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Arbitration Without Privity

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I. INTRODUCTION

IT IS COMMONPLACE TO SAY of arbitration that it is consensual. A claimant initiates arbitration because it has agreed with the defendant that any dispute between them will be thus resolved. Either party can commence proceedings as a claimant; once an arbitration has started, the defendant may raise a counterclaim.

This is the arbitration world as we know it today. Hundreds of thousands of international contracts adhere to this basic framework, more or less dependable in individual cases. But explorers have set out to discover a new territory for international arbitration. They have already landed on a few islands, and they have prepared maps showing a vast continent beyond. This new world of arbitration is one where the claimant need not have a contractual relationship with the defendant and where the tables could not be turned: the defendant could not have initiated the arbitration, nor is it certain of being able even to bring a counterclaim.

The first island of discovery was the *SPP v. Republic of Egypt (Pyramids Oasis)* case, discussed *infra*, where an aggrieved investor successfully initiated International Centre for Settlement of Investment Disputes (ICSID) arbitration on the basis of a unilateral promise contained in an investment promotion law.

The maps that suggest the emergence of a new continent are to be found in other such investment laws, and in bilateral investment treaties. Although

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legal experts predicted many years ago that such texts would prove reliable,[1] some of them are in fact tentative and ambiguous, suffering from explicit limitations in scope as well as from doubts as to their interpretation. In 1993 and 1994, however, two extraordinary multilateral treaties were finalized, namely the North American Free Trade Agreement (NAFTA)[2] and the Energy Charter Treaty,[3] which are both explicit in terms and vast in scope. They seek to establish a comprehensive regime for all aspects of investments. Their provisions range from the right of non-discriminatory treatment and the prohibition of export-related import quotas to the principle of non-interference with contractual relations and the entitlement to repatriate income in convertible currency. By allowing direct recourse by private complainants with respect to such a wide range of issues, these treaties create a dramatic extension of arbitral jurisdiction in the international realm. They will provide focal points of this article, because they may presage a new era of confidence in the drafting, interpretation, and application not only of other such treaties, but also of national laws and bilateral investment treaties (BITs).

This new approach to the resolution of international disputes offers the hope of sanctioning legal rights in individual cases brought directly by the aggrieved party. It grants innumerable present and future investors the right to arbitrate a wide range of grievances arising from the actions of a large number of public authorities, *whether or not any specific agreement has been concluded with the particular complainant*, and so impels us to reconsider fundamental assumptions about the international legal process as it affects investors abroad. The new approach is obviously of a different nature from methods of dealing with aggregate complaints brought by governments on behalf of their nationals before preconstituted public bodies such as the World Trade Organization

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[1] *See, e.g.*, Broches, Bilateral Investment Protection Treaties and Arbitration of Investment Disputes, in The Art of Arbitration, Liber Amicorum Pieter Sanders 63 (J.C. Schultsz & A.J. van den Berg eds., 1982).

[2] North American Free Trade Agreement (NAFTA), reprinted in 32 ILM 289, 605 (1993).

[3] Energy Charter Treaty, Dec. 17, 1994, reprinted at page 258 of this issue.

(WTO).[4] Thus a large empty space begins to be filled in the embryonic structures of the international legal process.

II. INVESTMENT PROTECTION LAWS

The principle that national investment laws may create compulsory arbitration without privity is beyond cavil. The Report of the Executive Directors of the World Bank that accompanied the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (ICSID Convention) stated in paragraph 24 that "a host State might in its investment promotion legislation offer to submit disputes arising out of certain classes of investments to the jurisdiction of the Centre, and the investor might give his consent thereto in writing." In other words, unless the law is abrogated in the interim, an investor may wait until a dispute has arisen to announce its intention to avail itself of the arbitral mechanism—which until that moment is compulsory only as to the State.

If this principle is not understood or accepted, one must conclude that the 138 States that have signed the ICSID Convention (as of November 1995) did so in ignorance. (Of course a State would be perfectly free to sign the ICSID Convention with the firm intention *never* to refer to ICSID in an investment law. It is only the *possibility* of using the mechanism that is at issue here.)

This does not however mean that the existence and scope of "offers to submit" contained in national legislation are uncontroversial. In the *Pyramids*

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[4] On the other hand, to improve the rule of law through the evolving mechanisms discussed in this article should certainly be considered as consistent with the strengthening of the old General Agreement on Tariffs and Trade (GATT) disputes process through the WTO's new Dispute Settlement Board as it emerged in the Uruguay Round's so-called Understanding on Rules and Procedures Governing the Settlement of Disputes. Under the GATT system, decisions could be paralysed by the absence of consensus. Now, consensus is required to *reject* decisions. Whereas the GATT approach focused on finding an outcome reasonably calculated to be acceptable to both sides, the new Understanding gives scope for decisions based on purely legal considerations. Failure to abide by a decision may trigger a regulated right of retaliation.

Eloquent proof of the recognition of increased effectiveness lies in the creation of a new seven-member appellate body required to uphold, modify or reverse the legal findings and conclusions of a Panel within sixty days (ninety in certain cases). *See generally* Kohona, Disputes Under the World Trade Organization—An Overview, 28 J. World Trade L. 23 (1994). Even more eloquent evidence is the reported creation by the United States of a special monitoring commission that may authorize U.S. withdrawal from the WTO (subject to a Presidential veto) if it believes that Dispute Settlement Board decisions have been repeatedly unfair over a five-year period.

Oasis case,[5] for example, the claimant relied on a provision in a 1988 Egyptian investment law to the effect that:

> Investment disputes in respect of the implementation of the provisions of this Law shall be settled...within the framework of the Convention for the Settlement of Investment Disputes between the State and the nationals of other countries [sic] to which Egypt has adhered by virtue of law no. 90 of 1971, where it applies.

The Government of Egypt contended that this text was insufficient to create compulsory jurisdiction. For one thing, although the just-quoted passage was published in English by the General Authority for Investment in brochures made available to investors, the Government argued that only the official Arabic text of the investment law should be given weight, and thus initiated a scholarly debate on the correctness of the imperative form of the verb "shall." The Government also argued that use of the expressions "within the framework of the Convention" and "where it applies" implied the need for separate consent to ICSID jurisdiction. Furthermore, it took the position that the simple reference to the Convention was insufficient to create compulsory arbitral jurisdiction since the Convention provides for conciliation as well as arbitration. Although each of these objections was rejected by the Tribunal, they illustrate both the extreme care with which jurisdiction clauses should be drafted and the eagerness with which a defendant in a particular instance is likely to seize on any ambiguity that might arguably defeat jurisdiction.

It is widely understood that in a later case involving the Arab Republic of Egypt, another claimant investor also successfully relied on this form of legislative consent to ICSID.[6] The claimant in the case of *Gaith Pharaon v. Republic of Tunisia* similarly relied on an article in the 1969 Tunisian Investment Code as a foundation for ICSID jurisdiction. As the result of a settlement of the case, the objections raised by the State were never decided.[7]

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[5] Of the many episodes of this dispute, the only one relevant for present purposes is the Decision on Jurisdiction handed down by the ICSID tribunal presided by Judge Jiménez de Aréchaga on 14 Apr., 1988, excerpts of which were published in 16 Y.B. Com. Arb. 28 (1991). (The author acted for the Claimant in the case.)

