment treaty tribunal may come across that are governed by host state law. It was submitted by reference to investment treaty arbitration practice that the laws and the regulations of the host state supply answers to these particular questions, such as definition of property, the conditions of transfer of title, and whether the alleged contractual right is binding and enforceable. Through this discussion, it was readily apparent that although in some areas the general application of host state law is clear, when it comes to the actual application of the domestic law to specific issues of legality and existence of rights underlying the investment, the discussion becomes more nuanced.

Finally, Part I of the Thesis was concluded by outlining the methods of ascertaining the contents of the host state law. As it was set out in Chapter 4, there are various methods for ascertaining the contents of host state law, including the text of the legal provisions of host state law, expert testimony on matters of domestic law, and the rulings of the courts of the host state. It was indicated in this Chapter that amongst all of the possible means, the prime tool for ascertaining the contents of the host state law is the decisions and judicial practices of host state courts.

Bearing in mind the significance of domestic law of the host state in settling certain subject-matter jurisdiction issues as described above, i.e., the creation and existence of rights/interests over properties and assets and the legality of investment, domestic law of the host state plays a prominent role in determining the jurisdiction *ratione materiae* of an investment treaty tribunal, leaving very little playing field for international law in this respect.[1] Indeed, whilst it is the domestic law of the host state that determines whether valid and enforceable rights exist, the role of international law would be to determine whether such rights are protected by the treaty.[2] Being mindful of these observations, although much will depend on how the case is pleaded in each individual dispute, generally speaking, it is now arguable that domestic law has indeed "frequent centrality to the outcome of the case".[3] In this light, it cannot be argued that, in international disputes, municipal laws function merely as 'facts'.[4] Surely, one can now

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[1] One possible role for international law could be providing lists of limitations, exclusions, and exceptions in the 'definitions' clause of an investment treaty or defining the terms 'property' or 'asset' directly by an agreement in the treaty or through subsequent agreement and/or subsequent practice.

[2] M Sasson, *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer Law International 2017) 103.

[3] In 2017, Jarrod Hepburn concluded with dismay that "the place of domestic law in [investment treaty] arbitrations has received somewhat less attention, notwithstanding its frequent centrality to the outcome of the case …" J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 3-4. Additionally, already in 2003, Douglas had observed that: "With disturbing frequency, questions of municipal law relating to aspects of the investment are brushed aside as peripheral or dealt with superficially by tribunals …" Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (2003) 74 BYIL 273. See also VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (2006) 23(4) J Int'l Arb 287 (characterising the role of the national law of the host state in foreign investment treaty arbitrations as 'vital' and 'enduring'.)

[4] In *Certain German Interests in Polish Upper Silesia*, for instance, the PCIJ held that:

> [f]rom the standpoint of International Law and of the Court which is its organ, municipal laws are merely facts which express the will and constitute the activities of States, in the same manner as do legal decisions or administrative measures.

See *Certain German Interests in Polish Upper Silesia* (*Germany v. Poland*), Judgment, P.C.I.J. Rep. Series A, No. 7, 1926 (25 May 1926) p 19. See also *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL *(*formerly *EnCana Corporation v. Government of the Republic of Ecuador)*, Partial Dissenting Opinion of Horacio A. Grigera Naon, 30 December 2005 [12] (disagreeing with the application of domestic law to the question of the existence of investment and stating that "[…] the local laws, administrative acts and practices

fairly criticise an opinion which treats local laws as mere 'facts' in investment treaty arbitrations.[5] Furthermore, it is not even accurate to argue that, when applied as 'law', domestic law will be confined to certain incidental and preliminary questions.[6] In point of fact, one could firmly say that domestic law applies to a number of preliminary but fundamental questions in an investment treaty arbitration. In particular, through these discussions, it was shown that domestic law of the host state supplies the 'substantive aspects' of the rights underlying investments. The substantive aspects include the existence as well as the legality of a property right.[7]

Part II of this work commenced its mission by narrating the history, contents, and the fate of the classical 'localisation' theory. There, it was discussed that the backbone idea of the 'localisation' theory was that the fate of an investment contract dispute should be decided by the laws and the courts of the host state. Put differently, those who supported the 'localisation' theory put forward the viewpoint that the applicable law of foreign investment contracts should be the municipal laws of the host state and that any dispute arising from such contracts should be decided by the courts of the host state. Chapter 5 of this Thesis addressed this theory and described how it was wiped out by the developed countries. This Chapter was concluded by looking into the phenomenon of bilateral investment treaties which were effectively the last terminating effort for the annihilation of the 'localisation' theory.

Thereafter, in Chapter 6, it was shown that both the more recent investment treaty arbitration practice, and to some extent, the trends in investment treaty-making attest to the fact that the role of domestic law in investment treaty arbitrations, in particular, and as stated in Chapters 2 and 3 of the Thesis, in matters concerning jurisdiction *ratione materiae* is nowadays more outstanding and clear. For instance, if one were to consider previous case law which touched upon such matters, one would have most probably faced silence on the role of the host state law by the arbitral tribunal or would have witnessed that the tribunal would have merely alluded to such a role without being elaborative on the point. One reason that could explain the previous approach could be the unfamiliarity of arbitrators with domestic law or their hesitance to vocally apply

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and other conduct attributable to the host State at the moment they had the effect of operating the deprivation of property, are *facts* to be freely evaluated by the arbitrators to determine if the foreign investor's entitlement to protection under international law has been infringed at a specific moment in time or not."); *Vladimir Berschader and Moïse Berschader v. The Russian Federation*, SCC Case No. 080/2004, Award, 21 April 2006 [96] (stating that: "The Vienna Convention provides no role for the domestic law of contracting states in the interpretation of international treaties. Therefore, in the instant case, it is clear that Russian national law is of no relevance in this regard. While Russian law may be relevant in establishing certain factual circumstances involved in the merits of the case, it has no role to play in determining the jurisdiction of the Tribunal."); *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. The Argentine Republic*, ICSID Case No. ARB/09/1, Decision on Jurisdiction, 21 December 2012 [217]-[218] (holding that reference to domestic law in certain jurisdictional areas is for the purpose of determining "a question of fact"); R Jennings & A Watts (eds), *Oppenheim's International Law* (Vol. 1, 9th edn, Longman 1992) 83 (stating that: "From the standpoint of international law, a national law is generally regarded as a fact with reference to which rules of international law have to be applied, rather than as a rule to be applied on the international plane as a rule of law; and insofar as the International Court of Justice is called upon to express an opinion as to the effect of a rule of national law it will do so by treating the matter as a question of fact to be established as such rather than as a question of law to be decided by the court"); G Sacerdoti, 'Investment Arbitration under ICSID and UNCITRAL Rules: Prerequisites, Applicable Law, Review of Awards' (2004) 19(1) ICSID Rev-FILJ 25-26.

[5] M Sasson (n 2) 1-3.

[6] O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 108; C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (2014) 1(1) McGill Journal of Dispute Resolution 17 (where he states that in such situations domestic law is "incidentally applied").

[7] M Sasson (n 2) 147.

domestic law in an international dispute. However, if one considers the current practice, one realises that investment treaty arbitral tribunals are usually more express on this reality and deal with the role of the host state law in a more comprehensive manner.

Furthermore, it was argued in Chapter 7 that the more recent practice of investment treaty arbitration as well as trends in treaty rulemaking attest to the fact that the courts of the host state have nowadays a much more prominent role through interventions and determinations on various issues related directly or indirectly to matters in dispute in investment treaty arbitrations. For instance, it was shown that when there is a question about the interpretation of domestic law, investment treaty tribunals tend to refer to the practice and rulings of the courts of the host state in order to determine the meaning and the scope of the term in question. Furthermore, in many instances, a prerequisite of admissibility of the case or finding of a violation of a substantive standard of the investment treaty is that the investor should have had recourse to the local remedies in the first place.

