BENEFITING FROM EXPERIENCE: DEVELOPMENTS IN THE UNITED STATES' MOST RECENT INVESTMENT AGREEMENTS

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The number of international instruments providing for investor-State arbitration has surged over the past few years, and the trend shows no signs of abating. This is not surprising since no competing model to investor-State arbitration has emerged that can better serve the needs of both foreign investors and host States wishing to attract foreign investment.

While the United States may have been surprised to find itself defending against multiple claims submitted under NAFTA Chapter Eleven,[1] it remains committed to the institution of investor-State arbitration. In fact, over the past two years the United States' investment program has been reinvigorated. The United States revised its Model Bilateral Investment Treaty in 2004 and, since that time, has signed a bilateral investment treaty (BIT) with Uruguay and is negotiating a BIT with Pakistan. The U.S. has also continued to negotiate Free Trade Agreements (FTAs), like the NAFTA, that contain investment chapters. The United States negotiated the first two of these post-NAFTA FTAs, both of which entered into force in

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[1] North American Free Trade Agreement, U.S.-Can.-Mex., Dec. 17, 1992, 32 I.L.M. 605 (1993) [hereinafter NAFTA].

2004, with Singapore and Chile. Subsequently, the United States signed comprehensive FTAs with Morocco and Australia, the latter of which entered into force in 2005.[2] And the United States Congress recently approved the Dominican Republic-Central America FTA, the United States' first multilateral FTA since the NAFTA. Canada's and Mexico's investment treaty programs likewise have been increasingly active.

Each of the United States' post-NAFTA agreements embodies changes that reflect the negotiating objectives set forth in the Trade Promotion Authority Act of 2002.[3] Many of these objectives, as well as the resulting changes made to the agreements, have their origin in the United States' experience with NAFTA Chapter Eleven arbitration. In broad terms, the significant changes include the clarification of standards of certain substantive provisions, as well as modifications made to promote the transparency of investor-State arbitration, improve the efficiency of arbitrations, deter the filing of frivolous claims, and ensure the consistency of interpretations of similar obligations across agreements. These changes are briefly summarized below.[4]

I. CLARIFICATION OF STANDARDS

In its most recent investment agreements, the United States has clarified the meaning of the minimum standard of treatment and expropriation provisions. These clarifications do not change the nature of the substantive obligations that existed under the United States' prior agreements; instead, they merely elucidate, for the benefit of tribunals charged with interpreting the treaty, the Parties' intent in agreeing to those obligations.

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[2] The recently concluded U.S.-Australia Free Trade Agreement contains an investment chapter, but does not provide for investor-State arbitration. The decision to exclude investor-State arbitration from that agreement was made because the United States and Australia share a common legal tradition, have longstanding economic ties, and investors of both nations have expressed confidence in operating in each other's markets. *See* U.S.-Australia FTA Summary of the Agreement (July 15, 2004), *available at* http://www.ustr.gov/Trade_Agreements/Bilateral/Section_Index.html (follow "Australia Free Trade Agreement" hyperlink; then follow "Summary of U.S.-Australia FTA" hyperlink).

[3] *See* Bipartisan Trade Promotion Authority Act of 2002, Pub. L. No. 107-210, 116 Stat. 993, 19 U.S.C. §§ 3801-3813.

[4] The following discussion outlining the changes made in the United States' recent agreements has been adapted from a paper entitled, "An Overview of Investment Provisions and Investor-State Arbitration," presented at an October 2003 "Litigating Takings Claims" conference sponsored by Georgetown University Law Center's Environmental Law & Policy Institute.

In response to misinterpretations advanced by some claimants and adopted by certain NAFTA investor-State arbitral tribunals, in July 2001, the NAFTA Free Trade Commission ("FTC") adopted an interpretation of the NAFTA's minimum standard of treatment provision, Article 1105(1).[5] That Interpretation provides that Article 1105(1) prescribes the customary international law minimum standard of treatment to be accorded to investments of investors of another NAFTA Party.[6] It also provides that the concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens. Finally, the Interpretation provides that a determination that there has been a breach of another provision of the NAFTA or of a separate international agreement does not in itself establish that there has been a breach of Article 1105(1).