[6] Manufacturers Hanover Trust Company v. Arab Republic of Egypt and General Authority for Investment and Free Zones. A settlement was reached in this case after a decision on jurisdiction had been rendered. *See* ICSID Cases, Doc. ICSID/16/Rev. 4, at 29 (July 31, 1995).

[7] Order of Discontinuance dated 21 Nov. 1988, cited in ICSID Cases, *supra* note 6, at 26. (The author acted for the Claimant.) In December 1994, an ICSID arbitration was initiated against the State of Albania by Tradex Hellas, a Greek investor, on the basis of an arbitration provision in the Albanian investment law (*Id.* at 32).

III. BILATERAL INVESTMENT TREATIES

The potential operation of BITs in this context was illustrated in the ICSID case of *Asian Agricultural Products Ltd. v. Republic of Sri Lanka*, where the claimant, a Hong Kong company, took the position that Sri Lanka had made an undertaking to arbitrate claims by investors by virtue of Article 8(1) of the U.K.–Sri Lanka BIT. The Centre's jurisdiction was not challenged by the respondent. The Tribunal noted that the claimant's request for compensation remained outstanding without reply for more than the cool-down period defined in the BIT and that "hence AAPL became entitled to institute the ICSID arbitration proceedings." The case thus went forward, and an award was rendered in favor of the investor to compensate for the destruction of a shrimp farm, which had been occupied by governmental security forces in violation of the State's duty under the treaty to provide protection and security.[8] A host of similar BIT provisions seek to create international arbitral jurisdiction.

It would however be exceedingly difficult to prepare an inventory of all BITs.[9] Even if the exercise were limited to the 100 countries most active in international trade[10] the task of determining the potential existence of 5,000 inter-State agreements would be overwhelming. For present purposes, a few examples will serve to demonstrate two propositions:

1) the contents of BITs vary greatly: as much as any individual country might like to impose its own idea of a standard BIT, the varying negotiating strength of the other side has the effect of rendering most countries' portfolios of BITs quite heterogeneous;
2) in particular, the scope and nature of third-party access to international arbitration through BIT mechanisms are so different from one BIT to the next that one cannot speak of a dominant practice; each BIT must be examined on its own.

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[8] 6 ICSID Rev.—FILJ 526 (1991); 30 ILM 577 (1991); 17 Y.B. Com. Arb. 106 (1992); excerpts in French translation in 119 Journal du droit international 217 (1992). Three subsequent ICSID arbitrations, currently pending, have been brought by investors also invoking BITs, signed by Zaire, Malaysia, and Albania respectively.

[9] *See generally* M. Sornarajah, The International Law on Foreign Investment (1994); Peters, Dispute Settlement Arrangements in International Treaties, 22 Neth. Y.B. Int'l Law 91 (1991). Current BITs are published in ICSID's multi-volume collection of Investment Treaties, published by Oceana Publications.

[10] It is not preposterous to consider that 100 countries might be relevant; quite small countries may be involved in significant international disputes. An indication to this effect is the fact that in 1993 parties from 94 different countries had recourse to arbitration under the Rules of the International Chamber of Commerce. *See* Chronique, 121 Journal du droit international 1032 (1994).

To take the case of France, the simplest situation is one where the BIT has been signed with a country that is very eager to receive investment (and perhaps from which France perceives it is unlikely to *receive* investments) and is willing to extend very wide and unqualified access to international arbitration. Thus, Article 8 of the Franco-Paraguayan BIT of 1978 gives investors, in simple unqualified language, the right to seek ICSID arbitration. Similarly, though with a slight nuance, Article 10 of the Franco-Czechoslovak BIT of 1990 entitles an investor to seek ICSID arbitration (or United Nations Commission on International Trade Law (UNCITRAL) arbitration if either relevant State is not an ICSID member at the relevant time) if it has not been given satisfaction within six months of raising a complaint.

A different situation arises when one or both signatory States are more selective, perhaps because neither wishes to undertake in advance that every investor will be able to bring an international case against the host State. One response is to give *qualified* access to international arbitration. Thus, Article 8 of the Franco-Polish BIT of 1989 gives an investor the right to seek ad hoc arbitration if it has not been given satisfaction within six months of raising a complaint, *but this right relates only to disputes concerning expropriation.* Similarly, Article 10 of the Franco-Moroccan BIT of 1975 also gives investors the right to seek ICSID arbitration, provided that the matter:

- concerns a "productive investment" having been approved by the host State and guaranteed by the State of the investor;
- is of a legal nature and concerns reparations for violations of provisions of the agreement that establish rights to be compensated in the event of expropriation, to repatriate revenues or capital, and to use expatriate personnel; and
- has not been dealt with satisfactorily by "internal recourse" within a two-year period.

To take yet another example in this vein, Article 8 (combined with paragraph 4 of the Annex) of the P.R.C.-France BIT of 1984 gives an investor the right to seek UNCITRAL arbitration if it has not been given satisfaction within six months of raising a complaint, but this right relates only to disputes concerning the "amount of compensation" to be paid in the event of

expropriation. (Article 4 requires compensation to be "appropriate," "without delay," "practically feasible" and "freely transferable.")[11]

BITs entered into by the U.S.S.R. (which have been reaffirmed by the Russian Federation, pending possible renegotiations) were paradoxical in that they were occasionally quite complex, but nevertheless had the effect of creating access to arbitration for a very wide range of disputes. Thus, for instance, Article 7 of the U.S.S.R.-France BIT of 1989 gives an investor the right to seek ad hoc arbitration if it has not been given satisfaction within six months of raising a complaint, this right being limited to "the administration, maintenance, enjoyment or liquidation of an investment...in particular but not exclusively with respect to the effects of a [State] measure concerning the transport or sale of goods, to expropriations, or to transfers defined in Article 5." Article 5 ensures "free transfer of payments connected with investments," including revenues, fees, repayments of loans, liquidation of investments, an "appropriate portion" of expatriate salaries, and compensation in the event of expropriation. Article 1(c) defines "investment" as including "assets" and "rights" of any nature, in particular but not exclusively "obligations, claims, or rights to any performance having an economic value...."

This broad definition goes beyond the everyday meaning of the word *investment*. It would encompass a wide range of purely contractual rights—not only ones owed by the host States, but also others that might merely be affected by State action—and could thus greatly expand the scope of arbitrable disputes. It is therefore highly significant to note that this particular provision recurs in a wide range of BITs. An identical definition appeared as early as 1978 in exactly the same place (Article 1(c)) in the France-Paraguay BIT of 1978; it shows up in the same Article 1(c) in the BITs entered into in 1990 by France with Poland and the Czech and Slovak Federal Republics. A near-identical definition appears in Article 1(a)(iii) of a series of BITs entered into by the U.K. with, e.g., Colombia (1994), India (1994), South Africa (1994), Lithuania

[11] Given the P.R.C.'s prominence and recent concerns about the legal security of investments there, it may be of interest to note further examples of P.R.C. BITs. Article 12 of the P.R.C.-Australia BIT gives investors access to ICSID arbitration if both States are parties to the ICSID Convention at the relevant time. Otherwise, the investor may bring an ad hoc arbitration. The scope of the reference appears to be broad: "a dispute between a Contracting Party and a national of the other Contracting Party relating to an investment or an activity associated with an investment." Article 10 of the P.R.C.-Polish BIT, on the other hand, gives access to neutral ad hoc arbitration only if an investor wishes to challenge the amount of compensation following an expropriation, and only if his complaint is not "solved" within one year by internal recourse. This limited approach is similar to those followed in Article 8 of the P.R.C.-Malaysian BIT, in Article 11 of the P.R.C.-Japan BIT (where the period for internal recourse is limited to six months), and in Article 13 of the P.R.C.-New Zealand BIT, although the degree of detail concerning the envisaged arbitral procedure is very different in each case.