These developments in investment treaty law with regard to the laws and the courts of the host state, taken overall, leave any reasonable bystander with one plain conclusion: The 'localisation' theory has to some extent resurfaced. This is not to suggest that these developments have fully revived the 'localisation' theory. To be sure, one could only strongly argue for a 'partial' revival of the 'localisation' theory. I use the phrase 'revival of the localisation theory' because the new developments have brought back to life the determinative roles of the host state law and host state courts, the two pillars of the 'localisation' theory, in international investment disputes. Furthermore, these determinations by the laws and the courts of the host state are indeed effective and important since, in certain cases, the determination by the laws of the host state, or the courts of the host state for that matter, is the end of the story for a significant part or all of the case. In one of his earlier articles on investment treaty arbitration, Schreuer describes investment arbitration as a 'voyage' by the sea. He warns that before "embarkation, the passengers need to have their passports checked", otherwise, there will be no journey.[8] The arbitral tribunal sets a passport check for investors to ascertain jurisdiction. If the passport is not valid or there is no visa, there will be no journey at all. Assume that the preliminary point in dispute in an investor-state arbitration is whether the contract constituting alleged contractual rights has been validly entered into under the municipal law of the host state. If the answer to this question is negative, then, as far as the alleged contractual rights in question are concerned, no claim can be upheld. Indeed, even if a given claim is very strong on the merits, for instance, a viable expropriation claim, but the case suffers from the lack of a subject-matter jurisdiction element, like illegality pursuant to the host state law or the non-recognition of the alleged right/interest by the host state law, the claimant's case would still fail. In *Accession Mezzanine v. Hungary*, in spite of the fact that the tribunal had noted and recognised the wrongfulness of the respondent's conduct in the tender process, it nevertheless dismissed the claimant's case for lack of jurisdiction.[9] For the same reason, in *Alasdair Ross Anderson et al v. Republic of Costa Rica*, the tribunal stated that considering the all-encompassing nature of the respondent's defence, a finding of illegality by the tribunal "would constitute a complete bar to the entire case advanced"

[8] C Schreuer, 'Investment Arbitration - A Voyage of Discovery' (2005) 2(5) TDM 4.

[9] *Accession Mezzanine Capital L.P. and Danubius Kereskedöház Vagyonkezelö Zrt. v. Hungary*, ICSID Case No. ARB/12/3, Award, 17 April 2015 [190], [200].

by the claimants.[10] Furthermore, it is arguable, and it was shown in this Thesis, that the more the courts of the host state are engaged directly or indirectly in an investment treaty arbitration, the more is the law of the host state engaged (*qui elegit judicem elegit jus*) since courts of the host state are obliged and/or tend to apply their own municipal law. Similarly, the more the laws of the host state are engaged in such arbitrations, the more significant becomes the role of the domestic courts of the host state since the best place to find the actual application and interpretation of host state law is the jurisprudence of host state courts. This mutual effect can be properly named as the synergetic interaction between host state law and host state courts in investment treaty arbitrations. In this sense, the role and the function of the laws and the courts of the host state cannot be under-appreciated any longer.

I though use the term 'partial revival' of the 'localisation' theory since the laws and the courts of the host state do not necessarily have a say in every investment treaty arbitration case. As to the role of the courts of the host state, it should be mentioned that some investment treaties include the courts of the host state as an available option for the investor to opt for in the case of an investment treaty dispute. Even certain recent treaties have selected the courts of the host state as the only forum the aggrieved investor can refer to in case of an investment treaty claim. In the first situation, i.e., the availability of the courts of the host state amongst other venues, the investor does not usually opt for the courts of the host state when it has the option of international arbitration available unless the arbitration proceedings are deemed much more expensive, the dispute is not of a massive or sensitive nature, or the courts of the host state are well-equipped to justly and fairly deal with investment treaty disputes. As to the second situation, i.e., the courts of the host state being the only available forum to resolve the dispute, two observations come to mind: firstly, despite the recent developments, such approach in investment treaties is not yet widespread and even remains, arguably, even rare. Secondly, if the investor has an arbitration clause in its contract with the host state, it might try to circumvent the bilateral investment treaty's dispute settlement provision by invoking the arbitration clause of the pertinent contract. Bearing this in mind, the answer to the question of whether the second limb of the 'localisation' theory has been completely revived in the context of investment treaty arbitration is in the negative. On the other hand, the relevant matters in which the laws of the host state have a say should firstly arise in a case so that the laws of the host state could play their role. One could very well imagine a case, and there are many out there, in which there is no question of *ratione materiae* jurisdiction at all. Furthermore, when such matters do arise in a case, there could be other matters within the same case which are governed by international law rather than municipal law. Therefore, because the matters regulated or affected by the determinations and/or interventions of the laws and courts of the host state are limited and such matters do not necessarily arise in every single case, the more reasonable characterisation of these new developments would be to label them as 'the partial revival of the localisation theory'. All in all, it is reasonably defendable to say that the 'localisation' theory has been partially revived in the field of investment treaty arbitration with the laws and the courts of the host state occupying more decisive areas in the land of investor-state dispute settlement.

Although it is always difficult to predict the future, one can only guess that given the recent trends observed in concluding bilateral and multilateral investment treaties by

[10] *Alasdair Ross Anderson et al v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010 [43]. See also VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (n 3) 268 (stating that "… jurisdictional questions … may bring foreign investment arbitration to *an abrupt end*…") [emphasis added].

Western and developing countries, the practice of investment treaty arbitrations, as well as the growing importance to respect the sovereignty of states, the role of the domestic laws and national courts of the host state will be more meaningful and more outstanding as time goes by. This is all happening at a time when Western countries are having their second thoughts on the effectiveness and legitimacy of international arbitration as a means for resolving investment treaty disputes. This has apparently concerned some so far as to label these developments as the 'emergence of a 'NEO-NIEO''[11] or 're-statification' of investment dispute settlement.[12] Therefore, the movement seems to be towards the 'localisation' rather than 'internationalisation'.

[11] CN Brower & S Melikian 'We Have Met The Enemy And He Is US!' Is the Industrialized North 'Going South' on Investor–State Arbitration?' (2015) 31(1) Arb Int'l 19–26.

[12] CN Brower & S Blanchard, 'From "Dealing in Virtue" to "Profiting from Injustice": The Case Against "Re-Statification" of Investment Dispute Settlement' (2014) 55 Harvard International Law Journal Online.

## Samenvatting (Dutch Summary)

### De rol van het nationaal recht van de gaststaat in de vaststelling van de materiële bevoegdheid van investeringstribunalen: de gedeeltelijke herleving van de 'localisatie-theorie'

In dit proefschrift is aangetoond dat, naast de bepalingen van investeringsverdragen zelf, het toepasselijke recht inzake bilaterale en multilaterale investeringsverdragen een combinatie is van nationaal recht en internationaal recht. Dit proefschrift heeft de potentiële omstandigheden waarin het nationale recht in investeringsarbitrage wordt toegepast als 'feit' en als 'recht' geanalyseerd. Met bijzondere aandacht voor de toepassing van het nationale recht in de belangrijke kwestie van de materiële bevoegdheid van arbitragetribunalen, onderzocht dit proefschrift de verschillende situaties waarin het nationale recht zou kunnen worden toegepast als 'recht' bij de bepaling van de materiële bevoegdheid van tribunalen, de basis van een dergelijke toepassing, de modaliteit voor het vaststellen van de inhoud van het nationale recht, en de gevolgen van de toepassing van het nationale recht bij de vaststelling van de bevoegdheid van een tribunaal op basis van een investeringsverdrag. Bovendien is in dit proefschrift, naast de aandacht voor de rol van het nationale recht in de materiële bevoegdheid, ook de belangrijke rol van de nationale rechtbanken van het gastland bij de beslechting van geschillen tussen investeerders en staten onderzocht in het licht van nieuwe ontwikkelingen in de rechtspraak van investeringstribunalen en de bepalingen van recente investeringsverdragen. Uit die analyse blijkt dat door de geleidelijke invoering van bepalingen betreffende het nationaal recht en nationale rechtbanken in investeringsverdragen, gekoppeld aan ontwikkelingen in de arbitragepraktijk en investeringsverdragen, investeringsarbitrage tot op zekere hoogte 'gelokaliseerd' is. Dit betekent dat gaststaten erin zijn geslaagd hun juridische relatie met buitenlandse investeerders op zijn minst tot op zekere hoogte te 're-lokaliseren'. Met andere woorden, v hebben, met name door recente ontwikkelingen, de controle, die ze enigszins verloren hadden toen de 'lokalisatietheorie' overtroffen werd door de 'internationalisering' en de toevloed aan bilaterale investeringsverdragen, verstevigd.

Door de analyse in de hoofdstukken 1-4 van dit proefschrift heb ik bepaalde algemene conclusies kunnen trekken.