The minimum standard of treatment provision in the United States' most recent investment agreements incorporates the text of the FTC's July 2001 Interpretation directly into the provision itself. These recent agreements also provide further elaboration on what is meant by "fair and equitable treatment" and "full protection and security."[7]

In addition, while the scope of the expropriation provision has

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[5] The Free Trade Commission is comprised of the trade ministers of each of the three NAFTA Parties. NAFTA art. 2001 (providing that the FTC shall be comprised of cabinet-level representatives of the Parties or their designees). Interpretations by the FTC of provisions of the NAFTA are binding on Chapter Eleven tribunals. NAFTA art. 1131(2).

[6] FTC Interpretation of Chapter Eleven of the NAFTA (July 15, 2001), http://www.state.gov/documents/ organization/38790.pdf. For further background on the issue of the interpretation of the minimum standard of treatment provision, *see* Andrea J. Menaker, *Standards of Treatment: National Treatment, Most Favored Nation Treatment and the Minimum Standard of Treatment* (2002) *in* APEC WORKSHOP ON BILATERAL AND REGIONAL INVESTMENT RULES/AGREEMENTS (published by the Ministry of Economy, Mexico, for the APEC Secretariat), http://www.apec.org/ content/apec/apec_groups/committees/committee_on_trade/investment_experts.html (follow "Workshop on Bilateral and Regional Investment Rules/Agreements" hyperlink); J.C. Thomas, *Reflections on Article 1105 of NAFTA: History, State Practice and the Influence of Commentators*, 17 ICSID REV.: FOREIGN INV. L.J. 21 (2002).

[7] *See, e.g.,* United States – Chile Free Trade Agreement, art. 10.4(2)(a), (b), Jun. 6, 2003, *available at* http://www.ustr.gov/assets/Trade_Agreements/Bilateral/ Section_Index.html (follow "Chile Free Trade Agreement" hyperlink; then follow "Final Text" hyperlink; then follow "Investment" hyperlink) (providing that "'[F]air and equitable treatment' includes the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world; and (b) 'full protection and security' requires each Party to provide the level of police protection required under customary international law.").

remained unchanged from that in NAFTA Chapter Eleven, a few minor changes were made to the text of the provision in the United States' recent agreements. Those agreements also contain an annex on expropriation. Both the provision itself and the annex make clear that the expropriation provision incorporates basic customary international law principles of expropriation. The annex also explains that, in accordance with customary international law principles, an expropriation requires that there be a taking of a property right or property interest. Finally, the annex sets forth a number of factors that tribunals should take into consideration when determining whether an indirect expropriation has occurred.[8]

II. TRANSPARENCY

Central among the procedural innovations in the United States' post-NAFTA agreements are changes to maximize the transparency of the proceedings. While one of the perceived advantages of international commercial arbitration is often thought to be its confidential nature, confidentiality has been widely perceived as inappropriate for investor-State arbitrations.[9] Investor-State tribunals lack authority to order States to change their laws, and their decisions have no precedential value. Nevertheless, because investor-State disputes often involve issues of public concern and any award in favor of an investor will be paid out of the public fisc, the public has shown an increasing interest in monitoring and participating in these arbitrations.

Against this backdrop, early NAFTA investor-State arbitral

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[8] These factors parallel the factors considered by U.S. courts in analyzing takings claims, namely, the economic impact of the government action, the extent to which the government action interferes with distinct, reasonable investment-backed expectations, and the character of the government action. *See, e.g.,* U.S. Model BIT, Annex B at 4 (a)(i)-(iii), http://www.ustr.gov/assets/Trade_Sectors/Investment/ Section_Index.html (follow "U.S. Model Bilateral Investment Treaty (BIT)" hyperlink). The annex provides that these enumerated factors are not exclusive and may not be dispositive in any given case. *See, e.g., id.* Finally, the annex provides that "[e]xcept in rare circumstances, nondiscriminatory regulatory actions by a Party that are designed and applied to protect legitimate public welfare objectives, such as public health, safety, and the environment, do not constitute indirect expropriations." *See, e.g., id.* at 4(b).