(1993), Peru (1993), Ukraine (1993), Uzbekistan (1993), United Arab Emirates (1992), Turkey (1991), U.S.S.R. (1991), Argentina (1990), the Czech and Slovak Federal Republic (1990), Morocco (1990), Panama (1983), and Paraguay (1981). (The first three were not yet ratified as of early 1995.)

France and the U.K. have shown, in negotiating BITs, a marked determination to include the widest possible range of intangible assets within the definition of "investment," including not only the one under discussion but also a number of others, from "mortgages, liens and pledges" to "intellectual property rights and goodwill." The U.S. model BIT includes all of these and goes yet further, as Mr. Sornarajah has pointed out, to encompass licenses, permits, and other rights created under public (administrative) law.[12]

This wide notion of "investment" is not limited to BITs where a western State is involved. Thus, the 1982 Japan-Sri Lanka BIT, which gives investors the right to institute ICSID arbitration (or conciliation), refers in Article 1(1)(b) to "claims to money or to any performance under contract having commercial value." A similar provision is to be found in the China-Japan BIT of 1988 (although the scope of arbitrability is severely restricted, thus neutralizing much of the ostensibly broad scope of the definition of "investment").

Although the U.S.S.R. accepted this wide definition in its BITs with France and the U.K., it appears in a more restricted form in the U.S.S.R.-Korea and the U.S.-Russian Federation BITs of 1990 and 1992, respectively, where "claims to money or to performance" must be "associated with" (Korea) or "directly related to" (U.S.) the investment. As for the U.S.S.R.-Germany BIT of 1989, it does not contain any cognate provision allowing contractual rights *per se* to be treated as an investment.

The concept of exhaustion of local remedies as a prerequisite for access to international arbitration is spelled out in some detail in a number of BITs. The relevant details generally include a definition of the local authorities to be seized, or a time limit beyond which the investor may go to arbitration even if the local authority has not yet pronounced itself. These kinds of details obviously constitute crucial protection for the investor, who is thus assured that the exhaustion requirement is not used to make the promise of arbitration illusory (because the defendant State can always invent another authority that ought to have been seized, or more simply yet have the matter strung out like an international version of Dickens' fictional *Jarndyce v. Jarndyce*).

Turning to BITs that do not contain an exhaustion requirement, two conclusions seem compelling:

1) if the text of the BIT expresses the right of access to international arbitration in simple, declarative, unqualified sentences, it would

[12] *See* Sornarajah, *supra* note 9, at 241.

seem astonishing to read such a requirement into the text as an implied condition—especially given the fact that BITs typically treat much less fundamental matters with scrupulous explicitness;

2) the straightforward first conclusion is strengthened considerably when one considers such unqualified BIT provisions in the light of BITs that do contain an exhaustion requirement; given the commonly observed limitations on that requirement, such as those mentioned above—definition of the relevant local authority, obligation to give a local decision within a certain amount of time on pain of nullification of the requirement—it would be staggering to consider that States that do not take care to define *any* exhaustion requirement in their BITs should be in a better position to reject the investor than those who negotiate precise definitions and scope.[13]

In this connection, one should be aware that BITs may contain indirect waivers of any exhaustion requirement. Thus, the many BITs that refer to ICSID arbitration fall within the scope of Article 26 of the ICSID Convention, which creates a presumption of such a waiver.

To conclude this review of the potential effect of BITs: there is no substitute for analysis on a BIT-by-BIT basis.[14] It cannot be said that there is today a coherent *corpus* of BITs that allow arbitration without privity. Some allow arbitration only in relation to specifically approved investments. Other BITs, as typified by most such treaties entered into by the P.R.C., limit arbitrability only to certain types of disputes, and even then only subject to certain procedural preconditions. Yet Mr. Sornarajah is plainly mistaken when he affirms that the foreign investor's right to use the remedy exists only if there is *also* an arbitration clause in "the contract" concluded by the foreign party.[15] His assertion is backed by neither authority nor textual analysis. If such a remarkable limitation had been envisaged by the drafters of BITs, it would have been explicit. BITs most often do not require any State-investor contract at all. They

[13] This argument did not arise in the ELSI Case (U.S.A. v. Italy) decided by the International Court of Justice, [1989] ICJ Rep. 15 (Judgment of 20 July 1989), which was based on an old Treaty of Friendship, Commerce and Navigation and requires qualification in the light of modern practice in the context of BITs. Moreover, the focus in ELSI was jurisdiction to hear the State-to-State dispute; the issue was the availability of diplomatic protection, not arbitration. *See* Peters, *supra* note 9, at 135. The primary relevance of the holding, if any, would therefore be limited to the State-to-State jurisdiction clause that is invariably to be found in BITs.

[14] *See* Salacuse, BIT by BIT, 24 Int'l Law. 655 (1990).

[15] *See* Sornarajah, *supra* note 9, at 267. Mr. Sornarajah would thus reduce the entire purpose of the frequently appearing provisions envisaging arbitration of investors' grievances to that of transforming a State's breach of a contractual obligation to arbitrate, owed to the investor, into a corresponding breach of a treaty obligation owed to the investor's home State.

typically specify the type of arbitration that would be available to aggrieved investors. If Mr. Sornarajah were right, BITs would simply refer, e.g., to "such reference to arbitration as may have been defined in the approved investment contract." But an overwhelming majority of BITs reviewed by the present author go much farther.[16] Doubtless there are persons still with us who cannot shake off a mindset crystallized in the 1970s that recoils when faced with the prospect that a State might have to account for its actions before an international tribunal. Such ideologues, if given the power to write BITs as they fancy, would doubtless have charted the road to arbitration through the eye of their thinnest needle. But that is not what has happened. With most BITs, the investor is standing on a broad highway.

IV. THE LOMÉ CONVENTIONS

This serial treaty is the first *multilateral* instrument to play a role in the developments that interest us here. More precisely, its last two manifestations, namely Lomé III and Lomé IV, have made a contribution to the development of arbitration without privity. The contribution has not been brilliant, as we shall see, but it is significant nonetheless.[17]

The Lomé Conventions have since 1975 regulated the relationship between the European Community and the African, Caribbean and Pacific (ACP) Group of States. An important agent for the implementation of the Conventions has been the European Development Fund (EDF), which is headquartered in Brussels but has offices throughout the ACP regions. Numerous contracts for the building of infrastructure are awarded under EDF funding. The Lomé Conventions have sought in various ways to regulate the resolution of disputes under such contracts. Article 238(1) of Lomé III, for example, provided:

> Any dispute arising between the authorities of an ACP State and a contractor, supplier or provider of services, candidate or tenderer, on the occasion of the placing or performance of a contract financed by the Fund shall be settled by arbitration in accordance with procedural rules adopted by the Council of Ministers.