In de eerste plaats is in hoofdstuk 1 aangetoond dat, ongeacht de brede formulering van bepalingen omtrent het toepasselijke recht in investeringsverdragen, de rol van het nationale recht van de gaststaat bij het bepalen van de bevoegdheid van een tribunaal en de gegrondheid van de zaak alomtegenwoordig is. Er werd ook aangetoond dat terwijl het nationale recht meestal als 'feit' aanzien wordt bij het bepalen van de gegrondheid van de zaak, datzelfde nationale recht meestal als 'toepasselijke recht' aanzien wordt bij de behandeling van bevoegdheidskwesties, in het bijzonder bij de behandeling van de materiële bevoegdheid van een investeringstribunaal. Verschillende vraagstukken betreffende de materiële bevoegdheid van een investeringstribunaal hebben immers een directe of indirecte band met het recht van de gaststaat. Dergelijke vraagstukken omvatten onder meer de definitie en de vaststelling van de rechten die gepaard gaan met investeringen, de rechtmatigheid van investeringen en, in bepaalde gevallen, de formele goedkeuring van de investering. In hoofdstuk 1 werd ook besproken dat er twee belangrijke juridische gronden zijn om de toepassing van het recht van de gaststaat te rechtvaardigen: om de eigendomsrechten van buitenlandse investeerders te identificeren en om de (on)rechtmatigheid van een investering vast te stellen. In hoofdstuk 1 van dit

proefschrift is aangetoond dat het recht van de gaststaat van toepassing is op de bovengenoemde aspecten van de materiële bevoegdheid, hetzij omdat de verdragsluitende partijen bij het investeringsverdrag dit uitdrukkelijk of impliciet zijn overeengekomen, hetzij omdat de toepassing van het recht van de gaststaat volgt uit de aard van de kwestie die ter beoordeling ligt. In het laatste geval is het nationale recht van toepassing omdat het gaat om een kwestie die verband houdt met de soevereiniteit van de gaststaat ten aanzien waarvan het algemeen internationaal recht geen toepasselijk regel heeft. In dergelijke situaties, en in de afwezigheid van een overeenkomst door de verdragsluitende staten of door een daaropvolgende bijzondere overeenkomst of praktijk van die staten met betrekking tot de definitie en/of bepaling van de relevante kwestie, vereisen algemene rechtsbeginselen de toepassing van het nationale recht op de betrokken aangelegenheden. In hoofdstuk 1 van dit proefschrift is ook vastgesteld dat een correcte analyse van het conflictenrecht met zich meebrengt dat het meestal het recht van de gaststaat is die deze materie bepaalt.

In hoofdstuk 2 van dit proefschrift, dat specifiek het vraagstuk inzake de vaststelling van de rechtmatigheid van de investering conform het recht van de gaststaat behandelt, werd aangetoond dat het voornamelijk het recht van de gaststaat is dat op dit vraagstuk van toepassing is omdat een meerderheid van de investeringsverdragen expliciet of impliciet naar deze verwijzen bij het bepalen van de rechtmatigheid van de investering. Bovendien heb ik ook aangetoond dat als het internationale recht inderdaad als doel heeft internationale investeringen te beschermen, algemene rechtsbeginselen ook de toepassing van het recht van de gaststaat op de rechtmatigheid van een investering vereisen. Bijgevolg worden, volgens die algemene rechtsbeginselen, investeringen die in strijd zijn met het recht van de gaststaat niet beschermd door het internationale recht. Daarom werd in hoofdstuk 2 aangetoond dat zelfs indien het onderliggend investeringsverdrag niet verwijst naar de toepassing van het recht van de gaststaat, deze toch zal bepalen of een investering rechtmatig is. Vervolgens ging ik in op de ‘temporele’, ‘formele’ en ‘inhoudelijke’ omvang van de rechtmatigheidsvereiste. Wat de minder controversiële ‘tijdelijke’ en ‘formele’ aspecten van het rechtmatigheidsvereiste betreft, concludeerde ik dat, afhankelijk van de formulering van de rechtmatigheidsvereiste, bij de analyse, die een tribunaal op basis van een investeringsverdrag moet ondernemen bij de beslissing of een investering in overeenstemming is met het recht van de gaststaat, rekening gehouden moet worden met alle bindende en afdwingbare wetten en regels van de gaststaat die van kracht waren op het ogenblik van de aanvang van de investering. Wat de moeilijkere vraag van de ‘inhoudelijke’ strekking van de rechtmatigheidsvereiste betreft, wijdde ik een lange discussie aan een overzicht van de relevante arbitragebepalingen in investeringsverdragen -die inconsistent bleken te zijn-, de rechtsleer en de algemene beginselen inzake verdragsinterpretatie, om uiteindelijk tot de conclusie te komen dat de ‘inhoudelijke’ strekking van de rechtmatigheidsvereiste zich uitstrekt tot de fundamentele wetgeving van de gaststaat (hetzij de grondwet, de organische wetten en de dwingende wetten) evenals de ‘gewone’ wetgeving. Wat betreft de tweede groep, de ‘gewone’ wetten, concludeerde ik dat de schending van dergelijke wetten alleen de rechtmatigheidsvereiste zou kunnen schenden indien deze wetten worden geschonden met als doel de investering veilig te stellen of de winstgevendheid van de investering te verzekeren. Tot slot heb ik de gevolgen van de toepassing van het recht van de gaststaat op de rechtmatigheidsvereiste behandeld en geconcludeerd dat de bevinding door een arbitragetribunaal dat een investering gemaakt is in strijd met het recht van de gaststaat, resulteert in het afwijzen van de zaak wegens gebrek aan materiële bevoegdheid.

Vervolgens heb ik in hoofdstuk 3 een ander aspect van de materiële bevoegdheid geanalyseerd, namelijk het vraagstuk van de rol van het recht van de gaststaat bij het bepalen van het bestaan van de rechten en/of belangen die gepaard gaan met de investering. Eerst heb ik aangetoond dat, tenzij anders overeengekomen in het verdrag zelf, het internationale gewoonterecht geen regels bevat met betrekking tot eigendomsrecht. Dergelijke kwesties worden derhalve uitsluitend beantwoord door verwijzing naar en toepassing van nationale wetgeving. Algemene rechtsbeginselen en het conflictenrecht bevestigen dit. In de meeste gevallen eindigt een analyse van het conflictenrecht inderdaad in de toepassing van het recht van de gaststaat, op basis van hetzij de *lex situs* of de *lex contractus*. In deel één van dit hoofdstuk werd verwezen naar bepaalde investeringsverdragen die dit ook duidelijk stellen - het bestaan van rechten/belangen die gepaard gaan met de investeringen moeten bepaald worden door verwijzing naar het recht van de gaststaat. Bovendien is in dat hoofdstuk aangetoond dat als men op basis van een analyse op grond van het nationale recht tot de conclusie komt dat er op het moment van de aanvang van de investering geen juridisch bindend of afdwingbaar recht/belang bestond, het investeringstribunaal de zaak moet afwijzen wegens gebrek aan materiële bevoegdheid. Tot slot heb ik ook de verschillende aspecten van specifieke eigendoms- en contractuele kwesties, die een investeringstribunaal tegenkomt en die worden beheerst door het recht van de gaststaat, onderzocht. Met verwijzing naar de praktijk van investeringstribunalen is aangevoerd dat het de wetgeving en ander regels van het gastland is die een antwoord geven op deze specifieke vragen, waaronder de definitie van 'eigendom', de voorwaarden voor eigendomsoverdracht en de vraag of het vermeende contractuele recht effectief bindend en afdwingbaar is. Uit deze discussie bleek al snel dat, hoewel op sommige gebieden de algemene toepassing van het recht van de gaststaat duidelijk is, de discussie over de feitelijke toepassing van de nationale wetgeving op specifieke kwesties zoals de rechtmatigheid en het bestaan van aan de investering ten grondslag liggende rechten genuanceerder is.

Tenslotte werd deel I van het proefschrift afgesloten met de methode voor het vaststellen van de inhoud van de wetgeving van het gastland. Zoals in hoofdstuk 4 werd uiteengezet, bestaan er verschillende methoden om de inhoud van het recht van de gaststaat te bepalen, waaronder de tekst zelf van de wetgeving van het gastland, 'expert opinions' van deskundigen over nationale aangelegenheden, en de uitspraken van de rechtbanken van de gaststaat. In dit hoofdstuk is aangegeven dat van alle mogelijke methoden, het voornaamste middel om de inhoud van het recht van de gaststaat vast te stellen, de uitspraken en praktijken van de rechtbanken van het gastland zijn.