[9] There is disagreement among jurisdictions as to whether there is any inherent duty of confidentiality in international arbitration. *See, e.g., Esso Australia Res. Ltd. v. Plowman* (Austl. 1995) 183 C.L.R. 10 (Australian High Court finding no implied duty of confidentiality in arbitration); *Hassneh Ins. Co. of Israel v. Mew,* 2 Lloyd's Rep. 243 (Q.B. 1993) (English appellate court finding an implied duty of confidentiality in arbitration*); Bulgaria Foreign Trade Bank Ltd. v. A.I. Trade Finance, Inc.*, Case No. T 1881-99, 15 Mealey's Int. Arb. Rep. 291 (Swed. 2000) (Swedish Supreme Court finding no implied duty of confidentiality in arbitration).

tribunals disagreed on whether, for example, a disputing party could release to the public documents that were generated during the course of the arbitration. Moreover, even where no duty of confidentiality was assumed, the public generally was not granted access to hearings or given the opportunity to participate in the proceedings.

The United States' recent agreements address the transparency of proceedings in three main areas: (1) access to documents; (2) participation by non-parties; and (3) public access to hearings. All of the recent agreements provide for disclosure of documents generated during the course of an arbitration, with exceptions to protect the confidentiality of business proprietary information or documents otherwise subject to privilege. This position accords with the view of the United States and the other NAFTA Parties, reflected in the FTC's July 2001 Interpretation, that the NAFTA imposes no duty of confidentiality on the parties to an investor-State arbitration. In application of that Interpretation, the three NAFTA Parties agreed to release to the public in a timely manner all such documents (with appropriate redactions to ensure the protection of business confidential information) and created websites where these documents, including transcripts of hearings, are routinely posted.

The United States' recent agreements also expressly provide that the tribunal has the authority to accept non-party, or *amicus*, submissions. Prior to 2003, organizations applied for leave to participate as *amici* in two NAFTA investor-State arbitrations. In the first of those cases, the claimant argued that the tribunal lacked authority to accept submissions from non-parties. Mexico agreed with the claimant on this point, while both the United States and Canada contended that the UNCITRAL Arbitration Rules granted tribunals authority to accept such submissions. In both of these cases, the arbitral tribunals determined that they had authority to accept submissions from non-disputing parties.[10] On October 7, 2003, the NAFTA Free Trade Commission issued an interpretation of the NAFTA providing that there is no provision of the Agreement that limits a tribunal's ability to accept, in its discretion, written submissions from non-disputing parties.[11] At that same time, the FTC issued

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[10] *See Methanex Corp. v. United States of America*, Decision of the Tribunal on Petitions from Third Persons to Intervene as "Amici Curiae" (Jan. 15, 2001), *available at* http://www.state.gov/documents/ organization/6039.pdf; *United Parcel Service of America Inc. v. Canada*, Decision of the Tribunal on Petitions for Intervention and Participation as Amici Curiae (Oct. 17, 2001), *available at* http://www.state.gov/ documents/ organization/6033.pdf.

[11] This FTC Interpretation is available at http://www.state.gov/s/l/c3439.htm (follow "Statement of the Free Trade Commission on non-disputing party participation" hyperlink).

recommended procedures to govern the acceptance of submissions from non-disputing parties.[12] The investment chapters of the United States' recent agreements expressly provide that the tribunal has authority to accept *amicus* submissions.

These post-NAFTA agreements also provide that hearings in investor-State arbitrations will be made open to the public subject to appropriate logistical arrangements, except when keeping the hearing private is necessary to ensure the protection of confidential information. The governing arbitration rules generally provide that, absent consent of both disputing parties, hearings are held *in camera.* As a matter of policy, the United States has granted its consent to hold open hearings for all NAFTA investor-State arbitrations to which it is a party.[13] Canada and Mexico have done the same.[14] Accordingly, in several NAFTA Chapter Eleven cases where claimants have consented to opening the hearings to the public, the hearings have been broadcast to a room where members of the public may come and go as they please. The United States' recent agreements expressly provide for open hearings, rendering it unnecessary to secure a claimant's subsequent consent to open the hearings, as that consent will have been granted upon submission of the claim to arbitration in accordance with the procedures set forth in the agreement.