[16] This conclusion is shared by Professor Patrick Juillard of France, a knowledgeable and prudent specialist in the field of international economic law: Les conventions bilatérales d'investissement conclues par la France, 106 Journal du droit international 274, 289 (1979). *See also* Burdeau, Nouvelles perspectives pour l'arbitrage dans le contentieux économique intéressant l'Etat, 1995 Revue de l'arbitrage 3, 14.

[17] *See generally* Amissah, The ACP/EEC Conciliation and Arbitration Rules, 8 Arb. Int'l 167 (1992).

No such procedural rules were adopted with the result that, as "a transitional measure" under Article 238(3), disputes fell to be resolved under the rules of the International Chamber of Commerce (ICC). The effect was to provide compulsory arbitration without privity, available not only to contractors and suppliers, but also "candidates or tenderers." Unfortunately, however, like so many provisions of this complex treaty, Article 238 seems seldom to have been kept in mind by negotiators on any side. For example, many EDF-financed contracts were awarded even though they contained dispute resolution provisions contrary to Article 238.[18] Additionally, unlike the Energy Charter Treaty,[19] Article 238 of Lomé III did not provide a way out of such a conflict. Yet, however imperfect, Article 238 of Lomé III was in its conception a big step toward arbitration without privity.

Lomé IV was to take an almost equally great step backward. The ACP States having taken what Mr. Austin Amissah, an experienced Ghanaian barrister and consultant to the ACP General Secretariat, bluntly describes as "partly an emotional stand which cannot be rebutted altogether by rational argument,"[20] Lomé IV, signed in December 1989, replaced Article 238 of Lomé III with the following piece of equivocation appearing as Article 307:

> Any dispute arising between the authorities of an ACP State and a contractor, supplier or provider of services during the performance of a contract financed by the Fund shall:
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> (a) ...
>
> (b) in the case of a transnational contract be settled either:
>
> (i) if the parties to the contract agree, in accordance with the national legislation of the ACP State concerned or its established international practices, or
>
> (ii) by arbitration in accordance with the procedural rules which will be adopted by decision of the Council of

[18] The present author has acted for the Government of Kenya in two cases where foreign contractors brought International Chamber of Commerce (ICC) arbitration under the transitional regime of Article 238 irrespective of the fact that the relevant contracts contained clauses calling for reference to an arbitrator appointed by the Chief Justice of Kenya. In one of these cases, the Government of Kenya agreed to defend and counterclaim before the ICC tribunal. In the other, it objected to ICC jurisdiction; the claim was abandoned.

[19] Article 26 of the Energy Charter Treaty, as we shall see, gives investors the option to proceed under a previous agreement or under the arbitral proceedings contemplated by the Treaty. *See infra* at 248-254. Although less explicit, the net effect of NAFTA may be the same; as we shall see, an investor wishing to raise claims under NAFTA provisions must waive his right to "initiate or continue" other proceedings based on the same complaint. *See infra* at 000-000.

[20] *See* Amissah, *supra* note 17, at 170.

> Ministers at the first meeting following the signing of this Convention...

This is the kind of language that diplomats are happy to use to keep ideologues from being unhappy. It shows little concern for the happiness of future practitioners who will actually have to live with it. Specifically, the crucial subparagraph (b)(i) invites debates as to each of its three components. When and where must the parties "agree"? What is "in accordance"? Most importantly, may a State having accepted an arbitration clause referring to one of the best-known sets of international arbitration rules later argue that having done so was contrary to *its* "established [sic] international practice"?

Of course the foreign contractor may choose to avoid such debates by initiating arbitration under subparagraph (b)(ii). (Let us leave aside the disquieting possibility that the defendant then insists that there has been some form of agreement under subparagraph (b)(i) to resolve the dispute in another way, with the result that (b)(ii) is inoperative.) In fact the Council of Ministers did approve a set of rules in March 1990,[21] with the result that Article 307 clearly does stake out a road to arbitration without privity, however slippery the road may be.

It is clear that the intent of the draftsmen of the 1990 General Conditions of Contract for EDF-Financed projects[22] was to create a regime responsive to the perceived "desire of all parties—administrators, contractors, suppliers and consultants alike—to have conditions which would be uniformly applied."[23] This suggests that it was hoped that the unpredictable variety of methods allowed under subparagraph (b)(i) would in fact not be used, and that (b)(ii) would be uniformly applied. The trouble is that even if there is no challenge to the application of (b)(ii), the rules approved by the ACP-European Economic Community (EEC) Council of Ministers (although modelled on the UNCITRAL Rules and therefore otherwise by and large acceptable) contain a politically motivated provision that empoisons the whole system.

This defect relates to the designation of the Appointing Authority, which plays a crucial role in the operation of the UNCITRAL Rules or rules inspired thereby. The Appointing Authority fulfils three functions:

1) appointing arbitrators whenever necessary because of default or failure to agree by the parties;

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[21] Reprinted in 17 Y.B. Com. Arb. 325 (1992).

[22] Official Journal of the European Community, 1990 O.J. (L 382) 31.

[23] *See* Scott-Larsen, Introduction to the Procedural Rules on Conciliation and Arbitration of Contracts Financed by the European Development Fund, 17 Y.B. Com. Arb. 323, 324 (1992).

2) removing an arbitrator upon challenge based on "justifiable doubts or suspicion as to his impartiality or competence" (Article 11.2 of the EDF Rules);
3) consulting arbitrators as to the appropriateness of fees to be fixed by them.

Since arbitration is only as good as the arbitrator, the quality of proceedings under this regime depends on the reliability, neutrality, and professionalism of the Appointing Authority. Under the EDF Rules, as under the UNCITRAL Rules, the parties are invited to agree to the identity of the Appointing Authority (typically a specialized institution or the president thereof). But the fact is that parties often fail to do so.

Under the UNCITRAL Rules, it then falls to the Secretary-General of the Permanent Court of Arbitration (PCA) of The Hague to choose an Appointing Authority (i.e., *not* to act himself in that capacity). It would have been wise for the EDF Rules to follow this solution, but at the eleventh hour some delegates, more politically sensitive than practically sensible, discovered to their displeasure that in the history of the PCA its Secretary-General had never been an ACP national. While such a narrow focus on nationality is often misplaced, since there is no dearth of capable European arbitrators ready to consider the arguments of an ACP party with sympathy, one might admit the validity of this criticism on the level of appearances. But the eleventh-hour solution to this perceived problem was dramatically wrong.

The road taken (in Article 9.4) was to provide that in the absence of agreement either party may "request the most senior in rank from amongst the judges of the International Court of Justice at The Hague who are nationals of the ACP States and the Member States to exercise the powers of the Appointing Authority." In other words, whoever happens to be the most senior International Court of Justice (ICJ) member from either an EEC or an ACP country will act, not merely to designate the Appointing Authority, but in the capacity of that Authority.