Gezien het belang van het recht van de gaststaat bij het regelen van bepaalde kwesties inzake de materiële bevoegdheid, zoals hierboven beschreven, d.w.z. het creëren en het bestaan van rechten/belangen over eigendom en activa en de rechtmatigheid van investeringen, speelt het recht van de gaststaat een prominente rol bij het bepalen van de materiële bevoegdheid van een tribunaal. Dit laat weinig ruimte aan het internationaal recht.[1] Hoewel het recht van de gaststaat bepaalt of er geldige en afdwingbare rechten bestaan, bestaat de rol van het internationale recht er evenwel in om te bepalen of dergelijke rechten door het verdrag worden beschermd. [2] Gezien deze

[1] Een mogelijk rol voor het international recht kan erin bestaan een lijst met beperkingen, uitluistingen, en uitzonderingen te voorzien in deverdragsbepaling die 'investering' definieert, of de bepaling die de termen 'eigendom' of 'activa' definieert, hetzij in het verdrag zelf of in een naderhand gesloten overeenkomst of praktijk van de de verdragsstaten.

[2] M Sasson, *Substantive Law in Investment Treaty Arbitration: The Unsettled Relationship between International Law and Municipal Law* (Kluwer Law International 2017) 103.

observatie, en alhoewel veel zal afhangen van hoe de zaak in elk individueel geschil wordt bepleit, kan in het algemeen nu geargumenteerd worden dat het nationale recht inderdaad "frequent centrality to the outcome of the case" heeft.[3]. In dit opzicht kan niet worden betoogd dat nationaal recht in internationale geschillen slechts als 'feit' fungeert.[4] Om die reden kan men terecht de mening die nationaal recht behandelt als een louter 'feit' in investeringsarbitrage bekritiseren.[5] Bovendien is het niet juist te beweren dat, wanneer toegepast als 'recht', het nationale recht beperkt zal blijven tot bepaalde incidentele en voorlopige kwesties.[6] Men kan terecht stellen dat het nationale recht van toepassing is op een aantal inleidende, maar tegelijk fundamentele vragen in investeringsarbitrage. In het bijzonder is door deze discussie aangetoond dat het recht van de gaststaat de 'inhoudelijke aspecten' van de onderliggende rechten beheerst. De

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[3] In 2017 heeft Jarrod Hepburn geconcludeerd dat "the place of domestic law in [investment treaty] arbitrations has received somewhat less attention, notwithstanding its frequent centrality to the outcome of the case …" J Hepburn, *Domestic Law in International Investment Arbitration* (OUP 2017) 3-4. Te meer, reeds in 2003, had Douglas gesteld dat "With disturbing frequency, questions of municipal law relating to aspects of the investment are brushed aside as peripheral or dealt with superficially by tribunals …" Z Douglas, 'The Hybrid Foundations of Investment Treaty Arbitration' (2003) 74 BYIL 273. Zie ook VC Igbokwe, 'Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations' (2006) 23(4) J Int'l Arb 287 (die de rol van het national recht van de gaststaat in investeringsarbitrage gekaraktereseerd had als 'vital' en 'enduring'.)

[4] In *Certain German Interests in Polish Upper Silesia*, bijvoorbeeld, oordeelde het PHIJ dat:

> [f]rom the standpoint of International Law and of the Court which is its organ, municipal laws are merely facts which express the will and constitute the activities of States, in the same manner as do legal decisions or administrative measures.

Zie *Certain German Interests in Polish Upper Silesia* (*Germany v. Poland*), Judgment, P.C.I.J. Rep. Series A, No. 7, 1926 (25 May 1926) p 19. Zie ook *EnCana Corporation v. Republic of Ecuador*, LCIA Case No. UN3481, UNCITRAL *(*formerly *EnCana Corporation v. Government of the Republic of Ecuador)*, Partial Dissenting Opinion of Horacio A. Grigera Naon, 30 December 2005 [12] (waarbij de toepassing van nationaal recht op de vraag of een 'investering' bestaat, tegengesproken wordt: "[…] the local laws, administrative acts and practices and other conduct attributable to the host State at the moment they had the effect of operating the deprivation of property, are *facts* to be freely evaluated by the arbitrators to determine if the foreign investor's entitlement to protection under international law has been infringed at a specific moment in time or not."); *Vladimir Berschader and Moïse Berschader v. The Russian Federation*, SCC Case No. 080/2004, Award, 21 April 2006 [96] (warring gesteld wordtt: "The Vienna Convention provides no role for the domestic law of contracting states in the interpretation of international treaties. Therefore, in the instant case, it is clear that Russian national law is of no relevance in this regard. While Russian law may be relevant in establishing certain factual circumstances involved in the merits of the case, it has no role to play in determining the jurisdiction of the Tribunal."); *Teinver S.A., Transportes de Cercanías S.A. and Autobuses Urbanos del Sur S.A. v. The Argentine Republic*, ICSID Case No. ARB/09/1, Decision on Jurisdiction, 21 December 2012 [217]-[218] (waarin voorgehouden wordt dat de referentie naar nationaal recht in bepaalde jurisdictional kwesties las doel heeft bepaalde 'feitelijke kwesties' te beslissen); R Jennings & A Watts (eds), *Oppenheim's International Law* (Vol. 1, 9th edn, Longman 1992) 83 (waarin gesteld wordt dat : "From the standpoint of international law, a national law is generally regarded as a fact with reference to which rules of international law have to be applied, rather than as a rule to be applied on the international plane as a rule of law; and insofar as the International Court of Justice is called upon to express an opinion as to the effect of a rule of national law it will do so by treating the matter as a question of fact to be established as such rather than as a question of law to be decided by the court"); G Sacerdoti, 'Investment Arbitration under ICSID and UNCITRAL Rules: Prerequisites, Applicable Law, Review of Awards' (2004) 19(1) ICSID Rev-FILJ 25-26.

[5] M Sasson (n 2) 1-3.

[6] O Spiermann, 'Applicable Law' in P Muchlinski, F Ortino, and C Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 108; C Schreuer, 'Jurisdiction and Applicable Law in Investment Treaty Arbitration' (2014) 1(1) McGill Journal of Dispute Resolution 17 (waarin gesteld wordt dat in dergelijke situaties national recht incidentieel toegepast wordt).

inhoudelijke aspecten omvatten het bestaan en de rechtmatigheid van een eigendomsrecht. [7]

Deel II van dit werk begon met de geschiedenis, inhoud en de huidige staat van de klassieke 'lokalisatietheorie'. Daar werd besproken dat het voornaamste idee achter de 'lokalisatietheorie' erin bestond dat een geschil over een investeringscontract worden beslist zou moeten door het recht en de rechtbanken van de gaststaat. Anders gezegd, degenen die de 'lokalisatietheorie' steunden, waren de mening toegedaan dat het recht van toepassing op buitenlandse investeringsovereenkomsten het nationaal recht van het gastland moest zijn en dat elk geschil dat voortvloeit uit dergelijke contracten beslecht moest worden door de rechtbanken van het gastland zelf. Hoofdstuk 5 van dit proefschrift ging dieper in op deze theorie en beschreef hoe deze uiteindelijk werd weggevaagd door de Westerse staten. Dit hoofdstuk werd afgesloten met een onderzoek naar het fenomeen van bilaterale investeringsverdragen die het laatste stuk vormden in de complete vernietiging van de 'lokalisatietheorie'.

Vervolgens werd in hoofdstuk 6 aangetoond dat zowel de recentere praktijk van investeringstribunaal als, in zekere mate, recente trends in het sluiten van investeringsverdragen aantonen dat de rol van het nationale recht in investeringsarbitrage, en met name zoals vermeld in de hoofdstukken 2 en 3 van het proefschrift de toepassing van deze op de kwestie van materiële bevoegdheid, duidelijker en meer aanwezig is. Als men bijvoorbeeld eerdere jurisprudentie over dergelijke zaken zou analyseren, zou men hoogstwaarschijnlijk niets vinden over de rol van het recht van de gaststaat vinden, of moeten vaststellen dat deze kwestie door een arbitragetribunaal slechts marginaal besproken werd. Een reden die de vorige benadering zou kunnen verklaren, kan liggen in het feit dat de arbiters onbekend waren met het nationale recht, of aarzelden om expliciet het nationale recht toe te passen in een internationaal geschil. Als men echter de huidige praktijk in ogenschouw neemt, realiseert men zich dat investeringstribunalen gewoonlijk meer uitdrukking geven aan deze realiteit en de rol van de gaststaat op een meer omvattende manier behandelen.