III. IMPROVING EFFICIENCY AND DETERRING FRIVOLOUS CLAIMS

Several changes also were made in the United States' revised Model BIT and recent FTAs in order to improve the efficiency of investor-State arbitrations. Among these changes is a requirement that the claimant appoint an arbitrator to the tribunal at the time it files its Notice of Arbitration. The desirability of this new requirement became apparent as a result of the United States' experience with NAFTA investor-State arbitration.

Under the NAFTA, either party may request the appointing

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[12] *See id.*

[13] On October 7, 2003, the Trade Ministers of the United States and Canada issued a joint statement providing that their respective States would consent to open the hearings of all investor-State arbitration proceedings to which they are a party. *See* Office of the U.S. Trade Representative, NAFTA Commission Announces New Transparency Measures (Oct. 7, 2003), *available at* http://www.ustr.gov/Document_Library/Press_Releases/2003/October/NAFTA_Commission_Announces_New_Transparency_Measures. html.

[14] *See id.* On July 16, 2004, Mexico also agreed to open to the public hearings in investor-State arbitrations to which it is a party. *See* Office of the U.S. Trade Representative, FTC Joint Statement: A Decade of Achievement (July 16, 2004), *available at* http://www.ustr.gov/Document_Library/Press_Releases/2004/July/NAFTA_Free_Trade_Commission_Joint_Statement_-_A_Decade_of_Achievement.html.

authority to appoint the remaining arbitrators to the tribunal if the tribunal is not constituted within 90 days of the submission of the claim to arbitration.[15] Some claimants, however, have waited until this time period has almost elapsed before making their appointment, and then have immediately applied to ICSID to have the tribunal constituted. This tactic deprives the respondent of adequate time to make an informed choice as to its appointment. Other claimants have filed Notices of Arbitration, but have never proceeded with appointing an arbitrator. This approach forces the respondent to choose between two equally unfavorable courses of action – taking the initiative to constitute the tribunal or effectively allowing the claimant to toll the NAFTA's three-year limitation period by filing a claim within the appointed time, but not proceeding with that claim.[16] The requirement that the claimant appoint an arbitrator with the filing of its Notice of Arbitration addresses both of these problems.

In order to expedite the dismissal of frivolous claims, the United States' new investment agreements also contain a provision requiring tribunals to address as a preliminary matter an objection that a claim fails as a matter of law. At least one tribunal applying the UNCITRAL Arbitration Rules in a NAFTA investor-State arbitration determined that it lacked authority to address admissibility objections, as opposed to jurisdictional objections, in a preliminary phase. The United States' recent agreements ensure that such issues may be dispensed with at a preliminary phase, thus potentially avoiding the time and cost of an evidentiary hearing. In accordance with the procedures set forth in these agreements, respondents also may request that the tribunal decide on an expedited basis objections that the claim fails as a matter of law, as well as objections that the tribunal lacks competence. If such a request is made, the objections must be raised within the strict timeframes set forth in the agreements, which also provide the time within which the tribunal must render a decision on any such objection.

Finally, the United States' recent agreements make explicit the tribunal's authority to award reasonable costs and attorneys' fees to a State if the claim is dismissed at a preliminary stage and the tribunal determines that the claim was frivolous. The tribunal is likewise empowered to award such costs and fees to the claimant if it

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[15] In the United States' recent agreements, the time before a party may request that the ICSID Secretary-General appoint the remaining members of the tribunal has been shortened from 90 days after the claim has been submitted to arbitration to 75 days after the claim has been submitted. *See, e.g.,* 2004 U.S. Model BIT, art. 27(3).