This is highly unsatisfactory to any practitioner envisaging an arbitration under the EDF Rules—no matter which side he is representing. First, the identity of the Appointing Authority will be accidental and therefore unpredictable. Second, the judge in question is unlikely to have had occasions to build up a routine way of handling this delicate and controversial function, and therefore is likely to operate very slowly or erratically, to the frustration of the parties. Third, ICJ judges tend to be specialists in public international law, a realm often far removed from the private law concerns of these arbitrations, and light-years away from the construction law expertise that is relevant to so many EDF-financed contracts. The odds are therefore slight that they will have a true feeling for the special skills required in the arbitration. Fourth, ICJ

judges are not professional administrators of arbitration, and are unlikely to be proficient in organizing challenge actions or giving meaningful advice with respect to the assessment of arbitrators' fees.

Mr. Amissah's defence of this solution, to the effect that the relevant ICJ judge will be free to "consult with persons more conversant with the area of competence required for the arbitrator(s),"[24] alarms more than it convinces. Modern international practice demands transparence and predictability. Nor is his explanation of the unsuitability of "the usual authorities used for the purpose" persuasive in its stress on "the ground that membership of ACP nationals in these institutions was nil or negligible."[25] The fact is that there are distinguished ACP nationals, experienced and knowledgeable in the area of international arbitration, on both the ICC International Court of Arbitration and on the London Court of International Arbitration, to take the two leading all-purpose institutions. There was no reason why the solution of referring to the most senior in rank could not have been used with reference to one of these bodies rather than to the ICJ. The inference seems quite clear: the draftsmen of the EDF Rules felt obliged to opt for a political rather than a professional solution, and this is a pity indeed.

It is of crucial importance for developing countries to get a fair shake when they participate, as claimants or defendants, in international arbitrations. The present author has represented half a dozen African governments, in a score of such proceedings with large amounts at stake, and has concluded that western investors or contractors are perfectly ready to deny them that fair shake—if the rules or the tribunal allow them to get away with it. (In other words, western businessmen are just as prone to take advantage of Africans as of each other.) But this does not mean that disputes should be resolved in a way that is weighted *against* the foreign party, or that *neutral* proceedings do not take satisfactory account of some imagined handicap borne by the host country. Parties from developing countries can and do succeed in international arbitration.[26]

It may well be that the unfortunate direction taken under Lomé IV will not have a heavy effect in practice. After all, it is limited to EDF-financed contracts in the ACP countries. It concerns suppliers, not financiers or investors. It appears that in practice, close monitoring by local EDF representatives of contracts between suppliers and local authorities has had a salutary moderating

[24] *See* Amissah, *supra* note 17, at 176.

[25] *Id.* at 175.

[26] *See* Paulsson, Third World Participation in International Investment Arbitration, 2 ICSID Rev.—FILJ 19 (1987). *See also* Kemicha, Future Perspectives on International Commercial Arbitration in the Arab Countries, ICCA Congress Series, No. 6, at 221 (1993).

effect in resolving disputes at an early stage, well before any arbitration is initiated. And even when arbitration arises, it may well be that the relevant contract contains an agreement under Article 307(b)(i) that obviates the use of the unsatisfactory mechanism of (b)(ii), or one by which a professional Appointing Authority is designated. Nevertheless, Lomé IV stands as an example of politics prevailing over professionalism, and therefore one not to be followed. As we shall now see, the two far more important multilateral treaties that have emerged since Lomé IV happily opted for more practical and reliable solutions.

V. NAFTA

The substantive provisions of the North American Free Trade Agreement are beyond the scope of this discussion. It suffices to recall that NAFTA contains a Chapter Eleven entitled "Investment," and that Section A thereof establishes:

- standards for treatment of investors (whichever is better of either national or most-favored-nation treatment; thereby putting an emphatic end to Mexico's long insistence on the Calvo Clause under which Latin American States refused to accept the notion of foreigners' entitlement to anything but national treatment);
- freedom from performance requirements (e.g., obligations to export, to favor domestic suppliers, or to transfer technology);
- the right to control investments using senior managers of any nationality;
- the right to repatriate without delay and in a freely usable currency all profits, fees, or other proceeds resulting from investments;
- conditions of expropriation (notably: public purpose, non-discrimination, and compensation at "fair market value...immediately before the expropriation took place").

These provisions apply to a wide range of investments. (There are, however a number of exceptions—some specific to each of the three signatory States—beyond the scope of this article.) "Investment" is defined in Article 1139 to include, beyond traditional concepts like enterprises and securities, tangible and intangible "property" as well as "interests" under construction contracts, concessions or "other contracts where remuneration depends substantially on the production, revenues or profits of an enterprise." On the other hand, claims to money under simple sales contracts or trade credit are excluded.

Section B contains the relevant dispute resolution mechanisms.[27] It defines how investors may initiate international arbitration against a State on the grounds that the latter has "breached an obligation" under Section A. Essentially, an investor has the choice under Article 1120 of either ICSID arbitration (i.e., under the ICSID Convention or, if the relevant States are not signatories thereof, the ICSID Additional Facility) or UNCITRAL arbitration.

Section B contains a number of technical provisions that merit attention. First of all, no submission to arbitration may be made until six months have elapsed from the "events giving rise to the claim." This protects the host State from trigger-happy investors mounting instant challenges to actions of public officials that they feel violate Section A, and gives the State some breathing room to refine or adjust controversial measures.

One of the further conditions precedent to arbitration, defined in Article 1121, is that an investor must "consent" to arbitration when he submits a claim. This notion, which would be nonsense in the traditional context of international arbitration, is a consequence of arbitration without privity; or, to put it in another way, it creates privity at the time of initiating arbitration. This is important for the finality of awards; otherwise the defendant State would be exposed to a lose/lose proposition where an unfavorable award would be final but a favorable one could be resisted by the investor for lack of an agreement *by him* to arbitrate (whether under the ICSID Convention or the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards).[28]

The point just considered of course becomes particularly acute whenever the State wishes to raise a counterclaim. Such a counterclaim would most naturally arise when the State is in a position to assert breaches of *contractual* duties owed by the investor to the State. It is therefore logical to find that NAFTA (here reflecting more careful thinking than the Lomé Convention)[29] requires in Article 1121 that an investor wishing to initiate arbitration under Section B waive any right to "initiate or continue...any proceeding with respect to the measure of the [defendant State] which is alleged to be a breach" of the relevant substantive NAFTA provisions.

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[27] The present author advised the Government of Mexico with respect to Section B.

[28] The value of this provision was recognized by the Energy Charter Treaty, which mirrored it in Article 26. *See infra* at 248-254. A strong argument could be made to the effect that claimants at any rate consent implicitly to arbitration when initiating the proceedings, and that the request for arbitration in and of itself satisfies any requirement—such as that of the New York Convention—that an agreement to arbitrate must be in writing. Thus the absence of the condition precedent just described need not be fatal. On the other hand, its existence has the considerable merit of precluding debate.

[29] Although perhaps not an airtight solution for all situations. *See infra* note 32.