Verder werd in hoofdstuk 7 betoogd dat de recente praktijk van arbitragetribunalen, en de recente trends in het sluiten van investeringsverdragen aantonen dat de rechtbanken van het gastland tegenwoordig een veel prominentere rol spelen door middel van interventies en vaststellingen inzake verschillende kwesties die direct of indirect verband houden met investeringsgeschillen. Er werd bijvoorbeeld aangetoond dat wanneer een vraag betreffende de interpretatie van het nationale recht zich stelt, arbitragetribunalen meestal verwijzen naar de praktijk en uitspraken van de rechtbanken van het gastland om de betekenis en de draagwijdte van de relevante bepaling vast te stellen. Bovendien is in bepaalde gevallen de vereiste dat de investeerder in de eerste plaats gebruik moet maken van de lokale rechtsmiddelen, een ontvankelijkheidvoorwaarde voor de vordering of een voorafgaande voorwaarde om een schending van een inhoudelijke bepaling van het investeringsverdrag vast te stellen.

De ontwikkelingen in investeringsverdragen inzake het recht en de rechtbanken van het gastland, laten in het algemeen een redelijke omstander achter met een duidelijke conclusie: de 'lokalisatietheorie' herleeft enigszins. Dit wil niet zeggen dat deze ontwikkelingen de 'lokalisatietheorie' volledig heeft doen herleven. Men kan immers alleen beargumenteren dat heropleving van de 'lokalisatietheorie' 'gedeeltelijk' is. Ik gebruik de uitdrukking 'herleving van de lokalisatietheorie' omdat de nieuwe ontwikkelingen de bepalende rol van het recht én de rechtbanken van de gaststaat -de twee pijlers van de 'lokalisatietheorie'-, bij internationale investeringsgeschillen hebben

[7] M Sasson (n 2) 147.

doen ‘herleven’. Bovendien is de determinerende rol van het recht en de rechtbanken van de gaststaat effectief en belangrijk, aangezien in sommige geschillen de bepalingen van het recht en uitspraken van de rechtbanken van de gaststaat het einde van het verhaal betekenen. In een van zijn eerdere artikelen over investeringsarbitrage beschrijft Schreuer investeringsarbitrage als een ‘reis’ aan zee. Hij waarschuwt dat voor “inscheping, de passagiers hun paspoorten moeten laten controleren”, omdat er anders geen reis zal zijn.[8] Het arbitragetribunaal stelt een paspoortcontrole in voor beleggers om hun bevoegdheid te bepalen. Als het paspoort niet geldig is of als er geen visum is, zal er helemaal geen reis zijn. Stel dat in een arbitrage tussen een investeerder en een staat, één van de geschilpunten betrekking heeft op de vraag of het contract dat vermeende contractuele rechten met zich meebrengt, geldig is aangegaan onder het recht van het gastland. Indien het antwoord op deze vraag ontkennend is, kan geen enkele vordering worden aanvaard met betrekking tot de vermeende contractuele rechten in kwestie. Zelfs als een bepaalde claim gegrond zou zijn, bijvoorbeeld een gegronde vordering betreffende een onteigening, zal de zaak alsnog falen bij gebrek aan materiële bevoegdheid, wegens onrechtmatigheid op grond van het recht van het gastland, of de niet-erkenning van het vermeende recht/belang door het recht van de gaststaat. In *Accession Mezzanine v. Hungary*, ondanks het feit dat het tribunaal de onrechtmatigheid van het gedrag van de verweerder in het aanbestedingsproces vastgesteld en erkend had, heeft het tribunaal de vordering van de eiser niettemin afgewezen wegens onbevoegdheid.[9] Om dezelfde reden verklaarde het Tribunaal in *Alasdair Ross Anderson et al v. Republic of Costa Rica* dat, gezien de alomvattende aard van de verdediging van de verweerder, een vaststelling van onrechtmatigheid door het tribunaal “would constitute a complete bar to the entire case advanced”.[10] Verder kan geargumenteerd worden, en is in dit proefschrift aangetoond, dat hoe meer de rechtbanken van de gaststaat direct of indirect betrokken zijn bij een investeringsarbitrage, hoe meer het recht van de gaststaat relevant is (*qui elegit judicem elegit jus*), aangezien rechtbanken van het gastland verplicht zijn en/of geneigd zijn hun eigen recht toe te passen. Evenzo, hoe meer het recht van de gaststaat betrokken is bij dergelijke arbitrages, des te belangrijker de rol van de nationale rechtbanken van de gaststaat wordt, aangezien de rechtspraak van de rechtbanken van de gaststaat de beste vindplaats is voor de toepassing en interpretatie van het recht van de gaststaat. Dit wederzijdse effect kan terecht als een synergetische interactie tussen het recht van de gaststaat en de rechtbanken van de gaststaat in investeringsarbitrage worden genoemd. Om die reden kan de rol en de functie van het recht en de rechtbanken van het gastland niet langer worden onderschat.

Ik gebruik evenwel wel de term ‘gedeeltelijke heropleving’ van de ‘lokalisatietheorie’, aangezien het recht en de rechtbanken van het gastland niet noodzakelijkerwijs inspraak hebben in elke investeringsarbitrage. Wat de rol van de rechtbanken van het gastland betreft, moet worden opgemerkt dat sommige investeringsverdragen de rechtbanken van het gastland opnemen als één van de beschikbare opties die de investeerder kan kiezen in het geval van een geschil op basis van een investeringsverdrag. Bepaalde recente verdragen hebben zelfs de rechtbanken van het gastland opgenomen als het

[8] C Schreuer, ‘Investment Arbitration - A Voyage of Discovery’ (2005) 2(5) TDM 4.

[9] *Accession Mezzanine Capital L.P. and Danubius Kereskedöház Vagyonkezelö Zrt. v. Hungary*, ICSID Case No. ARB/12/3, Award, 17 April 2015 [190], [200].

[10] *Alasdair Ross Anderson et al v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award, 19 May 2010 [43]. See also VC Igbokwe, ‘Determination, Interpretation and Application of Substantive Law in Foreign Investment Treaty Arbitrations’ (n 3) 268 (stating that “… jurisdictional questions … may bring foreign investment arbitration to *an abrupt end*…” [emphasis added].

enige forum die de investeerder *moet* gebruiken in het geval van een geschil op basis van een investeringsverdrag. In de eerste situatie -de beschikbaarheid van de rechtbanken van de gaststaat samen met andere opties- kiest de investeerder meestal niet voor de rechtbanken van de gaststaat wanneer de investeerder eveneens kan opteren voor internationale arbitrage, tenzij de arbitrageprocedure als te duur beschouwd worden, het geschil niet complex of gevoelig van aard is, of de rechtbanken van het gastland goed zijn uitgerust om op een rechtvaardige en billijke manier geschillen op basis van investeringsverdragen te behandelen. Wat de tweede situatie betreft, namelijk indien de rechtbanken van het gastland het enige beschikbare forum zijn om het geschil te beslechten, moeten twee opmerkingen gemaakt worden: ten eerste, niettegenstaande de recente ontwikkelingen, is een dergelijke aanpak in investeringsverdragen redelijk beperkt; een dergelijke aanpak blijkt zelfs eerder zeldzaam te zijn. Ten tweede, als er een arbitrageclausule voorzien is in het contract tussen de investeerder en de gaststaat, kan de investeerder proberen het geschillenbeslechtingsforum in het bilaterale investeringsverdrag te omzeilen door een beroep te doen op de arbitrageclausule in het desbetreffende contract. Rekening houdend met deze vaststelling, is het antwoord op de vraag of het tweede onderdeel van de 'lokalisatietheorie' volledig nieuw leven is ingeblazen in de context van investeringsarbitrage dus eerder negatief. Anderzijds moeten de relevante vraagstukken, waarop het recht van de gaststaat van toepassing is, eerst aan de orde komen in een zaak zodat het recht van de gaststaat de haar toegekende rol kan spelen. Men kan zich uiteraard ook voorstellen dat er in sommige zaken, en er zijn effectief verschillende dergelijke zaken, helemaal geen materiële bevoegdheidskwesties spelen. Bovendien, indien er wel materiële bevoegdheidskwesties spelen, kunnen het kwesties zijn die door het internationaal recht eerder dan het recht van de gaststaat beheerst worden. Omdat de aangelegenheden die gereguleerd of beïnvloed worden door de bepalingen en/of interventies van het recht en/of rechtbanken van de gaststaat beperkt zijn, en dergelijke aangelegenheden eveneens niet noodzakelijkerwijs in elk zaak aanwezig zijn, lijkt de karakterisering van deze nieuwe ontwikkelingen als 'gedeeltelijke heropleving van de lokalisatietheorie' bijgevolg gepaster. Al met al is het redelijk verdedigbaar te stellen dat, door de meer beslissende rol die het recht en de rechtbanken van de gaststaat innemen in het beslechten van geschillen tussen staten en investeerders, de 'lokalisatietheorie' op het gebied van investeringsarbitrage gedeeltelijk nieuw leven is ingeblazen.

