

Principles of International Law in an International Investment Dispute

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Abstract

This essay primarily focuses on the applicability of principles of International law in an International investment disputes between countries. The scope and ambit of international law is vast and hence there is a need to study all the principles relating to an investment dispute at one place at the same time. Every country intends to improve its bilateral relations with other countries and hence investment plays a pivotal role in strengthening those relations. There are many situations because of which an investment dispute may arise and therefore it is quintessential to understand the principles revolving around an International Investment Dispute. This essay includes the detail analysis of Exhaustion of local remedies rule both in International law as well as in Indian context. Further the essay talks about the principles of customary international law that revolves around an investment dispute. These principles are Special and differential treatment, presence of a legal dispute, principles of MFN and NT, standard of treatment of foreign investors and legitimate expectation.

Exhaustion of local remedies rule under International Investment Law

The exhaustion of local remedies rule requires that a foreign national allegedly harmed by a state must first seek to redress the alleged harm before the administrative and judicial system of that state, until a final decision has been rendered, before seeking diplomatic protection or initiating international proceedings directly against the state. The purpose of this rule is “honouring the host state’s sovereignty” by affording its domestic legal system the opportunity to settle the dispute before the initiation of international arbitration.³ It follows the logic that, “before a state may exercise diplomatic protection, the foreign national must have sought redress in the host state’s domestic legal system”⁴. The International court of Justice held that ELR is a well-established rule of customary international law generally applied in diplomatic protection claims, to give the State where the

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³ Ambiente Ufficio S.P.A. v. The Argentine Republic, ICSID Case No. ARB/08/9, Decision on Jurisdiction and Admissibility, para. 602 (Feb. 8, 2013).

⁴ (Newcombe & Paradell, 2009, p. 6)

violation occurred, an opportunity to redress it by its own means, within the framework of its domestic legal system, before resorting to international proceedings.⁵

Presence of ELR rule under various Bilateral Investment Treaties

It is the opinion of the International Court of Justice that it is unable to accept an important principle of customary international law should be held to have been tacitly dispensed with, in the absence of any words making clear an intention to do so. The ELR rule is not a new rule and has its presence in customary international law. Under several BIT's⁶ concluded by countries which says that a dispute may only be submitted to arbitration if it continues to exist after litigation in domestic courts for a specified time.

Significance of ELR rule in claims of Expropriation

Expropriation involves a taking of property⁷ especially of foreign companies. Expropriation can be by outright seizure or by an act or series of acts which render the assets of a company useless, therefore amounting to expropriation⁸.

Whenever we talk about the existence of exhaustion of local remedies rule in the claims of expropriation, it is very important to note that in expropriation claims, the investor cannot argue that the investment lost its value and then point to some government action or administrative fault to claim that an internationally wrongful expropriation occurred. The ICJ held that, in these cases, the investor's failure to seek redress before domestic authorities may disqualify the international claim, not because there is a requirement of exhaustion of local remedies but because the very reality of conduct tantamount to expropriation is doubtful in the absence of a reasonable, not necessarily exhaustive, effort by the investor to obtain correction.⁹

How can ELR rule be Bypassed?

International courts and tribunals in various landmark cases have taken a broader view on the topic and have excused the ELR rule. Lets us understand one such exception in the Indian context. Whenever we talk about litigation in India, the first thing that comes to our mind is pendency of suits and the effective applicability of the saying that "Justice delayed is justice denied." In the landmark case of Abaclar v. Argentina¹⁰ tribunal

⁵ Switz. v. U.S., (Interhandel case), 1959 ICI 6 (Mar.21)

⁶ Treaty between the Federal Republic of Germany and the State of Israel concerning the Encouragement and Reciprocal Protection of Investments, Ger.-Isr., (June 24, 1976), art. 10, para. 5, 1 Agreement between the Government of the People's Republic of China and the Government of the Republic of Côte d'Ivoire on the Promotion and Protection of Investments, China-Côte d'Ivoire, art. 9, para. 3, (Sept. 30, 2002), Agreement between the Council of Ministers of the Republic of Albania and the Government of the Republic of Lithuania on the Promotion and Protection of Investments, Alb.-Lith., art. 8, para. 2, (Mar. 28, 2007), Agreement between the Government of the Republic of Korea and the Government of the Republic of Indonesia Concerning the Promotion and Protection of Investments, Indon.-S. Korea, (Feb. 16, 1991), art. 9, para. 2. Retrieved from <http://investmentpolicyhub>.

⁷ S.D. Myers v. Canada 121 ILR, pp. 72, 122.

⁸ Starrett Housing v. Iran, Interlocutory Award No. ITL 32-24-1, 19 December 1983

⁹ Generation Ukraine, Inc. v. Ukraine, ICSID Case No. ARB/00/9, Award, para. 20.30 (Sept. 16, 2003).