In the course of drafting and negotiating Section B, it became clear that a door was being opened that could create unprecedented difficulties in the event that a controversial State measure affected a large number of investors. It is not unimaginable that hundreds or even thousands of investors would consider that, say, a new tax operated in a discriminatory fashion in violation of NAFTA. It would be a hardship for a State to have to manage its defence in a hundred cases. Worse, one might imagine a hundred awards with a wide range of inconsistent results. Accordingly, Article 1126[30] (entitled "Consolidation") provides that a State may demand the empaneling of a "super-tribunal" operating under the UNCITRAL Rules. If it were convinced that common issues were being raised in pending cases, such a tribunal could assert priority jurisdiction over all or part of those cases.

VI. THE ENERGY CHARTER TREATY

The techniques employed in Chapter Eleven, Section B of NAFTA significantly influenced Article 26 of the Energy Charter Treaty—the latest and most ambitious multilateral treaty to date. It is remarkably far-reaching; indeed, as compared with the gradual development of national protection laws and BITs, it represents a quantum leap—both in terms of the mechanisms it makes available to the complainant and in terms of the magnitude of their potential application. These advances should be considered in light of the equally significant fact that 49 States (as well as the European Communities *per se*) signed the Treaty on 17 December 1994, including major producing or purchasing powers in the energy field (e.g., France, Germany, Italy, Japan, Kazakhstan, the Netherlands, Russia, Spain and the United Kingdom). Japan and Norway (among others) made statements to the effect that they expected to sign in 1995; the same position was understood to be taken by Uzbekistan and Turkmenistan. The stated reason why the United States has for now declined to sign is not that the Energy Charter Treaty goes too far, but that it falls short of ensuring investors' substantive rights to the same extent as BITs concluded by the United States.[31]

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[30] As a matter of anecdotal interest, it might be mentioned that the Article 1126 mechanism was first conceived and drafted on the back of a menu on a Sydney-Hong Kong flight, and then faxed to Mexico with doubts that an idea as unusual as this could withstand the rigors of intensive tripartite negotiations involving large teams of civil servants. Surprisingly it survived. If the mechanism ends up being of some use, this episode will not be allowed to be forgotten. If it creates havoc, the reader is asked to be prepared to forget even this footnote.

[31] U.S. Government Statement, European Energy Charter Treaty Meeting, Lisbon, 15 Dec. 1994, reprinted in 34 ILM 556 (1995).

A. The Mechanism

The operation of Article 26 may be generally described as follows:

- an investor who is a national of a signatory State may use the mechanism for any claimed violation of Part III of the Treaty (entitled "Investment Promotion and Protection");
- there is a cooling period of three months (relatively short in comparison to most similar provisions in BITs);
- if the investor is not satisfied, it has a wide range of options with respect to where it may seek redress: the courts or administrative tribunals of the host State, any jurisdiction provided for by a previous agreement, or arbitration under the Treaty;
- if the investor wishes to avail itself of arbitration under the Treaty, it has the further option of choosing among three sets of rules: those of ICSID (either those of the ICSID Convention or the ICSID Additional Facility), UNCITRAL, and the Arbitration Institute of the Stockholm Chamber of Commerce;
- irrespective of the type of arbitration chosen, the dispute must, under Article 26(6) be decided "in accordance with this Treaty and applicable rules and principles of international law";
- signatory States may make two types of limited reservation: to exclude disputes already submitted by the investor to a competent forum; or to exclude claims under specific contracts between the defendant State and the investor.

Article 26 inspires two general comments. First, by contrast to a number of exhortatory but fuzzy provisions in the Treaty that bespeak political compromise and are bound to generate what is commonly called soft law, Article 26 is unambiguous, technical, and precise. Unlike the politically motivated and ultimately unsatisfying text of the Lomé Convention (discussed *supra*), Article 26—which resembles Article 1120 of NAFTA—was clearly drafted with an eye to practical realities and with the intent of fashioning a reliable mechanism. Second, the unmistakable thrust of Article 26 is to eliminate procedural or jurisdictional wrangling by creating a regime that strongly favors the use of neutral arbitration to sanction violation of the Treaty to the detriment of investors. This can be seen in the wide range of options granted to the claimant. For example, reference to a previously agreed forum is only a possibility, but not a requirement. This means that a defendant minded to be obstreperous will find no comfort in the fact that a dispute is only *partially* covered by a contract containing an arbitration clause; a claimant apprehensive of the limited authority of arbitrators operating under such a clause may wipe the slate clean and opt for one of the three types of arbitration defined in Article 26 without

regard to what had been agreed before. Indeed, any defect in an arbitration clause might be cured in this manner by relying on Article 26.[32]

A few specific provisions also merit particular attention. First, the fact that the claimant may choose among the ICSID, UNCITRAL and Stockholm Institute rules gives a welcome degree of flexibility in light of the particular circumstances of each case. The ultimate choice may be affected by the amount in dispute, the issues raised, the nationalities of the parties, the venue thought desirable and the effect of the choice of rules on the composition of the arbitral tribunal.[33] Further, the reference to the Treaty and to international law as the source of norms to be applied by arbitral tribunals operating under Article 26 stands in contrast to other laws or treaties that either make the national law of the host State exclusively applicable, or allow reference to international law only in a suppletive or corrective fashion. Additionally, the drafters of Article 26 followed NAFTA in requiring an investor wishing to initiate arbitration without privity to create privity by accepting that his commencement of proceedings under the Treaty also means that *he* consents to them for the purposes of satisfying jurisdictional requirements. The implications are similar to those discussed above with respect to NAFTA. Lastly, on the whole, the mechanism created by Article 26 makes it impossible for States accused of having violated Treaty obligations to act as judge and party. Article 26 creates access to a neutral international forum, operating beyond the control of the host State. This is a dramatic step, and one that runs counter to the sovereign-rights ideology that has characterized the past discourse of a number of the States that have now signed the Energy Charter Treaty. To what extent is its acceptance attributable to a profound alteration of attitudes to the legal security of foreign investments; or to a come-what-may eagerness not to be left behind in the movement to create a favorable investment climate; or yet again to a failure to understand the radical consequences of Article 26? Different explanations may account for the attitude of different States. (It is somewhat difficult to accept ignorance as an explanation, given the repeated and well-publicized initial reluctance on the part of some signatories—in particular Norway—to accept the

[32] If there is an issue whether arbitrators operating under Article 26 are authorized or required to admit counterclaims, the fact that the claimant had chosen to disregard a pre-existing arbitration clause under which the new respondent could have brought a claim would intuitively weigh in favor of admissibility. The opposite conclusion could lead to utterly unattractive situations when the defendant initiates a second arbitration under the original clause, each case thus casting a shadow on the other.

[33] An uncharacteristic technical deficiency of Article 26 is that it does not define the Appointing Authority (which may remove as well as appoint arbitrators) in the event the claimant chooses the UNCITRAL Rules. This means that the Secretary-General of the Permanent Court of Arbitration in The Hague would have to be approached to nominate the Appointing Authority—a factor of complication and unpredictability.

Treaty's arbitration provisions precisely on the grounds that they went too far in neutralizing sovereign control.)