Hoewel het altijd moeilijk is om de toekomst te voorspellen, kan men alleen maar gissen of de rol van het recht en de rechtbanken van de gaststaat betekenisvoller en belangwekkender zal worden naarmate de tijd verstrijkt, in het licht van de recente trends die zijn waargenomen bij het sluiten van bilaterale en multilaterale investeringsverdragen door Westerse en ontwikkelingslanden, de praktijk van investeringsarbitrage, en het groeiende belang om de soevereiniteit van staten te respecteren. Dit gebeurt overigens op een moment dat Westerse staten twijfels hebben over de effectiviteit en legitimiteit van internationale arbitrage als middel om geschillen op basis investeringsverdragen te beslechten. Dit heeft blijkbaar een danige invloed gehad dat sommigen deze ontwikkelingen aangewezen hebben als 'emergence of a 'NEO-NIEO'' [11] of 're-statification' van de beslechting van investeringsgeschillen.[12] Om die reden lijkt de evolutie meer gericht te zijn op 'lokalisatie' dan op 'internationalisering'.

[11] CN Brower & S Melikian 'We Have Met The Enemy And He Is US!' Is the Industrialized North 'Going South' on Investor–State Arbitration?' (2015) 31(1) Arb Int'l 19–26.

[12] CN Brower & S Blanchard, 'From "Dealing in Virtue" to "Profiting from Injustice": The Case Against "Re-Statification" of Investment Dispute Settlement' (2014) 55 Harvard International Law Journal Online.

# Curriculum Vitae

Reza Eftekhar (Dezfool, 18 July 1986) took his bachelor's degree in law from Shahid Beheshti University of Tehran (*cum laude*). Reza took his LL.M. degree in International Commercial Law from Shahid Beheshti University of Tehran (*cum laude*).

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## International Conventions, Treaties, and International Instruments

### Bilateral Investment Treaties

**Albania**

Agreement between the Kingdom of Spain and the Republic of Albania on the Promotion and Reciprocal Protection of Investments, signed on 05 June 2003, entered into force on 14 January 2004.

**Argentina**

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments, signed on 11 December 1990, entered into force on 19 February 1993.

Agreement between the Government of the Argentine Republic and the Government of the Republic of France for Reciprocal Protection and Promotion of Investments, signed on 03 July 1991, entered into force on 03 March 1993.

Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Argentine Republic, signed on 20 October 1992, entered into force on 01 October 1994.

**Armenia**

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Armenia for the Promotion and Protection of Investments, signed on 27 May 1993, entered into force on 11 July 1996.

**Australia**

Agreement between Australia and the Islamic Republic of Pakistan on the Promotion and Protection of Investments, signed on 07 February 1998, entered into force on 14 October 1998.

**Austria**

Agreement between the Republic of Austria and Malaysia for the Promotion and Protection of Investments, signed on 12 April 1985, entered into force on 01 January 1987.

Agreement between the Republic of Austria and the State of Kuwait for the Encouragement and Reciprocal Protection of Investments, signed on 16 November 1996, entered into force on 22 September 1998.

Agreement between the Republic of Austria and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 11 April 2002, entered into force on 01 December 2003.

Agreement for the Promotion and Protection of Investment between the Government of the Republic of Austria and the Government of the Kyrgyz Republic, signed on 22 April 2016, not yet entered into force.

**Belarus**

Agreement between the Government of the Lebanese Republic and the Government of the Republic of Belarus on the Promotion and Reciprocal Protection of Investments, signed on 19 June 2001, entered into force on 29 December 2002.

**Belgo-Luxemburg Union**

Investment Guarantee Agreement between Malaysia and the Belgo-Luxemburg Union, signed on 22 November 1979, entered into force on 08 February 1982.

Agreement between the Government of the Kingdom of Thailand and the Belgo-Luxemburg Economic Union on the Reciprocal Promotion and Protection of Investments, signed on 12 June 2002, entered into force on 19 September 2004.

Agreement between The Belgium-Luxembourg Economic Union, on the one hand, and Montenegro, on the other hand, on the Reciprocal Promotion and Protection of Investments, signed on 16 February 2010, not yet in force.

**Bosnia and Herzegovina**

Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Islamic Republic of Iran and the Government of Bosnia and Herzegovina, signed on 27 July 1996, entered into force on 02 June 2009.

**Bulgaria**

Agreement between The Government of the People's Republic of Bulgaria and The Government of the Republic of Cyprus on Mutual Encouragement and Protection of Investments, signed on 12 November 1987, entered into force on 18 May 1988.

**Cambodia**

Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of Cambodia and the Kingdom of the Netherlands, signed on 23 June 2003, entered into force on 01 March 2006.

**Canada**

Agreement between the Government of Canada and the Government of the Republic of Ecuador for the Promotion and Reciprocal Protection of Investments, signed on 29 April 1996, entered into force on 06 June 1997 (subsequently terminated).

Agreement between the Government of the Republic of Croatia and the Government of Canada for the Promotion and Protection of Investments, signed on 03 February 1997, entered into force on 30 January 2001.

Agreement between the Government of Canada and the Government of the Republic of Costa Rica for the Promotion and Protection of Investments, signed on 18 March 1998, entered into force on 29 September 1999.

Agreement between the Government of Canada and the Government of the People's Republic of China for the Promotion and Reciprocal Protection of Investments, signed on 09 September 2012, entered into force on 01 October 2014.

Agreement between Canada and Mongolia for the Promotion and Protection of Investments, signed on 08 August 2016, entered into force on 24 February 2017.

**China**

Agreement on Reciprocal Promotion and Protection of Investment between the Government of the People's Republic of China and the Government of the Islamic Republic of Iran, signed on 22 June 2000, entered into force on 01 July 2005.

Agreement between the Government of the People's Republic of China and the Government of the Republic of Cote D'Ivoire on the Promotion and Protection of Investments, signed on 30 September 2002, not yet entered into force.

Agreement between the Government of Canada and the Government of the People's Republic of China for the Promotion and Reciprocal Protection of Investments, signed on 09 September 2012, entered into force on 01 October 2014.

**Colombia**

Agreement between the Government of the Republic of Colombia and the Government of the Republic of Turkey Concerning the Reciprocal Promotion and Protection of Investments, signed on 28 July 2014, not yet entered into force.

**Costa Rica**

Agreement between the Government of Canada and the Government of the Republic of Costa Rica for the Promotion and Protection of Investments, signed on 18 March 1998, entered into force on 29 September 1999.

Agreement between the Swiss Confederation and the Republic of Costa Rica on the Promotion and the Reciprocal Protection of Investments, signed on 01 August 2000, entered into force on 19 November 2002.

**Cote D'Ivoire**

Agreement between the Government of the People's Republic of China and the Government of the Republic of Cote D'Ivoire on the Promotion and Protection of Investments, signed on 30 September 2002, not yet entered into force.

**Croatia**

Agreement between the Government of the Republic of Croatia and the Government of Canada for the Promotion and Protection of Investments, signed on 03 February 1997, entered into force on 30 January 2001.

The Agreement between the Government of the Republic of Croatia and the Government of the Republic of Indonesia on the Promotion and Protection of Investments, signed on 10 September 2002, not yet entered into force.

**Cyprus**

Agreement between The Government of the People's Republic of Bulgaria and The Government of the Republic of Cyprus on Mutual Encouragement and Protection of Investments, signed on 12 November 1987, entered into force on 18 May 1988.

Agreement between the Government of the Republic of Cyprus and the Government of the Hungarian People's Republic on Mutual Promotion and Protection of Investments, signed on 25 May 1989, entered into force on 25 May 1990.

**Czech**

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Czech and Slovak Federal Republic for the Promotion and Protection of Investments with Protocol, signed on 10 July 1990, entered into force on 26 October 1992.

Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 1991, entered into force on 01 October 1992.

**Ecuador**

Agreement between the Government of Canada and the Government of the Republic of Ecuador for the Promotion and Reciprocal Protection of Investments, signed on 29 April 1996, entered into force on 06 June 1997 (subsequently terminated).

**Egypt**

Agreement between The Government of The Republic of Finland and The Government of The Arab Republic of Egypt on The Promotion and Protection of Investments, signed on 03 March 2004, entered into force on 05 February 2005.

**El Salvador**

Agreement for the Reciprocal Promotion and Protection of Investments signed between the Republic of EI Salvador and the Kingdom of Spain, signed on 14 February 1995, entered into force on 20 February 1996.

**Finland**

Agreement between The Government of The Republic of Finland and The Government of The Arab Republic of Egypt on The Promotion and Protection of Investments, signed on 03 March 2004, entered into force on 05 February 2005.

**France**

Agreement between the Government of the Argentine Republic and the Government of the Republic of France for Reciprocal Protection and Promotion of Investments, signed on 03 July 1991, entered into force on 03 March 1993.

**Germany**

Treaty between the Federal Republic of Germany and Pakistan for the Promotion and Protection of Investments, signed on 25 November 1959, entered into force on 28 April 1962.

Agreement Between the Federal Republic of Germany and the Federation of Malaya Concerning the Promotion and Reciprocal Protection of Investments, signed on 22 December 1960, entered into force on 06 July 1963.

Treaty between the Federal Republic of Germany and the Kingdom of Swaziland concerning the Encouragement and Reciprocal Protection of Investments, signed on 05 April 1990, entered into force on 07 August 1995.

Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 18 April 1997, entered into force on 01 February 2000.

**Ghana**

Agreement between the Government of the Republic of Mauritius and the Government of the Republic of Ghana for the Promotion and Reciprocal Protection of Investments, signed on 18 May 2001, not yet entered into force.

Agreement between the Government of the Republic of Ghana and The Government the Republic of Guinea for the Promotion and Protection of Investments, signed on 18 May 2001, not yet entered into force.

Agreement between the Government of the Republic of India and the Government of the Republic of Ghana for the Reciprocal Promotion and Protection of Investments, signed on 05 August 2002, not yet entered into force.

**Guinea**

Agreement between the Government of the Republic of Ghana and The Government the Republic of Guinea for the Promotion and Protection of Investments, signed on 18 May 2001, not yet entered into force.

**Hungary**

Agreement between the Kingdom of the Netherlands and the Hungarian People's Republic for the Encouragement and Reciprocal Protection of Investments, signed on 02 September 1987, entered into force on 01 June 1988.

Agreement between the Government of the Republic of Cyprus and the Government of the Hungarian People's Republic on Mutual Promotion and Protection of Investments, signed on 25 May 1989, entered into force on 25 May 1990.

**Indonesia**

The Netherlands and Indonesia: Agreement on Economic Cooperation, signed on 07 July 1968, entered into force on 17 July 1971.

Agreement between the Government of The Republic of Indonesia and the Government of the Republic of India for the Promotion and Protection of Investments, signed on 10 February 1999, entered into force on 22 January 2004.

The Agreement between the Government of the Republic of Croatia and the Government of the Republic of Indonesia on the Promotion and Protection of Investments, signed on 10 September 2002, not yet entered into force.

**India**

Agreement between the Government of The Republic of Indonesia and the Government of the Republic of India for the Promotion and Protection of Investments, signed on 10 February 1999, entered into force on 22 January 2004.

Agreement between the Government of the Kingdom of Thailand and The Government of the Republic of India for the Promotion and Protection of Investments, signed on 10 July 2000, entered into force on 13 July 2001.

Agreement between the Government of the Republic of India and the Government of the Republic of Ghana for the Reciprocal Promotion and Protection of Investments, signed on 05 August 2002, not yet in force.

Treaty between The Republic of Belarus and The Republic of India on Investments, signed on 24 September 2018, not yet entered into force.

**Iran**

Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Islamic Republic of Iran and the Government of Bosnia and Herzegovina, signed on 27 July 1996, entered into force on 02 June 2009.

Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Republic of Turkey and the Government of the Republic of Iran, signed on 21 December 1996, entered into force on 13 April 2005.

Agreement between the Government of the Lebanese Republic and the Government of the Islamic Republic of Iran on The Reciprocal Promotion and Protection of Investments, signed on 28 October 1997, entered into force on 14 May 2000.

Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Italian Republic and the Government of the Islamic Republic of Iran, signed on 10 March 1999, entered into force on 08 August 2003.

Agreement on Reciprocal Promotion and Protection of Investment between the Government of the People's Republic of China and the Government of the Islamic Republic of Iran, signed on 22 June 2000, entered into force on 01 July 2005.

Agreement on the Promotion and Reciprocal Protection of Investments between the Kingdom of Spain and the Islamic Republic of Iran, signed on 29 October 2002, entered into force on 13 July 2004.

Agreement between the Slovak Republic and the Islamic Republic of Iran for the Promotion and Reciprocal Protection of Investments, signed on 19 January 2016, not yet entered into force.

Agreement between Japan and the Islamic Republic of Iran on Reciprocal Promotion and Protection of Investment, signed on 05 February 2016, entered into force on 26 April 2017.

**Iraq**

The Protocol between the Governments of the State of Kuwait and the Republic of Iraq on the Promotion of the Movement of Capital and Investments between the Two Countries, signed on 25 October 1964, entered into force on 07 June 1966.

**Italy**

Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Italian Republic and the Government of the Islamic Republic of Iran, signed on 10 March 1999, entered into force on 08 August 2003.

**Japan**

Agreement between Japan and the Islamic Republic of Iran on Reciprocal Promotion and Protection of Investment, signed on 05 February 2016, entered into force on 26 April 2017.

**Kazakhstan**

Agreement between the Government of the Republic of Kazakhstan and the Government of the Republic of Uzbekistan on the Promotion and Protection of Investments, signed on 02 June 1997, entered into force on 08 September 1997.

Agreement between the Government of the Kingdom of Sweden and the Government of the Republic of Kazakhstan on the Promotion and Reciprocal Protection of Investments, signed on 25 October 2004, entered into force on 01 August 2006.

**Kuwait**

The Protocol between the Governments of the State of Kuwait and the Republic of Iraq on the Promotion of the Movement of Capital and Investments between the Two Countries, signed on 25 October 1964, entered into force on 07 June 1966.

Agreement between the Republic of Austria and the State of Kuwait for the Encouragement and Reciprocal Protection of Investments, signed on 16 November 1996, entered into force on 22 September 1998.

**Kyrgyzstan**

Agreement for the Promotion and Protection of Investment between the Government of the Republic of Austria and the Government of the Kyrgyz Republic, signed on 22 April 2016, not yet entered into force.

**Lebanon**

Agreement between the Government of the Lebanese Republic and the Government of the Islamic Republic of Iran on The Reciprocal Promotion and Protection of Investments, signed on 28 October 1997, entered into force on 14 May 2000.

Agreement between the Government of the Lebanese Republic and the Government of the Republic of Belarus on the Promotion and Reciprocal Protection of Investments, signed on 19 June 2001, entered into force on 29 December 2002.

**Malaysia**

Agreement Between the Federal Republic of Germany and the Federation of Malaya Concerning the Promotion and Reciprocal Protection of Investments, signed on 22 December 1960, entered into force on 06 July 1963.

Investment Guarantee Agreement between Malaysia and the Belgo-Luxemburg Union, signed on 22 November 1979, entered into force on 08 February 1982.

Agreement between the Republic of Austria and Malaysia for the Promotion and Protection of Investments, signed on 12 April 1985, entered into force on 01 January 1987.

**Mauritius**

Agreement between the Government of the Republic of Mauritius and the Government of the Republic of Ghana for the Promotion and Reciprocal Protection of Investments, signed on 18 May 2001, not yet entered into force.

**Mongolia**

Agreement between Canada and Mongolia for the Promotion and Protection of Investments, signed on 08 August 2016, entered into force on 24 February 2017.

**Montenegro**

Agreement between The Belgium-Luxembourg Economic Union, on the one hand, and Montenegro, on the other hand, on the Reciprocal Promotion and Protection of Investments, signed on 16 February 2010, not yet in force.

**Netherlands**

The Netherlands and Indonesia: Agreement on Economic Cooperation, signed on 07 July 1968, entered into force on 17 July 1971.