[16] Although such a claim might be submitted to arbitration within the three-year period prescribed by NAFTA Articles 1116(2) and 1117(2), the claim nevertheless might be barred under equitable principles recognized in international law.

determines that the State raised a frivolous preliminary objection to a claim. While tribunals generally have authority to award costs and fees under the governing arbitration rules, the tendency in Chapter Eleven arbitrations has been for tribunals to order each party to bear its own costs. One notable exception is the recent award in *Methanex Corp. v. United States of America,* where the tribunal ordered Methanex to bear all of the costs for the arbitration and to reimburse the United States for the costs of its legal fees.[17] With this new provision, tribunals may make awards of costs and fees more frequently, thus providing further deterrence to frivolous filings.

IV. CONSISTENCY IN INTERPRETATIONS OF INVESTMENT PROVISIONS ACROSS AGREEMENTS

The United States' most recent agreements retain the provisions in the NAFTA intended to ensure proper and consistent interpretations of the treaty's provisions. These agreements contain provisions, like NAFTA Article 1128, that permit non-disputing Parties to make submissions on issues of treaty interpretation. They also allow the Parties to adopt interpretations of provisions of the treaty that are binding on investor-State tribunals.

The newest agreements, however, also contain two innovations intended to further promote the proper and consistent interpretation of treaty provisions. First, the agreements provide for an interim review procedure permitting the disputing parties to comment on a draft award before the award is finalized. This procedure is similar to one used in the World Trade Organization, and may provide tribunals with the opportunity to correct certain language or inaccuracies, thus avoiding future interpretive problems. Second, the agreements envision the possibility of creating an appellate or similar procedure to ensure consistent interpretations by tribunals of each agreement and of similar provisions across investment agreements. The new Model BIT, for instance, provides that the parties agree to consider, within three years, whether to establish a bilateral appellate body or similar mechanism for purposes of reviewing awards rendered pursuant to the BIT.[18] It also provides that if a separate multilateral agreement enters into force between the Parties that establishes an appellate body to review awards rendered by investor-State tribunals, the Parties shall attempt to reach agreement that such multilateral body review awards

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[17] *Methanex Corp. v. United States of America*, Final Award of the Tribunal on Jurisdiction and Merits (Aug. 3, 2005), *available at* http://www.state.gov/documents/organization/51052.pdf.

[18] 2004 U.S. Model BIT Annex D.

rendered pursuant to the BIT as well.[19]

Finally, it is worth noting that ICSID is contemplating amendments to both the ICSID Convention and Additional Facility Arbitration Rules that address some of these same areas.[20] In their latest iteration, these proposed amendments include provisions to increase the transparency of ICSID proceedings, as well as an expedited review procedure for certain objections. Although ICSID initially contemplated the creation of an appellate facility, that proposal is not currently being pursued by ICSID.

The refinements reflected in the United States' recent investment agreements are intended to result in more efficient proceedings and ensure continued support for investor-State arbitration. While the provisions in the United States' new BITs and FTAs do not directly apply to the NAFTA, the NAFTA Parties, through FTC Interpretations and policy statements, have incorporated some of these improvements into the NAFTA context as well. Moreover, to the extent that ICSID adopts rule changes, these will affect NAFTA investor-State claims that are filed under the ICSID Additional Facility rules.[21] As for the future, we can expect to see further refinements made to investment treaties as States continue to gain experience with investor-State arbitration.

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[19] *Id.* at art. 28(10).

[20] *See* Working Paper of the ICSID Secretariat, "Suggested Changes to the ICSID Rules and Regulations" (May 12, 2005), *available at* http://www.worldbank.org/icsid/052405-sgmanual.pdf.

[21] At present, claims submitted to arbitration under NAFTA Chapter Eleven cannot be made under the ICSID Convention Arbitration Rules because neither Mexico nor Canada is a Party to the Convention. *See* Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Mar. 18, 1965, art. 25(1), T.I.A.S. No. 6090, 17 U.S.T. 1270 (limiting the jurisdiction of the Centre to disputes arising between a Contracting State and a national of another Contracting State).