¹⁰ ICSID Case No. ARB/07/5

analysed the consequences of non compliance of time limited litigation and further it was concluded that the dispute will not be resolved within 18 months and this will cause undue delay and cause futility to the affected party. The futility exception discussed above can be better understood by the landmark case of Ambiente Ufficio v. Argentina¹¹ where the tribunal concluded that the futility exception applies to both the requirements to pursue and to exhaust local remedies. The last exceptions arises out of a simple question i.e. What if the judiciary is not independent? This exception was discussed in detail in the landmark case of Ickale v. Turkmenistan¹² where the tribunal analysed the scenario based on the allegations of unfairness of proceedings and lack of Independence in the courts of Turkmenistan and concluded that if the authority which is entrusted to conduct fair proceedings is that independent then the situation will fall under the futility exception and hence the ELR rule can be bypassed in the respected matter.

Significance of ELR rule in India

It is important to note that India's initial investor-friendly approach to investment treaties started undergoing a sea-change after the case of White Industries in 2011. Thereafter, several cases were filed against India between 2011 and 2016. As a result of the growing surge of BIT claims, India unilaterally terminated several BITs in 2016. In 2016, India introduced a Model BIT with an exhaustive chapter on 'Settlement of Disputes between an Investor and a Party'. The India Model BIT, 2016 may appear to protect the State but the changed Indian judicial system has geared up to protect investors and commercial players. In the last two years, significant efforts have been made by the Indian legislature and judiciary in providing effective and efficient dispute redressal machinery for commercial disputes. In 2015, India enacted the Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts Act ('Commercial Courts Act') to cater to commercial disputes of a specified value, create special courts to adjudicate and amend civil procedure for speedy and efficient disposal of commercial matters. A commercial dispute includes disputes related to transactions of the nature of dealing in mercantile documents, partnership agreements, intellectual property rights, joint ventures, shareholders agreements or exploitation of natural resources.

Presence of ELR rule under the New Indian Model BIT, 2016

The model bilateral investment treaty talks about a procedure that needs to be followed before a dispute can be submitted to arbitration.¹³ The procedure puts an obligation on the disputed investor that it must first submits its claim before the relevant domestic courts or administrative bodies of the Defending Party for the purpose of pursuing domestic remedies in respect of the same measure or similar factual matters for which a breach of this Treaty is claimed. Such claim before the relevant domestic courts or administrative bodies of the Defending

¹¹ ICSID Case No. ARB/08/9

¹² ICSID Case No. ARB/I0/24

¹³ Article 15, The New Indian Model BIT of 2016

Party must be submitted within one (1) year from the date on which the investor first acquired, or should have first acquired, knowledge of the measure in question and knowledge that the investment, or the investor with respect to its investment, had incurred loss or damage as a result¹⁴

It further says that after exhausting all judicial and administrative remedies relating to the measure underlying the claim for at least a period of five years from the date on which the investor first acquired knowledge of the measure in question, no resolution has been reached satisfactory to the investor, the investor may commence a proceeding under this chapter by transmitting a notice of dispute ("notice of dispute") to the Defending Party¹⁵ and further the bilateral investment treaty says that for no less than six (6) months after receipt of the notice of dispute, the disputing parties shall use their best efforts to try to resolve the dispute amicably through meaningful consultation, negotiation or other third party procedures. In all such cases, the place of such consultation or negotiation or settlement shall be the capital city of the Defending Party.¹⁶

Role played by commercial courts of India in enforcing ELR rule

The Commercial Courts Act provides an express explanation while defining commercial disputes. It also provides that a commercial dispute shall not cease to be a commercial dispute merely because one of the contracting parties is the State or any of its agencies or instrumentalities or a private body carrying out public functions. The explanation clearly envisages governmental contracts and disputes arising there from to be commercial disputes. A typical investor-State dispute would fall under the ambit of a commercial dispute. Considering the high stakes often involved in such disputes, they would certainly fulfil the threshold of 'specified value' of INR 1,00,00,000 (approximately USD 1,55,000) to fall within the jurisdiction of commercial courts.

The special courts include Commercial Courts (at the District Court level), Commercial Division (where original jurisdiction vests in the High Court) and Commercial Appellate Division (established in the High Courts to hear appeals from Commercial Courts and Commercial Division). Commercial courts have already started functioning under the jurisdiction of the Delhi High Court, Bombay High Court, Himachal Pradesh High Court and the Gujarat High Court. Further, the Commercial Courts Act provides for appointment of more judges with special expertise in handling commercial disputes; to ensure adequate and continuous training facilities for the judges.