Agreement on Reciprocal Encouragement and Protection of Investments between the Kingdom of the Netherlands and the Republic of Turkey, signed on 27 March 1986, entered into force on 01 November 1989.

Agreement between the Kingdom of the Netherlands and the Hungarian People's Republic for the Encouragement and Reciprocal Protection of Investments, signed on 02 September 1987, entered into force on 01 June 1988.

Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 1991, entered into force on 01 October 1992.

Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Argentine Republic, signed on 20 October 1992, entered into force on 01 October 1994.

Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of Cambodia and the Kingdom of the Netherlands, signed on 23 June 2003, entered into force on 01 March 2006.

**Pakistan**

Treaty between the Federal Republic of Germany and Pakistan for the Promotion and Protection of Investments, signed on 25 November 1959, entered into force on 28 April 1962.

Agreement between Australia and the Islamic Republic of Pakistan on the Promotion and Protection of Investments, signed on 07 February 1998, entered into force on 14 October 1998.

**Philippines**

Agreement between the Federal Republic of Germany and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 18 April 1997, entered into force on 01 February 2000.

Agreement between the Republic of Austria and the Republic of the Philippines for the Promotion and Reciprocal Protection of Investments, signed on 11 April 2002, entered into force on 01 December 2003.

**Portugal**

BIT between the Portuguese Republic and the Government of the Republic of Venezuela, signed on 17 June 1994, entered into force on 07 October 1995.

**Russia**

Agreement between the Government of the Kingdom of Thailand and the Government of the Russian Federation on the Promotion and Reciprocal Protection of Investments, signed on 17 October 2002, not yet entered into force.

**Slovakia**

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Czech and Slovak Federal Republic for the Promotion and Protection of Investments with Protocol, signed on 10 July 1990, entered into force on 26 October 1992.

Agreement on Encouragement and Reciprocal Protection of Investments between the Kingdom of the Netherlands and the Czech and Slovak Federal Republic, signed on 29 April 1991, entered into force on 01 October 1992.

Agreement between the Slovak Republic and the Islamic Republic of Iran for the Promotion and Reciprocal Protection of Investments, signed on 19 January 2016, not yet entered into force.

**Spain**

Agreement for the Reciprocal Promotion and Protection of Investments signed between the Republic of EI Salvador and the Kingdom of Spain, signed on 14 February 1995, entered into force on 20 February 1996.

Agreement on the Promotion and Reciprocal Protection of Investments between the Kingdom of Spain and the Islamic Republic of Iran, signed on 29 October 2002, entered into force on 13 July 2004.

Agreement between the Kingdom of Spain and the Republic of Albania on the Promotion and Reciprocal Protection of Investments, signed on 05 June 2003, entered into force on 14 January 2004.

**Swaziland**

Treaty between the Federal Republic of Germany and the Kingdom of Swaziland concerning the Encouragement and Reciprocal Protection of Investments, signed on 05 April 1990, entered into force on 07 August 1995.

**Sweden**

Agreement between the Government of the Kingdom of Sweden and the Government of the Republic of Kazakhstan on the Promotion and Reciprocal Protection of Investments, signed on 25 October 2004, entered into force on 01 August 2006.

**Switzerland**

Agreement between the Swiss Confederation and the Republic of Costa Rica on the Promotion and the Reciprocal Protection of Investments, signed on 01 August 2000, entered into force on 19 November 2002.

**Thailand**

Agreement between the Government of the Kingdom of Thailand and The Government of the Republic of India for the Promotion and Protection of Investments, signed on 10 July 2000, entered into force on 13 July 2001.

Agreement between the Government of the Kingdom of Thailand and the Belgo-Luxemburg Economic Union on the Reciprocal Promotion and Protection of Investments, signed on 12 June 2002, entered into force on 19 September 2004.

Agreement between the Government of the Kingdom of Thailand and the Government of the Russian Federation on the Promotion and Reciprocal Protection of Investments, signed on 17 October 2002, not yet entered into force.

**Turkey**

Agreement on Reciprocal Encouragement and Protection of Investments between the Kingdom of the Netherlands and the Republic of Turkey, signed on 27 March 1986, entered into force on 01 November 1989.

Agreement between the Republic of Turkey and Turkmenistan Concerning the Reciprocal Promotion and Protection of Investments, signed on 02 May 1992, entered into force on 13 March 1997.

Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Republic of Turkey and the Government of the Republic of Iran, signed on 21 December 1996, entered into force on 13 April 2005.

Agreement between the Government of the Republic of Colombia and the Government of the Republic of Turkey Concerning the Reciprocal Promotion and Protection of Investments, signed on 28 July 2014, not yet entered into force.

**Turkmenistan**

Agreement between the Republic of Turkey and Turkmenistan Concerning the Reciprocal Promotion and Protection of Investments, signed on 02 May 1992, entered into force on 13 March 1997.

**United Kingdom**

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Czech and Slovak Federal Republic for the Promotion and

Protection of Investments with Protocol, signed on 10 July 1990, entered into force on 26 October 1992.

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Argentina for the Promotion and Protection of Investments, signed on 11 December 1990, entered into force on 19 February 1993.

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Armenia for the Promotion and Protection of Investments, signed on 27 May 1993, entered into force on 11 July 1996.

**Uzbekistan**

Agreement between the Government of the Republic of Kazakhstan and the Government of the Republic of Uzbekistan on the Promotion and Protection of Investments, signed on 02 June 1997, entered into force on 08 September 1997.

**Venezuela**

BIT between the Portuguese Republic and the Government of the Republic of Venezuela, signed on 17 June 1994, entered into force on 07 October 1995.

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Netherlands Model BIT (2004).

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US Model Bilateral Investment Treaty (2012).

Model Text for the Indian Bilateral Investment Treaty (2015).

Netherlands Model Investment Agreement (2018).

**Treaties with Investment Provisions**

North American Free Trade Agreement (NAFTA), adopted on 17 December 1992, entered into force 01 January 1994, 107 Stat 2057, CTS 1994 No. 2.

Trade and Economic Co-Operation Agreement between the Caribbean Community (CARICOM) and the Government of the Republic of Cuba, signed on 05 July 2000, entered into force on 01 January 2001.

United States – Singapore Free Trade Agreement, signed on 06 May 2003, entered into force 01 January 2004.

Comprehensive Economic and Trade Agreement (CETA) between Canada, of the One Part, and the European Union And Its Member States, signed on 30 October 2016, not yet entered into force.

Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), signed on 08 March 2018, not yet entered into force.

**International Conventions**

African Union Convention on Preventing and Combating Corruption, signed on 11 July 2003, entered into force 05 August 2006 (2004) 43 ILM.

Civil Law Convention on Corruption, signed on 04 November 1999, entered into force on 01 November 2003, 2246 UNTS 3.

Convention for the Protection of Human Rights and Fundamental Freedoms (European Convention on Human Rights), adopted on 04 November 1950, entered into force on 03 September 1953, 213 UNTS 222.

Convention on Certain Questions Relating to the Conflict of Nationality Laws, signed on 12 April 1930, entered into force on 01 July 1937, 179 LNTS 89.

Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention), adopted on 18 March 1965, entered into force on 14 October 1966, 575 UNTS 159.

Criminal Law Convention on Corruption, signed on 27 January 1999, entered into force 01 July 2002, 2216 UNTS 225.

Energy Charter Treaty (ECT), adopted on 17 December 1994, entered into force on 16 April 1998, 2080 UNTS 100.

European Convention on Nationality, signed on 06 November 1997 in Strasbourg, entered into force on 01 March 2000, 2135 UNTS 123.

Inter-American Convention against Corruption, signed on 29 March 1996, entered into force on 06 March 1997, (1996) 35 ILM.

OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, signed on 21 November 1997, entered into force on 17 December 1997 (1998) 37 ILM.

Vienna Convention on the Law of Treaties (VCLT), signed on 23 May 1969, entered into force, 27 January 1980, 1155 UNTS 331.

United Nations Convention against Corruption, signed on 31 October 2003, entered into force on 14 December 2005, 2349 UNTS 41.

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'Charter of Economic Rights and Duties of States' GA Res 3281, XXIX, 12 December 1974.

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'United Nations Declaration against Corruption and Bribery in International Commercial Transactions' GA Res 51/191, 16 December 1996.

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Draft United Nations Code of Conduct on Transnational Corporations (1984) 23(3) ILM.

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