It is illuminating to compare Article 26 with the corresponding provisions of the currently circulating discussion draft Regulations of the P.R.C.'s Ministry of Geology and Mineral Resources on Foreign Investment in Exploration and Exploitation. Reflecting the typical aversion of P.R.C. legislative draftsmen for anything that escapes State control, Article 47 of this text provides that any challenge to a refusal to grant a mining license must be brought before a Chinese court and be decided under Chinese law. This provision suggests (a) how far the P.R.C.'s mindset must change before it could follow the many emerging market economies that have signed the Energy Charter Treaty and (b) that in the meanwhile, an investor should be more willing to spend vast sums exploring in some other country where its right to obtain a mineral license may be sanctioned by a neutral international tribunal.

B. The Scope of Potential Application

To make an inventory of the types of substantive disputes that may be submitted to arbitration would be a vast undertaking beyond the scope of this article. This is quite fortunate for the author. The contents of the Treaty are far-ranging and complex in their potential ramifications. To be fully understood, they must be read in the light of, inter alia, trade law; competition law; international agreements regarding transportation and currency controls; regional common market treaties; and the existing framework for the regulation of the energy industry. Furthermore, many provisions of the Treaty were, as already noted, left fuzzy, and subject to interpretation. Finally, a number of provisions are arguably contradictory. In a word, to make categorical statements at this stage as to what may or may not come under the purview of Article 26 arbitration would be foolhardy.

What *can* be said with confidence however is that a staggering variety of causes of action are arguably within the scope of Article 26. As has been seen, Article 26 may be invoked in relation to any alleged breach of Part III of the Treaty. Part III provides notably for the following:

- non-discriminatory and national treatment of investments;
- minimum standards under international law (including treaties);
- eschewing barriers such as domestic-content requirements, export-related import quotas, and restrictions on access to foreign exchange;
- entry and work permits for "key personnel";
- compensation for requisitioned assets or assets destroyed by use of excessive force in the event of armed conflict or disturbance;

- "prompt, adequate and effective" compensation in the event of expropriation;[34]repatriation of capital, profits, and contract payments in convertible currency.

The breadth of the potential complaints hereunder is reminiscent of what may be imagined in connection with NAFTA. (See the discussion *supra*. On the other hand, the Energy Charter Treaty contains no NAFTA-like mechanism of a super arbitration in the event the same governmental action gives rise to a number of complaints from different investors, thus creating the risk of a State having to face a multiplicity of proceedings, and potentially inconsistent outcomes.) Furthermore, the defined terms under Article 1 of the Treaty follow the example of the more progressive BITs by including among the kinds of assets to be considered as an investment "claims to money and claims to performance pursuant to contract having an economic value and associated with an Investment."[35] But the Treaty goes further than this. For one thing, it includes "Returns" as an investment, and defines this term very broadly:

> "Returns" means the amounts derived from or associated with an Investment, irrespective of the form in which they are paid, including profits, dividends, interest, capital gains, royalty payments, management, technical assistance or other fees and payments in kind.[36]

For another, it adds the specifically industry-oriented definition of investment as "any right conferred by law or contract or by virtue of any licenses and permits granted pursuant to law to undertake any Economic Activity in the Energy Sector."[37] It should surprise no one that *economic activity* is also given a wide definition, with reference to "exploration, extraction, refining, production, storage, land transport, transmission, distribution, trade, marketing, or sale."[38]

On the other hand, Article 26(8) makes clear that in the event that acts of a public authority are ruled to be in violation of the Treaty, that authority may

[34] Readers familiar with the international law of responsibility of States will recognize this formulation as the one originally expressed by U.S. Secretary of State Cordell Hull in a Note of 21 July 1938 to the Mexican Government. It has been supported by western governments and jurists ever since, but in the 1970s and 1980s its strength was eroded by a vigorous challenge from non-western officials and lawyers who felt that the application of the "prompt, adequate and effective" standard favored foreign capitalists while tying the hands of policy makers in capital-importing countries. *See, e.g.*, Sornarajah, *supra* note 9, at 359 et seq. Its reappearance in the Energy Charter Treaty is a remarkable turn of events.

[35] *See* Energy Charter Treaty, *supra* note 3, at art. 1(6)(c).

[36] *Id.* at art. 1(9).

[37] *Id.* at art. 1(6)(f).

[38] *Id.* at art. 1(5).

pay monetary damages in lieu of any other remedy.[39] In other words, arbitral tribunals operating under Article 26 will be barred from annulling governmental acts or ordering specific performance or *restitutio in integrum* against governmental entities. This prudent limitation does not however reduce the breathtaking scope for potential causes of action.

To give a flavor of the possibilities (although doubtless more to inspire reflection than to state conclusions) Professor Thomas Wälde of the University of Dundee's Centre for Petroleum and Mineral Law and Policy has suggested the four following illustrations:[40]

1) Mitsubishi imports oil into France. It is assigned an uneconomic port for inspection, and French officials make it difficult for Japanese executives to obtain work permits. Mitsubishi may bring a Treaty arbitration against the French Government.
2) Although it has already made significant investments in the country, British Gas is not granted new power station licenses in Italy while State companies obtain such licenses. It may bring a Treaty arbitration against the Italian Government.
3) A foreigner buys a petrol station in Dundee and applies for a permit to carry out an expansion. The local government rejects the application while granting such a license to a Scottish competitor. The foreigner may bring a Treaty arbitration against the *U.K.* Government.
4) The EU grants subsidies for new business development—but they are not available to a Japanese company in the energy business. The Japanese company may now consider bringing Treaty arbitration against *the European Commission.*

Instead of attempting to evaluate the susceptibility or otherwise to arbitration under Article 26 of specific types of grievances, one might simply note that the proponents of the Treaty were fully aware of the potential impact of Article 26. This is clear from their frequent references to the right to neutral international arbitration as one of the Treaty's "four pillars." Indeed, on the day

[39] This provision should be compared with Article 1135 of NAFTA, which provides that a tribunal may award only monetary damages or the restitution of property. Mexico was particularly insistent on eliminating the possibility for international tribunals to annul national enactments. Curiously, the Energy Charter Treaty's version in terms applies only to awards "concerning a measure of a sub-national government or authority," thus suggesting anomalously that a tribunal could order specific performance against a national government but not one of its subdivisions. At any rate, as a matter of practice, international arbitral tribunals operating outside the realm of inter-State disputes have traditionally been reluctant to order specific performance against States.

[40] Introductory remarks, European Energy Charter Treaty Conference, London, 27 Jan. 1995.

the Treaty was signed, the public announcement by the U.K. government, after urging U.K. investors "to take full advantage of the enormous opportunities the Treaty brings," referred to only four substantive provisions of the Treaty; the third one mentioned was the entitlement to international arbitration.[41]

Will Article 26 be thought by investors to be a Horn of Plenty, but by host governments to be a Pandora's Box? Such a result would be unfortunate, because it would likely generate a backlash. What States have done, they may undo; not being parties to the Treaty, private investors would not be in a position to stop them.