Principles of Customary International Law

Presence of a legal dispute

¹⁴ Article 15.1, The New Indian Model BIT of 2016

¹⁵ Article 15.2, The New Indian Model BIT of 2016

¹⁶ Article 15.4, The New Indian Model BIT of 2016

Whenever a matter is posed in front of an international court or tribunal, the basic requirement for a matter to be heard is that the matter should be a legal dispute and not any other dispute. The International Court of Justice has noted that while political aspects may be present in any legal dispute brought before it, the Court was only concerned to establish the dispute in question was a legal dispute in the sense of dispute capable of being settled by application of principles and rules of international law.¹⁷

Consequently, it is the function of the court of the Court to deal the disputes by applying the international conventions, rules expressly recognized by the states, international customs, general principles of law recognized by the states and judicial decisions and teachings of the most highly qualified publicists of various nations.¹⁸

Special and Differential Treatment

The term Special and Differential Treatment ('S&D') within the World Trade Organization (WTO) legal system describes preferential provisions and flexibilities regarding trade policies disciplines which allow a differentiated treatment for developing countries and least-developed countries by justifying deviation from the most-favoured-nation clause¹⁹. At the conclusion of the Tokyo Round in 1979, the principle of Preferential Treatment was given a permanent status in GATT which later came to be known as enabling provision. Para 2 of the declaration states that preferential treatment shall be granted under four circumstances and one of which is regional and global arrangements entered into by the developing countries in context of any general or specific measures concerning developing countries.

Principles of MFN and NT

The principle of MFN plays a significant role under GATT/WTO. The appellate Body Report, EC stated that it is 'the cornerstone of the GATT' as well as 'one of the pillars of the WTO trading system'²⁰ and 'it has been both central and essential to assuring the success of a global rules-based system for trade in goods'²¹. Under the WTO agreements, countries cannot normally discriminate between their trading partners. It suggests special treatment, but in the WTO it actually means non-discrimination — treating virtually everyone equally²².

¹⁷ The Armed Actions (Nicaragua v. Honduras) case, ICJ reports, 1988, pp.16, 91; 84 ILR, pp. 218, 246, Certain expenses of the United Nations case, ICJ reports, 1962, pp. 151, 155; 34 ILR, pp. 281, 285.

¹⁸ Article 38, The ICJ statute

¹⁹ Eduardo Tempone, Special and differential Treatment, Encyclopedia entries, Max Planck Encyclopedia for Public International Law, December 2014

²⁰ Appellate Body Report, US-Section 211 Appropriations Act, Para.297

²¹ Ibid

²² WTO | Understanding the WTO - principles of the trading system, Wto.org

The national treatment (NT) is deemed as a pole of WTO²³. Imported and locally-produced goods should be treated equally — at least after the foreign goods have entered the market²⁴. The same should apply to foreign and domestic services, and to foreign and local trademarks, copyrights and patents. This principle of “national treatment” (giving others the same treatment as one’s own nationals) is also found in all the three main WTO agreements²⁵. Its main purpose is to prevent discrimination between imported and domestic products of the members of the GATT²⁶. The European Community, Mexico and Canada submitted a complaint against the USA in which the US 1986 tax legislation imposed a higher tax on imported products compared to domestic products; this treatment was found to be discrimination between domestic and imported products²⁷.

MFN treatment has been a central pillar of trade policy for centuries. The United States included an MFN clause in its first treaty, a 1778 treaty with France²⁸. MFN and NT were the core obligations of commercial policy under the Havana Charter where Members were to undertake the obligation “to give due regard to the desirability of avoiding discrimination as between foreign investors”²⁹. Similarly, most of the investment treaties around the world incorporates the the principle of MFN and NT³⁰.

Economic Emergency justifying violation of MFN and NT.

Economic emergency justifies derogation from MFN and NT treatment obligation. This is provided for under GATT Article XIX, which allows states to adopt measures otherwise WTO –inconsistent, where a surge in import causes or threaten to cause injury to domestic industry³¹.In this regard, it is imperative, for the purpose of protecting domestic industry, that the Member state may adopt measures restricting import competition for a period, however temporary in order to allow the domestic industry time to adjust to the new economic realities. Such measures are called safeguard measures³².

²³ The appellate Body Report, EC-Tariff Preferences, para.10

²⁴ WTO | Understanding the WTO - principles of the trading system, Wto.org

²⁵ Article 3 of GATT, Article 17 of GATS and Article 3 of TRIPS

²⁶ Moawiah Milhem,Most-Favoured-Nations (MFN) and National Treatment (NT) principles under GATT and GATS,Brunel University Law School,London, 2013, 12/3/2019,https://www.academia.edu/5518155/Most-Favoured-Nations_MFN_and_National_Treatment_NT_principles_under_GATT_and_GATS

²⁷Johan H. Jakson, ‘Dispute Settlement and the WTO emerging Problem’ (1988) Oxford Journals;(L/6175-34S/136)