Fortunately it seems likely that the outcome will be more balanced, and therefore more stable. First of all, attitudes to Article 26 are unlikely to develop in a vacuum, but rather crystallize in reaction to the success of the Treaty as a whole. If on balance it provides an effective means for regulating the transnational energy industry (in terms of stabilizing as well as promoting orderly development; in the interest of consumers as well as producers, investors as well as capital importers), Article 26 is likely to be seen as part of a beneficial package. Second, arbitrations brought under Article 26 will not open the floodgates to easy victories by claimants; the substantive provisions of the Treaty contain ammunition for respondents as well, enabling them to defend their actions on the grounds of sovereign prerogatives that the Treaty reserves in certain areas. Third, the very presence of Article 26 should serve as a powerful impetus to more responsible management by public authorities of the energy sector. Laws, regulations, tenders, and contracts must be prepared with far greater care when one knows that they may be tested, by a neutral authority, for conformity with international obligations. This can only help the transnational environment.

In other words, when saying correctly that the arbitral mechanism is sufficiently important that it should be referred to as a "pillar" of the Treaty, its proponents were not leading their governments into a foolish adventure.

VII. CONCLUSIONS

We are witnessing an explosive proliferation of texts seeking to provide legal security for investments across borders. A recent survey noted that of 891 BITs "on record," 533 were signed or entered into force after January 1990.[42]

[41] Department of Trade and Industry Press Release, 19 Dec. 1994, quoting Mr. Charles Wardle, Parliamentary Under-Secretary of State for Industry and Energy.

[42] 34 ILM 1151 (1995).

Some 45 developing and former socialist countries have in the same period enacted new investment laws or codes.[43] NAFTA or the Energy Charter Treaty are unique new multilateral treaties that cover a vast range of transactions.

This proliferation coincides with a fundamental convergence of views as to the need for legal security. As Antonio Parra writes in a recent essay: "The new investment laws, bilateral treaties and multilateral instruments reflect a remarkable consensus on questions that not long ago were controversial."[44] One of the manifestations of this development is nothing less than a new dimension for international arbitration, requiring a new understanding of the process.

American lawyers will recall how intensely the issue of privity was debated in the early 1960s with respect to a seller's liability for defective products causing harm to users or consumers who have had no dealings with the seller. Professor William Prosser was inspired to write two of the most often cited articles in American jurisprudence, entitled "The Assault Upon the Citadel"[45] and "The Fall of the Citadel."[46] His metaphorical citadel was precisely that of *privity*. Its "fall" gave the buyer a right of direct action against unknown upstream sellers. The rule of privity would no longer restrict him to seeking relief against his immediate retailer. In the modern marketplace, this result was indispensable, because most retailers have no part in making or assembling the product, and are in no position to inspect great varieties of pre-packaged products. Furthermore, to restrict the plaintiff to an action against his immediate retailer would often deprive him of any effective remedy due to the latter's inability to meet an award of damages—while the true party at fault, the manufacturer, is often a large and profitable enterprise.

Another citadel of privity is now proving pregnable, this time in the realm of international arbitration. Aggrieved foreign investors often cannot point to any breach of a contract to which they are a party. Even if they can, their local contracting party may often avoid responsibility for the breach by reason of an act of *force majeure* or the like. The injury is caused by a third party, often a governmental authority. To examine the legitimacy of its action, international law has traditionally required the intervention of yet another third party, namely the investor's own government, exercising the right of diplomatic protection. Whatever may have been its value in securing the physical safety of individuals, this mechanism has proved itself unworkable as a way of protecting business interests in the context of contemporary international economic life. Defendant

[43] Parra, The Scope of New Investment Laws and International Instruments, text at footnote 1 (forthcoming in R. Pritchard, ed., Development, Investment and the Law.)

[44] *Id.*, text after footnote 17.

[45] 69 Yale L.J. 1099 (1960).

[46] 50 Minn. L. Rev. 791 (1966).

States are irritated when another State requires them to defend the legitimacy of their acts.[47] At the same time, foreign ministries have often been embarrassed and notoriously reluctant to shoulder the burden of presenting complaints raised by their nationals. And the complainant would typically at any rate prefer to be the master of his own initiative, both because he is convinced that he is better equipped to marshal evidence and develop arguments with relation to what may be a very complex problem, and because he understands that wider countervailing diplomatic objectives may cause the officials of his government to pull punches.

The possibility of direct action—international arbitration without privity—allows the true complainant to face the true defendant. This has the immense merit of clarity and realism; these virtues, and not eloquent proclamations, are the prerequisites of confidence in the legal process.

It is of course too early to tell whether this new field of international arbitration will fundamentally alter practice or remain a marginal feature. What is already clear however is that this is not a subgenre of an existing discipline. It is dramatically different from anything previously known in the international sphere.[48] It could presage an epochal extension of compulsory arbitral jurisdiction over States, at the behest of private litigants who wish to rely on governmental undertakings even though they have not contracted for a forum. The aim here is not to take anything away from States, but to help ensure that foreigners have faith in their promises. The objective is not arbitration that *favors the foreigner*, but one that simply favors *neutrality*. This is what the Guidelines, submitted to the Fall 1992 meeting of the Development Committee of the Board of Governors of the International Monetary Fund (IMF) and the World Bank, refer to as *independent* arbitration, further defined in Section V(2) as a process where "the majority of the arbitrators are not solely appointed by one party to the dispute."

As final revisions were being made to this article, the report from the April 1995 workshop in Wellington on the Organization for Economic Cooperation and Development (OECD) Multilateral Agreement on Investment became available. The Investment Agreement has since 1991 been under the joint consideration of the Committee on International Investment and Multinational Enterprises and the Committee on Capital Movements and Invisible Transac-

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[47] Mr. I.F.I. Shihata has written that the availability of direct action presents the advantage of depoliticizing the dispute. *See* Shihata, Towards a Depoliticization of Foreign Investment Disputes: The Roles of ICSID and MIGA, 1 ICSID Rev.—FILJ 1 (1986).

[48] Professor Burdeau has suggested, *supra* note 16, at 16, that the closest parallel may be drawn with the European Convention on Human Rights: "giving unidentified individuals a right of recourse against a State in order to give effect to the latter's undertakings, pursuant to an international treaty, to accord a certain treatment to private persons."

tions. This may be the next great advance. The fundamental idea is to create a new multilateral treaty with "legally binding obligations and enforcement proceedings;" its framework is described as possibly encompassing "liberalization, investment protection and dispute settlement;" it is intended for OECD member States and non-member States alike. Such a document would then supplant BITs, which are threatening to create confusion by their variety of formulations. In other words, what is envisaged is a *global charter* for a legal regime applicable to all types of investments, overarching both regional and sectorial treaties—such as NAFTA and the Energy Charter Treaty. One of five Working Groups is concentrating solely on "dispute settlement." While specific mechanisms are still under study, the Working Group has referred to the "ample precedents in BITs and other investment agreements."

Future prospects for this development in international arbitration may depend on whether national governments—many of whom may not have appreciated the full implications of the new treaty obligations discussed in this article—take fright and reverse their tracks. That may in turn depend on the degree of sophistication shown by arbitrators when called upon to pass judgment on governmental actions. Arbitration without privity is a delicate mechanism. A single incident of an adventurist arbitrator going beyond the proper scope of his jurisdiction in a sensitive case may be sufficient to generate a backlash. But if the mechanism is applied judiciously, it will help fill a void that now exists in the absence of compulsory jurisdiction, and thus contribute to enhancing the legal security of international economic life.