²⁸ Treaty of Alliance with France, 1778

²⁹ Article 3(1), German 1998 Model Treaty, Article 3 Netherlands Model BIT; Article 3, Albania/United Kingdom BIT 1996; Article 10.3 US-Chile FTA

³⁰ Agreement on SAARC Preferential Trading Agreement (SAPTA); Agreement on South Asian Free Trade Area (SAFTA); Comprehensive Economic Corporation Agreement between Government of Republic Of India and Government of Malaysia; Comprehensive Economic Partnership Agreement Between The Republic Of India and Japan; Comprehensive Economic Partnership Agreement Between The Republic of India and Korea

³¹GATT 1994:General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization

³² Agreement on Safeguard and also the transitional safeguard measure under China Accession Protocol

These are laws that enable domestic industries to request increases in import tariffs that are above the bound rates and are applied in a discriminatory fashion³³. They are called remedies because they are intended to correct for unfair trade practices and unexpected changes in trade patterns that are damaging to those industries that compete with imports³⁴.

Standard of treatment of foreign investors.

Customary international law, rooted in state practice, provides a minimum standard of protection to investors³⁵. Minimum standard³⁶ is a part of fair and equitable treatment required by customary international law. Till the nineteenth century, international law enjoined host countries to obey the international minimum standard in the treatment of foreign investors and their property³⁷. However, if host countries breach this standard, they have to take state responsibility to foreign investors³⁸.

There is no doubt about the fact that “fair and equitable” is a principle; that this principle is a general principle of international law; and that the general principle of international law exists independently of the conventional support expressing it³⁹.

Treatment of Investors as stipulated in Art 3.2 of BIT

In the New Indian Model BIT, Article 3.2⁴⁰ states that each party shall provide proper standard of protection to the investors where full protection refers to physical security to the investors.

That test is, broadly speaking, whether aliens are treated in accordance with ordinary standard of civilisation⁴¹; full protection and security, which is usually understood as the obligation for the host State to adopt all reasonable measures to physically protect assets and property from threats or attacks which may target particularly foreigners or certain groups of foreigners⁴².

Violation of legitimate expectation

³³GATT 1994:General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization

³⁴ Policy and Theory of International Trade, Steve Suranovic - Introductory Trade Issues: History, Institutions, and Legal Framework, 2019

³⁵Fair and Equitable Treatment Standard in International Investment Law”, OECD Working Papers on International Investment, 2004/03, OECD Publishing.<http://dx.doi.org/10.1787/675702255435>

³⁶I. Brownlie, Principles of Public International Law, Oxford, Sixth Edition 2003, p. 502:

³⁷ Samuel K. B. Asante,*The International and Comparative Law Quarterly*, Vol. 37, No. 3 (Jul., 1988), pp. 588-628, Hein online

³⁸ Lise Johnson & Oleksandr Volkov, Investor-State Contracts, Host-State “Commitments” And The Myth Of Stability In International Law, 13/3/2019

³⁹Juillard, op. cit. n. 33, pp. 132-34.

⁴⁰ Article 3.2, New Indian Model BIT of 2016

⁴¹US and Mexico General Claims Commission, Harry Roberts Claim, United Nations, Reports of International Arbitral Awards, 1927, IV, 77,

⁴²OECD (2004), “Fair and Equitable Treatment Standard in International Investment Law”, OECD Working Papers on International Investment, 2004/03, OECD Publishing.<http://dx.doi.org/10.1787/675702255435>

A legitimate expectation is said to arise “as a result of a promise, representation, practice or policy made, adopted or announced by or on behalf of government or a public authority”⁴³. This was when an individual receives any benefit then he can hope to continue receiving it. In the context of something that traders can rely upon, it is something “*held by a reasonable person as to matters likely to occur in the normal course of his affairs*”⁴⁴.

When economic, regulatory or other conditions general or specific to the investment undergo changes negatively affecting the investment’s value, they may be seen as a breach of legitimate expectations prevailing at the time the investment is made⁴⁵.

Conclusion

All the principles mentioned above are the ones which prevail primarily on occurrence of an international investment dispute. The interpretation and implementation of these principles have a direct bearing on the result and outcome of investment dispute between the nations. The interpretation of these principles should be done in a broader sense and not in a strict manner. All the primary sources of international which are binding on the nations were analysed in the essay along with case laws as a secondary source which are used by the courts and tribunals as guiding principles.

⁴³ Ng Siu Tung (n 1 above), p 600, para 92.

⁴⁴ Josephine Woods, Lorna Woods, Philippa Watson; Steiner and Woods, EU Laws(11th Edition, Oxford) Pg 150

⁴⁵ Fair and equitable treatment, UNCAD series on issues in International Investment Agreements II, United Nations, New York and Geneva, 2012